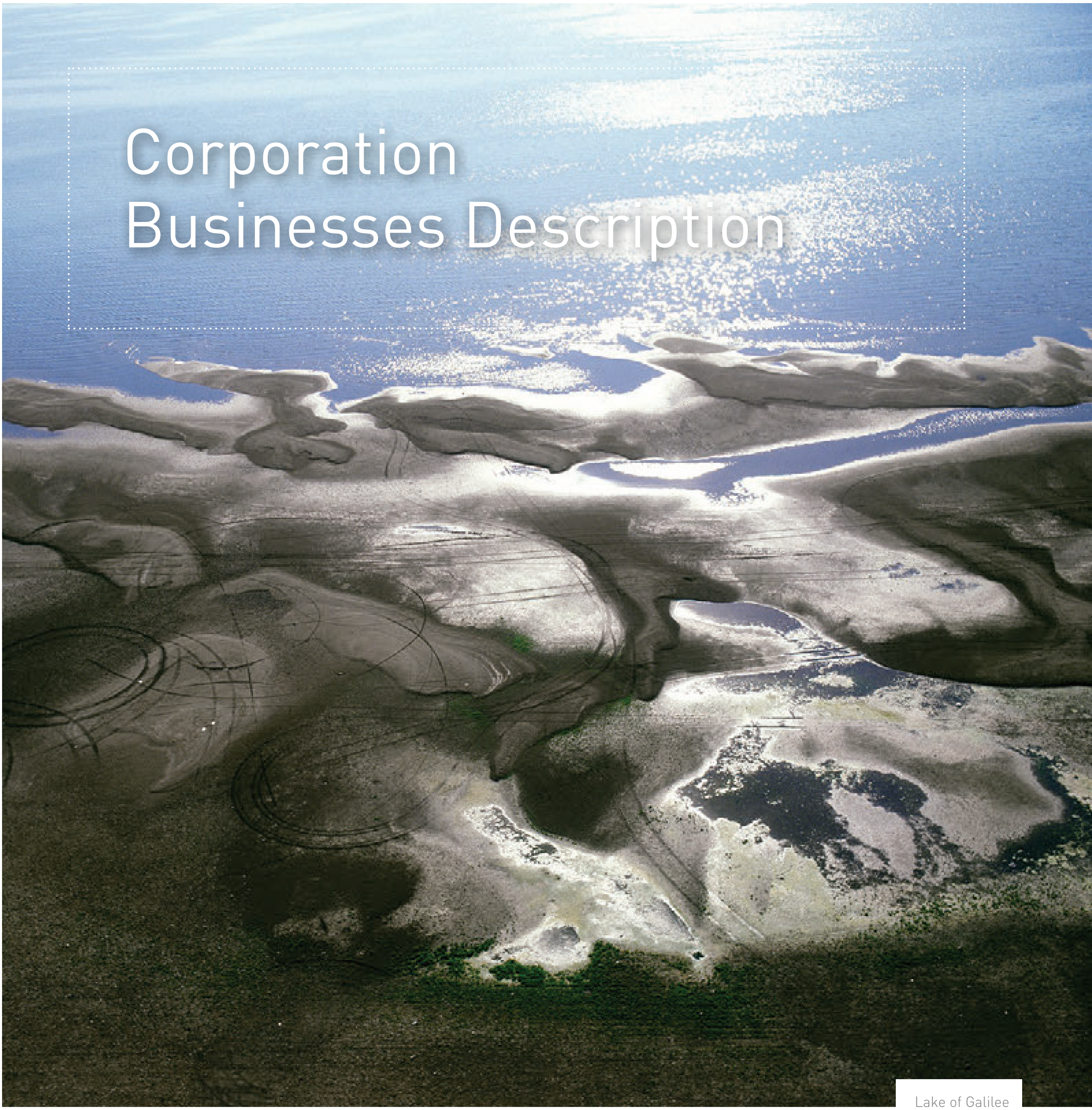
Corporation Businesses Description



Lake of Galilee

Comment regarding the implementation of the Securities Regulations provisions (Periodic and Immediate Reports) – 1970 ("Securities Regulations") in this report

According to regulation 8c of the Securities Regulations, the provisions of regulations 8 (b), 8a and 8b to the Securities Regulations do not apply to information in a periodic report of a corporation that consolidated or consolidated in a relative manner an insurer or that the insurer is an affiliated company, if this information refers to an insurer.

Most of Migdal Insurance and Financial Holdings Ltd.'s holdings are Migdal Insurance Company Ltd., which is an insurer, as defined in the Supervision Law of Insurance Businesses – 1981, and the main material company in the Group. The Group also includes companies which are active in the pension and provident area: Migdal Makefet Pension and Provident Funds Ltd. and Yozma Pension Fund for the Self Employed Ltd., which also hold an insurer license, and Migdal Makefet also holds a license of a provident funds' managing company.

This report, in respect of the Group's insurance, pension and provident businesses, is edited in accordance with the Supervision Regulations of Insurance Businesses (Report Particulars) – 1998, and in accordance with the circulars of the Commissioner of the Capital Market, Insurance and Savings in the matter of describing the Corporation's businesses in the insurance companies' Periodic Report, as published from time to time ("**the Commissioner Circulars**"). The Commissioner's circulars set the structure of the reporting and the information that will be included in insurance companies' Periodic Report. In this Report, the Company also implemented the Commissioner's provisions as to "Abbreviation of FS", that was issued pursuant to the publication of the ISA's position on this matter.

Chapter 1 to this report should be read together with its other parts, including the Notes to Financial Statements.

Future forecasting information contained in this report

In this report, the Company included future forecasting information regarding itself and other companies held by it, as defined in the Securities Law – 1968 (henceforth, "**the Securities Law**"). This mentioned information includes, inter alia, forecasts, objectives, estimates and evaluations that relate to future events or matters, whose fulfillment is uncertain and outside the Group's control. Future forecasting information in this report will be usually identified by statements such as "the Group foresees", "the Group expects", "the Group estimates", "the Group believes", "the Group intends to", "the Group is examining", "the Group plans to" and similar expressions.

Future forecasting information is not an empirical fact and is only based on the Company management's subjective estimate, which, among other things, based its assumptions on a the analysis of general information, which it had during the editing of this report, including public publications, studies and surveys, which did not commit to the correctness or to the integrity of the contained information, and whose preciseness was never examined by the Company's management independently.

Also, the fulfillment and/or non-fulfillment of this future forecasting information is uncertain and may be affected by factors that may no be assessed in advance and they may not be controlled by the Group, including risk factors that characterize the Group's activity as detailed this report, as well as developments in the general environment and the external factors that may affect the Company's activity, as detailed in this report.

Therefore, although the Company management believes that its expectations, as described in this report, are reasonable, the readers of this report are hereby warned that the actual future results may be different than those displayed in the future forecasting information contained in this report.

The future forecasting information contained in this report refers only to the date in which it was written, and the Company does not undertake to update or change this information, as additional information is brought to its attention regarding this mentioned information.

The amounts specified in this chapter and in the Board of Directors report are, usually, (unless specified otherwise) stated in NIS million.

The amounts stated in the Financial Statements are usually (unless specified otherwise) specified in NIS thousands.

The Group's businesses are in areas that require extensive professional knowledge, in which many professional terms are used, that are essential to the understanding of the Group's businesses. In order to present the Corporation's businesses as clearly as possible, the Group's businesses description includes the usage of these terms, whenever necessary, and explanation and clarifications. The description of insurance products and insurance coverages described in this chapter is only for the sake of this report, and the full binding conditions are the ones described in the insurance plan or in the Articles of Association of the relevant funds, and it does not constitute advising and shall not serve for interpreting insurance plans or Articles of Association as mentioned.

CHAPTER 1 - CORPORATION BUSINESSES DESCRIPTION

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Introduction to the Corporation Businesses Description chapter

1. Glossary - Definitions

This report will use the definitions detailed henceforth for the reader's convenience:

Advice and Marketing Law and/or Marketing and Advice Law and/or Pension Marketing Law	The Law of Supervision on Financial Services (Practicing Advice and Marketing of Pensionary Products) – 2005.
"Bachar Legislation"	The Competition Enhancement Act, the Marketing and Advice Law, The Provident Funds Law.
Bank Leumi and/or Leumi	Bank Leumi le-Israel Ltd.
Capital Markets Group and/or Migdal Capital Markets Group	Capital Markets Group and all the companies controlled by Migdal Capital Markets.
Commissioner of Insurance and/or the Commissioner and/or the Commissioner of Capital Markets	The Commissioner of Capital Market, Insurance and Savings.
The Company and/or the Corporation and/or Migdal Holdings	Migdal Insurance and Financial Holdings Ltd.
Companies Law	The Companies Law – 1999.
Competition Enhancement Act	The Competition Enhancement and Reduction of Centrality and Conflict of Interests on the Israeli Capital Market Act -2005.
Contribution Fees	The amounts deposited by beneficiaries (or deposited for them) in a pension or provident fund.
Designated Bonds	CPI-linked government bonds which the State issues for the insurance companies and the pension funds, with an interest and for a period that are set in advance. In life assurance – Hetz bonds and in pension – Meiron and Arad bonds are issued.
Earned Premium	Premium that refers to the reported year.
Eliahu Insurance and/or Eliahu	Eliahu Insurance Company Ltd.
Equity Regulations	Regulation of Supervision on Financial Services (Insurance) (Minimum Equity Required of Insurer) – 1998.
Fees	Amounts included in the insurance fees designated to cover the insurers' expenses.
Financial Product	As per its meaning pursuant to the Joint Investments Trust Law.

Free Investments	The share of the assets which is not invested in designated bonds.
General Fund	A pension fund that may not invest in designated bonds.
Generali	Assicurazioni Generali S.p.A.
The Group and/or Migdal Group	Migdal Holdings and the companies held by it.
Income Tax Regulations	Income Tax Regulations (Rules for the Approval and Management of Provident Funds) – 1964.
Institutional Organ	An insurer and a managing company, as defined in the Law of Supervision.
Insurance Benefits	Amounts that should be paid upon the occurrence of an insurance event according to the policy.
Insurance Fees	Total premium and fees paid by insureds to insurers pursuant to an insurance agreement (policy) that is not an investment contract.
Insurance Fund	An insurance fund which was approved as per the Provident Funds Law.
Insured and/or Beneficiary	A life assurance insured and a pension and provident funds beneficiary.
Investment Regulations and/or Regulations regarding Ways of Investment	Control of Financial Services (Provident Funds) (Rules of Investments that apply to Institutional Organs) Regulations 2012 and/or the Regulations of Supervision on Insurance Businesses (an insurer's ways of capital and funds investment and liability management) – 2001, as the case may be.
Law of Joint Investments Trust	The Joint Investments Trust Law – 1984.
Law of Practice Regulation	The Law of Practice Regulation in Investment Advising, Investment Marketing and Investment Portfolio Management – 1995.
Law of Supervision	The Law of Supervision on Financial Services (Insurance) – 1981.
Long Term Savings Assets	As defined in Clause 31 a to the Supervision Law.
Managing Company	A company that manages a pension fund or a provident fund.
Migdal Agencies	Migdal Holdings and Management of Insurance Agencies Ltd.
Migdal Capital Markets	Migdal Capital Markets (1965) Ltd.
Migdal Health	Migdal Health and Quality of Life Ltd.

Migdal Insurance and/or Migdal	Migdal Insurance Company Ltd.
Migdal Makefet and/or Makefet	Migdal Makefet Pension and Provident Funds Ltd.
Mivtach Simon	Mivtach Simon Insurance Agencies Ltd.
New Plans	Life assurance policies that are marketed as of 1.1.2004.
New Pension Fund	A pension fund established after 1.1.1995.
Old Pension Fund	A pension fund established prior to 1.1.1995.
Peltours	Peltours Insurance Agencies Ltd.
Pension Fund	A provident fund that pays annuities and is not an insurance fund.
Pensionary Product	As per its meaning following the Marketing and Advice Law.
Premium	The insurance fees, including fees.
Provident Fund	As defined in the Law of Supervision on Financial Services (Provident) (provident funds include educational funds).
Provident Fund Law	The Law of Supervision on Financial Services (Provident) – 2005.
Securities Law	The Securities Law - 1968.
Sagi Yogev	Sagi Yogev Insurance Agencies (1988) Ltd.
Shaham	Shaham Insurance Agencies (1977) Ltd.
TACC Law	Traffic Accident Casualty Compensation Law - 1975 ("TACC").
Yozma for Self-Employed	Yozma Pension Fund for Self-Employed Ltd.

Part A – Group Activity and the Description of its Businesses Development

2. Group activity and the description of its businesses development

2.1 General

Migdal Insurance and Financial Holdings Ltd. was incorporated in Israel on August 13th, 1974 under the name "Leumi Insurance Holdings Ltd.", and is a holding company.

The Corporation holds:

- Migdal Insurance Company Ltd. ("**Migdal Insurance**" or "**Migdal**") (100%) and its subsidiaries, through which the Group performs its insurance, pension and provident activity.
- Migdal Capital Markets (1965) Ltd. ("**MCM**") (100%)[1] and its subsidiaries, through which the Group performs its financial services activity.
- Migdal Health and Quality of Life Ltd. ("**Migdal Health**") (100%), which concentrates the non-insurance activity of the Group in the area of health and quality of life services as well as other services interfacing with the Group's activities, and holds several companies carrying out these activities, and whose activity, as of the publication of the report, is non-material[2].
- Mivtach Simon Agencies Management Ltd. ("**Mivtach Management**") (100%), which concentrates all of the other non-insurance activity in other areas related to the Group activities, and holds several companies which carry out these activities and their activities, as of the publication of the report, is non-material[3].

The Company shares are traded in the Tel Aviv Stock Exchange ("**TASE**").

Transfer of control in the Company – up until October 29th, 2012, the Company's controlling shareholder was Generali, which held, directly and indirectly[4], 727,057,341 ordinary shares of NIS 0.01 each, constituting 69.135% of the issued and fully paid share capital of the Company ("**Control shares**") (Generali and Generali companies which held control shares shall be referred to as "**Generali Group**"). At that time, Generali transferred the control shares[5] to Eliahu Insurance Company Ltd. ("**Eliahu Insurance**" or "**Eliahu**").

Mr. Shlomo Eliahu and Ms. Haya Eliahu are the final holders of Eliahu Insurance, inter alia, via the companies Shlomo Eliahu Holdings Ltd. and Eliahu Brothers Trusteeship and Investments Company Ltd., fully owned by them[6]. Upon the transfer of control shares, the new controlling shareholder of the Company is Mr. Shlomo Eliahu ("**controlling shareholder**").

As the Company was informed by Eliahu Insurance, 315,496,828 Company ordinary shares of NIS 0.01, which constitute approx. 30% of the issued and fully paid share capital of the Company ("**pledged shares**") were pledged by Eliahu Insurance in favor of Bank Leumi as a guarantee for the liabilities taken by Eliahu Insurance

[1] Until December 31st, 2010, MCM was held through Migdal Investments Management 2001 Ltd. (whose name was changed to Migdal Health).

[2] The activities of the held companies are non-material and their results, as the case may be, are not attributed to sectors of activity. For specification regarding the companies held by Migdal Health, see Regulation 11 in the Chapter of Additional Details on the Corporation.

[3] The activities of the held companies held by Mivtach Management are non-material, as the case may be, are included within the financial services sector and/or not attributed to sectors of activity. For specification of the companies held by Mivtach Management, see Regulation 11 in the Chapter of Additional Details on the Corporation.

[4] Generali held shares in the Company directly and through two companies, Participatie Maatschappij Graafschap N.V and Participatie Maatschappij Transhol B.V.

[5] For details regarding Eliahu Insurance's holdings, see Clause 5.2 hereinafter.

[6] To the best knowledge of the Company, the shareholders of Eliahu Insurance Company Ltd. are: Mr. Shlomo Eliahu, holding 25.14% of capital and 98% of management shares, Ms. Haya Eliahu (holding 0.02% of capital and 2% of management shares), Shlomo Eliahu Holdings Ltd. (holding 61.7% of capital) and Eliahu Brothers Trusteeship and Investments Ltd. (holding 13.14% of capital). The shareholders of Shlomo Eliahu Holdings Ltd. are Mr. Shlomo Eliahu, holding 83.31% and Ms. Haya Eliahu, holding 16.69%. The only shareholder in Eliahu Brothers Trusteeship and Investments Ltd. is Shlomo Eliahu Holdings Ltd. (100%).

towards Bank Leumi, and for this purpose Eliahu Insurance transferred the pledged shares to Adad Trust Company Ltd. ("**the trustee**") (a trustee company of the law office)[7].

For additional details regarding the transactions that were conducted on October 29th, 2012 (the date upon which the control in the Company was transferred), see Clause 5.2 hereinafter, "**transactions in Company's shares**".

Within the completion of this transaction, Mr. Sergio Balbinot and Mr. Alessandro Corsi resigned from their position as Directors in the Company and in any other company of the Company in which any of them served as a Director.

Messrs. Shlomo Eliahu, Israel Eliahu and Ofer Eliahu were coopted as Directors in the Company. Mr. Shlomo Eliahu and Mr. Israel Eliahu were also coopted as Directors in Migdal Insurance, starting from October 29th, 2012.

See also the Company's Immediate Report issued on October 29th, 2012, Reference No. 2012-01-266412.

The sale of shares by Bank Leumi – as of December 31st, 2012 Bank Leumi held approx. 9.8% of the Company's issued capital.

As the Company was informed by Bank Leumi, on January 3rd, 2013 and January 7th, 2013 Bank Leumi sold 53,500,000 Company ordinary shares of NIS 0.01, constituting approx. 5.1% of the Company's issued and fully paid capital. See Bank Leumi's Immediate Reports dated January 3rd, 2013, Reference No. 2013-01-04302, and January 8th, 2013, reference No. 2013-01-008235.

For additional details regarding the transactions carried out by Bank Leumi in Company shares, see Clause 5.2 hereinafter, transactions in Company's shares.

After this sale, as of January 8th, 2013, to the Company's best knowledge, Bank Leumi holds approx. 49,505,104 Company ordinary shares of NIS 0.01, constituting approx. 4.7% of the Company's issued and fully paid capital, see the Company's Immediate Report dated January 8th, 2013, Reference No. 2013-01-008517[8].

2.2 The Group's holdings structure diagram

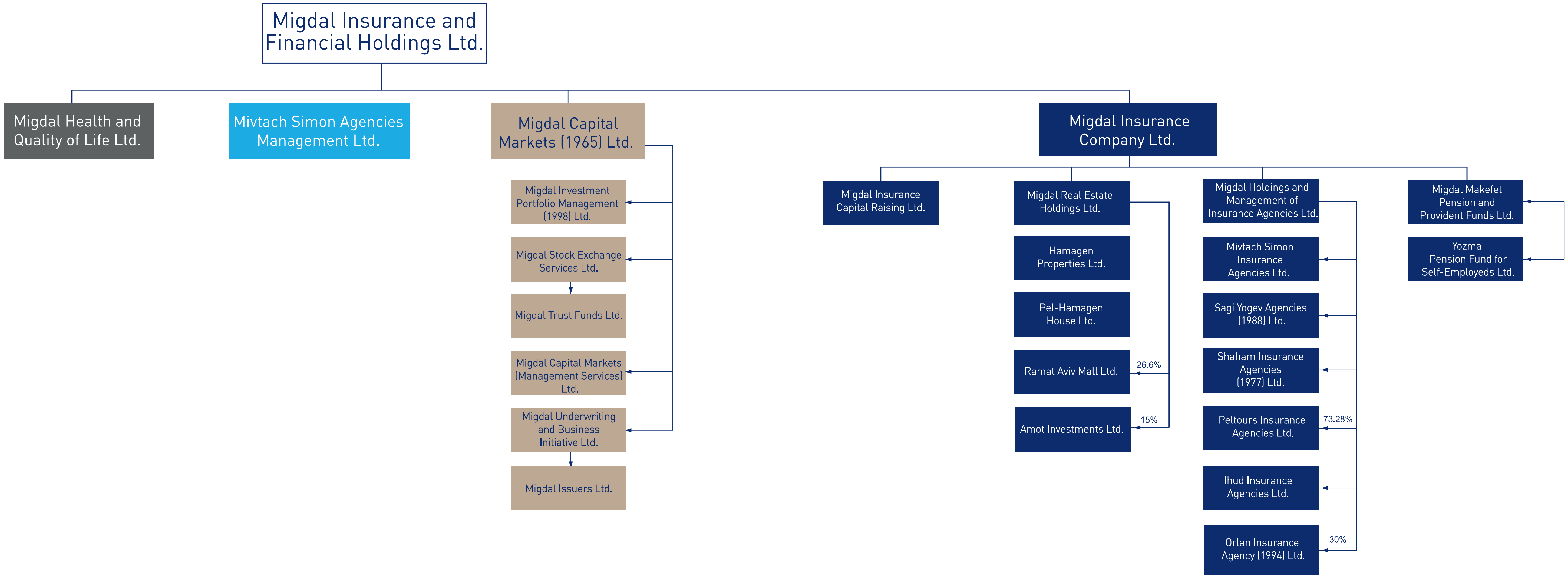
Enclosed please find a schematic diagram of the Company's main holdings, just before the Report's publication.

A full list of the Company's subsidiaries and affiliated companies as of the date of the report is detailed in the chapter Additional Details regarding the Corporation, within Regulation 11.

[7] The trustee submitted to the Company an annullable power of attorney, empowering Eliahu Insurance to participate in all the Company shareholders meetings (annual and extraordinary) and vote in these meetings in respect of the above mentioned shares. The power of attorney may be cancelled via a written notification by the trustee and / or Bank Leumi to the Company.

[8] There is a historic difference between the Company's books and those of Bank Leumi regarding the quantity of shares held by Bank Leumi, and this is a negligible difference.

Group Holdings Structure
December 31st, 2012



Notes:

1. The holdings structure includes the main companies in the Group. For additional details regarding holdings in subsidiaries and affiliated companies as of December 31st, 2012, see also Regulation 11 to the Additional Data on the Corporation.
2. For the control structure in Migdal Holdings, see Clause 2.1 to the Corporation Businesses Description Report.
3. The companies described herewith are held at 100%, unless specified otherwise.

2.3 The Group's businesses description

The Group operates in the areas of insurance, pension and provident and in the area of capital market and financial services.

The Group's **insurance activity** is performed through Migdal Insurance.

The Group's **pension and provident activity** is performed through:

- Migdal Makefet Pension and Provident Funds Ltd. ("**Migdal Makefet**" or "**Makefet**") which manages the Group's new pension funds ("**Makefet Ishit**" and "**Makefet Complementary**"), as well as all of the Group provident funds.
- Yozma Pension Fund for the Self-Employeds Ltd. ("**Yozma for Self-Employeds**" or "**Yozma**"), which manages the old pension fund Yozma Pension Fund for Self-Employeds.

The Group's **financial services activity** is performed through Migdal Capital Markets.

Holding of insurance agencies - the Group also holds insurance agencies, mainly concentrating in Migdal Holdings and Management of Insurance Agencies Ltd. ("**Migdal Agencies**"), which is fully controlled by Migdal Insurance. These insurance agencies are engaged in life assurance and LTS, health and general insurance[9].

The activity of the insurance agencies in the area of life assurance, long term savings and health insurance, is mainly concentrated in Mivtach Simon Insurance Agencies Ltd. ("**Mivtach Simon**") and its subsidiaries, in Sagi Yogev Insurance Agencies (1988) Ltd. ("**Sagi Yogev**") and its subsidiaries, and in Shaham Insurance Agencies (1977) Ltd. ("**Shaham**").

The activity of insurance agencies in general insurance is carried out mainly by Peltours Insurance Agencies Ltd. ("**Peltours**") and its subsidiaries[10].

Related / interfacing activities – also, subsidiaries/related companies of the Company established and/or executed acquisition of companies/activities. Which provide related/interfacing services to the Group's activities, and these activities are non-material, see Clause 4.5 hereinafter.

Other investment activity - in addition, and as part of the activity in the areas of activity described hereinafter, the Group also deals with diversified investment activity which includes investments in securities, bonds and other financial assets (negotiable and non-negotiable), financing, credit, financial derivatives, real estate and holding of various companies which are engaged in areas related to insurance or to the Group's activities. The investment activity is performed mainly against various insurance reserves, as well as against the equity required for insurance businesses and capital surpluses of the Group's companies.

Risk management - the Company manages its areas of activity, using methods of risk management. In its activity, the Group emphasizes the management of risks to which it is exposed, in order to identify and assess the potential impact of these risks on the future financial condition of the Group companies and insureds. For additional details regarding risk management see Note 37 to the Financial Statements as well as Part G to this Report.

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[9] The results of the insurance agencies are included in other sectors of activity. One agency, Club 50 Insurance Agency Ltd. (Club 50 agency) (that the Company increased its holdings in it this year), is held via Migdal Health, for more details see also Clause 3.3.1 hereinafter.

[10] Peltours also has non-material activity in the area of health insurance.

3. Material changes in the Company business in the reported year until the publication of the report

3.1 Absorption of new business in general insurance

3.1.1 On November 18th, 2012 an agreement was signed between Migdal Insurance and Eliahu Insurance regarding the absorption of Eliahu Insurance's "new business in general insurance" as per its definition hereinafter of Eliahu Insurancee in Migdal Insurance, as described hereinafter ("**the agreement**"). The agreement was signed after the approval of the terms of engagement by the Company's and Migdal Insurance's Audit Committee and BoD on November 8th, 2012 and November 11th, 2012, respectively. The engagement was brought to the approval of these organs in the Company pursuant to the provisions of Regulation 1 (2) to the Companies Regulations (Reliefs in Transactions with Interested Parties) – 2000 ("**Relief Regulations**") since it is a transaction that may benefit both the Company and Migdal Insurance. For the Company's Immediate Report regarding this matter see the Immediate Report issued on November 12th, 2012 regarding the approval of an engagement in a transaction with the controlling shareholder of the Company that does not require the GM's approval, pursuant to regulation 37 a (5) to the Securities Regulations (Periodic and Immediate Reports) - 1970 and Regulation 1 (2) to the Relief Regulations, Reference Nos. 2012-01-277401 and 2012-01-277848), ("**Immediate Report**"). Furthermore, see also the Company's Immediate Reports dated October 16th, 2012, Reference Nos. 2012-01-257034 and 2012-01-257364).

3.1.2 Within the agreement, Eliahu Insurance undertook to strive and do anything necessary so that new policies to customers insured by Eliahu Insurance in the area of general insurance, whose insurance period starts after January 1st, 2013 ("**new policies**", **Eliahu customers**", and "**new business in general insurance**", respectively) shall be signed with Migdal Insurance in 2013, and transfer to Migdal Insurance (subject to the law) any requested business information and perform any requested action in order to ensure continued and immediate production of new policies of Eliahu customers in Migdal Insurance.

3.1.3 Pursuant to the agreement, the new business in general insurance shall be against no consideration from Migdal Insurance to Eliahu Insurance, unless such consideration is agreed upon in the future, as set forth in Clause 3.1.6 hereinafter.

3.1.4 Pursuant to the agreement, as of January 1st, 2013, the following actions were taken:

(a) Eliahu Insurance transferred to Migdal Insurance the list of all the agents with whom Eliahu Insurance is engaged in the area of general insurance ("**Eliahu agents**"), the agreements with them and any relevant ancillary information. Also, Eliahu Insurance and Migdal Insurance outlined the way Eliahu agents should be addressed with an offer to Eliahu customers to renew/sign in Migdal new policies (all or part thereof – as decided by Migdal Insurance), starting from January 1st, 2013, under the conditions set forth by Migdal Insurance, as set forth in the agreement. Accordingly, agreements were signed with Eliahu agents, that part of them were also Migdal Insurance agents, and they arranged the conditions regarding new business in general insurance. As detailed in the Immediate Report, the terms of engagement with Eliahu Insurance, Migdal Insurance has no commitment to engage in new policies and it will engage in new policies with Eliahu customers that it would choose to engage with,

with no undertaking for certain conditions, and also the engagement will be as per its discretion, including, when necessary, underwriting. It is also clarified, for the removal of doubt, that Migdal Insurance will not bear any liability vis-à-vis Eliahu agents and/or customers, referring to a period preceding the beginning of insurance in Migdal Insurance or referring to a policy not signed by Migdal Insurance.

(b) Migdal Insurance submitted for approval a new CMBI tariff for 2013, and the sale and renewal of Migdal Insurance CMBI, including renewals of new business in general insurance of Eliahu Insurance, is performed as per this tariff. In the property and homeowners lines, Migdal Insurance is working towards an interim period in both tariffs, until the systems are prepared and the agents are connected to Migdal's systems pursuant to the outline submitted to the MoF.

(c) Migdal absorbed about 40 employees who are working on the absorption of new business in general insurance.

(d) Migdal Insurance decided to use Eliahu Insurance's information systems for the activity of production and engagement vis-à-vis Eliahu agents in the lines of CMBI, comprehensive motorcar and homeowners. This system /serves as a front system vis-à-vis these agents, and the management of policies is performed on Migdal's systems, and is fed by compatible interfaces. In the other lines, activity is fully conducted in Migdal's systems. Accordingly, the terms of confidentiality and information security in respect of the computerization services that are granted, as set forth above, were outlined.

3.1.5 Enclosed please find data regarding Eliahu Insurance general insurance's scope of premium, based on the data provided in Eliahu Insurance's[11] FS (in NIS thousand):

Lines	**Gross premiums 1-9/2012**	**Breakdown of premiums 1-9/2012**	**Gross premiums 1-9/2011**	**Gross premiums 2011**	**Gross premiums 1-3/2012**
CMBI	322	49.1%	340	419	127
Casco	241	36.6%	235	283	101
Property lines	74	11.3%	71	84	33
Liability lines	20	3.0%	22	25	10
Total premiums	**657**	**100%**	**668**	**811**	**271**

[11] From Eliahu Insurance's Financial Statements, as they appear in the MoF website.

3.1.6 **Negotiations regarding Eliahu's payment**

(a) Pursuant to the agreement, as early as possible, and anyway by June 30th, 2013 (or another date agreed upon by the parties), Migdal Insurance (via the organs defined by its Audit Committee and BoD) and Eliahu Insurance, shall negotiate the payment in respect of new business in general insurance. It is hereby clarified that Migdal Insurance does not have to agree to any payment, and that in order to outline its position regarding this matter, Migdal Insurance may rely on all the relevant circumstances regarding the new business in general insurance, as they were prior to the engagement. Furthermore, and without derogating from the above, Migdal Insurance will implement any calculation method and/or evaluation, that will be defined by the competent organs, as per its sole discretion, and may determine the assumptions upon which any payment should be made, all as per its discretion and pursuant to the decisions of its competent organs.

(b) **If the parties agree about payment**, the transaction will be brought to the approval of the Company's and Migdal Insurance's competent organs as an "extraordinary transaction" with the controlling shareholder, as defined in the Companies Law – 1999 ("**the Companies Law**"), and the payment of the consideration will be subject to receiving all the required approvals as per the provisions of Clause 275 to the Companies Law.

(c) **If the parties do not reach a consent regarding payment** - if the parties do not reach a consent regarding payment or if the payment is not duly approved by the Company's and Migdal Insurance's competent organs by June 30th, 2013 (or another date, if the deadline is postponed with the parties' consent) ("**the last date for consent**"), then Eliahu Insurance's liabilities regarding the absorption of new business in general insurance shall stop being effective starting from the last date for consent, as well as:

(1) Migdal Insurance will give back to Eliahu Insurance the list of Eliahu agents given to it ("**the list**") and shall not keep any copy of the list. It is hereby clarified that giving back the list to Eliahu Insurance as set forth above:

- Will not undermine Migdal Insurance's right to financial results stemming from the execution of the absorption of new business in general insurance, both vis-à-vis Eliahu's customers and vis-à-vis Eliahu's agents; and

- For the removal of doubt, it will not undermine Migdal Insurance's right to address Eliahu customers and Eliahu agents and/or continue the commercial relations with them and/or offer Eliahu customers who bought new policies in Migdal Insurance to continue engaging with it for the acquisition of policies in the future.

(2) Eliahu Insurance will be entitled to negotiate with another insurance company as per its choice, without derogating to Migdal Insurance's rights set forth above, and for this purpose Eliahu insurance will be entitled to transfer to the other insurance company the list and all the information about Eliahu Insurance's agents and insureds as it had it as of December 31st, 2012, so that the other insurance company as set forth above may offer them to renew the policies with it starting from after the last date for consent and on. It is clarified that this Clause does not exempt Eliahu Insurance (or its Senior Officers

or controlling shareholders) from any duty that applies to them as per the Law towards Migdal.

(3) Migdal Insurance shall not pay any consideration to Eliahu and no other limits will apply to its activity (except the non-usage of the list) and Eliahu will have no complaint nor demand towards Migdal in respect of all the activities that were made as per above (or in relation with its termination) and/or in respect of not reaching a consent about the payment due to any reason and/or the non-approval of payment in the Company's and Migdal's competent organs due to any reason.

(d) As of the publication of this Report, the parties have not reached such agreements.

3.1.7 For additional details, see also Note 38 d to the FS.

3.1.8 **The agreement's provisions regarding indemnification**

Within the agreement it was agreed that Eliahu Insurance shall indemnify Migdal Insurance (as per the set mechanism) in respect of any liability that will apply to Migdal Insurance or a claim or demand that will be filed against it (including fees and other reasonable expenses in this regard) or any damage that will be incurred by it in respect of one or more of these cases: any liability or responsibility regarding Eliahu customers whose reason is prior to the date upon which any new policy is signed in Migdal Insurance; any liability or responsibility towards Eliahu agents that is not related with new policies or regarding Migdal Insurance's activity vis-à-vis the agents as to the new policies; regarding Eliahu employees – in respect of claims or arguments of any Eliahu employee who have not started being employed by Migdal Insurance, or the rights of Eliahu employees who have started being employed by Migdal Insurance, stemming from the period that preceded their employment in Migdal Insurance or in respect of any claim or argument of any employee who started being employed by Migdal, and which is based on their previous employment in Eliahu (such as claims of continuity, sequence, change in wage conditions, etc.); any other liability or responsibility towards a third party whose reason or origin is in a period prior to January 1st, 2013; any other exposures of Migdal Insurance in respect of Eliahu's activity in the past or in the future.

3.2 **Second tier capital raising**

In the reported period, Migdal Insurance Capital Raising Ltd. ("**the issuing company**"), a subsidiary (100%) of Migdal Insurance, performed the following private issuances to classified investors:

3.2.1 An issuance of 500,000,000 bonds (Series A) par value, of NIS 1 par value each, against the total amount of NIS 500 million, performed in January 2012.

3.2.2 An issuance of 324,656,000 bonds (Series B) par value, of NIS 1 par value each, against the total amount of NIS 324.6 million, performed in December 2012.

(Series A and Series B bonds shall be referred to as "**the bonds**").

The bonds were rated as Aa2 by Midroog Ltd.

The bonds were issued pursuant to the content of the trust deed signed between the issuing company and Reznik, Paz, Nevo Trustees Ltd. "**trust deed**") and were registered for trading in the TACT-institutional system.

The consideration of the bonds issuance was deposited at Migdal Insurance, and it serves as hybrid second tier capital in Migdal Insurance, see Note 7e to the Financial Statements. Migdal Insurance undertook to bear the payment of all the amounts that will be required for the payment of bonds to their holders.

The balance of deferred issuance expenses as of December 31st, 2012 totals approx. NIS 3.7 million, see Note 24 e to the Financial Statements.

For additional details regarding the terms of bonds and trust deed, see Note 24 e to the Financial Statements, as well as the Company's Immediate Reports dated January 2nd, 2012, Reference No. 2012-01-003681 and December 30th, 2012, Reference No. 2012-01-323316.

3.3 Agreements for the acquisition of rights/activities

3.3.1 The acquisition of rights in 50 Plus Ltd.

In November 2012 the transaction for the acquisition of the balance of rights in 50 Plus Ltd. ("**50 Plus**") was completed, such that Migdal Health increased its share in this company from 50% to 100%, and as of that date it fully controls this company. The increase of Migdal Health's share in 50 Plus is pursuant to the Group's plan to increase its involvement in the area of the Third Age, including the development and concentration of various services and products to the Third Age population. See the Company's Immediate Report dated October 18th, 2012, reference No. 2012-01-259395.

3.3.2 Pilat transaction

In February 2013 a subsidiary of the Group, Hi-Capital Ltd. ("**Hi-Capital**"), held by Mivtach Management, acquired the activity of Pilat (Israel) Ltd. ("**Pilat**"). Within the activity acquisition, Hi-Capital undertook to absorb some of Pilat's workers. Pilat engages in the area of providing advising services in the area of human capital, and in August 2012 a temporary liquidator was appointed for it. The activity's acquisition was performed within Pilat's liquidation procedures. Migdal Holdings extended a loan to Mivtach Management for the acquisition's financing, see the Company's Immediate Report dated November 11th, 2012, Ref. No. 2012-01-276528[12].

4. The Group's areas of activity

The Group operates in the areas of insurance, pension and provident and in the area of capital market and financial services. The Group's key areas are as follows:

4.1 The area of life assurance and long term savings (area A)

The area of life assurance and long term savings includes the lines of life assurance, pension and provident, and it mainly focuses on savings for retirement (under various types of insurance policies, pension funds and provident funds including

[12] The amount that was extended by Migdal Holdings to Mivtach Management, was extended as a loan from Mivtach Management to Hi-Capital. In addition, in June 2012 Mivtach Management extended a loan of NIS 1.6 million to Hi-Capital, whose consideration was converted in February 2013, into Hi-Capital shares, such that in February 2013 Mivtach Management holds approx. 70% of Hi-Capital's share capital. It should be noted that the terms of the loan included a right for Mivtach Management to convert the loan to shares as per its discretion, therefore starting from June 2012, Hi-Capital is considered as a consolidated company.
In addition to the payment for the acquisition of Pilat, Hi-Capital extended to Pilat Group Ltd., which is a public company, a loan in the amount of NIS 1.6 million, to be paid in July 2013, and may be converted into Pilat Group shares (at approx. 19%). In February 2013 the Court approved the creditors arrangement between Pilat Group and its creditors, among them Hi-Capital, pursuant to Clause 350 to the Companies Law.

educational funds[13]), as well as on insurance coverages for various risks, such as: death, disability and PHI.

This area is the main area of activity in which the Group is engaged, which, in 2012, constitutes about 87%[14] of the total insurance premiums and contributions fees.

In the reported year, two material issues that came into effect on January 2013 were regulated, and they would have a material impact on this area, the reform in management fees and the regulation regarding annuity coefficients, as described in Clauses 9.2.8 and 9.2.9 hereinafter. In light of this changing reality, the Company re-examined its deployment regarding its business strategy, and regarding this issue see Clause 57 to Part E hereinafter.

4.2 **The area of health insurance (area B)**

This area focuses both on health insurances that entitle for financial compensation in respect of dread diseases and LTC, and on health insurances that provide indemnification for medical expenses, while most of the proposed coverages under this frame are: medical insurances of the type "surgery", "transplants", medications, special treatments abroad, dental insurance, personal accidents for insurance periods exceeding one year, riders, etc.

4.3 **The area of general insurance (area C)**

The area of general insurance includes all the insurance lines except life assurance and long term savings, and long-term health insurances. The main insurance coverages granted in this area are property insurance and liability insurance.

Under **the area of general insurance**, the Group is active in the following lines of activity:

4.3.1 **The area of CMBI** - focuses on coverage whose acquisition by car owners or drivers is mandatory under the Law (Motor Vehicle Insurance Ordinance (revised version) - 1970, which provides coverage for bodily injuries (to the car driver, passengers or pedestrians) as a result of using motor vehicles as per the law of compensation for car accident victims – 1975.

4.3.2 **The casco area** - focuses on coverage of property damages to the insured car and coverage of property damages that the vehicle might cause to a third party.

4.3.3 **The area of other general insurance lines** - includes other general insurance lines that are not vehicles. Focuses mainly on property insurance (that are not vehicles) and liability insurance, and is characterized by coverages for specific risks or "packages" for houses, businesses etc., which combine several insurance coverages and also includes the health lines which provide short-term coverages, such as personal accidents.

4.4 **The area of financial services (area D)**

This area mainly includes financial asset management services (mutual funds management, portfolio management and hedge funds management) and investment marketing[15] (marketing of structured products and hedge funds), execution services on the Stock Exchange and in regulated markets (brokerage) and custody, underwriting services and investment banking.

[13] Educational funds allow beneficiaries to save monies for training purposes and are considered both a pensionary product and a financial product, and the amounts accrued may be withdrawn after a membership of six years.

[14] The premium rate stemming from life assurance businesses out of total insurance premiums is approx. 78%.

[15] The "investment marketing" service is similar to the "investment advising" service, but the service provider has an affinity to institutional organs or is a related entity to institutional organs. Since institutional organs operate under Capital Markets Group, it renders "investment marketing" services and not "investment advising" services.

4.5 **Other**

The Group has related/interfacing activities in the following issues:

4.5.1 **Holding insurance agencies** – mainly via Migdal Agencies, operating in life assurance and LTS, in health insurance and general insurance, see Clause 2.3 above.

4.5.2 **Related activities/services**

(a) Migdal Health, via the companies held by it, conducts related/interfacing activities to the Group's activities, mainly in the area of quality of life and Third Age[16]. The activities of these companies are not material and their results are not attributed to areas of activity.

(b) Mivtach Management, via the companies held by it, also conducts related/interfacing activities to the Group's activities, mainly in the area of providing services in the area of HR, economic advising and marketing and integration of software and Internet solutions to HR[17]. The activities of these companies are not material and their results are included under the area of financial services and/or are not attributed to areas of activity, as detailed in the Note below.

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

5.1 **Investments in the Company's capital in the last two years until the publication date of this report**

In the last two years there were no investments in the Company capital, except for transactions in respect of issuing option warrants and their realization pursuant to long-term plans for Senior Officers in the Company and employees in the Group, see Note 22 to the Company's Financial Statements.

5.2 **Specification of the material transactions conducted by interested parties in the Company in the Corporation's shares**

Enclosed please find details regarding the material transactions executed in the Company's shares by interested parties in 2011, 2012 and in 2013 until the publication of this report.

[16] Migdal Health holds the following companies: BrainSpa Ltd. (at 50%), which is a company that engages in activities related to the development of programs and methods dealing with cognitive regression, 50 Plus Ltd. (at 100%), whose main activity is the management of a customers club for the Third Age, Club 50 Insurance Agency Ltd. (fully controlled (at 100%) by 50 Plus Ltd.), which is an insurance agency, Infomed – Medical Websites Ltd. (at 51%), whose main activity is the operation of an Internet website regarding health, and B-Well Quality of Life Solutions Ltd. (fully controlled (at 100%) by Infomed, engaging in healthy lifestyle and fitness.

[17] The companies held by Mivtach Management as of the date of this Report are: Hi-Capital Ltd. (at 70%), engaging in providing services in the area of HR, and which holds Talent HR Systems Ltd. (at 50%), Yevulim Financial and Business Consultations Company Ltd. (at 50%), dealing with economic and business advising, and Talent HR Systems Ltd. (at 25%), dealing with the marketing and implementation of software systems and Internet solutions for HR. Their activity is not material and their results are not attributed to lines of activity. In addition, Mivtach Management holds Arxcis Global Wealth Management Ltd., which engages in providing investment management services via portfolio managers. Its activity is not material, and its results are included within the area of financial services.

Holder's name	Transaction type	Transaction date	Quantity and type of securities	Share price in NIS	Transaction amount in NIS million	Rate in capital and voting in %
Generali Group	Transfer of shares in off-Exchange transaction (1)	29.10.2012	727,057,341 ordinary NIS 0.01 shares	4.86	3,532.27	69.135
Eliahu Insurance Company Ltd.	Transfer to a trustee (2)	29.10.2012	315,496,828 ordinary NIS 0.01 shares	-	-	30
Eliahu Insurance Company Ltd.	Transfer of shares in off-Exchange transaction (3)	1.1.2013	700,613 ordinary NIS 0.01 shares	-	-	-
Bank Leumi	Share transfer (4)	3.1.2013	48,250,000 ordinary NIS 0.01 shares	5.72	275.99	4.6
Bank Leumi	Share transfer (5)	7.1.2013	5,250,000 ordinary NIS 0.01 shares	5.72	30.03	0.5

(1) On October 29th, 2012 a transaction in which Generali Group transferred the control shares to Eliahu Insurance was completed. As the Company was informed, the amount paid against the transferred shares is Euro 705 million. Prior to the acquisition, Eliahu Insurance held 2,110,968 Company ordinary shares, which constitute 0.201% in the Company, see the Company's Immediate Report dated October 29th, 2012, Reference No. 2012-01-266463. In addition, Eliahu Insurance, within Eliahu Insurance's profit participating portfolio assets, held 700,613 Company ordinary shares of NIS 0.01, and these were transferred to Harel Insurance Company Ltd., as described in Note (3) below.

(2) As the Company was informed by Eliahu Insurance, Eliahu Insurance pledged 315,496,828 Company ordinary shares of NIS 0.01 in favor of Bank Leumi le-Israel Ltd., which constitute approx. 30% of the Company's issued and paid up capital as a guarantee for the liabilities taken by Eliahu Insurance towards Bank Leumi, and for this purpose, Eliahu Insurance transferred the pledged shares to Adad Trust Company Ltd., see the Company's Immediate Report dated October 29th, 2012, Reference No. 2012-01-266412.

(3) As the Company was informed by Eliahu Insurance, Eliahu Insurance transferred 700,613 Company ordinary shares of NIS 0.01. This share transfer was within the completion of a transaction pursuant to which Eliahu Insurance sold all its activity in the area of life assurance and health insurance to Harel Insurance Company Ltd. ("**Harel**"), and within this transaction, Eliahu Insurance's profit participating portfolio assets (that the Company shares were part thereof as described above) were also endorsed from Eliahu Insurance to Harel.

(4) As the Company was informed by Bank Leumi, on January 3rd, 2013 Bank Leumi sold shares to several entities, as described above. Bank Leumi informed that it reached an understanding with another buyer, regarding the sale of additional Company shares, see below. As the Company was informed by Bank Leumi, the Bank undertook towards the buyers that except the additional sale to the buyer as set forth above, it will not sell Company shares until April 8th, 2013. See the Immediate Report issued by Bank Leumi on January 3rd, 2013, Reference No. 2013-01-004302.

(5) As the Company was informed by Bank Leumi, on January 7th, 2013 Bank Leumi sold the quantity of shares mentioned above to the other buyer mentioned above. The quantity constitutes approx. 0.5% of the Company's issued and paid-up capital. See the Immediate Report issued by Bank Leumi on January 8th, 2013, Reference No. 2013-01-008235, as well as the Immediate Report issued by Bank Leumi on January 8th, 2013, Reference No. 2013-01-008517.

6. Dividend distribution

6.1 Henceforth are details regarding dividends paid by the Company in the last two years:

Date of declaration on dividend[18]	General meeting approval date	Distribution date	Sum in NIS million
26/3/2012	24/4/2012	15/5/2012	150
15/3/2011	28/4/2011	28/4/2011	150

All dividends distributed as mentioned are cash dividends. The distribution of the abovementioned dividends was made from the profits and distributable surpluses, and did not require a Court's approval.

6.2 **External restrictions in dividend distribution and equity requirements**
In the last two years, no external restrictions affected the Company's ability to distribute dividends, and the Company knows of no external restrictions that may affect its future distribution of dividends, except for the general legal restrictions which apply to dividend distribution under the Companies Law and except external restrictions regarding the ability of Migdal Insurance and managing companies in the Group to distribute dividends, as set forth below.

The regulations and circulars issued by virtue of the Supervision Law and the Provident Law affect Migdal Insurance's ability as an insurer, or the ability of managing companies to distribute dividend in cash. Apart from the general requirements of the Companies Law, there are restrictions under the legislative arrangements applied to insurers and managing companies, according to which insurers and managing companies may distribute a dividend only if their remaining equity after the dividend distribution totals at least half the equity required under such legislative arrangements. Also, there are provisions regarding the scope of liquid assets against the minimum equity required as well as provisions regarding assets that should be included within the capital surpluses.

For details regarding the restrictions on dividend distribution in the Group's institutional organs, and capital requirements from insurers (Migdal Insurance) as well as from managing companies in the Group, see Note 7 e to the Financial Statements.

[18] The said declaration date is the date of BoD decision, recommending to the General Meeting about a dividend distribution.

Part B - Financial Information Regarding the Company's Areas of Activity

7. Summary of the Group's activity results

This Chapter contains data regarding the results of the Group's activity. In addition to the data presented in this part, see the data below as well as in the BoD Report, Clause 1.3.

Following is a breakdown of **income for the period before tax** in the Group's Financial Statements as per the Group's areas of activity, as well as **income for the period** (NIS million).

	2012	2011	2010
Profit from life assurance and long term savings	95	407	787
Profit from health insurance	97	37	80
Profit (loss) from general insurance	112	(15)	141
Profit from financial services	11	19	72
Total profit before tax from areas of activity	**315**	**448**	**1,080**
Other (1)	34	62	86
Profit before tax	**349**	**510**	**1,166**
Income tax	122	213	384
Income for the period	**227**	**297**	**782**

Following is a breakdown of **comprehensive income for the period before tax** in the Group's Financial Statements as per the Group's areas of activity, as well as **comprehensive income for the period** (NIS million).

	2012	2011	2010
Comprehensive income from life assurance and long term savings	216	143	842
Comprehensive income from health insurance	102	28	84
Comprehensive income (loss) from general insurance	184	(96)	118
Comprehensive income from financial services	11	19	72
Total comprehensive income before tax from areas of activity	**513**	**94**	**1,116**
Other (1)	113	35	87
Comprehensive income before tax	**626**	**129**	**1,203**
Income tax	221	83	393
Comprehensive income for the period	**405**	**46**	**810**

(1) The Other item mainly contains the results of the Group insurance agencies' activity, related activities / activities that interface with the Group activity, which take place under Migdal Health and Mivtach Management in non-material volumes, as well as net investment income (including income from associates) that are not imputed to the areas of activity.

For additional details regarding the income for the period and comprehensive income for the period as per areas of activity, see Notes 3 b, 3 c and 3 d to the Financial Statements. For explanations regarding the development in income for the period and comprehensive income for the period, including details as per quarters, see Clauses 1.2, 1.3 and 1.7 to the BoD Report.

8. Financial information according to the Group's areas of activity

Following are key financial data divided by areas of activity between 2010 and 2012 (in NIS million).

8.1 Area A – life assurance and LTS (long term savings) area

Financial information (in NIS million)

Life assurance businesses

	2012	2011	2010
Gross earned premiums	7,357	6,847	6,245
Premium less reinsurance	7,199	6,667	6,109
Income for the period before tax (1)	5	318	717
Comprehensive income for the period before tax	119	56	772
Minority share in profit before tax	-	-	-

	31.12.2012	31.12.2011
Liabilities in respect of non-yield dependent insurance and investment contracts (gross)	24,488	23,094
Liabilities in respect of yield dependent insurance and investment contracts (gross)	58,799	50,317
Total insurance liabilities (gross)	83,287	73,411

Pension fund management

	2012	2011	2010
Collected contribution fees	4,386	3,919	3,418
Revenues from management fees (2)	286	252	223
Income for the period before tax (3)	71	68	59
Comprehensive income for the period before tax	78	-66	59

	31.12.2012	31.12.2011
Total managed assets	32,305	27,173

Provident fund management

	2012	2011	2010
Collected contribution fees	1,765	1,689	1,627
Revenues from management fees	140	143	146
Income for the period before tax	19	21	11
Comprehensive income for the period before tax (4)	20	21	11

	31.12.2012	31.12.2011
Total managed assets	14,559	13,580

(1) In the Group's businesses there are additional income/expenses from savings management monies, which are included within the profit before tax detailed in the aforementioned data, and which were not detailed in other items of such data. These income/expenses include management fees in profit participating policies, and income/expenses stemming from financial spread in guaranteed yield policies (the difference between investment income and investment income imputed to insureds). These income/expenses are included in various clauses in the life assurance business report.

(2) Income from management fees are less sale incentives for beneficiaries.

(3) Profit from pension funds management also includes payments made by Makefet and Yozma for the Self-Employed, less Migdal's operational and marketing expenses in respect of these businesses. For further details, see Clause 11.2 in Part C hereinafter.

(4) Profit from provident funds management in 2010 also includes the payments made by the managing companies (before the provident merger) Migdal Gemel and Migdal Platinum, less Migdal's operational and marketing expenses in respect of such transactions. For further details, see Clause 11.2 in Part C hereinafter.

For details regarding the developments in the data presented in the financial information in the area of life assurance and long term savings, including the development of premiums and contribution fees, development of income from management fees in pension funds and provident funds, and development of profit (loss) before tax, see Clause 1.3.2 in the BoD Report, and Notes 3 c, 25 and 27 to the Financial Statements.

8.2 Area B – health insurance area

Financial information (in NIS million)

	2012	2011	2010
Gross earned premium	692	615	556
Premium less reinsurance	630	552	510
Income for the period before tax	97	37	80
Comprehensive income for the period before tax	102	28	84

	31.12.2012	31.12.2011
Insurance liabilities (gross)	1,616	1,389

Hereunder are additional details regarding premiums, profit (loss) for the period, comprehensive income (loss) for the period and insurance liabilities according to the main products:

Long term care insurance	2012	2011	2010
Gross premiums	201	181	161
Premium less reinsurance	195	173	155
Profit (loss) for the period before tax	3	(56)	(10)
Comprehensive income (loss) for the period before tax	4	(57)	(9)

	31.12.2012	31.12.2011
Insurance liabilities (gross)	1,132	936

Medical expenses	2012	2011	2010
Gross premium	294	259	238
Premium less reinsurance	266	231	223
Income for the period before tax	52	61	55
Comprehensive income for the period before tax	55	55	57

	31.12.2012	31.12.2011
Insurance liabilities (gross)	212	191

Other	2012	2011	2010
Gross premium	197	176	157
Premium less reinsurance	169	148	132
Income for the period before tax	42	32	35
Comprehensive income for the period before tax	43	30	36

	31.12.2012	31.12.2011
Insurance liabilities (gross)	272	261

For further details about the developments in the data presented in the financial information in the area of health insurance, including the development of premiums, profit (loss) for the period and comprehensive income (loss) before tax, see Clause 1.3.3 to the BoD Report, and Notes 3 b and 25 to the Financial Statements.

8.3 **Area C – general insurance area**

Financial information (in NIS million)

	2012	2011	2010
Gross premium (including fees)	1,406	1,446	1,403
Premium less reinsurance	952	962	922
Profit (loss) for the period before tax	112	(15)	141
Comprehensive income (loss) for the period before tax	184	(96)	118

	31.12.2012	31.12.2011
Insurance liabilities (gross)	3,709	3,866

Following are further breakdowns regarding premiums, profit (loss) for the period and comprehensive income (loss) for the period in the following sub-lines: compulsory motorcar bodily injury (CMBI), property motorcar, and other general insurance lines.

For further details about the developments in the data presented in the financial information in the area of general insurance, including the development of premiums, profit (loss) for the period and comprehensive income (loss) for the period before tax, see Clause 1.3.4 to the BoD Report, and Notes 3 d and 25 to the Financial Statements.

8.3.1 Compulsory motorcar bodily injury (CMBI) line
Financial information (in NIS million)

	2012	2011	2010
Gross premium (including fees)	266	258	255
Premium less reinsurance	261	253	249
Income for the period before tax	104	57	93
Comprehensive income for the period before tax	142	14	81

	31.12.2012	31.12.2011
Gross insurance liabilities	1,427	1,457

Following is the composition of profit before tax in CMBI between 2010 and 2012 (in NIS million):

	Profit in respect of the open years(1)	Profit in respect of the underwriting year released in the reported year(2)	Adjustments in respect of the underwriting years released in previous years(3)	Activity not included in the calculation of reserves(4)	Total income for the period (5)
2012	14	41	52	(3)	104
2011	5	23	33	(4)	57
2010	24	29	42	(2)	93

(1) This column includes the actual investment profits / (losses), while the accrual was imputed 3% real annual yield, as well as o cover of losses from previous years (in respect of underwriting years 2010 and 2011).

(2) Underwriting years released in reported years 2012, 2011 and 2010 are 2009, 2008 and 2007, respectively. The increase in profit in 2012 vs. 2010 and 2011 was affected by an increase in investment profits, and an update of the actuarial evaluation.

(3) Adjustments due to a change in actuarial valuation of outstanding claims and changes in investment profit in respect of these reserves. The increase in adjustments in 2012 vs. 2010-2011 was affected by an increase in income from investments and an update of the actuarial evaluation.

(4) Losses in respect of the activity excluded from the reserve calculation in 2010 to 2012 stem from expenses which, under the rules, cannot be imputed to accrual.

(5) The residual insurance losses ("**Pool**") reduced the income for the period in 2012 by approx. NIS 8 million, in 2011 by approx. NIS 20 million, and in 2009 by about NIS 25 million.

Following are aggregate financial data in CMBI between the underwriting years 2005 and 2012 (in NIS million):

	Open underwriting years				Closed underwriting years			
Underwriting year	**2012**	**2011**	**2010**	**2009**	**2008**	**2007**	**2006**	**2005**
Gross premium	271	256	256	308	325	297	319	343
Aggregate profit (loss) in respect of underwriting year	1	3	10	63	67	56	85	108
Surplus of income over expenses (accrual)	6	6	23	-	-	-	-	-
Investment income out of aggregate profit / surplus in respect of underwriting year	8	22	40	80	91	85	96	96

The enhanced competition, as well as the tariff reduction significantly reduced the profitability embedded in this area. In addition, the volatility in profits from investments substantially affects the development of profit and accrual throughout the years.

The decline in accrual and aggregate profit in the open underwriting years vs. the aggregate profit in the closed underwriting years, mainly stems from the fact that 3% real annual yield imputed in the open years, as well as investment profits, which are, as mentioned, a key factor in long-term lines' profitability, have not yet accumulated. Another reason that may be accountable is the price reduction during the period due to competition in the line. It should be noted that the reserves in the CMBI line are not capitalized – see Note 37 b. 3. c to the Financial Statements.

8.3.2 **Property motorcar (Casco) insurance line**
Financial information (in NIS million)

	2012	2011	2010
Gross premium (including fees)	351	371	357
Premium less reinsurance	350	357	357
Profit (loss) for the period before tax	(13)	(45)	5
Comprehensive income (loss) for the period before tax	(8)	(50)	4

	31.12.2012	31.12.2011
Insurance liabilities (gross)	230	244

8.3.3 **Other general insurance lines**
Financial information (in NIS million)

	2012	2011	2010
Gross premium (including fees)	790	817	791
Premium less reinsurance	342	338	317
Profit (loss) for the period before tax	20	(27)	43
Comprehensive income (loss) for the period before tax	50	(59)	33

	31.12.2012	31.12.201
Insurance liabilities (gross)	2,051	2,165

Additional information
In other general insurance lines, the total premiums originated from insurance policies as to which a specific contract was purchased in 2012 for reinsurance coverage at over 90% is approx. NIS 177 million in gross terms, and approx. NIS 4 million in retention terms.
Following are data presented by division between property lines and liability lines:

Property lines

	2012	2011	2010
Gross premium (including fees)	535	550	530
Premium less reinsurance	156	160	146
Profit (loss) for the period before tax	7	1	6
Comprehensive income (loss) for the period before tax	10	(2)	5

	31.12.2012	31.12.2011
Insurance liabilities (gross)	578	675

Liability lines

	2012	2011	2010
Gross premium (including fees)	254	266	261
Premium less reinsurance	186	179	171
Profit (loss) for the period before tax	13	(28)	37
Comprehensive income (loss) for the period before tax	41	(58)	28

	31.12.2012	31.12.2011
Insurance liabilities (gross)	1,473	1,490

Following is the composition of income for the period before tax in liability insurance between 2010 to 2012 (NIS million):

	Profit (loss) in respect of the open years[(1)]	Profit (loss) in respect of the underwriting year released in the reported year[(2)]	Adjustments in respect of the underwriting years released in previous years[(3)]	Activity not included in the calculation of reserves[(4)]	Total profit (loss) for the period
2012	8	2	8	(5)	13
2011	(4)	(5)	(15)	(4)	(28)
2010	8	11	23	(5)	37

(1) This column includes the actual investment profits / (losses), while the accrual was imputed 3% real annual yield, as well as the cover for losses from previous years.

(2) Underwriting years released in the reported years 2012, 2011 and 2010 are 2009, 2008 and 2007, respectively. The loss released in respect of underwriting year 2009, vs. loss from underwriting year 2008, was affected by an increase in income from investments. Also, the decline in released profit in respect of underwriting years 2008 and 2009 vs. underwriting year 2007 was affected by an erosion in the underwriting profit.

