Europay (Eurocard) Israel Ltd.

Annual Report

For the year ended December 31, 2012

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Europay (Eurocard) Israel Ltd.

Board of Directors' Report

For the Year Ended December 31, 2012

ISRACARD GROUP

Board of Directors' Report on the Financial Statements as at December 31, 2012

At the meeting of the Board of Directors held on February 27, 2013, it was resolved to approve and publish the audited financial statements of Europay (Eurocard) Israel Ltd. (hereinafter: "**the Company**" or "**Europay**") for the year 2012.

Description of the General Development of the Company's Business

The Company was established and incorporated in Israel in 1972 as a private company. In July 2009, control of the Company was transferred from Bank Hapoalim B.M. (hereinafter: "**Bank Hapoalim**") to Isracard Ltd. (hereinafter: "**Isracard**"), which is controlled by Bank Hapoalim.

The Company is an "auxiliary corporation," according to the definition of this term in the Banking Law (Licensing), 1981 (hereinafter: "**auxiliary corporation**"). The Company has no subsidiaries or other investee companies.

The Company, jointly with Isracard, issues credit cards that combine the Isracard and MasterCard brands (hereinafter: "**MasterCard cards**"), which are issued by the Company for use abroad and by Isracard for use in Israel, under a license granted to the Company by MasterCard International Incorporated (hereinafter: "**the MasterCard Organization**"). In addition, the Company clears transactions with merchants that have agreements with it which are executed in Israel in foreign currency, using MasterCard cards issued abroad by companies in the MasterCard Organization, and paid to the merchant in foreign currency.

Contractual engagement between the Company and Isracard – Under an agreement between the Company and Isracard, its parent company, Isracard administers and operates, on behalf of the Company, issuance and clearing activity in Israel of transactions executed with merchants using MasterCard cards (hereinafter: "**the Arrangement**"). The Company participates in all costs common to Isracard and the Company, according to its relative share of the relevant activity. In return for Isracard's activity in the operation of the Arrangement, the Company pays a fee and other payments to Isracard, as agreed between the parties.

The Company is part of the Isracard Group, which consists of the following companies: Isracard, Poalim Express Ltd. (hereinafter: "**Poalim Express**"), Aminit Ltd. (hereinafter: "**Aminit**"), and the Company.

Dividend distribution – In May 2012, the Company distributed a dividend to its shareholders in a total amount of NIS 174 million.

Following the distribution of the dividend, Isracard acquired 7,699 common shares from Mizrahi Bank, constituting 1.8% of the issued and paid-up common share capital of the Company. Following the completion of this transaction, Isracard holds 100% of the shares of the Company.

Economic Environment and the Effect of External Factors on the Company's Operations

Developments in the Global Economy

The debt crisis in the developed countries peaked during the last year, especially in Europe. Consequences were felt throughout the world, and global growth slowed. The large debts of Europe's peripheral countries were the focus of the crisis; bond yields functioned as a barometer of its severity. Massive intervention by policymakers was necessary in order to restore confidence to the markets and prevent decline. Stability was in fact achieved during the second half of the year, particularly after the publication of the plan for purchases of the bonds of the distressed countries by the European Central Bank. It is important to note that notwithstanding the signs of recovery, a genuine solution to the problem of the large sovereign debts has not yet been found; as long as these economies do not resume growing, the need to service the debts is still a sword hanging over the global economy in general, and the European economy in particular. Overall for the year, according to estimates by the International Monetary Fund, world economic growth slowed to an annual rate of 3.2%. The developed economies grew at a moderate rate of 1.3%, as the bulk of the contribution to growth derived from the developing markets, which grew by 5.1%. Central banks worldwide worked to stimulate growth, maintaining expansionary monetary policies, which were also made possible by the relatively low inflation.

Growth in the United States accelerated slightly over the last year, mainly due to improvements in private consumption and in the real-estate market. Growth in 2012 totaled 2.3%. Although the unemployment rate in the US fell from 8.5% at the end of 2011 to 7.8% by the end of 2012, the American economy is still lacking about 4 million jobs in order to return to pre-crisis employment levels. The US is also facing the problem of high public debt, although its characteristics are different than in Europe. The US has the ability to raise capital at relatively low prices, but the political disagreements between the Democratic administration and the Republican-majority House of Representatives has made budget policy management difficult.

The Eurozone economy experienced a 0.4% GDP contraction in 2012, and the average unemployment rate in the Eurozone countries reached a high of 11.8% in November. Decisions made in the Eurozone over the year indicated a desire to keep it whole: Greece, the Eurozone's weakest link, received two aid packages, once it had implemented a debt settlement for private investors. A bailout fund was also made available to commercial banks in the crisis countries, and agreements were reached regarding the establishment of a uniform supervision mechanism for banks. It was resolved that in the future the central bank would buy bonds of countries in crisis, subject to certain limits. To date, Italy and Spain have not yet applied to the fund, but the decisive action seems to have largely restored confidence to the financial markets.

Growth slowed slightly in the emerging markets as well, primarily in China, India, and Brazil. The weight of these economies in global terms continued to increase; they currently account for the most substantial contribution to world growth. During the year, there were increasing concerns that the slowdown in growth rates in China might expose the Chinese economy to crises in real estate and in banking. The Chinese administration responded with measures to stimulate growth, and figures for the fourth quarter pointed to a slight improvement.

The Israeli Economy

Economic Activity in Israel

The Israeli economy posted 3.2% growth in 2012. Growth rates slowed during the year; in the fourth quarter, the economy grew by only 2.5%, in annualized terms. The main cause of the slowdown was the stagnation in exports, apparently due to the global situation. Growth rates cooled in private consumption and in investments as well, including investments in residential construction. Monetary policy was expansionary, and the same can be said for fiscal policy, although taxes were raised during the second half in response to a significant deviation from the deficit target.

The labor market remained strong in 2012, with the unemployment stable at 7%, and a 3.5% increase in the number of employed persons, although most jobs added were in the public sector, in the education and health-care segments.

Following difficulties with the approval of the state budget for 2013, general elections to the Knesset were moved to the earlier date of January 22, 2013. The new government to be established will have to cope with the need for deep budget cuts during a downturn in economic growth.

Natural gas from the Tamar reservoir will begin to arrive in the second quarter of 2013, according to estimates. The inflow of gas is expected to lead to reduced imports of energy materials to Israel; these imports soared over the last two years, due to the cessation of natural gas imports from Egypt. The natural gas is expected to contribute to economic growth, but its contribution to employment and to household incomes is likely to be minor, at least initially.

Fiscal and Monetary Policy

The budget deficit for the last year significantly exceeded the original target, reaching NIS 39 billion, or 4.2% of GDP, versus the target of 2%. Most of the deviation occurred on the revenue side, which was affected by the slowdown in growth, despite tax hikes in the second half. Expenditures deviated from plans as well, due to wage agreements, defense spending, and the adoption of the Trajtenberg Committee's recommendations. The state budget for 2013 was not approved, and the Knesset elections were held earlier as a result, as noted.

An expansionary monetary policy was maintained over the last year. The central bank's interest rate was lowered from 2.75% in January to 2.0% in December, and to 1.75% in January 2013. This policy was influenced by the low interest rates in the developed countries, the cooling of the local economy, and the lack of danger to price stability in the short term. The central bank took several steps aimed at halting the increase in mortgages and cooling down the housing market over the last year.

Inflation and Exchange Rates

The consumer price index rose by 1.6% in 2012, slightly below the midpoint of the target range. Government actions led to relatively large price changes, such as a 70% decrease in prices of preschools, which became free of charge from the age of three, as part of the Trajtenberg Committee recommendations, and mobile communication prices, down by 7%. By contrast, the price of electricity rose by 10%, and prices of other basic products were affected by the increase in indirect taxes during the year. Inflation in the developed countries has been tempered by surplus production capacity and, especially, high unemployment rates. This situation has also had a substantial impact on inflation in Israel, preventing inflationary pressures. The expansionary monetary policy seemed to affect housing prices, which rose by 5.7% in the twelve months ended in November, according to a survey by the Central Bureau of Statistics, completing a 73% rise relative to 2007.

The shekel appreciated by 2.3% against the US dollar and by 0.8% against the currency basket. The Bank of Israel did not intervene in currency trading during the year. The Bank of Israel’s foreign-currency reserves grew by USD 1 billion, to USD 75.9 billion. Foreign investors continued to reduce their investments in bond and short-term notes (Makams), due to limits imposed on such investments by the central bank. This process began in 2011; most foreigners’ Makam holdings were sold by mid-2012.

The Credit-Card Industry in Israel

As at the reporting date, the following companies operate in the area of credit-card issuance and clearing in Israel: (1) the Company and Isracard, which issue and clear MasterCard and Isracard credit cards, respectively; (2) Poalim Express Ltd., a sister company of Isracard, which issues and clears American Express credit cards; (3) Aminit Ltd., a sister company of Isracard, which issues and clears Visa credit cards; (4) Leumi Card Ltd. (hereinafter: "**Leumi Card**"), which, to the best of the Company's and Isracard's knowledge, issues Visa and MasterCard credit cards, and clears Visa, MasterCard, and Isracard credit cards; (5) Cartisei Ashrai Leisrael Ltd. (hereinafter: "**CAL**"), which, to the best of the Company's knowledge, issues Visa and MasterCard credit cards, and clears Visa, MasterCard, and Isracard credit cards; and (6) Diners Club Israel Ltd. (hereinafter: "**Diners**"), to the best of the Company's knowledge a subsidiary of CAL, which issues and clears Diners credit cards.

The credit-card companies in Israel issue and clear the international credit cards noted above (American Express, MasterCard, Visa, and Diners) under licenses granted by the relevant international organizations.

In recent years, two notable trends have been evident in the credit-card issuance sector in Israel: (1) issuance of non-bank credit cards by credit-card companies, usually linked to customer clubs or consumer or other entities; (2) expansion of the range of services offered by credit-card companies in the area of credit and financing to cardholders and merchants, including through the issuance of "revolving credit" credit cards, which allow cardholders to determine debit amounts and dates according to their needs and ability.

The credit-card industry in Israel is characterized by high, dynamic regulatory intervention in the business of the companies operating in this area, both due to the fact that each of the companies is an "auxiliary corporation," and in relation to their activity in the area of credit cards. This regulation includes the Charge Cards Law, 1986 (the "**Charge Cards Law**") and the derived regulations; the Banking Law (Customer Service), 1981 (the "**Banking Law (Customer Service)**"); and the Anti-Money Laundering Law, 2000 (the "**Anti-Money Laundering Law**") and the order issued under its power by the Bank of Israel. In addition, various directives of the Supervisor of Banks apply to credit-card companies in Israel, including Proper Conduct of Banking Business Directive No. 470, which regularizes the activity of credit-card companies, as well as guidelines derived from Proper Conduct of Banking Business Directives No. 201-211, which establish risk-management standards aimed at reinforcing the financial robustness and stability of banking systems.

For further details, and with regard to various directives in the area of cross-clearing of Visa, MasterCard, and Isracard credit cards imposed on credit-card companies in Israel by the Antitrust Commissioner, and the opening of the credit-card market – see the section "Restrictions and Supervision of the Company's Operations," below.

Profit and Profitability

The net loss of the Company in 2012 totaled NIS 4 million, compared with net profit of NIS 2 million in 2011.

The return of (loss)/profit before taxes on average equity reached (4.3%) in 2012, compared with 1.1% in 2011.

The return of net (loss)/profit on average equity reached (4.7%) in 2012, compared with 0.9% in 2011.

Developments in Balance-Sheet Items

The balance sheet totaled NIS 7 million on December 31, 2012, compared with NIS 185 million at the end of 2011.

Equity as at December 31, 2012 totaled NIS 7 million, compared with NIS 185 million on December 31, 2011.

The ratio of equity to the balance sheet reached 100% on December 31, 2012, similar to December 31, 2011.

The ratio of capital to risk-adjusted assets under the capital measurement and adequacy directives reached 140% on December 31, 2012, compared with 194.7% on December 31, 2011.

The minimum capital ratio required by the Bank of Israel is 9%.

Pursuant to the instructions of the Bank of Israel, the risk appetite of the Company as a part of the Bank Hapoalim Group has been defined as a ratio of total capital to risk-adjusted assets at a rate of 12.5%, in effect beginning in the first quarter of 2011.

Description of the Company's Business

Credit-Card Issuance

General

A credit-card company issues credit cards to its customers (credit-card holders). Credit-card holders use the card as a means of payment to merchants, and the merchants provide the credit-card holders with goods or services. Customers join the credit-card system by signing a credit-card contract with the issuer and receiving the credit card. Credit-card holders make a commitment to repay amounts owed arising from their use of the credit card.

The issuer collects various fees from the cardholder and interchange fees or merchant fees from the clearer or merchant, respectively, for card issuance and operational services.

As at the date of the report, several companies issuing bank and non-bank credit cards operate in the credit-card issuance sector in Israel: the Company, Isracard, Poalim Express, Aminit, Leumi Card, CAL, Diners, and Israel Postal Bank Ltd. This field is characterized by a high level of competition.

Bank cards issued by the Company and Isracard are distributed to owners of accounts at banks with which the Company and Isracard have agreements, including Bank Hapoalim, Mizrahi-Tefahot Bank Ltd., Bank Yahav for Government Employees Ltd. ("**Bank Yahav**"), First International Bank of Israel Ltd., Bank Massad Ltd., Bank Otsar Hahayal Ltd., and Bank Poaley Agudat Israel Ltd. (jointly, the "**Banks Under Arrangement**").

As noted, Isracard administers and operates credit-card issuance and clearing activity on behalf of the Company.

Critical success factors in the operating segment. In the opinion of the Company, the main critical success factors in the Issuance Segment are the following: (1) the ability to issue credit cards under an international license; (2) brand image; (3) the collaboration with banking corporations, particularly Bank Hapoalim, for the distribution and issuance of credit cards, including the integration of a bank card with the credit card issued to the customer; (4) high-quality, experienced human capital; (5) quality of customer service; (6) a supporting operational system including information systems, technologies, communications, and advanced infrastructures; (7) a technological level allowing response to changes and the development of new products; (8) a system of risk management and credit controls; (9) the ability to recruit and retain customers through a supporting marketing system; (10) agreements to establish customer clubs; and (11) operational efficiency and preservation of size advantage.

Key entry barriers in the operating segment. The key entry barriers in the provision of credit-card issuance services are the following: (1) the need to obtain a license from an international organization to issue the brand and receive the right to use its logo, which may involve high monetary costs; (2) compliance with certain qualifications as a condition of receiving an issuer's license; (3) the need for broad financial resources and extensive knowledge in order to carry out the investments necessary to issue cards and the investments in technological infrastructures, including a supporting operational system, sophisticated information and communications systems, a risk-management and credit-control system, information security, advertising, and widely deployed sales and marketing; (4) the structure of the credit-card industry in Israel, which has a high penetration rate; and (5) the need for capital in order to comply with the directives of the Supervisor of Banks regarding the ratio of capital to risk-adjusted assets.

Substitutes for the products of the operating segment. Payment methods such as cash, direct debits, electronic bank transfers, checks, gift cards, and prepaid cards constitute substitutes for the services provided by credit-card companies in Israel.

Products and Services

The Company, jointly with Isracard, issues credit cards that combine the Isracard and MasterCard brands. The cards are issued by the Company for use abroad and by Isracard for use in Israel. These cards are issued both as bank cards and as non-bank cards, and are used as means of payment for transactions and for cash withdrawals, locally and internationally.

In addition, the various additional products and services offered through Isracard include More brand revolving credit cards, allowing cardholders to determine the terms of repayment; loans for specific purposes for private and business customers; various credit plans based on Isracredit plans; various types of all-purpose loans based on credit facilities in credit cards; various options for spreading payments; and information services and certifications.

Contractual Arrangements with Banking Corporations

In general, the various agreements of the Company and Isracard with the Banks Under Arrangement grant each bank the authority to determine which of its customers are entitled to register for the credit-card arrangement of the Company, and to recommend the customer's registration for the card arrangement to the Company. As a rule, each such bank is responsible for accepting all sales slips and debits executed by the customer on the day of presentation of the sales slips or debits to the bank. The aforesaid various agreements also include payment arrangements and the relevant terms with each of the Banks Under Arrangement.

Customers – Cardholders

The credit cards issued by the Company serve customers in various sectors, such as private customers, corporate employees, and corporate purchasing, including B2B (business-to-business payment transfers).

As at the date of the report, there are no cardholders (bank and/or non-bank) whose share of the volume of transactions executed using the Company's credit cards constituted 10% or more of the total volume of transactions in the Company's and Isracard's credit cards in 2012.

Marketing and Distribution

The Company's marketing activity in the area of credit-card issuance is conducted through Isracard, which administers and operates credit-card issuance activity on behalf of the Company, on several levels: joint activity with the Banks Under Arrangement in the issuance of bank cards, marketing of non-bank cards, joint activity with customer clubs with regard to the issuance of both bank cards and non-bank cards, and marketing and sales promotion, including through large-scale marketing campaigns, joint offers with leading entities in the various sectors, the operation of a telemarketing center, direct mail, salespeople, the website, and more.

Within the activity of customer clubs, the Company customarily enters into agreements with various entities representing various customer groups, in arrangements in which the Company issues credit cards to the members of those customer groups (the "**Club Members**"). The cards issued to the Club Members usually grant them discounts, benefits, and special services at a range of merchants that accept the club's cards. Entities participating in the Company's customer-club activity include workers' organizations, professional organizations, and commercial corporations interested in issuing club cards to their customers and/or employees through credit cards. The range of different types of credit cards issued by the Company includes credit cards issued jointly with organizations and clubs, and with consumer, professional, and other entities, such as Hever cards for career military personnel and retirees, Life-Style club cards, Ashmoret cards for members of the Israel Teachers Union, Hot cards for members of the Union of Engineers and Technicians in Israel, Members cards for members of the Israel Bar Association and of the Institute of Certified Public Accountants in Israel, cards for Rafael Advanced Defense Systems Ltd., cards of retail chains, and more.

Competition

The credit-card issuance field is characterized by a very high level of competition, which has intensified in recent years, encompassing all activities and population segments relevant to this sector.

Competition over cardholders is apparent on several levels: (1) registration of new customers (who do not own credit cards or who own credit cards of competing companies) for a credit-card arrangement with the Company/Isracard, and the retention of existing customers and prevention of desertion to competitors, which requires the investment of efforts and resources; (2) competition over the wallet of cardholders (who may hold charge cards issued by several companies) with the aim of leading customers to carry out the major portion of their routine consumption using credit cards issued by the Company and Isracard (instead of cash or checks), while increasing the mix of products issued by the Company and Isracard and/or increasing the volume of use of such products; and (3) offers of non-bank credit services through revolving credit cards or through loans for cardholders, as an addition and/or alternative to credit granted by banks and other financial institutions.

For details regarding the credit-card companies operating in Israel, see the section "The Credit-Card Industry in Israel," above.