(3) Adjustments due to a change in actuarial valuation of outstanding claims and changes in investment profit in respect of these reserves. Income in 2012 was affected by an increase in investment profit vs. 2011. The loss in 2011 was partly affected by a decrease in investment income, as well as by an update of the actuarial evaluation of outstanding claims in respect of old years.

(4) Loss in respect of the activity excluded from the reserve calculation stems from expenses which, under the rules, cannot be imputed to accrual.

Following is a specification of accrued financial data in liability insurances for the underwriting years 2005-2012 (in NIS million):

	Open underwriting years			Closed underwriting years				
Underwriting year	**2012**	**2011**	**2010**	**2009**	**2008**	**2007**	**2006**	**2005**
Gross premium	239	268	267	254	249	256	243	242
Aggregate profit (loss) in respect of underwriting year	(4)	(1)	3	11	(3)	1	38	42
Surplus of income over expenses (accrual)	17	15	5	-	-	-	-	-
Income from investments out of aggregate profit/surplus in respect of underwriting year	6	15	25	41	45	50	49	59

The decline in accrual in the open underwriting years vs. the aggregate profit in the closed underwriting years, partly stems from the fact that 3% real annual yield imputed in the open years, as well as investment profits, which are, as mentioned, a key factor in long-term lines' profitability, have not yet accumulated. Another reason that may be accountable is a certain decline in prices, as well as an increase in the actuarial estimate of the outstanding claims.

It should be noted that the reserves in the liability lines are not capitalized – see Note 3 7b. 3. c to the Financial Statements.

8.4 **Area D – financial services area**
Financial information (in NIS million)[(1)]

	2012	**2011**	**2010**
Revenues			
From external shareholders	198	231	305
From other areas of activity	11	5	4
Total revenues	**209**	**236**	**309**
Costs which do not constitute revenues of other areas of activity	191	219	
Costs which constitute revenues of other areas of activity	7	(3)	(4)
Total costs	**198**	**216**	**237**
Out of which goodwill amortization expenses	1	3	2
Income for the period before tax	**11**	**20**	**72**
Comprehensive income for the period before tax	**11**	**20**	**72**
Total assets in the balance sheet	**727**	**736**	**866**

	31.12.2012	**31.12.2011**
AUM	23,933	19,723

(1) The data of income, expenses and profit before tax include the results of the financial services activity performed in MCM, as well as the results of Arxcis Global Wealth Management Ltd., held by Mivtach Management and other revenues/expenses.

Part C – Description and Information on the Company's Areas of Activities

Area A – Life Assurance and Long Term Savings

9. General information about the area of life assurance and long-term savings

9.1 General

9.1.1 The Group engages in all the lines of life assurance and long term savings (LTS) – life assurance, various types of pension funds and provident funds, including training funds. In life assurance the Group is the largest in the sector, while in the line of pension, it is the second largest.

The area of life assurance and long term savings[19] mainly focuses on retirement period savings ("**the saving**"), as well as insurance coverage of various risks, such as death, disability and PHI ("**the risk**").

This area is characterized by vast regulation and considerable, frequent regulatory changes, which are not executed at once, which affect the area, and whose main goal is taking steps to refine the market, increase consumer awareness and enhance competition in the area.

9.1.2 **Shift of the savings monies from investments in designated bonds to free investments**

(a) **Life assurance**
Most life insurance plans sold until 1990 by insurance companies were guaranteed-yield (CPI-linked plus interest). The insurance company invested most of its reserves, mainly in designated bonds (Hetz bonds) guaranteeing CPI-linkage plus interest (between 4%-6.2%). The insurance company benefits from the difference created between the profits from investing in such bonds and its liabilities towards the insureds, as set forth in the insurance policies. This difference often ranges between 1%-1.2% of accrual ("**the spread**" and/or "**the financial spread**"). The remaining reserve is invested in free investments according to the limits set under the investment regulations. Such plans will be called "**guaranteed**-yield" or "**non-profit participating**".

Throughout the year, the Group redeemed, as per the MoF approval, part of the designated bonds in order to achieve surplus yields, and the reserves were invested in free investments as aforesaid. The Group cannot repurchase designated bonds in respect of some of the reserves redeemed by it, as said, therefore the Group's exposure under free investments has increased.

In 1992, after gradual reduction during the preceding two years, the issuance of designated bonds to new insurance plans has been entirely discontinued[20].

As of 1991, the suggested insurance plans are not guaranteed-yield. The yield to which the customer is entitled is set based on the results that the insurer's investments generate from the policyholders' savings ("**profit participating portfolio**" or "**profit participating**" or "**yield-guaranteed plans**") less management fees from accrual.

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[19] The training funds included in the provident funds line in life assurance and LTS, allow members to accumulate monies for training purposes and enjoy tax benefits. The monies accrued in training funds may be withdrawn for training purposes after 3 years of fund membership, and after 6 years of fund membership they can be withdrawn for any purpose. Hence, training funds can be regarded as medium-term savings before retirement age.

[20] In respect of the plans sold until that time, the State continues to issue designated bonds also in respect of the monies which, under the insurance plan terms, may be deposited in these policies after the change.

For data concerning profit participating and guaranteed-yield insurance plans, as reflected in the Group reserves, see Clause 11.1 hereinafter.

(b) **Pension funds**
In the past, the old pension funds enjoyed the issuance of designated bonds which, on top of linkage differentials, bear guaranteed interest at an effective rate of approx. 5.57% to cover their liabilities by at least 93% of their assets. The remainder, if any, was invested in free investments as per the Income Tax Regulations.

In 1995, the old pension funds were closed to new beneficiaries and new, actuarially balanced pension funds were established. The designated bonds rate was minimized and the new comprehensive pension funds were issued designated bonds bearing guaranteed interest at an effective rate of approx. 5.05%[21], at up to 70% of their assets and the remainder was invested in free investments as per the Provident Funds Regulations.

In 2003 and 2004 the issuance of designated bonds to the comprehensive pension funds (old and new) was discontinued, until the rate of the funds' designated bonds, as said, dropped to 30% of their total assets. The issued designated bonds to such funds bear interest of an effective rate of approx. 4.86%, on top of linkage differentials. The remainder of the assets is invested in free investments as per the Income Tax Regulations[22].

(c) **Provident funds**
Since the mid 80's, no designated bonds were issued to the provident funds[23].

9.1.3 **Structure of profitability in the area**

(a) **Structure of premiums / contribution fees**

Premiums received from the insured in **life assurance** usually include the main following components:

Risk component – to cover various risks such as death, disability and occupational disability.

Savings component – the amount designated by the insured for savings.

Expenses and management fees component – for operational and marketing expenses.

The contribution fees received from beneficiaries in a **pension fund** include similar components.

In provident funds – the contribution fees are aimed at covering the savings component.

[21] In 2004, the effective interest rate was changed to 4.86% in respect of Arad bonds issued as of that day.
[22] The change came into effect as to the new pension funds in September 2003 and as to the old pension funds in January 2004. In the balanced old pension funds compensation was guaranteed under terms set by the Commissioner, both due to reducing the designated bonds issuance and decline of interest rate in respect of such bonds, for the proposed legislation regarding "the safety cushion" see Clause 10.3.2 (b) (2) hereinafter.
[23] Except for guaranteed-yield provident funds. The Group does not manage such funds.

(b) **The basic structure of profitability**

(1) **Life assurance**

The basic profitability in life assurance stems from the following main components:

- In guaranteed-yield policies – the spread in the guaranteed-yield life assurance portfolio ("**the financial spread**").
- In the profit participating portfolio - management fees out of accrual in the profit-participating portfolio (the fixed or variable management fees, taking into account the relevant years in which the insurance policies were issued).
- Insurance profit/loss from the risk component – the difference between the collected premium for the risk coverage and the actual risk realization (claims and annuity payments). The difference between the collected premium to cover the risk and the actual cost of the risk is affected, among other things, by an actuarial setting of the tariffs, mortality rates, actual morbidity rates along the policy's life and "life expectancy" development (as to annuity paying insurance plans). Changes in actuarial assumptions and forecasts that affect the future risk forecast, or any change in assumptions used for calculating the insurance liabilities, may lead to material changes in the calculation of required reserves and financial results. Regarding the above, see Note 37 b 3 b ("Insurance risk in life assurance and health insurance policies") to the Financial Statements.
- The difference between the management fees out of the premium component for marketing and operational expenses and the actual expenses.

When insureds withdraw monies before the end of the insurance period, sometimes they have to pay a redemption fine. The rate of this penalty, if any, depends on the type of the insurance plan, the seniority of the insured and in managers insurance – also on the circumstances of early redemption. Insurance plans marketed as of 2007 no longer include a redemption fine. In case of early redemption, an accounting profit is sometimes recorded due to the release of reserves.

The insurance company's profitability from selling life assurance policies is mainly based on the aggregate result of those components throughout the policy life. Therefore, the persistency level of existing policies ("**portfolio persistency**"), as well as the examination of the actuarial assumptions which form the basis for calculating the reserves, are extremely important for the insurance company's profitability level in the long term.

The reported profitability of insurance companies in the annual Financial Statements is also affected by accounting rules regarding the recognition of revenues and deferral of expenses, by the asset revaluation method, the development of actuarial provisions, and changes in actuarial assumptions affecting the size of the insurance reserves

Income from investments against insurance and capital reserves have a material impact on insurance companies' profits, especially life assurance-biased insurance companies, in light of the large scopes of the Group's assets and reserves invested in the capital market. Changes in the capital market, including changes in the interest rate, CPI, exchange rates and embedded yields and other investments on the market have a critical impact on the Group's profits. Regarding this matter, see also Clause 46.3 in Part E hereinafter.

When examining transactions that combine several products of this area of activity, the Group measures the overall profitability of the various products and components.

(2) **Pension funds**

In pension funds, the source of revenues of the managing companies is the management fees they collect (from contribution fees and from accrual), and the profitability is the difference between the net management fees (after discounts) and the actual operational and marketing expenses. Claims payments in pension funds (including annuity payments) have no direct effect on the profitability of the managing company, since the insurance is mutual and the claims risks are incurred by the insureds.

In pension funds, all of the yield from beneficiaries' monies investments, less the management fees from accrual after discounts, is imputed to beneficiaries, therefore the effect of investment results on the pension fund managing company's profits, is reduced to the direct effect derived from the overall scope of accrual in the pension fund from which the management fees are derived for the pension fund managing company.

(3) **Provident funds**

In provident funds, the source of revenues of the managing companies is the management fees they collect from accrual, and profitability is the difference between the management fees, after discounts, and the actual operational and marketing expenses.

In provident funds, as in pension funds, all of the yield from beneficiaries monies' investments, less the management fees from accrual, is imputed to beneficiaries, therefore the effect of investment results on the provident fund managing company's profits, is reduced to the direct effect derived from the overall scope of accrual in the provident fund, from which the management fees are derived for the provident fund managing company.

As of January 2013, pursuant to the management fees reform, provident funds may collect management fees also from contribution fees, see Clause 9.2.8 (b) (3) hereinafter.

9.2 Legislative restrictions and key changes in the area

In the last years the area has undergone and is undergoing comprehensive changes and is characterized by constant regulation, and it has affected and is affecting the area in a material manner. In 2011-2012 the Commissioner strived towards the implementation of the measures published in 4Q10 in order to enhance the competition in the pensionary savings market. Enclosed herewith please find the key changes / the issues that were carried out in the last decade, with an emphasis on the reforms and changes that occurred / were suggested in the reported period.

9.2.1 Reforms / changes in life assurance plans (2004 and 2007)

In 2004 and 2007 material changes have been made in life assurance plans with a savings component, which mainly addressed the obligation to separate and clearly present the three components of the premium in the policy: savings, insurance coverage (risk) and expenses (management fees and additional payments permitted for collection); changes that affected the increased transparency of insurance products while separating their various components and changes in the savings management fees and setting capital requirements, which exposed the life assurance line, inter alia, to reduced profitability in new insurance plans.

The increased transparency continues to be the Commissioner's guideline in regulating other issues related with insurance plans in recent years.

9.2.2 **Key changes in the new pension funds line (2003-2004)**

In these years, the main changes in the new pension funds line were reflected, inter alia, in the fact that the new pension funds were transferred to the control of insurance companies and investment houses, see the market share distribution Clause 16.1 hereinafter, and a transition was made from Defined Benefits (DB) funds to Defined Contributions (DC) funds[24], the terms of designated bonds were changed, management fees were changed, and the age of retirement was raised.

9.2.3 **Capital market reform – the Bachar legislation (2005)**

In this reform new laws were legislated (the Advice and Marketing Law and Provident Funds Law), and amendments were made to existing laws, which affected the area. For specification of the said laws, see Clauses 45.2.2 and 45.2.5 to Part E hereinafter.

The Bachar legislation regulated the practice of advice and marketing of pensionary savings products, within the Advice and Marketing Law, and inter alia there is a separation between the advice component and marketing for pensionary products, and the duties imposed on the consultant / marketing agent regarding the marketing and distribution of the pensionary product were set forth.

One of the key issues, which is the by-product of this reform, is increasing the end customer's involvement in the process of purchasing pensionary products. The Bachar Legislation diverted the focus towards the end-customers so as to increase their level of involvement and impact. This is reflected, inter alia, both in the possibility granted to employees to choose the type of pensionary product, and the institutional organ from which they want to purchase the selected product, and by pension advising binding the provision of individual counseling to individual employees.

Other additional legislative arrangements enacted after this reform continued to encourage the trend of increasing the employee's / end-customer's involvement. In the reported year, the **Bill for the Supervision of Financial Services (Pensionary Advice, Marketing and Clearing Systems) (Amendment No. 5) – 2012** was published, setting, inter alia, that employees who want to conduct a transaction in pensionary products may execute it via the license-holder of his/her choice; employers may not stipulate such a transaction by a certain license-holder and should not stipulate granting benefits to employees in the execution of a pensionary transaction by the license-holder.

The Bachar legislation also restricted LTS holdings by imposing limitations on "material holding" in this area. For the Group's holding of LTS assets and additional details on this matter, see Clause 9.4 hereinafter.

[24] **DB fund** – a pension fund where the rights of old age, disability and survivors are accrued at tranches. The insureds accumulated an imputed yield-dependent pension amount (pension tranche) against payment of all contribution fees as per the factors set in the fund Articles by age, sex, year of birth etc.; **DC fund** – a pension fund where the savings component for old age is accrued from the contribution fees deposited in the fund, from which management fees and cost of risk (for disability and survivors annuity) and expenses (for investment and/or reinsurance) are deducted, while adjusting the accrued eligibility balance to the fund yield on its investments and actuarial balance mechanism.

9.2.4 **The pensionary products reform 2008 (Amendment No. 3)**[25] **– diverting the LTS product to annuity channel**

In January 2008 the products reform came into effect. The reform in pensionary products is a continuation of the MoF policy as reflected in the last decade, of preferring annuity products over lump-sum products, and the continuation of other reforms it initiated in the area, with the purpose of refining the LTS market.

Up until the pensionary products reform, it was possible to deposit the savings for retirement (long-term savings) in two possible savings tracks:

Lump-sum track ("**lump-sum funds**") – in lump-sum funds, the savings monies can be withdrawn upon retirement as a one-time sum. This track existed in provident funds for provident benefits, and in lump-sum insurance policies.

Annuity track ("annuity funds") – in annuity funds, the savings monies cannot be withdrawn as a one-time sum upon retirement, but only as monthly annuity (pension). This track existed in pension funds and in annuity insurance policies.

The pensionary reform cancelled the abovementioned distinction as regards monies deposited in provident funds for provident benefits and severance pay as of January 2008, and stipulated that all pensionary savings monies deposited as of the aforementioned date will be deposited in an annuity fund.

It was further stipulated, that two types of annuity provident funds will exist (for this purpose, an insurance plan approved as an insurance fund and a pension fund are perceived as a provident fund):

Paying fund to annuity – a provident fund that pays an annuity directly to eligible members.

Non-paying fund to annuity – a provident fund that does not pay an annuity directly to eligible members, from which monies cannot be withdrawn (excluding the severance pay component, or in exceptional cases determined in the legislative arrangement) except by transferring them to a paying fund to annuity.

Up until the pensionary products reform, the decision as to the savings monies upon retirement age was made at the time of deposit, while taking into consideration tax arrangements relevant at the date of the deposit. After the reform, the decision regarding the pensionary savings monies will be made just before retiring, after securing a minimal annuity layer.

Savings monies (except for withdrawing severance pay monies, and specific cases defined in the legislative arrangement, where monies can also be withdrawn from a non-paying fund) will be withdrawn only from provident fund paying to annuity, and will be allowed through the payment of annuity.

[25] Namely, the Law of Supervision of Financial Services (Provident Funds) (Amendment No. 3) – 2008.

The pensionary products reform also cancelled the tax discrimination given to deposits in pension funds, stipulating that all pensionary savings products shall grant savers the same tax benefits.

Following the changes in the pensionary products reform, the marketing of lump-sum insurance funds was terminated; all monies deposited in these funds starting from January 2008 are designated for annuity, and these funds became, at the said date, a "non-paying fund to annuity"[26].

9.2.5 **Mandatory pension regulation**

As of January 2008, by virtue of an **expansion order for comprehensive pension insurance in the market as per the Collective Agreement – 1957**, the duty to produce comprehensive pension insurance in respect of all salarieds in the market subject to the terms set in the Expansion Order, was applied.

9.2.6 **Mobilization of all pensionary products**

As of January 2009, it is possible to mobilize all pension saving monies of all pension products, insurance, pension and provident funds and all the institutional organs managing pension saving, while maintaining the continuity of the insureds' rights, pursuant to the conditions set in legislative arrangements, in order to enhance competition in the area.

9.2.7 **The establishment of a pension clearing house and the regulation of data transfer in a "unified structure"**

As part of the trend of refining the pensionary savings market, the Commissioner promotes the establishment of a pension clearing house. **The Supervision of Financial Services Law (Pension Advice and Marketing) (Amendment 3) - 2011** anchors in a principal legislation the establishment and regulation of a central pension clearing house ("**clearing house**") in the pension savings market. For details regarding the provisions of the above mentioned Law, see Clause 45.2.5 (c) in Part E hereinafter.

Following a tender published by the Commissioner in the reported year regarding the establishment of a clearing house, the Commissioner informed that a supplier was selected for the execution of the establishment and operation of the clearing house. In order to promote that establishment, the tender sets forth that the State shall participate with NIS 10 million, that will be granted as a special grant to the winning supplier, upon the operation of the first phase. The evaluation is that the first stage of the clearing house activity, which is the handling of requests for receiving/transferring information, shall be completed during 3Q13, and the last phase, which is the possibility to deposit and mobilize monies between the various organs via the clearing house, should be completed in July 2015.

The Circular "Duty to Use a Pension Clearing House" (that was published in March 2012 and was amended in August 2012) mandates institutional organs and license holders to work via the clearing house when receiving certain services related with information and requests that will be transferred via the clearing house and mobility requests. Alongside the duty to work through the clearing house form the operations set in the Circular, it was determined that users will incur all of the connectivity and connection maintenance costs to the pension clearing system and will be bound to pay usage fees pursuant to the Commissioner of Insurance provisions and rules of the system approved by the Commissioner of Insurance. A draft Circular

[26] It should be noted that in order to encourage the continued savings within the original insurance fund, the Company added an Appendix "Annuity Follow-Up Plan" to some lump-sum insurance plans, which allows, under certain conditions, the guarantee of guaranteed annuity conversion coefficients, pursuant to the conditions of the follow-up plan.

February 2013 regulates the usage fees that suppliers may collect from users and users should pay to suppliers.

Along with promoting the establishment of the clearing house, the Commissioner published additional arrangements regarding mandating institutional organs to use a "unified structure" for the communications and the transfer of data and information between the producing, marketing, distributing entities and the various users of information, including via the clearing house. These arrangements refer to setting a unified format for the transfer of data and information, the definition of the data structure, the data outline, and circumstances, if existing, requests for data transfer should be accepted (receiving proxies).

The regulation of the processes for the transfer of information and monies via the clearing house and the supplier's winning in the tender for the establishment of the pension clearing house published by the MoF, including the amount by which the institutional organs shall participate may constitute another layer in the refinement of the pension savings market.

9.2.8 **The management fees reform in pensionary products – arrangements regarding management fees**

As of January 1st, 2013, the management fees reform came into effect. The arrangements relevant to the management fees reform are: the **Regulations for the Supervision of Financial Services (Provident Funds) (Management Fees) – 2012, Regulations for the Supervision of Financial Services (Insurance) (Terms in Insurance Contracts) (Amendment) – 2012 and Income tax Regulations (Rules for the approval and management of provident funds) (Amendment No. 4) – 2012**. Furthermore, the Commissioner published several Circulars and/or draft Circulars aimed at continuing the regulation of management fees collection and additional complementary arrangements related to management fees of pension products.

The management fees reform is one of the material changes that occurred in the reported period, and its implementation started on January 2013.

The aim of the management fees reform is setting a unified model for the collection of management fees in the three pensionary savings products (insurance policies recognized as provident funds, pension and provident) as described herewith. In the unified model, management fees are collected both on deposits and accrual. Furthermore, there was a change in the maximum management fees that may be collected as detailed hereinafter.

(a) **Management fees in profit participating policies, in pension and in provident <u>until the management fees reform</u>** – where management fees shall be as follows:

(1) **Insurance plans**

- **Plans marketed until the end of 2003** – the insurance company is entitled to fixed management fees of up to 0.6% per year of accrued assets ("**the accrual**") plus up to 15% of the real yield, less fixed management fees ("**variable management fees**").

  If real losses were accrued, the insurance company is not entitled to variable management fees, until it covers the accrued loss as per a mechanism set forth in the Commissioner's provisions.

- **Plans marketed as of January 1st, 2004 and up to the management fees reform** – derived from the insurance reform in 2004, such plans distinguish between the parts of the premium and the savings, risk and expenses components (management fees). The management fees are divided into management fees from premium (current deposits) and management fees from accrual. The insurance company is entitled to fixed management fees from accrual regardless of the investment results, i.e. are not variable management fees. The management fees rate that may be collected from accrual as to insurance plans recognized as insurance funds – shall not exceed 2% per year[27].

  In 2012, the average management fees rate from accrual in these plans in the Group is approx. 1.23% (New J Fund).

  As to the management fees from premium, three models were set for calculating management fees from premium: the first is the fixed model (fixed percentage up to 11% of the premium and up to 1% of the accrued saving), the second is the descending model (starts at 13% and later descends to up to 5% of the premium and up to 1% of the accrued saving), the third is the flexible model, allowing to convert some of the management fees from accrual into management fees from premium according to a preset index.

  In 2012, the average management fees rate from premium in these plans in the Group is approx. 3.85%.

(2) **Pension**

A managing company of a new comprehensive pension fund may collect management fees from both the contribution fees, at up to 6%, and from the accrual, at no more than 0.5% per year[28].

For details regarding the average rate of management fees from accrual in the new pension funds managed in the Group, see Clause 9.7.1 hereinafter.

(3) **Provident**

A managing company of provident funds could collect management fees from accrual only, at no more than 2% per year.

For details regarding the average rate of management fees from provident funds managed in the Group, see Clause 9.7.2 hereinafter.

[27] Regarding insurance plans that are not recognized as a provident fund marketed starting from August 2007 – it was possible to collect, with the Commissioner's approval, management fees to accrual in a rate not exceeding 2% per year, i.e. over the cap, however, in this case it was possible to collect management fees from accrual only. The Group did not market such insurance plans.

[28] A general new pension fund (in the Group, Makefet Complementary) could collect, as of January 2006 and up to the management fees reform, management fees in one of two ways: (1) from contribution fees – at a rate that does not exceed 3%, from the accrued rights balance at no more than 0.5%, out of which the fund payments to the member – at a rate lower than 2% or NIS 40 linked per month, the lower of the two – as long as the total management fees, as of the 4th year to the member's membership, shall not exceed 2% of the accrued rights balance; (2) a rate that does not exceed 2% of the value of the accrued rights balance.

(b) **Changes in management fees <u>following the management fees reform</u>**:

(1) **Insurance plans**

- **Insurance plans recognized as provident funds (insurance funds) marketed starting from January 2013**[29]
  As of January 1st, 2014, the maximum management fees that insurance companies may collect in these plans shall not exceed 1.05% of accrual per year, and no more than 4% on current payments (deposits).

  In the transition period, i.e. from January 1st, 2013 till December 31st, 2013 ("**the transition period**"), the maximum management fees that may be collected shall not exceed 1.1% of accrual per year, and no more than 4% on current payments.

  Also, there is a maximum rate from annuitants – up to 0.6% per year on all assets against the fund's liabilities to the annuitants.

- **Insurance plans not recognized as provident funds marketed from January 2013 (i.e. individual plans not recognized as provident funds)**
  As of January 1st, 2013, the maximum fixed management fees that insurance companies may collect in these plans shall not exceed 1% of investments' revalued value (deposits).

  The Commissioner may approve management fees exceeding these rates, provided they do not exceed 2% of the investments portfolio's revalued value.

  The Commissioner may approve higher management fees in respect of the investments portfolio management, provided only management fees as a rate from the investments portfolio's revalued value are collected.

(2) **Pension**

- **New comprehensive fund** – there was no change in the management fees rate as described in Clause 9.2.8 (a) (2) above, however, there are new provisions regulating the management fees rate in the period of annuity payment, and referring to beneficiaries who were not detected, as described in Clause 9.2.8 (c) (2) hereinafter.
- **New general fund** – management fees were changed, and they are as described in Clause 9.2.8 (b) (1) above, for insurance plans recognized as insurance funds.

(3) **Provident**

- In provident funds (which are not provident funds as described in the following paragraph, or sectorial provident funds) the novelty is that it will be possible to collect management fees from deposits, and the maximum management fees rate from accrual was also changed. As of January 1st, 2013, the maximum management fees, both from accrual and from deposits is as described in Clause 9.2.8 (b) (1) above, for insurance plans recognized as insurance funds.

[29] It is hereby clarified that the change in the maximum management fees in insurance plans applies to insurance plans marketed starting from January 1st, 2013, and does not apply to existing plans.

- Managing companies of training funds, provident funds under personal management, central provident funds, sick leave provident funds, annual leave provident funds and provident funds for other purposes ("**other funds**"), may collect management fees from accrual at a rate that would not exceed 2% per year (unchanged compared with the existing situation).

(c) Additional issues that were regulated with regards with the management fees rate:

(1) **Management fees from annuities** – there are arrangements regarding the maximum management fees collectable from annuities, and usually this rate would be 0.6% of accrual per year**.**

(2) **Management fees from beneficiaries with whom contact was lost** – there are provisions regarding the maximum management fees rate collectible from the accounts of beneficiaries with whom contact was lost during the period in which there was no contact, including regarding the undetected beneficiaries of beneficiaries who were deceased, as long as no contact was created. Beneficiaries with no contact and the period with no contact were defined in the Detection Regulations. The maximum management fees rate for those with no contact shall not exceed 0.3% per year of the accrued balance in the account, either on the monthly rate collected by the institutional organ upon losing connection with the beneficiary, or the date upon which the institutional organ was informed of the beneficiary's demise, the lower of the two**.**

Also, for the event the institutional organ contacts beneficiaries with whom contact was lost as per the provisions set in the regulations, the institutional organ will be entitled to retroactively collect management fees such that the management fees collectable in respect of this period will not exceed 0.5% of the accrued balance in the beneficiary's account, instead of 0.3%, or the management fees collected from the beneficiaries before the contact was lost, the lowest of the two.

(3) **Proposal for setting minimum management fees** – there is a bill for the Amendment of the **Control of Financial Services (Provident Funds) (Minimum Management Fees) - 2012** (published in October 2012) regarding the setting of minimum management fees for accounts in provident funds with low accruals (as per the definition set forth in the amendment mentioned above the reference is to new insurance funds, provident funds and comprehensive pension funds).

(4) In light of the reduction in management fees rate, and in order to bring about a reduction in the costs related to the operation of provident funds:

- **Draft Control of Financial Services (Money Withdrawal from Provident Funds) (Accounts with Low Accruals) (Temporary Orders) – 2012,** published in October 2012, setting forth in a temporary order for one year, that beneficiaries may withdraw monies in a lump sum from provident funds if no monies were deposited since January 1st, 2012 and on, if the total accrued amount for the beneficiaries in all their accounts in the provident fund as of January 1st, 2013 is lower than NIS 5,000.
- **Draft Institutional Organs Circular regarding the Merger of Accounts by a Managing Company**, published in October 2012, asking to regulate the merging of provident funds belonging to a beneficiary holding several accounts in

the same fund pursuant to the terms set forth in the Draft Circular.

(5) **Restrictions for granting discounts on management fees and notifications regarding changes in management fees** – in addition to the changes in the management fees structure and rate as described above, the Circular regarding **Management Fees in Pensionary Savings Instruments**, published in December 2012 (effective as of March 1st, 2013), sets forth a minimal period for extending management fees (about at least two years subject to restrictions), and mandates sending notifications any time there is a change in management fees collected from beneficiaries, including the minimal advance period before raising management fees (no later than two months and no less than four months under the conditions set forth in the Circular).

(d) The regulation referring to management fees in pensionary savings products, is the implementation of another measure in the MoF plan for enhancing the competition in the area, is a material change that affects the area, and regarding the Company's estimates regarding the impact of the management fees reform, see Clause 9.2.12 (c) hereinafter.

9.2.9 **The regulation regarding annuity coefficients**

Another material change that occurred in the reported period and which constitutes one of the most significant changes in the area, is the regulation regarding annuity coefficients as set forth below[30].

The regulation regarding annuity coefficients is made, inter alia, in light of the increase in life expectancy and the risk related with the uncertainty as to the improvement in life expectancy.

Position paper – updating the demographic assumption array in the pension funds and life assurance. The position paper is divided into three main parts:

The first part (Chapters B and C) deals with the update of the demographic assumption system ("**default**") for the pension funds and the calculation of annuity in insurance companies, according to data received from pension funds and insurance companies.

The second part (chapter D) examines the improvement of life expectancy in Israel, reviews assumptions in various countries concerning improved life expectancy rates, and includes findings and recommendations concerning future improved rates of life expectancy and the derived implications from such future improvement on the insurance sector – rate of reserves and their formation.

The third part (chapter E) examines the ability of insurance companies to handle changes in future life expectancy and relevant findings and recommendations.

[30] The regulation regarding annuity coefficients is reflected in the following legislative arrangements: position paper – update of the demographic assumptions array in pension funds and life assurance (whose draft was published in July 2012 and the final position paper published in November 2012) "position paper"), a Circular from November 2012 regarding Annuity Coefficients Embedding Life Expectancy Guarantee, a Circular from November 2012 regarding the Extension of the Validity of the Life Expectancy Guarantee, a Circular from January 2013 – the Way for Calculating the Actuarial Balance and the Coefficients of Pension Funds' Articles of Association, a Circular dated March 2013 – Circular regarding Reserves for Annuity Payment in Life Assurance Policies.

(a) Update of the demographic assumptions array

(1) **Life assurance** – the Circular 2007-1-3 "Calculation of Reserves for Annuity Payment in Life Assurance Policies" ("**Fefferman Circular**") regulated the need to follow up on the accuracy of reserves in respect of life assurance policies allowing annuities and the way to calculate reserves for these policies, including for SAR, all pursuant to the conditions set forth in the above mentioned Circular.

Pursuant to the changes reviewed in the position paper and the change in the demographic assumptions, including the findings and recommendations as to the future improvement rate in life expectancy, in March 2013 the Commissioner published a Circular substituting the Fefferman Circular, and it includes updated demographic assumptions for the calculation of reserves for annuity payments, and there are principles regarding the reserves calculation and enhancement. The Circular also regulates updated rules compared with what was set forth in the Fefferman Circular. For additional details see Note 37 b 3 b) (5) to the Financial Statements, "changes in the main assumptions that served for the calculation of insurance liabilities".

In the Company's FS as of 2012, the Company updated its estimates regarding liabilities for annuity based on the updated estimates regarding life expectancy and future improvements included in the Reserves Calculation Circular as set forth above, as well as based on the aggregate experience in the Company.

Therefore, the Company executed an immediate provision for SAR, which reduced the comprehensive income by approx. NIS 257 million, before tax. For additional details see the Note in the FS, as set forth in the previous paragraph, as well as the statement made by the life assurance actuary attached to the FS.

(2) **Pension** – in January 2013 the Circular "**the Way for Calculating the Actuarial Balance and the Coefficients of Pension Funds' Articles of Association**" (which substituted the Circular published in December 2012), updating the assumptions based on which the actuarial balance and the coefficients of pension funds should be calculated, following which pension funds' managing companies should update the Articles of Association, taking into account the updated actuarial assumptions.

(b) **Regulation of the marketing of insurance plans that combine savings with guaranteed annuity coefficients**

Based on the findings and recommendations set forth in the position paper, referring, inter alia, to the improvement in life expectancy in Israel and to insurance companies' ability to cope with future changes in life expectancy, there is a regulation regarding the marketing of insurance plans combining savings with annuity coefficients embedding life expectancy guarantee ("**guaranteed annuity coefficients**"), as detailed herewith. This regulation included also a reference to the marketing of these plans in the interim period, i.e. from July 2012 to December 31st, 2013, as described hereinafter.

(1) **The prohibition of the marketing of life assurance plans that include guaranteed annuity coefficients**

As of January 1st, 2013, insurance companies may not market life assurance plans that combine savings and include guaranteed annuity coefficients ("**insurance coverage for longevity**"), except in the following cases:

- From the age of 60 – to whoever completed at least 60 years at the time of sale, provided the plan also meets the following principles:
  The longevity insurance coverage shall be priced as an independent and separate component, with disclosure to insureds, or, alternately, insurance plans with insurance coverage for longevity that are not priced as an independent and separate component, as set forth above, provided the conditions set forth by the Commissioner are met, may be marketed.

  The payment for longevity insurance coverage shall be identical for all insureds who purchase it, subject to differentiations based on actuarial characteristics.

- **Cancellation and mobilization** of existing contract – whoever has an insurance contract with longevity insurance coverage, and wants to cancel the entire existing contact and mobilize the monies in the existing contract to a new insurance contract that includes longevity insurance coverage, under the conditions set forth in the Circular.

- **Marketing arrangements in the interim period** – in addition, there are restrictions regarding the scope of life assurance contracts with guaranteed coefficients sold by virtue of permits granted in the interim period, i.e. in 2012 and 2013. In 2013 the scope should not exceed NIS 75 million, and the number of life assurance contracts with guaranteed coefficients that may be sold by an insurance company by virtue of such permits in 2013 should not exceed 6,000. Furthermore, the condition for the coming into effect of a marketing permit of insurance plans with guaranteed coefficients for 2013 is the approval of a business plan that should be approved by the Commissioner.

(c) **Implications –** the annuity coefficients reform, pursuant to which, inter alia, insurance companies may not market insurance plans that include guaranteed annuity coefficients is the most material change in the area, which, along with the change in management fees in insurance plans recognized as provident funds, affect the area in a material manner and these changes affect, inter alia, the structure of pensionary savings products in general, and the Group's profitability, and forces it to deploy towards this changing situation.

Regarding the Company's evaluation of the impact of this reform, see 9.2.12 hereinafter, and regarding the Company's strategy, see Clause 57 hereinafter.

9.2.10 **Allowing managing companies to market pensionary savings-related insurance products**

Another measure taken by the Commissioner in the implementation of the plan for the enhancement of competition in the area is allowing the acquisition of insurance coverages via provident funds' managing companies (companies managing pension and provident")[31].

[31] The relevant provisions are: Regulations of Control of financial services (Provident Funds) (Insurance Coverages in Provident Funds) – 2013 ("**Insurance Coverage Regulations**") published in January 2013, and the Institutional Organs Circular 2012-9-20 regarding the Acquisition of Insurance Coverages via Provident Funds' Managing Companies ("**Circular regarding the Acquisition of Insurance Coverages**"), published in December 2012.

The Insurance Coverages Regulations include provisions regarding the types of insurance in which beneficiaries in provident funds shall be insured, the conditions for maintaining insurance coverage after the deposits to provident funds are discontinued, provisions referring to insurance fees that may be collected, including provisions referring to a situation whereas the insurer is a related party of the managing company. Also, there are provisions regarding the acquisition of collective insurance coverages by the managing company, including when the insurer is a related party of the managing company.

The Insurance Coverages Circular regulates the rules pursuant to which managing companies may file a request for receiving a permit for marketing insurance coverages via individual insurance policies, and there are provisions regarding maintaining insurance coverage in individual insurance, notifying insureds regarding duplicity in insurance coverage, if the provident fund's Articles of Association were changed, etc.

The regulation regarding allowing the acquisition of insurance coverages via a managing company is another layer in regulation, aimed at simplifying and unifying the products in this area and increasing the changeability of the products in the area, in order to enhance the competition in the area.

9.2.11 **Additional material arrangements in the reported period**

(a) Arrangements regarding the establishment of insurance plans and their approval

For the Commissioner's intention to change the existing rules regarding the establishment of insurance plans and pension and provident Articles of Association, such that institutional organs will be required to inform the Commissioner about the establishment of products before these products are marketed, without having to wait for the Commissioner's approval as a condition for starting their marketing, see Clause 45.2.12 to Part E hereinafter.

(b) Arrangements related to marketing agents'/advisors' commissions

(1) **Insurance agents' commissions** – a **draft of the Supervision of Financial Services (Insurance) (Brokerage fees) Law - 2012** (its third draft was published in May 2012) is pending. The draft is aimed at regulating the commission payment to insurance agents and inter alia, the following issues: the composition of the brokerage fees paid to insurance agents; restrictions as regards the ratio between commissions of different types paid to insurance agents; the regulation of payment of the brokerage fees to several licensees simultaneously; it sets instructions as to the discontinuation of payment for insureds with whom contact was lost or undetected beneficiaries. The regulation reduces certain incentives and also regulates giving various incentives in respect of sales and incentives in respect of service.

(2) **Circular regarding the Power of Attorney to License Holders** – in December 2012 a Circular regarding the Power of Attorney to License Holders, regulating provisions as to a unified wording for power of attorney forms to holders of pensionary license and setting arrangements regarding the validity of the power of attorney and its application, the way it is used and the way institutional organs refer to the power of attorney, and inter alia, there is a duty to present to the institutional organ a power of attorney from the customer, in the structure and conditions set forth in the Circular. The aim of the Circular is, inter alia, preparing the organs operating in this area for the transfer of information and the execution of transactions via computerized and unified forms, including via the clearing house. The Circular

will come into effect on May 1st, 2013, and for products in which customers received advice or marketing by the license holder before the application date, and as long as the transactions in the product are not executed via the clearing house, on July 1st, 2017.

(3) **The argumentation document** – in October 2012, a draft Circular regarding the rules and provisions referring to the Argumentation document that license holders should give to customers upon recommending the acquisition of a pensionary product, was published. The draft Circular is aimed at expanding the provisions regarding the argumentation document in the previous Circular that was published on this matter.

(4) **Pensionary advising commissions** – the draft **Regulations of Supervision of Financial Services (Provident Funds) (Distribution Commissions) (Amendment) - 2012** is pending. The draft Regulations are aimed at regulating distribution commissions also in respect of insurance products included in the type of pensionary product under the Advice Law, see Clause 45.2.3 (E) to Part E hereinafter.

(c) Arrangements regarding the investment of LTS monies

(1) **Investment Rules for all Institutional Organs** - in July 2012 the **Control of Financial Services (Provident Funds) (Rules of Investments that apply to managing companies) - 2012** came into effect, and the **Circular regarding Rules of Investments that Apply to Institutional Organs) - 2012** was published (the Regulations and Circular will be jointly referred to as "**New Investment Rules**").

As per the New Investment Rules, as of that date, unified investment rules will apply to pensionary savings products (pension funds, provident funds, profit participating policies), and the differentiation that existed in this matter between the Investment Rules for provident and pension funds' assets and those that applied to profit participating policies' assets was cancelled, and some Investment Rules were amended. The New Investment Rules are vast, fort the description of the main issues, see Clause 45.2.9 to Part E hereinafter.

(2) **Proposal for investment management as per default tracks (SMART model)**

A **Draft Control Regulations of Financial Services (Provident Funds) (Establishing Default Tracks) – 2012** (SMART model) is pending. It intends to regulate the establishment of investment tracks, including default tracks, along with adjusting the investments' risk to the customers' characteristics. Clause 10.2.9 to the Company's Periodic Report for 2011 describes the principles of that proposal.

(3) **Investment policy in specialized tracks, and investment track's names**

A draft Institutional Organs Circular, published in October 2012, regarding the investment policy in specialized tracks, and investment track's names in pensionary savings products, is pending. The draft Circular is aimed at setting unified rules for the adjustment of investment tracks' name to the investment policy in the track, setting rules for the management of investment tracks, as well as setting rules regarding the notification of beneficiaries if an investment policy is amended or an investment track is discontinued.

9.2.12 **Company's estimates regarding the impact/implications of material reforms and arrangements in the area**

The proposed regulation regarding the annuity coefficients as described above, along with the management fees reform, which came into effect on January 2013, are an "**undermining change**" that occurred during the reported period, and they may change the area materially.

The trend recorded during the last decade is that the legislator and the Commissioner introduce arrangements aimed at refining the market, along with an increase in consumer awareness and an enhancement of competition in the area.

The main characteristics of new life assurance products, which were mainly the guaranteed conversion coefficients and management fees set forth in the contract, which were the main differentiating characteristics compared with other savings products in the area, are changing since 2013 following the reform in annuity coefficients.

The management fees reform, which regulates both the determination of a unified model of management fees for the area's products, and the reduction of maximum management fees in insurance products recognized as provident funds in the new plans, the possibility that managing companies may market, in addition to the savings component, also insurance products (another characterization that differentiated between provident funds and life assurance plans), constitutes another phase in the regulatory arrangement, aimed at unifying and simplifying pensionary products, and they also constitute the continuation of the Commissioner's trend in order to enhance the competition in the area.

The legislative arrangements aimed at earmarking the monies for annuity in the products' reform, unifying tax rules to all LTS channels, introducing mandatory pension, the possibility to mobilize pension savings monies, are characterized by the fact that they reflect the legislator's trend to expand the pensionary coverage and secure current annuities after retirement, along with an increase in free choice and mobilization between the various producers and products. These trends were expressed, inter alia, in an accelerated growth in the pension line in recent years, compared with activity in life assurance and the provident line. For growth rates in the pension line compared with life assurance and provident, see Clause 9.5 hereinafter.

The increase in life expectancy, the increase in the annuity savings channel, the increase in the public's awareness to pensionary savings and in people receiving annuities upon retirement, the mandated money deposit for annuities, public tastes, the coping with the decline in yields, also due to developments in the macro-economic environment, exposed the insurance companies to the risk of longer longevity of insureds and their survivors. The proposed regulation in annuity coefficients is aimed at coping with the risk related with uncertainty as to life expectancy, for insurance companies.

The legislative arrangements aimed at increasing end customers' involvement in the acquisition of pensionary products, the pending regulation regarding the reduction of employees in the acquisition of pensionary products as described in Clause 9.2.3 above, the promotion of the establishment of the pension clearing house, the change in the remuneration model for agents as described in Clause 9.2.11 (b) (1) above, etc., may indicate a trend of further refinement in the market, that may also change the customers mix and distribution channels, including arrangement managers. From a world in which most of the pensionary savings in producing entities originate from arrangements with employers, wherein employees received comprehensive solutions for pension arrangements, there is a desire to create a reality in which the individual will have a greater weight, for creating personalized pensionary arrangements, along with direct access, mainly through the clearing house, to the producing entities. All the above may also contribute towards refining the competition, alongside with a higher ability for individual customers vis-à-vis the producing entities, as well as vis-à-vis employers / arrangement managers.

The proposed regulation regarding annuity coefficients, pursuant to which it no more possible to market insurance plans with guaranteed annuity coefficients, along with the other measures taken by the Commissioner in order to enhance the competition in order to refine the market, the simplification and unification of the product, including the change in arrangements related to the management fees rate in pension products, will affect mainly in these aspects according to the Company, in addition to the immediate impact on the amount of reserves as detailed in Clause 9.2.9 (a) (1) above.

(a) **The development of two secondary markets in the area** – the market of active savers, to whom pension savings products will be offered until the age of retirement, and a market for the age of retirement – the Third Age market.

The products that will be offered on the active savers market will be products that include savings and a similar insurance coverage, and the competition between the various producers shall focus mainly on the parameters of price, yield, the quality of insurance coverage and service.

In the market for the age of retirement, it will be possible to select from several products at the age of retirement, and the saving market product will be mobilized to this market, and it will rely also on lump sum deposits of large amounts in favor of guaranteeing annuity, which will be transferred from other saving channels. The competition between the various producers shall focus mainly in the parameters of annuity conversion coefficients, the variety of annuity tracks, management fees and service.

The change in the products' structure and the simplification and unification of products on the active savers market shall affect, inter alia, also the different profitability among the area's products.

(b) **Pension savings products' configuration** – the main characteristics differentiating between the insurance products and pension and provident products, as set forth above, were cancelled. As a result, one of the relative advantages of the saving product in insurance over other saving products in the area (pension and provident) was undermined. The trend of accelerated growth in the pension line and in the sale of new pensions. At the expense of selling life assurance plans shall continue, and even intensify, also following the new reforms. The differentiating characteristic in the pension line, i.e. the issuance of designated bonds only for pension funds, although at a lower rate as set forth in Clause 9.1.2 (b) above, constitutes, after the annuity coefficients reform, a significant differentiating characteristic compared with insurance products, that may accelerate the continued growth in the pension line.

(c) **Reduction of management fees** – the management fees reform shall reduce the management fees collected by institutional organs in the Group, compared with the management fees that would have been collected without that change, regarding insurance products that will be sold starting from January 1st, 2013 and regarding management fees in respect of beneficiaries with whom contact was lost, and it may also increase the lapse rates of policies with higher management fees, sold by the Company in the past, and their substitution or mobilization to new policies with lower management fees. The Company estimates that the reform in annuity coefficients, pursuant to which it will be prohibited to sell life assurance plans that combine savings and include a guaranteed annuity coefficient, may moderate this phenomenon and differentiate the current portfolio.

(d) **Differentiating the current portfolio** (life assurance plans that include guaranteed annuity coefficients which were marketed in the annuity coefficients prior to the reform) – the Company estimates that life assurance plans sold starting from 2001, which include guaranteed annuity coefficients, may be less exposed to the risks of cancellations and surrenders due to the reform in annuity coefficients, in which it will be possible to guarantee an annuity coefficient only after the age of 60 years.

(e) **The impact on distribution channels** – the configuration of savings and insurance products that will be derived pursuant to the proposed changes and the public tastes referring, inter alia, to the pension line products, will also affect the area's distribution channels, both on the structure of remuneration and on the extent of impact and increase of one distribution channel at the expense of another distribution channel. In addition to the above, the arrangements regarding the increase of involvement on behalf of end customers vis-à-vis the producing entities / employers / arrangement managers as described above, might affect the customers mix and the structure of distribution channels in the area (direct, arrangement managers, marketing agents/advisors). Most of the Group's pension savings portfolio originates from arrangements with employers, arrangement managers, whereas employees received comprehensive solutions for pension in competitive conditions. The reduction in the involvement of these may affect the extent of their involvement, including the extent of their impact and their remuneration structure.

In addition, the management of LTS by institutional organs, both till the age of retirement and afterwards (which is also derived by the various changes in the area) increased the regulation both s regards the management and supervision over the LTS assets investments, including on the capital market, as well as regards the intensification of supervision, enforcement, control and management mechanisms of risk as far as investment management is concerned, regarding the capital requirements for institutional organs, and the expansion of information and disclosure that should be provided by institutional organs regarding investment management, and all the above will impact the expenses related thereof, including fix expenses.

Besides the above, institutional organs should cope both with the decline in interest rates and the achieving of yields in excess in assets management (which affects the scope of assets from which institutional organs' management fees are derived), as well as reductions in management fees from accrual in savings products since January 2013, including a decrease in management fees due to the competition in the area.

The pensionary savings market is refining, the competition in the area is increasing and it will focus around the new products that will be offered by the entities on the market to their customers, both till the age of retirement and after the age of retirement, the quality of service, management fees, yields achieved compared to the risk level, the structure of remuneration of distribution channels and their features, the operational streamlining of institutional organs based on this changing reality, the computerized, organizational and operational infrastructure at their disposal, the stability of institutional organs including their ability to comply with capital requirements, the marketing and distribution system at the disposal of institutional organs, the behavior of insureds regarding the selection of products, etc.

The above mentioned changes are material changes. In the next future there will be significant deployment. The new products which started being marketed starting from January 2013 have not been integrated yet, and it is not clear yet whether the products launched in the beginning of 2013 are in their final configuration. According to the Company, there are additional issues that require complementary arrangements, including legislative arrangements, in light of which it will be possible to develop products, which, on the one hand, would provide a solution to the fact that it is impossible to market an insurance product that includes a guaranteed annuity coefficient, and on the other hand, would provide a more advanced solution compared with pension. The above will have a long term and significant impact, and it may affect, inter alia, the products mix, the distribution map, and the products' profitability. The Company is deploying towards the integration, organization and implementation of the "changing world" following the new arrangements, including the examination and development of products, which will embed relative advantages compared with other products, and with the above, it will cope with this changing market and the increasing competition, all in order to take advantage and maintain the Group's leading status in the area of pensionary savings, including the various aspects and the advantages over the competitors.

The new arrangements in the area, along with the changes that occurred in the area on the last decade, affect and will affect the entire chain of value in the area, including the Company's expenses structure and rates, whether due to an internal streamlining or due to the need to cope with this changing market, including the reduction in management fees rates, both due to the reduction in the management fees rate and the non achievement of yields in excess, including searching for and finding sources of profit in new markets/areas.

According to the Company, the deployment and coping of players including the Company, on this changing market, will be gradual over a long period, and they involve complex processes, part of which will be reflected in the upcoming deployment period in which, inter alia, the configuration of new products, their integration on the market and their related implications, will be set, and the other part will be reflected in the longer term. The extent of impact shall be determined by the business developments on the market, on the one hand, and the deployment and adjustments that will be implemented by the Group on the other hand, including the measures that will be taken, both in the short term and in the longer term, in order to cope with this changing market.

The Company is unable to assess all the impact of these changes on its Financial Statements. The changes in the demographic assumptions array immediately affect the way for calculating the reserves that must be kept by Migdal Insurance against its liabilities, as set forth in Clause 9.2.9 (a) (1) above, and these necessarily affect the Group's financial results and profitability.

In Note 37 b 3 b) (4) to the Company's Financial Statements includes sensitivity analyses regarding the impact of lapse rates. Furthermore, in the "Report regarding Migdal Insurance's EV", attached to the Company's FS as of March 31st, 2012, Clause 3.6 includes a sensitivity analysis in respect of businesses included in life assurance and health insurance as of December 31st, 2011, regarding parameters included in the above mentioned Clause.

For the Group's coping with the competition in the area and the Company's strategy also in light of the changes in this changing market, see Clause 16.2.1 hereinafter, as well as Clause 57 to Part E hereinafter.

Information in this paragraph as regards the implication and/or the Company's deployment for anything concerning the implementation of the proposed changes including sensitivity analyses, is future-forecasting information as per its definition in the Securities Law – 1968, based on the current and/or proposed legislative arrangements, regarding which it is still unknown whether they will be final provisions, and all the additional arrangements required as a result of implementing the planned measures are still unknown. Furthermore, the aforesaid is based on assumptions, estimates and forecasts regarding future events whose realization is uncertain and which are beyond the Company's control. All the above may not materialize if the provisions are amended or updated or changed in a way that is different than the forecast, or if they do not materialize.

9.3 Description of the insurance lines and insurance coverages included in the area

The area of life assurance and long term savings focuses on savings and risk.

The savings activity within life assurance and pension is promoted by State authorities, mainly through tax incentives, various provisions in Labor laws, issuance of designated bonds to pension funds etc., which constitute an important consideration when customers choose this area's products.

The Income Tax Ordinance and Income Tax Regulations also define the provision rates of employees, employers and self-employed insureds to provident funds, including insurance plans recognized as provident funds, and the tax benefits granted to pension saving, also at the time of their withdrawal and changes in the tax regime also affect the products of this area.

The main products offered in this area are the various life assurance plans, pension and provident funds.

In life assurance, insurance companies offer an insurance product that enables to combine both savings and risk (death and PHI risks). Up to the regulation regarding annuity coefficients as described in Clause 9.2.9 above, the product allows the receipt of annuity upon retirement and usually it comprises two features set forth in the contract – guaranteed conversion factors against changes in life expectancy in certain cases set forth in the insurance plans, and management fees rate.

In life assurance, the insurance company's liability towards the insured is a contractual liability established by an insurance contract – the policy. In an insurance contract the insurance company usually undertakes to pay the insurance benefits upon the occurrence of the risk event, even if exogenous changes have occurred, for better or worse, that it has not taken into account in the assumptions underlying the policy upon its proposal (such as increase in life expectancy, change in disability rates, etc).

Pension funds also offer a product allowing the combination of savings and risk, as said, as well as the receipt of annuity upon retirement. This product is proposed based on the "mutual insurance" principle in which, inter alia, the rate of annuity, both upon the occurrence of a risk event and upon retirement, is affected by the actuarial surplus or deficit accumulated in the pension fund, which is to be distributed among the fund beneficiaries.

Actuarial surplus or deficit may occur if the number of disability and mortality events in the insured population does not comply with the demographic assumptions of the fund, since the pension fund calculates the risk cost for disability and survivors insurance and the conversion factors for pension upon retirement based on these assumptions.

In pension funds, joining the fund is based on the fund's Articles of Association. When modifications are necessary in the Articles of Association, the managing company adjusts the Articles subject to the approval of the Commissioner of Capital Market. The rights to which members or their survivors are entitled in the fund will be as per the funds' Articles of Association, as they were at the date of occurrence of the rights-entitling event.

As long as the legislative arrangement is not changed, new comprehensive pension funds may invest up to 30% of assets in designated bonds, see Clause 9.1.2 (b) above.

Up till 2013, provident funds offered a savings product only, without the ability to combine the risk component, or to receive annuity. In provident funds there is no actuarial risk component, and beneficiaries are entitled to the yield achieved in practice less investments-related management fees. In provident funds, too, joining the fund is based on the fund's Articles of Association, and the management fees collected from beneficiaries are not fixed, and are subject to change.

Starting from January 2013, provident funds managing companies may offer insurance coverages as described in Clause 9.2.10 above, to their beneficiaries.

The regulatory trend, expressed in the last decade and was significantly reflected in the reported period, is the simplification and \unification of the area's products. Regarding the changeability of products in this area, see Clause 9.6 hereinafter.

9.4 Restrictions, legislation, standardization and special constraints that apply to the area of activity

As described above, the activity in this area is subject to vast regulation and strict supervision. The supervising organ is the Capital Markets Division. This area comprises unique regulation regulating its activity, which mainly includes the Law of Supervision and the Regulations issued by its virtue from time to time, the Provident Funds Law, the Provident Funds Regulations, the Pension Marketing Law, the Insurance Contract Law – 1981, as well as Circulars and instructions issued by the Commissioner from time to time.

The activity in the area of insurance requires receiving an insurer's license from the Commissioner of Insurance and a permit to operate in the various areas of insurance, regarding each and every insurance line in which the company is engaged. Insurance companies in the Group have insurer licenses in the lines of insurance they are engaged in.

The Group's pension activity also requires an insurer license, as well as a permit to operate as a managing company from the Commissioner of Insurance and Income Tax Commissioner. In addition, each pension fund managed by a managing company must possess an annual license for managing a provident fund. The companies managing pension funds in the Group and the funds they manage, including provident funds managed by Migdal Makefet, possess the above mentioned licenses and permits.

Restriction of market share and avoiding centralization – the Bachar legislation stipulated that no permit shall be granted to purchase or hold[32] an insurer or provident fund, if the buyer's or holder's market share, including that of their controlling shareholders and organs they control in the LTS area as defined in the said legislation, exceeds 15% of the total LTS assets ("maximum market share"). In accordance with the data published by the Commissioner in a circular dated December 2012, the total LTS assets, as at September 30th, 2012 totals approx.

[32] As to material holding in the area of LTS to receive such permit, the following parameters will not be taken into account: (1) change in the market value of managed LTS assets (2) change in the value of all LTS assets (3) joining of insureds / members to insurance plans / provident funds so that the total of assets grows, except for joining following an engagement or merger with another institutional organ.

NIS 595.5 billion. The maximum market share, as per the said calculation, and as per the aforementioned date, is approx. NIS 89.3 billion.

The Group holds, as at September 30th, 2012 and based on the aforesaid database, approx. 17.1% of total LTS assets.

In addition, there are entry barriers to the area as described in Clause 45.4.1 in Part E hereinafter, including equity requirements and skills in the area of risk management.

For additional details on restrictions and other legislative arrangements in the area, see also Clause 45 in Part E hereinafter.

9.5 Changes in the scope of activity in the area and its profitability, and in the customers mix

Institutional organs operate in the Israeli market, whose economic, political and security condition affect its sales in the area, the volume of insurance claims and various costs involved in their operation. Deterioration in the level of employment, including a decline in the number of employees, an increase in unemployment rate, reduced salaries – all affect the volume of new sales and the lapse and surrender rates in life assurance and LTS. In addition, escalation in the market and employment conditions may bring about an increase in bad debts, more claims, less purchased coverages etc.

Furthermore, regulatory changes in the areas of insurance and LTS have a significant impact on the scope of activity, portfolio persistency and profitability.

Based on life assurance premium data in the years 2010 up until September 2012, and the data regarding contribution fees and net accruals[33] in the years 2010-2012[34], there is a distinct trend of increased aggregate activity in the area of life assurance and LTS, especially in pension and life assurance.

In life assurance, in the first nine months of 2012 growth was recorded in the market (5%), which was moderate compared with growth in 2011 (approx. 9%).

In the pension line, the last two years recorded an accelerated growth (in 2012 approx. 18% and in 2011 – approx. 20%) compared with life assurance activity. In the provident line, there was a moderate growth in contribution fees (approx. 3% in 2012 and approx. 5% in 2011) and negative net accrual in 2012 and 2011, following a positive net accrual in 2010.

In the aggregate scope of activity in terms of managed assets, in 2012 there was an increase in the total products in the area (approx. 13%), which was affected by increases on capital markets and the net current accrual, following a slight increase last year (approx. 1%), which was affected by price decreases on capital markets.

The weight of the life assurance line in terms of managed assets increased from approx. 34.8% in December 31st, 2011 to approx. 35.0% in December 31st, 2012, the weight of the new pension funds line increased from approx. 16.8% in December 31st, 2011 to approx. 18.6% in December 31st, 2012, and the weight of the provident line decreased from approx. 48.4% in December 31st, 2011 to approx. 46.3% in December 31st, 2012.

For details regarding the scopes of activity and profitability in the area of life assurance and LTS in the Group and on the market, see Clause 1.3 in the BoD Report and Note 3 c to the Financial Statements.

For details regarding premiums and the composition of income in life assurance as per types of policies and their issuance date, see Note 18 b to the Financial Statements as well as Clause 1.7.3 in the BoD Report.

[33] Net accrual is defined as contribution fees plus net transfer of members, less surrenders.

[34] Based on the MoF website data, including Pension-Net, Gemel-Net and Bituach-Net.

9.6 Alternatives to products and the relevant changes

Among the area's various products (except for training funds) there is a relatively high changeability, since they provide similar needs to the same target audience.

The main parameters used to differentiate between the area's products include, inter alia, the difference between an insurance contract and the Articles of Association of pension funds and provident funds, granting guaranteed conversion factors in annuity insurance plans vs. lack of guarantee in pension funds, and non annuity paying plans in provident funds, and the materiality and scope of ancillary insurance coverages. The annuity coefficients reform as described in Clause 9.2.9 above, pursuant to which it is impossible to market insurance plans that include annuity coefficients up to the age of 60, as well as the possibility for managing companies of pension and provident funds to acquire insurance coverages starting from January 2013, cancel these differentiating characteristics between the area's products.

The tax benefits granted in training funds, and the minimum savings period required therein (6 years), are unique characteristics of training funds – hence, there is no substitute for training funds.

Among the area's products and other financial products (e.g., long-term deposits) there is lower changeability, since these products, usually, do not include two material elements (which do exist in the area's products) – tax benefits and a combination of risk and savings.

Regulatory changes, mainly changes in various tax benefits and the unification of tax benefits for the products, the setting of a unified model for management fees in savings products, the inability of insurance companies to market insurance plans that include guaranteed conversion coefficients for annuity, the possibility that managing companies of provident funds may market insurance coverages, may materially affect the internal changeability of the area's products, and the changeability level between them and other financial products, such that the differentiating characteristics that existed between the various products in the area were reduced.

9.7 Pension and provident – maximum statutory management fees and management fees collected in practice by the managing companies

9.7.1 Pension funds

Following are the maximum management fees statutorily allowed, management fees collected in practice, sales incentives granted to beneficiaries and average management fees in the years 2010-2012.