In order to cope with competition, the Company, through Isracard, which administers and operates credit-card issuance activity on behalf of the Company, takes the following main actions: (1) investment of resources to improve service to cardholders, retain cardholders as customers, and increase customer loyalty; (2) innovation – response to customers' needs by developing new products and services to supply the requirements of the Company's customer segments and market needs, and development of alternative products and services to compete with prevalent means of payment such as cash and checks; (3) reinforcement of status and image through advertising, benefits, and various offers for cardholders; and (4) marketing and sales promotion activity, including through the contractual engagements with the Banks Under Arrangement.

Positive factors affecting the Company's competitive standing include the following, among others: (1) the licensing agreement with the MasterCard Organization for the issuance and clearing of credit cards; (2) the arrangement with Isracard for the management and operation of credit-card issuance and clearing activity; (3) the Company and Isracard are the leaders in the area of credit-card issuance in Israel and have the largest quantity of issued cards in Israel; (4) professional, skilled, experienced human capital; (5) the Company's image and brand; (6) the Company and Isracard have long-term agreements with the Banks Under Arrangement for the issuance of credit cards; (7) the Company and Isracard's system of agreements with customer clubs and organizations, representing a variety of segments of Israel's population; (8) the range of products and services offered to a broad spectrum of customers; (9) an advanced service system allowing a high quality of customer service; and (10) a robust capital structure and positive cash flow.

Negative factors affecting the Company's competitive standing include, among others, technological improvements that create the possibility of development of alternative means of payment in areas such as cellular phones, which may cause a decline in the demand for credit-card issuance; and the entry of retail and other entities into the issuance field and/or expansion of activity of existing competitors, including through strategic ventures and collaborations for card issuance.

Credit-Card Clearing

General

In clearing services, the clearing credit-card company makes a commitment to merchants that subject to compliance with the terms of the agreement between them, the debits incurred by holders of cards cleared by the clearer when purchasing goods or services from the merchants will be settled by the clearer. The clearer accumulates debits for transactions executed in the credit cards cleared by the clearer with a particular merchant that has signed a clearing agreement with it, in return for a fee (called the "**merchant fee**"), and secures and transfers to the merchant the payments incurred by the credit-card holders who executed transactions using credit cards with that merchant.

As at the date of the report, several credit-card companies operate in the credit-card clearing segment in Israel: the Company, Isracard, Poalim Express, Aminit, Leumi Card, CAL, and Diners. Competition in this field is intense, encompassing all areas of activity within the segment.

The Company has clearing agreements with merchants in various industries. In addition to clearing services, it offers merchants various financial services, such as loans, advance payments, sales-slip discounting, and marketing and operational services, including an option for payment in installments, flexible crediting dates, targeted information, and sales-promotion campaigns.

In response to a request by the Economics Committee, in April 2011, the Company lowered fees for approximately 7,000 small businesses in peripheral regions, by 10% to 15% of the basic fee for the full year. The fee reduction offer will continue for another year, until April 2013, both for merchants included in the earlier offer and for new merchants who joined during the period of the previous offer. In November 2012, the Company lowered fees by 30% for approximately 7,000 merchants in southern Israel and in the conflict areas, with the option to suspend loan principal payments for three months.

Credit-card companies authorized to issue Visa and MasterCard cards and to clear transactions executed using these cards can clear Visa and MasterCard cards, according to each company's authorizations. In addition, on May 15, 2012, the market for clearing of the Isracard brand was opened, and merchants can now switch clearers for this brand. With regard to the reduction of the interchange fee, beginning on November 1, 2011, and with regard to the approval of the arrangement, including all of its terms, see Note 4A to the Financial Statements. With regard to the government bill passed by the Knesset plenum in August 2011, see Note 4A.2 to the Financial Statements.

Critical success factors in the operating segment, and changes therein. In the opinion of the Company, the main critical success factors in the Clearing Segment are the following: (1) the ability to clear credit cards under an international license; (2) available sources of financing for investment in new technological infrastructures necessary in order to provide clearing services and upgrades of existing infrastructures; (3) specification and development of suitable clearing systems and maintaining a high technological level; (4) high-quality, experienced human capital; (5) quality of service to customers of the Clearing Segment – merchants – and the ability to recruit and retain merchants through a supporting sales and marketing system; (6) provision of related services to merchants, including various marketing, financial, and operational services; (7) operational efficiency and utilization of size advantage; (8) accumulated experience in the area of clearing of credit cards; and (9) a robust capital structure and available sources of financing.

Key entry barriers in the operating segment. The key entry barriers in the provision of credit-card clearing services are the following: (1) the need for financial means, experience, and extensive knowledge in order to carry out the necessary investments in technological infrastructures, an operational system, and large-scale advertising and marketing; (2) the need to obtain a license from international organizations to clear the brands under their ownership, while continually complying with the terms stipulated in each license and with the rules of the relevant organization; (3) deployment of a communications system to allow clearing; (4) the need to perform clearing services on a large scale in order to recover the investment in infrastructures, clearing systems, and other costs; (5) development of a reliable information system for account settlement; and (6) a sales, recruitment, and customer service system.

Substitutes for the products of the operating segment. Alternative means of payment such as cash, standing orders, bank transfers, and checks constitute substitutes for payment by credit card.

Products and Services

The Company clears transactions with merchants that have agreements with it, executed in Israel using MasterCard cards issued abroad by members of the MasterCard Organization, in foreign currency, and paid to the merchant in foreign currency, mainly in return for a merchant fee, as noted above. Isracard administers and operates credit-card clearing activity on behalf of the Company.

In addition, the Company offers marketing and operational services, through Isracard, such as sales-promotion campaigns, information regarding credits of the merchant, joint advertising campaigns, unique marketing information, and benefits, all at a high quality of service backed by advanced technological infrastructures.

Segmentation of Income from Products and Services

All income from merchants and all expenses related to recruitment and routine handling of merchants relevant to the Company were allocated to the Company's activity. The main income and expense items are in accordance with the Company's agreement with Isracard for the management and operation of credit-card issuance and clearing activity.

Customers

The Company's customers in the Clearing Segment are numerous, varied merchants that have entered into agreements with it. As at the date of the report, the Company did not derive revenues from any individual merchant constituting 10% or more of the total revenues of the Company and Isracard in 2012.

Marketing and Sales

The Company's marketing and sales activity in the Credit-Card Clearing Segment is conducted through Isracard (which manages and operates credit-card issuance and clearing activities on behalf of the Company), based on the principle of focusing on merchants' needs, through a targeted sales and support system.

The Company's key objectives in its marketing activity in this area are: (1) to retain merchants as customers by providing marketing and operational services, including information regarding past and future credits of the merchant, advertising campaigns and unique marketing information, benefits, and programs at a high level of service; (2) to strengthen image; and (3) to recruit new merchants.

The Company operates a website designed for its business clients at www.isracard.co.il, which provides financial information regarding the merchant's credits and expanded business information, among other matters, and allows credit applications to be filed.

Competition

The credit-card clearing field is characterized by a very high level of competition. For a list of credit-card companies operating in this area in Israel, see "The Credit-Card Industry in Israel," above. In the opinion of the Management of the Company, the Company and Isracard are the leaders in this area in Israel.

Competition in the clearing sector is focused on recruiting new merchants for clearing agreements with the Company, retaining existing merchants as customers of the Clearing Segment, and preventing desertion to competitors, which requires the investment of extensive efforts and resources and high sales and marketing expenses.

Another aspect of competition in the clearing sector is focused on the development of financial and operational products and services for merchants, to increase the volume and/or amounts of transactions executed with each merchant. The credit-card companies have expanded the mix of products and services offered to merchants by offering marketing and financial services.

In order to cope with the competition in this area, the Company, through Isracard, which administers and operates credit-card clearing activity on behalf of the Company, takes the following main actions: (1) a competitive, prudent rate policy (merchant fees); (2) increased collaborations with merchants; (3) investment of resources to improve service, retain merchants as customers, and increase customer loyalty, while adapting products and services to each merchant's unique needs; (4) operation of a professional, experienced, skilled sales and marketing system specializing in providing solutions for the various merchants, and an experienced, professional, skilled service system supported by advanced technological systems.

Positive factors affecting the Company's competitive standing include the following, among others: (1) the licensing agreement with the MasterCard Organization for the issuance and clearing of credit cards; (2) the arrangement with Isracard for the management and operation of credit-card issuance and clearing activity; (3) a supporting marketing, sales, and service system specializing in providing suitable solutions to merchants, and containing professional, skilled, experienced manpower; (4) a brand with presence and power; (5) an advanced technological infrastructure allowing response to the needs of the various merchants; and (6) a robust capital structure and positive cash flow.

Negative factors affecting the Company's competitive standing include, among others, regulation, technological improvements that create the possibility of development of alternative means of payment in areas such as cellular phones, which may cause a decline in credit-card clearing; and merchants' ability to switch clearers in MasterCard, Isracard, and Visa brands at their discretion.

For details regarding regulatory restrictions applicable to the Company under antitrust laws, see the section "Restrictions and Supervision of the Company's Operations."

Seasonality

Credit-card transactions (issuance and clearing) are linked directly to private consumption and seasonality in Israel, as well as to the seasonality and rate of incoming tourism to Israel.

Intangible Assets

The Company holds a long-term Principal Member license from the MasterCard Organization for the issuance and clearing of MasterCard cards in Israel. In addition, as a member of the MasterCard Organization, the Company has a general right to use the brands owned by the MasterCard Organization, primarily "MasterCard."

In the course of their operations, the Company and Isracard are subject to the provisions of the Protection of Privacy Law, 1981 and the regulations enacted under that law, including the duty to register a database (as defined in the Protection of Privacy Law) in accordance with the requirements of the law and in accordance with their agreements.

Human Capital

All employees of the Company are on loan to Isracard, in accordance with the arrangements prevailing between the companies.

Service Providers

Isracard – An arrangement is in place between the Company and Isracard, under which Isracard administers and operates credit-card issuance and clearing activity on behalf of the Company. For further details, see "Contractual engagement between the Company and Isracard Ltd.," above.

Financing

The Company finances its operations through its own means. Among other matters, the directives of the Supervisor of Banks include restrictions affecting the ability of banking corporations in Israel to extend credit beyond certain volumes, including limits referring to the total indebtedness of a "single borrower" or of a "group of borrowers" (as these terms are defined in the directives), and to the total indebtedness of the six largest borrowers of a banking corporation. The Company, as part of the Bank Hapoalim Group, may be limited from time to time in receiving credit from other banking corporations due to these directives. According to the Company's estimates as at the date of the report, it has no effective restriction in receiving credit under the aforesaid directives.

Taxation

For details regarding the Company's taxation status, see Note 7 to the Financial Statements.

Restrictions and Supervision of the Company's Operations

As a company engaged in issuing and clearing charge cards, laws and directives related to its activity apply to the Company. These charge-card laws impose duties and restrictions on the operation of credit-card companies, including the Company, in the areas of the issuance and clearing of charge cards. In addition, various directives issued by the Supervisor of Banks and applicable to credit-card companies apply to the Company, such as Proper Conduct of Banking Business Directive No. 470 (Charge Cards), which regularizes the operation of credit-card companies that are auxiliary banking corporations and of banking corporations with regard to the operation of charge-card systems. Additional Proper Conduct of Banking Business Directives also apply to credit-card companies.

In addition, the Company is an "auxiliary corporation" under the Banking Law (Licensing). As a credit-card company and as an auxiliary corporation, a further system of rules, orders, and regulations applies to the Company, including: the Banking Law (Licensing); the Bank of Israel Law, 1954; the Banking Ordinance; the Banking Law (Customer Service), 1981 and the derived secondary legislation; and a system of directives, guidelines, and position statements of the Supervisor of Banks at the Bank of Israel.

The aforesaid laws and directives extensively affect the conduct of the Company's business (similar to other credit-card companies), including its contractual engagements, its manner of conduct, and the management of its financial resources.

In addition to the laws relevant to the Company's activity as an auxiliary corporation and as a credit-card company, various items of legislation apply to the Company which regularize its routine operations, including the Restrictive Trade Practices Law, 1988 (the "**Restrictive Trade Practices Law**"); the Interest Law, 1957; the Agency Law, 1965; the Control of Prices of Commodities and Services Law, 1957; the Control of Commodities and Services Law, 1996; and the Protection of Privacy Law, 1981 and the subsequent regulations.

Antitrust Issues

Most of the Company's activity is performed for the Company and on its behalf by Isracard. In the area of clearing, this activity includes clearing of transactions executed with merchants in Israel in foreign currency using MasterCard cards issued abroad. Isracard clears, for itself, transactions executed with merchants in Israel using MasterCard and Isracard cards issued in Israel, and transactions executed in Israel in Israeli currency using MasterCard cards issued abroad.

Reports by Isracard and by Bank Hapoalim indicate, among other matters, that in October 2006, Isracard and Bank Hapoalim, together with other credit-card companies (not including the Company) and other banks, filed a request with the Antitrust Tribunal to approve a restrictive arrangement under the terms formulated and agreed upon with the Antitrust Commissioner. An amended cross-clearing arrangement, revising the earlier agreements, was submitted to the Tribunal on December 28, 2011; this arrangement is in effect from the date of its approval until December 31, 2018. A ruling handed down by the Antitrust Tribunal on March 7, 2012 approved the amended arrangement, including all of the terms thereof.

A common technical interface for the credit-card companies Isracard, Aminit, Leumi Card, and CAL began to operate in June 2007, for the clearing of transactions executed in Israel using Visa and MasterCard cards issued in Israel. Expansion of the activity of other companies in clearing transactions executed in Israel using MasterCard cards may influence the Company's activity and detract from its revenues, despite the fact that its activity is focused on the clearing of transactions executed using MasterCard cards issued abroad.

Although the Company is not directly associated with the processes described above, the Company estimates that these processes, or part of such processes, may influence the Company's activity and impair its revenues, despite the fact that its activity is focused on clearing transactions in MasterCard cards issued abroad. The Company cannot estimate which of the factors mentioned will materialize, when such factors may materialize, or the extent of their impact.

Additional Regulation

1. A private bill was submitted to the Knesset in March 2010, according to which credit-card companies must note in their statements to cardholders whether a transaction performed by the cardholder constitutes a transaction in a missing document. This bill was passed in a preliminary reading on May 26, 2010, and transferred to the Economics Committee to be prepared for a first reading. On May 23, 2010, a ministerial committee made the decision to promote this bill through regulations, in coordination with the Ministry of Justice.

   In accordance with these decisions, following discussions of this matter with the Ministry of Justice, an agreement was reached regarding the execution of the amendments under both of the aforesaid bills in Proper Conduct of Banking Business Directive No. 470, Charge Cards (hereinafter: the "**Directive**"). A draft amendment of the directive was distributed in June 2011.

   The private bill on reporting of transactions in a missing document passed in the first reading in August 2011. If the matters addressed by the bill are included in the Directive, as noted above, it is likely that the legislation on this matter will not be promoted.

   In November 2011, the matters addressed by the aforesaid bills were formulated into binding directives, through amendments to Directive 470, as noted above. The amendment of the Directive has no effect on the Company.

2. A government bill approved by the Knesset plenum and published in the Official Gazette of the Government of Israel in August 2011 concerns, among other matters, the area of discounting, as well as a directive whereby an issuer that issues ten percent or more of the number of charge cards issued in Israel, or an issuer of charge cards used to execute at least ten percent of the amount of transactions executed in Israel, shall be required to contract with a clearer for cross-clearing of transactions in the charge card which it issues. The directives of this law have been in effect beginning on May 15, 2012. This law has a negative effect on the Company; however, at this stage the Company cannot estimate the full actual extent of this effect.

3. Pursuant to an instruction published by the Bank of Israel in November 2011, banking corporations and credit-card companies must provide disclosure in their board of directors' reports of any group of borrowers whose net indebtedness on a consolidated basis (after the permitted deductions) exceeds 15% of the capital of the banking corporation or credit-card company, as detailed in the instruction. This instruction shall apply from the financial statements as at September 30, 2011, to the financial statements as at September 30, 2012. The duration of the instruction was extended to September 2013 in January 2013. As at the date of this report, there is no group of borrowers whose net indebtedness on a consolidated basis exceeds 15% of the capital of the Company (as defined in Directive 313).

4. In December 2011, a government bill was passed in the first reading and transferred to the Constitution, Law, and Justice Committee to be prepared for the second and third readings. The bill sets forth several amendments to the Prohibition of Money Laundering Law and the Prohibition of Terrorism Financing Order, including with regard to reporting duties and the duty to receive identifying information. Discussions are also being conducted by the Constitution, Law, and Justice Committee regarding various amendments to the Money Laundering Prohibition Order applicable to banking corporations.

   In July 2012, a proposal to amend the Prohibition of Terrorism Financing Law, concerning the procedure for declaring terrorist organizations and terrorist operatives in Israel, was passed in a second and third reading.

5. In February 2012, the Constitution, Law, and Justice Committee approved an amendment to the Charge Card Regulations, pursuant to which the Supervisor will be able to issue directives that differ from the current text of the regulations with regard to the delivery of statements to customers. Directive 470 was amended accordingly in September 2012. The Company estimates that this amendment will have no effect on the Company.

6. In March 2012, the Justice, Technology, and Information Authority issued a draft guideline concerning restrictions on the collection of identification numbers by database owners. If the draft becomes binding in its current format, it is likely to have an impact on the Company; however, the Company cannot estimate the extent of this impact.

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7. In May 2012, the Knesset plenum passed a private bill, in a second and third reading, pursuant to which the Governor of the Bank of Israel would have the authority to set rules regarding the minimum font size for notifications sent to senior citizens (as defined in the Senior Citizens Law, 1989). The Company estimates that if such rules are established, they will have no material effect on the Company.

8. In June 2012, the Knesset plenum passed a government bill, in a first reading, which would update the list of causes with regard to conditions considered depriving conditions in uniform contracts, and establish rules with regard to the authority of the Uniform Contracts Court. At this stage, the Company cannot estimate whether the aforesaid bill will result in legislation, and if so, its implications for the Company, if any.

9. In July 2012, the Knesset plenum passed a government bill, in a first reading, for the promotion of competition and reduction of concentration. A discussion on this matter was held on August 29, 2012.

10. In July 2012, a private bill was passed in a second and third reading, according to which a condition in a uniform contract establishing a minimum rate for the CPI shall constitute a depriving condition. This amendment has been in effect beginning on November 12, 2012. The Company has prepared for the implementation of the law. The Company estimates that this law will have no material effect on the Company.