For the total management fees collected by the managing companies of the pension funds (both the old pension fund and new pension funds) in 2012 and total AUM, see Clause 11.2 hereinafter.

Old pension fund

Old fund (Yozma for the Self-Employed)	2012	2011	2010
		In percentage	
Statutory management fees [(1)]			
Rate of management fees from contributions fees	10.00	10.00	10.00
Rate of management fees from accrual	0.60	0.60	0.60
Rate of management fees collected in practice			
Rate of management fees from contribution fees	9.22	9.32	9.47
Rate of management fees from accrual	0.60	0.60	0.60
Sales incentives granted to beneficiaries			
Rate of management fees from contribution fees	-	-	-
Rate of management fees from accrual	-	-	-
Total average management fees rate[(2)]			
Rate of management fees from contribution fees	9.22	9.32	9.47
Rate of management fees from accrual	0.60	0.60	0.60

(1) Changes in maximum management fees in the management fees reform do not apply to old pension funds.

(2) The average management fees rate is the management fees collected in practice (less discounts granted to beneficiaries), and less sales incentives.

New pension funds

Comprehensive new pension funds	2012	2011	2010
		In percentage	
Rate of statutory management fees[(1)]			
Rate of management fees from contribution fees	6.00	6.00	6.00
Rate of management fees from accrual	0.50	0.50	0.50
Rate of management fees collected in practice			
Rate of management fees from contribution fees	3.97	3.95	4.08
Rate of management fees from accrual	0.36	0.37	0.38
Sales incentives granted to beneficiaries [(2)]			
Rate of management fees from contribution fees	0.05	0.04	0.05
Rate of management fees from accrual	-	-	-
Total average management fees rate[(3)]			
Rate of management fees from contribution fees	3.92	3.91	4.03
Rate of management fees from accrual	0.36	0.37	0.38

(1) The management fees reform as described in Clause 9.2.8 (b) (2) above did not change the maximum management fees rate in new pension funds, except setting additional arrangements regarding the maximum management fees rates from annuitants and beneficiaries with whom contact was lost, as described in the above mentioned Clause.

(2) Acquisition of complementary insurance coverages ("umbrellas") in 2010-2012 for beneficiaries, that are not included in the insureds' accrual, was presented within the sales incentives granted to beneficiaries.

(3) The average management fees rate is the management fees collected in practice (less discounts granted to beneficiaries), and less sales incentives.

(4) The rate presented in 2012 is after the discontinuation of the engagement with Customer A as defined in Note (1) to Clause 10.3.3 hereinafter, that the scope of assets and the scope of contribution fees of this Customer are as described in the above mentioned Clause, however the management fees rate collected by the managing company was significantly lower than the average management rate collected by the fund. As a result of the decline in the scope of assets and the scope of contribution fees in respect of this Customer, and the way to calculate the average management fees rate, in fact the erosion in effectiveness in the average management fees rate was not reflected.

New general pension funds			
		In percentage	
Rate of statutory management fees from accruals[(1)]	2.00	2.00	2.00
Rate of management fees collected in practice from accruals	1.11	1.09	1.07

(1) For the change in the maximum management fees rate in new general pension funds – see Clause 9.2.8 (b) (2) above.

9.7.2 Provident funds' managing companies

The maximum statutory annual management fees rate in provident funds, up until the reform in management fees – was up to 2.0% of accrual[35].

Upon the management fees reform, which came into effect in 2013, the maximum management fees in provident funds were changed – see Clause 9.2.8 (b) (3) above.

The maximum management fees rate in training funds are unchanged.

For the total management fees collected by the managing company (Migdal Makefet) in 2010-2012, see Clause 11.2 hereinafter.

Following is a specification of the management fees collected in practice, on average for 2010-2012, in % of accrual, in the funds that were active during that period:

	2012	**2011**	**2010**
		In percentage	
Total provident funds	**0.99**	**1.05**	**1.08**
Training Funds [(2)]			
Migdal Training Fund for Salarieds and Self-Employeds	1.08	1.15	1.18
Migdal Kahal Training Fund			
General track	0.94	0.95	0.99
General Maoz track	1.11	1.20	1.25
Stock-based track	1.16	1.23	1.30
CPI-linked track	1.07	1.16	1.25
Oversees track	0.98	1.12	1.06
Government bonds tracks	1.01	1.23	1.33
Short NIS track	1.08	1.18	1.25
Big general track	1.19	1.27	1.38
Bonds track	1.07	1.19	1.23
Forex track	1.06	1.27	1.34
Kosher track	1.02		
Migdal Platinum Training General Track		1.28	1.32
Migdal Platinum Training Platinum Track		1.18	1.26
New Makefet Training Fund			1.16

[35] The managing company had a provident fund for Migdal Insurance Company Ltd. employees which does not accept new deposits, whose management fees under the Articles of Association is 0%.

	2012	2011	2010
		In percentage	
Provident Funds for Benefits and Severance Pay			
Migdal for Benefits and Severance Pay	0.91	1.04	1.11
New Makefet Provident Fund for Benefits and Severance Pay(1)			0.89
Provident Fund of Migdal Insurance Ltd.'s Employees(1)			0.00
Migdal Platinum for Benefits (3)			
General track	1.15	1.24	1.32
Stock-based track	1.17	1.24	1.24
CPI-linked track	1.03	1.12	1.19
Oversees track	1.16	1.20	0.99
Government bonds tracks	1.01	1.23	1.31
Short NIS track	1.15	1.25	1.40
Platinum track		1.17	1.23
Big general track	1.16	1.25	1.34

	2012	2011	2010
		In percentage	
Central fund for Severance Pay			
Migdal Platinum for Employers	0.97	0.91	0.91
Migdal Central Fund for Provident Benefits	0.92	1.14	1.16
Other			
Makefet Sick Leave	0.42	0.42	0.42
Makefet Budgetary Fund	0.40	0.40	0.39

(1) In 2011, under the provident funds merger done in the Group, Makefet Training Fund was merged into Migdal Training and Makefet Provident Benefits and Migdal's Employees Fund was merged into Migdal Provident Benefits and Severance Pay.

(2) On January 1st, 2012, the merger of tracks in training funds came into effect as described hereinafter: the training fund "Migdal Kahal Training became a fund with a structure of ta rack fund. Under this framework, the assets started being managed within a general investment track named "Migdal Kahal Training General Track (Fund No. 386). The training fund Migdal Platinum Training, including its tracks, was merged into Migdal Kahal Training via the transfer of investment tracks and/or their merger into Migdal Kahal Training, as described hereinafter: Migdal Platinum Training General Track was merged into the track of Migdal Kahal Training General Track (Fund No. 386; the track Migdal Platinum Training Barometer Track was merged into the track Migdal Platinum Training Big Afikim (Fund No. 1157). The funds in Migdal Platinum Training, detailed hereinafter, were transferred into Migdal Kahal Training as new investments tracks: Big Afikim track (Fund No. 1157), Short NIS track (Fund No. 864), long term track (Fund No. 865), CPI-linked track (Fund No. 866), overseas track (Fund No. 868), stock-based track (Fund No. 869), bonds track (Fund No. 199), and Forex track (Fund No. 777). Migdal Maoz Training Fund was transferred into the Fund as a new investments track Migdal Kahal Training (Fund No. 599). Within the procedure and as an integral part thereof, there was an amendment to the Articles of Association of Migdal Kahal Training, such that: the name of Maoz Training Fund, which was transferred into the Fund as a new investments track, was changed to Migdal Kahal Training Maoz General Track, the name of Migdal Kahal Training Big Afikim Track was changed to Migdal Kahal Training Big General Track, and the name of Migdal Kahal Training Long Term Track was changed to Migdal Kahal Government Bonds Track.

(3) On January 1st, 2012, the merger of tracks in the provident fund also came into effect, as follows: in the provident and benefits fund Migdal Platinum for Benefits and severance Pay, the track Migdal Platinum for Benefits Barometer Track was merged into Migdal Platinum Benefits Big Afikim Track (Fund No. 1156). Within the change, the fund's Articles of Association was amended, such that now the track Migdal Platinum for Benefits Big Akikim is named Migdal Platinum for Benefits Big General, and the track Migdal Platinum for Benefits Long Term was changed to Migdal Platinum for Benefits Government Bonds.

10. The area's main products and services

10.1 General

The products sold in this area are: in life assurance – insurance policies; in pension funds – rights according to Articles of Association; in provident funds - rights according to Articles of Association. The products sold by the Group in this area are sometimes intertwined[36].

10.2 Life assurance

10.2.1 General

There are several types of basic life assurance policies combined with savings:

(a) **Managers insurance** – this policy is an insurance plan which is recognized as a provident fund (insurance fund), as defined under the Provident Funds Law, which combines saving for retirement and insurance coverages in case of death and occupational disability. The deposits to the policy are that of both employer and employee to severance pay, provident benefits and occupational disability. The fact that these policies are recognized as provident funds is that they entitle to tax benefits granted to provident funds. Prior to Amendment No. 3, it was possible to withdraw the savings for retirement also as a lump-sum withdrawal pursuant to the policy terms. The target audience is employers and their employees. Up until the reform in annuity coefficients as described in Clause 9.2.8 (b) (1) above, the withdrawal of an annuity in insurance plans that allowed withdrawing an annuity, was pursuant to annuity tracks set forth in the plan's conditions, and for some annuity tracks that were proposed, the annuity conversion coefficient was guaranteed, pursuant to the terms of the plan,

In 2012, these insurances[37] constitute about 67% of the Group's life assurance premiums, similar to 2011.

(b) **Individual insurance** (**with a savings component**) – designated for self-employed and individuals and includes two types:

(1) Policies that are approved as provident funds, i.e. enjoying tax benefits (self-employeds' policies). Until the end of 2003 the material insurance conditions of the policies that were offered to self-employeds were identical to the conditions of individual policies. As of 2004, the material insurance conditions of self-employeds' policies were made equal to those of managers' insurance.

(2) Policies that are not approved as provident funds, i.e. which do not enjoy tax benefits, except for 25% credit of the paid premium for death coverage included in the plan.

In 2012, individual insurances[38] constitute about 18%, and the other products constitute about 15% of the Group's life assurance premiums, similar to 2011.

The data referring to individual insurance in the tables in Clause 11.1 hereinafter include data regarding individual insurance both for policies acknowledged as provident funds (policies for the self-employeds) and for policies that are not acknowledged as provident funds.

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[36] This item includes a general and concise description of insurance products and insurance coverages. The full binding conditions are the ones set forth in each policy. The description is for reporting purposes only and shall not be used to interpret the policy in any way.
[37] Excluding ancillary coverages.
[38] Excluding ancillary coverages.

Investment tracks – as of 2004, the Group offers a choice between several investment tracks offered in insurance plans. As of 2006 the Company has been also offering the Life Cycle track within the investment tracks framework in some insurance plans. This track is comprised of three investment periods, at a decreasing risk level during the period, and a mechanism moving the pension savings monies between the periods at dates and as per parameters preset and defined in the plan (achieving yield for the transfer, insureds' age etc.). This track guarantees insureds, upon retirement, under certain terms and after a minimum period set forth in the plan, a safety net of guaranteeing CPI-linkage of the savings money in the track, less management fees. In March 2011 the marketing of this investment track was discontinued in its previous format, and instead the Company offers the Life Cycle 2011 track, which is composed of three investment cycles whose characteristics are similar to those described above. However, in this track the safety net was limited according to the conditions set in the plan. This investments track is no longer offered in insurance plans starting from January 2013, and as of that date it was also closed for new joiners in existing insurance plans.

10.2.2 **Managers insurances**

Managers' insurance policies are divided into several plans, according to their marketing date. **Traditional managers' insurance** (mainly endowment and annuity) (which was common until 1983); **Adif (Yoter)** managers' insurance (which was common as of 1983 until the end of 2003) and **new plans marketed since January 2004**.

(a) **Traditional managers' insurance (mainly endowment, annuity and pure savings)**

Endowment insurance includes two components: savings and risk, the amount of which is determined ahead of time according to the insured's age and underwriting terms set upon joining the insurance. The insurance amount is derived from the first premium transferred by the employer, and is fixed and linked to the policy's basic index upon entry. The cost of saving and risk coverages is intertwined. The insurance amount is paid at the end of the insurance period (mostly at the age of 65) as accumulated savings or in case of death occurred before the end of the insurance period. The proportional share of the risk component in case of death gradually diminishes from the insurance amount according to the policy's surrender value accrual. The endowment insurance, which was sold until the beginning of the 1990s, was often CPI-linked, including all its components, namely the premiums, the insurance amounts and the surrender value were indexed. If the wages grew beyond the CPI increase rate, this type of managers insurance cannot be increased and another policy had to be produced which would reflect this wage growth.

This product was the only product sold until 1982, and its share in total sales decreased ever since.

Annuity insurance is a traditional policy in which most of the premium is designed for paying annuity upon retirement. The future due annuity and the premium amounts are determined upon the production of the policy. Most policies of this kind, which were sold until the 1990s, were CPI-linked.

(b) **Adif managers' insurance (in the Group, the trade name of these policies is Yoter and Migdal My Investments)**

This policy was developed in 1983 and marketed until the end of 2003. This was the primary life assurance policy sold in the line. This product's main characteristics are as follows:

The policy enables dividing the premium into two components: a certain percentage which is accrued as savings (including coverage for annuity, which includes risk of prolonged life expectancy) and the rest of the premium is designated to acquire risk in case of death and operational and marketing expenses. The breakdown of the premium between the savings component and the risk component was set by the insured. Until the end of the 1990s, the basic rate which was designated for savings in these policies was usually 72% and above, while in the beginning of 2000's, the basic rate designated for savings was usually 80% and above.

Expense rate – in the policies participating in the investment profits, the expense rate is defined as a fixed rate of 0.6% of accrual, plus 15% real accrued spread, if such spread exists.

Starting October 2001, the Group enabled choosing between several investment tracks (bonds, shares, Forex etc.).

(c) **New plans marketed as of 2004**

As of 2004, the Group markets insurance plans that include the trade name Migdalor, which, from time to time, were adjusted to the changes were recorded in the legislative arrangements. In these plans, following the reform in life assurance, there is a separation between the components of savings, risk and management fees. Coverage for death or occupational disability may be purchased. The balance of premium that is not paid for the acquisition of the coverage insurance and expenses, is aimed for the savings that may be withdrawn or as capital or as annuities, depending on the relevant years (starting from 2008 the monies are for annuity savings only).

As to management fees, there are two types of plans – one in which the expense rate to premium decreases gradually, and the second is a fixed expense rate to premium, along the policy's entire life.

Starting from 2004 insurance plans that include savings are also divided into insurance plans recognized as provident funds and insurance plans that are not recognized as provident plans.

Some of the products that were marketed and/or are marketed allow lump sum deposits against receiving an immediate annuity or a deferred one, depending on the conditions of the insurance plans in the relevant periods. Some of the insurance plans that were marketed in the past guaranteed a secured interest rate or a minimal yield, depending on the conditions set forth in the insurance plans.

10.2.3 **Plans marketed as of January 2013** – in 2013, after the coming into effect of the management fees reform and the annuity coefficients reform, as described in Clauses 9.2.8 and 9.2.9 above, the Group adjusted the insurance plans, both those recognized as provident funds and those not recognized as provident funds, to the changes in legislative arrangements.

10.2.4 **Various risk products**

(a) **Pure insurance risk - individual**

Life assurance in case of death without a savings component. This insurance guarantees the beneficiaries a predetermined insurance amount if the insured passes away during the insurance period. The amount of the insurance can be a one-time amount, or a predetermined monthly payment for a predetermined period, depending on the relevant insurance plan. The insurance period is between one year and several years, usually not beyond the age of 65. In certain cases it can be extended until the age of 75. The premium in respect of this insurance plan usually changes every year or every five years.

(b) **Pure life assurance risk - collective**
Life assurance in case of death without a savings component. This insurance is marketed to large groups of similar features, and the collection is usually made in one payment for the entire group beneficiaries. The insurance amounts are usually the same for all the group's beneficiaries, or are determined pursuant to various criteria such as marital status, etc.

10.2.5 **Occupational disability insurance**

(a) **Occupational disability insurance – individual**
Coverage guaranteeing a monthly compensation of no more than 75% of the salary in case of occupational disability, and exemption from premium payments. The compensation is paid as long as the insured is occupationally disabled or until the end of the insurance period (usually at age 65 or 67), the earlier of the two. The employers and self-employed were granted tax benefits in respect of provisions to such coverage under certain restrictions.

(b) **Occupational disability insurance – collective**
This insurance is marketed to large groups that share common characteristics, and the collection is usually made in one payment for the entire group members. The insurance amounts are usually the same for all group beneficiaries, or set by various criteria, such as family status etc.

10.2.6 **Occupational disability insurance**

Death by accident insurance – insurance which guarantees a lump sum payment in case of death caused by accident.

Disability by accident insurance – insurance which guarantees a lump sum payment in case of disability caused by accident. The amount of the lump sum compensation is set according to the determined disability percentage.

For details regarding premiums of various products, see Clause 11.1 hereinafter.

10.3 Pension products

10.3.1 **General**

The proposed pension plans are based on the pension funds Articles of Association.

As mentioned in Clause 9.3 above, the pension products differ from life insurance in that they are a mutual insurance plan and acquiring rights based on Articles of Association that may be changed from time to time, as per the Articles of Association effective at the time of entitlement.

(a) **Old pension funds**
The Group has an old pension fund for the self-employed, which is managed by Yozma Pension Fund for the Self-Employed Ltd. This fund is an old pension fund based on personal actuarial balance mechanism. The fund was closed to new joiners following the pension funds reform in 1995. The fund was approved as an annuity paying provident fund according to the Income Tax Regulations, of the comprehensive pension type.

(b) **New pension funds**
The Group has two new pension funds managed by Migdal Makefet, a new comprehensive fund – **Migdal Makefet Ishit** and a general pension fund – **Migdal Makefet Complementary**.

Migdal Makefet Ishit is a pension fund designated for current deposits of employees and self-employed members up to the allowed ceiling for deposits. The fund offers a variety of pension tracks that include insurance coverage in case of disability and death. The savings part in the fund is paid as old age pension as of retirement age.

Migdal Makefet Complementary is a general pension fund designated for current deposits, including deposits in amounts exceeding the allowed ceiling for new pension funds, and it also allows making one-time deposits. Starting from January 2008, in addition to saving for old age pension starting from age 60, this fund offers a variety of pension tracks that include insurance coverage in case of disability and death, and as of that date it also operates as a comprehensive pension fund. This fund is not entitled to designated bonds.

As of 2011 Migdal Makefet has been also offering investment tracks in the said pension funds.

10.3.2 **Amendments to pension funds' Articles of Association**

(a) In the reported year, Migdal Makefet Complementary's Articles of Association were amended as to the structure and rate of management fees that managing companies may collect, pursuant to the management fees reform as described in Clause 9.2.8 (b) (2) above.

(b) Expected amendments in the Articles of Association:

(1) Pursuant to the annuity coefficients reform and the Commissioner Circular mentioned in Clause 9.2.9 (a) (2) above, regarding a change in the array of demographic assumptions in pension funds, the managing companies should update the Articles of Association of the funds under their management.

(2) **Safety cushion for old pension funds** – a **Bill for the Amendment of the Control of Financial Services (Insurance) (Amendment No. 27) (Safety Cushions for Old Pension Funds) Law – 2012** is pending. This Bill proposes to anchor in the Control Law the granting of a safety cushion to old pensions in the arrangement, pursuant to the conditions and in the scopes set forth as detailed in the Bill. Furthermore, it is proposed to include another separate safety cushion for old pension funds not included in the arrangement, including Yozma Pension Fund for Self-Employeds, as per the principles and conditions detailed in the Bill. The proposed safety cushion is aimed at covering the deficit that might originate in the funds following the decline in the expected interest rates, based on which the funds' balances in the funds' balance sheets are calculated ("interest rate curve") compared with an interest of 4%, CPI-linked. Changes in the interest rate curve are the main reason for the volatility in the amount of annuities paid by pension funds to those entitled.

In order to moderate the impact of the changes in the interest rate curve, it is suggested that old pension funds not included in the arrangement, to receive monies from the State's budget pursuant to arrangements and subject to the conditions set forth in the Bill, however, in order to receive a safety cushion, old pension funds are required to introduce changes to their Articles of Association, as follows: increasing the retirement age, reducing annuities to those who want to receive annuities before retirement age, reducing annuities to those who want to receive annuities before the updated retirement age, deducting amounts from annuities whose rate varies between 0.25% and 1.75% for about 5 years.

The fund's management examines the aforesaid Bill and negotiating vis-à-vis the Commissioner in the MoF, in order to examine the proposals and the implications over the fund's liabilities and the deriving impact on beneficiaries' rights.

10.3.3 **Following are details about the pension plans offered by the Group (in NIS million)**:

Type of fund	Name of the fund	Name of the managing company	Date of establishment	Pension contributions in 2012 (1)	Managed assets as of 31/12/2012 (2) (3)
Old, rights-based	Yozma Pension Fund for the Self-Employed	Yozma Pension Fund for the Self-Employed Ltd.	1981	25	1,448
New	Migdal Makefet Ishit	Migdal Makefet Pension and Provident Funds Ltd.	1995	4,296	30,518
New, general	Migdal Makefet Complementary	Migdal Makefet Pension and Provident Funds Ltd.	2003	65	339
Total funds				**4,386**	**32,305**

(1) The contribution fees do not include money transfers in respect of beneficiaries' transition from one fund to another. The money transfers to the Group's new pension funds totaled approx. NIS 297 million, while the money transfers from the Group's new pension funds to other funds totaled approx. NIS 1,066 million.

Out of the amount of transfers from the Group to other funds as set forth above, approx. NIS 490 million are attributed to a customer of Migdal Makefet, whose contribution to contribution fees in 2011 totaled approx. 5.0% of the total pension fund's contribution fees, and approx. 1.9% of AuM as of December 31st, 2011 ("**Customer A**"), that the engagement with him was discontinued in July 2012 following a tender published by him. Migdal Makefet decided, due to commercial and competitive discretions, not to participate in it.

(2) The assets in Migdal Makefet Ishit include assets totaling approx. NIS 29,170 million managed in a general track, approx. NIS 79 million that are managed in the religious authorization track, approx. NIS 30 million managed in the stock-based track, approx. NIS 24 million managed in the short term track, approx. NIS 62 million managed in the bonds and deposits track and approx. NIS 1,153 million managed in the pensioners track.

(3) The assets in Migdal Makefet Complementary include assets totaling approx. NIS 314 million that are managed in a general track, and approx. NIS 25 million that are managed in the pensioners track. In the other investment tracks, immaterial sums are invested.

For comparative data as regards contribution fees and managed assets, see Clause 11.2 hereinafter.

10.4 Provident products

10.4.1 General

Provident funds are established according to the Provident Funds Law and their rights are established under the Provident Funds Law and the various provident funds Articles of Association. The monies invested in the provident funds are usually designated for the medium term (training funds) and the long term (personal funds for provident benefits and severance pay) and they benefit from various tax benefits. As of 2008, following the products reform, provident funds are used for deposits to annuity, but not as paying funds to annuity.

The scope of provident funds assets managed by the Group, as at December 31st, 2012, totals approx. NIS 14.6 billion.

10.4.2 **Specification of main provident products**

Training fund - the fund is aimed at both employees and self-employed. It allows beneficiaries to accumulate monies for training purposes, while enjoying tax benefits. The accrued monies of the fund may be withdrawn for training purposes after three years of membership in the fund. After six years of membership in the fund, the monies can be withdrawn for any purpose. After the Bachar Legislation, training funds have become a product that is considered both a pension product and a financial product, so that a marketing agent of financial products can also market it.

Personal fund for provident benefits and severance pay – the fund is aimed at both employees and self-employed. The deposits in the fund are on a monthly basis for employees. Self-employed persons may deposit monies periodically.

Central provident fund for severance pay – the fund is aimed at employers who wish to accrue monies for guaranteeing employees' severance payments. The beneficiary is the employer and the accrual of monies is centralized at the employer's name for the employees. The provisions for the fund are recognized as expenses for the employer and the monies are at his disposal until they are released on behalf of the employee. Following Amendment No. 3 to the Provident Funds Law, as of January 2011, central provident funds for severance pay may not absorb new monies.

Sick pay provident fund – allows the employer to accrue monies in the fund for payment of sick leave.

Central provident fund for participation in an unfunded pension – the fund is aimed at managing the sums deducted by employers, defined in The Economic Recovery Plan Act (Legislative Amendments for the Achievement of the 2003 and 2004 Economic Policy and Budgetary Objectives) - 2003, from the salary of an employee employed by that employer, namely employers to whom an unfunded pension arrangement applies. The deduction rate as of 2005 is 2% of the employee's salary. In some of the funds, the Group allows beneficiaries to choose between different investment tracks.

In some of these provident funds the Group allows beneficiaries to choose various investment tracks.

10.4.3 **Amendments to the provident funds Articles of Association in the reported year**:

In the reported year, several changes were made in the Articles of Association of some provident funds in which there was a change in the structure and rate of maximum management fees, allowing managing companies to collect management fees in the relevant funds pursuant to the management fees reform as described in Clause 9.2.8 (b) (3) above.

Proposal for a standard Articles of Association – in January 2013 the Commissioner of Insurance published a Draft Circular regarding "Standard Articles of Association for Non-Paying Provident Funds, Provident Funds for Benefits, and Individual Provident Funds for Severance Pay". The draft is aimed at creating homogeneity between the provident funds' Articles of Association and match between the law provisions and legislative arrangements and the managing companies' Articles of Association.

10.4.4 **Following are data about the provident funds managed through Migdal Makefet**:

Migdal Makefet, which also manages new pension funds, also manages a variety of provident funds of different features, according to the type of fund and nature of investments. Following are data of the provident funds managed through Migdal Makefet in the reported year (the financial data are in NIS million)[39]:

Name of the fund	Date of establishment	Contribution fees in 2012	Managed assets as of 31/12/12
Training funds			
Migdal Training Fund for the Self-Employed and Salarieds	1997	532	2,501
Migdal Kahal Training Fund			
General track	1979	881	7,931
General Maoz track	1998	13	165
Stock-based track	2003	12	92
CPI-linked track	2003	9	87
Overseas track	2003	1	7
Government bonds track	2003	49	468
Short NIS track	2003	39	305
General Big track	2005	116	759
Bonds track	1996	28	310
Forex track	2002	0	3
Religious authorization track	2012	1	5

[39] Not all tracks were operated.

Name of the fund	Date of establishment	Contribution fees in 2012	Managed assets as of 31/12/12
Provident funds for provident benefits and severance pay			
Migdal Provident Funds for Provident Benefits and Severance Pay	2002	62	1,008
Migdal Platinum for Provident Benefits			
General track	2004	5	120
Stock-based track	2003	1	16
CPI-linked track	2003	1	57
Overseas track	2003	0	2
Government bonds track	2003	4	185
Short NIS track	2003	1	50
General Big track	2005	5	213
Central fund for severance pay			
Migdal Platinum for Employers	2003	0	9
Migdal Central fund for Severance Pay	2002	0	213
Other			
Makefet Sick Leave	2005	0	32
Makefet Budgetary	2008	4	20
Total		**1,764**	**14,558**

(1) The contribution fees do not include money transfers in respect of beneficiaries' transition from one fund to another. In 2012, the money transfers to the Group provident funds totaled approx. NIS 592 million, while money transfers from the Group's provident funds to other funds totaled approx. NIS 1,026 million (including money transfers between the companies managing provident funds in the Group).

For comparative data as regards contribution fees and managed assets, see Clause 11.2 hereinafter.

11. Data breakdown of products and services

11.1 Life assurance

Following are data, in NIS million, about life assurance products between the years 2010-2012, divided into profit participating portfolio, guaranteed-yield and other insurances.

The association of the products in the said breakdown is based on the nature of the insurance reserve held against the main product to which the product is attached. The term "guaranteed-yield" includes both plans against which designated bonds were issued, and guaranteed-yield plans, although no designated bonds were issued in their respect[40].

[40] The Group offered several life assurance plans that combine savings and guarantee CPI-linking and a certain interest for a predetermined period, however these insurance plans are not backed by designated bonds, but in other financial arrangements made by the Company in order to back up the linking and interest differences for the pre-set period in these plans.

Year 2012

Gross premiums	Profit participating portfolio	Guaranteed-yield	Other	Total
a. Managers insurance				
Adif (Yoter)	1,992	309		2,303
Traditional	10	50		60
Policies issued starting from 1.1.2004	2,541			2,541
b. Individual insurance				
Adif (Yoter)	228	56		284
Traditional	45	33		78
Policies issued starting from 1.1.2004	964	45		1,009
c. Pure risk insurance				
Individual	444		26	470
Collective			79	79
d. Occupational disability insurance	428		54	482
e. Other	43		11	54
f. Total gross premium	**6,695**	**493**	**170**	**7,358**
Receipts in respect of investment contracts (1)	272			272
g. Insurance liabilities	**58,920**	**23,435**	**1,127**	**83,482**

(1) For the classification of "investment contracts", see Note 2 I 1 i) to the Financial Statements.

For investments parallel to the above liabilities, see Note 37 c to the Financial Statements.

In 2012, premiums in the amount of approx. NIS 203 million of the product Migdal Batuach and Migdal Batuach 2009, which guarantee yield although no designated bonds were issued against them, were included in the profit participating portfolio (the marketing of these plans was discontinued in March 2011).

The premiums and receipts in respect of investments contracts include the transfer of monies to Migdal Insurance from other entities in respect of incoming mobilization, which totaled in 2012 approx. NIS 409 million. For further details, including data about money transfers from Migdal Insurance to other entities, see Note 18 e to the Financial Statements.

Year 2011

Gross premiums	Profit participating portfolio	Guaranteed-yield	Other	Total
a. Managers insurance				
Adif (Yoter)	1,979	307		2,286
Traditional	11	57		68
Policies issued starting from 1.1.2004	2,209			2,209
b. Individual insurance				
Adif (Yoter)	239	56		295
Traditional	51	37		88
Policies issued starting from 1.1.2004	810	30		840
c. Pure risk insurance				
Individual	397		28	425
Collective			105	105
d. Occupational disability insurance	411		63	474
e. Other	44		12	56
f. Total gross premium	**6,152**	**487**	**208**	**6,846**
Receipts in respect of investment contracts				
g. Insurance liabilities	**50,431**	**22,093**	**1,079**	**73,603**

For investments parallel to the above liabilities, see Note 37 c to the Financial Statements.

Year 2010

Gross premiums	Profit participating portfolio	Guaranteed-yield	Other	Total
a. Managers insurance				
Adif (Yoter)	1,962	310		2,272
Traditional	12	62		74
Policies issued starting from 1.1.2004	1,849			1,849
b. Individual insurance				
Adif (Yoter)	242	57		299
Traditional	57	41		98
Policies issued starting from 1.1.2004	659	12		671
c. Pure risk insurance				
Individual	341		28	369
Collective			115	115
d. Occupational disability insurance	383		61	444
e. Other	43		11	54
f. Total gross premium	**5,548**	**482**	**215**	**6,245**
Receipts in respect of investment contracts				
g. Insurance liabilities	**49,013**	**20,977**	**1,203**	**71,193**

For investments parallel to the above liabilities, see Note 37 c to the Financial Statements.

11.2 Pension funds

Following are data about the managing companies of pension funds between 2010-2012, in NIS million:

Yozma for the Self-Employed - Old pension fund

	Revenues from management fees						
	Management fees from assets	**Management fees from contribution fees**	**Less sale incentives to beneficiaries**	**Total**	**Income for the period before tax**	**Collected contribution fees**	**Total managed assets**
2012	9	2	-	11	3.3	25	1,448
2011	8	2	-	10	4.4	27	1,327
2010	8	2	-	10	4.5	26	1,308

The "income for the period before tax" data reflect the management fees income received by Migdal from the managing company, less commissions and expenses Migdal paid in respect of said activity.

Migdal Makefet - new pension funds

	Revenues from management fees						
	Management fees from assets	**Management fees from contribution fees**	**Less sale incentives to beneficiaries**	**Total (1)**	**Income before tax(1) (2)**	**Collected contribution fees(3)**	**Total managed assets**
2012	106	169	2	273	70	4,361	30,857
2011	93	149	2	240	65	3,892	25,846
2010	79	136	2	213	59	3,392	23,090

Data about collected contribution fees and total managed assets include Makefet Ishit and Makefet Complementary.

For further details about the financial data presented in the above tables, see Clause 8.1 in Part B above.

(1) The presented profits for the period are the profits of the managing company after settling with Migdal Insurance as set forth in Note (2) hereinafter.

(2) Some of the institutional organs' employees in the Group are employed jointly, mainly the Customer and Distribution Channels Division employees, Investment Division employees and some of the HQ Division employees. In 2010 the allocation of costs and settlements between Migdal Insurance and Migdal Makefet in respect of the joint services was based on a settlement formula set by a model of allocating expenses in respect of pension or provident activity, as the case may be, which is attributed to the relevant managing company. As of 2011, the allocation of costs and settlements in respect of the joint services was based on an updated expenditure allocation formula which reflects G&A expenses in practice in respect of the pension and provident activity attributed to the managing company. The settlement formula is based on economic parameters that are examined from time to time. In addition, the managing company bears the cost of payment to various marketing agents. Furthermore, there are additional payments in respect of computerization services, investments management and other expenses. Also, as of January 2011 the investment management of some of the provident funds managed by Migdal Makefet is done through Capital Markets Group for a predefined consideration.

(3) The collected contribution fees do not include data regarding money transfers in respect of beneficiaries transferring from one fund to another. For data regarding money transfers in 2012 as said, see Clause 10.3.3 above.

11.3 **Provident funds**

Following are data regarding profit from provident activity between 2010-2012, in NIS million:

	Revenues from management fees (from assets)	Income for the period before tax(1)	Collected contribution fees(2)	Total managed assets
2012	140	19	1,765	14,559
2011	143	20	1,689	13,580
2010	146	16	1,627	14,316

(1) It should be noted, that the profit presented in 2010 is the profit of the provident funds' managing companies before the structural change in the provident funds that was executed in 2011. Starting from 2011 profit is presented as part of the provident activity in the managing company Migdal Makefet which also manages the provident funds, and also includes the settlements with Migdal Insurance as described in Note (2) of the previous table.

(2) The collected contribution fees do not include data regarding money transfers in respect of beneficiaries transferring from one fund to another. For data regarding money transfers in 2012 as said, see Clause 10.4.4 above.

12. Customers

12.1 **General**

The Group’s customers are divided into three main groups: employers and employees, individuals and self-employed, and collectives. In all three groups there is a wide dispersion of customers. In the new pension funds managed by Migdal Makefet and Kahal Training Fund there is a concentration of large customers, which are not related to each other, but are characterized by a centralized engagement with the beneficiaries through Employees' Committee, Employees' Association or the employer.

The Group does not have customers who constitute 10% or more of its total premiums and contribution fees in the area of life assurance and LTS.

12.2 **Life assurance**

Following are data regarding the premiums breakdown in life assurance in 2011-2012:

	2012		2011	
	NIS million	Breakdown in %	NIS million	Breakdown in %
Employers (managers insurance)	5,340	73	4,982	73
Individuals and self-employed (individual insurance)	1,913	26	1,727	25
Collectives	105	1	138	2
Total	**7,358**	**100**	**6,847**	**100**

12.3 **Pension funds**

Following are data regarding the breakdown of contribution fees in pension funds in 2011-2012:

	2012		2011	
Pension funds (new and old)	**NIS million**	**Breakdown in %**	**NIS million**	**Breakdown in %**
Salaried beneficiaries(1)	4,151	95	3,775	96
Individual and self-employed members	235	5	144	4
Total	**4,386**	**100**	**3,919**	**100**

(1) The contribution fees from Customer A as defined in Note (1) to the Table in Clause 10.3.3, with whom the engagement was discontinued in July 2012, totaled approx. NIS 200 million in annual terms.

12.4 **Provident funds**

Following are data regarding the breakdown of contribution fees in provident funds in 2011-2012:

	2012		2011	
Provident funds	**NIS million**	**Breakdown in %**	**NIS million**	**Breakdown in %**
Salaried beneficiaries	1,498	85	1,390	82
Individual and self-employed members	268	15	299	18
Total	**1,766**	**100**	**1,689**	**100**

12.5 **Rate of surrenders**[41]

In 2012, the rate of surrenders from the average reserve in **life assurance** totaled about 2.3% vs. about 2.4% in 2011.

In **pension**, the surrender rate from accrual totaled approx. 5.8% in 2012 vs. approx. 3.9% in 2011. The increase was affected by the discontinuation of the engagement with Customer A as per its definition in Note (1) to the Table in Clause 10.3.3 above.

In **provident**, the surrender rate from accrual totaled approx. 17.3% in 2012 vs. approx. 16.6% in 2011.

13. Marketing and distribution

13.1 Life assurance

Most of the Group's insurance plans are marketed through affiliated insurance agents, including agencies held by the Group, which are an important marketing and distribution channel for the Group in respect of all LTS products marketed by the Group. Most of the agreements with agents are not exclusive, and the agents, including the Group-held agencies, work with other insurance companies as well.

In 2012, the share of Group-held agencies (including data about sub-agents of said agencies) in life assurance premiums totaled approx. 31.2%, vs. 31.8% in 2011.

Among the Group Customer Division employees who handle the Group's sales, there are also pensionary marketing agents (acquisition supervisors) whose role is encouraging agents to make new sales. Part of these marketing agents' salary structure is based on the sales of the agents for whom they are responsible.

[41] Surrender rate, including outgoing mobilization.

Some of the collective policies, as well as other policies in a limited scope, are marketed through direct sale by the Group.

13.2 Pension and provident

Migdal Makefet holds three distribution channels parallel to marketing the pension and provident funds it manages, through the Customers Division:

Direct distribution – through pensionary marketers who are part of the Customers Division, working directly vis-à-vis employees' committees and trade unions, including by participating in tenders they publish.

External pensionary marketers (insurance agents) – through the insurance agents, including the Group's agencies.

Pensionary advisors – via a number of banking institutions with whom it is engaged in distribution agreements.Migdal Makefet has engaged with several banks in distribution agreements to distribute the pension funds it manages.

The share of distribution channels is as follows:
Pension - direct sales – about 32% of the contribution fees (30% in 2011), sales through agents – about 67% of the contribution fees (69% in 2011), out of which about 29% of the contribution fees (33% in 2011) are through agencies held by the Group, and sales through banks – approx. 1% of the contribution fees (similar to 2011).

Provident - direct distribution – about 50% of AuM (53% in 2011), insurance agents – about 29% of AuM (27% in 2011) and banking corporations - approx. 21% of AuM (20% in 2011).

13.3 Commissions

13.3.1 Insurance agents

The Group pays variable commissions to insurance agents in respect of marketing its products; the commission rate varies according to the sold plan and to individual agreements entered with the agents.

The commission structure in **life assurance**:
Current commissions from premium - the commissions paid to agents are “flat commissions”, i.e. the same commission is paid for several years, after which a collection fee that is usually lower than the flat commission is paid (in most of the Group-marketed insurance plans, the commission is paid for 15 years and in others, for 10 years); in certain products the commission is paid at a fixed rate out of the management fees from accruals; “portfolio persistency commission” – that is usually derived from the agents’ portfolio persistency level in respect of insurance plans sold starting from June 2001 from the scope of their insurance portfolio and the meeting of sales objectives, and in addition a commission from accrued savings in respect of paid up insurance plans sold after June 2001 is paid, subject to compliance with objectives; prizes/grants –usually this commission is derived from the scope of sales and the agents' compliance with the sales objective set for them, and in some savings policies the commission is calculated as a function of parameters that affect the product profitability, and it is paid subject to the arrangements referring to the cancellation of policies in a predetermined period. In addition, the Group holds sale campaigns under which it remunerates agents with additional prizes and/or grants; in certain insurance products – fixed commissions are paid, which are based on the scope of accrual in the policy or scope of accrual transferred as a lump sum deposit.

The structure of commissions in respect of **pension products**' marketing is:

Current commissions from contribution fees at a fixed rate from the contribution fees collected in practice; prizes/grants – the Group pays agents a commission which is usually derived from the scope of sales and the agents' compliance with the sales objective set for them, as a function of parameters that affect the product profitability, and it is paid subject to cancellations as described above regarding life assurance policies. In addition, the Group holds sale campaigns under which it remunerates agents with additional prizes and/or grants; sometimes the Group pays fixed commissions derived from the scope of accrual.

The commissions paid to insurance agents in respect of marketing **provident funds** are, usually, at a fixed rate of the management fees of accrual collected in practice.

Starting from January 2013, the following changes were made: the portfolio persistency commission in respect of new sales of products that will be sold starting from 2013 in managers' insurance and self-employeds was cancelled; there are several changes regarding the classification of commissions as a function of sales volume; the period for the non-cancellation of policies as described above was extended.

The Group sometimes extends loans to its agents, secured by future commission flows or other collaterals. The loans are extended at commercial terms within the general terms set forth by the Commissioner.

For the proposed changes in agents' commissions, see Clause 9.2.11 (b) above.

13.3.2 **Pension advisors**

In their role as pension advisors, banks are entitled to distribution commissions as per the Distribution Regulations regarding Pension and Provident Products. For the distribution commission rate see Clause 45.2.3 (e) in Part E hereinafter.

Migdal Makefet has distribution agreements with Leumi Bank and Discount Bank, according to which these banks will distribute Kahal Training Funds (which were purchased from the said banking corporations) in return for the maximum distribution commission set in the Distribution Regulations. The effect of agreements regarding Kahal Training Fund is for a period of 10 years starting July 2007.

In addition, Migdal Makefet has other distribution agreements with some of the banking corporations referring to the new pension funds and other provident funds it manages. These distribution agreements do not set a period and can be terminated by early notification. The undertaking is paying maximum distribution commissions as per the Distribution Regulations. Some of these agreements also include arrangements in the event that the maximum rates of distribution commissions will change.

13.3.3 **Commission rates**

(a) **Life assurance**

The commission rate out of premium in life assurance totaled approx. 8.1% in 2012 vs. approx. 8.2% in 2011.

The average commission rate in the first year from the new annualized premium totals approx. 25.4% vs. approx. 29.1% in 2011.

The weighted commission rate in terms of present value, without taking into consideration cancellation assumptions, totals approx. 7.6% vs. approx. 9.4% in 2011. This rate reflects the commissions' future flow capitalization vs. the premiums' future flow capitalization.

(b) **Pension funds**
The commission rate out of contribution fees in the new pension funds totaled approx. 2.8% in 2012, similar to 2011.

(c) **Provident funds**
The commission rate from accrual totaled some 0.2% in 2012, similar to 2011.

14. Reinsurance

For reinsurance, including the types of agreements in reinsurance and the commissions received or paid to reinsurers – see also Clause 47 in Part E hereinafter.

Life assurance - the Group acquires reinsurances in respect of the risk component of life assurance policies (death, disability and occupational disability risks). The scope of the reinsurance premium in the Group's life assurance is about 2.9% of the current premium.

Reinsurance for death, disability and occupational disability risks is preformed via Surplus or Quota share Treaties.

Furthermore, there are facultative treaties, performed in order to cover risks embedded in specific policies.

In 2012, the coverage ceiling in a Surplus treaty for insurance of death risk is approx. NIS 8,568 thousand per insured, and in a Quota share treaty for insurance of occupational disability risk, the coverage ceiling for monthly compensation is approx. NIS 47.7 thousand per insured.

In 2012, the Company had a reinsurance treaty for coverage of death cases in catastrophic events at an amount of approx. USD 150 million, over USD 80 million in case of war, and over USD 40 million in case of earthquake.

In the reported year, reinsurance treaties in life assurance were usually made with A plus rated companies (as per S&P rating, or the rating of another rating company whose rating was converted as per an index set forth under the Investment Regulations).

For data regarding the premium paid to reinsurers, reinsurers' share in claims, as well as commissions paid by reinsurers, see Notes 3 b, 3 c and 37 to the Financial Statements.

The Group has several reinsurers, whose share in the life assurance reinsurance premiums in the reported year is 10% or more, as follows:

		2012		2011	
Name of reinsurer	**Rating according to S&P[42]**	**Reinsurance premium ceded to the reinsurer (in NIS million)**	**Rate out of total reinsurance premiums in life assurance in percentage**	**Reinsurance premium ceded to the reinsurer (in NIS million)**	**Rate out of total reinsurance premiums in life assurance in percentage**
Generali	A	66.7	42	81.7	46
Swiss Re	AA-	27.3	17	31.3	17
Munich Re	AA-	30.1	19	33.5	19

Pension – Makefet Ishit pension fund has a reinsurance treaty for the coverage of death in catastrophic events (without coverage of plague). The total compensation is USD 50 million, over retention of USD 15 million, in case of multiple injuries including war and earthquake. The coverage ceiling per insured is approx. USD 1 million. The cost of reinsurance premiums is paid off the fund assets.

[42] The rating set forth in the table is effective as at the date close to the report publication.

The Makefet Comprehensive pension fund has a quota reinsurance treaty covering 90% in case of death and/or disability of the active fund beneficiaries who are not in the basic old age track, paid as per the fund Articles of Association. Coverage is obligatory and is up to an amount at risk of approx. NIS 4.5 million in case of death and approx. NIS 7 million in case of disability, for each insured. The cost of reinsurance premiums for 2012 is paid off the assets of the active beneficiaries who are not in the basic old age track.

15. Suppliers and service providers

The Group has agreements for the procurement of products and professional services in various areas. The Group companies bear, like any other insurer, the expenses related with the insurance event insured by the policy. These expenses include covering the cost of various services covered by the insurance policies. In addition, the Group acquires ancillary services for the settlement of insurance claims in various areas, such as attorneys, investigators and medical experts.

Migdal Makefet receives operating services from Leumi Capital Markets Services Ltd.(previously "Leumi Gemel") for some of the provident funds it manages and some provident funds were operated via another supplier ("another supplier") until December 2012. The agreement with Leumi Gemel was first signed for a period of 5 years as of July 15th, 2007, with an automatic renewal for one year, every year, and it referred mainly to the provident funds acquired from Bank Leumi and Discount Bank in 2007 (mainly Kahal Training Fund). As part of Migdal Makefet's deployment towards the merger of provident funds of the same type managed by it, it was agreed that Leumi Gemel shall grant operation services for all provident and training funds managed by Migdal Makefet, as well as those operated by the other supplier. The funds that were previously operated by the other supplier were added in January 1st, 2013, and the agreement is effective for three years. For details regarding this engagement, see the Company's Immediate Report dated January 15th, 2013, Reference No. 2013-01-013635.

Regarding receiving services from Migdal Capital Markets and the joint employment with Migdal Insurance, see Note (2) to Table 11.2 above.

For the types of suppliers who are not unique to this area of activity, see Clause 48 in Part E hereinafter.

16. Competition

16.1 Market data

16.1.1 Life assurance

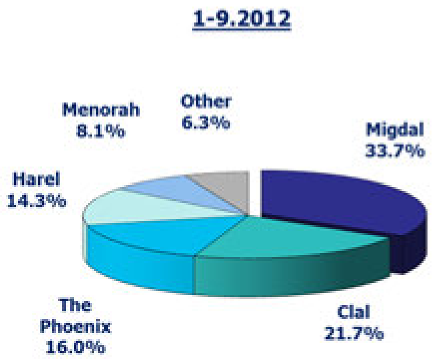
The life assurance line is held by five main groups (Migdal, Clal, The Phoenix, Harel, and Menorah), which constituted, in the first nine months of 2012 about 94% of the total premiums in the line[43].

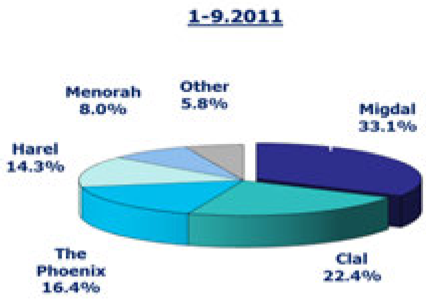
Migdal Group is the largest, leading group in the life assurance line.

The following charts detail the breakdown of life assurance premiums and insurance liabilities between the insurance groups in the first nine months of 2011 and 2012[44]:

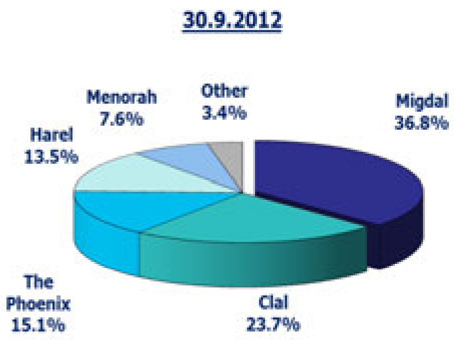
[43] The data are based on a processing of MoF reports published on the website ("Managerial reports").
[44] The data are based on a processing of MoF reports published on the website ("Managerial reports").

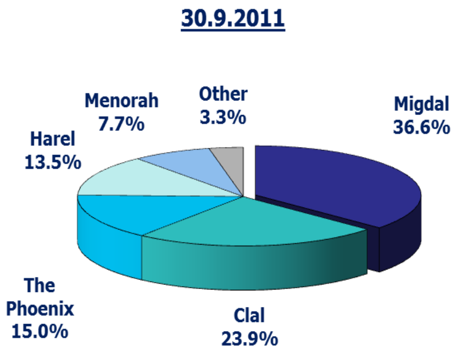
Distribution of life assurance premiums





Distribution of insurance liabilities in life assurance





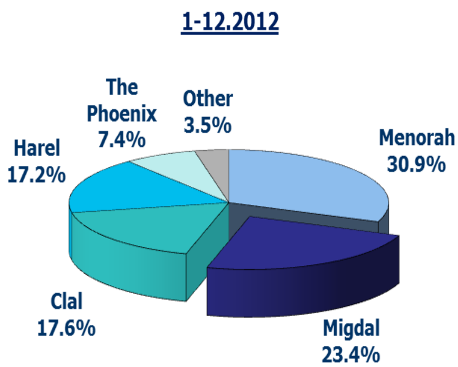
16.1.2 **New pension funds**

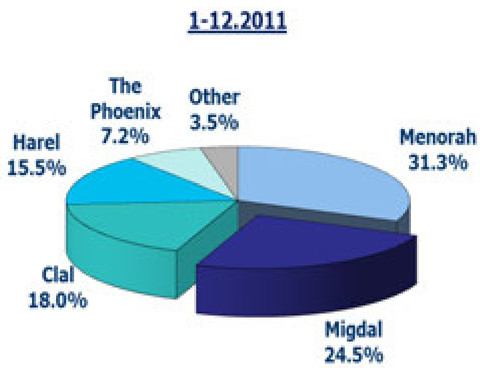
Based on contribution fees for 2012, insurance companies in the pension line[45] hold a market share of about 98% of the new pension funds' contribution fees, out of which the four insurance groups – Menorah, Migdal, Clal and Harel, hold a market share of about 89%.

Migdal Group is second largest, while the largest group in the new pension funds line is Menorah Mivtachim Group.

The following charts detail the breakdown of contribution fees, managed assets and net accruals in the new pension funds.

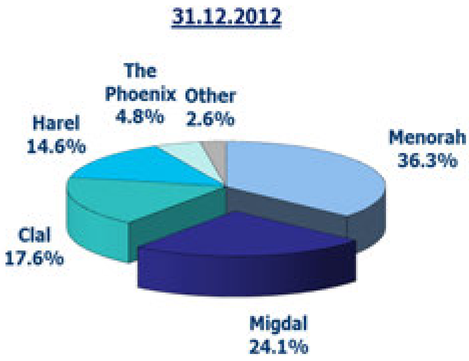
Distribution of contribution fees in the new pension funds

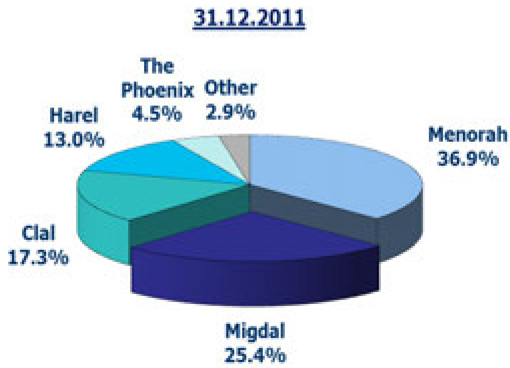




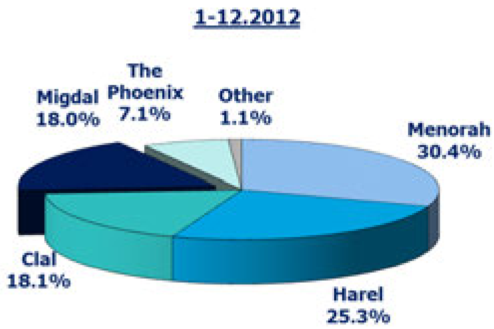
[45] Based on Pension-Net website data (new and general pension funds)

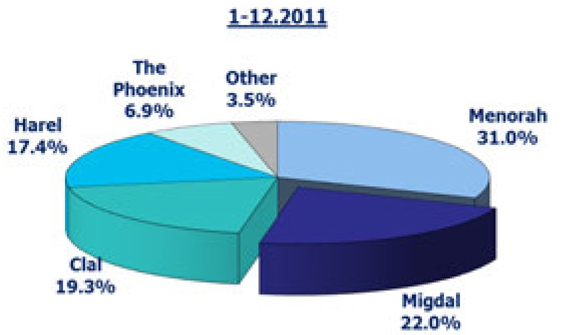
Distribution of managed assets in the new pension funds





Distribution of net accrual in the new pension funds

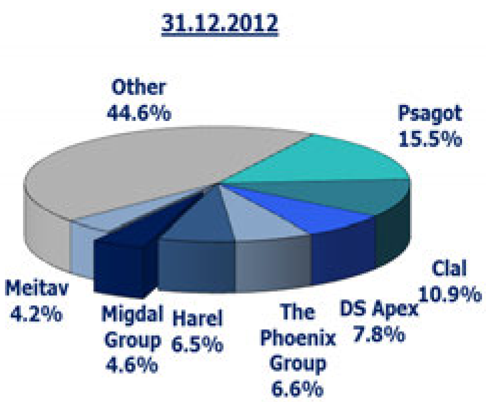


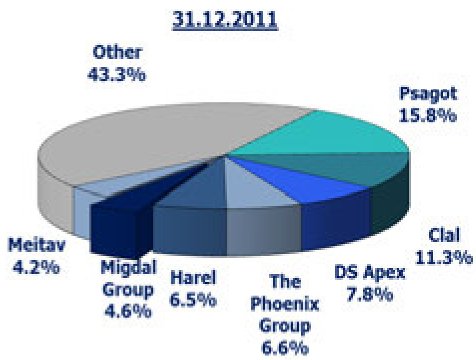


16.1.3 **Provident funds**

In the provident funds line, private investment houses, insurance companies and funds designated for employees in a certain sector / line / plant operate, and they are not "open" to the public.

The following charts detail the breakdown of provident funds' assets by types of controlling corporations, and main entities active in the market[46]:



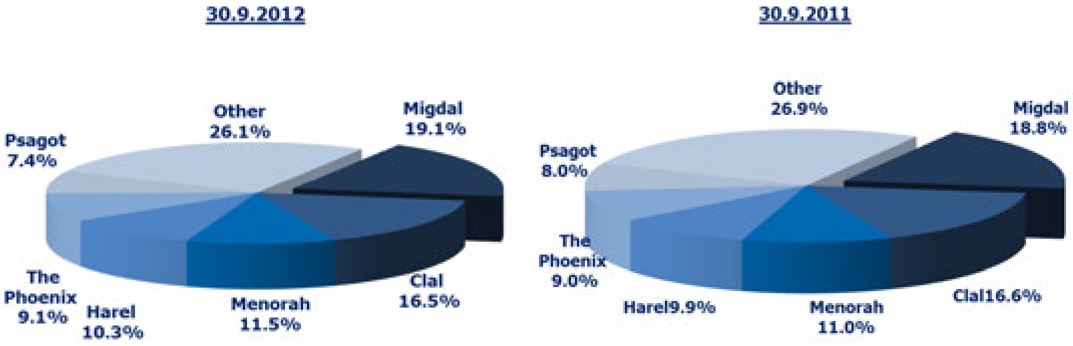


In the training funds line, the Group's market share as at December 31st, 2012 totaled approx. 10.0% of managed assets, vs. 10.6% as at December 31st, 2011.

[46] The data of Excellence Investment House are presented under The Phoenix Group.

16.1.4 **Life assurance, new pension funds and provident funds**

As at September 30th, 2012, and based on life assurance insurance liabilities and managed assets in the new pension funds and provident funds[47], the Group is leading.



16.2 **Competition and the Group's main methods of handling competition**

Competition in the life assurance and LTS areas is very harsh both between the different lines, which are mainly insurance, pension and provident, and between the different producers within the lines, so that every institutional organ competes both against the other institutional organ in the same line and against the institutional organ from the other line, inter alia, due to the nature of pensionary products, which are substitute products in the area.

Institutional organs also compete with other financial entities, which market other investment products, as to products in whose respect there are no tax benefits.

16.2.1 **Following are the Group's main methods of handling competition, inter alia:**

(a) **Creating a platform which offers a variety of products, consolidating activities and taking advantage of economies of scale** –

The Group, whose larger part of the insurance portfolio is the life assurance portfolio, has been aiming for several years, to increase its involvement and establish its position both in the pension and provident lines.

Within this policy, the Group expanded its pension- and training funds-related activity and performed several changes related, inter alia, to the merger of activities, concentrating the operation, distribution and service activity, and now the Group has a platform through which it offers customers a variety of products in this area, including combining all insurance and LTS products.

Developing products – the Group continues to work on adjusting the products it offers its customers to their needs and to changing market conditions, and on developing new and unique products that seek to answer the needs of changing market demands. The Group identified the Third Age area, as a developing market and it expands its activity in this area.

Achieving yield and developing investment products – the Group acts towards achieving yields in excess over its competitors with relation to the risk level in asset management, and towards developing investment products and investment tracks that are unique to the Group.

[47] The data are based on a processing of MoF reports published on the website, and include all life assurance assets.

Retaining and reinforcing the relationship with customers and improving customer service – the Group focuses on deepening the customer share and increasing the Group profitability, both at product level and customer level, including portfolio persistency, developing and adjusting insurance plans / pension tracks, so that it encourages insureds to leave their money under the Group management. Alongside, it strive towards improving service, including improving computerization systems, and reinforcing control arrays in order to improve service and information delivered to customers as regards a variety of the Group products.

Expanding the marketing and distribution array – the Group works on deepening the professional and ongoing relations with the various distribution channels of its marketed products, and on developing activities of distribution channels to expand the services rendered to such entities and expand the technological enhancements available to these distribution channels.

Operational streamlining – the Group continues to focus on high-quality employees strength and human capital, along with an examination of across-the-board processes and cost structures, with the purpose of improving its operational efficiency.

In spite of the ever growing competition, the Group emphasizes the examination of business profitability over time, while taking advantages of the economies of scale, adjusting sales incentives and examining tools to consider profitability which will allow it to make informed decisions for conducting profitable businesses.

(b) Other major factors affecting the Group's competitive status are mainly:

Long term experience in the areas of life assurance and LTS, and the Group being the leading company in life assurance and pension lines;

The Group's reputation;

The Group employees' knowledge, experience and quality;

The Group's financial strength and economies of scale.

The larger part of the Group's life assurance portfolio includes guaranteed-yield policies as well as policies guaranteeing better annuity coefficients than the ones currently offered, relative advantages, which the pensionary advisor should take into consideration when recommending pensionary products, which may contribute to portfolio persistency even in today's escalating competition.

Furthermore, in this respect, also see Clause 57 below, business strategies and targets

The information included in this paragraph includes future-forecasting information, and reflects the Group's estimates. It is not yet clear whether the mentioned situation will last much longer, or if and to what extent it will escalate or become moderate. The mentioned competition's implications are hard to estimate, especially in light of the various reforms in the area, including the planned reforms following which the overall area's players map may change, as well as the distribution and consultation channels. The Group estimates that adequate preparation may reduce the threats and increase the likelihood of taking advantage of the market's opportunities.

Area B – Health Insurance

17. General information about the area of health insurance

17.1 General

Health insurance is aimed at compensating or indemnifying the insured in respect of medical expenses in cases of insured's injury as a result of disease or accident.

In Israel there are several layers providing health services coverages:

The first layer – the basic health basket ("**health basket**" and/or "**the basic basket**") whose coming into effect and scope were set by the National Health Insurance Law-1994 ("**Health Law**") and the regulations in its virtue, which all Israeli residents are entitled to receive through one of the HMOs;

The second layer – complementary health services excluded from the health basket ("**Shaban**" - **additional health services**), which the National Health Insurance Law allows HMOs to offer to their insureds, in return for participation fees ("**Shaban Programs**") (Maccabi Magen, Meuhedet Adif, Clalit Mushlam, Leumit Silver/Gold);

The third layer – private health insurances purchased from insurance companies.