11. In July 2012, the Economics Committee held a discussion of the recommendations of the Committee for Increased Competition in the Banking Industry. The public was permitted to submit comments on the interim report until August 15, 2012. In addition, on August 14, 2012, the Bank of Israel published a draft of rules issued as a supplementary measure to the publication of the interim report of the Committee for the Examination of Increased Competition in the Banking Industry, in order to promote and improve the efficiency of the formal proceeding, reflecting the main points of the recommendations of the report in the area of fees. Following the completion of the process of consultation with the members of the Advisory Committee on Banking, and the examination of the responses of the parties who submitted their comments on the recommendations of the interim report in writing, a final version of the rules will be formulated. The Banking Rules concerning fees were published in November 2012, and took effect in January 2013. Among other matters, the rules cancel the fee for changing debiting dates of credit cards. In addition, the service provided by a clearer to a discounting service provider was declared a service subject to supervision. The Company estimates that this amendment will have no material effect on the Company.

12. In August 2012, the Knesset plenum approved an increase of the rate of value-added tax by 1 percent starting September 1, 2012.The Knesset plenum also approved an increase of the rate of income tax on individuals and the rate of employers' contributions to National Insurance. For further details, see Note 7 to the Financial Statements.

13. In October 2012, the Economics Committee passed a private bill, in a second and third reading, according to which customers should be notified before the immediate repayment of a loan granted to them by a banking corporation is demanded, or before a legal proceeding is initiated, as detailed in the bill. At this stage, the Company cannot estimate whether the aforesaid bill will result in legislation, and if so, its implications for the Company.

    In October 2012, the Knesset plenum passed the bill for dispersal of the 18th Knesset, in a second and third reading. The election recess began on October 16, 2012 and continued until the 19th Knesset took office on February 5, 2013. Legislative proceedings for private bills can continue in the 19th Knesset if they were passed in a first reading by the 18th Knesset, and if the law of continuity has been applied to them.

14. In November 2011, a government bill was passed in a first reading and transferred to the Constitution Committee for preparation for the second and third reading, concerning the establishment of an administrative enforcement mechanism to serve as an alternative to enforcement in a criminal proceeding with regard to violations of the Protection of Privacy Law. The committee discussion scheduled for July 2012 was canceled. In August 2012, a legislative memorandum was issued amending the Protection of Privacy Law, aimed at improving compliance with the provisions of the Protection of Privacy Law and regularizing the protection of information in computerized databases. The public was permitted to submit comments on the memorandum until August 28, 2012.

15. In January 2013, the Supervisor of Banks issued a circular concerning an amendment to Proper Conduct of Banking Business Directive No. 342, "Liquidity Risk Management." The circular was issued as part of the Supervisor of Banks' efforts to strengthen the robustness of the banking system. The amendment of the directive is aimed at strengthening and simplifying liquidity risk management at banking corporations, and constitutes an interim phase in advance of the future adoption in Israel of the Basel III recommendations concerning liquidity.

    The revised directive clarifies the need to maintain a liquidity cushion against predicted liquidity needs under stress scenarios, with a one-month horizon; details the Supervisor's expectations for risk monitoring on a group basis; establishes a requirement to examine the structure of sources of financing in conjunction with financing needs from a long-term perspective; and adds to the qualitative requirements for liquidity risk management.

    The Supervisor of Banks has not established specific rules for credit-card companies with regard to the aforesaid requirements, but mandates the qualitative requirements for risk management and holding of liquid assets to be fulfilled according to the needs of the company, with the necessary adjustments.

The implementation of the amendments to Directive 342 will begin in July 2013, with the exception of Section 16 concerning the stable credit ratio, which will take effect at the end of 2013.

16. With regard to new accounting standards and new directives of the Supervisor of Banks in the period prior to implementation, see Note 1G to the Financial Statements.

Legal Proceedings and Contingent Liabilities

1. As at the date of this report, several legal claims have been filed against the Company, arising from the ordinary course of its business, in immaterial amounts. Based on the opinion of its legal advisors, the Company estimates that the financial statements include adequate provisions, in accordance with generally accepted accounting principles, to cover possible damages arising from all of the claims, where such provisions are necessary.

2. In July 2010, the Company filed an appeal of its income-tax assessment for 2006. The dispute between the Company and the Tax Authority with regard to the tax assessment for 2006 concerns the sale of the shares of MC. In the opinion of the Company, the sale should be treated as an event requiring capital-gains tax, rather than as an event of redemption of shares, which carries a different taxation rate. Following a preliminary hearing held at the District Court of Tel Aviv, and after the Company submitted its summations, the Company and the Tax Assessment Officer reached a settlement in which the Company will pay a total of NIS 850,000. On December 31, 2012, the District Court approved the settlement and granted it the status of a ruling.

3. Indemnification of directors and other officers: The Company has undertaken a commitment to indemnify directors and other officers of the Company, as they may be from time to time. The indemnification letter approved by the general assembly on February 12, 2012, with the approval of the Audit Committee and the Board of Directors, was adjusted to changes in legislation. The amount of the indemnification to be provided by the Company under this commitment to all insured parties of the Company in aggregate in respect of one or more indemnity events shall not exceed 30% of its equity, according to the most recent (annual or quarterly) financial statements known before the actual payment.

Objectives and Business Strategy

The Company's key objectives and strategies are the following:

1. Maintaining the level of revenues and profitability.

2. Expansion of the distribution and sales-promotion base in order to develop the area of non-bank cards.

3. Continued implementation of the club strategy.

4. Maintaining brand image.

5. Extending collaborations with merchants.

6. Ongoing improvement in quality of service to banks, clubs, merchants, and cardholders.

7. Maintaining a high technological level: innovation and support for product and service development and for improvements in efficiency.

8. Targeted actions to create customer preference for the credit cards issued by the Company and make these cards customers' first choice.

9. Working in accordance with the ethical code of the Company.

Risk Management Policy

The Company's activity involves various financial risks: credit risks, which represent the risk that a borrower client or merchant will default on scheduled payments as defined in the agreement with the borrower; market risks deriving from exposure to changes in interest rates, exchange rates, and inflation; and liquidity risks. In addition, the Company is exposed to operational risks, which refer to losses arising from faulty processes, human errors, system failures, and external events.

The Company is also exposed to various qualitative risks, such as reputation risk, strategic risk, regulatory risk, legal risk, and compliance risk.

Risks are managed pursuant to Proper Conduct of Banking Business Directive No. 339 and in compliance with Proper Conduct of Banking Business Directives No. 201-211 (Capital Measurement and Adequacy).

According to a decision of Management, each member of Management manages operational risks in the area of activity for which he or she is responsible. In addition, the Head of Finance and Administration is responsible for market and liquidity risks, the Head of Credit and Financial Services is responsible for credit risks, the Head of Strategy is responsible for strategic risk and regulatory risk, and the Legal Advisor is responsible for the management of legal risk. The Company has a Head of Risk Management with the status of a member of Management. In addition, the organizational structure of the Risk Management Department was updated in the format outlined by the Bank of Israel. Among other matters, the functions of the department include independent supervision of the manner of management of risks at the Company, monitoring of risks, reports to Management and to the Board of Directors, validation of risk-measurement systems, involvement in the establishment of risk-management policies, and examination of the effectiveness of the Company's risk-management processes. In order to manage and minimize risks, the Company makes use of supporting computerized systems, among other means.

The Risk Management Committee of the Board of Directors was established during 2011. The Risk Management Forum headed by the CEO began to operate in 2011. The forum convenes quarterly, with the aim of ensuring adequate control coverage for risk-management processes and formulating an ongoing process for the improvement of effectiveness of risk-management control mechanisms at the Company, at the level of the risk-taking divisions, the independent control units in the divisions, and the Risk Management and Security Division.

Operational Risks

The Company has established a policy for the management of operational risks, as required by the Bank of Israel.

Within operational risk management, the organizational structure supporting the management of operational risks has been defined, including the roles of the Board of Directors and the Management Committee on Risk Management headed by the CEO. In addition, the Subcommittee on Operational Risk Management has been established, headed by the Head of the Risk Management Department; members of the committee include controllers from all departments of the Company and other officers such as the Compliance Officer, the officer responsible for money-laundering prevention, and the Head of Information Security.

As part of the management and control of operational risks, and as part of the compliance with Proper Conduct of Banking Business Directives No. 201-211 (Capital Measurement and Adequacy) in this area, the following steps have been taken:

- Operational risks identified in new processes and products.
- Appropriate controls established.
- Operational risk management and control system updated routinely.
- Business continuity plan and emergency preparedness plan established.
- Emergency procedures at the Company updated.

Market and Liquidity Risks

1. Market Risk Exposure and Management

The business activity of the Company is exposed to market risks arising from volatility in interest rates, exchange rates, the consumer price index, and the value of securities.

The Company does not actively create exposure to market risks. Ongoing management of these risks is therefore aimed at monitoring of the risks in relation to the policies established by the Company.

The Company's market risk management policy is based on common practices in the banking system in Israel and on the current instructions of Proper Conduct of Banking Business Directives No. 201-211 (Capital Measurement and Adequacy) regarding market risk management, adjusted to the unique risk profile of the Company. This policy was approved by the Board of Directors of the Company in May 2012. The policy includes limits on financial exposures, aimed at reducing the damage that may be caused by changes in the various markets and in rates of interest, foreign currency, the CPI, and shares. The Board of Directors of the Company updates these limits from time to time. The market risk management philosophy is congruent with the policy described in the Company's basic risk management document.

In addition, the Company has a designated function for the management and control of risks independently of the business functions. The Risk Management Department performs control over material risks at the Company; its roles are defined in the basic risk management document.

The Company manages market risks based on a comprehensive, integrative view, ensuring the optimal utilization of the capital and assets of the Company in order to achieve its strategic and business objectives while maintaining its stability. Market risks at the Company are managed by the Head of Finance and Administration.

In order to implement the requirements of the market risk management policy, Isracard, which administers and operates the Company's operations, as noted above, uses a targeted automated asset and liability management system.

A. Linkage Base Risk

This risk is defined as exposure to currencies and to the consumer price index, expressed as the loss that may occur as a result of the effect of changes in currency exchange rates and in rates of the consumer price index on the difference between the value of assets and liabilities.

The Company applies a comprehensive policy for the management of market risks in Israeli and foreign currency, designed to support the achievement of business objectives while assessing and limiting the losses that may arise from exposure to market risks.

B. Exposure to the Value of Securities

The Company's policy establishes a limited possibility for the execution of transactions in fixed-income, risk-free securities.

C. Derivative Financial Instruments

In general, the Company’s policy states that no activity for the purpose of trading in derivative financial instruments shall be conducted, with the exception of activity for the purpose of economic hedging.

2. Liquidity Risk Exposure and Management

The goal of the liquidity risk management process is to ensure, taking into account the risk tolerance that has been established, the Company's ability to finance the increase in its assets and to settle its liabilities on time, without falling into difficulties and without incurring material losses, including losses that may result from damage to reputation caused by an inability to finance the Company's business operations.

Liquidity risk includes the following risks: Liquidity raising risk – Risk arising from damage to the ability of the Company to raise liquidity, as a result of a loss of confidence in the Company by the market, which may result from events of damage to its reputation or damage to the market in which the Company operates.

Market liquidity risk – Risk arising from a comprehensive crisis in the markets, leading to a credit crunch, without connection to the Company's performance. Risk of impairment of liquid assets – Exposure to risk as a result of erosion of the value of liquid assets, which may damage the ability of the corporation to finance liquidity gaps.

The Company implements a comprehensive liquidity risk management policy, which was approved by the Board of Directors in November 2011. The policy is based on the prevalent sound practices in the Israeli banking system and on the current instructions of Proper Conduct of Banking Business Directives No. 201-211 (Capital Measurement and Adequacy) and Proper Conduct of Banking Business Directive No. 342 (2011 Draft on Liquidity Risk Management).

This policy is achieved by maintaining routine monitoring of the liquidity position of the Company through the use of an internal liquidity risk management model, monitoring of the indicator system for the identification of liquidity pressures, examination of extreme scenarios, and the use of an auxiliary system for current flow management. However, the disposable capital of the Company is given as credit to cardholders and merchants, and invested in deposits with banks in NIS.

Liquidity risks at the Company are managed by the Head of Finance and Administration.

Credit Risk

Credit risk is the possibility that borrowers or counterparties may default on their obligations under the agreed terms.

The credit policy of Isracard is approved each year by the Board of Directors of the Company. The credit policy addresses principles for granting credit, the type of exposure in each segment of activity, quantitative and qualitative exposure limits, credit concentration, pricing and collateral, handling customers experiencing difficulties, and the hierarchy of credit-granting authority.

The credit-management system relies on the delegation of credit authority at different levels. The overall responsibility for direct handling of customers rests with several authorized parties, leading to improved capability to manage credit risks and monitor and control the credit-granting process. Isracard routinely monitors and tracks borrowers through control reports generated at various cross-sections and frequencies.

Isracard regularly invests resources in training employees responsible for making decisions and assessing risks in the area of credit, and in improving the computerized control tools and information systems available to them.

Isracard also carries out routine control of internal and regulatory limits on the level of indebtedness of a single borrower and of a group of borrowers, in accordance with the requirements of Proper Conduct of Banking Business Directive No. 313 of the Bank of Israel.

Isracard monitors and supervises transactions with related persons, in accordance with Proper Conduct of Banking Business Directive No. 312, and files reports pursuant to Directive No. 815 of the Supervisor of Banks.

Isracard's credit-risk management is based on several statistical models, which are used to establish a score for each customer or merchant. This score is used to support decisions regarding the type of credit, volume of credit, and interest rate set for the customer or merchant. The models are tested periodically for quality and calibration and are established in accordance with internal and regulatory requirements.

As at the reporting date, the Company does not grant credit.

Credit Control Unit

The Company receives services for the purposes of credit control from Isracard, under the responsibility of the Head of Credit and Financial Services.

Capital Measurement and Adequacy

The Company assesses its capital adequacy. Starting with the financial statements as at December 31, 2009, the Company uses the standardized approach in the calculation of capital adequacy, in accordance with Proper Conduct of Banking Business Directives No. 201-211 (Capital Measurement and Adequacy).

The assessment is performed by a summation of capital and sorting of assets by risk rates and market-risk evaluations, with the addition of operational risk. Capital adequacy is determined by calculating the rate of capital out of total assets, weighted by the risk rate, as noted above, plus the market risk and the operational risk.

The Basel II recommendations establish three pillars, as published by the Supervisor of Banks and as integrated into Proper Conduct of Banking Business Directives 201-211:

- Pillar I: Minimum capital adequacy, with reference to levels of credit risks, market risks, and operational risks.
- Pillar II: Establishment of a system for management and control of the various risks, including supporting systems, risk management policy documents, and internal assessment of capital adequacy against the aggregate risks involved in the activity of the corporation.
- Pillar III: Disclosure requirements under the Basel II directives.

Basel III

1. On October 26, 2011, the Supervisor of Banks issued a letter entitled "Preparation for the Adoption of the Basel III Recommendations." According to the letter, the banking system in

Israel will adopt the recommendations of "Basel III: A regulatory framework for more resilient banks and banking systems," published in December 2010, after formulation and with adjustments. On December 11, 2011, the Supervisor of Banks issued a letter entitled "Draft Translation of Amendments to the Framework for Capital Measurement and Adequacy – Basel II," which contains amendments to the Basel II directives concerning securitization and market risks. On May 28, 2012, the Supervisor of Banks issued a letter entitled "Basel III – The position of the Supervisor of Banks."

The Basel III directives change the structure of regulatory capital, including through a focus on reinforcement of the components of capital, and the imposition of limits on the types of instruments to be included in Tier 1 capital and in Tier 2 capital. The directives also establish two new capital cushions: a cushion for the protection of capital and an anti-cyclical cushion, aimed at increasing supervision and adjusting the capital requirement to the risk profile of the company. In addition, the directives add a new limit, the leverage ratio, to the existing capital-adequacy ratios, and address liquidity ratios. The Company is examining the effect of these instructions, and will begin to implement them subject to the adoption of the instructions by the Supervisor of Banks. With regard to the effect on the core capital ratio, see the section "Capital Adequacy," below.

2. Minimum core capital ratios – In March 2012, the Supervisor of Banks issued a circular to all banking corporations and credit-card companies concerning the establishment of a minimum capital ratio higher than the current requirement. According to the directive, all banking corporations will be required to maintain a minimum core capital ratio of 9% by January 1, 2015. The core capital ratio is to be calculated in accordance with the Basel III directives and the adjustments to be established by the Supervisor of Banks.

   In addition, a large banking corporation whose total consolidated balance-sheet assets constitute at least 20% of the total balance-sheet assets in the banking system in Israel will be required to maintain a minimum core capital ratio of 10% by January 1, 2017.

   The Company is studying this directive and its expected implications in connection with the formulation of a revised capital plan, with the aim of ensuring the implementation of the directive and compliance with the new core capital ratio requirements.

Risk Appetite

The Board of Directors of the Company has defined its risk appetite and risk capacity, in line with the strategy and future business plans of the Company. Risk appetite reflects and defines the risk level to which the Company is willing to be exposed, or which it is willing to accept or sustain, during the ordinary course of business. Risk appetite serves as the basis for the allocation of resources and capital.

Risk capacity reflects the risk level which the Company will not exceed even in the event of the materialization of extreme scenarios. In light of the above, the maximum risk level undertaken by the Company during the ordinary course of business is lower than its risk capacity.

The Management of the Company is responsible for routine monitoring, and ensures through the definition and enforcement of appropriate risk limits that the Company operates within its declaration regarding risk appetite and risk capacity, as defined, through the use of risk limits, among other means.

Capital Adequacy Target

The capital target of the Company is the appropriate level of capital required in respect of the various risks to which the Company is exposed, as identified, estimated, and evaluated by the Company. This target is higher than the minimum regulatory capital requirement, and includes the capital requirements with respect to Tier 1 risks, in addition to capital with respect to Pillar II risks and a capital “cushion” enabling the Company to withstand losses in the event of external crisis events (extreme scenarios), while complying with the minimum regulatory capital requirement. This target takes into account actions by the Management of the Company aimed at reducing the risk level and/or enlarging the capital base.

The following are the Company's capital-adequacy targets:

The Company’s target ratio of core capital to risk-adjusted assets is 7.5%.

The Company’s target ratio of total capital to risk-adjusted assets is 12.5%.

Capital Management

The goal of capital management is to achieve compliance with the detailed risk-appetite definitions and the objectives of the Company, as established by the Board of Directors of the Company, subject to regulatory directives in the area of capital requirements, while striving to allocate capital efficiently. Accordingly, capital management shall:

- Ensure the existence of a capital base serving as protection against unexpected risks to which the Company is exposed, supporting business strategy, and allowing compliance at all times with the minimum regulatory capital requirement (refers to the mix and amount of capital backing the strategy and risks of the Company).
- Address future developments in the capital base and capital requirement;
- Strive for efficient allocation of capital during the ordinary course of business of the Company.

Guiding Principles in Capital Management

Capital management is an annual process with a rolling planning horizon of three years. Capital management is considered an integral part of the Company's strategic and financial plan. Capital management is based on the growth plans of the various business units, with the aim of assessing capital requirements during the period of the plan, and is used in the strategic planning process, in connection with feasibility and capital allocation to units.