The health insurance market is an evolving market, characterized by high growth rate and harsh competition, which is affected by many changes. Inter alia, by the main following factors:

- The gap between the scope of health services provided by the State under the basic health basket and civilians' need for enhanced health services due to the increase in life expectancy and life quality.
- Government policy in the area of health including expansion or reduction of the services provided under the health basket or Shaban programs.
- Technological improvements in the area of medicine.
- An increase in life expectancy and improved life quality require expensive medical resources, such as medications and advanced medical treatments.
- HMO's complementary services are not satisfactory regarding the issue of LTC (Long Term Care), transplantations, medications, surgeries abroad etc., and there is a demand for buying such insurance coverages privately.

The insurance coverages proposed by the insurance companies are mainly divided into the following layers:

17.1.1 Alternative insurance – private insurance replacing the services provided in the health basket and/or Shaban. In such insurance, insurance monies are paid regardless of the entitling rights in the basic layers (coverage from the very first Shekel).

17.1.2 Complementary insurance – private insurance where the paid insurance monies are well beyond the health basket and/or Shaban. Namely, the paid insurance monies are the difference between actual expenses spent by the insured and the expenses to which he is entitled to from the health basket and/or Shaban.

17.1.3 Added insurance - private insurance providing services excluded from the health basket and/or Shaban. This insurance, too, pays the insurance monies from the very first Shekel.

Private health insurance are offered as individual insurances (individual policies for insureds) ("**individual insurance**") and collective insurance agreements ("**collective insurance**").

Individual insurance - are mostly long-term insurance plans (for the insured's whole life or a fixed preset age), even if the insured's medical condition changes during that period.

Insurance plans are mostly long-term, and some are characterized by accumulating considerable reserves for long periods. Changes in assumptions and actuarial forecasts regarding the future risk (such as morbidity rates, life expectancy development and claim application development (e.g., in LTC) and more), may bring along material changes in the provision sums. Due to the considerable weight of such reserves, the revenues from investments against insurance reserves in this area, materially affect the profitability of the area, as well as the difference between the collected premium for risk coverage and the actual risk realization.

Furthermore, since most insurance plans are long-term plans, where risk could change considerably, insurance companies found it difficult to commit to a premium which would not change over the years. Therefore, insurance companies were given the possibility, within the insurance policy, to change the premiums tables for existing insureds, subject to the Commissioner of Insurance approval. The Commissioner Circular dated July 2005 regulates the principles and terms underlying the examination of insurance companies' requests for tariff changes for changing existing insureds' tariffs. Some provisions arranging specific insurance coverages (e.g. LTC), in the Circular mentioned in Clause 17.2 hereinafter include provisions regarding the change in premiums during the insurance period.

Collective insurance - the terms of the collective insurance agreements are set in negotiations between the insurer and the entity representing the group, and they apply to all individuals included in the relevant group. Usually, such agreements are signed for preset periods of time of several years, the premiums are lower than premiums paid in similar individual policies, and sometimes the terms of the collective policy insurance coverage are larger than those of individual policies. As of July 2010, the Financial Services Control Regulations (Insurance) (Collective Health Insurance) – 2009 regulate the basic principles of collective health insurance, for details see Clause 17.4.4 hereinafter. For special arrangements that apply to collective LTC insurance, see Clause 17.2 hereinafter.

17.2 **Changes in the area of LTC and LTC insurance (current and proposed)**

17.2.1 Principles for the preparation of LTC insurance plan (individual and collective)

(a) In December 2012, the Commissioner published the Circular regarding the Preparation of LTC Insurance Plan, regulating the principles for the preparation of LTC, individual and collective insurance policies (which substituted current regulations on this matter, including the Circular dated March 2012).

The Circular provisions refer mainly to the following issues: (a) the insurance period in LTC insurance (both individual and collective policies) will be for the entire life of insureds (unlike the previous situation in collective policies, in which the insurance period was limited); (b) a standard and minimal definition of the insurance event in the case of LTC; (c) setting the minimal entitlement level of insureds upon the occurrence of an insurance event; (d) the pricing of premium shall not rely on a subsidy between various age groups and genders and the number of years of age in every group shall not exceed five years; (e) the premium shall be fixed or enhanced, determined at the age of 65 at the latest, and even then the increase would be up to 4% before CPI-linking; (f) the conditions and the way to determine disposal values and surrender values in these policies in the should the premium payment is discontinued; (g) restrictions and rules regarding the changes in premium for existing insureds were determined; (h) provisions regarding proper disclosure that should be submitted to insureds before they adhere to insurance, the data that should be included in the insurance particulars page and in the insurer's website, and the data and documents that should be submitted upon filing a claim, were set forth; (i) Provisions regarding the duty to offer an alternative in which insurance benefits be given in respect of treatment at the insured's home were determined.

The provisions apply to LTC insurance policies that will be marketed or renewed starting from January 1st, 2013, and to LTC insurance collective policies, which were marketed or renewed starting from the Circular's publication date (December 19th, 2012), but it was possible to renew collective insurance policies that do not comply with the Circular's provisions, provided its insurance period ends on December 31st, 2013, at the latest. Furthermore, some Circular provisions (especially those referring to the changes that were introduced) do not apply to LTC collective insurance policies in which HMOs are the policyholders for their members.

(b) **Collective LTC insurance – outline for older insureds**
In January 2013 the Commissioner published **an outline for older insureds in collective LTC insurance**, pursuant to the letter issued by the MoF in August 2011, prohibiting the sale of such plans or their renewal, beyond the end of 2013 under the conditions set forth.

Pursuant to the proposed outline, which will be regulated as per the Regulations and the Circular, insurers will offer insureds whose LTC insurance was discontinued, to renew the collective insurance in an outline policy ("outline policy") if they do not suffer from an LTC condition and they are insured under collective LTC insurance or were insured in such an insurance in the last three years ("target population"). Within the outline, there are timetables for extending an offer to join the outline, to the policy owners, it was determined that insureds from the target population of the policy owner who asked to join the outline policy shall be added to the outline policy and will be entitled to buy additional coverage ("the additional coverage"). Should policy owners decide not to join the outline policy, the members of the target population may shift to an individual policy pursuant to the terms of the Commissioner's Circular on this matter. The renewal of insurance in the outline policy shall be without examining previous medical condition and without a qualification period. It was decided that insurers should submit to the Commissioner's approval an actuarial model pursuant to the conditions set forth in the Appendix to the outline, until May 1st, 2013. The outline will come into effect on October 1st, 2013.

The arrangements offered in the area of LTC insurance are, inter alia, in light of the cost of insurance risk in older age and the improvement in life expectancy. The Company is examining the proposed arrangements in the area of LTC insurance, however, since not all arrangements on this matter have been outlined, including those referring to HMOs population, the Company is unable to assess the implication of the proposed arrangements.

The information included in this paragraph includes future-forecasting information and it reflects the Company's estimates.

17.2.2 **The intention to create a homogenous LTC policy for all HMOs**
In December 2013 insurance companies received wording version of the **Control of Financial Services (Insurance) (Collective LTC Insurance**

for HMOs members) Regulations – 2013. The draft Regulationsset forth rules for collective LTC insurance sold to HMOs members. The main issues in the proposal are that the insurance plan shall include identical minimal conditions for all insureds in the various HMOs, the definition of the insurance event will be identical and the terms of exclusions will be identical, the insurance amounts will depend on the original adherence age of beneficiaries to the original HMO's LTC insurance, insurance amounts in years 4 and 5 will be 75% of the amount to which they are entitled in the first years, the premium shall be set forth with a breakdown into ages by each HMO separately, with a weighting set forth by the Commissioner of Insurance in order to maintain the same gap in all ages between the HMOs, it is possible to join at any age (subject to examining previous medical condition), there is a prohibition on stipulations regarding other products, the insurance amounts and premiums shall be linked to the CPI, there will be no qualification period and the waiting period shall be 60 days.

The policy shall include a continuity clause for individual policies under the pre-determined conditions. It is proposed that the provisions shall come into effect as of January 1st, 2014.

The Company (unlike competing insurance companies) does not have agreements with the HMOs for collective LTC insurance. The inclusion of homogenous rules for collective LTC insurance plans for HMOs as proposed above may increase the competition between insurance companies as to the conditions that will be offered to HMOs towards the date upon which HMOs will have to renew the current collective insurances pursuant to the new rules that will be regulated.

The information included in this paragraph includes future-forecasting information and it reflects the Company's estimates.

17.2.3 **LTC insurance as part of the Health Law**

The Ministry of Health would like to promote a reform in the public LTC insurance. The aims of this reform are: setting one entity that bears the general responsibility, a coverage for the entire old people's population that needs LTC, in an adequate and sustainable scope for years, increasing the efficiency of the array of medical-LTC services supply, decreasing the burden on households and increasing families' ability to cope with the burden, and long term planning and deployment, all along with expanding the National Health Insurance Law and appropriate budgeting (raising the Health Tax). The proposed arrangements regarding this matter have not been determined yet, and the Company is unable to assess the implications of this reform, if it is outlined at all.

17.3 **Proposed change in insurance coverage for dread diseases**

In March 2013 the Commissioner published a second draft regarding the **Preparation of an Insurance Plan for Dread Diseases**. The draft Circular would like to determine principles for the preparation of an insurance plan for dread diseases (asking to change the current Circular on this matter from 2003), and the main proposed changes are as follows: the definition of diseases in the insurance plan shall be worded pursuant to common medical definitions (unlike the previous situation, whereas the Circular defined the insurance event/disease) and shall cover at least severe and common cases of the disease; mandating insurers to check at least once every two years the need to update the definitions; should the insurer decide that the definitions must be updated, there are arrangements regarding addressing existing insureds soliciting them to shift to the new policy that would include the updated definitions, along with maintaining insurance continuity, pursuant to the conditions set forth in the draft Circular.

17.4 Limitations, legislation, regulation and special constrains applied to the area

17.4.1 General

In addition to the provisions and arrangements that apply to insurance areas in general, regarding this matter see also Clause 45 to Part E above, there are specific legislative arrangements that apply to the area of health, including, inter alia, regulatory instructions published by the Commissioner of Insurance and which somehow refer to most of the aspects of health policies, including dealing with them and marketing them.

The regulatory instructions shall refer mainly to the following issues: provisions as to the arrangement of proper disclosure at the stage of the proposal, reports, including annual reports, and documents that must be delivered to insureds both in the proposal stage and throughout the policy life. Provisions obliging insurance companies to include minimum settings as regards the following subjects in the insurance plans: insurance events, medical procedures, different diseases, medications etc., and obligating insurers to include compulsory insurance coverage in certain insurance plans or the possibility of insurance continuity.; provisions regarding changes in tariffs in health insurance for existing insureds etc.

17.4.2 National Health Insurance Law

The National Health Insurance Law - 1994 ("**The Health Law**"), effective as of January 1995, states that every Israeli citizen is entitled to health services included in the health services basket provided by the HMOs. The Law states that HMOs are liable for anyone registered thereof to provide them with their full health services, and that the health services included in the health services basket are provided in Israel, as per medical discretion, at reasonable quality, within a reasonable time and reasonable vicinity to the insured residence. In exceptional cases set in the National Health Insurance Regulations (Health Services in Foreign Countries) – 1995, the insureds may get financing for health services abroad.

The Health Law amendment of 1998 stated that the HMOs may offer their insureds additional health services – Shaban program, as per terms set under the Law.

The Health Law amendments of 2008 limited the services that HMOs may offer their insureds in the following issues: prohibition to include LTC services in the Shaban program; prohibition to include life saving or life prolonging medications in the Shaban programs.

As of July 2011, the reform regarding dental treatments for children was expended, and came into effect gradually. It provides preventive and preservative dental treatments for children aged up to 12 within the health services basket through HMOs.

Regarding the MoH plan regarding the reform on public LTC insurance, see Clause 17.2.3 hereinafter.

17.4.3 **The Supervision of Insurance Businesses Regulations (Terms in Insurance Contracts) (Provisions as to Prior Medical Condition) – 2004** – limit insurers' ability to restrict the scope of insurance coverage due to prior medical condition. These regulations set a maximum period under which such scope of insurance coverage in respect for prior medical condition may be limited. However, the regulations allow setting restrictions due to prior medical condition for a longer period, as per the conditions and arrangements set forth in the Regulations.

17.4.4 **The Supervision of Financial Services (Insurance) (Collective Health Insurance) Regulations – 2009**. These regulations are aimed at regulating the basic principles of collective health insurance. The provisions determine, inter alia, who may serve as the policyholder of collective health insurance, the duties imposed on the policyholder, provisions as to insureds' joining, provisions as to uniformity in setting insurance fees subject to age or gender indications related to insurance risk, provisions as to the disclosure to be provided and documents to be delivered to insureds, restrictions as to the duration of the insurance period, provisions as to the provision of continuity right to insureds in certain cases, provisions as to double insurance, prohibition of commission payment to policyholders, duty of registration management and the duty to submit annual reports to insureds.

17.5 **Changes in the scope of activity in the area and its profitability**

For additional details regarding scopes of activity in the area in the Group and on the market, as well as results of activity and financial information in the area of health insurance, see Clause 8.2 to Part B above, Clause 1.3.3 in the BoD Report, as well as Notes 3 b and 19 to the Financial Statements.

17.6 **Alternatives to products and changes therein**

Some of the coverages proposed in the products of this area have alternatives provided by the health services, both as per the basic health basket and those provided by the Shaban. Changes in the basic health basket or in the insurance coverages offered by the Shaban affect the size of the relevant market, as well as the coverages offered in the line.

18. The area's main products and services

The main products sold in this area include medical expenses coverage, and the main proposed coverages are: "surgery" type medical insurance, "transplantations" type insurance, special treatments abroad, medications, dental insurance, riders etc. ("**medical expenses**"), coverage for diseases and severe medical events and LTC. Furthermore, there are insurance coverages for foreign travel insurance and personal accidents for over one year.

The insurance coverages are offered both as independent policies or as an insurance component that accompanies other policies.

18.1 **Medical expenses insurance**

This category offers several insurance plans:

18.1.1 **"Surgery" type health insurance** – mainly provides coverage for expenses involved in private surgeries in Israel and abroad, including Shaban's complementary plan for surgery in Israel.

18.1.2 **"Transplantations" type health insurance** – mainly provides coverage for expenses involved in organ transplants abroad and/or special treatments.

18.1.3 **"Medication" type insurance** – mainly provides coverage in respect of medications that are not included in the National Health Basket.

18.1.4 **Dental insurance** – mainly provides the insureds with coverage of expenses in respect of dental treatments based on several coverage layers: conservative, gums, restorative, grafts and Orthodontics. This coverage is currently marketed by the Group only as collective insurance[48].

18.1.5 **Service riders** – various coverages given to insureds such as physiotherapy treatments, consultations with psychologists, complementary medicine treatments, house calls by physicians as well as ambulatory coverages such as consultations with physicians, diagnostic medical tests, managers' screening tests and preventive medicine checks.

[48] For the inclusion of preventive and conservative dental treatments for children in the Health Basket, see Clause 17.4.2 above.

18.2 **Dread disease insurance**
An insurance coverage which provides the insureds with compensation in case of discovering one of the dread diseases listed in the insurance plan, or insurance coverage for a certain disease set forth in the plan.

18.3 **LTC insurance**
An insurance which mainly guarantees the insureds a monthly compensation payment (at an amount preset in the policy) in case they become LTC-dependent under the definition set in the policy, and after the preset waiting period in the policy.

The monthly compensation amount is for a limited period or for the insureds' whole life, as per the policy terms. In insurance plans marketed up until 2012, the monthly compensation was indexed to the investments portfolio, as per the conditions set forth in the plan. Starting from 2012, the marketed insurance plan indexes the monthly compensation amount in the event of LTC condition to the CPI, as per the terms of the plan.

Under certain conditions, in case of discontinuing the premium payment before the end of the insurance period, the insured is entitled to partial insurance coverage, according to the policy terms.

As per the Commissioner instructions from April 2004, an individual insured under collective LTC insurance is entitled to purchase a lifetime continuance policy without undergoing repeated underwriting or revision of his/her health condition in terms set in the Commissioner circular for that matter.

In 2012 the Company launched an LTC insurance plan, in which the monthly compensation for the insured, in the event of LTC as per the terms of the policy, will be CPI-linked, under the conditions set forth in the plan.

For the changes in LTC insurance plans, see Clause 17.2 above.

18.4 **Healthy Investment** – a plan combining medical insurance for surgery and compensation in case of dread disease. In addition, as per the plan terms, the insured may be reimbursed with premiums had he not claimed the policy. This plan is no longer marketed.

18.5 **Personal accidents** – a plan compensating insureds in respect of damage they incurred as a result of an accident. The coverage is multi-annual and is provided in the event of death, burns, fractures, LTC condition, hospitalization or disability, when they are caused following an accident, and may also include coverage for temporary occupational disability.

18.6 **Travel insurance** - it provides indemnification for expenses related to medical events that occurred abroad as well as an indemnification in respect of third party damages and luggage.

19. Data breakdown for products and services

Following are the main data regarding the area of activity in the years 2010-2012 (in NIS million):

	2012	2011	2010
Gross premiums	692	615	556
Premiums less reinsurance (in self retention)	630	552	510
Increase in liabilities and payments in respect of gross insurance contracts	520	394	438
Increase in liabilities and payments in respect of insurance contracts in retention	491	361	414

Following is a breakdown of gross premiums and insurance liabilities divided into yield-dependent and other, as well as gross premiums breakdown by key products.

	2012			2011			2010		
	Yield-dependent	**Other**	**Total**	**Yield-dependent**	**Other**	**Total**	**Yield-dependent**	**Other**	**Total**
LTC insurance	184	17	201	171	10	181	151	10	161
Dread disease insurance	5	146	151	6	138	144	6	128	134
Medical expenses insurance		294	294		259	259		238	238
Other		46	46		31	31		23	23
Total premiums	**189**	**503**	**692**	**177**	**438**	**615**	**157**	**399**	**556**
Insurance liabilities	1,264	352	1,616	1,071	318	1,389	965	289	1,254

The continued increase in gross premiums in 2011 and 2012 is mainly due to an increase in premiums from individual insurances due to an ongoing increase in new sales. The upward trend is apparent in all individual products marketed by the Group.

The changes in liabilities and payments in respect of insurance contracts in 2010-2012 mainly stem from changes in yields achieved on capital markets and an increase in the activity in the portfolio.

For further details see Note 19 to the Financial Statements.

20. Customers

Health insurances are offered as both individual insurances (personal policy for the insured) and within collective insurance agreements.

Following is a table describing the customers' breakdown in the health area by gross premiums in 2012 and 2011 (in NIS million and percentage):

	2012		2011	
Customers features	**Gross premiums**	**Breakdown in percentage**	**Gross premiums**	**Breakdown in percentage**
Individual insureds	634	92	575	94
Collective insurances	58	8	40	6
Total area of activity	692	100	615	100

The increase in the weight of collective insurance to total premium in this area concentrates mainly in the medical expenses line.

In terms of premiums, the lapse rate in individual policies from valid policies at the beginning of the year totaled approx. 7.8% in the reported year vs. approx. 6.9% in 2011.

The Group has no single customer whose revenues in this area constitute 10% or more of the total premiums in the area.

21. Marketing and distribution

21.1 **General**

Marketing in this area is mainly performed by the Group's array of affiliated agents - see Clause 50 in Part E hereinafter. Also, a small part of policies are marketed in direct sale by the Group.

21.2 **Commissions**

In individual health insurances – the Group pays insurance agents variable commissions in respect of product marketing, and the commission changes according to the sold plan.

The structure of commissions is often: current commissions from premiums – the commissions paid are "flat" commissions, namely of similar rate throughout the entire policy life, and these are set in individual agreements with the agents. "Portfolio persistency commissions" in respect of insurance plans sold after June 2001, often derived from the agent's portfolio persistency level, the scope of his insurance portfolio and performance of sales objectives; rewards / grants – a commission which is usually derived from the scope of sales and the agent's fulfillment of his preset sales objective, and subject to arrangements referring to policy cancellations in a pre-set period. In addition, the Group initiates sale campaigns under which it rewards agents with additional rewards and/or grants.

Sometimes the Group extends loans to its agents, upon future commission flow surety or other sureties. The loans are extended at commercial terms under rules set by the Commissioner.

In collective health insurances – the commissions are paid at an agreed upon rate of the premium.

In 2012 the average commission rate from gross premiums in the health area totaled approx. 24.2% vs. approx. 21.9% in 2011. The increase was affected by an increase in commission rates and in new sales.

In 2012, the Group had no agent whose scope of premiums exceeded 10% of the area's volume of premiums.

The scope of share of the Group-held agencies (including data of sub-agents of such agencies) in health insurance premiums totaled approx. 25.9%, vs. approx. 22.5% in 2011.

22. Reinsurance

The Group purchases reinsurances in respect of the risk element in health policies (transplantation, dread disease, LTC and medication insurance risks to HMO insureds).The scope of reinsurance premiums in the Group's health insurance totals approx. 9.0% of the current premium.

Reinsurance for LTC coverage is done at surplus agreement. Reinsurance for transplantations, dread disease and medications outside the health basket coverage is done at quota share agreement.

There are also facultative reinsurances, which are signed to cover risks embedded in specific policies.

In dread disease insurance quota share agreement, the coverage cap is approx. NIS 732 thousand per insured; in transplantation insurance quota share agreement, there is no cap; in medications outside the health basket quota share agreement, as aforesaid, the coverage cap is approx. NIS 15,000 thousand per insured.

In most reinsurance treaties described above, the Company is paid flat commissions from the premium ceded to reinsurers, and in addition, the Company receives profit commission that is usually calculated as a rate out of the underwriting profit.

In some reinsurance treaties, the reinsurer may demand changes in the treaty also for existing insureds, if certain conditions set forth in the treaty are met.

In the reported year, health reinsurance treaties were usually engaged with A and up rated companies (as per S&P rating, or the rating of another rating company whose rating was converted as per an index set forth within the Investment Regulations).

The Group has several reinsurers in this area, whose share in the reinsurance premiums in general insurance in the area in the reported constitutes 10% or more, as follows:

		2012		2011	
Name of reinsurer[49]	**Rating according to S&P**[50]	**Reinsurance premium ceded to reinsurer (in NIS million)**	**Share out of total reinsurance premiums in health insurance in percentage**	**Reinsurance premium ceded to reinsurer (in NIS million)**	**Share out of total reinsurance premiums in health insurance in percentage**
Hannover Re	AA-	33.9	54	33.4	53
Swiss Re	AA-	23.9	38	23.7	38

[49] Generali's share in the reinsurance is immaterial, at approx. 1%.
[50] The rating in this table is as of just before the publication of this report.

23. Suppliers and service providers

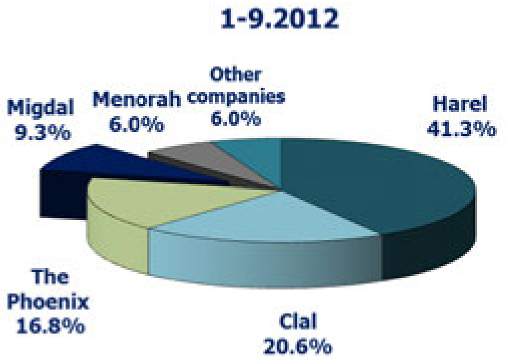
The Group has agreements for the procurement of products and professional services in various areas. The companies in the Group bear, like any other insurer, expenses related with the insurance event insured by the policy. In the health area, such expenses include covering the cost of various services covered by insurance policies, such as riders attached to the insurance policy, e.g. agreements with private hospitals as to surgeries and other treatments, agreements with medical services suppliers, including local and foreign physicians, laboratories and institutes, pharmacies, service providers in the area of riders, as well as agreements with companies gathering medical material and companies conducting functional evaluation of insureds. In addition, the Group purchases ancillary services for insurance claims settlement in various areas, such as attorneys, investigators and medical specialists, inter alia, in dental insurance. For suppliers who are not unique to this area, see Clause 48 in Part E hereinafter.

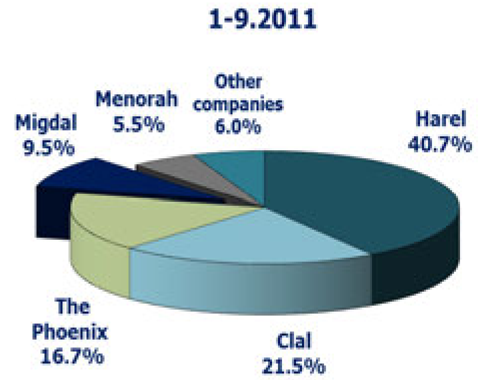
24. Competition

The health insurance area in Israel is mostly held by the largest five insurance groups - Harel Group, Clal Group, The Phoenix Group, Migdal Group and Menorah Group.

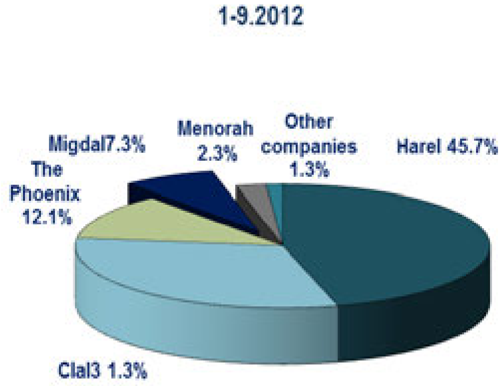
In the health area there is harsh competition, which stems, inter alia, from multiple competitors and similar products. The weight of collective insurances in the area is ever growing. In collective insurances, the multiple advisors in the area, in light of the said competition, brought along a significant price reduction, low profitability and sometimes even losses. Enclosed are market share data[51]:

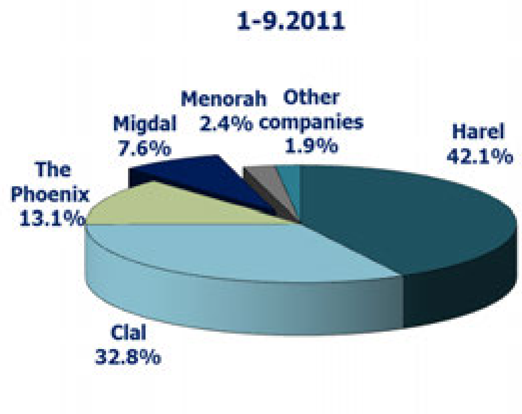
In health insurance businesses:





In LTC businesses:





[51] The market data in health insurance are based on a processing of the MoF reports published on the Internet ("**managerial reports"**).

As per the annual report of the Commissioner of Capital Markets, Insurance & Savings, in 2011, the Group's share totaled approx. 10% of the health insurance market[52], while in LTC it totaled approx. 8%, in medical expenses insurance – approx. 11%, and in dread disease insurance – approx. 25%.

In individual health insurance business, which constituted the Group's main activity, the Group's share totaled approx. 19%, while in LTC it totaled approx. 22%, in medical expenses insurance – approx. 16%, and in dread disease insurance – approx. 27%.

In 2011 the collective insurance totaled approx. 50% of the total premiums in the health insurance market under the said coverages.

The Company is striving towards expanding its activity also in the area of collective insurances, in which it did not focus up until now, with an emphasis on business reception policy, expanding the actuarial information data, with an efficient claims management.

[52] Excluding disability, foreign workers and other insurances.

Area C – General Insurance

25. General information about the area of general insurance

25.1 General

The area of general insurance includes all insurance lines except life assurance and long term savings and long term health insurances. The area includes the following sub-lines: CMBI, casco and other general insurance lines.

The main differences between the general insurance area lines and risk insurances included in the life assurance and LTS and health insurance area are expressed, inter alia, in the insurance period of policies sold in the area and in the policies' indemnification basis.

For the absorption of new business in general insurance, starting from January 1st, 2013, see Clause 3.1 to Part A above.

25.2 The area's structure and changes therein

25.2.1 CMBI

(a) **General**

The activity in this area is providing insurance coverage by virtue of the Motorcar Insurance Ordinance (New Version) - 1970 ("**motorcar insurance ordinance**"). According to the motorcar insurance ordinance, every person who uses a vehicle, or who allows another person to use it, must have a valid policy.

The CMBI policy covers, according to the motorcar insurance ordinance, the owner of the vehicle and the driver from any liability they may bear according to the Traffic Accident Casualty Compensation Law - 1975 ("**TACC**") due to bodily injury caused by the use of a motorcar to the driver, to the passengers, or to pedestrians hit by the vehicle.

Starting from October 2010, in the CMBI line there is a standard CMBI policy, for details regarding this standard policy, see Clause 25.4.4 hereinafter.

Pursuant to the TACC, a person injured in a car accident may receive compensation from the vehicle insurer, as per the compensation scope set in the TACC Law, without having to prove the guilt of any of the people involved in the accident. This liability is subject to certain exceptions set in the TACC Law, depriving the eligibility to compensation under the Law.

The sum of insurance benefits in this area is unlimited (mainly the medical expenses component) except for certain heads of torts such as “pain and suffering” whose amount is limited, and compensation in respect of salary loss, which is limited to three times the average monthly wage.

Claims in this area are characterized by a "long tail", namely sometimes a long period elapses from the occurrence of the event until the final settlement of the claim, therefore the estimate of the pending claims’ sum in the Financial Statements is done through model implementation and actuarial estimates.

For the updated Law provisions published in January 2013 regarding the calculation of insurance reserves in general insurance, see Note 37 b 3 c (6) to the Financial Statements.

(b) **Differential tariffs (risk adjusted) and the supervision on tariffs**

In the CMBI area there is a database operator, an entity established according to the Motorcar Insurance Regulations (Establishment and Management of Databases) - 2004 ("**database regulations**").

The database operator is responsible for managing the database and producing reports which will serve, inter alia, to evaluate the risks in the CMBI area, and determine the pure risk cost on which the basic tariff relies ("**the basic tariff**"). As of April 2010, Ron Actuarial Intelligence Ltd. ("**database operator**") was appointed operator of the database. As per the database regulations, insurance companies must submit to the database operator data regarding the particulars of the motorcar and the driver in all CMBI policies issued by them, as well as regarding claims filed during the quarter, on a quarterly basis.

The tariff setting principles in CMBI were regulated based on instructions set forth by the Commissioner of Insurance. Based on these instructions, the parameters insurers may use to set the tariff, and the procedures to which insurers must adhere regarding the approval of insurance fees including maximum tariffs they may charge, were set.

The maximum tariff that may be charged in CMBI, starting from November 2009 is 90% if the residual insurance tariff.

As to CMBI for vehicle fleets and collectives, tariffs are not subject to such limitations, but the Commissioner of Insurance must be informed in case of any deviation. Vehicle fleets are defined as containing at least 40 vehicles under the same ownership and under the same insurer, while collectives contain at least 100 vehicles under the same insurer, as long as the main goal of the collective's association is not insurance making.

The parameters for setting the tariff include: engine size, gender and/or age of the youngest driver using the vehicle on a permanent basis, the time period the latter has had his/her driver's license for this type of vehicle, number of former claims and/or number of license deprivation in the last three years of all permanent drivers, and the existence of airbags in the vehicle. The purpose of using these parameters is to adjust the insurance premium to the insured risk.

The Group uses a differential tariff, based on the driver's age and engine size of the insured vehicle, assuming that these two parameters are the most material in order to assess risk and set the premium, and through these parameters, the Group will be able to focus on types of insureds with low risk level, along with increasing the quantity of policies and maintaining the area's profitability.

Some of the other insurance companies also rely on other parameters, such as former claims and/or deprivation of license, the driver's gender and safety measures. The fact that other companies use other parameters as well may affect the customer mix of insurance companies in this line.

Competition in the line affects, inter alia, the tariffs. The tariff reductions and the competition in the line have a material implication on the results of insurance companies reported within the general insurance businesses. Due to implementing the accounting method of surplus accumulation, the effect is expressed in the Financial Statements after three years, see also Clause 1.3.4 in the BoD Report hereinafter.

(c) **Residual insurance (“the Pool”)**

The purpose of residual insurance is to provide insurance, which is compulsory by law, to vehicle owners who cannot obtain insurance coverage from commercial insurance companies (such as motorcycles, dune buggies and other motor vehicles rejected by the insurance companies). Insurances to such types of vehicles often involve losses.

Residual insurance is regulated in the Motorcar Insurance Regulations (Residual Insurance Arrangement and Mechanism for Setting the Tariff) - 2001 ("**the arrangement regulations**"). The residual insurance arrangement relies on co-insurance of all insurers. For additional details regarding the arrangement regulations see Clause 25.4.2 hereinafter. Pursuant to the arrangement regulations, from time to time, the Commissioner publishes the residual insurance tariffs.

Pursuant to the regulations, all insurance companies operating in the area of CMBI participate in "the pool" and each bears the pool's losses or profits as per its relative share in the CMBI market in the previous year[53].

(d) **Karnit and payments to Karnit**

The Traffic Accident Casualty Compensation Fund – Karnit, is a corporation established following the TACC law, whose role is to compensate a casualty who is entitled to such compensation by virtue of this law, and who cannot file the insurance company for compensations due to one of the following events: the liable driver is unknown, the driver does not have CMBI or the insurance does not cover the liability, the insurer of the motorcar is liquidated or appointed an authorized manager.

According to the Traffic Accident Casualty Compensation Order (Fund Finance) (Amendment) – 2003, insurance companies must pay Karnit 1% of the net insurance monies in respect of CMBI policies.

Furthermore, under the 2009 Law of Economic Efficiency, amendments were made to the Motorcar Insurance Ordinance, to the TAAC Law and to the Health Insurance Law. Pursuant to these amendments, as of January 2010, the insurance responsibility for rendering medical services included in the second addition to the National Health Law and the list of medications included in the decree as per Clause 8 (g) to that Law ("**services included in the Health Law**"), regarding road accident casualties was transferred from insurance companies to HMOs.

Insurance companies will continue to be liable to insureds for the other medical services that are not included in the services included in the Health Law.

Pursuant to the Traffic Accident Casualty Order (Finance of Service Rendering Costs) – 2009, insurance companies must transfer to Karnit is 9.4% of insurance fees as collected by them in the preceding month in respect of all the CMBI policies they issued.

(e) **Handling CMBI frauds**

[53] In February 2013 the Pool's GM decided to amend the Pool's Articles of Association, such that the share of companies participating in the Pool shall be determined by the end of the current year, and the amendment is subject to the approval of the Commissioner of Insurance. In 2012 the Company's share was approx. 6.2%. For the Company's share in the Pool's losses, see Note (5) to the Table in Clause 8.3.1 to Part B above.

The establishment and management of databases as set forth in Clause 25.4.3 hereinafter, and the Commissioner circulars in this regard, regulate the usage of databases in order to detect CMBI frauds.

As of February 2010, a new CMBI certificate for private and commercial vehicle of up to 3.5 tons and motorcycles is produced after verifying, through an online query during the underwriting process, at least the particulars of the information detailed in the Commissioner circulars in this matter, and the terms of the Regulation.

Among other things, the Commissioner circulars as to the use of databases state that only persons who are authorized to access the database shall use them, regulate the appointment of such persons, the reports and statements that they must submit to the Commissioner and the database operator, impose the duty to set a unified procedure for handling discrepancies between the insured's particulars submitted to the insurer and the data included in the database, regulate the notification sent by insurers to insureds in case of such discrepancies and the insured's right to appeal. Furthermore, the circulars contain provisions that prohibit or restrict the insurer as far as the cancelling of a CMBI policy and the collection of additional premium for data included in the database which was not checked in advance by the insurer, are concerned.

(f) “**Light heavy” clearance outline**

Under CMBI activity, the Insurance Companies Association operates a clearance system aimed at transferring payments automatically between motorcar insurers as per the TACC Law and the Compensation for Traffic Accident Casualty Order (Arrangements for the Distribution of the Burden of Compensation Between Insurers) – 2001. See Clause 31.2.1 hereinafter.

(g) **Motorcar insurance**

As of January 1st, 2013, the Commissioner approved the production of CMBI insurance for motorcars under the Company's coverage (outside of the Pool's framework). The scope of such insurances is not material.

25.2.2 **Casco (property-motorcar) insurance**

(a) **General**

Casco insurance is an elective insurance and is the most common voluntary insurance under general insurance. Casco insurance includes the coverage of property damages to the insured's vehicle and property damages to third parties. In this chapter, "**comprehensive insurance**" means coverage of both the insured vehicle property damages and property damages caused to a third party by the insured vehicle.

Casco insurance is divided into two main groups according to the types of vehicle:

Insurance for private and commercial vehicles of up to 3.5 tons that grants insurance coverages as per the terms of the standard policy set forth in the Supervision of Insurance Business Regulations (Conditions of Contract for Insurance of a Private Vehicle) – 1986 ("**casco regulations**").

Insurance for other types of vehicles such as trucks of over 3.5 tons, motorcycles, heavy equipment, agricultural equipment etc. under a policy that is not subject to the terms of the standard policy, that includes comprehensive coverage and/or property damage to a third party.

The standard policy sets the version and minimal conditions for casco insurance which may be changed by the insurance company only if the change is in favor of the insured. It is possible to add extensions to the standard policy regarding the scope of coverage and covered risks. Approx. 91% of vehicles insured by the Group in casco insurance are private vehicles or commercial vehicles of up to 3.5 tons.

The tariff for casco requires approval, as well as approval of the policy in its entirety, by the Commissioner of Insurance, and is a differential actuarial tariff (which is not uniform for all insureds and is risk adjusted). The above mentioned tariff is based on several parameters, related with the vehicle insured in the policy (such as make, model, type of protection etc.) and with the insured's characteristics (number of drivers, drivers' age, past claim experience etc.).

The underwriting process is partly performed through the tariff itself, and partly through the Group's underwriting policy as set forth from time to time.

(b) **The fight against car theft**

From January 2006 the Insurance Companies Association and the Car Rental and Leasing Companies Association have an agreement with the Ministry of Public Security and the Israeli Police, regarding the operation of the anti-car theft unit – **Etgar**. The police unit is partly financed by governmental sources, and partly by insurance companies and other entities.

It should be noted that in the calculation made by the Company based on the data submitted by the police, the frequency of car theft in 2012 decreased by approx. 8.0% compared with 2011. On the other hand, in the Group there was an increase of approx. 9% compared with 2011.

25.2.3 **Other lines in general insurance**

The Group's activity in this area focuses on property insurances and liabilities insurances. Under this framework, the Group also includes its activity in personal accident insurances defined as short-term health insurances (this activity is not material for the Group).

Regarding most of the coverages included in the other lines in general insurance as described henceforth, the Group engages with foreign reinsurers in order to spread the risks it takes and thus minimize its exposure.

(a) **Property insurance**

Property insurances are aimed at providing insureds with coverage against physical damage to their property. The main risks covered in property policies are fire hazards, explosion, burglary, earthquake and natural disasters. Property insurances sometimes include coverage for consequential damage (loss of profit) due to physical damage caused to the property. Property insurances play a significant role in homeowners insurance, businesses insurances, engineering insurances, goods in transit (marine, terrestrial, aerial) etc.

In most cases, the property insurance policies are issued for a period of one year. Also, in most cases, claims in respect of such policies are clarified upon the occurrence of the insurance event.

(b) **Liabilities insurances**

Liability insurances are aimed at covering an insured's liability, by law, in respect of damage he may inflict upon a third party. The main types of insurance are: third party liability insurance, employers' liabilities insurance and other liability insurances, such as professional liability, product liability and Directors and officers (D&O) liabilities insurance. Insurances are usually sold in the framework of business insurances, engineering insurances etc.

The liability insurance policies are usually issued for one year. However, the pace at which claims in this line progress is longer and may take several years, for several reasons: the damage covered in the policy is caused to a third party who is not insured in the policy, the time elapsed between the occurrence of the event and the time of establishing the liability and damage and filing the claim, is relatively long. In many cases it involves a relatively complex factual and legal inquiry, both regarding the insured's liability and the scope of damage. The limitation period in respect of the cause of claim is longer than the customary limitation period in property insurance.

In some of the liability insurances (mainly third party and employers' liability), coverage is usually event-based, namely the coverage is for events that occurred during the insurance period and the claim can be filed after the end of the insurance period, subject to limitation.

In the other liability insurances (mainly professional liability, product liability and D&O liabilities insurance), coverage is usually based on the claim filing date, namely coverage is for claims that were filed only during the insurance period, even if the cause was created prior to the insurance period commencement.

25.3 **Description of insurance lines and insurance coverages included in the area**

For the description of insurance coverages, see Clause 26 hereinafter.

25.4 **Restrictions, legislation, regulation and special constraints that apply to the area, including developments in legislative arrangements in this area published in the period starting 2011 Periodic Report publication until now**

CMBI

25.4.1 **Traffic Accident Casualty Compensation Law - 1975 ("TACC" and the regulations by its virtue)**
The goal of this Law is making the question of guilt redundant in a compensation arrangement, and creating a fast mechanism for clarifying the eligibility to compensation and to setting their rate. The Law defines, inter alia, the term “car accident”, who is eligible to compensation, who pays the compensation, form of calculating the compensation, and the evidence-related laws and rules used in this special arrangement.

A draft Bill for the **Traffic Accident Casualty Compensation Law – (Amendment No. 24) – 2012** ("TACC Law") is pending, and it deals with introducing several changes in the key definitions of the TACC Law.

Motorcar Vehicle Insurance Ordinance (New Version) – 1970 ("Motorcar Vehicle Ordinance").

This Ordinance imposes on a car owner the duty to insure the car owner himself, as well as any other person driving the car, against any liability they may incur, including as per the TACC Law, due to bodily damage caused to another person by or following the use of the motor vehicle, as well as insuring the car owner and the car driver, upon consent of the owner, against bodily injury caused to them in a car accident. The Ordinance sets terms to be included in the insurance contract including ineffective limitations in the insurance contract.

25.4.2 **Regulations of Motor Vehicle Insurance (Residual Insurance Arrangement and Mechanism for Setting the Tariff) – 2001 ("Arrangement Regulations")**

The arrangement regulations regulate, inter alia, the establishment of a joint corporation of insurers, the managing corporation of the CMBI Database Ltd. ("**the Pool**"), that will manage the residual arrangement as mentioned above, the share of every company in that insurance as mentioned above, the way the corporation is managed, the settlement of accounts of the joint insurance, including arrangements regarding setting residual insurance tariffs and the duty to sell insurance to anyone approaching the said corporation.

25.4.3 **Regulations of Motor Vehicle Insurance (Establishment and Management of Database) - 2004**

The regulations regulate the way the insurance frauds database operates and its relations with insurers. In these regulations, "insurance frauds" is defined, inter alia, as providing a false or misleading fact to an insurer, in the underwriting and policy issuance stages, or in the stage of filing a claim in order to receive compensation. The regulations state who may establish and manage databases, what will be the particulars that insurers will provide to the database operator, the way the information will be submitted by the operator to the insurer, setting a person in charge of preventing frauds with the insurer, appointing persons in charge of preventing frauds at the insurer, appointing persons who are authorized to peruse the databases, distribution of financing databases among insurers, etc.

25.4.4 **Regulations of Law of Supervision of Financial Services (Insurance) (Terms of CMBI contract) - 2009**

These regulations effective from October 1st, 2010 set a unified wording for CMBI standard policy, which will constitute the standard and binding insurance. The standard policy regarding CMBI that was offered is both for an ordinary policy and a trade policy (a policy for those holding several vehicles temporarily for trade purposes).

The standard policy sets forth the wording and minimal terms for CMBI that may not be changed by the insurance company. It is possible to add an expansion appendix regarding the scope of coverage to the policy, upon the Commissioner's approval. The regulations also set a version of the insurance certificate that insurers should issue under the motor vehicle insurance.

25.4.5 **Subrogation agreement with the National Insurance Institute of Israel (NII)**

As per Clause 328 to the National Insurance Institute Law (combined version) – 1995, the NII has the right to claim from a third party to pay back annuities paid or hat will be paid by the NII, if the case serves as a cause for charging a third party as per the Civil Wrongs Ordinance or the TAAC Law. In 1978 and 1979 agreements were signed between insurance companies in Israel, including the Group, and the NII, aimed at regulating the legal relationship stemming from the NII's right of subrogation as mentioned above. Under the agreement, the cases in which the NII may and is entitled to sue Migdal for a subrogation claim in respect of insurance monies and injury monies paid by the NII and the scope of reimbursement that Migdal has to pay back, when relevant. The reserves for outstanding claims include provisions also in respect of these claims.

The NII informed the insurance companies about the cancellation of the agreement with it[54]. The Insurance Companies Association is negotiating with the NII as to the new arrangement practices[55]. As at the reported date, a new agreement regulating the relationship with the NII has yet to be signed. As per the Group's estimate, the implications of a new agreement with the NII depend on the outcome of the deliberations with the NII, and on the content of the agreement that will be signed with it. In 2012 the Company made a provision for this matter, in a non-material amount.

Motor Casco Insurance

25.4.6 **Regulations of the Supervision of Insurance Businesses (Conditions of Contract for Insurance of a Private Vehicle) – 1986**

These regulations set forth the wording of the standard policy for casco insurance, and in April 2012 amendments were introduced to the Regulations' wording and in the wording of the standard policy, which came into effect on October 1st, 2012. The standard policy sets a wording and minimal conditions for casco insurance, that insurance companies may not change. Vehicles weighting 3.5 tons to 4 tons were excluded from the standard policy.

Part of the changes in the standard policy might have an effect on the average claim in this area of activity, however, the Group estimates that the impact on the amount of claims will not be material.

26.5.4 **Establishment of a database containing history of car accidents**

The Used Car Sale (Entitlement for Information and Proper Disclosure) Law – 2008 states, inter alia, that buyers of used cars may receive from the insurer of the car, any information it possesses.

The Insurance Companies Association taking actions to establish a database containing details about the vehicles registered in the database. The database will include particulars of the car, former insurers of the car, details about any insurance claims and accident damages. The database information will be available to both the buyers of used cars and to insurers joining the database. As of the date of this report, the establishment of the aforementioned database was not yet completed.

In June 2012 the Ministry of Transportation informed that it intends to establish a database that would also include the cars' insurance history. The database shall include historical data going 7 years backwards, as well as current information. The information will be available to the public, against payment. The usage of this database will be available during 2013.

Other general insurance lines

25.4.8 **Supervision of Insurance Businesses (Conditions of Contract for Home Insurance and Content) Regulations, 1986**

These regulations set forth the minimal terms of the homeowner comprehensive policy – the standard policy for homeowners. As per the terms of the standard policy, insureds may buy coverage for buildings or content coverages, with or without coverage in respect of earthquake. The conditions of the standard policy may only be changed in favor of the insureds. It is possible to expand the standard policy regarding the insured scope of coverage, risks, property, and liabilities. A draft **Supervision of Insurance Businesses (Conditions of Contract for Home Insurance**

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[54] The NII informed most insurance companies about cancellation of the agreement starting January 2009. As to Migdal – the agreement cancellation commences in January 2010.

[55] The Israel Antitrust Authority General Director gave a stipulated exemption for the management of these negotiations and it is in effect until November 2013.

and Content) Regulations (Amendment) – 2013 is pending, asking to introduce amendments to the Articles of Association and the standard policy.

General – regarding the area of general insurance

25.4.9 **Arrangements related to the calculation of insurance reserves in general insurance, changing the current situation**
The **Supervision of Insurance Business Regulations (Insurance) (Calculation of Reserves in General Insurance) – 2013**, published in February 2013, and the Circular published in January 2013 – the **Insurance Circular regarding the Calculation of Insurance Reserves in General Insurance,** relate to the update of existing law provisions regarding the calculation of reserves in general insurance. The main change that will upon the amendment's coming into effect, starting from the FS as of March 31st, 2014, is the cancellation of the reserve for surplus of revenues over expenses ("**surplus reserve**"). There are also instruction as to the calculation of reserves and the insurance lines in which the surplus reserve calculation will be performed. In addition, in July 2012 the Commissioner of Insurance published a position paper regarding **Best Practice for the Calculation of Insurance Reserves in General Insurance for the Financial Reporting**. For additional details regarding the arrangements related to changes in the calculation of insurance reserves in general insurance, see Note 37 b 3 c (6) to the Financial Statements.

25.4.10 **Proposal for changing products' regulation** – a Bill and draft Circulars regarding a change in the principles for the approval of insurance plans, see Clause 45.2.12 to Part E hereinafter.

25.4.11 In August 2012 the **Supervision of Insurance Business Regulations (Maximum brokerage fees in construction insurance with housing loans) - 2012** were published. The Regulations state that the brokerage fees that will be paid by insurers to insurance agents due to comprehensive structure insurance shall not exceed 20% (including VAT) of the insurance fees collected by the insurer from the insured. The Regulations also apply to brokerage fees in respect of insurance contracts with housing loans, coming into effect on the date of beginning and on, including in respect of insurance contracts with loans that were renewed on the date of beginning and on, even if it was entered before. The Regulations came into effect on January 1st, 2013. There are transitory provisions for 2013-2014, such that in each of these years, the maximum brokerage fees shall be 130% and 25% of the insurance fees collected from the insured, respectively.

25.5 For details regarding the scopes of activity and profitability in the area of general insurance in the Group, see Clause 8.3 to Part B above, Clause 1.3.4 in the BoD Report, as well as Notes 3 b and 3 d to the Financial statements.

26. The area's main products and services

26.1 Summarized description of the product (proposed insurance coverages) and unique features

26.1.1 **CMBI**
The product is a policy covering bodily injuries as a result of using a car, which must be acquired according to the Motorcar Ordinance, and its coverage is uniform and designated to provide insurance coverage to vehicle owners and drivers, against any liability they might incur as per the TACC, in respect of bodily injuries as a result of using a vehicle by the car's driver, passengers or pedestrians injured by the car.

Unique features

Product uniformity – the product is uniform, and it is mandatory to buy it, as mentioned above. The policy is a standard policy, as described in Clause 25.4.4 above.

Absolute liability and lack of need to prove guilt – the right of accident casualties to compensation is absolute and there is no need to prove guilt.

Compensation cap – the coverage as per CMBI policy is not limited in amount; the coverage limits are set forth by the TACC.

When the insurance comes into effect – the insurance coverage in CMBI comes into effect only after insurance fees were fully paid.

A long time until final outlining of an underwriting year – policies in CMBI are usually issued for one year. However, the pace at which claims in this line progress is longer and may take several years, due to the time that elapses between the occurrence of the event and the time of final outlining of damage and claim settlement. In many cases it involves a relatively complex factual and legal inquiry, both regarding the insured's liability and the scope of damage, the limitation period in respect of the cause of claim is longer than the customary limitation period in property insurance ("**Long Tail**"). This affects the profitability structure as described in Clause 1.3.4 in the BoD Report.

26.1.2 **Casco insurance**

The policy covering property damages and property damages to a third party for private and commercial vehicles of up to 3.5 tons is anchored, as already mentioned in Clause 25.4.6 above, in the Casco regulations. The standard policy sets the version and minimal conditions for casco insurance, which may be changed by the insurance company only if the change is in favor of the insured.

The coverages in the standard policy are damage which might be caused to the vehicle as a result of an accident, theft, fire etc., as well as property damages that the vehicle might cause to a third party. The standard policy also offers expansions in the scope of coverage and covered risks.

Under the service riders, the Group offers various coverages including glass breakage, road and towing services and alternative car etc.

The insurance policy for vehicles that are not private and commercial up to 3.5 tons (which is not a standard policy) is suitable for insuring other vehicles, such as trucks, trailers, taxis, motorcycles etc. The policy conditions are not subject to the terms of the standard policy, and therefore may be tailored to specific customers.

26.1.3 **Other general insurance lines**

(a) **Property insurance**

(1) **Homeowners insurance**

Homeowners insurance include building insurance and content insurance, based on property insurances plus liability insurances related to homes (third party liability and employers' liability in respect of housekeeping employees).

This is a key product in the individual insurances whose basic coverage is subject to minimal terms set by the standard policy terms for homeowners insurance, as detailed in Clause 25.4.8 above. Also, the product tariffs are supervised and approved by the Commissioner of Insurance.

The underwriting of this product is based on a basic tariff (with some variance regarding parterres) through analyzing the specific risk. The claims in respect of such policies are quickly outlined and the time elapsed between the occurrence of the insurance event and the claim settlement is usually a few months.

Furthermore, under the policy, the Group offers various service riders including water damages, repair of electric appliances and computers, emergency services and doctor’s house visits, that are sold together with the homeowners’ insurance policy.

The main target audience for this product is individual customers.

Furthermore, the Group offers another product, "structure insurances for mortgage", which is a policy for building only, whose main target audience is mortgage banks borrowers. This policy is sold both through the banks' insurance agencies and through the Group's agents.

(2) **Business insurance**

Business insurance is property, buildings and content insurance, which are used for business needs against fire risks and associated risks (risks coverage sold together with fire risks coverage, such as coverage for burglary, explosion and earthquake). This coverage is extendable to consequential damage coverage, namely loss of profits.

This product is usually sold as part of an "umbrella" policy, which includes several coverages (property and liability coverages), aimed at combining into one policy all coverages needed for the business. The Group offers various businesses, such as offices, hi-tech companies and others, a variety of insurance plans meeting their specific needs.

Since the risk level involved in these complex insurances is higher, the Group's policy is to spread the risks through engagements with reinsurers, as mentioned in Clause 47 to Part E hereinafter.

The underwriting of this product is mostly based on the specific risk analysis and in large corporations insurance, on individual negotiations with the reinsurers. Most claims in respect of such policies are quickly outlined and the time spread between the occurrence of the insurance event and the claims settlement usually takes only few months.

The main target audience for this product is small to medium businesses, as well as very large corporations.

(3) **Other property insurances**

This framework includes diversified insurance products in the area of property, such as marine and aviation insurances (watercraft, aircraft, goods in transit), contractor’s insurances, mechanical engineering equipment insurance, fidelity insurance and all risks insurance. The Group's scope of activity is not material.

(4) **Personal accident insurance**

Personal accidents insurance compensates the insured in respect of any damage caused to him/her due to an accident. Coverage is granted against death or disability as a result of an accident, and may also include coverage for temporary occupational disability.

(b) **Liability insurances**

(1) **Third party liabilities insurance** – the purpose of this product is to protect insureds from liability which they might bear, in respect of damage they caused, by negligence, to a third party. The coverage is adjusted to the insureds' activity and the limit of liability in the policy is determined by the insureds, at their discretion, based on the risk level to which they are exposed, in their opinion. This product is sold both as an independent individual policy (third party liability coverage only), and as part of an "umbrella" policy, which includes several coverages (property and liability coverages), whose aim is to combine into one policy all coverages required for the business.

(2) **Employers' liability insurance** – the purpose of this product is to protect employers from liability which they might bear, in respect of damage they caused, by negligence, to one of his employees, during and due to his work. Coverage in these policies is provided above the sums provided by the National Insurance Institute of Israel, which handles work accidents. The limit of liability in such policies is set in advance, in some cases, but it is possible to acquire a higher limit of liability, according to the insureds' evaluation of their exposure to damages that might be caused to their employees.

This product is sold both as an independent individual policy (employers' liability coverage), and as part of an "umbrella" policy, which includes several coverages (property and liability coverages), whose aim is to combine into one policy all coverages required for the business.

(3) **Other liabilities insurances** – within the framework of liabilities insurances there are also other products, including product liability insurance, professional liability insurance and Directors and Senior Officers liability insurance policies. As opposed to the previous liability insurances, coverage in these products is provided for submitted (but not necessarily occurred) claims throughout the policy life, although the policy often also includes reference to the date of the occurrence of event.

26.1.4 **Alternatives to products and changes therein**

(a) CMBI – as mentioned above, it is a unique product that must be purchased.

(b) Casco – large corporations with large car fleets, including leasing companies, sometimes tend not to insure their vehicles and bear the risk. Part of the insurance cover granted under casco through riders may be purchased separately in companies that provide these services.

(c) Other general insurance lines – the various products in casco and liabilities are unique to insurance companies, and may not be perfectly replaced by non-insurance products. However, it is possible to reduce the need for insurance coverage by taking measures in order to manage and decrease risk.

The insurance products in the area, except CMBI, are voluntary.

27. Data breakdown for products and services

27.1 CMBI

Following are the main data regarding CMBI in the years 2010-2012 (in NIS million)

	2012	2011	2010
Gross premium	266	258	255
Premium less reinsurance (retained)	261	253	249
Increase in liabilities and payments in respect of insurance contracts – gross	188	233	243
Increase in liabilities and payments in respect of insurance contracts retained	198	240	244

A moderate increase in premium in 2010-2012, stemming from an increase in the quantity of policies. In 2012 the increase in the quantity of policies was affected, inter alia, by a decrease in tariffs, in spite of a discontinuation of the insurance of some State employees (the premium in their respect is approx. NIS 8 million). The changes in liabilities and payments in respect of insurance contracts in 2010-2012 mainly stem from updates in the estimate of outstanding claims for old underwriting years, as well as due to changes in inflation rates, which affected the increase of outstanding claims.

In 2012, the decline in the increase in liabilities and payments in respect of insurance contracts vs. 2011, was affected by an improvement in the claims experience, which led to a decrease in the actuarial estimate of outstanding claims, as well as a decrease in inflation rate, which affected the change in the cost of claims.

27.2 Casco

Following are the main data regarding casco in the years 2010-2012 (in NIS million):

	2012	2011	2010
Gross premium	351	371	357
Premium less reinsurance (retained)	350	370	357
Increase in liabilities and payments in respect of insurance contracts – gross	272	318	274
Increase in liabilities and payments in respect of insurance contracts retained	272	318	274

The changes in the scopes of premiums were significantly affected by the insurance of some State employees in 2011 (the premium in their respect is approx. NIS 14 million) since the Company won a tender, and the insurance of this group as discontinued in 2012.

Regarding the increase in liabilities and payments in respect of insurance contracts, see details in the following table.

The gross and retained data are similar since the Group does not acquire reinsurance in this line, except for an agreement in a non-material scope – see Clause 30.2 hereinafter.

Following is the breakdown of gross paid claims in the years 2010-2012 (in NIS million):

	2012	2011	2010
Theft	24	29	22
Accidents	223	239	228
Other (1)	36	39	36
Total paid claims	283	307	286
Change in liabilities	(11)	11	(12)
Total liabilities and payments in respect of insurance contracts, gross	**272**	**318**	**274**

(1) Including indirect expenses for claims settlement

In 2012 there was a decrease in the cost of claims in all types of damages, following an increase in 2011. The decline was significantly affected by an improvement in the incidence of accident damages. The cost of theft also decreased in 2012, in spite of an increase in the incidence of theft in the Group, as detailed in Clause 25.2.2 (b) above, following a decrease in the average damage value.

27.3 Other general insurance lines

Following are the main data regarding other general insurance lines in the years 2010-2012 (in NIS million):

	2012	2011	2010
Gross premium	790	817	791
Premium less reinsurance (retained)	342	338	317
Increase in liabilities and payments in respect of insurance contracts – gross	386	554	496
Increase in liabilities and payments in respect of insurance contracts retained	238	270	232

Following is the breakdown of data into casco and liabilities:

Property lines (1)

	2012	2011	2010
Gross premium	535	550	530
Premium less reinsurance (retained)	156	160	146
Increase in liabilities and payments in respect of insurance contracts – gross	207	353	238
Increase in liabilities and payments in respect of insurance contracts retained	57	53	50

(1) In the above table, the relevant data for personal accidents insurance and other property insurances are included within the property lines.

The decrease in gross premiums in property lines in 2012 vs. 2011 is mainly affected by a decrease in the scope of insured businesses and a change in the insurance period in several corporate businesses, which was partly offset due to an increase in the scope of premiums in homeowners insurance. The increase in premiums in 2011 vs. 2010 was due to an increase in the number of policies, partly offset by a change in insured periods in several corporate businesses fully covered by reinsurance.

The high level of liabilities and payments in respect of insurance contracts, gross, in property lines in 2011 was due to two large claims mostly covered by reinsurance.

Following is the breakdown of gross paid premiums in homeowners line in 2010-2012 (in NIS million):

	2012	2011	2010
Burglary	23	19	15
Water damage	28	23	22
Fire	12	12	12
Other [1]	24	25	20
Total paid claims	87	79	69
Change in liabilities	-2	(3)	4
Total gross liabilities and payments in respect of insurance contracts	**85**	**76**	**73**

(1) Including indirect expenses for claims settlement.

The increase in paid claims in homeowners insurance in 2010-2012 was mainly affected by a continuous increase in the inventory of policies.

Liability lines

	2012	2011	2010
Gross premium	254	266	261
Premium less reinsurance (retained)	185	179	171
Increase in liabilities and payments in respect of insurance contracts – gross	179	201	258
Increase in liabilities and payments in respect of retained insurance contracts	180	216	182

The decline in in gross premiums in 2012 vs. 2011 was mainly due to the discontinuation of the insurance of a large business, fully covered by reinsurance.