The following table lists the required disclosures under Pillar III.

Capital Adequacy

1. Capital for the calculation of the capital ratio

	December 31, 2012	December 31, 2011
	In NIS millions	
Core capital and Tier 1 capital	7	185
Total overall capital	**7**	**185**

2. Weighted balances of risk-adjusted assets

	December 31			
	2012		2011	
	In NIS millions			
	Weighted balances of risk-adjusted assets	Capital requirement	Weighted balances of risk-adjusted assets	Capital requirement
Credit risk	4	*-	92	8
Operational risk	1	*-	3	*-
Total weighted balances of risk-adjusted assets	**5**	***-**	**95**	**8**

* Amount lower than NIS 0.5 million.

3. Ratio of capital to risk-adjusted assets

	December 31, 2012	December 31, 2011
	In percent	
Ratio of core capital and Tier 1 capital to risk-adjusted assets	140.0	194.7
Ratio of total capital to risk-adjusted assets	140.0	194.7
Minimum total capital ratio required by the Supervisor of Banks	9.0	9.0

The Company is examining the effects of the Basel III directives, based on the drafts and position statements of the Supervisor of Banks, as published from time to time, including the effect of the implementation arrangements that have been established. The initial implementation date of the aforesaid directives has not yet been determined.

No effect on the core capital ratio as at December 31, 2012 is expected, assuming full implementation of the directives.

As noted, this estimate is based on the drafts and position statements of the Supervisor of Banks; there may be changes to the final directives that may affect the Company's aforesaid estimate.

Applicability of Implementation

Requirements regarding capital measurement and adequacy apply to the Company. In addition, the Company is consolidated by Isracard Ltd., which is also subject to these requirements. In general, the capital requirements of the Company are based on its financial statements, which are prepared according to Proper Conduct of Banking Business Directives 201-211 (Capital Measurement and Management).

Structure of Capital

Structure of Regulatory Capital

Pursuant to the directives of Proper Conduct of Banking Business Directives 201-211 (Capital Measurement and Management), credit-card companies must maintain a ratio of capital to risk-adjusted assets of no less than 9% of the weighted average of the on- and off-balance-sheet risk-adjusted assets.

Capital measurement for the purposes of this directive is based on the division of capital into Tier 1 capital and Tier 2 capital. Tier 1 capital consists of equity.

Limits on the Capital Mix

The directive establishes limits on the capital mix in the various tiers; the main limits relevant to the Company are the following:

Total core capital shall constitute at least 70% of Tier 1 capital, after the required deductions from the capital in this tier only.

Total Tier 2 capital and Tier 3 capital shall not exceed 100% of total Tier 1 capital, after the required deductions for the capital in this tier only.

Structure of Capital

Set out below is the composition of capital for the purpose of calculating the capital ratio.

	December 31, 2012	December 31, 2011
	In NIS millions	
Core capital and Tier 1 capital		
Paid-up common share capital	1	1
Retained earnings	6	184
Total core capital and Tier 1 capital	7	185
Total eligible capital	**7**	**185**

Capital Adequacy

The Company applies the standardized approach to the assessment of its regulatory capital adequacy (with respect to credit risks, market risks, and operational risks).

The Company performs an internal process of assessment of its capital adequacy, within which a multi-year plan has been created for attainment of the capital-adequacy objectives. This plan takes into consideration the Company's present and future capital needs, according to its strategic plans, as compared to its available sources of capital. The plan addresses all present and future risk-adjusted assets of the Company, according to the required allocation under Proper Conduct of Banking Business Directives 201-211 (Capital Measurement and Management), with reference to the capital-adequacy targets and risk appetite.

Risk-Adjusted Assets and Capital Requirement

Set out below are risk-adjusted assets and capital requirements in respect of credit risk, market risk, and operational risk.

	December 31, 2012		December 31, 2011	
	In NIS millions			
	Weighted balances of risk-adjusted assets	Capital requirement	Weighted balances of risk-adjusted assets	Capital requirement
Credit risk:				
Banking corporations	4	*-	92	8
Total credit risk	4	*-	92	8
Operational risk	1	*-	3	*-
Total weighted balances of risk-adjusted assets / capital requirement	**5**	***-**	**95**	**8**

* Amount lower than NIS 0.5 million.

	December 31, 2012	December 31, 2011
Total capital ratio and Tier 1 capital ratio		
Capital for the calculation of the capital ratio (in NIS millions)	7	185
Ratio of core capital and Tier 1 capital to risk-adjusted assets	140.0%	194.7%
Ratio of total capital to risk-adjusted assets	140.0%	194.7%
Minimum capital ratio required by Supervisor of Banks – Pillar I	8.0%	8.0%
Minimum capital ratio required by Supervisor of Banks – Pillar II	1.0%	1.0%
Total minimum capital ratio required by Supervisor of Banks	9.0%	9.0%

Credit Risk – General Disclosure Requirements

Pursuant to the directives of the Supervisor of Banks concerning the measurement and disclosure of impaired debts, credit risk, and the allowance for credit losses, and the amendment of the directives on the treatment of problematic debts, beginning on January 1, 2011, the Company has implemented the American accounting standards in this area (ASC 310) and the position statements of the bank supervision agencies in the United States and of the Securities and Exchange Commission in the United States, as adopted in the Public Reporting Directives. In addition, beginning on that date, the Company has implemented the directives of the Supervisor of Banks concerning the treatment of problematic debts. The implementation of the aforesaid directives has no effect on the Company, given that Isracard operates and administers issuance activity and clearing activity in Israel of transactions executed with merchants using MasterCard cards, on behalf of the Company.

Credit Risk Management

Credit risk is one of the risks managed, monitored, and controlled by the Company, as a necessary characteristic of its activity as a company engaged in granting credit. The credit risk management process aids the Company in reviewing risk according to the component product mix.

Activity of the Company in the area of credit-risk management:

- The Company sets limits on the granting of credit , by risk rating, with segmentation by credit products (according to the products' risk weighting), in order to prevent damage to the quality of the Company's credit portfolio, thereby reducing credit risk arising from borrower quality.

- The Company conducts internal controls of credit-risk management by assigning a risk weighting to each type of credit product, according to its derived risk. For example, in certain cases, references are made to the type of product sold by the merchant and to its supply times; the longer the supply time of the product, the higher the probability of a failure to deliver the product to the customer.

- The Company sets sectoral limits in order to prevent sectoral concentration in the credit portfolio.

- The Company acts in accordance with the guidelines of the Bank of Israel in Directive No. 313, Limits on the Indebtedness of a Single Borrower and of a Group of Borrowers. Applying this directive and setting internal limits reduces borrower concentration risk.

- The Company has set internal limits on its exposure to financial institutions, in congruence with the risk appetite approved by the Board of Directors.

The Company monitors and supervises transactions with related persons, in accordance with Proper Conduct of Banking Business Directive No. 312, and files reports pursuant to Directive No. 815. The Company tracks damages arising from the abuse of credit cards.

Principles of Credit Concentration Risk Management

- In accordance with the second pillar of Basel II, the Company calculates an internal capital allocation, as required, against concentration risks.

- Borrower concentration – routine monitoring of the major borrowers of the Company; compliance with limits required in Proper Conduct of Banking Business Directive No. 313 (Single Borrowers and Borrower Groups) of the Bank of Israel. In addition, the Company reports to the Bank of Israel on a quarterly basis, in accordance with the directive.

Assigning Risk Ratings to Customers Based on Statistical Models

- The Company routinely invests in models for rating the credit risk of private and business customers. The models are matched to the credit products, economic conditions, and target population to receive the credit.
- Models are divided as follows:
  1. AS (application scoring) model for new customers;
  2. BS (behavior scoring) model – a behavioral model for customers of the Company;
  3. SME (small-medium enterprise) model – a model for business clients.
- The risk-rating models are used to support decisions regarding the type of credit, volume of credit, and interest rate set for the customer or merchant.
- The development of risk ratings in the credit portfolio is routinely controlled and monitored.
- The models are tested periodically for quality and calibration by the Model Development Unit in the Credit and Financial Services Division, and validated by the Risk Management Department (the second level of controls).

Establishing the Hierarchy of Credit Granting Authority

The establishment of the hierarchy is aimed at maintaining the quality of the Company's credit portfolio, while supervising credit approvals, according to the appropriate professional authority. Credit is granted at the Company according to a hierarchy of authority, including:

- Authorization for maximum exposure according to the authority of the responsible party (in accordance with the risk-rating model).
- Defined authorizations for deviations for exceptional transactions, according to the authority of the responsible party.
- Defined hierarchy of authority for the establishment of the interest rate for the credit.

Exposure to Financial Institutions

The Company's operations involve exposure to financial institutions, in Israel and globally:

- Credit-card companies in Israel and globally – Cross-clearing activity occurs between the Company and credit-card companies in Israel. In addition, the Company has exposure to global credit-card companies.
- Banks in Israel – Credit-card activity under the responsibility of banks is conducted with customers' accounts at Israeli banks. In addition, deposits and hedging transactions create exposure to the bank with which the transaction was executed.

- Foreign financial institutions – Activity with overseas entities or activity by foreigners in Israel: deposits of foreign currency with financial institutions abroad. The Company's exposure is immaterial.

The Company routinely monitors these exposures and reports exceptions from limits.

Credit exposure to financial institutions results from:

- Transactions in credit cards issued by banks with which the Company has arrangements – the exposure is formed when the Company uses its own funds to finance the time gap between the date of crediting the merchant and the date of transfer of the payments by the Banks Under Arrangement. If a bank becomes insolvent, there is a risk that the funds may not be transferred to the Company, which would then absorb the losses.

- Deposits with banks – deposits performed by the Company with banks create an automatic exposure to such banks.

Independent Supervision

The Chief Risk Officer maintains independent supervision of the manner in which credit risks are managed at the Company. This supervision includes:

- Checking compliance with credit policy directives and with the instructions of the Bank of Israel.

- Active involvement in establishing credit policy, including credit limits. Control over the implementation of credit policy.

- Identifying new risks and emerging risks.

- Reporting the results of the monitoring to senior management and to the Board of Directors.

- Monitoring risk-assessment models.

Reports to Management and the Board of Directors and Compliance with Policies and Procedures

- The Company's credit policy is updated and approved by the Board of Directors each year, according to developments at the Company, in the industry, and in the economy.

- The Company's Management is provided with data on the Company's credit-portfolio mix each month. The mix presents the segmentation of the portfolio in terms of credit products, sectors, risk ratings, geographical distribution, compliance with regulatory and internal limits, a risk-return analysis, and more.

- The credit-portfolio mix is presented to the Board of Directors of the Company on a quarterly basis.
- The Chief Risk Officer submits an independent report to Management on the control over credit-risk management each month.
- The Chief Risk Officer submits an independent report to the Board of Directors each quarter.
- Working procedures at the Company are updated routinely by the various departments.

Credit Exposures

The following tables present details of credit exposure by risk weightings, with segmentation of the exposure by counterparty (segment), before and after credit-risk mitigation.

Gross credit risk exposures, by principal type of credit exposure:

	December 31, 2012		December 31, 2011	
	Balance-sheet credit risk		Balance-sheet credit risk	
Type of exposure	Credit	Total balance-sheet credit risk	Credit	Total balance-sheet credit risk
	In NIS millions			
Banking corporations	7	7	185	185
Total exposures	**7**	**7**	**185**	**185**

Average gross credit risk exposures, by principal type of credit exposure:

	December 31, 2012		December 31, 2011	
	Balance-sheet credit risk		Balance-sheet credit risk	
Type of exposure	Credit	Total balance-sheet credit risk	Credit	Total balance-sheet credit risk
	In NIS millions			
Banking corporations	10	10	184	184
Other assets	-	-	*-	*-
Total exposures	**10**	**10**	**184**	**184**

* Amount lower than NIS 0.5 million.

Credit Risk Mitigation (CRM)

Amounts of exposure, before/after credit-risk mitigation, according to the standardized approach

Credit Risk Weighting

The following table presents details of credit exposure, before and after credit-risk mitigation.

		December 31, 2012		
	Rating	**0%**	**50%**	**Credit exposure**
Banking corporations	Unrated	-	7	7
Total		**-**	**7**	**7**

		December 31, 2011		
	Rating	**0%**	**50%**	**Credit exposure**
Banking corporations	Unrated	-	185	185
Total		**-**	**185**	**185**

Credit Risk Weighting

The Company implements the standardized approach to determine risk weightings to apply to the counterparty. The standardized approach requires the use of independent ratings by international rating agencies.

Credit rating agencies used:

Credit rating agency	Used for
Moody's	Corporations, banks
S&P	Corporations, banks
Fitch	Banks

Adjustment of each agency's scale to risk groups: The Company uses standard mapping.

General Disclosure Regarding Exposures Related to Counterparty Credit Risk – OTC Derivatives

The Company's policy states that no activity for the purpose of trading in derivative financial instruments shall be conducted. The only activity in derivative financial instruments permitted to the Company is for the purposes of economic hedging.

No transactions in derivative financial instruments were executed during the reported period.

Hedging Interest-Rate Exposures

The financial activity of the Company is usually characterized by a parallel between the average duration of assets and liabilities (mainly short-term); i.e. customers' activity ("debtors in respect of credit cards") versus liabilities to merchants ("creditors in respect of credit-card activity"). However, the Company also extends credit for the medium term (usually up to one year, and sometimes up to three years). In addition, the Company grants credit at fixed interest rates, which creates a gap in durations and generates exposure to changes in interest rates during the ordinary course of the Company's operations.

Hedging Foreign Currency Exposures

The Company's currency exposure is managed through daily matching of assets and liabilities in foreign currency (and linked to foreign currency) through foreign currency current accounts with banks, where the goal is to bring the net position to zero at the end of each day.

The Company occasionally uses forward contracts to hedge currency risk in long-term purchasing transactions.

Disclosure by Companies Using the Standardized Approach

General

The Company accounts for all of its assets and liabilities using the standardized measurement approach, as defined in Proper Conduct of Banking Business Directives 201-211 (Capital Measurement and Management).

The Company does not have a trading portfolio, and all of its assets and liabilities are part of the banking book.

Strategy and Processes

The Board of Directors of the Company approves the market risk management policy of the Company on an annual basis. The Board of Directors is involved in risk management, particularly in setting limits and restrictions for the volume of activity and exposures.

The Company's strategy in the management of market risks is to minimize risks arising from its main areas of activity (issuance, clearing, and credit); the Company has a very low "risk appetite" for market risks.

Within this strategy, the Board of Directors and Management of the Company approve the Company's policy document, on an annual basis. The policy document is based on the following key principles:

- **Organization and control** – A market and liquidity risk management function headed by the Head of Finance and Administration; an internal investment committee headed by the Chief Risk Controller; the Audit Committee; and the Board of Directors.
- **Procedures and policies** – The areas of responsibility and authority in the area of risk management assigned to Management, the Board of Directors, the Audit Committee, and specialized functions such as the Risk Manager are formalized in clear, accessible documentation, with the aim of ensuring uniform implementation in the organization.
- **Risk management processes** – Processes are in place for the routine identification of exposures, risk assessment, examination of controls, and risk minimization processes (including limits).
- **Tools and technologies** – A computerized system supporting risk assessment, risk management, reporting, monitoring, and planning.
- **Reporting and monitoring of risks** – Reports from each business line of the Company to the central Market and Liquidity Risk Management Unit in a structured process, in which exposures are reported to Management and to the Board of Directors; proper intra-organizational communication channels ensure timely reporting of issues that need to be addressed.

For the purpose of the control and management of market and liquidity risk, the Financial Management Unit in the Finance and Administration Division, under the authority of the Head of Market and Liquidity Risk, works to identify, measure, monitor, and report on market and liquidity risks, in practice, on a routine basis.

Structure and Organization of Market Risk Management Function

The market risk management system of the Company is based on an integrative system for the management of exposures, composed of the following functions:

Market Risk Manager

The Head of Finance and Administration is the manager of market risks at the Company. Within this framework, he is responsible for the formulation, implementation, and absorption of a comprehensive policy for the management of all market and liquidity risks to which the Company is exposed (currency, CPI, interest rate, securities, liquidity), including:

- Responsibility for financial exposures at the Company, subject to limits approved by the Board of Directors.
- Procedures for monitoring and control on matters related to exposure management.
- Conducting a biweekly financial meeting to formulate activity in the area of market and liquidity risks (the investment committee).
- Monthly reports on market and liquidity risk to the Board of Directors.
- Management of foreign currency risks, including decisions regarding hedging of long-term foreign currency exposures.
- Asset and liquidity management (ALM).
- Routine measurement and control of the market and liquidity risk indices of the Company.
- Preparation of reports on interest-rate risks.
- Analysis of results and preparation of findings for discussion by Management and the Board of Directors.

Chief Risk Officer

The Chief Risk Officer of the Company is responsible, as part of his duties, among other matters, for control of the market risks of the Company. Within this framework, he is responsible for controlling the Company's market risk management policies and processes.

The Chief Risk Officer assists the Board of Directors of the Company in approving and examining the market risk management strategy and the policy rules in this area, with reference to new products and processes at the Company.

The Chief Risk Officer assists Management in the control of the market risk strategy approved by the Board of Directors by examining compliance with policies and procedures for the identification, measurement, monitoring, and control of market risks. The Chief Risk Officer reports directly to the CEO of the Company and performs independent control of the exposure to market risks.

Nature and Volume of Risk Reporting and Measurement Systems

An RMS (Risk Management System) has been acquired, and has been in use since the first quarter of 2010. The RMS serves as a strategic instrument for the management of market risks to which the Company is exposed as a result of gaps between the nature of assets and liabilities.

Risks are measured in the following reports:

ALM reports: fair value, duration, internal rate of return, interest rate gap, cash flows.

Stress reports: tests of the sensitivity of the portfolio to changes in risk factors.

ISRACARD GROUP

Risk Monitoring and Minimization Policy

Interest-Rate Exposure Management

Exposure is monitored through reports on the effect of changes in interest rates. In the event that an exception from the limits established is identified, the exposure is reduced by considering fixed-rate credit granting activity and considering the purchase of interest-rate hedging transactions.

Foreign Currency Exposure Management

Transactions are hedged using derivative and other financial instruments at banks. The Company's policy is to bring foreign currency exposure to zero. However, immaterial exposures form as a result of differences in timing between the dates of calculation and the dates of accounts settlement in foreign-currency transactions. The Company monitors these differences and buys and sells foreign currency in order to hedge the exposure.

Operational Risk

Operational risk is managed by the members of Management at the Company, each with regard to the area for which he or she is responsible. The Head of Risks and Security at the Company is responsible for independent supervision of the management of risks at the Company (second level). The management of operational risks at the Company is intended to minimize losses by establishing orderly processes aimed at reducing the operational risks to which the Company is exposed. In this process, authority and responsibility frameworks are established, and a culture of operational risk management is instilled in all managers and employees.

Capital Requirement in Respect of Operational Risk

	Capital requirement	
	December 31, 2012	December 31, 2011
	In NIS millions	
Operational risk	*-	*-

* Amount lower than NIS 0.5 million.

The Company has a policy for the management of operational risks, which includes the following objectives:

- To manage operational risks as an integral part of the working processes of the Company, including the introduction of new products and processes.
- To maintain effective controls of risks according to risk ratings.
- To ensure effective identification of operational risks in all of the main processes at the Company.
- To create a work culture that encourages an organizational culture of risk management.
- To report loss events on a regular basis, according to the rules defined in the policy.
- To comply with legal and regulatory requirements regarding operational risks.
- To manage and allocate capital optimally in respect of operational risks.
- To establish a business continuity and emergency preparedness plan.

Within its operational risk management policy, the Company has defined the supporting organizational structure in detail, including the duties and responsibilities of the Board of Directors, Management, the Chief Risk Officer, the Information Systems Division, the departmental risk controllers, and the various business units.

Once every three years, the Company performs a survey of operational risks, as follows:

- Full mapping of all operational processes at the Company.
- Classification of the processes into groups, according to the classification methodology in Proper Conduct of Banking Business Directives 201-211 (Capital Measurement and Adequacy).
- Mapping of all controls relevant to each risk, including residual risk, and additional recommended controls if necessary.
- Rating of risk levels in each process on a scale of the level of damage / expected frequency.
- Implementation of a multi-year action plan to reduce material risks and increase controls where necessary.

Each quarter, the Chief Risk Officer reports to Management and the Board of Directors on operational risks, as follows:

- Material damage events and consequent actions taken.

- New operational processes at a high level of risk and actions taken to increase controls and minimize risk.
- Approval of changes in operational risk policy.

All events of damage at the Company are collected into a single database. All material events (the materiality threshold as at December 2011 is NIS 10,000) are reported on a quarterly basis to Management and the Board of Directors. The events are analyzed in order to ensure that a relevant operational process exists and that the existing controls are sufficient in order to reduce the risk of an additional event. If necessary, additional controls are added to the process.

Material operational risks are mitigated by:

- Adding controls for identification and prevention, according to risk level.
- Acquiring appropriate insurance, including property insurance, professional liability insurance, and insurance against fraud, embezzlement, and computer crimes.

Prohibition of Money Laundering and Financing of Terrorism

The legislation applicable to credit-card companies in Israel with regard to the prohibition of money laundering and financing of terrorism is the following:

- The Money Laundering Prohibition Law, 2000.
- The Money Laundering Prohibition Order (Identification, Reporting, and Record-Keeping Duties of Banking Corporations for the Prevention of Money Laundering and Terrorism Financing), 2001.
- The Terrorism Financing Prohibition Law, 2005.
- Proper Conduct of Banking Business No. 411 of the Bank of Israel, Prevention of Money Laundering and Terrorism Financing and Identification of Customers (this directive was updated in December 2011).

Order for the Prohibition of Trade with the Enemy

The Company applies controls with regard to private customers and merchants defined as high risk.

The Company maintains routine controls in several areas, in order to ensure that it possesses the required information and documents, in accordance with the directives. Any gaps are addressed and resolved.

Employees are required to maintain current knowledge in this area through computerized tutorials. In addition, specific training sessions are held for the various departments concerned with the prohibition of money laundering and financing of terrorism.

The Company's procedures are updated and expanded from time to time in order to fully cover all topics in accordance with the requirements.

The Compliance Officer coordinates the Compliance Committee, the Compliance Trustees Forum, and the Money Laundering Prohibition Team.

Routine reports are submitted to the Israel Money Laundering Prohibition Authority regarding ordinary transactions (pursuant to the directives of the Order) and unusual transactions. In addition, monthly reports are submitted to the Bank of Israel.

Critical Accounting Policies

The financial statements of the Company are prepared in conformity with generally accepted accounting principles in Israel and in accordance with the directives and guidelines of the Supervisor of Banks, the main points of which are described in Note 1 to the Financial Statements, "Significant Accounting Policies," in the section concerning the implementation of accounting principles. When preparing the financial statements, the Management of the Company uses assumptions, estimates, and evaluations that affect the reported amounts of assets and liabilities (including contingent liabilities), and the results reported by the Company.

Some of these estimates and evaluations involve uncertainty, and may be affected by possible future changes.

The Management of the Company is of the opinion that the estimates and evaluations applied during the preparation of the financial statements are fair, and were made to the best of its knowledge and professional judgment, as at the date of preparation of the financial statements.

Contingent Liabilities

The Management of the Company includes sufficient provisions in the financial statements, to the extent necessary, to cover possible damages arising from all legal claims, based on legal opinions. In most legal proceedings, external legal counsel is obtained. These assessments by legal advisors are based on the best of their judgment, taking the stage reached by the proceedings into consideration.

It should be taken into account that in the legal field, “certain” or “near certain” estimates cannot be made, not only in the initial stages of the claim, but until a ruling is handed down. Accordingly, the outcome of the proceedings may differ from the estimates performed. In light of the foregoing, the actual outcomes of legal claims may differ from the provisions made.

Discussion of Risk Factors

The main risk factors to which the Company is exposed have been mapped. This mapping and the assessment of the risks and of the effects thereof are subjective estimates by the Management of the Company.

Risk factor		Brief description	Effect
1.	Overall effect of credit risks	Risk arising from borrowers' failure to fulfill their obligations to the Company. Deterioration in the stability of the various borrowers may have an adverse effect on the Company's asset value and profitability. To minimize this risk, the Company has a defined credit policy and exposure limits with regard to borrowers/sectors in the various segments of activity, by risk level.	Medium
1.1.	Risk in respect of the quality of borrowers and collateral	Deterioration in the quality of borrowers and in the value of collateral provided to the Company to secure credit may have an adverse effect on the probability of collecting the credit. The Company has a credit policy and exposure limits with regard to different types of borrowers in the various segments of activity and products, and a process is in place for the control of compliance with these limits.	Medium
1.2.	Risk in respect of sectorial concentration	Risk arising from a high volume of credit granted to borrowers belonging to a particular sector of the economy. Deterioration in business activity in such an economic sector may lead to damage to repayment capability and to the value of collateral provided by some borrowers belonging to the sector.	Low
1.3.	Risk in respect of concentration of borrowers/ borrower groups	Present or future risk arising from deterioration in the condition of a large borrower or group of borrowers relative to the credit portfolio, which may cause an adverse effect on the probability of collecting the credit. The Bank of Israel has set limits on the maximum exposure to borrowers and groups of borrowers, and control of compliance with these limits is carried out routinely.	Low
2.	Effect of market risks: interest rate / inflation / exchange rate risks	Present or future risk to the Company's revenue and capital arising from changes in interest rates, currency exposures, and exceptional changes in the consumer price index. Such changes may cause the Company to suffer losses and/or a reduction in revenue.	Low

Risk factor		Brief description	Effect
3.	Liquidity risk	Present or future risk to the Company's revenue and capital arising from an inability to supply its liquidity needs. In exceptional demand and supply situations in the financial markets, unplanned costs may be incurred in raising resources. The Company has taken action to diversify its liquidity sources.	Low
4.	Operational risk	Present or future risk to the Company's revenue and capital that may arise from failed or faulty internal processes, human actions, system malfunctions, or external events. This includes the risk of embezzlement and fraud as well as legal risk, but does not include strategic risk and reputation risk. Failures related to one of the aforesaid factors may cause possible damage to profitability. The Company has an operational risk management policy, and operates units, procedures, and systems in the areas of human resources, information security, security, process control, survivability and recovery, and more.	Medium
5.	Legal risk	Present or future risk to the Company's revenue and capital resulting from unexpected events such as legal claims, including class-action suits, inability to enforce contracts, or rulings against the Company, which may cause damage to the Company's profitability.	Low
6.	Reputation risk	Damage to the Company's reputation as a stable, credible credit-card company in the eyes of customers, business partners, and regulatory agencies may lead to the transfer of customers' activity to other companies, causing damage to the Company's activity and profitability.	Low
7.	Competition	The credit-card industry in Israel is characterized by a high level of competition, both in the area of bank cards and in the area of non-bank cards, as reflected in the loss of customers or reduction of customers' activity, or the termination of the contractual engagement with one of the Banks Under Arrangement, and entails extensive, constant investments in customer recruitment and retention (cardholders and merchants).	Medium

Risk factor		Brief description	Effect
8.	Regulation and legislation	Present or future risk to the Company's revenue and capital arising from legislation and/or directives of various regulatory agencies that cause changes to the Company's business environment. Such changes may occasionally influence the Company's activity, revenue, and ability to offer certain services, and/or may obligate the Company to carry out technological and other investments at considerable cost, while disrupting schedules for development of other planned services. Also see the section "Restrictions and Supervision of the Company's Operations," above.	Medium
9.	Strategic risk	The risk of damage to the Company's profit and capital as a result of business decisions and/or the implementation of business decisions. Strategic risk is influenced by external and internal risk factors.	Medium
10.	Cessation of operation of a bank in Israel	The cessation of operation of a bank in Israel, in particular one of the Banks Under Arrangement, including due to collapse as a result of insolvency, could lead to a situation in which that bank is unable to meet its obligations under its agreements with the Company, and may lead to a situation in which the Company is unable to fully or partially collect debits owed to it by customers of the relevant bank.	Medium
11.	Cessation of operation of an international credit-card organization	The cessation of operation of an international credit-card organization, in particular the MasterCard Organization, may materially impair the Company's operations and financial results. In addition, collapse or insolvency of one of the Affiliate Members of the Company (a Principal Member) could lead to a situation in which the Company is obliged to bear debts, damages, and liabilities in amounts that may be material, leading to damage to its financial results.	Medium

Information Security and Cyber Risks

On December 6, 2012, the Supervisor of Banks issued a final letter on "Effects of information security and cyber risks on the report to the public." According to the letter, banking corporations and credit-card companies are required to assess information-security risks and take all relevant information into consideration, including past cyber attacks and the severity and frequency of such incidents. This includes a requirement to assess the probability of cyber attacks and the qualitative and quantitative volume of information-security risks, including potential costs and other implications arising from disruptions of activity or from the illegal use of assets or of sensitive information. In addition, the adequacy of preventive actions taken to minimize information-security risks and cyber attacks must be taken into consideration.

Cyber attacks may result from intentional attacks or from unintentional events. Among other matters, cyber attacks include obtaining unauthorized access to computerized systems with the aim of making illegal use of assets or of sensitive information, damaging information, or disrupting activity. Cyber attacks may be carried out in a manner that does not require obtaining unauthorized access, such as in the case of attacks designed to shut down website services.

As a result of cyber attacks, banking corporations and credit-card corporations may bear significant costs, and may suffer negative consequences, including, among others:

1. Theft of financial assets, intellectual property, or other sensitive information of the banking corporation, of its customers, or of its business partners;
2. Disruption of the activity of the banking corporation or of its business partners;
3. Recovery costs;
4. Additional expenses in the area of protection and information security;
5. Loss of income as a result of unauthorized use of proprietary information, or due to failure to retain or attract customers following an attack;
6. Legal claims;
7. Damage to reputation.

In the opinion of the Company, the extent of the effect of information security and cyber attack risks is moderate.

Disclosure Regarding the Internal Auditor

The Company receives internal audit services from Bank Hapoalim B.M. (hereinafter: “**the Bank**”).

Information regarding the Internal Auditor – Mr. Jacob Orbach has served as Chief Internal Auditor of the Company from January 1, 2010. Mr. Orbach has worked at the Bank Hapoalim Group since 1980, and is employed full-time. He holds a B.A. degree in Economics from Tel Aviv University and has experience in the areas of banking and auditing. Mr. Orbach meets the conditions stipulated in Section 3(A) of the Internal Audit Law, 1992 (hereinafter: the “**Internal Audit Law**”). The Internal Auditor is not an interested party of the Company or its subsidiaries, and holds no other office in addition to his position as Chief Internal Auditor of Bank Hapoalim and of some of the subsidiaries in the Bank Group (including the Isracard Group), as required under Section 146(B) of the Companies Law and Section 8 of the Internal Audit Law.

The appointment and termination of internal audit employees are subject to approval by the Internal Auditor; internal audit employees receive instructions on audit-related matters only from the Internal Auditor or from internal audit executives authorized by him; in general, internal audit employees do not hold other positions in addition to internal auditing; Internal Audit employees are authorized to sign on behalf of the Company only documents related to audit work, as required under the directives of Section 8 of the Banking Rules (Internal Audit), 1992 (hereinafter: the "**Audit Rules**"). The Internal Auditor is a full-time employee of Bank Hapoalim, with the rank of a Member of the Board of Management, Deputy to the General Manager.

Appointment method – The appointment of the Internal Auditor was approved by the Board of Directors of the Company on December 29, 2009, following the recommendation and approval of the Audit Committee on December 29, 2009.

Superior officer of the Internal Auditor – The Chief Internal Auditor reports organizationally to the Chairperson of the Board of Directors.

Work plan – Internal auditing is conducted in accordance with an annual work plan and a three-year long-term work plan. The work plan for 2012 was derived from the multi-year plan, which is based on the following, among other matters: risk assessment at audited units; embezzlement and fraud survey; updated organizational structure of the Company; audit rounds at various units; and findings discovered in previous audits. In order to formulate the work plan, the audit team held discussions and consultations with the Chairperson of the Board of Directors and the CEO of the Company. The audit work plan also includes examination of the approval processes of material transactions, if any, all based on a comprehensive perspective with a focus on risks.

Following the formulation of the audit work plan by Internal Audit, the plan was submitted for discussion by the Audit Committee; subsequently, taking the committee's recommendations into consideration, the plan was discussed and approved by the Board of Directors.

The Internal Auditor has the discretion to diverge from the work plan in response to changing, unexpected needs. The work plan includes resource allocation for audits of special events and unplanned audits, including audits by demand of authorized parties, such as the Board of Directors, the Audit Committee, Company management officials, and regulators. Material changes to the work plan are discussed and approved by the Audit Committee and by the Board of Directors. The Internal Audit work plan also addresses the activity of subsidiaries.

Auditing resources – 23 audit days were invested directly at the Company in 2012. Activities outsourced by the Company to its parent company Isracard are audited within the internal audit at that company. The volume of resources in internal auditing is determined according to the multi-year work plan, which is based on a risk survey.

Remuneration – Mr. Orbach was not remunerated by the Company. Auditing is supplied through outsourcing, and the Company pays the Bank for the internal auditing services based on the number of work days of the auditors. In the opinion of the Board of Directors, the aforesaid payments are not such that would affect the professional judgment of the Internal Auditor.

Performing the audit – Internal Audit at the Company operates under laws, regulations, directives and guidelines of the Supervisor of Banks (including Proper Conduct of Banking Business Directive 307, The Internal Audit Function, which took effect on July 1, 2012), professional standards, professional guidelines of the Institute of Internal Auditors in Israel, and guidelines of the Audit Committee and of the Board of Directors.

Having examined the Internal Audit work plan and the actual execution of said plan, the Board of Directors and the Audit Committee believe that the Company's internal auditing complies with the requirements established in the professional standards and in the directives of the Supervisor of Banks.

Access to information – Internal Audit has unrestricted access to all information at the Company, including constant unmediated access to the Company's information systems, including financial data, as necessary to perform its duties.

Internal Auditor's report – Internal Audit reports, including periodic reports, are submitted in writing. Audit reports are submitted to the Chairperson of the Board of Directors, the Chairperson of the Audit Committee, and the CEO of the Company, and are also distributed to the members of the Audit Committee. Audit reports are discussed by the Audit Committee.

Summary of Internal Audit activity – A summary of audit activities for 2011 was submitted to the Audit Committee in March 2012, and discussed by the committee on July 2, 2012. A summary of audit activities for 2012 is expected to be submitted to the Audit Committee during the first quarter of 2013.

Evaluation of the activity of the Internal Auditor by the Board of Directors – In the opinion of the Board of Directors and of the Audit Committee, the volume, nature, continuity of activity, and work plan of Internal Audit are reasonable under the circumstances, and are sufficient to realize the Company's internal auditing objectives.

Disclosure Regarding the Procedure for Approval of the Financial Statements

The Board of Directors of the Company is the organ charged with overarching control at the Company. As part of the procedure for approval of the Company's financial statements by the Board of Directors, a draft of the financial statements and a draft of the Board of Directors' report are delivered for perusal by the members of the Board of Directors several days prior to the meeting scheduled for the approval of the reports. The CEO of the Company reviews the ongoing activity of the Company and the effect of this activity on its results, and highlights material issues for the members of the Board of Directors.

During the meetings (the meeting of the Audit Committee and the meeting of the Board of Directors), the financial statements are discussed and approved, and the Head of Finance and Administration reviews main items in the financial statements, material issues in financial reporting, material evaluations and critical estimates implemented in the financial statements, the plausibility of the data, including an analysis of the results in relation to the results of the corresponding period in the previous year and in relation to the budget, and material changes in the accounting principles applied.

This meeting is attended by representatives of the Company's external auditors, who add their comments and insights with regard to the financial statements and with regard to any clarification required by the members of the Board of Directors.

Any significant flaws discovered in the establishment or operation of internal controls over financial reporting are also presented to the Audit Committee and to the Board of Directors. The reports are signed by the Chairperson of the Board of Directors, the CEO of the Company, and the Chief Accountant.

The Board of Directors

In 2012, the Board of Directors of the Company continued to set forth the Company's strategy, policy, and the guiding principles for its activity.

The Board of Directors addressed the approval of the quarterly and annual financial statements (further to the discussion and recommendations of the Audit Committee); the organizational structure of the Company; establishment of policy on manpower, salaries, retirement terms, and the remuneration system for employees and senior executives; and supervision and control over ongoing business operations executed by Management and the congruence of these operations with the policies of the Company.

The plenum and the Audit Committee held detailed discussions of the various aspects of the Company's activity.

17 meetings of the plenum of the Board of Directors and 14 meetings of the Audit Committee were held in 2012.

Directors with Accounting and Financial Expertise

Pursuant to the Public Reporting Directives of the Supervisor of Banks, the Company must specify the minimum number of directors with "accounting and financial expertise" which it has determined should serve on the Board of Directors and the Audit Committee. The Board of Directors of the Company has determined that the appropriate minimum number of directors with accounting and financial expertise on the Board of Directors and the Audit Committee is two. Note that at the reporting date, the number of directors with accounting and financial expertise, according to their education, qualifications, and experience, is eight. The number of directors on the Audit Committee with accounting and financial expertise, according to their education, skills, and experience, is three.

Members of the Board

Irit Izakson Chairperson of the Company from the beginning of October 2008.

Also serves as Chairperson of Isracard, Aminit, and Poalim Express; Chairperson of the Credit Committee of the Board of Directors of Isracard and of the Board of Directors of Poalim Express; and member of the Credit Committee of the Board of Directors of Aminit.