The changes in liabilities and payments in respect of insurance contracts in 2010-2012 are mainly due to updates in the evaluation of outstanding claims regarding old underwriting years, as well as changes in inflation rates, which affected outstanding claims.

The decrease in liabilities and payments in respect of insurance contracts in retention in liability lines in 2012 vs. 2011was mainly affected by the fact that last year, there was a deterioration in claims experience, which led to an increase in the actuarial evaluation of outstanding claims in respect of old underwriting years, and there was a loss in respect of underwriting year 2008. In addition, there was a reduction in inflation rate, which caused a change in the cost of claim.

The decrease in liabilities and payments in respect of insurance contracts, gross, in liability lines in 2011 vs. 2010 is due to an update in the evaluation of reinsurers' liabilities.

For additional details regarding the financial results see Clause 1.3.4 to the BoD Report and Notes 3b and 3d to the Financial Statements.

28. Customers

28.1 CMBI

The Group's customers in this line are individuals, collectives (employers or employee unions with whom the Group engages in agreements insuring all corporate cars), companies with car fleets, including companies whose occupation is car-related, such as car rentals and leasing companies. Since the line's product is uniform, the coverage price and service quality are the main factors in choosing the insurance company.

Following are data regarding the breakdown of activity in CMBI according to gross premium in 2010-2012 (in NIS million and in percentage):

	2012		2011	
Customers' characteristics	**Gross premium**	**Breakdown in percentage**	**Gross premium**	**Breakdown in percentage**
Individual insureds and small business customers (not car fleets)	202	76	183	71
Collectives, vehicle fleets and car-related occupation companies	64	24	75	29
Total area of activity	**266**	**100**	**258**	**100**

The decrease in the weight of collectives, car fleets and companies dealing with cars, out of the Group's total gross premium vs. 2011, was mainly due to the discontinuation of State employees insurance.

In 2012, the rate of renewals in CMBI, in terms of premium from policies that were valid in the previous year, totaled approx. 67%, vs. a renewal rate of approx. 70% in 2011.

In light of the harsh competition and the existence of a differential tariff in CMBI, there are many cases in which CMBI is purchased from one insurance company and casco insurance from another. In the line of CMBI, customers who are also insured in casco insurance, constitute about 59% of premiums in this line in 2012, vs. approx. 62% in 2011.

Following are details regarding customers' seniority in CMBI in terms of premium turnover for 2012 and 2011 in percentage:

Year	**New policies**	**1 year**	**2 years**	**3 years and more**	**Total**
2012	39	22	12	27	**100**
2011	41	18	12	29	**100**

The high rate in 2011 was affected by the Company's winning the tender for insuring part of State employees. In 2012 the high rate was maintained in spite of the discontinuation of this insurance.

28.2 **Motor Casco insurance**

The Group's customers in this line are individuals, collectives (employers or employees unions with whom the Group engages in agreements insuring all corporate cars), companies with car fleets, including companies whose occupation is car-related, such as car rentals and leasing companies.

Following are data regarding the breakdown of activity in casco according to gross premium in 2011-2012 (in NIS million and in percentage):

	2012		2011	
Customers' characteristics	**Gross premium**	**Breakdown in percentage**	**Gross premium**	**Breakdown in percentage**
Individual insureds and small business customers (not car fleets)	284	81	287	77
Collectives, vehicle fleets and car-related occupation companies	67	19	84	23
Total area of activity	**351**	**100**	**371**	**100**

The decrease in the weight of collectives, car fleets and companies dealing with cars, out of the Group's total gross premium vs. 2011, was mainly due to the discontinuation of State employees insurance.

In 2012, the rate of renewals in casco, in terms of premium from policies that were valid in the previous year, totaled approx. 70%, vs. approx. 72% in 2011.

In the line of casco, customers who are also insured in CMBI, constitute about 79% of premiums in this line in 2012, vs. approx. 76% in 2011.

Following are details regarding customers' seniority in casco in terms of premium turnover for 2012 and 2011 in percentage:

Year	**New policies**	**1 year**	**2 years**	**3 years and more**	**Total**
2012	29	22	14	35	**100%**
2011	34	18	12	36	**100%**

The relatively high rate of new policies in 2011 was affected by the Company's winning the tender for insuring part of State employees, as set forth above.

28.3 **Other general insurance lines**

The Group's customers in other general insurance lines are diversified: individuals, small businesses, large companies, collectives and corporations, including mortgage banks borrowers.

Following is a table describing the distribution of customers in other general insurance lines according to gross premium in 2011-2012 (in NIS million and in percentage):

	2012		**2011**	
Customers' characteristics	**Premium**	**Breakdown in percentage**	**Premium**	**Breakdown in percentage**
Individual insureds and small business customers	486	62	468	57
Collectives and corporations [(1)]	304	38	349	43
Total area of activity	**790**	**100**	**817**	**100**

(1) Including insurance for mortgage banks borrowers, which is under collective insurance in run-off.

The decrease in the weight of collectives and large corporations to total gross premium in the Group compared with 2011, was due to a the non-renewal of several corporate insurances and a change in the insurance periods in several large businesses, as well as an increase in the scope of premiums in individual customers insurance.

In this line there is a trend of maintaining long-term relations with the insurance company, thus the renewal rate is relatively high. This may be explained by the importance attributed by insureds to the insurance company's professionalism, as well as coverage continuity.

In 2012, the renewal rate in homeowners insurance line[56] in terms of premium from policies that were valid in the previous year totaled approx. 96%, unchanged compared with 2011.

Following are details regarding customers' seniority in homeowners insurance[57] in terms of premium turnover for 2012 and 2011 in percentage:

Year	New policies	1 year	2 years	3 years and more	Total
2012	15	14	10	61	**100%**
2011	18	11	8	63	**100%**

29. Marketing and distribution

29.1 **General**

The Group markets its products through an array of insurance agents with whom it is engaged, which is the main marketing channel for the insured. The agents array usually works with several insurance companies.

From time to time, the Group engages in direct negotiations with companies having car fleets or with customers in the car-related businesses, mainly in CMBI or casco.

In other general insurance lines, the Group also has a unit specialized in providing combined and complex insurance solutions, especially for corporate businesses active in Israel (**"CRD"**). In order to offer these customers the unique insurance solutions, the unit also offers specific reinsurance arrangements through facultative reinsurance arrangements, i.e. coverage for risks embedded in specific policies, and in this framework, most of the coverage or all of it is insured in reinsurance.

The commission paid to agents in this area is calculated in agreed-upon percentage from premium, while the commission rate changes according to the specific line.

In 2012 the average aggregate commission rate in this area totaled approx. 15.1% of gross premium, vs. approx. 14.6% in 2011. The average commission rate in CMBI totaled approx. 6.2% vs. 5.0% in 2011, in casco – approx. 20.7% vs. 19.7% in 2011, in property and other lines – approx. 16.3% vs. 16.6% in 2011 and in liability lines – approx. 14.3% vs. approx. 12.2% in 2011. The changes in commission rates were affected by the change in the mix of insured businesses.

In 2012, the Group had no agent whose scope of sales exceeded 10% of the scope of premiums in this area.

30. Reinsurance

30.1 **CMBI**

The Group's liabilities in the CMBI line in 2012 are covered by excess of loss reinsurance. As a result of the reinsurance arrangement, exposure in respect of a single claim is limited. Within this agreement there is accumulative deductible of all claims beyond the set retained amount. As customary in this kind of contracts, no commissions are received from the reinsurers.

All reinsurers that took part in the insurance in this line are rated A or higher by S&P or another rating company, whose rating was converted as per an index defined by the investment regulations.

[56] Excluding insurance for mortgage banks borrowers, which are included within collective insurance in run-off.

[57] Idem.

Generali, which was the Company's controlling shareholder up to October 29th, 2012, rated A, participates in the scope of about NIS 1.2 million and at approx. 22% of reinsurance premium in this line. The total scope of premium for reinsurance companies in this line is not material.

30.2 **Motor Casco Insurance**

The line of casco is characterized by large dispersal and relatively small standard deviation of claims. In light of the above characteristics, the Group does not purchase reinsurance in this line, except an excess of loss type agreement, of insignificant scope.

All reinsurers that took part in this agreement are rated A and higher by S&P or another rating company, whose rating was converted as per an index defined by the investment regulations.

As customary in this kind of contracts, no commissions are received from the reinsurers.

30.3 **Other general insurance lines**

The main lines in which the Group purchases reinsurances in the area are for coverage of different types of property lines, including: contractors, engineering and marine and also for covering liability lines. The Group's reinsurance layout and policy in the area are very important to its ability to insure large or special risks. As a result of the various reinsurance arrangements, the Group's exposure in respect of a single claim is usually limited, according to the amounts agreed-upon between the Group and the reinsurers, from time to time, including the retained amounts. The maximum exposure and retained amounts are determined according to the Group's estimate of the expected damages or events, and the negotiations with the reinsurers.

In the property, contractors, engineering and marine insurance lines, the Group purchases proportional reinsurances such as quota share and surplus insurances, in which the reinsurers' participation is set as a fixed and equal percentage both in the premium and in the claim.

In proportional insurances, some of the reinsurers limited their participation to 5% of the exposure sum to earthquake events. In terror-related events there is a limitation of USD 50 million per event and USD 100 million per year.

In recent years, in some treaties commissions received from reinsurers are at fixed rate out of premium, and in others at variable rate according to the results. The engagements in these lines are done with reinsurers rated BBB or higher as per S&P or another rating company whose rating was converted as per an index determined under the investment regulations. In practice, most reinsurance premiums ceded in these lines are to reinsurers rated A- and higher.

In 2012, there was a significant increase in the cost of the Group's catastrophe insurances due to the change in the earthquake coverage mix, as well as due to an increase in the cost of catastrophe coverages due to large catastrophe damages in 2011 (earthquakes in Japan and New Zealand, Floods in Thailand, etc.).

In the treaties signed by the Group in 2013 in various types of property coverages, except earthquake coverage, there was an immaterial change regarding single risk coverage. In earthquake coverage some reinsurers limited their participation to events of 4% and more of the exposure amount, and the mix of reinsurance treaties was changed, such that the share of proportional treaties in the coverage increased. For excess of loss treaties, the Company decided to increase its participation in risk, along with increasing the required capital by approx. NIS 150 million.

In the liabilities lines, the Group purchases excess of loss reinsurance treaties, in which the retained amount is fixed and the reinsurer covers damage exceeding the set amount. As customary in such reinsurances, there are no commissions received from reinsurers. Such engagement treaties are done with insurers rated A- or higher as per S&P or another rating company whose rating was converted as per an index determined under the investment regulations.

In liability lines, the Group did not reach the ceilings set in the reinsurance treaties in the reported period, and has no outstanding claims in a scope which is close to the set limits.

30.4 **General**

In businesses where the insurance amounts exceed the scope defined in the relevant treaty and/or when the risk is excluded from the treaty with the reinsurer, and/or due to specific underwriting considerations, with adjustments to the treaties' frameworks and conditions, facultative reinsurance is purchased. Sometimes, within a comprehensive insurance arrangement, reinsurance treaties with unrated companies are included.

The Group has a few reinsurers, whose share in reinsurance premiums in general insurance in the reported year constitutes 10% or more, as follows:

		2012		2011	
Reinsurer's name	**Rating according to S&P [58]**	**Reinsurance premium ceded to the reinsurer (NIS million)**	**Share out of total reinsurance premium in general insurance in percentage**	**Reinsurance premium ceded to the reinsurer (NIS million)**	**Share out of total reinsurance premium in general insurance in percentage**
Generali [(1)]	A	161	35	189	39

(1) Including premiums in facultative reinsurance at 100%, in the amount of approx. NIS 56 million in respect of one insured.

For further details about reinsurance, exposure to catastrophe and details of reinsurance transactions with the parent company Generali, see Clause 47 to Part E hereinafter, as well as Notes 37 and 38 e to the Financial Statements.

31. Suppliers and service providers

The Group has agreements for the procurement of products and professional services in various areas. The Group companies bear, like any other insurer, expenses related with the insurance event insured by the policy. These expenses include covering the cost of various services covered by insurance policies, such as paying for hospitalization services and other medical services included in the insurance coverage, spare parts for car products etc. In addition, the Group acquires ancillary services for insurance claims paying up in various areas, such as attorneys, investigators and medical experts.

For suppliers who are not unique suppliers in this line see Clause 49.2 to Part E hereinafter.

[58] The rating in the table is as of just before the Report's publication date.

31.1 **Unique suppliers for the area**

31.1.1 **Data Car Israel Ltd**.

Within the claim management in this area, the Group uses, inter alia, an appraisal and motorcar software known as Audatex - which is represented and operated in Israel by Data Car Israel Ltd. ("**Data Car**"), that provides assessment software services to the Group, other insurance companies and car appraisers. As of August 2007, the Group owns all of Data Car's shares. The Commissioner authorized the Group to acquire all of Data Car's shares subject to stipulations imposed by him regarding the use of the Data Car software and future changes in the software and in Data Car's areas of occupation, and additional restrictions imposed on Migdal and on its relations with Data Car and other insurers.

The cost of services rendered by Data Car to the Group in respect of the assessment services in 2012 totaled a non material amount.

32.1.2 **Garages**

The Group is engaged in an agreement with approx. 210 garages throughout Israel, through which damages covered as per the policy's terms may be repaired, while granting certain benefits to insureds who choose to utilize this service.

31.2 **Special arrangements regarding claim management**

31.2.1 “**Light heavy” clearance outline**

Under CMBI activity, the Insurance Companies Association operates a clearance system aimed at transferring payments automatically between motorcar insurers as per the TACC Law and the Compensation Order for Road Accident Victims (Arrangements for the Distribution of Burden of Compensation Between Insurers) – 2001. The parties in the clearance system are all insurers, and it applies to accidents involving vehicles insured by policies.

Since in many cases insurance companies did not agree on liability, it was decided in 2006 to expand the authorities of the outline manager and give him arbitration authorities regarding liability disputes, both in the legal aspect and the factual aspect. The outline manager may receive an opinion from legal counselors, hire private investigators and even hear testimonies and collect evidence.

All insurance companies that joined the original outline also joined the expanded outline[59].

31.2.2 **"Benoam"**

The Insurance Companies Association engaged with the Israeli Arbitration and Dispute Settlement Ltd. Center (“**Benoam**”) – so that it provides arbitration services in subrogation claims of one insurance company towards another in respect of casco insurance in disputes not exceeding NIS 100,000. Insurance companies may join the arbitration arrangement whether they are members in the Insurance Companies Association, or not. Every insurer that joins it may leave by the end of every calendar year[60].

In July 2012 Migdal Insurance informed the Association and Benoam that it would leave the arbitration agreement as of the beginning of September

[59] In August 2006 the Anti-Trust Director General approved the expanded outline with no time limit, provided the Pool is not reflected in the outline. It was also stated that the arbitrator's rulings will not serve for issues outside the outline.

[60] The above arrangement received an exemption from an agreement in restraint of trade, stipulated by conditions. The exemption is effective till June 6th, 2014.

2012. Claims that will be received after that date, if they entail a dispute between insurance companies, shall be litigated in Court.

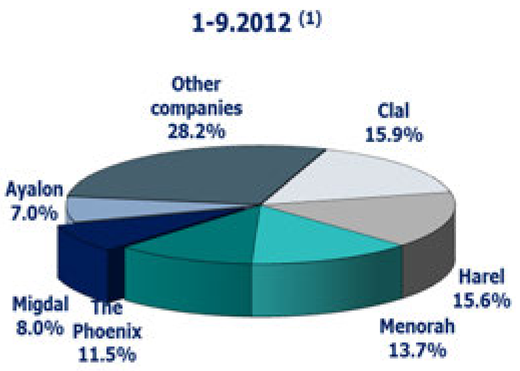
32. Competition

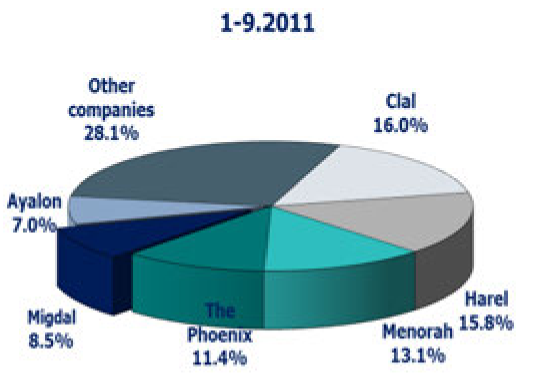
32.1 Market data

32.1.1 The area of general insurance

The five largest entities active in the area of general insurance in Israel are Clal Group, Harel Group, Menorah Group, The Phoenix Group and Migdal Group, which constituted approx. 65% of all gross premiums in general insurance on the market in the first nine months of 2012.

The following charts illustrate the breakdown of gross premium in the general insurance lines:



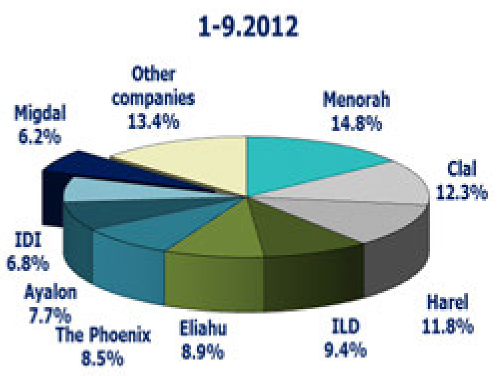


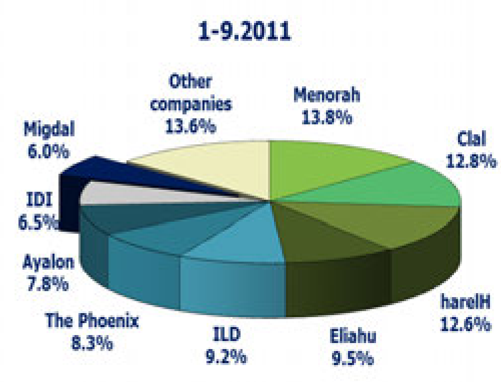
(1) Eliahu Insurance's market share totaled approx. 4.6% in the first nine months of 2012.

32.1.2 CMBI

The CMBI line involves 13 insurance companies, including direct insurance companies. The 5 largest entities operating in this area during the first nine months of 2012 are Menorah Group, Clal Group, Harel Group, ILD and Eliahu Insurance, which, in the first nine months of 2012, constituted approx. 57% of the total gross premium in this line.

The following charts illustrate the breakdown of gross premium in CMBI[61]:





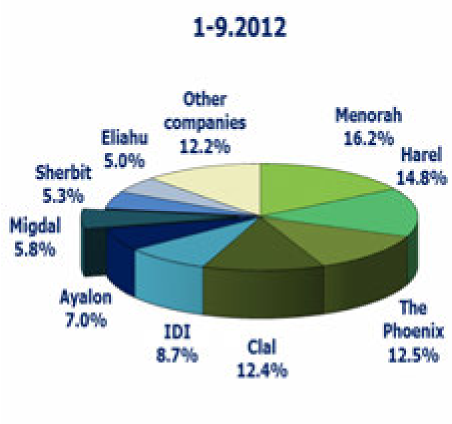
The weight of all direct insurance companies in this period totaled approx.9.2% out of total gross premium in the line, vs. approx. 8.7% in the corresponding period in 2011.

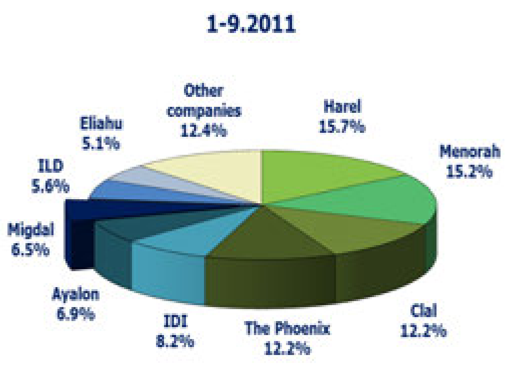
[61] The data are based on the processed MoF reports published in its website ("Managerial reports").

32.1.3 Casco line

Most insurance companies operate in the casco line, including insurance companies that market policies directly. The 5 largest entities operating in this line are Menorah Group, Harel Group, , The Phoenix Group, Clal Group and IDI direct insurance company, which constituted approx. 65% of the total gross premium in this line, in the first nine months of 2012.

The following charts illustrate the breakdown of gross premium in CMBI in casco[62]:





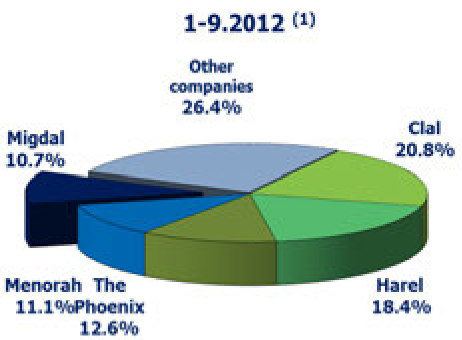
The weight of all direct insurance companies in this period totaled approx. 11.9% out of total gross premium in the line, vs. approx. 11.3% in the corresponding period in 2011.

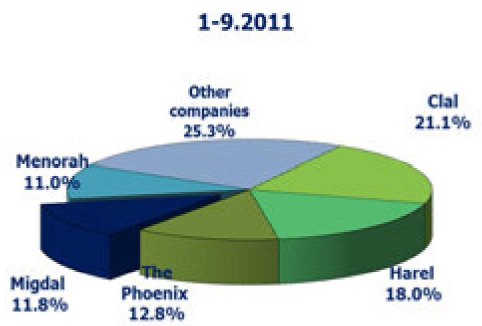
32.1.4 Other general insurance lines

Most insurance companies are active in the other general insurance lines, some of whom even market policies directly to individual customers.

In the first nine months of 2012, other general insurance lines in Israel were mainly held by the five largest insurance groups, which controlled about 74% of the market: Clal Group, Harel Group, The Phoenix Group, Menorah Group Migdal Group.

The following charts illustrate the breakdown of gross premium in other general insurance lines.

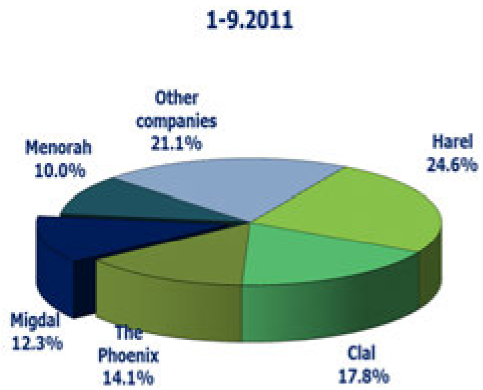




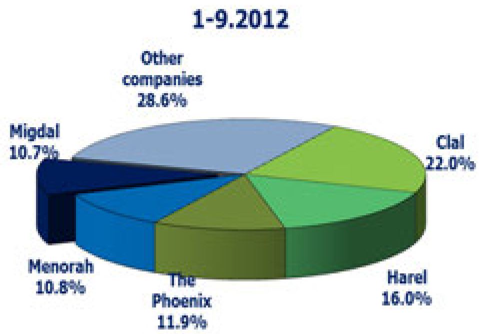
(1) Eliahu Insurance's market share totaled approx. 1.6% in the first nine months of 2012.

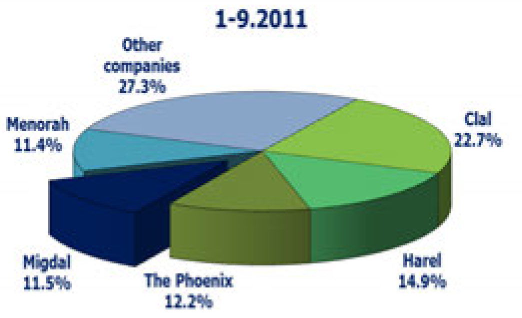
The following charts illustrate the breakdown of the gross premium in property lines (excluding CMBI):

[62] The data are based on the processed MoF reports published in its website ("Managerial reports").



The following charts illustrate the breakdown of the gross premium in property lines (excluding casco):





32.2 **Competition and the Group's main methods of handling competition**

32.2.1 **CMBI**

Insurance coverage in this line is uniform and competition focuses on the tariff and service. The market has a tariff comparison system managed by the MoF, of which the public is aware while conducting comparisons based on its data. The Group manages the tariff so that it permits it to compete on the customer segments it desires.

While in the past, insureds used to purchase comprehensive and CMBI insurance in the same insurance company, upon the enhanced competition, there are many cases in which the CMBI is purchased in one insurance company and casco in another.

32.2.2 **Motor Casco Line**

Competition in casco is harsh, which can be attributed to the lack of variance in the insurance coverage by different companies, and to the activity of direct insurance companies. In the car fleets and collectives, the competition is even harsher.

The Group offers insureds competitive prices while maintaining a planned profitability rate. To do so, it uses a differential tariff allowing it to focus on insureds groups which, to the Group's estimate, are characterized by relatively low risk. The Group checks the tariff regularly in order to quickly respond to market changes.

32.2.3 **Other general insurance lines**

The generators of competition in other general insurance lines are insurance companies fighting for their market shares, as well as insurance agents competing over customers and their representation. The competition in this area is also affected by global trends on the reinsurance market. In liability and property insurance for businesses, there are no standard policies and supervised tariffs, and there is a price decrease due to competition in the area.

The Group's policy is maintaining good profitability along with setting high-quality underwriting rules and implementing efficient and comprehensive control in the process.

The Group's estimate is future forecasting information based on existing provisions. This forecast may not materialize in case of legislative amendments which may not be predicted by the Company, or if the market behaves differently than the anticipated behavior upon the reported date.

Area D – Financial Services

33. General information about the area of financial services

33.1 **General**

The Group's activity in the financial services area is performed by Migdal Capital Markets (1965) Ltd. ("**Migdal Capital Markets**") and its subsidiaries ("**Capital Markets Group**"). Migdal Capital Markets was established in 1965 and was acquired by the Group in 2001.

The Capital Markets Group deals with financial asset management services, especially financial asset management services[63] (mutual funds management, portfolio management and hedge fund management) and investment marketing[64] (marketing structured products and hedge funds), execution services in the Stock Exchange and in regularized markets (brokerage), underwriting and investment banking. Furthermore, Capital Markets Group engages in managing various courses on the capital market, including preparation courses for the MoF and the ISA professional courses, via a subsidiary.

33.2 **The area of activity structure and its changes**

33.2.1 **General**

The financial services area is highly affected by the local and global capital market condition. The area is characterized by high volatility as a result of political and economic events both in Israel and abroad, affecting the securities rates in the Stock Exchanges and regularized markets. The financial services area is characterized by high regulation, and is affected by different regulatory decisions in the capital market, including the Israel Securities Authority (ISA), the Tel Aviv Stock Exchange Ltd. ("**the Stock Exchange**" / "**TASE**"), the Bank of Israel etc. This line involves continuous harsh competition, both on the part of various banking corporations (brokerage activity) and non-banking entities (all of the line’s activities).

33.2.2 **The activity of financial asset management and investments marketing in the Group** – includes mutual funds management (including mutual tracking funds, that are a passive/CPI-tracking mean for investment management), investment portfolio management and investments marketing and management of hedge funds. The activity is performed through the following companies – Migdal Trust Funds Ltd. (“**Migdal Funds**”), Migdal Investment Portfolio Management (1998) Ltd. ("**Migdal Portfolio Management**"), and Tau Hedge Funds Management Ltd. ("**Tau-Dragon**"), all companies in MCM Group[65].

[63] Until the end of 2010 Capital Markets Group was also active in the area of provident and training funds through Migdal Platinum, included within the area of life assurance and long-term savings - Area A above. A process of transfer of management rights of provident funds, previously managed by Migdal Platinum, to Migdal Makefet, which is a managing company of new pension funds and provident funds, was completed.

[64] The “investments marketing” service is equal to “investments advising” service, but the service provider is affiliated or related to institutional organs. Since institutional organs operate within Capital Markets Group, Capital Markets Group renders “investments marketing” services, instead of “investments advising” services.

[65] MCM holds, directly and indirectly, 100% of Migdal Funds' and Migdal Portfolio Management's share capital, and approx. 71% of Tau-Dragon's share capital.

In addition, the company deals with Family Office[66] activity via Arxcis Global Wealth Management Ltd.[67] ("**Arxcis**"). The activity of Tau-Dragon and Arxcis is limited and non-material at this stage, therefore the reporting about them is limited in this report.

33.2.3 **The brokerage activity in Capital Markets Group** – this activity is mainly rendering execution services in stock and derivatives in TASE and in Stock Exchanges and regulated markets overseas. This activity is performed by Migdal Stock Exchange Services (N.E.) Ltd. ("**Migdal Stock Exchange Services**"), which is a member of the Stock Exchange and in the Stock Exchange clearinghouse.

33.2.4 **The underwriting and investment banking activity in Capital Markets Group -** is performed by Migdal Underwriting and Business Initiatives Ltd. ("**Migdal Underwriting**").

33.2.5 **Extending courses activity in MCM Group** - this activity includes extending professional courses on the capital market and preparation courses for the MoF's and the ISA's professional exams. This activity is performed via MCM - the Finance Academy Ltd. ("**Finance Academy**"). The Finance Academy's activity is non-material at this stage, therefore the reporting about it is limited in this report.

33.3 **Limits, legislation, and special constraints applying to the area of activity**

The activity of the financial services area is subject to a lot of unique regulation, and to the duty to receive permits and licenses from various State authorities, and mainly the ISA and the TASE. Each of the companies in Capital Markets Group is subject to a different set of rules, laws, instructions and orders. Later on, we will bring a description of the main relevant provisions referring to all the types of services in this area of activity. In addition, enclosed please find the specifications of the main changes in legislative arrangements that occurred in the reported period:

33.3.1 **The reform in the area of ETFs and passive product management**

The ISA is promoting a reform in the area of index products (ETNs) from a regime of from a reporting governance (rules for the disclosure of reporting corporation) to a supervision governance that is currently common in the mutual funds sector. Thus reform is expressed in a pending Bill for the "'Joint Investments Trust Law (Amendment No. 21) (ETNs and ETFs) – 2012. The Bill is aimed at closing the gap that currently exists in the regulatory provisions that apply to index products and the mutual funds. In addition, the amendment proposal will allow creating a new type of mutual funds - ETF funds: closed tracking funds with special characteristics, traded on the TASE, aimed at achieving results that are as similar as possible to the change rate in the specific asset, and sets forth provisions that would apply to them. Within the reform, **Joint Investment Managers** may manage simultaneously one or more of the following arrangements - traditional mutual funds, ETFs or ETNs.

Furthermore, since ETNs and ETFs are alternative investment instruments, whose general characteristics are similar, it is suggested to apply a joint wording of the Regulations on this matter to ETFs and ETNs, in order to provide to the public an accessible platform for comparing these products,

[66] Help with choosing investment managers, including of hedge funds and other private investment funds, setting an asset allocation for each investment manager, supervising the composition of the various investment managers portfolios, follow up on the customers' expenses and concentrating the customers' financial information in one place etc.

[67] Until July 1st, 2011 this company was jointly owned by Mivatch Management and Migdal Capital Markets. On September 2nd, 2011, an agreement was signed between MCM and Mivtach Management, pursuant to which MCM's shares (23.46% in the company were transferred to Mivtach Management, effective as of July 1st, 2011. Since Mivtach Management is controlled by the Group, Arxcis' activity continues to be included in the financial services activity in this area.

including the unified calculation of the price of surrenders and the yield of their tracking assets' prices, and present these data in the media. This reform, if it is outlined, may allow Migdal Funds to continue developing and expanding the area of tracking mutual funds management, upon turning them into ETNs traded on the TASE.

33.3.2 **Road map: the ISA's objectives and plans for the next years**

In September 2012 the ISA published a road map that includes two parts:

(a) Strategy, projects and Work Plans.

(b) Proposals for certain reliefs in regulation.

According to the Company, these reliefs are not expected to bring about a significant change in the area of activity.

33.3.3 **General advising and marketing**

The ISA is promoting a regulation regarding providing general advice and investment marketing not aimed at being provided to a certain person or taking into account the particulars of a certain person, within a **Bill for the Arrangement of Occupation in Investment Advising, Investment Marketing and the Management of Investment Portfolios (Amendment No. 19) (General Investment Advising and General Investment Marketing) – 2012.** The Bill includes rules and reliefs as to providing investment advice in the media, including regarding advising and investment marketing with no personal features, and it is aimed to a non-specific public. The Bill would like to expand these rules and reliefs and create a differentiation and adjustments to the duties related to providing advising and investment marketing with no personal features to a non-specific target audience, since some of the duties set forth now pursuant to the Law, are irrelevant to providing this kind of service. According to the Company, this Bill shall increase the ability of those dealing with this area to market their products and services.

For additional details regarding the regulation in effect in this area, see Clause 43 hereinafter.

33.4 **Developments in the macro-economic environment and their implications on the area of activity**

33.4.1 **General**

In 2012 volatility was recorded on capital markets worldwide, due to the uncertainty on global financial markets and concerns regarding the debt crisis in Europe and global recession. In 2H12, the risk level embedded in the global financial markets, especially in debt-ridden countries, decreased, in light of monetary easing measures, taken by central banks on leading markets worldwide and expectations for additional QEs. Along with a decline in risk level, leading share indices worldwide increased, mainly in 3Q12.

For developments in the economy and on capital markets, see also Clause 2 in the BoD Report hereinafter.

33.4.2 **Area of asset management and investments marketing**[68]

The line of asset management is divided into 2 ways of management - traditional investment management (also called active management) and indices-tracking management (also called passive management). In 2012 there was a significant increase in the scopes of the mutual funds line and the indices products line:

[68] Data referring to the mutual funds line are based on Bizportal system data for 2012 and the data referring to ETNs are based on the TASE monthly review for December 2012. Regarding the portfolio management line, since there are no official data regarding this line, the Company is unable to refer to developments in this line.

	Traditional management / "active management" (in NIS billion)		**Indices tracking management / "passive management" (in NIS billion)**	
	Traditional funds	**Money market funds [69]**	**Tracking funds**	**Indices products**
2010	135.5	17.0	3.4	57
2011	106.2	33.2	2.9	56
2012	125.6	34.8	9.4	68.9
% change in 2012 vs. 2011	Approx. 18.3%	Approx. 4.8%	Approx. 224%	Approx. 23%

As you may see from the data above, the trends that characterized 2012 are as follows:

A change in the public's preferences - 2012 was characterized with a change in the public's preferences. Looking at the entire 2012 shows that the public's shift to funds with a low risk profile has changed, as part of the change in the public's preferences that increased its assets' risk towards the end of the year, in light of the positive trend on domestic and global Stock Exchanges. This trend was reflected in money raisings in money market funds and tracking funds.

Increased competition - due to the increased competition, several investment houses collected "negative management fees" in certain traditional funds managed by them, i.e. management fees that are lower than the distribution commissions paid in respect of the funds. As of the end of 2012, in respect of approx. 17% of the mutual funds line's assets no management fees are paid at all, or management fees that are lower than the distribution commission or equal to it are paid.

The competition between tracking funds and indices products - in 2012 investment houses continued to deploy towards the passive market regulation reform, as a result of which, the tracking funds will become ETFs and will be able to compete in a better way with index products[70], such that now all investment houses managing index products (in fact, all large investment houses) also manage tracking funds.

33.4.3 **Brokerage services line of business[71]**

The scope of brokerage activity is affected by the trading volume on the Stock Exchange and the volatility in the capital market. 2012 was characterized with price increases compared with 2011, however, there was a sharp decrease in trading volumes. In 2012 a trend of erosion in the profitability of the brokerage services extended by TASE members who are not banks, including Migdal Stock Exchange Services, due to several events, including the coming into effect of the Joint Investments Trust Law (Amendment No. 14) – 2010, the increased competition on behalf of banks in the area of trading services and the sharp decrease in trading volumes in Israel and worldwide. In 2012 there were mergers and acquisitions of

[69] Money market funds in NIS.
[70] For additional details regarding the reform in the line of index products and ETFs, see Clause 44.1.2 hereinafter.
[71] The data are based on the annual review of the Stock Exchange for 2010.

several investment houses in the line, including those of Meitav and DS[72], the sale of the TASE Member Harel, the sale of Clal Finance investment house's activity, including putting a TASE member from Clal Finance for sale[73].

Equity market

2012 started with price declines, TA-25 index decreased by approx. 4% in January-May 2012, following concerns that the crisis in Europe might expand. However, later on the trend was inverted due to actions taken by central banks worldwide, mainly the ECB and the Fed in the USA, which brought back optimism to the markets. In June-December 2012 TA-25 index increased by approx. 14%. In annual terms, the TA-25 index increased by approx. 9%, following a decline of approx. 18% in 2011. Price increases characterized most sectorial indices in 2012. TA-Finance Index and Yeter 50 Index increased by over 20% compared with 2011. Bluetech 50 index, that includes the large hi-tech and biomed companies, increased by approx. 16%, and on the other hand, TA-Communications index decreased by approx. 33%. Share trading was accompanied with low volumes and low capital raisings. The average daily volume totaled approx. NIS 1.1 billion in 2012, a 38% decline compared with the average daily volume in 2011. The reduction in volumes affected by geo-political developments in the Middle East and by the slowdown in the Israeli economy, following the crisis in the European economy and the slowdown in private consumption.

The bond market

On the bond market, unlike the equity market, in 2012 was an increase in the average daily trading volume, totaling approx. NIS 4.1 billion, exceeding that of 2011 by approx. 10%.

The trading in the bond market was characterized with price increases in 2012 in all bond indices (both government and corporate), mainly due to the low inflation and the cut in BoI interest rate during the year. The general government bond index increased by approx. 7.9% in 2012, following an increase of approx. 5% in 2011. Tel-Bond 60 index increased by approx. 8.5% in 2012, following a decrease of approx. 0.3% in 2011.

The scope of gross government raisings in 2012 totaled approx. NIS 82.3 billion, and was the highest in 20 years. The scope of net government also increased significantly due to an increase in the budget deficit, totaling approx. NIS 20 billion in 2012, compared with approx. NIS 3 billion in 2011.

Short term loans increased by approx. 2.6% by the end of 2012. The annual yield to maturity decreased and reached 1.8% by the end of 2012 vs. 2.6% by the end of 2011. The average trading volume in short term loans totaled approx. NIS 634 million, vs. approx. NIS 1.2 billion in 2010 and 2011. The public's holdings totaled approx. NIS 117.9 billon, compared with NIS 123.5 billion in the beginning of the year. Until November 2012, foreign residents sold short term loans in the amount of approx. USD 3.4 billion. Starting from March 2011 and up to November 2012, short term loans sales by foreign residents totaled the huge amount of approx. USD 12.7 billion, following the revocation of the exemption on tax for foreign residents' investments in short term loans as of July 2011.

[72] In May 2012 DS Apex Holdings Ltd. announced that it signed an agreement with Meitav Investments House Ltd.'s shareholders, pursuant to which DS Apex shall execute a merger by way of a share swap with Meitav's shareholders (via a tax-exempt merger as per its meaning in Clause 103 K to the Income Tax Ordinance (New Version) – 1961, such that DS Apex shall buy all of Meitav's share capital from Meitav's shareholders, against a share allocation in DS Apex to Meitav's shareholders.

[73] In January 2013 Clal Finance Ltd. announced its engagement (together with Clal Finance Batucha Investments Management Ltd.) in an agreement for selling all holdings in the investment portfolio activity and the mutual funds management activity to Harel Finances Investments Management Ltd. and Harel Finances Holdings Ltd.

Derivatives market

In 2012 the trade in options on TA-25 index was characterized with lower volumes. In 2012 approx. 234 thousand units were traded per day, approx. 34% less than 2011.

Trade volumes in index products

In the ETN market, there are currently 440 series – 266 ETNs on domestic and international share indices and 174 ETNs on bond and commodities indices. The public's holdings in all ETNs reached approx. NIS 58.3 billion in 2012, vs. approx. NIS 49.2 billion by the end of 2011. The average daily trade volume in ETNs constituted approx. 20% of the trade volumes in shares, vs. 14% of the volume of corporate bonds, vs. approx. 23% and approx. 18%, respectively, in 2011.

33.4.4 **Underwriting and investment banking**[74]

In 2012 the scope of share issuance, private allocations and option exercise was approx. NIS 3.4 billion only, vs. approx. NIS 5.5 billion in 2011 and approx. NIS 13 billion in 2010. About NIS 39 billion were raised in 113 issuances of companies' bonds, vs. approx. NIS 33 billion in 2011. Another approx. NIS 3.5 billion were raised in private bond allocations.

33.5 **Changes in the scope of activity of Capital Markets Group and its profits**

The revenues in the area of financial services mainly stem from management fees that are calculated as a rate of the scope of managed assets, from commissions in respect of brokerage services, underwriting and distribution commissions and securities gains/losses of independent investments (Nostro).

The scope of managed assets

Following is a specification of the development in the scope of assets managed by Capital Markets Group (in NIS million), for unrelated parties, with a breakdown between mutual funds, portfolio management and hedge funds, in 2010-2012:

	2012	**2011**	**2010**
Portfolio management(1)	5,110	4,258	5,333
Mutual funds(2)	18,712	15,350	14,215
Hedge funds	111[75]	115	123
Total	**23,933**	**19,723**	**19,671**

(1) The data refer to the scope of assets managed within the portfolio management line, net (excluding assets managed within the portfolio management held in mutual funds managed by Capital Markets Group, and excluding the asset management of mutual funds, provident funds and training funds managed by Capital Markets Group and/or the Group). As of January 1st, 2011, MCM Group extends investment management services to some of Migdal Makefet's provident funds (mainly those previously managed by Migdal Platinum). For details see Note (2) to Clause 11.2 above.

(2) Out of which about NIS 62.1 million were managed by external portfolio managers, who do not belong to Capital Markets Group, as of the end of 2012, vs. about NIS 104 million as of the end of 2011 and approx. NIS 364 million as of the end of 2010. On December 29th, 2011 Migdal Funds decided that in spite of the Appendix to the engagement agreement between the parties, the engagement between Migdal Funds and the external investment manager for the management of the funds' investment portfolios will not end, and Migdal Funds continues to negotiate with the external investment manager in order to sign an agreement in this regard.

[74] The data in this item are based on the Stock Exchange annual review for 2012.

[75] In addition to asset management as set forth above, the Group provided investment marketing services for hedge funds to various customers, and their scope of assets for these services totals NIS 7.2 million as of the end of 2012.

Revenues of the financial services area[76]

In 2012 there was a decrease in the scope of revenues of the financial services area. Total revenues in the financial services area in 2012 were approx. NIS 209 million, vs. approx. NIS 236 million in 2011 and vs. approx. NIS 309 million in 2010. Following is a specification of development in revenues of different segments comprising the financial services area between 2010-2012 (NIS million):

	2012	2011	2010
Revenues from old mutual funds management fees	143	166	185
Revenues from brokerage services (commissions)	40	51	62
Other revenues	5	5	1
Profits/losses from securities and finance expenses (net)	21	14	61
Total revenues of the area	209	236	309

In 2012 there was a decrease in the scope of revenues from the area, mainly due to a decrease in the scope of revenues in management fees in respect of the management of mutual funds and portfolios, mainly due to the reduction that was recorded in the average rate of management fees in mutual funds in 2012, compared with the average rate in 2011.

In addition, there was a decline in revenues from brokerage services following the coming into effect of Amendment No. 14 to the Joint Investments Trust Law, mentioned in Clause 43.1.3 (c) hereinafter, due to which Migdal Stock Exchange Services did not collect commissions on mutual funds managed by Migdal Trust Funds, which was reflected in a reduction in revenues from rendering brokerage services in 2012 compared with 2011. Furthermore, the decline in revenues was affected by a slowdown on global capital markets.

For details regarding income in the area of financial services, see Clause 1.3.5 to the BoD Report hereinafter.

33.6 **Developments in the markets of the area of activity and changes in the customers features**

For changes in the market share of players in the mutual funds line – see Clause 39 hereinafter. In lack of official publication, Capital Markets Group has no information about the share of the non-banking entities in the portfolio management line, brokerage and primary dealership, and underwriting and investment banking line[77].

33.7 **Alternatives to the financial services area's products and changes they are undergoing**

33.7.1 **Portfolio management and mutual funds**

The main alternative to the asset management services provided by the financial services area is self assets management, so that the customers decide how to manage their assets, usually through consulting bank investment advisors. The banking system saving plans and deposits serve as some alternative to the asset management services. Direct acquisition of securities and acquisition of ETNs on various indices (including on indices of securities overseas), constitute an alternative to mutual funds in general, and to tracking funds in particular. Until now, Capital Markets Group has not issued such ETNs, but at the beginning of 2008 it started managing tracking

[76] The data of revenues, expenses and income before tax including the results of activity of the financial services area performed MCM, as well as the activity of Arxcis Global Wealth Management Ltd., held by Mivtach Management and other revenues/expenses.

[77] The entities active in the financial services area are divided into two categories: banking and non-banking entities. Following the implementation of the Bachar Legislation, the banks, except U-Bank, ceased operating in the mutual funds management line.

funds, which are an alternative product to ETNs, and as of the end of 2012, it manages 22 tracking funds on various indices. Some of the structured products marketed in Israel are alternative products to mutual funds, or to investment in securities or in other financial derivatives. Capital Markets Group engages in marketing structured products, issued by third parties.

In addition to the above, there is certain changeability among some of the area's various products. Customers may purchase asset management services in the capital market both by receiving portfolio management services (tailor made services), and by acquiring units in mutual funds, such that mutual funds constitute some kind of alternative to the investment portfolio management services.

33.7.2 **Underwriting and investment banking**

Taking loans and credit from banks or other financial institutions, direct engagement with Israeli or foreign institutional organs, issuances without underwriting or capital raising through foreign Stock Exchanges constitute an alternative to the underwriting and distribution services granted by the underwriting and investment banking line.

33.8 **The structure of competition in the financial services area and changes it is undergoing**

The financial services area is characterized by harsh competition, inter alia due to the fact that the market is relatively small, and contains multiple competitors. In 2012, the trend of investment houses consolidation continued, decreasing the number of competitors in the various lines in the capital markets, inter alia because the fixed expenses that increase constantly due to the regulatory requirements in the various lines, and the erosion in management fees. For additional details see Clause 39 hereinafter.

34. The area’s main products and services

Following are the main services provided by Capital Markets Group:

Mutual funds management – in this framework, as of December 31st, 2012, Capital Markets Group manages 144 mutual funds, differing in their investments policy or their tax bracketing. Mutual funds enable investments in multiple various basic assets, while maintaining high liquidity. The mutual funds management activity is characterized by a distance between the customers and the funds manager, since most of the public investments in mutual funds are done through the banks.

Some of the mutual funds are managed via the investment management of a non-related external investment manager, who manages the investment portfolio of these funds in return for some of the management fees in their respect.

Following are additional details on mutual funds managed by Capital Markets Group, not via the investment management of the non-related external investment manager, as of December 31st, 2012 (in NIS millions)[78]:

[78] As per Bizportal system data for 31st, 2012.

Categories	Scope of assets of Capital Markets Group funds (NIS million)	Scope of assets of the categorized line funds (NIS million)	Capital Markets Group funds' average management fees in percentage	Categorized line funds' average management fees in percentage
Bonds in Israel – General	2,501	24,817	1.22%	1.17%
Bonds in Israel – Forex	26	392	1.42%	1.51%
Bonds in Israel - companies and convertible	1,743	21,213	1.00%	1.04%
Bonds in Israel – State	2,891	29,336	0.98%	0.94%
Bonds in Israel – NIS	2,356	31,616	0.66%	0.58%
Overseas bonds	88	5,416	1.15%	1.03%
Foreign funds of funds	2	2,315	0.40%	1.00%
Israeli funds of funds	-	244	-	0.00%
Elastic	13	911	2.92%	2.30%
Foreign general	-	63	-	0.40%
Money market fund – USD	28	955	0.31%	0.45%
Money market fund – NIS	3,317	34,795	0.15%	0.15%
Leveraged and strategic	338	925	3.05%	2.75%
Israeli shares	129	4,262	2.41%	2.69%
Foreign shares	197	2,982	2.87%	2.55%
Mixed	-	104	-	2.04%
Foreign residents	-	67	-	2.64%
Bond tracking	4,546	8,725	0.00%	0.07%
Share tracking	475	633	0.01%	0.02%
Total in 2012	**18,650**[79]	**169,771**	**0.63%**	**0.80%**
Total in 2011	**15,247**	**142,303**	**0.77%**	**0.90%**
Total in 2010	**13,851**	**156,609**	**1.19%**	**1.13%**

Investment portfolios management and investment marketing – in this framework the customers' assets are managed, or they are provided with investment marketing services, according to the investments policy agreed upon vis-à-vis the customers and customized to their needs, and pursuant to the provisions of the Practice Arrangement Law and the regulations thereof. The portfolio management and investment marketing activity is characterized by direct and personal contact with customers, who are mainly customers holding assets that exceed a certain minimum.

Brokerage services - in this framework there are execution services (inside and outside dealing) in securities and financial derivatives, traded in the Stock Exchange and in stock exchanges and regularized markets abroad, as well as custodian services for securities and financial derivatives. Sometimes credit is provided to customers for acquiring securities and making transactions in financial derivatives. Brokerage services are granted to customers who open an account for this purpose with Migdal Stock Exchange Services, through different ways: operating transaction rooms and trading rooms, providing e-trading platforms to customers in TASE and stock exchanges overseas, or providing online trading systems allowing direct access (FMR system). In order to provide brokerage services abroad, Migdal Stock Exchange Services has accounts with several foreign brokers. Migdal Stock Exchange Services also provides issuance and offering concentration services in offers for buy and sale. We note that some of the customers (usually institutional) receive execution services only, while custodian services are provided to those customers by banks / other TASE members.

[79] Also, Capital Markets Group manages mutual funds together with non-related external investment managers, whose scope of assets as of December 31st, 2012 totaled approx. NIS 62 million, see details in Note (2) to Clause 33.5 above.

Underwriting and investment banking services – services in the primary market - in this framework there are issuances of companies offering securities to the public in Israel as per a prospectus and private issuances of companies for institutional investors and other investors. The services provided under issuances for the public are divided into two main types: managing underwriters consortiums (alone or with others) while giving an underwriting liability or while giving only distribution services. In the last few years, most capital raisings were done through universal shelf registration statements, in a short, simple and relatively inexpensive procedure. In light of the above, in most capital raisings the underwriting companies served as distributors only, with no underwriting liability. The services provided under a private issuance are mostly similar to managing an issuance for the public, but private issuances are not usually accompanied with an underwriting liability.

Investment banking services – this framework includes, inter alia, capital raising, share distribution (Block Trade), off exchange dealing, initiative and assistance in M&As and financial advice.

35. Revenues and profitability breakdown of products and services

The financial services area does not include a set of products, whose revenues constitute 10% or more of the total Group's revenues.

36. New products

Capital Markets Group checks, on a regular basis, the development and issuance/distribution of new financial products, and regularly adjusts its products and services to customers' needs and market conditions.

37. Customers

The customers of the portfolio management and investment marketing line and brokerage services and primary dealership line - Capital Markets Group has a large number of scattered customers, divided into three main types:

37.1 **Private customers** – usually households whose scope of asset portfolio is relatively small.

37.2 **Eligible customers** - customers meeting the detailed criteria in the addition to the Regulation of investment advice, investment marketing and investment portfolio management Law (mainly training funds, provident funds, pension funds, local municipalities, authorities etc., whose scope of asset portfolios exceeds NIS 50 million). The scope of asset portfolios of these customers is usually relatively large, but on the other hand the level of management fees is competitive, since sometimes the engagement with them is the result of winning a competitive procedure.

37.3 Other external corporations and companies (that may not be defined as eligible customers) - usually public companies with equity that is lower than NIS 50 million, private companies etc. The scope of asset portfolios of these customers is usually relatively large (but usually lower than that of eligible customers), but on the other hand the level of management fees is competitive, since sometimes the engagement with them is the result of winning a competitive procedure.

The Group has no clear data as to the revenues distribution in this Clause.

We also note that Migdal Portfolio Management also manages the investment portfolios of eligible customers managed by Capital Markets Group and/or the Group (part of the mutual funds, provident funds and training funds managed by the Group).

The relative share of the customer types in the overall scope of the managed portfolios (excluding asset management of Capital Markets Group and/or the Group's managed mutual funds, provident funds and training funds, but including mutual funds managed by Capital Markets Group and held within the portfolio management branch under customers portfolios) by Capital Markets Group, as at December 31st, 2012, totaling approx. NIS 6,027 million[80], is approx.:

Type of customers	31.12.2012	31.12.2011
Eligible customers	46%	34%
Private customers	31%	32%
Companies and other corporations	23%	34%
Total	**100%**	**100%**

It should be mentioned that some of the customers receive from Capital Markets Group only portfolio management and investment marketing services, some are provided with brokerage services only (whether as independent customers or as customers whose account-based investments are managed by a portfolio manager [whether belonging to Capital Markets Group or not]), some receive only investment marketing services regarding hedge funds, and others receive various services simultaneously. We note that eligible customers usually receive execution services only from the brokerage services line, and the custodian services of securities and financial assets are provided to these customers by banks.

Capital Markets Group has many customers, and is not dependent on a single customer, or a small number of customers, whose loss will materially affect the financial services area.

Migdal Portfolio Management started expanding its activity in the area of investments portfolio management for customers whose accounts are managed in banks abroad. Capital Markets Group considers this as another source for expanding its activity and revenues.

Apart from the related eligible customers, as aforementioned, Capital Markets Group has one customer, who is a non-related eligible customer, whose scope of managed portfolio exceeds 10% of the overall scope of portfolios managed (excluding asset management of Capital Markets Group and/or the Group's managed mutual funds, provident funds and training funds) by Capital Markets Group (13%). However, Capital Markets Group has no customer from whom the Group's revenues constitute 10% or more of the total Revenues of the financial services area.

We note that the total revenues of Capital Markets Group from other areas of activity in the Group, in respect of brokerage and/or portfolio management activities provided to other areas of activity in the Group amounted to approx. NIS 10 million in 2012, and to approx. NIS 12 million in 2011.

Customers of the underwriting and investment banking line – Migdal Underwriting customers are mainly private and public companies that want to raise capital or issue their securities to the public, as well as interested parties in public companies. Migdal Underwriting relations with its customers are usually one-time relations. The underwriting and investment banking activities are not an ordinary or frequent event, not even in public companies, and usually require a relatively short process. The underwriting and investment banking line is not dependent on a single customer, or on few customers, whose loss would materially affect the area of financial services.

[80] Out of which about NIS 0.92 billion were invested in mutual funds units managed by Capital Markets Group.

38. Marketing and distribution

Capital Markets Group uses several marketing and distribution channels to distribute its products and services, the main of which are:

Marketing and distribution through banking corporations' investment advisors
This channel serves as the main channel for distributing mutual funds. Capital Markets Group's main activity in this channel is to inform investment advisors of its products and services, and provide them with the relevant information and marketing documentation. As of the date of this report, Migdal Funds engaged in distribution agreements with most of the banks. The distribution agreements state that the commission rate paid to those banks will be the maximum rate that the banks may collect from time to time as per the provisions of the Law. The distribution agreements with all banks are for an unlimited period or for a renewable period, whose termination is subject to prior notice of a few months.

Marketing and distribution (except regarding mutual funds) through a large number of different mediators, including referral by insurance agents, including agents working with the Group's Customer Division.
This channel is the main channel for the distribution of portfolio management and brokerage services of Capital Markets Group. With respect to customers that are referred to receive portfolio management services, Capital Markets Group is accustomed to pay these mediators commissions at a certain rate out of the management fees collected from the referred customers, and in some cases a one-time payment out of the scope of assets deposited by the referred customers, followed by commissions at a lower rate out of the management fees collected from the referred customers. As to customers referred to brokerage services, Capital Markets Group usually pays these mediators some of the commissions it collects, and sometimes a one-time payment in respect of each referred customer.

Direct approach to customers through Capital Markets Group employees, among other things, through taking part in tenders published by them, and initiated approach to public companies regarding the primary dealership and underwriting and investment banking lines.

Holding professional/marketing conventions.

TV, press and Internet-related advertising.

Capital Markets Group has no exclusivity agreements with any of the abovementioned marketing and distribution channels.

39. Competition

The factors which lead to competition in the area of financial services are the achieved yield (in relation to the risk level), the rate of management fees, the commissions' rate in respect of the different services and the quality of service.

39.1 Mutual funds management services[81]

According to data published by the Bizportal system, as of the end of 2012, 21 companies for mutual funds management operate in Israel, similar to their number in 2011. All in all, these companies manage together about 1,275 mutual funds. Among the mutual funds management companies, 8 manage assets exceeding NIS 10 billion, another 7 companies manage assets exceeding NIS 1 billion, and another 6 companies manage assets exceeding NIS 0.5 billion. In 2012 the scope of funds' assets in Israel increased from NIS 142.3 billion by the end of 2011 to NIS 169.8 billion by the end of 2012, out of which about NIS 34.8 billion in money market funds (NIS) and NIS 9.4 billion in tracking funds.

[81] As per data of Bizportal as for December 31st, 2012.

By the end of 2012, Migdal Funds is the fourth largest managing company as far as AuM are concerned, with about NIS 18.71 billion in managed assets (vs. approx. NIS 15.35 billion by the end of 2011)[82], and a market share of about 11% vs. 10.8% by the end of 2011. It should be noted that in the line of tracking funds, Migdal Funds is the largest company, and its market share is approx. 53.7%.
[83]:

Herewith are the main competitors in the mutual funds line [66]	Data as of the end of 2012	Data as of the end of 2011	Data as of the end of 2010
Name of competitor	**Market share**		
Psagot	16.8%	17.6%	18.4%
Harel-Pia	11.5%	12.0%	13.3%
Meitav	11.2%	11.8%	7.8%
Migdal Funds	11.0%	10.8%	9.1%
Excellence	11.0%	12.9%	12.5%
Altshuler Shaham	7.7%	3.2%	3.7%
DS	6.2%	6.9%	6.8%
Clal Finance	6.1%	6.2%	6.0%
IBI	4.8%	6.9%	7.3%

39.2 **Investment portfolio management and investment marketing services**

There are many portfolio managers in the portfolio management and investment marketing line. In lack of official publication, the Group cannot estimate the scope of portfolio assets managed by portfolio managers in Israel. As mentioned above, the scope of the net portfolio assets[84] managed by Capital Markets Group as of December 31st, 2012 is approx. NIS 5,110 million, and the gross[85] scope of assets is approx. 16,810 million. In addition to the above mentioned asset management, Capital Markets Group provides investment marketing services for hedge funds to various customers, whose scope of assets for these services totals NIS 7.2 million as of the end of 2012.

The names of Capital Markets Group's main competitors, to the best knowledge of the Group, regarding investment portfolio management and investment marketing services are Psagot Securities Ltd., Peilim Portfolio Management Company Ltd., Tachlit Investment House Ltd., Etgar Investment Portfolio Management Co. of the Mizrachi Tefahot Group Ltd., Altshuler-Shaham Ltd., Israel Brokerage & Investments (IBI) Ltd., Analyst Stock Exchange & Trading Services Ltd., Clal Finance Batucha Investment Management Ltd., Excellence Nessuah Investment Management Ltd. and Meitav Investment Management Ltd.

[82] In addition, Capital Markets Group manages mutual funds in a cooperation with external non-related investment managers, whose scope of assets was approx. NIS 104 million as of December 31st, 2011. For details see Note (2) to Clause 34.4.4 above.

[83] As per Kranot Meda Zahav and Bizportal data for 2010-2012. The data include market share stemming from funds managed by external non-related investment managers and money market funds.

[84] Excluding assets managed under the line of portfolio management held in the mutual funds managed by Capital Markets Group, and excluding asset management of mutual funds, provident funds and training funds managed by Capital Markets Group and/or the Group.

[85] Including assets managed under the line of portfolio management held in the mutual funds managed by Capital Markets Group, and including asset management of mutual funds, provident funds and training funds managed by Capital Markets Group and/or the Group.

39.3 **Brokerage services**

The Stock Exchange is comprised of 15 members which are banks and 14 members which are not banks[86].

According to the trading data published by the Stock Exchange, the average daily trading volume in stocks and convertibles, inside and outside the Stock Exchange dealing, in 2012, was approx. 1.1 billion, out of which Migdal Stock Exchange Services executed about 1.9%. At the end of 2012, Migdal Stock Exchange Services is rated 15th among the TASE members (banks included) as to stock and convertibles trading.

According to the trading data published by the Stock Exchange, the average daily trading volume in bonds, inside and outside the Stock Exchange dealing, in 2012, was approx. NIS 4.1 billion, out of which Migdal Stock Exchange Services executed about 1.5%. At the end of 2012, Migdal Stock Exchange Services is rated 14th among the TASE members (banks included) as to bonds trading.

According to the trading data published by the Stock Exchange, the average daily trading volume in short term loans (STL), inside and outside the Stock Exchange dealing, in 2012, was approx. NIS 0.6 billion, out of which Migdal Stock Exchange Services executed about 5.4%. At the end of 2012, Migdal Stock Exchange Services is rated 7th among the TASE members (banks included) as to short term loans trading.