Member of the Board of Directors of Bank Hapoalim from December 27, 1999.

Chairperson of the following Board Committees at Bank Hapoalim: the Finance and Prospectus Committee, and the Committee for Risk Management and Control and Basel II Implementation. Member of the following Board Committees at Bank Hapoalim: the Credit Committee and the New Products Committee.

Member of the board of directors of the following companies: Arison Holdings (1998) Ltd., Arison Investments Ltd., Shikun & Binui Ltd.

Member of the Board of Trustees of Ben-Gurion University; member of the Executive Board of the Association of Public Companies.

In the last five years, or during part of that period, served as a director at the following companies: Israel Corp. Ltd., Israel Chemicals Ltd., Dead Sea Bromine Company Ltd., Bromine Compounds Ltd., IDB Development Ltd.; however, she no longer serves at these companies.

M.Sc. in Operational Research, School of Business Administration, Tel Aviv University; B.A. in Economics, Tel Aviv University.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Ms. I. Izakson, she is not a family member of another interested party of the corporation.

Avi Idelson

Senior human-resources consultant for mergers and acquisitions and global systems, and a director of companies.

Member of the Board of Directors of the Company from January 31, 2010.

External director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks.

Member of the Audit Committee of the Board of Directors of the Company; Chairperson of the Committee from February 28, 2011.

Member of the board of directors of the following companies: Isracard, Poalim Express, Aminit, Mehadrin Ltd., Avi Idelson Management and Consulting Ltd.

Chairperson of the Audit Committee of the Board of Directors of Isracard; member of the following committees of the Board of Directors of Isracard: IT Committee, Credit Committee, Wage and Remuneration Committee.

Chairperson of the Audit Committee and member of the Credit Committee of the Board of Directors of Aminit; member of the Audit Committee and the Credit Committee of the Board of Directors of Poalim Express; member of the Balance Sheet Committee, the Audit Committee, and the Remuneration Committee of the Board of Directors of Mehadrin Ltd.

In the last five years or during part of that period, served as head of human resources and special consultant at the BSG Investments Group; member of the governing board of the Bank of Israel and head of human resources and administration; and a consultant to companies in the area of human resources for mergers and acquisitions and global systems.

Previously served as VP of human resources at Amdocs, and served in a series of positions at Bank Hapoalim B.M.: head of the Planning, Research, and Development Department; head of the Human Resources Management Department; and various positions in the areas of training, operations, and human resources.

B.A. in Sociology and Education Administration, Tel Aviv University; M.A. studies in the Department of Labor Studies at Tel Aviv University, specialized in human resources management and organizational development.

Courses in banking and management at Bank Hapoalim.

Various courses and seminars in the areas of option plans, mergers and acquisitions, integration processes, and strategy, at E&Y, Mercer, and Harvard University.

To the best of the knowledge of the Company and of Mr. A. Idelson, he is not a family member of another interested party of the corporation.

Lilach Asher-Topilsky

Member of the Board of Management of Bank Hapoalim B.M. and Head of Retail Banking at the Bank from October 1, 2010.

Member of the Board of Directors of the Company from November 18, 2003.

Chairperson of the board of directors of the following companies: Poalim Mortgages Insurance Agency (2005) Ltd. and Poalim Ofakim Ltd.

Also serves as a member of the Board of Directors of Isracard.

From December 2007 to October 2009, member of the Board of Management of Bank Hapoalim B.M. and Head of the Strategic Management Center at the Bank.

From October 2006 to November 2007, Head of the Marketing and Strategic Planning Division at Bank Hapoalim B.M.

From March 2005 to October 2006, Head of the Central Region at Bank Hapoalim B.M.

From March 2001 to March 2005, Head of the E-Banking Division in the Retail Area at Bank Hapoalim B.M.

M.B.A., Kellogg School, Northwestern University, U.S.; B.A. in Economics and Management, Tel Aviv University.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Ms. L. Asher-Topilsky, she is not a family member of another interested party of the corporation.

Ilan Grinboim

CEO of Eurocom Cellular Communications Ltd. from 2004.

Member of the Board of Directors of the Company from May 26, 2010.

External director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks.

Also a member of the board of directors of the following companies: Dash Apax Holdings Ltd., Isracard, and Aminit; and a member of the Wage and Remuneration Committee of the Board of Directors of Isracard.

M.B.A., Tel Aviv University; B.A. in Economics, Tel Aviv University.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Mr. I. Grinboim, he is not a family member of another interested party of the corporation.

Eldad Kahana

Attorney, Head of Central Legal Counsel Division, Bank Hapoalim B.M.

Member of the Board of Directors of the Company from August 8, 1979.

Member of the Audit Committee of the Board of Directors of the Company.

Also a member of the Board of Directors of Isracard and Aminit, and of the Audit Committees of these companies, and member of the Wage and Remuneration Committee of the Board of Directors of Isracard.

L.L.B., Hebrew University of Jerusalem.

To the best of the knowledge of the Company and of Mr. E. Kahana, he is not a family member of another interested party of the corporation.

Shmuel Lachman

Member of the Board of Directors of the Company from May 21, 2009.

External director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks.

Member of the Audit Committee of the Board of Directors of the Company.

CEO of Shiral 10 Ltd.

Also a member of the board of directors of the following companies: Isracard, Aminit, Poalim Express, the Association for the Wellbeing of Israel's Soldiers Ltd., Shiral 10 Ltd., and the Computer Direct Group Ltd.

Chairman of the Finance Committee and Member of the Governing Board of Shenkar College.

Chairman of the IT Committee of the Board of Directors of Isracard; member of the following board committees at Isracard: Audit Committee, Risk Management Committee; Chairman of the Credit Committee of the Board of Directors of Aminit; member of the Audit Committee of the Board of Directors of Aminit; member of the Audit Committee of Poalim Express.

In the last five years or during part of that period, served as a member of the board of directors of the following companies: Pangaea Israel (T.R.) Ltd., Dafron Ltd., One System Integration Ltd., IDB Holdings Ltd.; however, he no longer serves at these companies.

M.Sc., Industry and Management, Technion; B.Sc., Industry and Management, Technion.

Courses abroad, mainly at the IBM training center in Brussels, on management, marketing, balance-sheet analysis, and strategic management of companies.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Mr. S. Lachman, he is not a family member of another interested party of the corporation.

David Luzon

Served as a member of the Board of Management of Bank Hapoalim B.M. from April 1, 2000 to March 31, 2011.

Served as Head of Information Technology at Bank Hapoalim B.M.

Member of the Board of Directors of the Company from July 19, 2000.

Also a member of the Board of Directors of Isracard and of the following committees of the Board of Directors of Isracard: the IT Committee and the Risk Management Committee.

In the last five years or during part of that period, served as a member of the board of directors of the following companies: Poalit, and Malam-Team Ltd.; however, he no longer serves at these companies.

B.Sc. in Mathematics and Computer Sciences, Bar Ilan University.

To the best of the knowledge of the Company and of Mr. D. Luzon, he is not a family member of another interested party of the corporation.

Ran Oz

Member of the Board of Management of Bank Hapoalim B.M. from April 16, 2009.

Head of Finance, CFO at the Bank.

Member of the Board of Directors of the Company from June 25, 2009. Chairperson of the Wage and Remuneration Committee of the Board of Directors of the Company; member of the Risk Management Committee of the Board of Directors.

Chairperson of the board of directors of the following companies: Diur B.P. Ltd., Poalim Trust Services Ltd.

Deputy chairperson of the board of directors of the following companies: Poalim Capital Markets and Investment Holdings Ltd., Poalim Capital Markets Ltd., and Poalim Capital Markets - Investment House Ltd.

Member of the board of directors of the following companies: Sure-Ha International Ltd., Isracard Ltd., Europay (Eurocard) Israel Ltd. Aminit Ltd., and Poalim Express Ltd.

From 2008 to 2009, CFO of Intouch Insurance BV.

From 2007 to 2008, Deputy CEO and CFO at Bezeq the Israel Telecommunications Corp. Ltd.

From 2004 to 2007, CFO and Corporate VP at Nice Systems Ltd.

M.A. in Economics and Business Administration, Hebrew University of Jerusalem; B.A. in Accounting and Economics, Hebrew University of Jerusalem.

C.P.A.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Mr. R. Oz, he is not a family member of another interested party of the corporation.

Ruth Arad

Member of the Board of Directors of the Company from March 1, 2011.

External director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks.

Member of the Audit Committee of the Board of Directors of the Company.

Also a member of the board of directors of the following companies: Isracard and Aminit.

Chairperson of the Risk Management Committee of the Board of Directors of Isracard, member of the Audit Committee of the Board of Directors of Isracard, and member of the Audit Committee of the Board of Directors of Aminit.

Risk management advisor at HMS from the beginning of 2011.

In the last five years or during part of that period, served as chief risk controller at the Leumi Group, as a director at the Israel-United States Commerce and Industry Bureau, and at the Fisher Institute for Air and Space Strategic Studies; however, she no longer serves in these positions.

Ph.D. and M.A. in Financing and Statistics, Princeton University; B.A. in Mathematics and Economics, Tel Aviv University.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Dr. R. Arad, she is not a family member of another interested party of the corporation.

Moshe Amit

Member of the boards of directors of various companies.

Member of the Board of Directors of the Company from May 20, 2004.

Chairperson of the board of directors of Global Factoring Ltd.

Until December 31, 2012, also served as chairperson of Delek Israel Fuel Company Ltd.; from January 1, 2013, serves as a director at Delek Israel Fuel Company Ltd.

Also a member of the board of directors of the following companies: Isracard; Delek Group Ltd.; Saint Lawrence Bank, Barbados; Poalim Capital Markets Investment Bank Ltd.; Mega Retail Ltd. (formerly Blue Square Chain Properties & Investments Ltd.); AFI Development Plc, Cyprus; Krol Ltd., Allied Real Estate Ltd., Cargal Ltd. Member of the Credit Committee of the Board of Directors of Isracard.

Until December 2003, member of the Board of Management of Bank Hapoalim.

In the last five years or during part of that period, served on the board of directors of the following companies: The Phoenix Israel Insurance Company Ltd., Matav Cable Communication Systems Ltd., Bank Hapoalim Switzerland Ltd., Signature Bank New York Ltd.; and as Chairperson of the Board of Continental Bank Ltd. and Tempo Beer Industries Ltd.; however, he no longer serves at these companies.

B.A. in Social Sciences, Bar Ilan University.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Mr. M. Amit, he is not a family member of another interested party of the corporation.

Itzhak Amram

Member of the Board of Directors of the Company from September 25, 2011.

External director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks.

Member of the Audit Committee of the Board of Directors of the Company from April 23, 2012.

Also a member of the Board of Directors of Isracard and a member of the Risk Management Committee and the Audit Committee of the Board of Directors of Isracard.

LL.B.; member of the Israel Bar Association.

To the best of the knowledge of the Company and of Mr. I. Amram, he is not a family member of another interested party of the corporation.

Nitzana Adawi

Member of the Board of Directors of the Company from May 29, 2012.

External director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks.

Member of the Audit Committee of the Board of Directors of the Company.

Lecturer on finance, member of the teaching staff at the Open University, MBA program. Economic advisor to companies, in the areas of business development, valuations, business plans, investment feasibility tests, etc.

Member of the board of directors of the following companies: Isracard (from May 29, 2012) and Poalim Express (from May 29, 2011). Member of the Audit Committee of the Board of Directors of Isracard.

M.B.A., School of Business Administration, Tel Aviv University; B.A. in Economics, Tel Aviv University.

Director with accounting and financial expertise.

To the best of the knowledge of the Company and of Ms. N. Adawi, she is not a family member of another interested party of the corporation.

Yair Ben David

Served as a director of the Company under Proper Conduct of Banking Business Directive No. 301 of the Supervisor of Banks from May 1, 2001 to April 30, 2012. Member of the Audit Committee of the Board of Directors of the Company from April 26, 2009 to April 30, 2012.

Senior Members of Management

Dov Kotler

Chief Executive Officer of the Company from February 1, 2009.

CEO of the following credit-card companies: Isracard, Poalim Express, and Aminit.

Chairperson of the board of directors of the following companies: Tzameret Mimunim, Isracard (Nechasim) 1994, and Isracard Mimun.

Member of the board of directors of the following companies: Global Factoring Ltd., Amir Marketing and Investments in Agriculture Ltd., and H.E.O.H. Management Services Ltd.; member of the governing board of the Round Up Foundation.

M.B.A., Finance Section, Tel Aviv University; B.A. in Economics, studies in International Relations, Tel Aviv University; AMP (Advanced Management Program), Harvard University.

To the best of the knowledge of the Company and of Mr. D. Kotler, he is not a family member of another interested party of the corporation.

Yigal Bareket	Member of the Management of the Company from September 1, 2010. Head of Marketing. In the last five years or during part of that period, served as head of the private marketing division and the products and services division at Bezeq, and as head of marketing in the Internet sector at 013 Barak. B.A. in Communications and Management, College of Management. To the best of the knowledge of the Company and of Mr. Y. Bareket, he is not a family member of another interested party of the corporation.
Ronen Zaretsky	Member of the Management of the Company from December 18, 2005. Head of Technology. Served in the computer units of the IDF, most recently as commander of the IDF Manpower Computing Center, and held the rank of Colonel. M.A. in Public Administration, Bar Ilan University; B.A. in Computer Science, Economics, and Criminology, Bar Ilan University. Computer technician and computer practical engineer degree, Technological Training Center. Graduate of the IDF Command and Staff College. Vice president of Project Management Institute P.M.I. Israel (R.A.) Founder and active participant in Bridge of Light – A shared activity of high-tech industry workers, IDF soldiers, and the blind. Founder and joint authorized signatory of the Elul *Gemach* (charity organization), within the non-profit association of the Shaarey Tikvah synagogue and community Torah center.

To the best of the knowledge of the Company and of Mr. R. Zaretsky, he is not a family member of another interested party of the corporation.

Amir Kushilevitz-Ilan

Member of the Management of the Company from February 2011.

In the last five years or during part of that period, served as head of the Risk Management Department of the Company, and as head of the Credit Risk Model Section in the Risk Management Area at Bank Hapoalim.

M.B.A., Ben Gurion University; B.Sc., Aeronautics and Space Engineering, Technion.

To the best of the knowledge of the Company, Mr. A. Kushilevitz-Ilan is not a family member of another interested party of the corporation.

Ami Alpan

Member of the Management of the Company from February 27, 2007.

Head of Strategic Planning.

Serves as a member of the board of directors of the following companies: I.M.T. – The Central Vehicle Distribution Company Ltd., Life Style Customer Loyalty Club Ltd., Life Style Financing Ltd., Store Alliance.Com Ltd., and Tzameret Mimunim Ltd.

M.B.A., Tel Aviv University; B.A. in Management and Economics, Tel Aviv University.

To the best of the knowledge of the Company and of Mr. A. Alpan, he is not a family member of another interested party of the corporation.

Ron Cohen

Member of the Management of the Company from February 27, 2007.

Head of Credit and Financial Services.

During his service at the Isracard Group, established the non-bank credit system. The credit system was constructed under his management, taking into consideration and adapting to periodically changing regulatory needs.

Serves as a member of the board of directors of the following companies: Tzameret Mimunim Ltd., Global Factoring Ltd., Kidum Mivne Iguach Ltd.

Previously served as Head of Customer Relations in the Corporate Banking Area at Bank Hapoalim B.M., for ten years. His clients included leading companies in the Israeli retail market.

M.A. in Business Administration, Marketing, and Finance, Hebrew University of Jerusalem;

B.A. in Economics and International Relations, Hebrew University of Jerusalem.

To the best of the knowledge of the Company and of Mr. R. Cohen, he is not a family member of another interested party of the corporation.

Oren Cohen Butensky

Member of Management of the Company from June 2011.

Head of Customer and Merchant Service.

Member of the Board of Directors of Tzameret Mimunim Ltd. from April 4, 2012.

Previously served as head of sales at the sales company of MIRS Communications, SDM, and as head of Internet support centers at 012.

M.A. in Business and Marketing, Darby University; B.A. in Economics and Social Sciences, Bar Ilan University; B.A. in Psychology (Dean's List), Open University.

To the best of the knowledge of the Company and of Mr. A. Cohen Butensky, he is not a family member of another interested party of the corporation.

Ram Gev

Member of the Management of the Company from the end of March 2011.

Head of Finance and Administration.

Serves as a member of the board of directors of the following companies: Isracard (Nechasim) 1994 and Isracard Mimun.

Served as head of finance at Harel Finance until March 2011. Previously served as deputy manager of the corporate department at the Israel Securities Authority.

M.B.A. (specialized in finance), Hebrew University of Jerusalem; B.A. in Accounting and Economics, Hebrew University of Jerusalem.

C.P.A.

To the best of the knowledge of the Company and of Mr. R. Gev, he is not a family member of another interested party of the corporation.

Maora Shalgi

Member of the Management of the Company from May 1, 2011.

Head of Human Resources.

M.A. in Human Resources, Faculty of Labor Studies, Tel Aviv University; B.A. in Social Sciences and Liberal Arts, Open University.

To the best of the knowledge of the Company and of Ms. M. Shalgi, she is not a family member of another interested party of the corporation.

Ron Weksler

Member of the Management of the Company from October 2, 2011.

Head of Commerce and Sales.

Served as a director (with accounting and financial expertise) of Isracard and Europay, and as a member of the audit committees of these companies, until the end of September 2011.

Also serves as a member of the board of directors of Global Factoring Ltd.

Served in various positions at Bank Hapoalim B.M. from 2002.

Doctor of Philosophy and Ph.D. in Public Administration, Bar Ilan University; M.B.A., Bar Ilan University; LL.B., Tel Aviv University; B.A. in Accounting, Tel Aviv University.

To the best of the knowledge of the Company and of Mr. R. Weksler, he is not a family member of another interested party of the corporation.

Controls and Procedures Regarding Disclosure and the Company's Internal Controls over Financial Reporting

In accordance with the Public Reporting Directives of the Supervisor of Banks, the Chief Executive Officer and the Chief Accountant of the Company must each separately sign a declaration regarding their responsibility for the establishment and application of controls and procedures concerning disclosure and the Company's internal controls over financial reporting, pursuant to the provisions of Sections 302 and 404 of the law known as the “Sarbanes-Oxley Act,” enacted in the United States. The provisions of these two sections of the law were consolidated by the

Supervisor of Banks in Proper Conduct of Banking Business Directive 309 in September 2008, and the Public Reporting Directives were adjusted accordingly in June 2009.

The two directives of the aforesaid law have been implemented at the Company since their inception dates:

- The directive in Section 302 regarding the responsibility for the establishment and application of controls and procedures concerning disclosure has been implemented quarterly beginning with the financial statements as at June 30, 2007.

- The directive in Section 404 regarding the responsibility for the Company's internal controls over financial reporting has been implemented at year end, beginning with the financial statements as at December 31, 2008.