According to the trading data published by the Stock Exchange, the average daily trading volume in options on TA-25 index, in 2012, was approx. 234 thousand units, out of which Migdal Stock Exchange Services executed about 3.41%. At the end of 2012, Stock Exchange Services is rated 7th among the TASE members (banks included) as to trading volume in options on TA-25 index.

According to the trading data published by the Stock Exchange, the average daily trading turnover in USD options, was approx. 35 thousand units, out of which Migdal Stock Exchange Services executed about 8.62%. At the end of 2012, Migdal Stock Exchange Services is rated 4th among the TASE members (banks included) as to trading volume in USD options.

The names of Capital Markets Group's main competitors, to the best knowledge of the Company, regarding brokerage services are as follows: members of the Stock Exchange that are Israeli banks, foreign banks and investment houses (Citibank, HSBC, Merrill Lynch, Barclays Bank PLC, Deutsche Bank and UBS), as well as non-banking TASE members (Poalim Sahar Ltd., Israel Brokerage & Investments (IBI) Ltd., Clal Finance Batucha Investment Management Ltd., Meitav Trade Stock Exchange Ltd., Excellence Nessuah Stock Exchange Services Ltd., Psagot Securities Ltd., DS Investment House Ltd., Analyst Exchange and Trading Services Ltd., Citigroup Financial Products Israel Ltd., E-Broker Trading and Securities Ltd.).

In light of the significant increase in the banking system's activity in the area of securities trading, originating, inter alia, from a deviation in institutional customers' brokerage activity towards the banking system, along with a reduction in the commission figures on its behalf and in light of the coming into effect of the Duty for Mandatory Tenders in Funds (see Clause 43.1.3 (c) hereinafter), there was a marked deterioration in the ability to compete for TASE members that are not banks compared with the banking system in the area of brokerage services.

[86] Including 7 international entities - HSBC, Barclays Bank PLC, Citibank, Citigroup, UBS, Deutsche Bank and Merrill Lynch (which is a remote member).

39.4 **Underwriting and investment banking services**

In 2012 there was a mixed trend in the issuance market in Israel – in 2012 there were no IPOs, vs. IPOs of 8 companies in 2011, however the scope of raisings of bonds increased compared with its scope in 2011.

In 2012 Migdal Underwriting was the distributor of 21 public offerings and did not serve as an underwriter.

The names of Capital Markets Group's main competitors, to the best knowledge of the Company, regarding underwriting and investment banking services are as follows: Clal Finance Underwriting Ltd., Leumi Partners Underwriters Ltd., Menorah Mivtachim Underwriters and Management Ltd., Poalim IBI – Underwriting and Issuances Ltd., Apex Underwriting & Issue Management Ltd., Excellence Nessuah Underwriting (1993) Ltd., Rosario Underwriting Services (A.S.) Ltd., Meitav Issuances and Finances Ltd., Leader Issuances (1993) Ltd. and Brak Capital Underwriting Ltd.

39.5 **The main methods used by Capital Markets Group to handle competition, in all the financial services area lines are as follows:**

Striving towards high yields (relative to risk level) in assets management.

Increasing awareness to the performances and quality of Capital Markets Group's products, mainly among banks' investment advisors, who are the main marketing and distribution channel of the mutual funds.

Adjusting and diversifying the product basket offered to customers according to their needs and market conditions, including regarding foreign asset management.

Developing new products.

Advertising.

Using the Group's goodwill.

Using insurance agents who work with the Group as a source for customers’ referral.

Improving the customer services quality.

Competitiveness in the brokerage services line commission rate.

Maintaining current professional relations with institutional investors in Israel, who are the main target audience for the acquisition of securities, structured products and hedge funds.

Professionalism and high reliability.

40. Seasonality

The Company estimates that the financial services area, as a whole, is not characterized by seasonality.

41. Suppliers and service providers

Following is the Capital Markets Group's acquisition rate from its main suppliers relative to a share out of its overall expenses (which are not wages costs):

Supplier	Rate (in percentage)
F.M.R. Computers and Software Ltd.	Approx. 3.9%

Agreement to receive software services from F.M.R. Computers and Software Ltd. ("**FMR**") – Capital Markets Group is engaged with FMR in an agreement, according to which FMR provides Migdal Stock Exchange Services with the software, through which Migdal Stock Exchange Services instructs the Stock Exchange to execute securities and financial derivatives-related actions, and manages its Back Office array. In addition, FMR provides Migdal Funds with software for monitoring and revaluating its funds. Capital Markets Group is dependent on FMR, since replacement of the latter without prior deployment may materially harm its activity. Between Capital Markets Group and FMR there are negotiations regarding signing a new agreement, which will substitute the existing agreement for receiving software services. FMR claims that the existing agreement was cancelled by it in a notice that it submitted prior to the date of automatic renewal that was September 30th, 2012, however, Capital Markets Group disagrees. In practice, FMR continues to provide the services to companies in Capital Markets Group, pursuant to the existing agreement, and a new agreement has not been signed yet. We note that most of the non-bank TASE members and even some of the banks operate through the FMR software.

As to payments to the various distribution channels used by Capital Markets Group – see Clause 38 above.

42. Working capital

Customers' credit: Migdal Stock Exchange Services provides credit to its customers in order to acquire securities and financial derivatives. The scope of credit is limited according to the formula set in the Stock Exchange instructions, and calculated according to the different types of securities in the customer's portfolio. To guarantee the credit, different collaterals are given based on the Stock Exchange instructions. In 2012, the average NIS customer credit scope amounted to approx. NIS 43 million, and the average various Forex customer credit scope amounted to approx. NIS 27 million. It should be noted that the above credit is given to customers on a daily basis, and bears commercial interest.

Suppliers' credit: in 2012, the average suppliers credit scope was not material.

43. Restrictions and supervision applied to the financial services area

43.1 **Main laws and regulations** - hereunder is a summary of the legal provisions and arrangements that significantly affect this area of activity, changes that occurred during the reported period and new legal provisions that were legislated and/or published during the reported period:

43.1.1 **General**

(a) **Supervision and enforcement:** within the legislation of the Streamlining of ISA Enforcement Procedures Law (Legislative Amendments) - 2010 ("**Administrative Enforcement Law**"), starting from 2011 the entities supervised by the ISA are subject to the rules of supervision and administrative enforcement, along with the civil and penal enforcement. The Administrative enforcement Law is implemented in the various rules that apply to the entities supervised by the ISA, including fund managers, portfolio managers, underwriters, and regarding the trading in securities – also to TASE members, and expanded to a large extent the ISA's enforcement powers towards these entities. It should note that all the companies in Capital Markets Group that are supervised by the ISA as set forth above, adopted an internal enforcement plan as per the criteria published by the ISA in this matter by virtue of the Administrative enforcement Law.

Corporate governance: large portfolio management companies (with assets in the scope of at least NIS 5 billion or with over 1,000 customers), such as Migdal Portfolio Management and fund managers are subject to the rules of corporate governance set forth in the Law of Investment Regulation and the Joint Investments Law, as amended in 2011 within the Corporate Governance Law for Funds Managers and Portfolio Managers (Legislative Amendments) – 2011. These rules regulate, inter alia, the roles of the BoD and the Committees next to it, the duty to appoint an Audit Committee and its roles, the appointment of External Directors, provisions regarding the internal control and internal enforcement, risk management etc.

(b) **Reliability of supervised institutions** – In the **Administrative Enforcement Law**, the ISA was empowered to make decisions related to the reliability of the institutions supervised by it, such as revoking the permit, based on a list of circumstances that allegedly indicate a flaw in reliability. The list as mentioned above was published in November 2011.

43.1.2 **Mutual funds management**

(a) **The Joint Investments Trust Law- 1994 and the regulations and the Securities Authority's circulars by its virtue**

This Law and the Regulations and Circulars by its virtue regulate the licensing, the duties imposed on the fund manager as to the managed fund, corporate governance rules that apply to him, the way mutual funds should be established and managed, the assets that may be purchased and held and their rates, regulating the supervising and enforcement powers of the ISA, including administrative enforcement, towards the fund manager and fund trustee. Inter alia, the Laws sets forth the conditions and restrictions for receiving a control permit in a fund manager, equity and insurance demands and restriction of the market share which he may reach in case of buying mutual funds to 20%. Also, there are provisions regarding funds' classification for advertising purposes, the maximum distribution commissions that the fund manager may pay to distributors, etc.

On March 11th, 2013 an amendment to the Distribution Commissions Regulations was approved, within the Bill for **Joint Investments Trust Law (Distribution Commissions) (Amendment) – 2012.** Pursuant to the Amendment, the distribution commissions that distributors may collect from a fund manager will be reduced, and during six months fund managers undertook to reduce the fund managers' salaries accordingly, such that in this period the reduction in distribution commissions shall be "rolled" in favor of the unit holders. In addition, in order to ensure that the reduction shall continue to be "rolled" in favor of unit holders after this period as well, the ISA intends to introduce an amendment that would allow it to supervise the fund manager's salary within the Bill for Joint Investments Trust Law (Amendment No. 21) – 2012 and the Bill for Joint Investments Trust Law (Fund Manager's Salary) (Temporary Order) – 2012, which have not been approved yet.

(b) As of January 1st, 2013, pursuant to the **Banking Rules (Service to Customers) (Commissions) (Amendment) – 2012**, it will be impossible to collect securities deposit management fees for money market funds, in order to improve this product's attractiveness.

(c) In August 2012 the ISA published a **Circular regarding the Payment of Reduced Management fees for ETNs held in a fund**. Pursuant to the Circular, Migdal Funds engaged in an agreement with ETN managers, pursuant to which the management fees rate after discount shall not exceed 0.1% of the fair value of ETN held in a fund.

(d) In March 2012 the funds shifted, inter alia, to T+1 (instead of T) clearance. Because of this change, money market funds cleared at

T+1 became inferior to bank deposits that are cleared at T. For additional details, see Clause 43.1.3 (b) hereinafter.

(e) Planned amendments in the regulation that applies to fund managers

(1) In September 2012 the ISA published a **road map**: the objectives of the ISA and its plans for upcoming years. In this framework, the ISA is considering introducing several reliefs in the area of joint investments in trusteeship. According to the Company, these reliefs, should they be approved, are not expected to bring a significant relief to its activity.

(2) In May 2010 the Bill for **Joint Investments Trust Law (Amendment No. 15) – 2010** was published. The amendment includes changes in various clauses, including the possibility to collect differential management fees in the fund according to pre-set criteria, a limit on discounts according to pre-set criteria, etc.

43.1.3 **Brokerage services**

(a) **TASE supervision** – TASE members who are not banks, such as Migdal Stock Exchange Services, are subject to the supervision of the TASE pursuant to **TASE Articles of Association Provisions**. The TASE Articles of Association, rules and regulations, including by-laws of the TASE clearing house and by-laws of the Maof clearing house regulate the recording of different securities for trading, the trading forms in the TASE, the TASE membership, including qualification and members' admission procedures and the TASE's supervision over them, equity required from TASE members who are not banks, areas of activity allowed to TASE members, TASE members' duties towards the TASE and its other members, including certain reporting duties on TASE members that apply to public companies, including certain reporting duties that apply to public companies, the duties of TASE members towards their customers, etc. In this framework, TASE members must meet the requirements and standards set forth in the TASE Articles of Association, its instructions and rules regarding the existence of certain computerization systems, credit control systems, risk management, compliance etc.

Pursuant to the amendment of the TASE's Articles of Association that came into effect on June 30th, 2011, a new model for capital adequacy and liquidity for TASE members who are not banks was applied, and as per Migdal Stock Exchange Services's estimate at the time, it was supposed to bring about a significant increase in equity requirements. However, following the decline in trading volumes on the TASE and the gradual exit of mutual funds from brokerage activity within Migdal Stock Exchange Services, and also due to changes that were introduced later on by the TASE in the calculation of capital as per the above mentioned model, as of the date of the report, the increase in the minimal capital requirements that applies to Migdal Stock Exchange Services as a result of the new model was not as significant as previously estimated. As of December 31st, 2012 and as of the date of this report, Migdal Stock Exchange Services fully complies with the capital adequacy and liquidity requirements as per the new model, as set forth in the TASE Articles of Association.

(b) **The transfer of securities to clearance at T+1 and the transfer of mutual funds to clearance at T+1:** In March 2012 all the securities cleared in the TASE clearing house and all the units in mutual funds started being cleared at T+1 (instead of T). Options and future contracts cleared in the Maof clearing house will continue to be cleared at T. As a result of the change in the clearing rules, all these transactions in securities became outstanding transactions until their actual clearance. The change in the clearing rules imposed high handling fees on Migdal stock Exchange Services and/or its customers. Furthermore, the above mentioned change brought about an inferiority of money market funds cleared at T+1 compared with bank deposits cleared at T.

(c) **Restrictions on the scopes of commissions from related parties** – by virtue of the regulation that applies to institutional organs and fund managers, there is a restriction on the scope of commissions that these organs may pay from the assets managed by them, to a TASE member who is not a bank that is a related party, for brokerage services. Pursuant to these restrictions, commissions exceeding 20% of total commissions paid by the institutional organ or the fund during the year shall not be paid to TASE members that are a related party to these organs. Also, commission payment will be subject to the existence of a competitive procedure or a tender. Regarding institutional organs, these restrictions are regulated in the **Supervision of Financial Services Regulations (Provident Funds) (Buying and Selling Securities) – 2009**. Regarding fund managers, these restrictions are set forth in the amendment to **Joint Investments Trust Law (Amendment No. 14) – 2010 ("the Law of the Duty of Tenders in Funds")** as well as **the Joint Investments Trust Law (Holding Tenders and Examining the Relation of Trading Companies with Fund Managers)** – **2011**, that came into effect in December 2011. The coming into effect of the Duty to Hold Tenders in Funds Law materially reduced the scope of revenues of Migdal Stock Exchange Services from mutual funds and its profitability. It should also be noted that Migdal Funds held a tender for the activity related to future contracts traded abroad, options on these contracts traded abroad, options on indices traded abroad and bonds issued by governments traded abroad, and within it it selected one of the banks in order to serve as a securities agent of the funds within this activity, which was previously performed by Migdal Stock Exchange Services.

(d) **Anti-Money Laundering Law – 2000**. TASE members must comply with the rules for anti-money laundering by virtue of this Law and the Orders by its virtue, and in this respect, they are supervised by the ISA. This regulation sets forth a duty to identify and know the customers for TASE members' customers, and a reporting duty regarding customers' unusual transactions. In May 2011 a new order by virtue of this law came into effect, getting the requirements from TASE members to what is common and accepted worldwide, regarding the prohibition on money laundering, including **Know Your Client** duty, classifying each customer depending on the money laundering risk level, the duty to set a policy for managing money laundering management, etc.

43.1.4 **Portfolio management and investment marketing services**

(a) **Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Law - 1995 (“the Regulation Law”)** – this Law and the regulations and provisions thereof regulate required licensing, the duties imposed on portfolio managers, including the duties of fiduciary and care, the eligibility requirements, equity and insurance, corporate governance rules in large portfolio management companies, disclosure provisions regarding the portfolio managers' affiliation to institutional organs and financial assets, special consent provisions required from customers in the execution of transactions within the management of their investment portfolios, submitting periodic reports to customers, how to check customers' needs and instructions and the adjustment of services to these needs upon the beginning of the engagement, as well as in an initiated matter once a year, publishing and presenting yields, submitting reports to the ISA and regulating its supervision authorities including administrative enforcement, etc. and instructions, etc. The Law includes reliefs, including an exemption from the licensing duty, regarding providing services to eligible customers (such as supervised entities and companies with minimal required equity, as well as individuals who meet certain conditions). Within this regulation, lately two significant amendments came into effect: (1) In December 2012 **the Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Regulations (Reports) – 2012,** came into effect, setting unified rules for the presentation of information in periodic reports to customers. This Amendment required portfolio managers to execute an operational and computerization deployment in adjusting the reports to customers to the ISA's requirements. (2) In January 2013 there was a material increase in the fees that will be paid by the portfolio management company, within the Amendment to the **Regulation of Investment Advice, Investment Marketing and Investment Portfolio Management Regulations (Requests for Licenses, Tests, specialization and Fees) – 2012**. This Amendment shall increase the amount of Migdal Portfolio Management's expenses by a few hundred thousand NIS. It should be noted that during June 2012, the Knesset's Finance Committee approved a temporary order reducing the fees amounts for 2012-2016 by between 20% and 40% compared with the original updated fees amounts for these years.

(b) **Anti-Money Laundering Law – 2000**. This Law and the Orders by its virtue, regulate the duty to identify and know the customers for portfolio managers' customers, similar to the regulation that applies to TASE members in this regards. For details see Clause 43.1.3 (d) above.

(c) **Planned amendments in the regulation that applies to portfolio managers:**
As set forth in Clause 43.1.2 (e) (1) above, in September 2012 the ISA published a **road map: ISA objectives and plans for upcoming years**. In this framework, the ISA is considering introducing several reliefs in the area of portfolio management. These are only restricted reliefs that would apply mainly to small portfolio managers, therefore the Company does not expect these reliefs to bring a significant relief to its activity, if approved.

43.1.5 **Underwriting services**

(a) **The Securities Regulations (underwriting)** – **2007 – these Regulations** regulate the eligibility demands, new recording rules with the Israel Securities Authority, the duty to make deposits in trusteeship in the name of an attorney or CPA, insurance subsistence duty, exceptions to underwriters' activity, including restrictions on the possibility to serve as a pricing underwriter in certain issuances, reliefs that would allow foreign underwriters to operate in Israel, and reporting duties.

(b) **Restrictions on the scopes of commissions from related parties** – there are restrictions regarding the scope of acquisition by institutional organs in an issuance, in which a related party serves as an underwriter or as a distributor. These restrictions are set forth in the **Supervision of Financial Services Regulations (the Way Securities are Offered to the Public) – 2007** – that include restrictions on the scopes of sales by underwriters and distributors to institutional investors related to them, as well the **Supervision of Financial Services Regulations (Provident Funds) (Buying and Selling Securities) – 2009** – imposing restrictions on the quantity of securities that institutional investors related to underwriters and distributors may buy, within an issuance in which the related underwriters or distributors are involved. These restrictions limit the rate of sale or participation in an issuance up to 5% of the quantity sold in the offer or up to 10% - should the value of assets managed by all institutional organs that a related party to them is an underwriter or a distributor participating in the issuance or he sale exceeds NIS 10 billion, to institutional investors related to them.

(c) **Planned amendments in the regulation in the area of underwriting**:
In September 2011 the ISA published a **Bill for legislative amendments in the area of underwriting**, that includes a series of amendments, mainly, in a nutshell, as follows: changing the definition of the underwriter's identity similar to that in the USA, such that any entity participating in the distribution and marketing of the issuance constitutes an underwriter, therefore it is requested to bear liability over the issuance documents as an underwriter's liability. It was suggested to strengthen the underwriter's position as doorman by raising the benchmark of eligibility conditions required from underwriters, leaving investment houses under underwriting, using means of administrative enforcement extended to the ISA as per the current law, as well as reducing the scope of early liabilities that may be received before performing an issuance to the public. In addition, it was suggested setting a duty to publish the prospectus drafts signed by the underwriter, setting guidelines as to how to differentiate between the underwriter in an issuance and additional entities involved in its marketing and distribution that are not an underwriter in it, as well as updating the rules of conflict of interests in the activities of the underwriter and setting several additional disclosure duties. As per the estimate of Migdal Underwriting, if the recommendations in their current outline are approved, this will strengthen underwriters' position as an entity with a key role in the issuance process, it will increase the liability and legal risks stemming from it, increase the commissions required from issuing entities, will prolong the timetables for issuances, will strengthen the large underwriters and severely undermine small underwriters, as well as decrease the number of issuing companies and the number of issuances.

43.2 **Licenses and permits**
Following are the licenses and permits issued for the area of activity:

Migdal Stock Exchange Services – a member of the Stock Exchange, member of the Tel Aviv Stock Exchange Ltd. clearinghouse.

Migdal Portfolio Management – holds a portfolio management license.

Migdal Funds – serves as the manager of mutual funds in accordance with the Joint Investments Law, 1994.

Migdal Underwriting – registered in the underwriters’ register in accordance with the Securities Regulations (Underwriting) (Amendment) – 2007.

43.3 **Standardization and control** –Capital Markets Group's companies detailed above are committed to meet the requirements and standards set forth in the provisions of the regularizations and Supervision of Insurance Business that apply to them as set forth above, including the ISA and/or TASE instructions and provisions.

43.4 **Entry and exit barriers** – for entry and exit barriers see Clause 45.4 in Part E hereinafter.

Part E - Additional Information at the Entire Company Level

This part specifies issues which apply to all of the Group's areas of activity or to more than one area of activity, if not specified under the specific areas of activity.

44. Material changes in the economic surrounding and the effect of external factors on the activity

For a summarized description of trends, events and developments in the Group's macro-economic environment, which affect or are expected to affect the Group, see Clause 2 to the BoD Report.

45. Restrictions and supervision of the Corporation's activity, including entry and exit barriers

45.1 Regulation and supervision – general

As aforementioned in this report, the Group's activities in various areas is subject to multiple and unique regulation. The main laws and regulations applied to the Group will be described hereinafter, in addition to a description of the laws, regulations and Commissioner circulars, integrated in the Group's various areas of activity[87]. The body supervising the insurance businesses is the Commissioner of the Capital Markets, Insurance & Savings Division in the Ministry of Finance.

Furthermore, since the Company is a public company that issued securities to the public, it is subject to the Securities Laws provisions and is supervised by the ISA, as well as to the Companies Laws that apply to public companies.

The Group's activity in the area of financial services, via Migdal Capital Markets Group, is also subject to the Joint Investments Trust Law and the Regulations thereof and the supervision of the ISA. Regarding unique legislation in the area of financial services, see Clause 43 to Part C above.

45.2 Main laws and regulations

45.2.1 The Law of Supervision of Financial Services (Insurance) – 1981 ("The Supervision Law")

The Supervision Law states that the Commissioner of Capital Markets, Insurance & Savings in the Ministry of Finance shall be the Commissioner of Insurance, setting the Commissioner's roles and authorities, including authorizing the Commissioner to give instructions as to the operations and management of insurers and insurance agents, of their Senior Officers and everyone employed by them, in order to guarantee the proper management and interest securing of the insureds or customers, and avoid harming the insurer's ability to comply with its liabilities.

In accordance with the Supervision Law, the practice of insurance including insurance mediation, requires licensing, and the Supervision Law sets provisions as to the licensing of insurers and insurance agents, including their power to revoke licenses. Holding control means in the insurer and insurance agency requires permit granting, and the Supervision Law provisions include provisions as to receiving control and holding permits.

The provisions of the law also include prohibitions of "material holding" in the area of LTS, see Clause 9.4 in Part C above.

The Supervision Law includes various provisions as to the supervision of insurance businesses, inter alia, as to restrictions on business management, organs and position holders in the insurer, submission of

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reports, separation of life assurance businesses from other insurer businesses, including authorizing the Minister of Finance to set regulations in various issues associated with insurance supervision, such as equity, types of assets held by insurers and the way they are invested, the way reserves are calculated, setting insurance conditions for insurance plans and insurance fees etc., and provisions as to maintaining the stability of insurance companies, as well as provisions regarding securing the interests of insured's. The Commissioner may examine public complaints regarding insurers' actions regarding insurance matters. Should the Commissioner deem the complaint justified, he may instruct the correction of the flaw found in his examination.

The Supervision Law also includes provisions as to insurers' corporate governance. For more details in this matter, see also Clause 45.2.8 hereinafter.

The Supervision Law includes a series of provisions whose violation constitutes a criminal offense, and expands Senior Officers' liability to prevent offenses. Also, as to the Supervision Law, the Commissioner may impose penalties and civil penalties of significant sums without having to file an indictment. For the enforcement powers law that expanded the Commissioner's powers, see Clause 45.2.7 hereinafter.

(a) **Regulations issued by virtue of the Supervision Law.** By virtue of the Supervision Law, Regulations were set forth, dealing, inter alia, with the following matters: arrangements as to insurers' duty to hold insurance reserves as well as regulations setting forth the ways to calculate them and provisions as to ways of separating accounts and assets of life assurance businesses from the entire insurance businesses of an insurer, and separating the assets of profit participating life assurance businesses from those of other life assurance businesses, arrangements regarding capital requirements from insurance companies, including restrictions on dividend distribution (for details regarding capital requirements from insurers, see Note 7 e to the Financial Statements), arrangements regarding the approval of new insurance plans of various types, including their configuration, provisions regarding restrictions on the collection of additional insurance fees, extending benefits to insureds, currency homogeneity in insurance contracts, terms for linking policies, determining standard policies for certain types of insurance, provisions regarding premium reimbursements, provisions regarding travel insurance, provisions regarding management fees rates and their calculation, provisions regarding reporting to insureds, provisions referring to collective life assurance, and collective PHI insurance, etc. .

(b) **The third draft of the Supervision of Financial Services (Insurance) (Brokerage fees) Law - 2012** is pending. The draft is aimed at regulating the commission payment to insurance agents and inter alia, the following issues: the composition of the brokerage fees paid to insurance agents; restrictions as regards the ratio between commissions of different types paid to insurance agents; the payment of the brokerage fees to several licensees simultaneously and instructions as to the discontinuation of payment for insureds with whom contact was lost or undetected beneficiaries, commissions not due to compliance with sales objectives ("service commissions"), payment to the insurance agent that is not a direct money payment.

(c) For the main legislative arrangements referring to **corporate governance and ancillary arrangements**, see Clause 45.2.8 hereinafter.

(d) For the main legislative arrangements regarding the **management of institutional organ's investment management,** see Clause 45.2.9 hereinafter.

(e) For the main legislative arrangements regarding the **accounting policy, reporting and presentation rules and reports that should be submitted to the Commissioner,** see Clause 45.2.10 hereinafter.

(f) For the main legislative arrangements regarding **actuary, including reserve and risk management,** see Clause 45.2.11 hereinafter.

(g) For legislative arrangements regarding **products and regulatory changes in insurance, provident and pension products and the legislation of a regulatory codex,** see Clause 45.2.12 hereinafter.

45.2.2 **The Law of Supervision of Financial Services (Provident Funds) – 2005 ("Provident Funds Law")**

The Provident Funds Law was enacted as part of the Bachar Legislation, and has upgraded to the level of a law some of the various provisions formerly set forth in the Income Tax Regulations. The Law regulates the relationship between the member and the managing company, and the foundation of provident funds, their management and activity of the managing companies. The Law sets provisions as to the terms for permitting the licensing of the provident funds and managing companies, as well as provisions as to obtaining control and holding permits in managing companies. The Provident Funds Law applies some of the supervision provisions discussing holding control means in the insurer, also to holding control means in managing companies, including limits on "material holding" in the area of LTS.

The Provident Funds Law applies the supervision law provisions, discussing the appointment of organs and other position holders in the managing company, as described under Clause 45.2.1 hereinafter, and regulates the investment committee's activity, eligibility and functioning.

The Provident Funds Law also includes provisions as to the Commissioner's authority to give proper management instructions, similar to the Commissioner's authority to issue proper management instructions for an insurer, and similar provisions as to financial fines, civil penalties and penal offenses similar to the Supervision Law.

The Provident Funds law sets the employee's right to choose his own preferred insurance/pension-related arrangement, even if the agreement or law, state otherwise. An employer is prohibited from conditioning the money deposits in the provident fund selected by the employee, on choosing a certain fund or selecting one fund out of many on a list. At the same time, it was determined that provisions set in an agreement or in the law shall be used as default if the employee has not exercised his choice although he was given the chance to do so.

The Provident Funds Law also includes provisions regarding types of provident funds, terms of approval for provident funds, terms of payment for provident funds, terms of money withdrawal, provisions prohibiting the transfer, lien or foreclosure on beneficiary's rights in provident funds, the way monies and assets in provident funds are managed, provisions regarding payments that may be collected from provident funds' assets, provisions regarding merging and splitting of provident funds, and reports that should be submitted to insureds.

Some of the Provident Funds Law provisions also apply to insurance funds and insurers managing insurance funds, under the conditions set forth in the Provident Funds Law.

45.2.3 **Main regulations by virtue of the Provident Funds Law:**

(a) **Regulations of the Supervision of Financial Services (Provident Funds) (Money Transfer between Provident Funds) – 2008 ("Mobilization Regulations") –** these regulations regulate the transfer of pensionary products monies, and include provisions regarding the following: conditions for their transfer, restrictions to the transfer, timetables for transfers, the way money is transferred, transfer of the insurance liability, etc.

(b) **Regulations of the Supervision of Financial Services (Provident Funds) (Detection of Members and Beneficiaries) – 2012 ("Detection Regulations")**. These Regulations set forth the rules that institutional organs must comply with regarding the update of members' particulars, as well as the actions that institutional organs should take regarding the detection of members and beneficiaries with whom contact was lost. A circular dated February 2012, **Circular regarding the Procedure for Members and Beneficiaries Detection**, also regulates additional provisions related to the detection of members and beneficiaries. The Regulations regarding the detection of members and beneficiaries with whom contact was lost are effective as of January 1st, 2013, and there are temporary provisions regarding members / beneficiaries with whom contact was lost as of the effective date.

(c) **The Supervision of Financial Services Regulations (Provident Funds) (Management Fees) – 2012** – the Regulations set forth the maximum management fees in provident funds, including insurance funds, including management fees in accounts of members / beneficiaries with whom contact was lost. For details see Clause 9.2.8 in Part C above. The Regulations came into effect on January 1st, 2013.

(d) **The Supervision of Financial Services Regulations (Provident Funds) (Minimal Equity required from a Managing Company of Provident Funds or Pension Funds) - 2012** – the regulations set forth the minimal equity required from a managing company of provident funds or pension funds, and they set restrictions on dividend distribution. The Regulations came into effect in February 2012, and they also set forth temporary provisions regarding the enhancement of required capital. For details see Note 7 e to the Financial Statements.

(e) **Regulations of the Supervision of Financial Services (Provident Funds) (Distribution Commissions) – 2006** - these regulations set the maximal commission rates that will be paid to pensionary advisors, as well as that pensionary advisors will benefit from a uniform remuneration from all product manufacturers, while the terms of payment and service granted by the advisor to all manufacturers will be identical. The monthly distribution commission rate in respect of provident funds and pension funds in respect of executing a transaction, as well as in respect of continued membership in a fund shall not exceed 1/12 of 0.25% of the beneficiaries' accrued assets, except for beneficiaries accrued monies stemming from deposits made up to December 31st, 2005 – in which case the monthly commission rate shall not exceed 1/12 of 0.1%. Furthermore, the regulations also set distribution commission rates for monies accrued before that date, which were deposited in a provident fund that on the publication date of Bachar Legislation an organ that is not a banking corporation held a material holding in it and regarding monies deposited in provident funds controlled by a banking corporation. A draft for the amendment of these Regulations is pending, suggesting to regulate distribution fees also in respect of executing a transaction in insurance funds or insurance plans against death risk or PHI risk, included in the type of pensionary product as per its definition in the Advice Law. Also, it is suggested to set a unified maximum distribution commission for pensionary advisors in respect of transactions in all pensionary products set forth in the draft, that will be collected both from accrued assets and current deposits.

45.2.4 **Income Tax Regulations (Rules for the Approval and Management of Provident Funds) – 1964 ("Income Tax Regulations")**

The Income Tax Regulations regulated all the issues related with establishing, approving and managing provident funds, including regulating the licensing, equity and insurance of a managing company, the due payments to the provident funds, the tax benefits and tax rates, the use of provident fund monies, payments to beneficiaries, investing provident fund monies and restrictions as to investing monies in provident funds (including setting provisions regarding the appointment of investment committees and the duties imposed on managing companies as to provident fund management), provisions regarding the revaluation of their assets, the calculation of their profits and their distribution, management fees rates, provisions as to submitting reports to beneficiaries, submitting reports, the duty to have insurance, etc.

The Income Tax Regulations apply to pension funds, provident funds as well as insurance plans, which were approved as insurance funds (mainly managers' insurance).

Upon the legislation of the Provident Funds Law and the regulations by virtue of that Law, some of the provisions set forth in the Income tax Regulations were cancelled / amended / substituted, as the case may be.

45.2.5 **The Law of Supervision of Financial Services (Investment Advice and Investment Marketing) – 2005 ("the Marketing and Advice Law") and the regulations regulated by its virtue**

(a) The Marketing and Advice Law is a direct legislation of the Bachar Legislation, which regulates the practice of pensionary products advice and marketing, including setting provisions as to the duty of licensing and the terms, duties, prohibitions and restrictions applied to such practice, including provisions as to the practice of pensionary advice by banking corporations, provisions as to the supervision of a license holder, including the Commissioner's authority to issue provisions as to proper management and securing insureds businesses, provisions regarding the relations between the pensionary advisor/agent and the institutional organs, aiming at comparing relevant law provisions that apply to agents, to pensionary marketing agents and advisors as well, as well as well as provisions authorizing the Commissioner to impose civil fines and penalties, including penal sanctions.

The Marketing and Advice Law defined two practices requiring training and licensing – the advisor and the marketing agent – whose distinction is based on the existence of "affiliation", which is mainly receiving benefits regarding the execution of a transaction from the institutional organ or the belonging of a person to such organ (or he/she is an institutional organ). Bodies operating in the capital market are asked to choose between marketing and advice. However, a banking corporation and the bodies governing it or governed by it may only practice advice, except for exclusions that include, inter alia, structured products of the banking corporation which it is allowed to market. The practice of pensionary marketing was designated to institutional organs or pensionary insurance agents, who will receive a marketing license.

Duties of advisors and marketing agents – both the advisor and marketing agent of the pensionary product and the financial product were imposed general duties that include the fiduciary duty, the duty of care and the duty of adjusting the service to the customer, including adjusting the type of product to the customer out of all pensionary product types, after reviewing the customer's pensionary needs, composition of assets etc. The selection of the pensionary product makes a distinction. The advisor, including the banks, will be committed to give advice as to a variety of market-proposed relevant products, while the marketer may give advice as to products with which he is affiliated, and not as to the variety of market-proposed relevant products. The marketer is committed to inform his customers of the fact that he is a marketing agent and of the affiliation he has with the products he distributes. The advice process and product selection by the customer shall be accompanied by the appropriate documentation.

Marketing by institutional organs – the employees of institutional organs who market pensionary products will have to be "licensed marketing agents" (subject to various exemptions granted under the regulations from different exams, internship and other demands required to become a licensed marketing agent).

Various restrictions were also set for the engagement of a pensionary advisor with an employer, including prohibiting banking corporations from engaging with employers or employers association in order to give advice to employees.

By virtue of the Supervision Law provisions and the provisions of this law, regulations were set as to the licensing, training, internship and testing of insurance agents, pensionary advisors and pensionary marketers, including regulations as to exemption to advisors and marketers who practiced the pensionary area prior to the law publication.

(b) In July 2012, **the Bill of Law of Supervision of Financial Services (Advice, Marketing and Pensionary Clearing Systems) (Amendment No. 5) – 2012** was published, suggesting, inter alia, to set forth that employees who would like to conduct a transaction in a pensionary product may execute it via the license-holder of his/her choice; employers may not stipulate such a transaction by a certain license-holder and should not stipulate granting benefits to employees in the execution of a pensionary transaction by the license-holder.

(c) **The regulation of pensionary clearing house** – in March 2011 the Advice and Marketing Law was amended, to include a Chapter with provisions regarding the establishment and regulation of a central pensionary clearing house, regarding the control in such a company including its organs and position holders and equity, provisions regarding the usage of a pensionary clearing house, the way its operated and payments, provisions regarding information security and privacy.

By virtue of this Law, **Supervision of Financial Services Regulations (Advice, Marketing and Pensionary Clearing Systems (Information Security in a Central Pensionary Clearance System – 2012** were set, regarding provisions as to the issue of information security and keeping confidentiality regarding the pensionary clearing house operation.

45.2.6 **The Insurance Contract Law – 1981**

The Insurance Contract Law mainly regulates the relationship between the insurer and the insured (including the insurance agent's status), and sets various provisions regarding the main following issues: the essence of the insurance contract, the duty of disclosure and results of non-disclosure, the insurance period and the conditions for its cancellation or shortening, the status and rights of beneficiaries, provisions regarding the payments of insurance fees and their dates, provisions regarding changes in the insured risk, provisions regarding the way insurance monies are paid, including their limitation periods, different provisions which are specific to various types of insurance, such as life assurance, accident, disease and disability insurance, damage insurance, liability insurance etc.

45.2.7 **Arrangements related to enhancing enforcement authorities in institutional organs**

(a) **Law of Enforcement Enhancement on the Capital Market (legislative amendments) - 2011** (**"Enforcement Authorities Law**")

The Law of Enforcement Enhancement that was published in August 2011, significantly expands the Commissioner's enforcement authorities in the Law of Supervision of Financial Services (Insurance) - 1981, the Law of Supervision of Financial Services (Provident Funds) - 2005, and in the Law of Supervision of Financial Services (Advice, Marketing and Pensionary Clearing System) - 2005 (will be jointly referred to as "**the Supervision Laws**").

The Commissioner's search and investigation powers were expanded, and the powers regarding imposing a fine due to various breaches of the Law of Supervision were expanded.

In addition, the Enforcement Authorities Law also includes now the duty of the supervised corporation CEO or partner to supervise, and the lack of such supervision shall be considered as a constant breach of the aforementioned, and it will be possible to impose a fine as set forth except if there are satisfactory procedures for preventing breaches, including appointing a person on their behalf for the supervision and reasonable measures were taken for amending the breach and preventing its reoccurrence. Furthermore, it was set forth that insurers may not indemnify Senior Officers against a fine except due to payment to the breach's victim or reasonable expenses due to litigation regarding the fine, and even that, only when there is an appropriate provision regarding this matter in the Company's Articles of Association.

The provisions included in this Law may lead in the future to increasing measures of enforcement to be taken by the Commissioner towards the institutional organs supervised by him, and to an increase in the fines imposed by the Commissioner on institutional organs and insurance agents who violated his provisions.

(b) In July 2012 The Commissioner published a second draft to the **Compliance Risks Management in Institutional Organs Circular**, asking regulate the appointment of a compliance officer who would ensure the institutional organ's compliance with Law provisions, and the existence of an effective internal enforcement plan that would help the institutional organ's BoD and management comply with their responsibility and reduce exposure to compliance risks, and would be attributed to the institutional organs and managers' credit in the Commissioner's discretions in the Law implementation.

45.2.8 **Main provisions regarding the regulation of corporate governance of institutional organs and ancillary issues**

(a) **General**

The Bachar Law incorporated provisions to the Supervision Law, mainly regarding the regulation of insurers’ corporate governance, inter alia in the following issues:

(1) Some of the rules applied to organs, Senior Officers and control mechanisms in public companies, were expanded and also applied to insurers which are not public companies.

(2) Rules and appointment duties of actuary and risk manager were set, as well as appointing other position holders in the insurer, such as CEO, Director, internal auditor, and other Senior Officers set forth in the Commissioner instructions, which requires pre-approval by the Commissioner prior to the appointment. The Commissioner was also authorized to set rules as to the BoD slate, Investment Committees, eligibility of its members, ways of work and issues to be discussed in the Board and in its committees.

(3) The Commissioner’s supervision powers regarding the proper management of insurance companies and managing companies were expanded, and authorities or instructions formerly set forth by virtue of secondary legislation, were upgraded to level of legislation.

(b) **The Supervision Regulations of Financial Services (Insurance) (Board of Directors and its Committees), 2007 (“the Board of Directors Regulations”)** The BoD regulations focus on the BoD and its functioning, and inter alia, set rules as to the BoD slate, (at least one third of its members will only be external Directors and at least half of the external Directors should be professional experts [in the area of insurance] and at least half of the external Directors should be financial and accounting experts), the qualification of its members, rules to avoid conflict of interests, issues the BoD must discuss and decide on, attendance and quorum duty in its meetings, powers of the BoD committees, including exclusions to committees' delegation of powers, composition of the committees, including the Audit Committee, most of which will be composed of external Directors, and issues which must be raised in the Audit Committee. The BoD regulations include reliefs as to Directors of provident funds managing companies, which are not pension funds.

45.2.9 **Main provisions regarding investment management of institutional organs**

(a) **Supervision of Insurance Business Regulations (Ways for Investing Insurers' Capital and Funds and Liabilities Management - 2001 ("Regulations of Ways of Investment")**
The Regulations of Ways of Investment include, inter alia, pursuant to the amendments sets forth in the next paragraph, currently mainly regulate the provisions regarding the duty imposed on insurers to appoint two investment committees, one for managing the investment portfolio of the profit participating insurance, and the second for managing the Nostro investment portfolio, the slate of the committees, their roles and operation ways, restrictions on granting loans etc.

(b) In July 2012 the **Supervision of Financial Services Regulations (Provident Funds) (Rules of Investment Applying to Institutional Organs) - 2012 ("Investment Regulations")** came into effect, and the **Circular regarding Investment Rules Applying to Institutional Organs "(Investments Circular")** was published (the Investment Regulations and Investment Circular will be jointly referred to as "**New Investment Rules**") **.**

Pursuant to the new investment rules, as of that date unified investment rules shall apply to pensionary savings products (pension funds, provident funds, profit participating policies) and the current differentiation between the Investment rules for provident and pension funds' assets, and those that applied to the monies of profit participating policies, and some investment rules were changed.

The Investment Regulations empowered the Commissioner to set forth provisions regarding various issues. The Investment Circular sets forth additional provisions referring to the investment rules.

The New Investment Rules changed some of the existing investment rules, their scope is vast, and certain provisions were applied also to insurers' investments against non yield-dependent liabilities.

Inter alia, provisions regarding the control and holding means of control by insurers in other corporations, inter alia, it was determined that an insurer shall not control nor hold more than 20% of the means of control unless in the corporations detailed in the Regulations, which are (1) another insurer; (2) a managing company; (3) a corporation whose main occupation is holding real estate assets and their management; (4) corporate agent; (5) a corporation whose main occupation is investment management or extending credit for the insurer and for other institutional organs under its control (6) another type of corporation whose main occupation is related to the insurer's current activity. Investment in the types of corporations set forth in (5) and (6) above needs the Commissioner's approval in advance, there are provisions regarding required minimal equity against holding in such corporations.

The New Investment Rules also include temporary provisions that institutional organs should follow, pursuant to which , in order to adjust the slate of assets held by them to the new regulations detailed in the New Investment Rules, including regarding the continued holding of investments that were approved by the Commissioner before the publication of the New Investment Rules.

Migdal Insurance has investments and assets, regarding which, pursuant to the New Investment Rules, it may have to act pursuant to the temporary provisions. Inter alia, some investments may be gradually perceived as non-recognized assets, and accordingly, capital requirements may gradually increase up till January 1st, 2015 in an amount of approx. NIS 210 million, regarding this matter, see also Note 7 e to the Financial Statements.

(c) **Regulations of the Supervision of Financial Services (Provident Funds) (Asset Value Calculation) – 2009**

These regulations substitute part of the provisions of the Income Tax Regulations, and they are aimed at regulating the way the value of various assets managed by institutional organs should be calculated and the date upon which it should be calculated, and empower the Commissioner to set instructions regarding assets that are not negotiable securities.

The fair value of non-negotiable debt assets measured at fair value via profit and loss, as well as that non-negotiable financial debt assets that information regarding the fair value is given only for clarification needs only are determined via the capitalization of the estimate of cashflows expected in their respect. The interest rates that served for the capitalization are determined by a company that provides interest quotes regarding various risk ratings. For additional information regarding the calculation of fair value, see Note 12 f to the Financial Statements.

(d) **Regulations of the Supervision of Financial Services (Provident Funds) (Direct Expenditures due to the Execution of Transactions) – 2008**

These regulations regulate the types of direct expenditures that institutional organs may incur from the monies managed by it in respect of transactions in assets managed them, and these expenditures will not be included within the management fees collected from beneficiaries.

(e) **Control of Financial Services Regulations (Provident Funds) (Buying and Selling Securities) –2009**

These Regulations set forth, inter alia, conditions for the buying and selling of securities by institutional investors (the conduct of competitive procedures), as well as limits and conditions regarding the buying and selling of securities by institutional organs via their related parties.

(f) **Provisions referring to institutional organs' investment in non-governmental debentures (Hodak Committee)**

The Commissioner's Circulars regarding provisions referring to institutional organs' investment in non-governmental debentures (issued pursuant to Hodak Committee's final recommendations for determining parameters for institutional organs' reference, extending credit through non-governmental debenture purchases) set forth provisions that will apply over an institutional organ during the process of investing in non-government bonds.

45.2.10 **Main provisions regarding accounting policy, rules for reporting and presenting and reports that must be submitted to the Commissioner**

(a) **General**

The Supervision Law and regulations set by its virtue, inter alia, set provisions as to the accounting content, details and principles for preparing the insurance companies' Financial Statements, including the accounting aspect of handling insurers' assets and liabilities.

From time to time the Commissioner publishes Circulars and instructions related to the reporting rules for insurers and managing companies, and they are related to the accounting rules that should be implemented in insurers and managing companies' Financial Statements, including those related to international reporting standards, including those related to the required disclosure structure in Financial Statements.

Note 2 to the Group's Financial Statements includes the main accounting principles that serve the Group in preparing the Financial Statements.

(b) **Information as to embedded value (EV) in life assurance policies** - insurance companies operating in the life assurance line were forced to publish every year, together with the first quarter's Financial Statements, information regarding EV of long term life assurance policies (health insurance and life assurance) as of the end of the previous year. The EV report will be prepared according to the rules and instructions set forth in the report of the committee regarding EV publication appointed for that purpose and in accordance with the directives that the Commissioner issues from time to time. The Committee's rules and instructions are published in the MoF website.

45.2.11 **Actuary and risk management provisions, including provisions regarding Solvency II**

(a) **Rules for the execution of actuarial evaluations**

As part of the insurance activity, insurers are required to hold assets against liabilities.

The main actuarial rules, methods and assumptions, according to which the Group's insurance liabilities were set, are detailed in Notes 2 & 37 to the Financial Statements and in the actuary's statements in the lines of life assurance, health insurance and general insurance, attached to the Financial Statements.

From time to time, the Commissioner publishes circulars regarding instructions as to actuarial evaluation in life assurance, health insurance and general insurance, that regulate, inter alia, the scope of the actuarial evaluation to be conducted, including an increase in required provisions, the need to follow up on the reserve adequacy between life assurance policies that allow receiving annuities and completing them, the actuarial assumptions and the issues to be included in the actuarial report and statement, etc.

For provisions regarding the calculation of reserves in the area of insurance and LTS, as well as in the area of general insurance, published in the reported period, see Clause 9.2.9 (LTS) and Clause 25.4.9 (area of general insurance), to Part C above.

(b) **Duty of appointing an actuary and risk manager, their form of work and terms of eligibility**

The Supervision Law states that an insurer, including an insurer who is a managing company of a pension fund, must appoint an "appointed actuary" for each insurance line it practices, whose roles, among other things, are to advise the BoD and the CEO as to the extent of insurance liabilities of the insurer, or as to the actuarial balance of a pension fund managed by it, as relevant. In addition, the Supervision Law requires the appointment of a "risk manager" for each insurer and pension fund managed by it, whose roles, among other things, are to advise the BoD and the CEO as to risks faced by insurers and pension funds managed by them.

The Provident Funds Law applied the above provisions also to managing companies of provident funds, such that as of January 1st, 2010 it is mandatory to appoint a risk manager also in managing companies of provident funds.

The Commissioner published circulars setting rules as to the roles, authorities and forms of work of appointed actuaries and risk managers, and their relationship, including provisions regarding periodic reports that the risk manager should submit to CEO and the BoD and the yield-dependent Investment Committees in institutional organs. It was also set that in the event of institutional organs controlled by the same controlling shareholder, a joint risk management and control unit may be established for all these institutional organs, including yield independent liabilities of insurance companies, and appoint one risk manager for the group of institutional organs.

(c) **Deployment towards implementing the Solvency II provisions in insurers**

In July 2008, the Commissioner issued a circular regarding the deployment towards adopting the Solvency II provisions ("**the Directive**") alongside their application in EU countries. The directive constitutes a fundamental and comprehensive change of the regulation dealing with guaranteeing solvency and capital adequacy of insurance companies in EU countries, and is aimed at improving the protection of policyholders' monies.

The Directive includes a comprehensive examination of the risks to which insurance companies are exposed and setting standards to their management and measurement, while reflecting the risks embedded in their activity upon capital allocation. Furthermore, the directive also focuses on internal control and monitoring activities, as well as market discipline, disclosure and reporting.

Solvency II comprises of three key layers:

(1) Quantitative demands (mainly capital requirements) - evaluating liabilities towards insureds, assets held against liabilities and capital requirements in respect of exposure to insurance risks, market risks, credit risks and operational risks.

Two levels of required capital were set – Minimum Capital Requirement ("MCR") and Solvency Capital Requirement henceforth ("SCR"), representing different levels of supervision interference. Insurers may calculate the SCR based on a given standard formula or based on an internal model approved by the supervising authority.

(2) Qualitative demands - this layer concerns the supervision examination process focused on capital adequacy evaluation, as well as risk management framework and processes. Pursuant to this layer, supervisors may oblige insurers to allocate additional capital in respect of risks not taken into consideration in the first layer.

(3) Reporting and disclosure demands - increasing disclosure and requiring insurance companies to publish details about the risks to which they are exposed, their equity and the risk management framework they practice.

Pursuant to the circular, the requirements from each insurer:

- Appointing a team which will be responsible for implementing the Solvency II deployment, headed by a member of the Company management.

- Conducting a BoD discussion as to the Solvency II deployment: appointing a BoD committee which will be responsible for monitoring and controlling the deployment process, approving a multi-annual deployment plan towards implementing Solvency II (organizational and computerized), allocating resources for implementing the deployment.

- Reports on the progress of the deployment: to the BoD and the Commissioner, within the deadlines set forth in the Circular, including a disclosure in the BoD Report.

- Calculating the quantitative demands as per the quantitative evaluation survey (QIS4) provisions.

During the deployment period towards the implementation of the Directive, the Commissioner publishes Circulars regarding instructions for the calculation of capital requirements pursuant to the QIS4 model, that includes the quantification of the variety of insurances and financial insurances that insurance companies face, pursuant to the requirements set forth in the Commissioner circulars regarding this matter. Up until now, these instructions, including that of December 2012, described hereinafter, vary from one year to the other, and accordingly, the calculated results of capital requirements change as well.

In September 2012 the Commissioner published a letter regarding Israeli Solvency Governance, clarifying that due to the uncertainty regarding the timetables for the Directive implementation in Europe, the Commissioner suggests developing a risk-based solvency governance pursuant to the Directive and the promotion of a business culture that takes into account risk management discretions and capital allocation upon making decisions, that will rely of the principles of the Directive, with the necessary adjustments in Israel. In the letter, the Commissioner details the measures that he intends to take, including: Adjusting the regulatory framework to the Directive, based on the gaps that were mapped; a request for another submission of IQIS based on 2011 balance sheet data as per updated instructions for execution; a report regarding solvency as per IQIS will be conducted starting from mid-2013; the publication of the draft instruction for submitting ORSA report – (self evaluation of risks and solvency), submitting ORSA draft report to the Commissioner, after deliberating its findings in the BoD by the end of 2013. A final ORSA report will will be outlined by the end of 2014 and will be submitted to the Commissioner by insurers on an ongoing basis starting from 2015;

capital additions in case ORSA reports, IQIS results, corporate governance quality and risk management in the Company reveal the need to add them during 2015, pursuant to a methodology that will be published during 2014; in addition, a regulatory interference hierarchy will be institutionalized in case of a financial deterioration in the situation of an insurance company. Furthermore, after accruing the necessary experience in IQIS reporting results, new risk-based adequate capital requirements will be published and insurance companies will be required to have adequate equity.

In December 2012 the Commissioner published a Circular regarding Instructions for IQIS execution, pursuant to the letter published in September 2012, setting forth instructions for the execution of the IQIS survey by Israeli insurance companies, including clarifications and adjustments to the market characteristics and regulation in Israel. Pursuant to the Circular, insurers must submit to the Commissioner various reporting files as per the outline set forth in the Circular, and the Insurers' BoDs must deliberate the surveys' findings before submitting them to the Commissioner, as well as deadlines for submitting the reports to the Commissioner.

For additional details, regarding as to the Company's deployment towards the Directive implementation, see Clause 4.8 to the BoD Report, as well as Note 37 a 2 to the Financial Statements.

45.2.12 **Arrangements regarding change in regulation on products and future regulation codex**

(a) **Law memorandums for the change in regulation on products**

In September 2011 the Commissioner published the **Law Memorandum of Supervision of Financial Services (Insurance) (Amendment No.) - 2011 ("the Law of Supervision Insurance memorandum") and the Law Memorandum of Supervision of Financial Services (Provident Funds) (Amendment No…..) - 2011 ("the Law of Supervision (Provident Funds) memorandum") ("Law Memorandums regarding the Change in Regulation of Products")**

According to the memorandums, the Commissioner plans to change the supervisory regime over insurance plans and pension and provident Articles of Association ("**products**") and instead of supervising the products ahead of time, it is suggested to shift to a regime where a product must be notified before its marketing without having to wait for approval as condition to being marketed.

As complementary steps to the proposed change in the Commissioner's activity concerning products as described in the law memorandums for changing products' regulation, the Commissioner also published draft documents regarding the following:

(1) **Draft principles and guidelines for introducing an insurance plan.** The draft includes principles supported by elaborated illustrations, which, according to the Commissioner, an insurer should use when phrasing insurance plans, which refer to aspects of fairness and reasonability, and of disclosure and clarity. Insofar that the law memorandum draft concerning the change in the regulation of products is adopted, the Commissioner plans to check new and existing products according to the principles and guidelines set forth in the said draft.

(2) **Draft circular concerning an announcement of introducing insurance plans and provident funds' Articles of Association procedure** – the draft circular details the particulars and documents to be attached to the announcement about introducing an insurance plan, a collective insurance plan, a savings life

assurance plan, establishing a new provident fund and notifying any changes therein.

(3) **Draft actuarial appendix circular**. The draft defines the information required in the actuarial appendix attached to an insurance plan or Articles of Association of a paying annuity provident fund, based on the materiality of the plan to the company and a list of issues set forth in the draft, including how to update the Appendix.

The law memorandums concerning the change in the introduction of products, as well as the drafts concerning the principles and guidelines of the products and documents and information that must be submitted in this regard, should they be accepted, may impact the process of product launching in institutional organs. The company looks into the said drafts' provisions and cannot estimate the full scope of their impact, since, inter alia, there is no certainty as regards the final version of the applied provisions.

The information as regards the implementation and/or preparation of the company concerning the implementation of these provisions is future forecasting information based on drafts, while there is still uncertainty as to the final provisions and additional arrangements requested following the implementation of the planned steps.

(b) **Draft future regulation codex structure**
The aim of the draft codex is creating an updated and consistent regulative framework in all legislative layers that applies to institutional organs.

45.2.13 **Law for Protection of Wages – 1958**
The Law for the Protection of Wages protects employees in certain cases, when employers do not make provisions to provident funds as defined in the Income Tax Ordinance, including an insurance plan, which is acknowledged as a provident fund, including granting rights in certain cases where no such payments were received from the employer. Under the Provident Funds Law, the Law for the Protection of Wages was amended so that a penal offense was set, the penalty imposed on employers not transferring monies deducted from the employee's wages, has been increased, and Senior Officers in corporations were obligated to supervise and do their best to prevent such offense, a breach of which shall lead to penalty payment under the Penal Law.

45.2.14 **Arrangements regarding the Anti-Money Laundering Law**
The Anti-Money Laundering Law and the decrees by its virtue (mainly the anti-money laundering order (duties of identification, reporting and keeping records of insurers and insurance agents) – 2001 and the Anti- Money Laundering Order (duties of identification, reporting and keeping records of provident funds and companies managing provident funds) - 2001) ("Anti Money Laundering Order") – impose a duty on insurers, managing companies of provident funds and insurance agents, to record the particulars of service receivers in life assurance policies with a savings component, and provident funds, asking them to check and verify the identifying documents. In addition, they impose on insurance companies, managing companies and insurance agents, the duty of reporting the Authority of any specific activities, such as irregular activities perceived as suspicious activities. A draft amendment to the Anti-Money Laundering Order, published in July 2011, asking to expand the duties that will be imposed on institutional organs by virtue of that Law.

45.2.15 **Arrangements regarding the Protection of Privacy Law**

The Protection of Privacy Law – 1981 - this law includes provisions as to the protection of people's privacy, regulating, inter alia, the way a data repository should be registered, as well as provisions as to the duties of the data repository manager and its usages. From time to time, the Israeli Law, Information and Technology Authority (ILITA) publishes instructions regarding how to keep the information and the usage of personal information.

45.2.16 **The Class Actions Law – 2006 and Regulations thereof**

The law sets uniform rules for filing and managing class actions, and expands the option of filing a class action both in terms of corporations' standing and causes of claim, especially the expansion of being able to file class actions in the area of insurance. Considerations of the respondent's stability were explicitly set as one of the considerations for approving the class action. The Law also sets detailed arrangements as to leaving the claim and compromise option, and also instructs the foundation of a fund to finance class actions, the management of a class action registry etc.

Regulations set forth pursuant to the above mentioned Law set forth the law procedures for implementing Law provisions, and arrange the work procedures of the Fund for Financing Class Actions.

45.2.17 **Provisions regarding the Restrictive Trade Practices and Recommendation s of the Centralization Committee**

(a) In May 2012 the **Restrictive Trade Practices Law (Amendment No. 13) – 2012** was published. The Law deals with adding civil enforcement powers to the Israel Antitrust Authority, in addition to the current penal enforcement mechanisms.

(b) In July 2012, the Government published a **Bill for the Promotion of Competition and the Reduction of Centralization - 2012**. The Bill is a translation of the operative instructions of the conclusions of the Centralization Committee recommendation, which published its recommendations in February 2012. Part of the suggested amendments will be executed by a designated regulation, and part of them will be executed via amendments to the existing legislation, inter alia in the various supervision laws. Hereinafter the main issues of the Bill: considering all-economy centralization and sectorial competition discretions in right allocation, provisions as to limiting the control in companies in a pyramid-like structure, provisions regarding the separation of holdings in real and financial entities such as a prohibition on controlling and holding of a significant real entity and an entity controlling it, in a significant financial entity; there will be a prohibition on a simultaneous tenure of a Director in a significant real corporation and a significant financial entity; there will be a prohibition on a control by a controlling entity in a significant banking corporation in a significant financial entity that is not a banking corporation;

45.3 **Critical success factors**

45.3.1 **General success factors**

The following factors can be specified as the common success factors for all of the Group's various areas of activity:

Changes in the market, employment and capital market condition;

Regulatory demands, including control of tariffs;

Competition in the area;

Customer loyalty and portfolio persistency;

Quality of investment management, including the management of risks involved in all the Group's areas of activity;

Distribution channels, including their ability to increase demand and create new markets;

The variety of products and the ability to adjust them to market conditions and customer needs, including providing integrated solutions for the customers in respect of the Group's variety of products;

Quality of service to insureds, members and other customers, as well as agents;

Positioning the Company as a leading company in the life assurance and LTS area, while creating a brand that will enhance its competitive status;

Preservation and employment of high-quality human capital;

Computerization and technology level;

Operational efficiency and operational, marketing and sales expenses level;

Operation of efficient control and constant examination and improvement of working processes;

Robustness and stability.

45.3.2 **Success factors unique to the pension and insurance areas**

In addition to the aforementioned, the pension and insurance areas can be ascribed the following factors:

Level of the permitted management fees under the law, and the actually collected management fees;

Underwriting quality;

Actuary quality in pricing and reserves and their management;

Changes in life expectancy;

Frequency and severity of claims, including catastrophes;

Quality of claims management, including management of agreements with service providers and fraud control;

Protections and reinsurance cost;

Scope of tax benefits for customers (in the area of life assurance and LTS);

Technological and other developments in medicine including medical inflation;

Changes in the health basket.

45.4 **Entry and exit barriers**

45.4.1 **Entry barriers**

The main entry barriers of the Group’s various areas of activity are set by the provisions of the relevant laws which require obtaining licenses and permits.

(a) **Licenses and permits**

(1) **Insurance, pension funds and provident funds activity**

As per the Supervision Law, practicing insurance (including holding a pension fund managing company) requires the granting of an insurer license as per the Supervision Law ("**insurer license**"), holding of more than 5% of a certain type of control means in an insurer, which is conditioned on receiving a permit for holding control means from the Commissioner ("**holding permit**"), and control of an insurer or a corporation agent, which is also conditioned on a permit from the Commissioner ("**control permit**"). The management of provident funds also requires a license.

Among other considerations for granting an insurer or a corporation agent license, a holding permit and a control permit, the Commissioner takes into consideration a large variety of considerations, including presenting the action plans of the applicant, accommodating Senior Officers to their positions, the financial means, the experience and business background of the entities requesting the license or the permits, the capital market competition, including the insurance market, and its service level, the government's economic policy, arrangements as to reinsurance, staff etc. The Commissioner may set conditions and restrictions as to granting the permits, including the existence of a fixed and stable control nucleus in an insurer, a prohibition of putting lien on the control means included within the chain of control in an insurer, maintaining the controlling group's frame, including setting provisions or restrictions as to the sale or transfer of the control means to another.

Also, as per Clause 32 (c) to the Supervision Law, there is a prohibition on a material holding in the area of LTS. A material holding was defined as holding a market share exceeding 15% of all LTS assets.

As per the Provident Funds Law, the practice of provident funds, too, requires licensing a managing company under the said law. Also, holding more than 5% of a certain type of control means in an insurer, is conditioned on receiving a holding permit and a control permit. The aforementioned considerations as to granting licenses and permits in the insurer, also apply to provident funds, with the required changes. Provident funds for annuity are the same as insurers.

In April 2012 the Commissioner published a draft document regarding **Conditions for the Control and Holding of Institutional Organs**, detailing the principles for the criteria and general conditions for the control and holding of means of control in an institutional organ. Pursuant to the Draft, the intention is to request also from all the current controlling shareholders and holders who received a permit from the Commissioner, to comply with the requirements of the new policy, after the adjustment period, detailed in the above mentioned document.

The control permit shall refer to the entire holdings chain in an institutional organ, up to an individual who is the final controlling entity of the entire chain.

Among other discretions for the adjustment of the permit petitioner to receiving the permit shall include four main areas: personal and business honesty and integrity, financial robustness, planned investment strategy, business experience, his other occupations and businesses and the potential for conflicting interests in the supervised body.

The main issues included in the above draft are: the control structure and the way means of control are held in institutional organs, restrictions that would apply to the controlling shareholder including regarding the holding of a controlling shareholder in other real corporations and the types of corporations who will not be allowed to control a controlling shareholder in general, or an insurer in particular, as the case may be; the minimal holding rate required from a controlling shareholder in an institutional organ, the control chain structure and setting the ratio between the direct holding of the controlling shareholder in an institutional organ and the holding rate via the final holder and mechanisms for capital enhancement when necessary, instructions as to capital raising by the controlling shareholder, defining the debt ratio to the balance of the balance sheet in the borrowing corporation and in the other corporations in the control group, limits on extending credit by a single banking corporation and a prohibition on a lien on direct means of control in an institutional organ; instruments for the examination of the financial robustness of the control permit applicant and setting the ratio between equity and the value of the means of control and the means for measuring it[88].

(2) **Permits that were received following the transfer of control in the Company**

As set forth in Clause 2.1 to Chapter A above, on October 29th, 2012, a transaction pursuant to which the control in the Company was transferred to Eliahu Insurance.

Control permits granted by the Commissioner – upon the completion of the transaction, the permit for holding means of control and control in insurers ("**control permit**"), extended to Messrs. Shlomo Eliahu and Ms. Haya Eliahu, allowing them to hold, directly and indirectly, the means of control in Eliahu Insurance, Migdal Insurance, Migdal Makefet and Yozma, as per the conditions set forth in the control permit, came into effect. This control permit cancels the permit for holding means of control and control extended to Generali in Migdal Insurance, Migdal Makefet and Yozma, which was effective until the transaction's completion.

The control permit sets forth, inter alia, restrictions and limits as to the way means of control in Eliahu Insurance, Migdal Holdings, Migdal Insurance, Migdal Makefet and Yozma are held, as to maintaining the control structure and the minimal holding rate in the entities mentioned above, regarding the sale or transfer or issuance of means of control in each of the above mentioned entities, including a lien on them, regarding maintaining equity ratio

[88] Pursuant to the draft document – the guidelines are also asking a control permit in banking corporations. The document is a joint document of the Bank of Israel, the Commissioner of Banks and the MoF – Capital Market, Insurance and Savings Sector. In December 2010, a joint paper of the Commissioner of Insurance, the ISA and the Commissioner of Insurance, setting criteria of Fit and Proper of those asking to operate in the area subject to the supervision of the supervisors mentioned above, outlining a list of criteria referring to the above mentioned Fit and Proper test, the existence of one of the above mentioned criterions detailed in the list is a reason for examining the existence of a damage to the Fit and Proper test.

in all the institutional organs controlled by the controlling shareholders, as well as the conditions pursuant to which the controlling shareholders and Eliahu Group may receive management fees from the institutional organs controlled by the Company, or provide services to institutional organs controlled by the Company.

Mr. Shlomo Eliahu gave the Commissioner of Capital Market, Insurance and Savings a letter of undertaking signed on October 16th, 2012. Pursuant to that letter of undertaking (the scope of the control permit was stipulated by giving this letter), Mr. Shlomo Eliahu, being the controlling shareholder in Eliahu Insurance, Migdal Insurance, Migdal Makefet and Yozma ("**the insurers**"), must enhance Eliahu Insurance's and Migdal Insurance's equity to the amount set forth in the Regulations of Supervision on Insurance Businesses (Minimum Equity) Required of Insurers – 1998, or any other Regulation or Law that would substitute them, and enhance the equity of Migdal Makefet and Yozma to the amount set forth in the Regulations of Supervision on Financial Services (Provident Funds) (Minimum Equity Required Managing Companies of Provident Funds or Pension Funds) – 2012, or any other Regulation or Law that would substitute them ("**Equity Regulations**"). This undertaking is irrevocable and will be in effect as long as Mr. Shlomo Eliahu controls, directly and indirectly, the insurers set forth above.

As of the date of this report, the equity required from Migdal Insurance, Migdal Makefet and Yozma complies with the requirements of the Equity Regulations and the Provident Funds Law, as the case may be, see also Note 7 e to the Financial Statements.

Furthermore, upon of the date of completion, the Commissioner also allowed the lien on the mortgaged shares to Bank Leumi and their transfer to the trustee as set forth in Clause 2.1 to Part A above, pursuant to the conditions set forth in the permit.

Also, there is a control permit for holding means of control in insurance agencies that the Company holds means of control in them, that require receiving a permit.

BoI permit – since Mr. Shlomo Eliahu, prior to the completion date, held, directly and indirectly, including via Eliahu Insurance, means of control in Bank Leumi and Israel Union Bank Ltd. ("**the banking corporations**"), Mr. Eliahu informed the Company that he received permits for holding means of control pursuant to the Banking Law (Licensing) – 1981 in banking corporations, referring, inter alia, to his holdings in banking corporations via Eliahu Group as well as via the Company and its subsidiaries.

Within these permits, Mr. Shlomo Eliahu's holding rate in each of the banking corporations, via the Company and its subsidiaries, shall not exceed 5%, similar to the regulatory restrictions that currently apply to the Company regarding holding means of control in banking corporations (as of the date of this report, the holdings of the company and its subsidiaries in these banking corporations are: Bank Leumi - approx. 4.21% and Union Bank – approx. 0.47%)[89].

The Israel Antitrust Authority permit – on June 2th, 2012, the Israel Antitrust Authority General Director approved the merger between Mr. Shlomo Eliahu, Eliahu Insurance and the Company. The merger was approved subject to the following conditions: as of the transaction's completion date, the Company shall not engage (directly and indirectly)[90], in an agreement with related trading companies[91] for the execution of transactions in beneficiaries' assets, that the consideration in its respect shall be paid from the beneficiaries' assets, unless via a tender giving all trading companies an equal opportunity to participate in it ("**the tender**"), and in which at least four trading companies will participate.

The tender's documents shall be published in the Company's website and will include, inter alia, the entry requirements for participating in the tender, the way and deadlines for submitting offers, the engagement period and conditions thereof, as well as the way and criteria for selecting the winners.

The Company shall not negotiate with trading companies or anyone on their behalf, regarding the details of the tender and its conditions, before the publication of the tender documents and afterwards, until the selection of winners, except receiving clarifications regarding the offers submitted by the tender participants.

An offer by a related trading company may be selected in a tender only if the financial consideration to be paid by the Company as per this company's offer, is the lowest offered in the tender.

(3) **Financial services activity**

In order to perform various activities in the area of financial services, there is need to receive control permits and licenses from the various State authorities, especially the Securities Authority and the Stock Exchange. In their considerations for granting control permits and licenses, as mentioned, the relevant supervision authorities take a wide variety of considerations into account, including, inter alia, the credibility of the applicant and its controlling shareholder, as described above. Also, the sale or transfer of means of control in a traded company requires receiving a permit.

[89] In addition, to the Company's best knowledge, in the BoI permit that was given to Messrs. Shlomo Eliahu and Ms. Haya Eliahu regarding the holding of banking corporations, there are restrictions that apply to them regarding the continued holding of the controlling interest in the above mentioned banking corporations, including mandating the transfer of means of control held by them to a trustee.

[90] Regarding this matter, the Company means the Company, including a related person, as per the definition of this term in the Restrictive Trade Rules (General Provisions and Definitions) – 2006.

[91] **A Related Trading Company** was defined – a trading company, that at least 5% of its shares are held, directly and indirectly, by the controlling shareholder in Migdal, including a holding via a trustee, except a trading company which, upon the date of transaction completion, all its shares are held, directly and indirectly, by the Company.

Furthermore, a prohibition was imposed on the acquisition of a mutual fund or the control over a fund manager, if the buyer's or holder's market share, including their controlling shareholders and entities controlled by them in the area of mutual funds after performing the purchase, exceeds 20%.

Pursuant to the transfer of control in the Company, the TASE gave a permit for changing the control and for putting a lien on mortgaged shares in favor of Bank Leumi pursuant to the terms set forth in the permit.

(b) **Equity and limits on dividend distribution**

(1) **Insurance companies**
The Group's insurance activities require a minimum solvency margin demands, set in the minimum solvency margin regulations. The capital requirements are tested by the annual Financial Statements and interim reports of the insurer, and if the equity on the report date is smaller than required, the insurer must increase or reduce its scope of business, on the dates as prescribed by the law. As long as such equity is not completed, the insurer may not distribute dividends.

For information regarding equity required from insurers as per the legislative arrangements in effect, including arrangements regarding capital requirements pursuant to the implementation of the Directive as set forth in Clause 45.2.11 (c) above, adjusting capital pursuant to temporary provisions stemming as described in the New Investment Rules, restrictions regarding dividend distribution, including surplus amounts that may not be distributed, Migdal Insurance's equity management policy - see Note 7 e to the Financial Statements.

The minimal equity required in Migdal Insurance as at December 31st, 2012 is approx. NIS 3,546 million. The existing equity at that date is about NIS 4,995 million, out of which approx. NIS 45 million that are non-distributable surpluses.

In addition, pursuant to the temporary provisions as detailed in the New Investment Regulations, some investment may be gradually perceived as non-recognized assets, as detailed in Clause 45.2.9 (b) above and Note 7 e to the Financial Statements.

(2) **Managing companies of pension funds**
The Regulations of Supervision on Financial Services (Provident Funds) (Minimum Equity Required Managing Companies of Provident Funds or Pension Funds) – 2012 regulate the provisions related to the capital requirements from managing companies. These Regulations significantly expanded the capital requirements that existed before the publication of the above mentioned Regulations, and there are temporary provisions regarding the enhancement of required equity pursuant to the new requirements. Should the equity be lower than what is required in the Regulations, the managing company must enhance it up to the amount set forth in the Regulations. Dividend distribution is possible only if its equity is at least the equity required from it as per the Regulations. Also, equity investment rules were also set.

The minimal required equity from Migdal Makefet, that is a managing company of pension funds and provident funds is approx. NIS 106 million. The existing capital in Migdal Makefet as of December 31st, 2012 is approx. NIS 373 million, significantly higher than the equity requirements as of today, and than the full requirement on Migdal Makefet as of December 31st, 2014.

The minimal required equity from Yozma, that is a new pension fund managing company, is approx. NIS 10 million, which it may enhance gradually as per the temporary provisions, until the publication of the FS as of December 31st, 2013. The existing capital in Yozma as of December 31st, 2012 was approx. NIS 5 million. On March 7th, 2013, after the publication date of the FS, Migdal Insurance infused to Yozma another approx. NIS 2 million. After this infusion, and taking into account the deadlines set forth in the Regulation, Yozma complies with the Equity Regulations.

For additional details regarding Migdal Makefet and Yozma's equity, see Note 7 e to the Financial Statements.

(3) **Financial services companies**
Each of the different companies of the financial services area is required to have equity, sometimes even positive working capital and liquid assets, at amounts and percentages set in the relevant law provisions. In June 2011 provisions as to the implementation of a new model for financial stability of TASE members that are not banks came into effect. Under this model, the equity requirements, liquidity and rules for granting credit to customers by TASE members that are not banks, were updated. For details see Clause 43.1.3 (a) above. Furthermore, underwriting companies are requested to hold a deposit of at least approx. NIS 3 million, held in trustee by an attorney or a CPA.

(4) **Expertise, knowledge and experience**
The insurance and financial activity of the Group’s businesses requires specific professional knowledge, mainly in the area of actuary and risk management, and familiarity with the area’s markets, including the reinsurance market. Furthermore, experience in this activity, actuarial information and a rich database are very important for setting tariffs and underwriting of new businesses.

(5) **Minimum size (critical mass)**
In order to cover the high fixed operational costs required for the operation of the insurance and investment systems, including the need to answer the changing regulatory demands in the various areas, minimum scope of revenues is required.

45.4.2 **Exit barriers**
The main exit barriers of the Group’s activities are also set by the relevant provisions.

(a) **Insurance, pension and provident activity**

The liquidation or winding up of an insurer’s insurance businesses are subject to the supervision of the Commissioner of Insurance, who may instruct insurers to act in a certain way in the winding up of the business or ask the court to give an order stating that the liquidation should be made by the court or under its supervision.

Mergers, splitting up, management termination or voluntary winding up, require previous approval from the Commissioner. If an order application was made to appoint an official receiver or a temporary liquidator in a managing company, and such orders were not cancelled within a certain period set in the Provident Funds Law, or if management was not transferred to another managing company within the period set under the law, the Commissioner may apply his authorities regarding anything related to the provident fund stability, including appointing an authorized manager in accordance with rules set as to insurance companies.

In life assurance and pension businesses and “long-tail”-featured lines of general insurance businesses – the termination of activity is involved in an arrangement to continue realizing all of the insureds’ / members’ rights (Run-Off).

(b) **Financial services**

During 3 years from the date of the last prospectus that was signed by an underwriting company, it is not allowed to withdraw monies from a deposit that was deposited with a trustee

The liquidation of mutual funds managed by a fund manager is subject to arrangements to the **Joint Investments Trust Law – 1994**. Any sale or transfer of means of control in some of the companies in the area of financial services mandates the buyer to receive the permits set forth in Clause 45.4.2 (a) above, with the required changes.

46. Investments[92]

46.1 Structure of investment management of the Group's institutional organs

46.1.1 General

The BoD of every subsidiary, which is an institutional organ, outlines the overall investment policy in its areas of activity.

In its overall investment policy, the relevant institutional organ's BoD sets the strategy, objectives and exposure framework for the various investment channels, in each of the portfolios managed by it.

The Investment Committees which operate in the Group's insurance company, as well as in the pension and provident funds' managing companies, determine the investment policy specifically for each of the Group's entities.

The Group's institutional organs' investments management, except the investment management of some provident funds of Migdal Makefet, is conducted in the Group's investments array as described in Clause 49.1 hereinafter, that concentrates the knowledge, expertise and personnel required for investment management. The investment management of some of Migdal Makefet's provident funds as set forth is conducted via Migdal Capital Markets Group, as described in Note (2) to the Table in Clause 11.2 to Part C above.

46.1.2 Insurance

The various insurance liabilities monies are invested in different assets, according to the nature of liabilities, subject to the new investment regulations/investment principles which set various restrictions and frameworks adjusted to the nature and type of various liabilities.

The Supervision Law and investment ways regulations state, inter alia, that insurers’ BoDs must appoint two investment committees. One for managing the investment portfolio of monies to cover yield dependent liabilities (“**profit participating investment committee**”), and another for investing

[92] The Clause refers to investment management of insurers, pension funds and provident funds managed by a managing company, and not to the financial services area's investment management.

the insurer's equity, and investing monies to cover non-yield dependent insurance liabilities ("**Nostro committee**"). The Provident Funds Law provisions as to managing companies' investment committee also apply to the profit participating investment committee, regarding investment committee of managing companies.

The Commissioner's Circular regarding the management of credit risks in investments activity, states, inter alia, that the investments committees that manage all in all over NIS 5 billion and whose scope of credit exceeds 15% of all the assets managed by it must establish a Credit Committee. Credit Committees may be joint for the institutional organs controlled by the same controlling shareholder and pursuant to the conditions set forth in the Circular. The Group has a joint Credit Committee for Migdal Insurance and Migdal Makefet.

46.1.3 **Pension funds and provident funds**

The Income Tax Regulations / New Investment Rules regulate the management of savings money investments under the pension and provident activity, including the types of assets, restrictions and various frames for investments.

Similar to insurance companies regarding yield dependent liabilities, the Provident Funds Law states that a managing company of pension or provident funds must appoint an investment committee as to the monies managed by the said fund, and in certain cases, also Credit Committees as set forth above. In both pension funds and provident funds, it was stated that the Investment Committee shall comprise a majority of External Directors, and its roles are similar to the ones of yield dependent liabilities' Investment Committees, as detailed in Clause 59.1.1 to Part F hereinafter.

46.2 **Details of assets under management**

46.2.1 **Details about assets managed in the profit participating life assurance portfolio as of December 31st, 2012**

Hereunder is the breakdown of managed assets in Migdal Insurance, in a breakdown as per assets held against (profit participating) yield-dependent insurance liabilities, Nostro - assets held against liabilities in life assurance, and Nostro - assets held against liabilities in general insurance and equity:

	Proportional rate out of accrual monies in %		
	Assets held against yield-dependent insurance liabilities (profit participating)	Nostro - assets held against liabilities in life assurance	Nostro - assets held against liabilities in general insurance and equity
Negotiable bonds	27	10	44
Non-negotiable bonds	5	3	5
Designated bonds	1	69	0
Equities and options	17	2	3
ETNs, mutual funds, ETFs	27	2	5
Cash and cash equivalent	4	3	18
Deposits	2	5	0
Real estate for investment	6	2	4
Investment funds	5	1	0
Loans, receivables and other	6	2	3
Investments in investees	0	1	18
Total	100%	100%	100%

46.2.2 Breakdown of the managed assets in pension funds and provident funds, as of December 31st, 2012[93]

Hereunder is the breakdown of managed assets in pension funds	**Proportional rate out of accrual monies in %**						
Migdal Makefet Ishit	**General track**	**Religious authorization**	**Bond and deposits track**	**Short term track**	**Equity track**	**New pensioners account (annuitants)**	**Current payables account**
Cash and cash equivalent	2	5	11	12	10	3	1
Negotiable shares in Israel	9				21	3	4
Negotiable shares abroad	3						
Non-negotiable shares abroad	1						
ETNs in Israel	1	31	9		7	1	1
ETNs abroad	14	18			35	6	5
Negotiable government bonds	10	17	43	63		43	6
Non-negotiable government bonds (designated)	30	29	27	25	27	29	70
Negotiable corporate bonds	9		10			13	10
Non-negotiable corporate bonds	3					1	2
Negotiable mutual funds abroad	8						
Investment funds	3						
Deposits and loans	5						1
Real estate	2					1	
Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**

[93] The data of assets breakdown in pension and provident funds as per tracks, in the funds in which there are material assets.

	Proportional rate out of accrual monies in %					
Migdal Makefet Complementary	**General track**	**Religious authorization**	**Bond and deposits track**	**Short term track**	**Equity track**	**New pensioners account (annuitants)**
Cash and cash equivalent	5		4	11	7	4
Negotiable shares in Israel	10					2
Negotiable shares abroad	1					
ETNs in Israel	3	37	25		57	3
ETNs abroad	15	17			34	5
Negotiable government bonds	46	46	70	89		65
Negotiable corporate bonds	12		1			17
Non-negotiable corporate bonds	1					3
Negotiable mutual funds abroad	6					
Deposits and loans	1					1
Other					2	
Total	**100**	**100**	**100**	**100**	**100**	**100**

	Old Yozma (Yozma for Self-Employeds)
	Proportional rate out of accrual monies in %
Cash and cash equivalent	5
Non-negotiable bonds	35
Negotiable bonds	47
Deposits and loans	2
Real estate	
Other negotiable shares and securities	11
Other	
Total	**100**

Hereunder is the breakdown of managed assets in provident funds.

	Proportional rate out of accrual monies in %					
Training funds	**Cash and cash equivalent**	**Negotiable government bonds**	**Negotiable corporate bonds**	**Other negotiable shares and securities**	**Deposits, loans and other investments**	**Total**
Migdal Kahal Training						
General track	7	30	18	33	12	100
Equity track	12			86	2	100
Foreign track	39	5	28	28		100
Government bond track	10	90				100
Short term NIS track	8	92				100
CPI-linked track	10	57	31	2		100
General Big track	13	32	24	29	2	100
Bond track	10	46	31	5	8	100
Forex track	38	8	54	0		100
General Maoz track	13	29	53	2	3	100
Religious authorization track	11	27	32	30		100
Migdal Training Fund for Salarieds and Self-Employeds	7	25	21	38	9	100

	Proportional rate out of accrual monies in %					
Provident fund for provident benefits and severance pay	**Cash and cash equivalent**	**Negotiable government bonds**	**Negotiable corporate bonds**	**Other negotiable shares and securities**	**Deposits, loans and other investments**	**Total**
Migdal Platinum for Benefits						
General track	6	31	21	32	10	100
Equity track	8			92		100
Foreign track	25	9	33	32	1	100
Government bond track	9	91				100
Short term NIS track	6	94				100
CPI-linked track	8	58	31	5		100
General Big track	13	32	24	29	2	100
Migdal Provident Fund for Provident Benefits and Severance Pay	5	26	21	40	8	100

For information regarding the scope of assets managed in pension funds, see Clause 10.3.3 to Part C above.

For information regarding the scope of assets managed in provident funds and training funds, see Clause 10.4.4 to Part C above.

46.2.3 **General**

Within the investment policy for managing the insureds' and beneficiaries' monies in Migdal Insurance and Migdal Makefet, the Group strives towards diversifying its investment increasing exposure to investment channels overseas, and increasing its investments in the area of yielding real estate and credit, through partnerships and direct investment in companies.

Pursuant to the Commissioner Circular regarding the institutional organs' statement in advance as to their investment policy, the institutional organs in the Group publish their expected investment policy for all investment tracks managed by them, for the upcoming year, and the publication includes exposure rates to investment channels, including deviation ranges. If the investment policy was changed, or if there is a deviation compared with the conditions set forth in the Circular, an update to said policy is published.

The institutional organs in the Group published their expected investment policy for 2013 as per the Circular.

46.3 **Revenues from investments and their impact on insurers' and managing companies' profits**

Revenues from investments against insurance reserves and equity have a material impact on the profits of insurance companies. The scope of impact on profits depends on the characteristics of the insurance liabilities (Nostro, profit participating) and the terms of management fees in products against which the relevant reserve is held.

In profit participating policies issued from 2004 and on, all the yield from investments is imputed to insureds, while the insurer is entitled only to fixed management fees. In these products, the impact of the financial results on the profits of the insurance company is reduced to the impact deriving from the total scope of the assets from which the insurer's fixed management fees are derived.

In profit participating policies issued until December 31st, 2003, the yield from investments is imputed to insureds, while the insurer is entitled to fixed management fees as well as variable management fees derived from the real profit achieved after deducting the fixed managed fees. In these products, insurance companies' monetary results are also affected by volatility in yield imputed to insureds in light of the fact that variable management fees are collected from the real achieved yield after deducting fixed management fees.

In non-profit participating life assurance (in respect of the part of life assurance portfolio which is not backed by designated bonds), in general insurance and in capital, there is no full similarity between the linking basis of assets and linking basis of liabilities.

Thus, changes on capital markets, both, in Israel and worldwide, in interest rates, in CPI and in Forex rates may have a material impact on the Group's results of activity, especially taking into consideration the large scope of reserves managed by the Group. See also Note 37 to the Financial Statements.

Most of the Group's assets portfolio is invested in negotiable securities on the capital market, both, in Israel and worldwide, thus yields on the capital markets in the various channels may have a material implication both on yield achieved for the Group's customers and the Group's profits.

In pension and provident businesses, the yield from investments, less management fees from accrual after discounts, is imputed to members, therefore the effect of the investments results on the profits of the managing companies of the pension or provident funds, minimizes to an effect derived from the overall scope of accrual in the pension or provident funds, from which the management fees of the pension or provident funds' managing company, are derived.

46.4 **Investment in affiliates**

The Group has an investment balance of about NIS 605 million in affiliates (vs. approx. NIS 580 million in 2011). The increase in the investment balance is mainly due to income of affiliates in the amount of approx. NIS 64 million, less dividends in the amount of approx. NIS 39 million.

The main significant holdings in the affiliates are:

Ramat Aviv Mall Ltd. (previously Meqarqee Merkaz Ltd.) - this is a private company whose shares are held at approx. 73.4% by Melisron Ltd., that is a public company, and at approx. 26.6% by Migdal Insurance. The Company owns the Ramat Aviv Mall. The Mall complex also includes an office building and adjacent office space for rent. The Mall is managed by a management company fully owned by the Mall Company.

Amot Investments Ltd. ("**Amot**") - Amot is a public company, whose shares trade on the TASE, engaging, directly and indirectly, via corporations controlled by it, in renting, managing and maintaining assets in Israel, as well in acquiring, initiating and developing real estate for rent for self-use. Amot is a subsidiary of Alony Hetz Properties and Investments Ltd., a public company whose securities are also traded on the TASE. Migdal Insurance holds approx. 15.1%[94] of Amot's issued and paid up share capital.

[94] Migdal Insurance has the right to appoint another Director in Amot's BoD. Such a Director has not been appointed yet. In light of that potential right, the potential voting rate is 20%.

For additional details regarding these affiliates, including concise information regarding the financial situation and results of activity of these affiliates, see also Notes 7 a and 7 b to the Financial Statements.

For tax assessments as per the best judgment, issued against Migdal Real Estate Holdings Ltd., which holds Ramat Aviv Mall Ltd., see Note 21 d to the Financial Statements.

47. Reinsurance

47.1 General

As an integral part of practicing insurance, the Group operates to cover some of the insurance risks it takes via foreign reinsurers. The engagement with reinsurers has several advantages, mainly protection against high exposure risks and fluctuations in the behavior of risk. Reinsurance is adjusted to various risks according to the nature of risk and its level.

The acquisition of reinsurance is performed in policies or lines in which, to the Group's estimate, it is more efficient to cede the risk than to use the Company's capital. Internal actuarial estimates, various actuary or statistical models and claims experience, help the Group in assessing the required reinsurance level.

Reinsurance transactions are signed in the Company's various areas of activity, life assurance, health insurance and general insurance (property and liability insurances). The balance of risk imposed on the insurance company after ceding part of the risk to reinsurers is called "**retention**".

Usually there are two types of engagements in reinsurance:

47.1.1 **Contractual reinsurances** – the reinsurer receives in advance all the risks that the insurer takes upon itself, in a pre-defined line / area, during the treaty period and in the insurance scopes defined in the treaty ("**reinsurance treaty**"). Reinsurance treaties are signed and / or renewed, usually every year (usually in the beginning of a calendar year), and they cover, in the conditions set forth in them, a variety of risks included in the various insurance policies, sold by the Group during the activity period that the treaty applies for. Claims by virtue of the reinsurance treaties are paid both during that year and / or during the following years, subject to the Law of Limitation[95].

47.1.2 **Facultative reinsurance** - the reinsurers are addressed for every business separately, and they may accept or reject the proposed business. The engagement with the reinsurer is in order to cover risks embedded in specific policies ("**facultative reinsurance**"). Usually businesses will have this type of insurance when the insurance amount exceeds the insurance amounts covered by the reinsurance treaties mentioned in the previous paragraph, and / or when the risk is excluded from the reinsurance treaty and / or due to specific underwriting considerations and their adjustment to the outlines and terms of the treaties.

[95] In life assurance and health insurance, where the policies are for the long term, usually reinsurance treaties cover the policies sold in the area of activity to which the treaty refers, but their validity will be for the entire life of the policies that were sold until their cancellation, even if the reinsurance treaty is not renewed in the following years. In some reinsurance treaties in health insurance, the reinsurer may request changes in the treaty also for existing insureds if certain conditions set forth in the treaty are met, see Clause 22 to Part C above.

The customary structures of reinsurances are:

47.1.3 **Proportional reinsurances** – the reinsurers participate in the pro rata share of the risk, and in return they receive the same pro rata of premium. There are mainly two types of proportional reinsurance:

- **Quota Share**, in which the reinsurers participate in a pre-determined rate, in premium, risk and claims.
- **Surplus treaty** - in which the reinsurers participation rate varies from one risk to another, and from the moment it is defined, the reinsurers participate in the same rate in premium, risk and claims

47.1.4 **Non-proportional reinsurances** – the share of the reinsurers is not their share in premium. Usually, reinsurers do not pay commissions in non-proportional treaties. The main treaty in non-proportional reinsurance is **Excess of Loss**, in which reinsurers receive a payment deriving from the scope of the line to which the treaty refers, in return of which they cover damages exceeding a certain amount, per risk, claim or event, as they were set.

Reinsurance engagements in general insurance are usually conducted on an annual basis.

In life assurance and health insurance, reinsurance engagements are usually conducted with relation to a defined period, and apply throughout the entire life of the covered policies issued at such defined period. In some health insurance (LTC, medications insurance etc.), reinsurers may interrupt the insurance coverage during the agreement period, such that the agreement does not cover all the lives of issued policies, under certain conditions in the agreements.

In reinsurance transactions, the cedent insurance company pays reinsurers a premium. Reinsurers pay the cedent company payments in respect of claims, as well as commissions, depending on the structure of the reinsurance transaction. As already mentioned, usually, in non-proportional reinsurances, no commissions will be paid by reinsurers.

The commissions received from reinsurers are usually set as a share of the premium ceded to the reinsurers. Sometimes, the commission rate is fixed, regardless of the achieved results, and sometimes the commission rate depends on the underwriting results of the ceded businesses. Sometimes, Migdal receives a profit commission in addition to the fixed commission, which is calculated as part of the underwriting profit at the same risk (namely, a premium less claims and commissions).

Sometimes the Group also executes more complex transactions. Usually, these transactions are transactions in which the customer has global activity, both in Israel and abroad. The insurance coverage is given not only to the Israeli activity but also to activity overseas ("**multi-national transaction**").

Reinsurers' liabilities towards the insurance companies do not release the insurance companies from their liabilities towards their insureds, therefore reinsurers' financial stability affects the insurance companies – see Note 37 to the Financial Statements.

47.2 **Description of exposure policy to reinsurers**

47.2.1 **General**

As stated above, the Group acquires reinsurance under the framework of risk management policy. The reinsurance acquisition takes place in policies or lines in which, in the Company's opinion, it is more efficient to transfer the risk. Internal actuarial estimates, various models and former experience with claims, assist the Group in estimating the required reinsurance level.

There are two types of exposure to reinsurers:

- Exposure to open balances, and the risk that the reinsurer may not be able to cover its current and future liabilities. This exposure is managed via ongoing follow-up of the reinsurer condition in the global market, and the compliance with its financial liabilities.

- Exposure to a single large damage or accumulation of damages in respect of an especially large event. The accumulation is estimated based on the Maximum Possible Loss ("**MP**L") rate. This exposure is managed via an individual estimate of each of the reinsurers separately.

There are also exposure caps for the plan or for the scope of exposure to the reinsurer, depending on the reinsurer's equity.

The rating of reinsurers is based on the Standard and Poor's (S&P) rating, or on another rating company whose rating has been converted by an index set under the investment regulations.

47.2.2 **Life assurance**

For the description of the Group's exposure policy to reinsurers in the life assurance area– see Clause 14 to Part C above.

47.2.3 **Health insurance**

For the description of the Group's exposure policy to reinsurers in the health insurance area– see Clause 22 to Part C above.

47.2.4 **General insurance**

The Group protects itself from earthquake events, even from those occurring once in approx. 350 years. The estimate is achieved, inter alia, via the use of designated software for catastrophe-related risks estimate.

In the CMBI line, the Group acquires reinsurance up to an unlimited level, if possible, or, alternatively, to a level high enough to avoid any foreseen event.

In other lines, such as liabilities, the Group estimates the risk based on actuarial or statistical estimates and models, and claims experience, and acquires protection up to the required limit, in its opinion, under the policies sold by the Group.

Under the risk management policy, the Group distinguishes between the following types of businesses:

- **"Short tail"**[96] **businesses** – **low frequency** – includes medium to large corporations and businesses. Due to lack of Israeli-specific statistical data, the Group relies on models and estimates conducted by research institutes and universities, and acquires adequate reinsurance accordingly: proportional, facultative or excess of loss. The engagements are made with insurers rated BBB or higher.

- **"Short tail" businesses** – high frequency – mainly refers to property insurance of homes and small businesses. In such lines, the Group usually uses proportional or excess of loss agreements per event. The engagements are made with insurers rated BBB or higher.

- **"Long tail" businesses**[97]. – the covered risks are mainly liabilities and CMBI. Many of these claims end up in court, and sometimes, setting the indemnification level liability may take many years. In long tail business, since the Group must engage with reinsurers which, according to its estimate, are solvent on the long term, the number of reliable reinsurers is quite limited. Therefore, the Group policy in these types of businesses is to engage with reinsurers rated A- and higher. The selected type of reinsurance is mostly excess of loss.

  Sometimes, under an overall insurance arrangement, reinsurance with unrated companies are included.

  For additional details regarding exposure to reinsurers, see also Note No. 37 to the Financial Statements.

47.3 **Reinsurance transactions with Generali**

Generali, which was the Company's controlling shareholder up until October 29th, 2012, had and has a material share in the Group's reinsurances.

For details regarding transactions in reinsurance with Generali Group, including an undertaking given by Generali to the Company within the completion of the transaction for the transfer of control in the Company, see the description included within Regulation 22 Transactions with controlling shareholders or in which the controlling shareholders have a personal interest", and Note 38 to the Financial Statements.

47.4 **Exposure of reinsurers to catastrophe events - earthquake and natural hazards**

47.4.1 **Life assurance**

Regarding coverage in respect of catastrophe events in life assurance, see Clause 15 above.

47.4.2 **General insurance**

In respect of catastrophic events (earthquake and natural hazards), beyond coverage under proportional reinsurance agreements, the Group acquired "excess of loss" reinsurance for property and contractor lines in respect of the accumulated retention, at an exposure–defined amount which shall derive from such event, based on the Group estimate as to the expected damage or event due to catastrophe. In the risk estimate, as mentioned, the Group used, inter alia, international designated software based on mathematic models for catastrophic risk estimate. If an event occurs, whose extent of damage exceeds such estimate, the Group shall be exposed to losses that are not covered in reinsurance.

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[96] **Short Tail** – lines in which the time gap between the insurance event and the final outlining of damage and its payment is relatively short.

[97] **Long Tail** - lines in which the time difference between the insurance event and the final outlining and payment of the damage, is long.

As aforementioned, the Group protects itself against earthquake events, even such earthquakes whose intensity occurs once in 350 years.

In 2012, coverage of a weighted rate of 2.00% was acquired, representing a weighted MPL of 5.6% once every 350 years (before the insured's deductible), which was compatible with the forecasted business mix for that year.

In 2013, non-proportional coverage at weighed rates similar to those of 2012 was acquired, i.e. weighted non-proportional coverage of about 2.00%, representing a weighted MPL of 5.7% once every 350 years (before the insured's deductible). In 2012, the insurance sums covered under proportional reinsurance against earthquake total approx. NIS 154 billion, while the insurance sums in retention on which the Company protects through non-proportional reinsurance treaty total approx. NIS 67 billion.

The Group's policy in catastrophe risks ("short tail" risks) is to engage with reinsurers whose rating is at least BBB.

About 97% of exposure to earthquakes is covered by reinsurers rated A- and more.

The three reinsurers participating in catastrophe events reinsurance coverage, whose share of the total exposure exceeds 10%, are Generali (approx. 23%), Swiss Re (approx. 11%) and Hanover Re (approx. 10%). Generali was the controlling shareholder in the Group up to October 29th, 2012, which is, as already mentioned, an insurance company rated A as per S&P.

47.5 Summary of reinsurance results in general insurance (NIS millions)

Area of activity	Casco			CMBI (1)			Other property lines (see breakdown by premium types hereinafter) (2) (3)		
	2012	2011	2010	2012	2011	2010	2012	2011	2010
Premiums ceded to reinsurers	1.0	0.6	0.6	5.5	5.4	5.8	379.1	390.7	383.5
Reinsurers' results - income	1.0	0.5	0.4	15.2	12.1	6.0	190.9	36.6	134.8

Area of activity	Other liability lines (4)			Total		
	2012	2011	2010	2012	2011	2010
Premiums ceded to reinsurers	68.8	87.6	90.4	454.4	484.3	480.3
Reinsurers' results – income	69.1	97.2	3.0	276.2	146.4	144.2

Breakdown of other property lines by premium types			
	2012	**2011**	**2010**
Reinsurance premiums – proportional	272.8	267.2	264.9
Reinsurance premiums – non-proportional	10.8	9.7	10.1
Reinsurance premiums – coverage for catastrophe events(5)	95.5	113.8	108.5
Total reinsurance premiums	**379.1**	**390.7**	**383.5**

(1) The reinsurance results in CMBI mainly reflect the accumulated profit / (loss) of the underwriting year which ended three years prior to the reported year. The increase in CMBI results in 2011 and 2012 was affected by a decrease in outstanding claims of reinsurers in old underwriting years.

(2) The changes in reinsurance premiums in 2010-2012 are related to the overall increase in gross premiums in other property lines as detailed in Clauses 27.3, 28.3 and 30.3 to Part C above.

(3) In 2011, the decline in reinsurers results from other property lines was mainly due to two large claims mostly covered by reinsurance.

(4) Reinsurance results in other liability lines mainly reflect the aggregate income/(loss) of the underwriting year that ended three years before the reported year, as well as changes that mainly occurred in outstanding claims of reinsurers in old underwriting years. For example, in 2011 and 2012 there was a reduction in outstanding claims of reinsurers vs. an increase in 2010.

(5) The premium includes all types of reinsurance arrangements for catastrophe risks coverage (proportional reinsurance, facultative reinsurance and Excess of Loss reinsurance in order to cover accrued retention).

48. Suppliers and service providers

48.1 General

From time to time, the Group acquires products and services in various areas, for the operation of its businesses.

The Group is engaged with a large number of service providers, and they are selected based on their quality of service, availability, areas of expertise, commercial conditions, etc. Usually, such engagements are made for unlimited periods of time, and do not contain an exclusiveness arrangement.

The Group’s insurance companies also bear, like any insurer, the expenses involved in the insurance event insured in the policy. Such expenses include covering the cost of various services covered in the insurance policies (such as payment for hospitalization costs and other medical services costs included in the Group’s CMBI coverage or health policies, towing, repairs and spare parts included in comprehensive or third party motorcar policy etc.) (“**insurance claims costs**”).

The Group is engaged with some of the service providers and sets arrangements with them as to the prices and quality of services, including setting inclusive prices for the coverage or services rendered by these suppliers. The Group refers the insureds to these suppliers or provides various benefits as part of the referral to such suppliers. However, there are factors which the insured addresses, by choice, which the Group cannot affect in any way.

In addition, the Group’s insurance companies acquire related services to the payment of insurance claims in the various areas (lawyers, investigators, medical experts, risk evaluators, appraisers etc.) (“**related expenses**”).

The cost of the services included both in both insurance claims costs and related expenses, is imputed to the claims cost in the various insurance lines.

The main acquisitions from suppliers and service providers that are not imputed to the costs of claims in the various insurance lines are in respect of advertising services, computerization, maintenance etc. For additional details see Note 32 to the Financial Statements.

48.2 **Primary suppliers which are not unique to a specific area**

Following are several suppliers which are not unique to a specific area of activity, which were not described in the areas of activity:

48.2.1 **Assistance services**

Migdal Insurance undertook to acquire from Femi Premium Ltd. ("**Femi**") starting March 2007 all the assistance services granted to insureds by the riders sold under the motor casco insurance area (towing, glasses, alternate vehicle etc.), and most of the related services in the health and homeowners policies, including operating a national call center that is manned 24 hours a day. Migdal Insurance undertook to purchase these assistance services exclusively from Femi for a period of five years starting March 2007, under the conditions stated in the agreement.

As of March 2012, Migdal Insurance's undertaking to exclusively purchase the services from Femi as set forth above, was cancelled. An amendment to the agreement regulated its extension for another two years, and Migdal will have the right to terminate the agreement before the above mentioned period, after giving an advance notice. The amendment also regulates the various additional services that Migdal Insurance purchased from Femi not pursuant to the agreement from March 2007.

In an amendment to the agreement from February 2013, additional amendments were entered, pursuant to which, inter alia, the price of services referring to the riders in the area of general and health insurance were updated, and the agreement was extended by another three years starting from April 2013.

The scope of acquisitions from Femi in 2012 in respect of the acquired services from Femi amounted to approx. NIS 47 million, vs. approx. NIS 50 million in 2011. The cost of services acquired from Femi is imputed to the costs of insurance claims as described in Clause 48.1 above.

48.2.2 **Computer and software suppliers**

The Group is engaged with several hardware and software suppliers, which provide it with equipment and services, as well as in other agreements for the rendering of maintenance services in respect of data base and manpower services for development and maintenance of software. The forms of engagements include engagements at a fixed price per project, engagements by hourly tariff and engagements at price per unit. The replacement of service providers in the area of information systems involves costs and time, due to the know-how they accumulate, naturally, during the service provision. Sometimes dependency in the supplier is formed, in the short-run, due to the need to perform a project within a short time while accommodating regulatory changes, or a project on a certain topic in which the vendor is superior due to its accumulative knowledge.

The main hardware and software suppliers of the Group in the reported period are as follows:

(a) Software companies from which the Group acquires usage licenses for products and infrastructure (mainly Microsoft, Oracle and SAP). The annual payments made in respect of the acquisition of these licenses to each supplier are not material**.**

(b) Engagements related to the Group's main computer room storage and the establishment of a back-up site within the BCP project.

(1) In October 2006 the Group engaged with MED-1 IC-1 (1999) Ltd. ("**MED-1**"), which has a secured underground site in Petach Tikva, and which provides hosting and communication services for hosting the Group's main computer room at that site. The engagement is for 15 years, with the option for extending it by another year, at the conditions stated in the agreement. The engagement may be terminated by the Group and as per its discretion, before the end of the first period, subject to paying the amount stated in the engagement agreement. The ongoing payments under this engagement are not material.

(2) In 2011 the Company started executing a project aimed at upgrading and developing abilities of IT systems' technical business continuity, as part of the BCP and DRP project.

In September 2012, an agreement was signed with MED-1, regarding the establishment of a back-up site in Tirat Hacarmel. The engagement is for 10 years after delivering the site to the Group, with the possibility of extending it by another period every year, under the conditions set forth in the agreement (as of the date of this Report, the site has not been delivered yet). The engagement may be concluded by the Group, as per its discretion, before the end of five years after the delivery, subject to paying the amount stated in the engagement agreement.

48.2.3 **Additional services provided through outsourcing agreements**

The Group is engaged in outsourcing agreements in the following areas: providing vehicles to Group employees, printing services, document scanning and organization and methods. The sums paid in this framework are not material.

For the Group's engagements for rendering operations services in the area of provident funds, see Clause 15 to Part C above.

49. Human capital

The corporation is a holding company which does not use hired employees. The corporation CEO also serves as Migdal Insurance’s CEO, and is subject to the Corporation's Board of Directors.

49.1 The Group’s organizational structure

The insurance, pension and provident activity is conducted via several Divisions / Disciplines as follows:

Customers and Distribution Channels Division (as of 2013 it will be called the Customers, Service and Distribution Channels) – it concentrates the marketing and distribution activity and manages services for the Group customers and distributors, for all of the Group's institutional organs;

Long Term Savings (LTS) Division – concentrates the life assurance activity, as well as the pension and provident activity. This Division also manages institutional organs activity as regards the management of pension funds, provident funds and training funds[98].

Health Insurance Division – concentrates the health insurance activity

General and Reinsurance Division – concentrates the general and reinsurance activity.

Investments Array (**as of 2013, it will be called the Investments and Real Estate Array)** – concentrates the know-how, the expertise and the manpower required to manage the Group's institutional organs investments, that includes the area of beneficiaries' investments, real estate and hedge funds of the Group's institutional organs and the area of real investments, PE activity, credit and Nostro of companies in Migdal Group.

HQ Function (as of 2013, it will be called the HQ and group Coordination Division) – which are across-the-board functions, such as: finance, risk management, actuary, compliance and regulation, human resources, Company Secretariat, Legal Advice, control, O&M and operational risks, research, procurement, administration and logistics Discipline, SOX and investment control unit, were managed up to December 31st, 2012 by the HQ Division Manager, and some of the Discipline managers in the HQ Division, are also administratively, directly subordinated to the Group CEO.

Following the resignation of the HQ Division Manager by the end of 2012, as of January 1st, 2013, the issues of finances, actuary and Company Secretariat were concentrated under the **Finances and Actuary Division**. The areas of procurement, information security and the area of administration and logistics were concentrated along with the Computerization Services Unit aforementioned, into the **Technologies and Organizational Infrastructures Division**. The other HQ areas remained under the **HQ Division** (risk management, legal advice, compliance and regulation, SOX, operational risks, investments control, research and HR) report to the CEO.

Alongside the Divisions/Units set forth above, there is also Migdal Claims Management Ltd., which serves as the **Claims Management Unit**, which concentrates the claim payments / rights in all areas of insurance, pension and provident, which are handled by the Customers Division, and Migdal Technologies Ltd., that serves as the **Computerization Services Unit**, and provides IT systems services to the Group.

An **Internal Audit Unit** that serves the Group's companies. The Internal Auditor reports to the CoB.

The **Financial Services Discipline** is run in the Group mainly through Migdal Capital Markets Group, which operates as a separate unit, and performs the financial services activity.

The Group's **insurance agencies activities** are mainly concentrated in Migdal Agencies.

The activities conducted via **Migdal Health** and **Mivtach Management** (whose activities are not material, nor are their subsidiaries' activities, as of today) are conducted as separate units.

[98] As of January 2013, the LTS Division Manager serves also as the Health Insurance Division Manager, and as of March 2013, he also serves as the CEO of Migdal Health and Quality of Life Ltd.

49.2 **The Group's employees strength**

The Group has no clear distinction as to attributing all employees as per the areas of activity mentioned in this report, inter alia, since there are various units/divisions (such as employees of the HQ Function, Investments, Computerization Unit etc.) which provide services to more than one area of activity. As of December 31st, 2012, the Group hires about 4,316 employees (out of whom about 51 are hired through manpower companies), vs. about 4,304[99] employees (out of whom about 93 employees were hired through manpower companies) as of December 31st, 2011.

As of the said date, the Group's employees strength (including employees hired through manpower companies) can be divided in accordance with the following breakdown and the aforementioned organizational structure:

The Division / Unit	No. of employees as of December 31st, 2012	No. of employees as of December 31st, 2011
Group management and HQ function (1)	335	335
Customers and Distribution Channels Division	1,518	1,576
LTS Division	65	60
General and Reinsurance Division (2)	37	45
Health insurance Division (2)	11	-
Investments array	60	60
Migdal Claims Management – claims management unit	281	277
Migdal Technologies – Computerization Services Unit	339	333
Internal Audit Unit	19	20
Migdal Capital Markets Group	273	263
Group's insurance agencies	1,242	1,304
Mivtach Management	39	-
Migdal Health	97	31
Total	**4,316**	**4,304**

(1) In 2013 there was a change in the HQ Function, as described above. The data referring to the Group management and the HQ Function as of December 31st, 2012 include 151 employees, who, starting from January 1st, 2013, will be attributed to the Finances Division and 95 employees who will be attributed to the Technologies and Organizational Infrastructures Division.

(2) In 2011 the employees' strength referred to the General and Health Insurance Division, which, as of January 1st, 2012, was split into two Divisions: the General Insurance and Reinsurance Division, and the Health Insurance Division.

According to the aforementioned organizational structure, some of the Group employees, mainly employees of the Customers and Distribution Channels Division, Investments Division and some of the HQ employees, are jointly employed by the relevant institutional organs of the Group.

From the strength mentioned above, the group of Executive Senior Officers (who are not Directors) in the Group includes 26 employees ("**Executive Managers**"), and it includes Executive Senior Officers as detailed in Clause 49.7 hereinafter.

[99] The data regarding employees strength exclude employees who are employed by affiliates, and exclude data regarding employees who are employed by companies held at 50%, which are not material. In the reported year, the Company increased its holdings in two companies in which the holding rate as of December 31st, 2011 was 50%. If these companies were included in the employees' strength as of December 31st, 2011, the number of employees as of December 31st, 2011 would have been 4,413, instead of 4,304.

In 2012, there was a decrease in the number of employees in the Customers and Distribution Channels Division due to a streamlining in the LTS operation activity, including in the call center. Furthermore, there was a decrease in employees strength of the Group's insurance agencies following streamlining processes in the agencies. Within the engagement with Eliahu Insurance regarding the absorption of new business in general insurance, as set forth in Clause 3.1 to Part A above, as of January 1st, 2013, approx. 40 employees were absorbed in the General Insurance Division.

49.3 **Employment agreements**

The work relations between the Group and its employees are based on personal work agreements, except for few employees of Migdal Makefet, to whom a collective agreement applies.

The work agreements define their terms of employment, including basic salary, social benefits and ancillary benefits.

The Group is comprised of several employee groups, mainly supervisors and salespersons and some of the investment staffs in MCM Group, who are remunerated beyond the basic salary, also by salary derived from performances or in accordance with compliance with objectives and subject to the Law.

49.4 **Policy and principles for the remuneration of Senior Officers in the Company, Senior Officers and Managers in the Group's institutional organs as well as investments employees in institutional organs who are entitled to a variable component derived from performance**

49.4.1 During August 2010 the Company's BoD adopted a policy for Senior Officers of the Company, Senior Officers and Managers in the institutional organs[100], as well as for investment employees in institutional organs who are entitled to a variable component that is derived from their performance ("**plan participants**" or "**participant**" or "**Senior Officers in institutional organs**"), inter alia, pursuant to the instructions of the Commissioner of the Capital Market, Insurance and Savings as regards the Remuneration Policy of Senior Officers in Institutional Organs, dated November 29th, 2009 (Institutional Organs Circular 2009-9-24) ("**the Commissioner's Circular**").

49.4.2 Based on the remuneration policy and principles ("**policy**" or "**remuneration policy**"), as set forth by the Company BoD and also approved by each of the BoDs of the Group's institutional organs, annual remuneration plans will be set and approved individually every year by the relevant company BoD, as the case may be. It was clarified that the remuneration policy does not bind the BoD to set a remuneration policy, and at any time it may instruct conducting bonus calculations that are not detailed in the plan, or decide that no bonus shall be paid as per the plan, and it also may instruct changes or cancellations or suspensions of any plan, as determined by the Company BoD and under the conditions that were determined both in the policy and in the relevant plan.

49.4.3 The remuneration principles reflect the BoD emphases aimed at securing the existence of an appropriate balance between the desire to give incentives and preserve the plan participants and the need that the remuneration principles comply with the benefit of insureds, beneficiaries and savers and with the Group general strategy, as required in the Commissioner's Circular. The BoD emphases are expressed in the remuneration principles as follows:

[100].The institutional organs in the Group include Migdal Insurance, Migdal Makefet and Yozma, and for this Clause (Human Capital), also Migdal Technologies Ltd. and Migdal Claims Management Ltd. In this Clause, wherever institutional organs are mentioned, this means all the companies set forth in this Note.

(a) Adjusting the remuneration principles to the Group's financial situation and its long term targets - the remuneration principles include overall budget limits as well as personal caps for participants for whom the remuneration principles apply, both regarding cash remuneration and remuneration in Company shares. Furthermore, the remuneration principles include powers that are aimed at allowing the CEO and BoD managerial flexibility to deviate from the plan's provisions, all or part, due to discretions stemming from the benefit of the Company and Group.

(b) The remuneration principles should reflect the contribution of the unit in which the participant is employed, to the Group activity and results, in a way that is not disconnected from the Group in general - the remuneration objectives included under the remuneration principles are divided into objectives in various levels in the Group: (a) objectives related to the institutional organ's level; (b) objectives related to the area in which the participant is employed; (c) objectives related to the participant himself and his work.

(c) The remuneration principles should take into account a suitable balance between the bonus and the fixed component, in order to make sure that the bonus does not create conflicts with the institutional organ's interest – the remuneration components are limited by a cap set forth in the number of target salaries, which maintains a connection between the fixed component and the variable component. Thus, all remuneration components have personal caps. Finally, the Board of Directors has a managerial flexibility that allows deviating from the provisions of the plan under adequate circumstances.

(d) The remuneration principles should examine the performance of participants, both in reference to a pre-determined level of performance and a pre-determined level of risk – the remuneration principles include several components in order to prevent risks, in addition to the means of control that already exist in the organization. These components include imposing a bonus cap on an individual level as well as an overall budget cap, absolutely and as a function of Company performance. Besides the above, in the Investments Discipline there are performance indexes over a measurement period of three years that encourage achieving performance over time and not taking risks in order to achieve short-term performances.

(e) The remuneration principles should examine the performance of participants from a long-term perspective – the remuneration principles include, for participants in the Investments Discipline, measurement periods of three years for the most significant objectives as far as their weight is concerned.

(f) The remuneration principles will refer the minimal holding period of shares that the participants receives as part of remuneration, the long-term remuneration principles include a minimal holding periods of three years.

(g) The remuneration principles should examine the participants' performance also in relation to non-financial criteria – within the remuneration principles, inter alia, non-financial criteria such as an innovation index and service index, were adopted. Also, this is reflected in the manager's evaluation component within the short term remuneration plan, that includes reference to subjective and qualitative indexes such as initiative, innovation, management quality, loyalty to the organization, determination, personal progress, team work, interpersonal relationships, etc.

(h) The remuneration principles should include components that would provide managerial flexibility for addressing unusual circumstances in the Group activity - for this purpose, the remuneration principles include provisions that allow the Company management and/or the BoD to instruct a partial or full deviation from the remuneration policy, both for future plans and for current plans that apply to the Group. Also, the CEO received special authorities, both for reducing the grants to certain participants or a certain type of participants under the appropriate circumstances and under the limits set forth in the plan, as well as giving a special grant to a certain participants, subject to the Law.

49.4.4 The institutional organs' remuneration policy is published in Migdal Insurance's website, pursuant to the provisions of the Commissioner's Circular.

49.4.5 Pursuant to Amendment No. 20 to the Companies Law, the Company is examining the current remuneration policy as well, however, as of the date of this Report, no decisions were made yet.

49.5 **Annual grants for 2012**

49.5.1 Based on the remuneration principles as set forth in Clause 49.4.3 above, in March 2012 the Company BoD approved a bonus plan (annual grant) for 2012 for the plan's participants. The plan's participants include the CoB and CEO. For details regarding the remuneration plans approved for the plans' participants in 2012, see Clauses 50.8, 50.9 and 50.10 to the 2011 Periodic Report.

49.5.2 In March 2013 the Company BoD approved the granting of grants to the 2012 plans participants pursuant to the Company's results in compliance with its objectives set forth in the plan, and the grants to the CoB and the CEO in respect of 2012 were also approved, and the component in respect of the BoD discretion is subject to the Company's GM approval, see Immediate Report of the Company issued on March 19th, 2013, Reference No. 2013-01-011146.

49.5.3 Within the implementation of the 2012 plan, and in light of the cap set forth for annual grants in the plan, the annual grant was truncated by 15% across the board for all the Company's managers and employees in the Group's institutional organs, in order not to deviate from the bonus cap.

49.5.4 Accordingly, the bonus budget for the other employees in the institutional organs (not included in the plan) was derived, and it is mainly adjusted to the components of the position, personal performance and personal potential.

49.6 **Long term remuneration (including option allocation**)

On August 24th, 2010 the 2010 long term remuneration plan for Senior Officers and employees, including the Company's CoB and CEO, was approved, see the Company's Immediate Report dated August 25th, 2010, Reference No. 2010-01-598449. For additional details regarding the aforesaid remuneration plan as well as the option plan for Senior Officers and employees that were issued in previous years, see Note 33 to the Financial Statements.

In 2011-2012 no long term remuneration plans were approved.

49.7 **Senior Officers (not Directors)**

As of the date of this Report, the group of Senior Officers (who are not Directors) in the Group comprises 26 employees ("**Senior Executives**"), and it includes Executive Senior Officers detailed above.

The Group's Executive Senior Officers[101] are also employed under personal contracts detailing their terms of employment.

Often, Senior Officers and Senior Managers are entitled, under such contracts, to an adaptation grant which usually amounts to between 3 to 6 monthly salaries beyond the early notice period.

Some managers in the Group's Senior Managers have different and additional arrangements, stemming from various circumstances related with historic agreements or unique circumstances of recruitment and employment.

For additional details regarding the wages and remunerations in respect of 2012, including the terms of employment of the highest wages earners among the Executive Senior Officers of the Company and corporations controlled by it (including the Group CoB and CEO) and the remuneration paid to Directors in the Company, see Regulation 21 in "Additional Data on the Corporation".

49.8 **Insurance, exemption and indemnification arrangements**

For details regarding the exemption, insurance and indemnification arrangements in the Company, see regulation 29 a in "Additional Data on the Corporation ".

49.9 **Training and organizational development**

The Group invests many resources in professional training for employees and agents according to their position and the discipline in which they work, and it operates based on an organizational training and development program, which supports obtaining the Group’s goals in all organizational units on an ongoing basis and with agility, according to needs, and inter alia, sends its employees and agents to professional courses, conferences and relevant training.

The Group has plans for the promotion of the managerial and professional channel, as well as short "greenhouses" suited for new employees in the LTS array, and development of a variety of programs for the various managerial levels, which are training and qualification programs adjusted to the Group's professional needs. Also, from time to time, the Group holds enrichment workshops for Group employees regarding various issues.

50. Marketing and distribution

50.1 **General**

The Group's main marketing and distribution channels in the areas of insurance and LTS (excluding the area of financial services and the marketing and distribution in the area of financial services, see Clause 38 to Part C above) are as follows:

[101] Since 2010 the Group classifies its managers as "Senior Officers" its managers in the Company and institutional organs in the Group under the Companies Law, managers titled Assistant to CEO who actually report to the CEO. Furthermore, the classification includes managers whose position in terms of contents and materiality, including regarding institutional organs in consolidated companies as per the legislative arrangement that applies to them, positions that require reporting to the CEO or regarding whom there are regulatory provisions indicating that their position, as far as materiality is concerned, are "Senior Officers". On the other hand, managers titled Assistant to CEO who do not actually report to the CEO, whose position in terms of contents and materiality does not suit their title, no longer fall under the category of those considered "Senior Officers" in the Company as per the Companies Law, in light of reviewing the contents and materiality accompanying the types of positions fulfilled by the managers. The above mentioned classification had no implication on the managers included under "the Corporation's Executive Senior Officers", as detailed in Regulation 26 a in "Additional Data on the Corporation".

50.1.1 **Insurance agents and agencies / pension marketing agents**
This activity includes the activity of insurance agencies controlled by Migdal Agencies.

50.1.2 Directly through its workers, mainly in the area of pension and provident, through the Customers and Distribution Channels Division, in general insurance businesses, via a unit specialized in marketing to large businesses (CRD), as well as via the Company's website through which motorcar insurance and travel insurance are offered.

Migdal Agencies includes Ihud Agency, which performed the activity of a call center ("Ihud Direct"), that mainly offered CMBI, casco and homeowners insurance. After the date of the Financial Statements, it was decided to discontinue the telephone sales activity for motorcar and homeowners insurance, and it is suggested to customers to renew insurance via other insurance agents who work with the Group, including in-house agencies.

50.1.3 Banks – distribution and joining through pension advisors in the bank branches, regarding pension and provident products.

The Customers and Distribution Channels Division also concentrates, manages and operates the Group's various distribution channels.

The Group continues to provide life assurance and building insurance to mortgage bank debtors. The Group has engagements with insurance agencies held by banking corporations, regarding the marketing of insurance policies with mortgage loans.

Insurance agents and agencies
The Group's main marketing and distribution activity is currently conducted through insurance agents and insurance agencies (pension marketers as to pension products, and insurance agents as to non-pension products).

The Group has business relations with about 1,800 insurance agencies (corporations[102]) and insurance agents ("**agents**") around the country. The Group is engaged with most agents in life, pension and provident insurance business, health and general insurance business, and they conduct most of the Group sales. Most agents are not exclusive and also work with other insurance companies.