The Company routinely updates and documents existing processes; maps and documents material new processes; and examines the effectiveness of the procedures for internal controls over financial reporting through renewed examinations of the main controls.

Evaluation of Controls and Procedures Regarding Disclosure

The Management of the Company, in cooperation with the Chief Executive Officer and the Chief Accountant of the Company, has assessed the effectiveness of the controls and procedures regarding disclosure at the Company from the end of the period covered by this report. Based on this assessment, the Chief Executive Officer and the Chief Accountant of the Company have concluded that, from the end of this period, the controls and procedures regarding disclosure at the Company are effective in order to record, process, summarize, and report the information which the Company is required to disclose in its annual report, in accordance with the Public Reporting Directives of the Supervisor of Banks, on the date stipulated in these directives.

Internal Controls over Financial Reporting

During the fourth quarter ended on December 31, 2012, there was no change in the Company's internal controls over financial reporting that had a material impact, or could reasonably be expected to have a material impact, on the Company's internal controls over financial reporting.

Irit Izakson	**Dov Kotler**
Chairperson of the Board of Directors	Chief Executive Officer

Tel Aviv, February 27, 2013

Europay (Eurocard) Israel Ltd.

Management's Review

For the Year Ended December 31, 2012

ISRACARD GROUP

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Balance Sheet – Multi-Period Data

Addendum 1

Reported amounts

In NIS millions

	December 31				
	2012	**2011**	**2010**	**2009**	**2008**
Assets					
Other assets	7	185	183	183	182
Total assets	**7**	**185**	**183**	**183**	**182**
Liabilities					
Other liabilities	*-	*-	-	-	-
Total liabilities	*-	*-	-	-	-
Equity	7	185	183	183	182
Total liabilities and capital	**7**	**185**	**183**	**183**	**182**

* Amount lower than NIS 0.5 million.

Statement of Profit and Loss – Multi-Period Data

Addendum 2

Reported amounts

In NIS millions

	For the year ended December 31				
	2012	**2011**	**2010**	**2009**	**2008**
Net operating (expenses) income, under the agreement with Isracard Ltd.	(6)	(4)	(4)	(2)	(2)
Net interest income	2	6	4	4	8
Profit (loss) before taxes	(4)	2	(*-)	2	6
Provision for taxes on profit	*-	*-	*-	1	2
Net profit (loss)	**(4)**	**2**	**(*-)**	**1**	**4**
Basic and diluted net profit (loss) per common share (in NIS)					
Net profit (loss)	(9)	4	(**-)	2	9

* Amount lower than NIS 0.5 million.

** Amount lower than NIS 0.5.

Balance Sheet as at the End of Each Quarter – Multi-Quarter Data

Addendum 3

Reported amounts

In NIS millions

	2012			
	Q4	**Q3**	**Q2**	**Q1**
Assets				
Other assets	7	9	10	185
Total assets	**7**	**9**	**10**	**185**
Liabilities and capital				
Other liabilities	*-	*-	*-	*-
Equity	7	9	10	185
Total liabilities and capital	**7**	**9**	**10**	**185**

	2011			
	Q4	**Q3**	**Q2**	**Q1**
Assets				
Other assets	185	185	184	183
Total assets	**185**	**185**	**184**	**183**
Liabilities and capital				
Other liabilities	*-	*-	*-	*-
Equity	185	185	184	183
Total liabilities and capital	**185**	**185**	**184**	**183**

* Amount lower than NIS 0.5 million.

Statement of Profit and Loss as at the End of Each Quarter – Multi-Quarter Data

Addendum 4

Reported amounts

In NIS millions

	2012			
	Q4	**Q3**	**Q2**	**Q1**
Net operating expenses under the agreement with Isracard Ltd.	(2)	(1)	(2)	(1)
Net interest income	*-	*-	1	1
Profit (loss) before taxes	(2)	(1)	(1)	(*-)
Provision for taxes on operating profit	*-	*-	*-	*-
Loss	(2)	(1)	(1)	(*-)
Basic and diluted loss per common share (in NIS)	**(5)**	**(2)**	**(2)**	**(**-)**

	2011			
	Q4	**Q3**	**Q2**	**Q1**
Net operating expenses under the agreement with Isracard Ltd.	(1)	(1)	(1)	(1)
Net interest income	1	2	2	1
Profit before taxes	*-	1	1	*-
Provision for taxes on profit	*-	*-	*-	(*-)
Net profit	*-	1	1	*-
Basic and diluted net profit per common share (in NIS)	****-**	**2**	**2**	****-**

* Amount lower than NIS 0.5 million.

** Amount lower than NIS 0.5.

Certification

I, Dov Kotler, hereby declare that:

1. I have reviewed the annual report of Europay (Eurocard) Israel Ltd. (hereinafter: the "**Company**") for 2012 (hereinafter: the "**Report**").

2. Based on my knowledge, the Report contains no incorrect presentation of a material fact, and there is no presentation of a material fact missing from the Report that is necessary so that the presentations included therein, in light of the circumstances under which such presentations were included, are not misleading with regard to the period covered by the Report.

3. Based on my knowledge, the financial statements and other financial information included in the Report fairly reflect the financial position, results of operations, changes in equity, and cash flows of the Company, in all material aspects, for the dates and periods covered in the Report.

4. I, and others at the Company making this declaration, are responsible for the establishment and application of controls and procedures regarding the Company's disclosure[1] and internal control over financial reporting[1]; furthermore:

   A. We have established such controls and procedures, or caused such controls and procedures to be established under our supervision, aimed at ensuring that material information pertaining to the Company is brought to our knowledge by others at the Company, in particular during the preparation of the Report;

   B. We have established such internal control over financial reporting, or caused such internal control over financial reporting to be established under our supervision, intended to provide a reasonable degree of confidence with regard to the reliability of the financial reporting, and that the financial reports for external purposes are prepared in accordance with generally accepted accounting principles and with the directives and guidelines of the Supervisor of Banks;

   C. We have assessed the effectiveness of the controls and procedures concerning disclosure at the Company, and we have presented our conclusions with regard to the effectiveness of the controls and procedures concerning disclosure, as at the end of the period covered in the Report, based on our assessment; and

   D. We have disclosed in the Report any change in the internal control over financial reporting at the Company that occurred during the fourth quarter, and that had a material effect, or could reasonably be expected to have a material effect, on the internal control over financial reporting at the Company.

5. I, and others at the Company making this declaration, have disclosed to the auditors, to the Board of Directors, and to the Audit Committee of the Board of Directors of the Company, based on our most current assessment of the internal control over financial reporting:

A. Any significant deficiencies and material weaknesses in the establishment or application of internal control over financial reporting that can reasonably be expected to impair the Company's ability to record, process, summarize, or report financial information; and

B. Any fraud, whether material or immaterial, in which Management was involved, or in which other employees were involved who have a significant role in the internal control over financial reporting at the Company.

The aforesaid shall not detract from my responsibility, or from the responsibility of any other person, under any law.

[1] As defined in the Public Reporting Directives, "Board of Directors' Report."

Dov Kotler

Tel Aviv, February 27, 2013

Chief Executive Officer

Certification

I, Sigal Barmack, hereby declare that:

1. I have reviewed the annual report of Europay (Eurocard) Israel Ltd. (hereinafter: the "**Company**") for 2012 (hereinafter: the "**Report**").

2. Based on my knowledge, the Report contains no incorrect presentation of a material fact, and there is no presentation of a material fact missing from the Report that is necessary so that the presentations included therein, in light of the circumstances under which such presentations were included, are not misleading with regard to the period covered by the Report.

3. Based on my knowledge, the financial statements and other financial information included in the Report fairly reflect the financial position, results of operations, changes in equity, and cash flows of the Company, in all material aspects, for the dates and periods covered in the Report.

4. I, and others at the Company making this declaration, are responsible for the establishment and application of controls and procedures regarding the Company's disclosure[1] and internal control over financial reporting[1]; furthermore:

   A. We have established such controls and procedures, or caused such controls and procedures to be established under our supervision, aimed at ensuring that material information pertaining to the Company is brought to our knowledge by others at the Company, in particular during the preparation of the Report;

   B. We have established such internal control over financial reporting, or caused such internal control over financial reporting to be established under our supervision, intended to provide a reasonable degree of confidence with regard to the reliability of the financial reporting, and that the financial reports for external purposes are prepared in accordance with generally accepted accounting principles and with the directives and guidelines of the Supervisor of Banks;

   C. We have assessed the effectiveness of the controls and procedures concerning disclosure at the Company, and we have presented our conclusions with regard to the effectiveness of the controls and procedures concerning disclosure, as at the end of the period covered in the Report, based on our assessment; and

   D. We have disclosed in the Report any change in the internal control over financial reporting at the Company that occurred during the fourth quarter, and that had a material effect, or could reasonably be expected to have a material effect, on the internal control over financial reporting at the Company.

5. I, and others at the Company making this declaration, have disclosed to the auditors, to the Board of Directors, and to the Audit Committee of the Board of Directors of the Company, based on our most current assessment of the internal control over financial reporting:

A. Any significant deficiencies and material weaknesses in the establishment or application of internal control over financial reporting that can reasonably be expected to impair the Company's ability to record, process, summarize, or report financial information; and

B. Any fraud, whether material or immaterial, in which Management was involved, or in which other employees were involved who have a significant role in the internal control over financial reporting at the Company.

The aforesaid shall not detract from my responsibility, or from the responsibility of any other person, under any law.

[1] As defined in the Public Reporting Directives, "Board of Directors' Report."

Sigal Barmack

Tel Aviv, February 27, 2013

Manager of Finance and Accounting Department,
Chief Accountant

Report of the Board of Directors and Management on Internal Controls over Financial Reporting

The Board of Directors and the Management of Europay (Eurocard) Ltd. (hereinafter: the "**Company**") are responsible for the establishment and application of adequate internal controls over financial reporting (as defined in the Public Reporting Directives concerning the "Board of Directors' Report"). The system of internal controls at the Company was designed to provide a reasonable degree of confidence to the Board of Directors and Management of the Company with regard to the adequate preparation and presentation of the financial statements, which are published in accordance with generally accepted accounting principles and the directives and guidelines of the Supervisor of Banks. Regardless of the quality of planning of the internal control systems, any such system has inherent limitations. Thus, even if it is determined that these systems are effective, such systems can provide only a reasonable degree of confidence with regard to the preparation and presentation of the financial statements.

Management, under the supervision of the Board of Directors, maintains a comprehensive system of controls aimed at ensuring that transactions are executed in accordance with Management's authorizations, that assets are protected, and that accounting records are reliable. In addition, Management, under the supervision of the Board of Directors, applies measures to ensure that information and communication channels are effective and monitor performance, including the performance of internal control procedures.

The Management of the Company, under the supervision of the Board of Directors, assessed the effectiveness of the Company's internal controls over financial reporting as at December 31, 2012, based on the criteria established in the internal control model of the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, Management believes that as at December 31, 2012, the Company's internal controls over financial reporting are effective.

The effectiveness of the Company's internal controls over financial reporting as at December 31, 2012 was audited by the Company's external auditors, Somekh Chaikin Certified Public Accountants (Isr.) and Ziv Haft Certified Public Accountants (Isr.), as noted in their report on page 87. The auditors' report includes an unqualified opinion with regard to the effectiveness of the Company's internal controls over financial reporting as at December 31, 2012.

Irit Izakson	**Dov Kotler**	**Sigal Barmack**
Chairperson of the Board of Directors	Chief Executive Officer	Manager of Finance and Accounting Department, Chief Accountant

Tel Aviv, February 27, 2013

Europay (Eurocard) Israel Ltd.

Financial Statements

For the year ended December 31, 2012

ISRACARD GROUP

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Somekh Chaikin

Auditors' Report to the Shareholders of Europay (Eurocard) Ltd.

Pursuant to the Public Reporting Directives of the Supervisor of Banks on Internal Controls over Financial Reporting

We have audited the internal control over financial reporting of Europay (Eurocard) Ltd. (hereinafter: "the Company") as at December 31, 2012, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (hereinafter: "COSO"). The Company's Board of Directors and Management are responsible for maintaining effective internal control over financial reporting and for their assessment of the effectiveness of internal control over financial reporting, included in the accompanying Directors' and Management's reports on internal control over financial reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

The internal control over financial reporting of a credit-card company is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with accounting principles generally accepted in Israel (Israeli GAAP) and in accordance with directives and guidelines of the Supervisor of Banks. The internal control over financial reporting of a credit-card company includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and transfers of the assets of the company (including the removal of assets from its possession); (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with Israeli GAAP and in accordance with directives and guidelines of the Supervisor of Banks, and that receipts and expenditures of the company are made only in accordance with authorizations of the board of directors and management of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets (including removal of assets from its possession) that could have a material effect on the financial statements.

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

In our opinion, the Company maintained, in all material aspects, effective control over financial reporting as at December 31, 2012, based on criteria established in Internal Control – Integrated Framework issued by COSO.

We have also audited, in accordance with accepted auditing standards in Israel, and certain auditing standards applied in the audit of credit-card companies as determined by directives and guidelines of the Supervisor of Banks, the financial statements of the Company as at December 31, 2012 and 2011, and for each of the years in the three-year period ended on December 31, 2012. Our report dated February 27, 2013, expressed an unqualified opinion on the said financial statements, while drawing attention to Note 4A concerning antitrust issues.

Somekh Chaikin
Certified Public Accountants (ISR)

Ziv Haft
Certified Public Accountants (ISR)

Tel Aviv, February 27, 2013

Somekh Chaikin

Auditors' Report to the Shareholders of Europay (Eurocard) Ltd. – Annual Financial Statements

We have audited the accompanying balance sheets of Europay (Eurocard) Ltd. (hereinafter: "the Company") as at December 31, 2012 and 2011 and the balance sheets as at those dates, and the statements of profit and loss, reports on changes in equity, and statements of cash flows of the Company for each of the three years in the period ended on December 31, 2012. These financial statements are the responsibility of the Company's board of directors and management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Generally Accepted Auditing Standards in Israel, including standards prescribed by the Auditors Regulations (Manner of Auditor's Performance), 1973, and certain auditing standards applied in the audit of credit-card companies as determined by directives and guidelines of the Supervisor of Banks. These standards require that we plan and perform the audit with the aim of obtaining reasonable assurance that the financial statements are free of material misstatement. An audit includes examining, on a sample basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes an assessment of the accounting principles implemented and significant estimates used by the board of directors and by the management of the Company, as well as an evaluation of the fairness of the overall presentation in the financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as at December 31, 2012 and 2011, and the results of operations, changes in equity, and cash flows of the Company for each of the three years in the period ended on December 31, 2012, in conformity with generally accepted accounting principles in Israel (Israeli GAAP). Furthermore, in our opinion, these financial statements have been prepared in accordance with the directives and guidelines of the Supervisor of Banks.

Without qualifying our aforesaid opinion, we draw attention to Note 4A concerning antitrust issues.

We have also audited, in accordance with standards of the Public Company Accounting Oversight Board (United States) (PCAOB) concerning audits of internal control over financial reporting, as adopted by the Institute of Certified Public Accountants in Israel, the internal controls of the Company over financial reporting as at December 31, 2012, based on criteria established in the Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 27, 2013, expressed an unqualified opinion of the effectiveness of the Company’s internal control over financial reporting.

Somekh Chaikin
Certified Public Accountants (ISR)

Ziv Haft
Certified Public Accountants (ISR)

Tel Aviv, February 27, 2013

Balance Sheets

Reported amounts

In NIS millions

		December 31	
	Note	2012	2011
Assets			
Other assets	2	7	185
Total assets		**7**	**185**
Liabilities and capital			
Surplus of current income-tax provisions over advances paid		*-	*-
Contingent liabilities and special agreements	4		
Equity	3	7	185
Total liabilities and capital		**7**	**185**

* Amount lower than NIS 0.5 million.

Irit Izakson	**Dov Kotler**	**Sigal Barmack**
Chairperson of the Board of Directors	Chief Executive Officer	Manager of Finance and Accounting Department, Chief Accountant

Tel Aviv, February 27, 2013

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

Statements of Profit and Loss

Reported amounts

In NIS millions

	Note	For the year ended December 31		
		2012	2011	2010
Net operating expenses under the agreement with Isracard Ltd.	5	(6)	(4)	(4)
Net interest income		2	6	4
Profit (loss) before taxes		(4)	2	(*-)
Provision for taxes on profit	7	*-	*-	*-(1)
Net profit (loss)		(4)	2	(*-)
Basic and diluted net profit (loss) per common share (in NIS)		(9)	4	(**-)
Number of common shares used in calculation		427,699	427,699	427,699

* Amount lower than NIS 0.5 million.

** Amount lower than NIS 0.5.

(1) See Note 4.B.2 below.

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

Statements of Changes in Equity

Reported amounts

In NIS millions

	Paid-up share capital	Premium on shares	Total paid-up capital and premium	Retained earnings	Total equity
Balance as at December 31, 2009	**1**	***-**	**1**	**182**	**183**
Annual loss	-	-	-	(*-)	(*-)
Balance as at December 31, 2010	**1**	***-**	**1**	**182**	**183**
Annual net profit	-	-	-	2	2
Balance as at December 31, 2011	**1**	***-**	**1**	**184**	**185**
Annual loss	-	-	-	(4)	(4)
Dividend	-	-	-	(174)	(174)
Balance as at December 31, 2012	**1**	***-**	**1**	**6**	**7**

Statements of Cash Flows

Reported amounts

In NIS millions

	For the year ended December 31		
	2012	**2011**	**2010**
Cash flows from operating activity			
Annual net profit (loss)	(4)	2	(*-)
Adjustments:			
(Increase) decrease in other assets	178	(2)	*-
Increase (decrease) in creditors and credit balances	*-	*-	-
Net cash used in operating activity	**174**	**-**	**-**
Cash flows from financing activity			
Net cash from financing activity	**(174)**	**-**	**-**
Change in cash	-	-	-
Balance of cash at beginning of year	-	-	-
Balance of cash at end of year	-	-	-

* Amount lower than NIS 0.5 million.

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

Note 1 – Significant Accounting Policies

A. General

1. Europay (Eurocard) Israel Ltd. (hereinafter: the "**Company**") is a corporation incorporated in Israel in 1972 as a private company by Bank Hapoalim B.M. (hereinafter: "**Bank Hapoalim**"), which was the controlling shareholder of the Company until July 2009. In July 2009, Isracard, a company controlled by Bank Hapoalim, purchased the full holdings of Bank Hapoalim and of a subsidiary under its ownership in the Company. The holder of the permit for control of Bank Hapoalim is Ms. Shari Arison. The Company is an auxiliary corporation under the Banking Law (Licensing), 1981.

   The Company is primarily engaged in issuing MasterCard credit cards for use abroad, and in clearing transactions executed using MasterCard credit cards by tourists in Israel with merchants credited in US dollars.