From time to time, the Group provides training to agents, including organizing various conferences and functions. Under this framework, it also provides professional and technological training sessions and technological tools that assist them in their activity.

Part of the Group's marketing and distribution activity in the areas of insurance and LTS takes place through Group-controlled insurance agencies, as cited hereinafter.

50.2 **Distribution and marketing through Migdal Agencies**
Migdal Agencies is a subsidiary of Migdal Insurance and it concentrates the holding of insurance agencies in the Group. The Group's insurance agencies operate in the Group's areas of insurance and LTS, and some of them specialize in specific insurance lines.

Mivtach Simon, Sagi Yogev and Shaham are insurance agencies that concentrate the marketing and distribution activity in the area of life assurance and LTS and health insurance, while Peltours concentrates the marketing and distribution activity in the area of general insurance.

[102] Some insurance agents are corporations employing workers, and the workers of these insurance agencies or agents are not included in the figure stated above.

These agencies also work with other insurance companies apart from the Group.

Furthermore, some of the in-house agencies have technological means, through which they allow the transfer of financial transactions between the customer (end/employer) and pensionary producers, including the transfer of information between these entities.

Migdal Agencies also holds B-Diyuk Pension Arrangements Operation Insurance Agency Ltd., aimed at concentrating the Group agencies'[103] operation arrays and expanding their database infrastructures services.

The premiums received in 2012 from the Group's agencies (including data regarding these agencies' sub-agents) are as follows: 31.2% of the total **life assurance** businesses (vs. approx. 31.8% in 2011), approx. 29% of the total **pension** businesses (vs. approx. 33% in 2011), approx. 25.9% of **health** businesses (vs. approx. 22.5% in 2011) and approx. 10.6% of **general insurance** businesses (vs. approx. 9.5% in 2011).

For details regarding the manpower quota in Group agencies, see the Table in Clause 49.2 above.

50.3 **Regulation of agents / pensionary marketers / pensionary advisors**

Agents' activity is also supervised by the Commissioner of Insurance, and the provisions of the Insurance Contract Law, the Supervision Law and the Marketing and \Advice law (related to pensionary products), apply to their activity as well. The Supervision Law requires the existence of a written engagement agreement between the insurer and the insurance agent.

Insurance agents must keep the insurance fees collected from the insureds in a separate account until they are transferred to the insurer, and provisions were set as to the dates upon which insurance agents must transfer such monies to insurers.

The granting of loans and advance payments to agents by the insurance companies is also regulated in regulations and circulars, and among other things, the provisions set restrictions as to the granting of loans to agents, including the supervision of insurers' Nostro Investment Committee on the granting of such loans.

51. Fixed assets and facilities

The Group's fixed assets include land and office buildings, computers and software, vehicles, equipment, office furniture and leasehold improvements. For further details see Notes 4 and 6 to the Financial Statements. Following is a description of the Group's main fixed assets:

51.1 **Real estate – office buildings**

Total amortized cost of land, office buildings and leasehold improvements as of December 31st, 2012 amounted to approx. NIS 627 million vs. approx. NIS 533 million as of December 31st, 2011. The increase in cost is mainly due to the continuation of the project for building office buildings in Petach Tikva, mentioned hereinafter.

Following are details regarding the Group's main office buildings:

[103] In July 2011 the shares of this company, which were fully owned by Mivtach Simon, were transferred to Migdal Agencies.

Petach Tikva

The Group focuses most of its activity in one main geographical site in Petach Tikva. The Group owns four office buildings in Kiryat Aryeh, over a total office surface of approx. 49,000 square meters (vs. three office buildings with a total surface of approx. 24,000 square meters in 2011). During the reported period, the Group completed the population of the fourth building, and most of the activity of insurance agencies controlled by the Group (the fourth building includes a surface that has not been completed nor populated yet, of approx. 16,000 square meters). For additional information regarding the amounts invested in the land and office buildings in the Group, see also Note 6 to the Financial Statements.

The Group also rents, from third parties, other office areas in Petach Tikva of approx. 9,800 square meters and approx. 650 square meters of warehouses in proximity to its owned buildings.

Tel Aviv

The Group has an overall office area of approx. 5,500 square meters, located in Sa'adia Gaon Street in Tel Aviv, which are leased to the Group in a long term lease. Migdal Capital Markets Group has been using this building since January 2008.

Jerusalem and Haifa

The Group has office buildings in Jerusalem and Haifa, where its branches are located.

51.2 **Data regarding building surfaces that are part of Migdal Insurance's Nostro investments portfolio**

Location	**Square meters as of December 31st, 2012**	**Square meters as of December 31st, 2011**
Dan area	31,873	31,223
North of Israel	34,859	34,859
South of Israel	135	370
Lowland	3,604	3,604
Total	**70,471**	**70,056**

The above mentioned buildings mainly serve as office and commerce buildings.

In addition, Migdal Insurance holds real estate assets from monies managed for insureds, for additional information see Notes 8 and 39 to the Financial Statements.

51.3 **Computer systems and software**

The Group has information systems that include hardware, software and additional equipment, whose amortized cost as of December 31, 2012 totals approx. NIS 421 million[104] , vs. approx. NIS 403 million as of December 31st, 2011.

In 2012, the Group invested approx. NIS 164 million in computers, software and information system development, vs. approx. NIS 170 million in 2011. In 2012, the Group's total current computerization expenses amounted to approx. NIS 322 million vs. approx. NIS 271 million in 2011, see Notes No. 4, 6 and 31 to the Financial Statements.

[104] The Group's assets include computer systems comprised of hardware and software. Programs that constitute an integral part of the hardware, which cannot operate without the installed software, are classified as fixed property. However, licenses for stand-alone software which adds additional functions to the hardware, are intangible property

Migdal Technologies serves as the internal information technologies unit, and provides most of the various computerization services to the Group's different units and operates, whenever needed, various suppliers and software companies in order to provide the Group's computerization services.

The Group's main computer room is located in a secured underground site in Petach Tikva, of MED-1 Company. The Group also has a DRP backup site abroad, which is run by a Generali-controlled company. Within the BCP project for the construction of another back-up site in Israel that would allow RPO (Return Point Objective) of up to 4 hours and RTO (Return to Operation) of up to 24 hours, the Group engaged with MED-1 for the establishment of a back-up site in Tirat Hacarmel, and it also engaged with various suppliers / service providers in order to execute and complete this project.

The Group also intends to move the Group's main computer room, which is currently located in MED-1's site, to the office buildings in Petach Tikva, as part of the aforementioned project.

The Group's key systems are as follows:

Core systems: the activity in life assurance and LTS is mainly managed through the Life 2000 operational system and the procedural system BPR/BPM. These systems manage policies, benefit agreements, underwriting, collection, surrenders, claims, commission payments and other subsystems for insureds/beneficiaries management. The activity in general insurance is mainly managed in the AS-400 system. In this system, too the policies and collection processes, claims etc. are managed. The provident activity is mainly performed through designated systems whose services are obtained from third party vendors (outsourcing), Data Warehouse (DWH) systems, SAP system (mainly serving the Group's financial systems and for managing additional activities, including procurement and HR and wages management), investment management systems (back and front office), an annuity payment system, including the interface between them and external interfaces, see Clause 15 to Part C above.

Key ancillary systems: agents agreements system, CRM, CALL CENTER systems, proposal generator (in life assurance), document management system, system for managing and operating policies and payments to Third Age insureds, payroll payment system and Intellinks system for the supervision and control over the execution of operations in IT systems.

The Group is working on developing and upgrading its computerization systems from time to time, according to its needs and the needs of the Group companies, including the need to meet regulatory instructions from time to time.

52. Seasonality

52.1 LTS

Revenues from life assurance (as well as health insurance premiums), and revenues from management fees from pension funds and provident funds are not characterized by seasonality. However, because of the timing of the tax year, there is a certain seasonality in deposits from premiums / contribution fees to pensionary savings products in December, since in this month significant amounts are deposited in order to exhaust tax benefits.

Following is the breakdown of the quarterly gross premium earned in life assurance in 2010, 2011 and 2012 (in NIS million and percent):

	2012		2011		2010	
	in NIS million	In percent	In NIS million	In percent	in NIS million	In percent
First quarter	1,804	24.5	1,694	24.7	1,502	24.1
Second quarter	1,763	24.0	1,722	25.1	1,489	23.8
Third quarter	1,899	25.8	1,683	24.6	1,540	24.7
Fourth quarter	1,891	25.7	1,748	25.6	1,714	27.4
Total per year	**7,357**	**100**	**6,847**	**100**	**6,245**	**100**

Following is the distribution of the quarterly contribution fees in pension in 2010, 2011 and 2012 (in NIS million and percent):

	2012		2011		2010	
	in NIS million	In percent	In NIS million	In percent	in NIS million	In percent
First quarter	1,030	23.5	901	23.0	774	22.6
Second quarter	1,102	25.1	942	24.0	845	24.7
Third quarter	1,065	24.3	1,007	25.7	839	24.5
Fourth quarter	1,189	27.1	1,068	27.3	960	28.2
Total per year	**4,386**	**100**	**3,918**	**100**	**3,418**	**100**

Following is the distribution of the quarterly contribution fees in provident in 2010, 2011 and 2012 (in NIS million and percent):

	2012		2011		2010	
	in NIS million	In percent	In NIS million	In percent	in NIS million	In percent
First quarter	392	22.2	376	22.3	357	21.9
Second quarter	385	21.8	361	21.4	338	20.8
Third quarter	386	21.9	366	21.6	330	20.3
Fourth quarter	602	34.1	586	34.7	602	37.0
Total per year	**1,765**	**100**	**1,689**	**100**	**1,627**	**100**

52.2 **General insurance**

Revenues turnover from gross premium in general insurance are characterized by seasonality, which stems mainly from motorcar insurances of various employees groups and businesses' vehicle fleets, whose renewal dates are usually in January, as well as different businesses' policies, whose renewal dates are usually in January or April. The impact of such seasonality on the reported profit for the period before tax is mostly offset through the reserve for unexpired risks.

In the other expenses components, such as claims and other income components, such as revenues from investments, there is no significant seasonality, which is why there is no profit-significant seasonality. However, it should be mentioned that a harsh winter may bring about an increase in claims, mainly in the casco line, during the first and fourth quarters of the year, which in turn, leads to a reduction in the income for the period before tax.

In this context, it should be noted that in January 2013 there was a storm that caused damages estimated at approx. NIS 30 million in gross terms and approx. NIS 10 million in terms of retention.

Following is the distribution of the quarterly gross premium in general insurance in 2010, 2011 and 2012 (in NIS million and percent):

	2012		2011		2010	
	in NIS million	**In percent**	**In NIS million**	**In percent**	**in NIS million**	**In percent**
First quarter	478	34.0	491	34.0	476	33.9
Second quarter	369	26.2	382	26.4	400	28.6
Third quarter	306	21.8	310	21.5	285	20.3
Fourth quarter	253	18.0	262	18.1	242	17.2
Total per year	**1,406**	**100**	**1,445**	**100**	**1,403**	**100**

52.3 **Financial services**

The Company estimates that the entire area of finances is not characterized with seasonality.

53. Intangible assets

53.1 **General**

For its activity, the Group uses the companies' names and logos, part of which were not registered as trademarks.

53.2 **Data warehouses**

The institutional organs in the Group have various registered data warehouses, within which the data submitted by the Group's customers are saved. The data stored in the warehouses, regarding customers, includes data submitted by them when acquiring one of the Group's products, as well as additional data submitted to the Group, or located by the Group in relation with services it provides (such as information about handling insurance claims etc.). Furthermore, the institutional organs in the Group have registered data warehouses regarding the Group's agents, suppliers, Group employees etc., whose storage and registration in a computerized repository are mandatory by law. The databases serve the Group in the current operation of its businesses.

53.3 **Goodwill and cost surplus**

The Company accumulated goodwill and cost surplus, mainly upon the acquisition of insurance companies, insurance agencies, insurance portfolios, managing companies of pension funds, training funds and activities of mutual funds at a total net sum of about NIS 922 million, which are mainly ascribed to insurance portfolios and goodwill. For further details see Note No. 4 to the Financial Statements.

54. Legal procedures

54.1 **Legal procedures and others**

Against the Group there are pending material legal procedures, including class actions as per the Class Actions, as well as pending requests for approving claims as class actions. For information regarding pending material legal procedures against the Group, including requests for approving claims as class actions, including claims that have been concluded, see Note 39 to the Financial Statements.

54.2 **Large damage claims that have not reached legal procedures**

In 2012 there were no large damage claims that have not reached legal procedures.

54.3 **Rulings and rulings in principle regarding complaints/audits/data requests/fines - the Commissioner of Capital market, Insurance and Savings in the MoF**

From time to time, complaints are filed against the Group, including to the Commissioner. These complaints are handled on an ongoing basis by the Group's Ombudsman. The Commissioner's rulings on such claims, if and insofar that a ruling was made in their respect, are sometimes made, and in recent years, even more so, as across-the-board rulings as to a group of insureds. Before publishing the final wording of the ruling, the Commissioner submits the draft ruling to the Company, in order to hear its arguments.

Furthermore, under the supervision over insurers and managing companies in the area of insurance and LTS, from time to time the Commissioner conducts audits and/or examinations on his behalf in the Group's institutional organs, and/or conducts examinations and/or requests for receiving data. Under this framework, he sends requests and/or gives instructions regarding the Group's handling of various products, including instructions as to reimbursements, as well as instructions and/or provisions related to various operations performed by the institutional organs, including instructions for the correction of various actions.

Within these audits, and pursuant to the findings included in the audits that were performed and/or the data that were transmitted and/or will be transferred to it pursuant to his requests as set forth above, and if the Commissioner estimates that there was a breach, he imposes a fine under the administrative enforcement. Before imposing the fine, the Commissioner informs the institutional organs about his intention to impose a fine, and they are given the opportunity to express arguments against this intention.

In the Group there were several examinations/audits regarding various issues, including the management of insureds/beneficiaries rights in the pension fund Makefet, information security, corporate governance (institutional evaluation), actuary, Financial Statements, risk management etc.

Regarding corporate governance (institutional evaluation), in October 2012, after the Company submitted its opinion regarding the draft report on this matter, the Company received an audit report that includes a Chapter regarding the BoD and a Chapter regarding the Company's Internal Audit Array. Pursuant to the letter that accompanies the aforesaid report, corporate governance processes in the Company are implemented properly, except several findings detailed in the report regarding the Company's policy, the internal structure and working processes, and execution instructions were attached. The Company is striving towards improving the processes and implementing the recommendations, and it is negotiating with the Commissioner issues whose implementation it requested to postpone.

In February 2013, a fine in the amount of NIS 150 thousand was imposed on the managing company Migdal Makefet, following audit findings regarding the issue of beneficiaries' rights. For additional details on this matter, as well as regarding draft rulings in principle, see also Note 39 to the Financial Statements.

55. Financing

The Group finances most of its activity from its own resources. From time to time, the Group takes credit, mainly short term and long term banking credit.

Total short term and long term loans and credit as of December 31st, 2012 are approx. NIS 941 million vs. approx. NIS 237 million as of December 31st, 2011. The increase in the scope of loans is mainly due to a second tier capital raising via two private issuances to classified investments during 2012, less the current payment of long term and short term loans by the Group's companies.

Following is a specification of the denominated average interest rate on loans and credit received from banking sources, in various dates in the past, which were valid during the reported period:

	Short term loans	Long term loans
CPI-linked		3.70% (1)
Non-linked, variable interest		5.33% (3)
Forex linked, variable interest	1.97% (2)	

(1) Within the merger of the managing companies in the area of provident funds in January 2011, two loans from Bank Hapoalim that were taken in the past for the acquisition of Kahal's raining funds were assigned to Migdal Makefet. As of December 31st, 2012 the balance of loans is approx. NIS 34 million. The last loan payment will be in July 2013.
(2) Credit limits taken from time to time, mainly by Migdal capital Markets for its current activity, most amounts are CPI-linked. The balance as of December 31st, 2012 totaled approx. NIS 28 million.
(3) Loans in non-material amounts that were taken by the Group's subsidiaries.

Following is a specification of the denominated average interest rate on loans and credit received from non-banking sources, in various dates in the past, which were valid during the reported period:

	Short term loans	Long term loans
Second tier capital raising		3.05% (1)
Other loans		4.2% (1)

(1) For details regarding the second tier capital raising that was performed via two private issuances to classified investments, the terms of bonds and the trust deed, see Note 24 e to the Financial Statements.
(2) A loan extended by Ramat Aviv Mall to Migdal Real Estate Holdings Ltd. see details in Note 38 j 3 to the Financial Statements.

The New Investment Rules state that institutional investors and insurers should hold an asset only if their right in it is an ownership right, their control of it is entire, and the asset is not under any pledge or mortgage, except if otherwise permitted in the said Rules.

One of the subsidiaries which is not an insurance company, undertook to several banks to be pledge-negative, and this company pledged assets for a bank that provides it with clearing services regarding Maof activity. For details regarding pledges and guarantees see Note 39 2 f to the Financial Statements.

For further details regarding the loans and credit received by the Group, see Note 24 to the Financial Statements.

For further details regarding the equity required in institutional organs in the Group, see Note 7 e to the Financial Statements.

56. Taxation

For a description of the tax arrangements applied to the Group including tax rate changes, line-based agreements, tax assessments, reservations etc., see Note 21 to the Financial Statements.

57. Objectives and business strategy

The business environment and the increasing competition require the Company to examine, from time to time, its thinking and deployment as to its objectives and business strategy. The material changes, which came into effect in January 2013, which are the annuity coefficients reform and the management fees reform, as described in Clauses 9.2.8 and 9.29 to Part C above, affect the Company's main area of activity, which is LTS.

As a result of this changing reality, the Company's main strategic objectives are:

Preserving and strengthening the Group's status as a leading entity in the area of life assurance and LTS.

Maintaining good profitability over time, along with strengthening the general insurance arm. Constant improvement in customers' loyalty and satisfaction and distribution channels.

In order to maintain good profitability, the Group will diversify profit sources, will examine the insurance sales mix in order to improve profitability, will improve operational efficiency and resource management, and investment management that allows providing yields along with adjustment to the risk level.

In order to diversify the sources of profit, the Company will strive towards expanding its activity in the area of health insurance, by absorbing and implementing the new business in general insurance in the Company's activity, while trying to improve profitability in this area, expanding its activity in the area of health insurance, as well as expanding its activity and profitability in the area of financial services.

In addition, the Company will try to develop non-insurance activities in areas that are related to quality of life, health services and Third Age, including all their aspects, in order to diversify and balance the Group's sources of profit, including via cooperations with various entities dealing with the area and/or with these activities. The Company considers the population of insureds after the age of retirement (the Third Age) and its various aspects, as a developing market.

The Company is working for a constant improvement in customers' loyalty and satisfaction and distribution channels, that will be achieved via leadership in the service provided to customers and to distribution channels and via deepening customer shares.

In order to deepen the customer share and increase profitability, the Group will emphasize the creation of a platform, through which it will be able to create a long term basis for its relations with the end customers, inter alia by focusing on the end customers, deepening and strengthening the relations with them, providing solutions to customers and their families in all Group's activities, including preserving the life assurance and LTS portfolio and surrender prevention and policies cancellations, developing adequate products and services in various areas in which the Group operates, utilizing synergies between the Group's various activities and products, expanding the relations with customers and improving the customer's experience, all the above in order to provide them with value and increase their loyalty, as well as increase the Group's profitability both at the product and customer level.

Adjusting the distribution systems to the leveraging of selling abilities and customer persistency in the Group, along with adjusting sales incentives and building tools for the examination of profitability, that would allow it to make educated decisions in order to make profits.

The Company continues to strive towards achieving good yields for insureds and beneficiaries, along with adjustment to the risk level. For this purpose, the Group strives towards diversifying its investments, including expanding the investment activity for foreign markets and deepening investment in channels that would record, according to the Group, yield in excess, inter alia, in the areas of real estate and credit.

The Company will continue to act towards improving computerization systems and continue strengthening the control arrays, in order to improve the service and information extended to customers, regarding the various Group products, and support the portfolio persistency and sales abilities.

The continued implementation of the brand strategy, in order to position Migdal Group as the leading group in the area of LTS, offering a comprehensive array of solutions for pensionary savings and the implementation of the digital strategy for leadership in providing information and solutions via digital means to customers, agents, advisors in banks and employers, including supporting digitation of distribution channels and social networks.

The information included in this Part includes future forecasting information, and reflects the Group's estimates. These estimates are based, inter alia, on all the facts and data detailed in this Part. Actual results may be different from estimates in a material way due to changes that will occur in any of the aforesaid facts and data, and/or as a result of changes that may occur in the risk factors applicable to the Group in general, detailed in Part G hereinafter.

Part F – Corporate Governance[105]

[105] This Part and the description and data included thereof refer to Migdal Insurance only, and are brought pursuant to the Commissioner Circular regarding Corporation Businesses Description, Reference No. 2007-1-1.
For the attachment of the corporate governance questionnaire pursuant to the ISA's instruction as per Clause 36 a (b) to the Securities Law, see "Additional details on the Corporation – corporate governance questionnaire".

58. Number of BoD meetings in Migdal Insurance[106]

As of the date of this Report, Migdal Insurance's Board of Directors comprises 8 Directors, 3 of whom are External Directors. As of October 29th, 2012, Migdal Insurance BoD comprises 7 Directors, 3 of whom are External Directors.

In the reported year, 17 BoD meetings were held in Migdal Insurance. Following are data as to the BoD meetings held in 2012:

Meeting dates	No. of participating Directors
24.1.2012	4
21.2.2012	7
26.3.2012	6
24.4.2012	6
6.5.2012	6
29.5.2012	7
12.6.2012	6
3.7.2012	6
18.7.2012	6
1.8.2012	7
13.8.2012	5
13.9.2012	4
18.10.2012	6
8.11.2012	8
11.11.2012	6
27.11.2012	8
18.12.2012	8

59. Information regarding investment committees and committees next to the BoD

59.1 Investment Committees

59.1.1 Statutory Investment Committees (Profit Participating and Nostro)

In Migdal Insurance, the following Investment Committees were established:

Profit Participating Committee – a Committee for the investment of monies in order to cover yield-dependent liabilities ("**Profit participating**" and/or "**yield dependent**"). This Committee comprises 5 members, 1 of whom is a Migdal Holdings BoD member, 3 members comply with the eligibility terms of External Directors, and 1 is not a BoD member complying with the eligibility terms for a representative in such a Committee.

Nostro Investment Committee – a Committee for the insurer's equity and the investment of monies in order to cover non-yield dependent liabilities ("**Nostro**"). This Committee comprises 6 members, 5 of whom are Directors, including 2 External Directors, and 1 is not a BoD member complying with the eligibility terms for an External Director.

The functions of the Investment Committee include: setting the investment policy of insurers within the overall investments policy set forth by the BoD, approving certain transactions and holding rates in certain securities prior to their execution, outlining rules and procedures for investments management, guiding position holders dealing with insurers' investments as to the implementation of the investment policy set forth in their resolutions, making decisions as to the use of control means in corporations held by

[106] As set forth in Note 105, the description and data brought in this Part refer only to Migdal Insurance.

insurers, and setting standards to review the implementation of the preset investment policy and its control.

In addition to the aforementioned functions of the Committees, the Nostro Investment Committee is in charge of setting procedures for granting loans to insurance agents and setting terms, in accordance with the conditions set forth in the Commissioner's circular regarding this matter.

The Commissioner Circulars regarding credit management expanded the functions of the Investment Committee, and accordingly, the Investment Committee must also refer to setting credit rates, setting maximum exposures limits for credit, setting policy and rules for assessing collaterals, setting mechanisms and rules for identifying exposures, setting rules for pricing credit, extending credit to related parties etc.

Pursuant to the Regulations of Ways of Investment, the Profit Participating Investment Committee must convene at least once every two weeks.

In 2012, 27 meetings of the Profit Participating Investment Committee were held in Migdal Insurance (including meetings in a telephone round).

Pursuant to the Regulations of Ways of Investment, the Nostro Investment Committee must convene at least once a month.

In 2012, 13 meetings of the Nostro Investment Committee were held in Migdal Insurance.

59.1.2 **Joint Credit Committee for institutional organs**

As described in Clause 46.1.1 in Part E above, an Investment Committee that manages assets exceeding NIS 5 billion, and whose scope of credit exceeds 15% of all assets under its management, must establish a Credit Committee. The main function of the Credit Committees is deliberating all credit transactions, as defined in the Commissioner's circular in respect of management of credit risks during investment activities and investments in non-negotiable bonds. In non-negotiable bond transactions, the Committee deliberates only transactions exceeding a certain amount or rated lower than a certain determined rating, according to an authority hierarchy set forth by the Investment Committee.

The Credit Committee may be joint for institutional organs controlled by the same controlling shareholder, as per the rules set forth by the circular.

Members of the Credit Committee must have proven expertise and experience in the credit field. People dealing with investment management or granting credit in the institutional organ cannot be members of the Credit Committee. The Credit Committee shall comprise at least two members eligible to serve as External Directors. Members of the Investment Committee appointed as per the Circular's restrictions may also serve in the Credit Committee.

In Migdal Insurance, the Credit Committee comprises 4 members, out of whom 2 Directors are considered as meeting the requirements for External Director eligibility, and it serves as a joint Credit Committee to the Profit Participating Portfolio Committee and the Nostro Committee in Migdal Insurance, and to Migdal Makefet's Investment Committee.

In 2012, 24 Credit Committee meetings were held (including via a telephone round).

59.1 **Audit Committee**

The BoD Regulations set issues that must be deliberated and decided by the Audit Committee, in addition to the Audit Committee roles as per the Companies Law.

The issues that the Audit Committee must deliberate, at the least, as per the BoD regulations are: appointing and replacing the CPA, CPA fees, determining other services rendered by the CPA which are not auditing, approving a document of authorities and functions of the internal audit array, recommending fees and remunerations for the Internal Auditor and the audit array employees, setting rules as to maintaining the independence of the auditing CPA and the Internal Auditor, the opinion of the auditing CPA as to the insurers' Financial Statements, deliberating on control and procedures in order to secure disclosure in the Financial Statements, the adequacy of insurers' Financial Statements, including the accounting policy, the integrity of disclosure and review of insurers' internal controls (the last three issues may be delivered for discussion in the Financial Statements Committee under certain conditions, and in Migdal Insurance they were indeed transferred to the Financial Statements Committee), the provisions of any law and professional and ethical rules that apply to insurers, its Senior Officers and employees, approving the internal audit array's annual WP, deliberating the reports submitted by the Internal Auditor and its findings, recommending to the BoD regarding actions required by the audit reports on behalf of the Commissioner, approval in advance of investments in related parties, approving conflict transactions, setting procedures regarding employees' complaints, etc.

The Chairman of the Committee and most of its members will be External Directors. At least half of the members of the Audit Committee will have accounting and financial expertise.

The number of members in the Audit Committee will not be less than 3. The Audit Committee must convene at least 6 times during a calendar year.

The Audit Committee in Migdal Insurance comprises 4 members, 3 of whom are External Directors.

In 2012 the Audit Committee held 26 meetings.

59.2 **The Committee for the Examination of FS (Financial Statements Committee)**

The role of the Financial Statements Committee is deliberating and making decisions mainly regarding the following issues: ensuring that Migdal Insurance Financial Statements are audited or reviewed as decreed by law, adopting or changing accounting principles and rules for the preparation of Financial Statements, deliberating on accounting handling that refers to Migdal Insurance's transactions in general, and to extraordinary transactions in particular, estimating significant uncertainties in any issue the auditing CPAs of the Company see fit to bring to deliberation within the deliberation on the Financial Statements' approval, recommending the approval of the periodic Financial Statements and any other report related to the Financial Statements requiring approval by the BoD.

Pursuant to the BoD regulations, the Committee for the Examination of Financial Statements may execute the functions of the Audit Committee regarding the auditing CPA's opinion as to the insurer's Financial Statements, deliberation on control and procedures to secure disclosure in Financial Statements, the adequacy of the insurer's Financial Statements, including the accounting policy, the integrity of disclosure and review of the insurer's internal controls, provided all the members of the Financial Statements Committee have accounting and financial expertise and all the External Directors in the insurer who have accounting and financial expertise are members thereof.

In Migdal Insurance the Committee for the Examination of Financial Statements comprises 5 members, 3 of whom serve as External Directors, and it convenes at least once every quarter.

In 2012 the Financial Statements Committee held 7 meetings, including one consultation meeting.

59.3 **Seniors Compensation Committee**

This Committee is joint for Migdal Insurance and Migdal Holdings.

The Committee recommends to the qualified institutions regarding fees and benefits for Senior Officers, including the CEO and other Executive Senior Officers. The Seniors Compensation Committee also deliberates the short-term and long-term remuneration policy.

According to the BoD decision, the Committee comprises 4 Directors, 2 of whom are External Directors, and the Chairman of the Board who serves as Chairman of the Committee.

The Committee convenes when needed.

In 2012, the Committee held 2 meetings.

On January 14th, 2013, the Company's Bod and Migdal Insurance's BoD decided to cancel this Committee.

59.4 **Solvency II Committee**

In accordance with the Commissioner's circular issued in July 2008 regarding the preparation for Solvency II, in September 2008 a BoD Committee was established, which authorized and responsible for supervising and controlling the preparation for Solvency II, on behalf of the BoD, and sets its form of work and its reports to the BoD.

This Committee comprises 4 members, of whom 2 serve as External Directors and the Chairman of the Board.

In 2012, the Committee held 2 meetings.

59.5 **Computerization Strategy Committee**

This Committee is joint and made up of both Migdal Insurance and Migdal Holdings. It was established at the end of 2008 and as per BoD resolution, and comprises 5 Directors, 2 of whom are External Directors, and the Chairman of the Board of Directors.

The Committee convenes when needed. In 2012 it held 7 meetings.

60. Compliance officer

In June 2012, Mr. Amir Pasternak was appointed as Migdal Insurance's Compliance Officer. Mr. Pasternak has an LL.B degree and MBA degree. Before he was appointed as Migdal Insurance's Compliance Officer, Mr. Pasternak served as Migdal Insurance's enforcement and regulation department for five years.

Mr. Pasternak is employed on a full-time basis as the Compliance Officer, and as of the date of the report, two full-time employees report to him. For some of the tasks included in the Compliance Officer's work plan, the Compliance Officer also employs external professionals depending on the kind and complexity of the activity.

61. Ethical code

Migdal Insurance adopted an ethical code, aimed at the world of values by which the Group believes it should act as an "ethical lighthouse" for the Group's business and organizational conduct.

The ethical code provides the Group's key values regarding its conduct towards the stakeholders with whom it interacts, such as customers, agents, employees, reinsurers, suppliers, shareholders, the regulator and authorities, competitors, community and the environment, and it refers, inter alia, to issues such as the prohibition of conflict of interests, the prohibition of utilizing business opportunities, fair competition, confidentiality etc.

The ethical code may not, and does not pretend to, encompass all the required rules of conduct, and does not replace nor derogate from the laws, regulations and procedures applied to the Group, but constitutes an additional layer that reflects the Group's ideology.

The ethical code is published in the Company's website as sell, and it was assimilated by employees.

Part G – Risk Management

62. Threats, weaknesses and main risk factors in the Group's activity

Several main risk factors affect the Group's profitability and stability as to its activity, which mostly includes the insurance activity and LTS, and the financial services activity.

Institutional organs are required to appoint a risk manager. For details regarding the main risks, description of the risk management procedures and methods (including the risk management array), risk management policy, work processes and risks and control identification and management, sensitivity analyses of market risks and insurance risks, see Note 37 to the Financial Statements.

This part of the report that deals with risk factors also includes future forecasting information. Future forecasting information is uncertain information regarding the future, based on information that exists in the Company at the time of the report, and all estimates of the Group or its intentions at the time of the report. The results in practice may be materially different from the results estimated or implied by this information.

63. Main risk factors in the insurance and LTS activity

63.1 Macro risks

Economic and employment condition – the employment level has a significant effect on the Group business in the area of life assurance and long term savings. Deterioration in the employment level, decline in the number of employeds, increase in unemployment rates and employees' salary decreases affect the scope of new sales and cancellation rates in the portfolio. In addition, the overall economic condition affects the Group business in its various areas of activity. Economic recession may lead to an increase in bad debts, an increase in PHI claims, a decrease in acquired covers in policies and an increase in fraud levels.

The economic and employment condition may affect the capital market, see hereinafter.

Market risks – a large part of the Group's asset portfolio is recorded as per fair value, which is determined by the capital markets various risk factors' prices, both locally and globally, and not as per the original yields that existed upon the acquisition. Capital markets are characterized by volatility as a result of political, economic and security events in Israel and abroad. These fluctuations affect the changes in the prices of the various risk factors on the capital markets (such as changes in interest affecting the value of bonds, the price of assets such as shares, commodities, real estate etc., inflation, exchange rates etc.), and, in turn, on the value of the Group's assets portfolio.

In light of the large volumes of reserves, invested in financial assets and others, changes in the yields embedded in the capital market and other investments in the market, both in Israel and abroad, have a critical effect on the Group's reported profit for the period and the value of the life assurance portfolio, due to the changes in investment income in Nostro portfolios, both in life assurance and non-life insurance, and to the impact of changes in investment income on the variable management fees in the profit participating portfolio. The decline of asset value against the profit participating policies, pension funds and provident funds also reduces the fixed management fees collected in these portfolios.

In most of the Group businesses, the asset duration is not compatible with the duration of liabilities, mainly in life assurance liabilities, as well as long-term health insurance, pension and provident funds whose duration of liabilities is significantly longer than the asset duration. As a result, the interest decline has an effect of reducing future yields upon refinancing assets against liabilities, and reducing the EV of the life assurance portfolio, as well as reducing the future yield of beneficiaries' monies.

In general insurance, the interest decline has an impact of reducing the profitability of products derived from reduced income from investments against the reserves.

For additional information concerning market risks, including market risks that are specific to the company, see Note 37 to the financial statements.

Credit risks – the Group invests some of its assets in granting credit to different corporations and borrowers and also in deposits. Non-compliance of its liabilities due to deterioration in its solvency, as well as a decrease in the value of the guarantees, including insolvency, has an impact on the Group's business results.

Credit assets granted from beneficiaries' monies, as well as negotiable credit assets in the Nostro portfolios, calculated by fair value, are also affected by changes in the credit spreads as reflected in the capital market or in the downgrading of the debtor's credit rating. In addition, the Group is exposed in its activity to other debtors such as employers and insureds. An increase in cases of Israeli businesses' insolvency may also affect the scope of employers' debts due to not making payments in respect of deposits to pension insurance for their employees, which requires institutional organs in the Group to take measures.

For further information as to credit risks of the Company's debt assets, see Note 37 to the Financial Statements.

63.2 **Sectorial risks**

Insurance risks – the Group insurance companies sell insurance policies that cover various risks, such as life expectancy risks (death before retirement age and longevity risk to annuitants after retirement age("l**ongevity**")), disability, disease (including LTC, occupational disability, as well as professional disease), fire, natural disasters (catastrophe events, such as earthquakes), theft, burglary, liabilities in respect of bodily damage etc. The pricing of the policy and the actuarial evaluations as to the Company's insurance liabilities, are mainly based on past experience and known legal and regulatory status. Any change in the risk factors, in the frequency and severity of events, and in the legal and regulatory status, may affect the Group business results.

The duty, since 2008, to deposit monies to an annuity track, the public's tendency to prefer an annuity track over a lump-sum track at the age of retirement affect the Company's exposure to life expectancy/longevity risk and changes thereof.

The annuity coefficients reform, as described in Clause 9.2.9 to Part C above, has implications and an impact on the structure of all pensionary savings products and the Group's profitability.

It should be noted that in 2012, in the area of life assurance and LTS, the demographic assumptions regarding life expectancy, longevity and future improvements thereof were updated, therefore the Company updated its estimates as to its annuity liabilities. Also, as a result, in January 2013 the marketing of new insurance plans that include a guaranteed annuity coefficient was discontinued, unless under the restrictions set forth by the Commissioner regarding this matter. For details see Clause 9.2.9 to Part C above.

For additional information regarding insurance risks, including updated estimates as to annuity liabilities, see Note 37 to the Financial Statements.

Life assurance and long term savings portfolio persistency level – the Company’s life assurance and long term savings portfolio is exposed to policy cancellations and surrenders, as well as to accrual mobilization. The portfolio persistency level is mainly affected by growth in the economy and level of employment, regulatory provisions and the level of competition between various channels of LTS products, and the level of competition between all organs engaged in this area, which is ever growing. The insurance portfolio persistency level, including the transition between the long-term saving types (life assurance, pension and provident funds) with different profitability rates, has a significant impact on the profitability of insurance companies, as well as the EV of companies' insurance businesses for the long-term. Since the marketing of new insurance plans with a guaranteed annuity coefficient was discontinued, as set forth above, the Company estimates that life assurance plans sold as of 2011, which include guaranteed annuity coefficients, shall be less exposed to cancellation and surrender risks – see Clause 9.2.12 to Part C above.

For sensitivity tests as regards changes in the cancellation rates, see Note 37 to the Financial Statements.

Reinsurance – the Group companies acquire reinsurances in international markets. Changes in the risk prices and reinsurances volumes offered in these markets affect the profitability of the companies.

Reinsurance does not exempt direct insurers from their duty towards their insureds under the insurance policies, which makes the Group exposed to risks derived from uncertainty as to the reinsurers' ability to pay their share in the insurance to the Group companies, therefore reinsurers' financial stability and solvency may affect the insurance companies' business results. The Group companies' exposure which are backed by reinsurance are to reinsurers that are rated relatively high internationally.

For details about the Company's exposure to reinsurers risks, see Clauses 14, 22, 30 and 47 above and Note 37 b to the Financial Statements.

Regulatory changes – the Group companies are subject to vast regulation in its areas of activity. Changes in the provisions of the law or regulatory instructions affect the content of the companies’ activities and marketing feasibility of the products they market, as well as the companies’ financial reporting.

Regulation in the insurance and LTS areas significantly affects the collected tariff, including the level of management fees collected in the different products and the companies' expense level. Law provisions, directives and agreements as to the structure of savings in the economy, mainly pension-related savings, including its taxing implications, bring about changes in the line's scope of activity and the changeability between the various products, including their mobilization options. Also, changes in legislation and regulation may affect the Company concerning products sold in the past, both through retroactive application and their impact on the interpretation of agreements entered before, and as far as competition is concerned. As a result, these provisions affect the life assurance and long term savings portfolio of the companies and their future sales.

In the reported year, the management fees reform was published in Clause 9.2.8 to Part C above, which affects the configuration of pensionary savings products and their profitability, see Clause 9.2.12 to Part C above.

In addition, insurance companies are subject to capital adequacy requirements. Regulatory changes in the capital requirements may affect the companies' activities and volume.

Under the Solvency II implementation procedure, insurance companies may be requested further equity enhancements. For additional information see Notes 7 e and 37 to the Financial Statements.

Furthermore, the Company's insurance agencies are also subject to regulation, including regulation regarding the holding of agencies by insurers, as well as duties imposed on pension marketing agents. Changes in the provisions of the Law which relate to the insurance agencies' activities, affect the agencies' activity and profitability.

Enhancement of Competition – an increase in competition level in the Group's areas of activity may harm its profitability. In the last decade, the Commissioner, in his regulations, has been leading moves towards enhancing competition in the area, both regarding the extent of changeability between products, and the management fees rate and structure, mainly in LTS. For additional details regarding the competition in the LTS area and the impact of the management fees reform, see Clause 16.2 to Part C above.

Change in public preferences – the public's tendency to choose alternatives to products of the various areas, or alternative products under the various areas, or the public's tendency not to acquire insurance, may affect the demand for the Group's products and profitability in the various areas.

Legal precedents and the Commissioner's authority to make rulings in principle – the Group companies are exposed to judicial resolutions, including in class actions filed against other organs in the line and against it, and semi-judicial rulings made by the Commissioner of Insurance under his powers to discuss insureds' complaints and/or conduct audits, which constitute a binding legal precedent regarding the Group's activity, affecting the Group's activity by changes in liabilities and/or the incurring of costs that were unexpected upon the engagement.

63.3 **Unique risks of the Group**

Business mix – the Group's activity mainly focuses on life assurance and LTS, which constitutes approx. 87% of the total insurance premiums and contribution fees. Changes in this mix of various lines in the area of LTS, in growth in one line at the expense of another line, in one line's profitability over another line's, including the changes in management fees, may materially affect the Group activity results.

For additional details regarding the reform in life assurance see Clause 9.2 to Part C above.

Liquidity risks – uncertainty about the date in which the company will be requested to pay claims, surrenders and accrual mobilization as to the scope of negotiable assets and cash available at that time.

Legal proceedings – institutional organs in the Group are a party to legal proceedings, including class actions, and rulings by the Commissioner by virtue of his authority to handle claims and/or perform audits, which may bring along charges of material amounts and/or Group handling of insurance / pension / provident plans differently than it used to in the past, including financial penalties imposed upon it.

Damage to goodwill – the goodwill and reputation of the Group constitute an important factor in the Group's engagement with new customers and preservation of existing ones. Damage to its reputation may materially impair the Group businesses.

Operational risks – the Group operates at large scopes in various areas, such as insurance lines, investments, actuary, large corporations insurance, activity vis-à-vis reinsurers, activity vis-à-vis insurance agents, activity vis-à-vis employers, etc., exposing the Group to operational risks, such as errors, computer failures, fraud and embezzlement from inside or outside the organization, computer crimes, including unauthorized access to information systems. Under the operational errors unique to insurance activity, one can mention the exposure to the following main risks:

- Errors that may occur in the adjustment of reinsurance coverage to coverage granted to insureds, especially in large insurances.
- Actuarial errors have a considerable effect on the adequacy of tariff and insurance reserves.

- There is high dependency of the insurance activity on the Company's computerized systems, computer crimes, including unauthorized access to information systems, information security, backup options and the ability to recover and maintain business continuity in case of disaster, have a considerable effect on the Company activity.

- Negligence or failures by its employees and/or third parties operating for it during their activities, as well as malicious actions that may lead to substantial volumes of claims against the Group.

- Fraud and embezzlement on the part of its employees, customers or third parties operating for or with the insurer during insurance activity.

63.4 **Table of risk factors of insurance and LTS activity**

		Level of risk factor's effect on Group activity		
	Risk factors	**Great effect**	**Medium effect**	**Little effect**
Macro risks	Economic condition and employment level	V		
	Market risks	V		
	Credit risks		V	
Sectorial risks	Insurance risks			
	- Longevity and morbidity	V		
	- Other insurance risks		V	
	Portfolio persistency level	V		
	Reinsurance		V	
	Competition & competitors	V		
	Public preferences	V		
	Regulation	V		
	Legal proceedings (class actions and Commissioner authorities)	V		
Unique Group risks	Business mix		V	
	Liquidity risks			V
	Legal proceedings, including Commissioner authorities		V	
	Goodwill		V	
	Operational risks			
	- Dependency on information systems	V		
	- Other operational risks		V	

The degree of impact of risk factors on the Group is based on the Group's management estimates considering its scope and features of activity as of the reported date. It is possible that in practice, the level of effect will differ, given changes that will occur to the Group activity features or market conditions and/or decisions made by regulatory entities.

63.5 **BoD estimate of the risk management quality**

Note 37 to the Financial Statements introduces additional information concerning the main risks and their specification, the legal demands, description of risk management procedures and methods, including the risk management array, risk management policy of the company, work processes and identification of risks in insurance companies, risk management control, sensitivity tests etc.

The risk management area in the Company follows multi-annual WPs approved in the company, including tools for managing different risks to which the Group is exposed and their controls, while meeting regulatory requirements and Group business needs. These actions for the promotion of risk management also assimilate in the Group preparedness for implementing Solvency II provisions in Israel, both the ones it has already executed and those it plans to execute upon implementing that directive. Therefore, the BoD believes, and given the content set forth in Note 37 to the Financial Statements and in this Chapter, the insurer's quality of risk management is reasonable under the circumstances and as per the regulatory demands and it continues to improve the control and supervision of the risk management.

As aforesaid, this part of risk management, including the Clause concerning the BOD estimate, refers to the insurance and LTS activity.

64. Main risk factors in financial services' activity

64.1 Main risk factors in financial services' activity

The financial services area deals with various areas of the capital market, some of which are characterized by high volatility, inter alia due to the impact of political and economic events in Israel and abroad. The various risks to which the financial services area is exposed are related to trading activities in the Nostro accounts managed by the area-related companies, to the scope of assets managed for various customers (mutual funds and portfolio management), to the activity of customers who receive brokerage services (including credit extended to them), to legal risks and additional risks related to legal, operational and external matters such as competition and regulatory changes.

For the description of exposure to market risks and the way they are managed, see Clause 23 to the BoD Report.

The main risks in the financial services' activity are:

64.2 Macro risks

Market risks – political and economic events in Israel and abroad affect the scope of activity on the capital market, and as a result, the activity of the financial services' area, its assets and business results.

Companies engaged in the financial services area perform their own transactions in securities, financial assets and Forex in Nostro accounts. These transactions expose the financial services area to risks stemming from trading fluctuations in the various channels of the capital markets (share rates, bonds, currency rates, interest rates etc.), including due to political, security-related and economic events. Activity in brokerage accounts – activity in brokerage accounts is performed only if a back-to-back transaction may be performed, with no inventory activity and without holding a position for a long time. Activity in these accounts is aimed at collecting the remuneration to which MCM's subsidiary Stock Exchange Services) is entitled, deriving from the spread between the execution of both transactions between the two counter parties in the transaction. The subsidiary operates brokerage accounts in foreign bonds and structured products, corporate and government bonds and shares.

A subsidiary of MCM (Migdal Underwriting) is exposed to changes in securities rates in whose issuance it participated (as underwriter or distributor) and which it acquired, whether by its own initiative or due to exercising an underwriting liability.

Stock Exchange Services provides its customers with non-linked NIS or USD credit, as a function of the monetary interest rate on the market. Adverse material changes in the inflation or interest rate paid by the Company in respect of short-term loans it takes from banks, without parallel adjustment in the NIS or USD interest paid by customers, may impair the Company profitability.

64.3 **Sectorial risks**

Decline in the value of assets under management and scopes of activity – The results of the financial services area are directly affected by the total value of AUM managed by the financial services area. The results and yields of mutual funds and investment portfolios under management, as well as customers' preferences, affect the scope of AUM. A decrease in the scope of AUM may materially affect the profitability of the financial services area. Stock Exchange Services is affected by the volumes of trade on the Stock Exchange. The volatility characterizing the primary market and changes in institutional organs' preferences may materially affect Migdal Underwriting scope of activity.

Insolvency of Israeli and foreign financial institutions due to assets holding – Stock Exchange Services must keep its customers' cash in a customer trust account in banks, hence there is exposure in case of insolvency of such banks. In addition, the company holds foreign securities and financial assets of its customers with different foreign correspondents, who provide the company with custody services, hence there is exposure in case of insolvency of such correspondents.

Regulation – the area of financial services is subject to very broad regulation, which is changed and updated frequently. Additional regulatory changes and/or harsher demands with regard to existing regulatory requirements and/or non-compliance of financial services companies with regulatory demands may have a material impact on the businesses and/or results of the financial services area.

Underwriters' responsibility for misleading details in the prospectus - Migdal Underwriting is responsible for the content of the prospectuses it signs towards anyone who purchased securities in the issuance and towards whoever sold and/or purchased securities during trade on the Stock Exchange or in off-floor transactions, for damage incurred by them in case of a misleading detail in the prospectus. Being the manager of an underwriters' consortium, Migdal Underwriting is exposed to indemnification claims on behalf of other underwriters in the consortium.

64.4 **Unique risks in the financial services area**

Credit risks to customers – Stock Exchange Services extends credit to its customers on a regular basis in order to purchase securities and financial assets. Extending the credit is done under restrictions detailed in the Stock Exchange Articles of Association and directives and in accordance with the hierarchy of authorities for granting credit in the Company. The credit is secured by the customers' securities portfolio, but from time to time credit is extended upon the company's credit policy and after decision and approval of the Credit Committee, without full collaterals. In certain cases, the value of the customers' securities portfolio may be insufficient for covering credit.

Credit risks to custodian customers – Stock Exchange Services provides these customers with execution services only (without custody services), when at the end of the day, the transactions executed for them vis-à-vis the banks providing the custody services are cleared (for foreign customers, the TASE Articles of Association allows clearing the transactions at T + 2 without the transaction being considered as credit consumption) ("custodian customers"). If, for any reason, the clearing bank does not approve the transaction intake at the end of the day, the company is left with the position. In such case, the above risk is one of changing the price of securities / derivatives until execution of the reverse transaction to close the position (i.e. market risk). In case of loss as a result of closing the position, the custodian customer will owe the Company the loss amount, and in fact, will receive credit from the Company. Since custodian customers do not receive custody services from the company, in such case the Company will not hold collaterals against credit.

Credit risks in respect of activity in derivatives – Stock Exchange Services provides guarantees from its own assets in order to secure liabilities due to activity in Maof options and transactions in futures. At the same time, customers grant the company their securities portfolio as a collateral, as per the provisions of the Stock Exchange's Articles of Association and directives. In case of high volatility in the prices of base assets or in other extreme cases, the customers' securities portfolio value might not cover the exposure stemming from this activity towards the other parties in these transactions, such that the customer will receive in practice unauthorized credit (without sufficient collaterals) from Stock Exchange Services.

Legal risks – The financial services area is exposed to claims filed against it by customers, supervising authorities, suppliers or employees, claiming alleged incompliance with the provisions of the law and/or agreements and/or professional negligence.

Operational risks – the financial services area is exposed to risks related to the operation of its activity and to the functioning of various arrays under its responsibility, both computerized and human. Furthermore, the financial services area is exposed to negligence and embezzlements on the part of its employees, and to fraud on the part of customers. Flaws in trading systems and/or in communication lines along with human errors made by traders, may bring about non-execution or wrong execution of transactions, and expose the area to fluctuations in asset trade ordered by customers, and claims in material scopes. The area may be exposed to information security events, in which a third party tries to break into computer systems in order to perform unauthorized activity or to be exposed to unauthorized information.

The management of credit risks and market risks is performed through various online systems – flaws in these systems might bring about inaccurate control of activity. Flaws in the recording of phone calls received in the trade room of Stock Exchange Services may expose Stock Exchange Services to market risks, in case of clarifications with clients regarding their instructions. Stock Exchange Services allows its customers to perform Buy and Sell actions of securities and financial assets through the Internet. As a result, it is exposed to fraud on the part of customers and/or third parties.

Stock Exchange Services allows some of its customers to directly contact foreign brokers abroad, in order to give Buy and Sell orders for securities and financial assets. As a result, Stock Exchange Services is exposed to the possibility of foreign brokers allowing customers to execute transactions exceeding the customers' assets value with Stock Exchange Services, such that the customer will receive in practice unauthorized credit (without sufficient collaterals) from the Company.

Professional negligence of foreign brokers and/or clearing houses in Israel and abroad may expose the financial services area to claims in material scopes.

Damage to goodwill – the goodwill of the financial services area and its reputation are an important factor in engaging with new customers and maintaining existing customers. Damage to reputation might affect the businesses of the financial services area.

64.5 **Table of risk factors as to financial services area:**

	Risk factors	Level of risk factor's effect on financial services activity: Great effect	Medium effect	Little effect
Macro risks	Capital market risks	V		
Sectorial risks	A decrease in the value of AUM and in the scopes of activity	V		
	Insolvency of Israeli and foreign financial institutions due to asset holding	V		
	Regulation	V		
	Underwriters' responsibility for misleading details in the prospectus			V
Unique Company risks	Credit risks for ordinary customers		V	
	Credit risks for custodian customers			V
	Credit risks in respect of activity in derivatives		V	
	Legal risks		V	
	Operational risks	V		
	Damage to goodwill		V	

65. Risk factors in the Group's other activity

The activity of Migdal Health and Mivtach Management is non-material, therefore as per the Company's evaluation, the risk in their respect is non-material.

March 19, 2013

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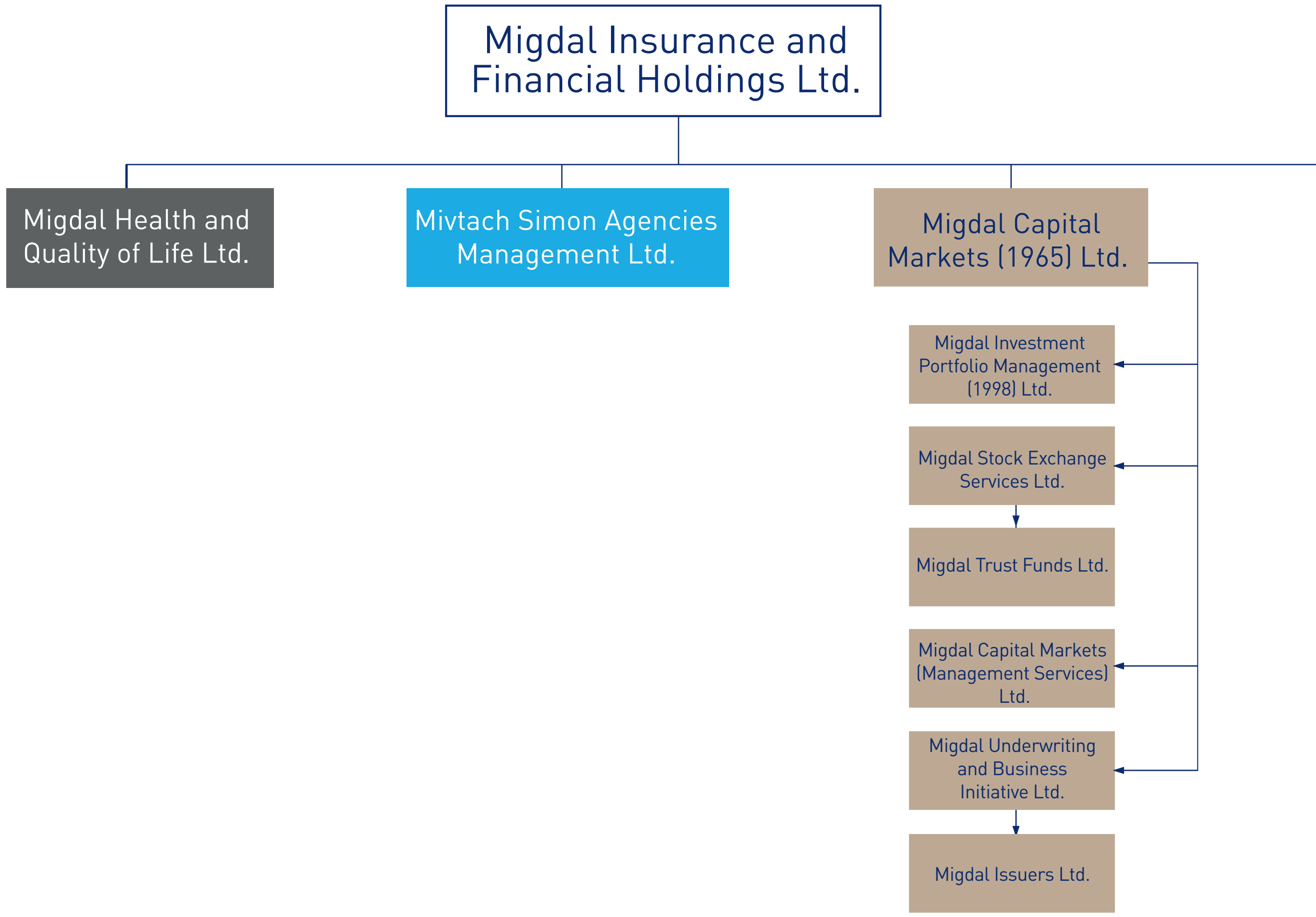
Migdal Insurance and Financial Holdings Ltd.

The names and titles of signatories:
Aharon Fogel, Chairman of the Board of Directors
Yonel Cohen, General Manager

Group Holdings Structure

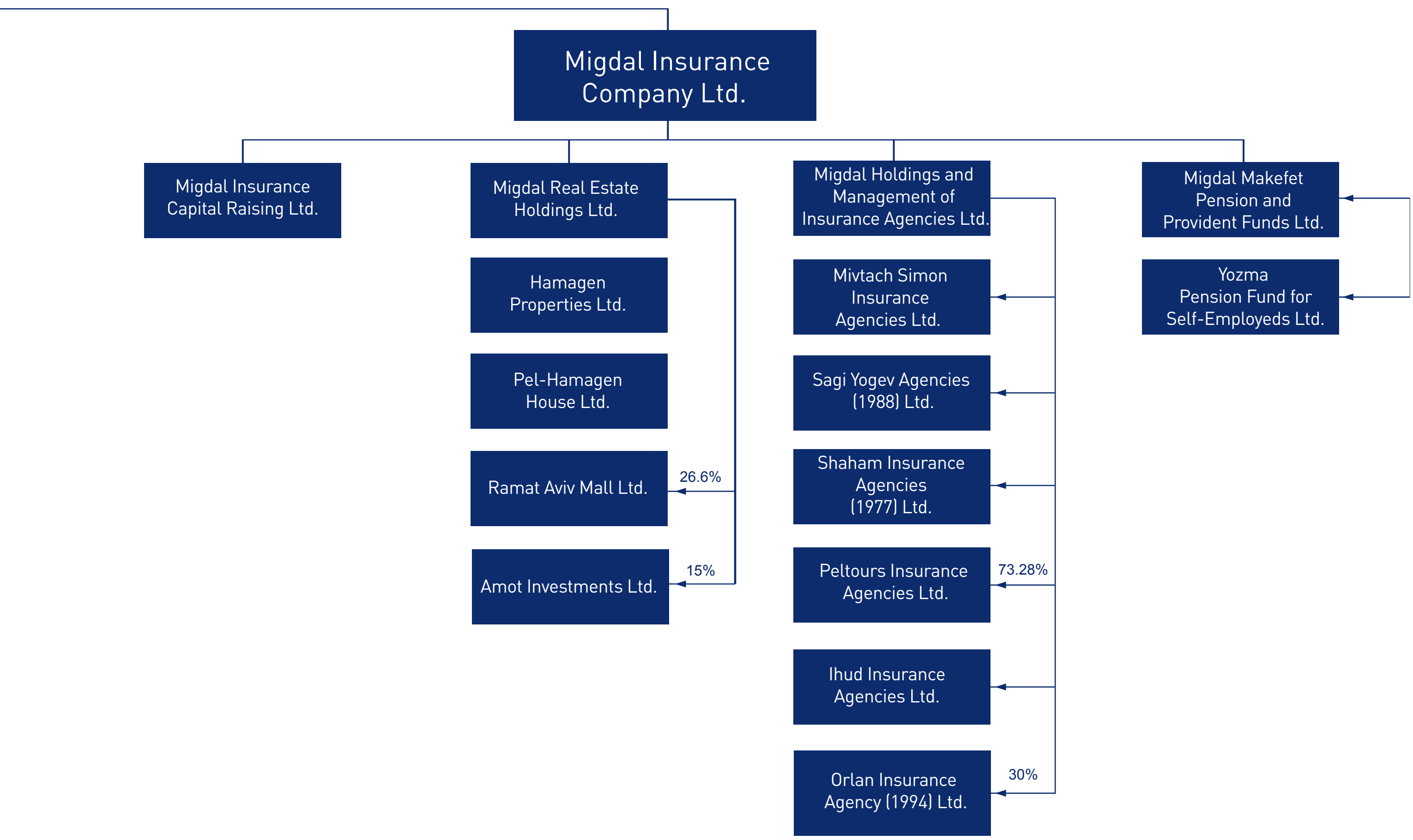
Mount Hermon

Group Holdings Structure
December 31st, 2012



Notes:

1. The holdings structure includes the main companies in the Group. For additional details regarding holdings in subsidiaries and affiliated companies as of December 31st, 2012, see also Regulation 11 to the Additional Data on the Corporation.
2. For the control structure in Migdal Holdings, see Clause 2.1 to the Corporation Businesses Description Report.
3. The companies described herewith are held at 100%, unless specified otherwise.


Migdal Insurance Company Ltd.
Migdal Insurance Capital Raising Ltd.
Migdal Real Estate Holdings Ltd.
Hamagen Properties Ltd.
Pel-Hamagen House Ltd.
Ramat Aviv Mall Ltd.
26.6%
Amot Investments Ltd.
15%
Migdal Holdings and Management of Insurance Agencies Ltd.
Mivtach Simon Insurance Agencies Ltd.
Sagi Yogev Agencies (1988) Ltd.
Shaham Insurance Agencies (1977) Ltd.
Peltours Insurance Agencies Ltd.
73.28%
Ihud Insurance Agencies Ltd.
Orlan Insurance Agency (1994) Ltd.
30%
Migdal Makefet Pension and Provident Funds Ltd.
Yozma Pension Fund for Self-Employeds Ltd.