   In May 2012, the Company distributed a dividend to its shareholders in a total amount of NIS 174 million. Following the distribution of the dividend, Isracard acquired 7,699 common shares from Mizrahi Bank, constituting 1.8% of the issued and paid-up common share capital of the Company. Following the completion of this transaction, Isracard holds 100% of the shares of the Company.

   The financial statements were prepared in accordance with generally accepted accounting principles in Israel (Israeli GAAP) and with the directives and guidelines of the Supervisor of Banks.

2. The annual financial statements were approved for publication by the Board of Directors of the Company on February 27, 2013.

B. Definitions

In these financial statements:

- **International Financial Reporting Standards (hereinafter: "IFRS")** – Standards and interpretations adopted by the International Accounting Standards Board (IASB), including IFRS and International Accounting Standards (IAS), and interpretations of these standards by the International Financial Reporting Interpretations Committee (IFRIC) or the Standing Interpretations Committee (SIC), respectively.

- **Generally accepted accounting principles (GAAP) for US banks** – Accounting principles which American banks traded in the United States are required to implement. These rules are established by the banking supervision agencies in the United States, the Securities and Exchange Commission in the United States, the Financial Accounting Standards Board in the United States, and other entities in the United States, and implemented according to the hierarchy established in FAS 168 (ASC 105-10), The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles,

Note 1 – Significant Accounting Policies (cont.)

B. Definitions (cont.)

which replaced FAS 162. In addition, as established by the Supervisor of Banks, despite the hierarchy established in FAS 168, it has been clarified that any position stated to the public by the bank supervision agencies in the United States or by the staff of the banking supervision agencies in the United States with regard to the manner of implementation of US GAAP constitutes GAAP for US banks.

1. The Company – Europay (Eurocard) Israel Ltd.
2. The Parent Company – Isracard Ltd.
3. Related parties – As defined in International Accounting Standard 24, excluding interested parties.
4. Interested parties – As defined in Paragraph 1 of the definition of an “interested party” of a "corporation" in Section 1 of the Securities Law, 1968.
5. Controlling shareholders – As defined in the Securities Regulations (Presentation of Transactions between a Corporation and its Controlling Shareholder in Financial Statements), 1996.
6. CPI – The consumer price index in Israel, as published by the Central Bureau of Statistics.
7. USD – United States dollar.
8. Adjusted amount – Nominal historical amount adjusted to the CPI for December 2003, in accordance with the directives of Opinion Statements No. 23 and 36 of the Institute of Certified Public Accountants in Israel.
9. Adjusted financial reporting – Financial reporting in values adjusted to changes in the general purchasing power of Israeli currency, in accordance with the directives of the Opinion Statements of the Institute of Certified Public Accountants in Israel.
10. Reported amount – Amount adjusted to the transition date (December 31, 2003), plus amounts in nominal values added after the transition date, less amounts subtracted after the transition date.
11. Cost – Cost in reported amounts.
12. Nominal financial reporting – Financial reporting based on reported amounts.
13. Functional currency – The currency of the main economic environment in which the company operates. Usually the currency of the environment in which the company generates and expends most of its cash.
14. Presentation currency – The currency in which the financial statements are presented.

Note 1 – Significant Accounting Policies (cont.)

C. Basis for Preparation of the Financial Statements

1. Reporting Principles

The financial statements of the Company are prepared in accordance with the Public Reporting Directives of the Supervisor of Banks. In preparing the financial statements, the Company implements, among other matters, certain IFRS and GAAP for US banks, in the following manner:

- **On matters related to the core business of banking** – Accounting treatment in accordance with the directives and guidelines of the Supervisor of Banks, and in accordance with GAAP for US banks that have been adopted as part of the Public Reporting Directives of the Supervisor of Banks.

- **On matters not related to the core business of banking** – Accounting treatment in accordance with Israeli GAAP and IFRS. International standards are implemented according to the following principles:

  - In cases in which a material issue arises that is not resolved in the IFRS or in the implementation instructions of the Supervisor, the Company treats the issue according to GAAP for US banks specifically applicable to these matters;

  - In cases in which there is no specific reference to material matters in the standards or interpretations, or there are several alternatives for the treatment of a material matter, the Company acts according to specific implementation guidelines established by the Supervisor;

  - Where an IFRS that has been adopted contains a reference to another IFRS adopted in the Public Reporting Directives, the Company acts in accordance with the IFRS;

  - Where an IFRS that has been adopted contains a reference to another IFRS that has not been adopted in the Public Reporting Directives, the Company acts in accordance with the Reporting Directives and with Israeli GAAP;

  - Where an IFRS that has been adopted contains a reference to a definition of a term defined in the Public Reporting Directives, a reference to the definition in the Directives shall replace the original reference.

2. Functional Currency and Presentation Currency

The financial statements are presented in New Israeli Shekels (NIS), the functional currency of the Company, rounded to the nearest million, except where otherwise noted.

3. Measurement Base

The financial statements were prepared based on historical costs. The value of non-monetary assets and items of capital measured on the basis of historical cost was adjusted to changes

Note 1 – Significant Accounting Policies (cont.)

C. Basis for Preparation of the Financial Statements (cont.)

in the CPI up to December 31, 2003, because the Israeli economy was considered a hyper-inflationary economy until that date. Beginning on January 1, 2004, the Company has prepared its financial statements in reported amounts.

4. Use of Estimates

The preparation of the financial statements in conformity with Israeli GAAP and the directives and guidelines of the Supervisor of Banks requires the Management of the Company to exercise judgment in the use of estimates, evaluations, and assumptions that affect the application of policies and the amounts of assets, liabilities, income, and expenses. It is hereby clarified that actual results may differ from such estimates.

In formulating the accounting estimates used in the preparation of the financial statements of the Company, the Management of the Company is required to make assumptions with regard to circumstances and events that involve significant uncertainty. The Management of the Company bases its judgment in establishing these estimates on past experience, various facts, external factors, and reasonable assumptions, according to the circumstances, as appropriate for each estimate.

The estimates and the underlying assumptions are reviewed routinely. Changes in accounting estimates are recognized in the period in which the estimates are amended and in every affected future period.

D. Reclassification

Due to the first-time implementation of certain accounting standards and directives of the Supervisor of Banks (see Sections E and F below), certain item headings in the financial statements and certain comparative figures were adjusted to the reporting requirements for the current period.

Items included in the statement of profit and loss:

Due to the initial implementation of the directives of the Supervisor of Banks regarding the new format for the statement of profit and loss (see Section E below), the reclassifications described below were performed in the financial statements for the years ended December 31, 2011 and 2010.

- The items profit from financing activity before provisions for credit losses and operating profit before taxes were changed to net interest income and profit before taxes, respectively.

Note 1 – Significant Accounting Policies (cont.)

E. First-Time Implementation of Accounting Standards, Updates of Accounting Standards, and Directives of the Supervisor of Banks

The Company has implemented the accounting standards and directives described below, beginning on January 1, 2012:

1. Directives concerning the format for the statement of profit and loss, established in the circular of the Supervisor of Banks on the format for statements of profit and loss of banking corporations and the adoption of GAAP for US banks concerning the measurement of interest income.

2. Certain IFRS and IFRIC interpretations referring to the implementation of these standards, as follows:

   - IAS 7, Statement of Cash Flows;
   - IAS 12, Income Taxes;
   - IAS 23, Borrowing Costs;
   - IAS 24, Related Party Disclosures.

3. Directives of the Supervisor of Banks on accounting for transactions between a banking corporation and its controlling party or a company controlled by the banking corporation.

The accounting policies of the Company, as detailed in Section F below, include the new accounting policies resulting from the implementation of the accounting standards, accounting standard updates, and directives of the Supervisor of Banks, and present the manner and effect, if any, of the initial implementation thereof.

F. Accounting Policies Implemented in the Preparation of the Financial Statements

1. Foreign Currency and Linkage

Transactions in Foreign Currency

Transactions in foreign currency are translated into the functional currency of the Company according to the exchange rate in effect at the dates of the transactions. Monetary assets and liabilities denominated in foreign currency at the reporting date are translated into the functional currency according to the exchange rate in effect at that date. Exchange-rate differences in respect of monetary items are the difference between the depreciated cost in the functional currency at the beginning of the year, adjusted for payments during the year, and the depreciated cost in foreign currency translated according to the exchange rate at the end of the year.

Note 1 – Significant Accounting Policies (cont.)

F. Accounting Policies Implemented in the Preparation of the Financial Statements (cont.)

CPI-Linked Assets and Liabilities Not Measured at Fair Value

Assets and liabilities linked to the consumer price index are included according to the linkage terms established for each balance.

Set out below are details regarding representative exchange rates and the CPI (2010 base = 100), and the rates of change therein:

	December 31		
	2012	**2011**	**2010**
Consumer price index (in points)	105.7	104.0	101.8
United States dollar exchange rate (in NIS per 1 USD)	3.733	3.821	3.549

	Percent change in the year ended December 31		
	2012	**2011**	**2010**
Consumer price index	1.6	2.2	2.7
USD exchange rate	(2.3)	7.7	(6.0)

2. Basis for Recognition of Revenue and Expenses

(1) Interest income and expenses are recognized on an accrual basis.

(2) Other income and expenses are recognized on an accrual basis.

3. Contingent Liabilities

The financial statements include sufficient provisions for legal claims, according to the assessment of Management and based on the opinions of its legal advisors. The disclosure is in the format set forth in the directives of the Supervisor of Banks, such that the claims filed against the Company are classified into three groups:

(1) Probable risk – the probability of realization of the exposure to risk is over 70%. Provisions are included in the financial statements in respect of claims in this risk group.

(2) Reasonably possible risk – the probability of realization of the exposure to risk is between 20% and 70%. No provision is included in the financial statements in respect of claims in this risk group, but disclosure is given.

Note 1 – Significant Accounting Policies (cont.)

F. Accounting Policies Implemented in the Preparation of the Financial Statements (cont.)

(3) Remote risk – the probability of realization of the exposure to risk is under 20%. No provision is included in the financial statements in respect of claims in this risk group and no disclosure is given.

Legal claims regarding which the Supervisor of Banks has determined that the Company is required to pay reimbursement are classified as probable, and a provision is made in respect of the claim commensurate with the amount that the Company is required to reimburse.

4. Expenses for Taxes on Income

Taxes on income include current and deferred taxes. Current and deferred taxes are allocated to the statement of profit and loss, unless the taxes arise from a transaction or event recognized directly in equity.

Current Taxes

Current tax is the amount of tax expected to be paid (or received) on the taxable income for the year, calculated according to the applicable tax rates under laws legislated or legislated in practice at the reporting date, including changes in tax payments referring to previous years.

Deferred Taxes

Deferred taxes are recognized with reference to temporary differences between the book value of assets and liabilities for the purposes of financial reporting and their value for tax purposes. The measurement of deferred taxes reflects the tax effects that will derive from the manner in which the Group expects, at the end of the reporting period, to recover or settle the book value of the assets and liabilities. The deferred taxes are measured according to the tax rates expected to apply to the temporary differences at the date when they are realized, based on laws legislated or legislated in practice at the balance-sheet date.

5. Earnings Per Share

The Company presents data on basic and diluted earnings per share with respect to its common share capital. Basic earnings per share are calculated by dividing the profit or loss attributed to holders of the common shares of the Company by the weighted average number of common shares in circulation during the year.

Note 1 – Significant Accounting Policies (cont.)

F. Accounting Policies Implemented in the Preparation of the Financial Statements (cont.)

6. Statement of Cash Flows

The statement of cash flows is presented with classification into cash flows from regular activity, investing activity (formerly "activity in assets"), and financing activity (formerly "activity in liabilities and capital"). Cash flows arising from main activities of the Company are classified under regular activity.

Effect of the Initial Implementation of the New Directives of the Supervisor of Banks Concerning the Statement of Cash Flows

The Company has implemented the new directives of the Supervisor of Banks concerning the statement of cash flows beginning on January 1, 2012, retroactively. The initial implementation of this standard had no effect, other than the change in presentation of item headings.

7. Fair value of financial instruments

The balance-sheet balance of financial instruments serves as an approximation of their fair value.

8. Segmental Reporting

A segment is a component of the Company engaged in activities from which it is likely to derive income and bear expenses, the results of operations of which are regularly examined by Management and the Board of Directors in order to make decisions regarding resource allocation and performance evaluation, and with regard to which separate financial information exists. The format for reporting on the segments of activity of the Company is established in the Public Reporting Directives of the Supervisor of Banks.

9. Related Party Disclosures

IAS 24, Related Party Disclosures, establishes the disclosure required of entities with regard to their relationships with related parties and with regard to unsettled transactions and balances with related parties.

In addition, disclosure is required for compensation to key management personnel. Key executives are defined as persons with the authority and responsibility to plan the activity of the entity, or to directly or indirectly guide and control the entity, including any director (active or inactive) of the entity.

As part of the adoption of the standard by the Supervisor of Banks, the format of the required disclosure in the financial statements was reclassified, in order to comply with the disclosure

Note 1 – Significant Accounting Policies (cont.)

F. Accounting Policies Implemented in the Preparation of the Financial Statements (cont.)

requirements of IAS 24 as well as the additional disclosures required under the Securities Regulations (Annual Financial Statements), 2010.

Effect of the Initial Implementation of the New Directives of the Supervisor of Banks Concerning Related Party Disclosures

The Company has implemented the new directives of the Supervisor of Banks concerning IAS 24, Related Party Disclosures, beginning on January 1, 2012, retroactively. For the purpose of the initial implementation of the standard, the Company mapped its relationships with related parties. Related parties were identified, in accordance with the new definition, as a result of the mapping process. For further information regarding transactions and balances with related parties, see Note 16 below.

The initial implementation of the standard had no effect on the financial statements, other than a change in presentation.

10. Transactions with Controlling Parties

The Company implements US GAAP for the accounting treatment of transactions between a banking corporation and its controlling party or a company controlled by the banking corporation. In situations where these rules do not address the accounting treatment, the Company applies the rules established in Standard 23 of the Israel Accounting Standards Board, Accounting Treatment of Transactions between an Entity and its Controlling Party.

Assets and liabilities regarding which a transaction has been executed with a controlling party are measured at fair value at the date of the transaction. Because a transaction on the equity level is involved, the Group allocates the difference between the fair value and the consideration from the transaction to equity.

Undertaking of Liabilities or Waivers

The Company removes the liability from the financial statements, according to its fair value at the extinguishment date. The difference between the book value of the liability and its fair value at the extinguishment date is allocated as profit or loss. In the case of undertaking of a liability, the difference between the fair value of the liability at the extinguishment date and the amount of the consideration established is allocated to equity. In the case of a waiver, the fair value of the forgiven liability is allocated to equity.

Note 1 – Significant Accounting Policies (cont.)

F. Accounting Policies Implemented in the Preparation of the Financial Statements (cont.)

Indemnification

The amount of the indemnification is allocated to equity.

Effect of the Initial Implementation of the New Directives of the Supervisor of Banks Concerning the Accounting Treatment of Transactions between an Entity and its Controlling Party

Beginning January 1, 2012, the Company has implemented the instructions established in the directives, prospectively, for all transactions between the Company and a controlling party executed after January 1, 2012. The initial implementation of these directives had no material effect on the financial statements.

G. New Accounting Standards and New Directives of the Supervisor of Banks in the Period Prior to Implementation

1. In July 2006, the Israel Accounting Standards Board published Accounting Standard No. 29, Adoption of International Financial Reporting Standards (IFRS). The standard stipulates that entities subject to the Securities Law, 1968 and required to report under its regulations shall prepare their financial statements according to IFRS for periods starting January 1, 2008 or later. The aforesaid does not apply to banking corporations and credit-card companies whose financial statements are prepared according to the directives and guidelines of the Supervisor of Banks. In June 2009, the Supervisor of Banks issued a letter concerning reporting by banking corporations and credit-card companies in Israel in accordance with IFRS, which establishes the expected manner of adoption of IFRS by banking corporations and credit-card companies.

Pursuant to the circular, the deadlines for reporting according to IFRS by banking corporations and credit-card companies are as follows:

- On matters related to the core business of banking – The Supervisor of Banks intends to reach a final decision, taking into consideration the schedule established in the United States and the progress of the convergence process between international and American standards.

- On matters not related to the core business of banking – Adopted gradually during 2011 and 2012. However, IAS 19, Employee Benefits, has not yet taken effect and will be adopted according to the instructions of the Supervisor of Banks, when such instructions are published, with regard to the timing and manner of initial implementation.

Note 1 – Significant Accounting Policies (cont.)

G. New Accounting Standards and New Directives of the Supervisor of Banks in the Period Prior to Implementation (cont.)

2. Directive Concerning the Format of the Statement of Profit and Loss of a Banking Corporation and the Adoption of GAAP for US Banks on Interest Income Measurement

A circular of the Supervisor of Banks was issued on December 29, 2011, with the aim of adjusting the Public Reporting Directives for the purpose of adoption of the rules established in US GAAP regarding nonrefundable fees and other costs. The directive establishes rules for the treatment of loan origination fees and direct loan origination costs. The eligible fees and costs, according to the criteria established in the directive, shall not be recognized immediately in the statement of profit and loss, but shall be taken into account in calculating the effective interest rate of the loan. In addition, the directive changes the treatment of credit commitment fees and costs, including credit-card transactions.

A circular entitled Date of Adoption of Section 310-20 of the Codification Concerning Nonrefundable Fees and Other Costs was issued on July 25, 2012. According to the circular, directives related to the adoption of US GAAP on the measurement of interest income will be implemented from January 1, 2014, forward.

The Company is examining the effects of the adoption of this directive on its financial statements.

Note 2 – Other Assets

Reported amounts

In NIS millions

	December 31	
	2012	2011
Isracard Ltd.[(1)]	7	185
Total other assets	**7**	**185**

(1) This balance is unlinked, and bears interest at the rate commonly used at Bank Hapoalim B.M. for weekly short-term deposits. For further details, see Note 4D below.

Note 3A – Equity

A. Composition

	December 31, 2012 and 2011	
	Registered	Issued and paid-up
	In NIS	In NIS
Common shares of NIS 0.0001	43	100

Note 3B – Capital Adequacy According to the Directives of the Supervisor of Banks[1]

Reported amounts

1. Capital for the calculation of the capital ratio

	December 31, 2012	December 31, 2011
	In NIS millions	
Core capital and Tier 1 capital	7	185
Total overall capital	**7**	**185**

2. Weighted balances of risk-adjusted assets

	December 31, 2012		December 31, 2011	
	In NIS millions			
	Weighted balances of risk-adjusted assets	Capital requirement	Weighted balances of risk-adjusted assets	Capital requirement
Credit risk	4	*-	92	8
Operational risk	1	*-	3	*-
Total weighted balances of risk-adjusted assets	**5**	***-**	**95**	**8**

* Amount lower than NIS 0.5 million.

3. Ratio of capital to risk-adjusted assets

	December 31, 2012	December 31, 2011
	In percent	
Ratio of core capital and Tier 1 capital to risk-adjusted assets[1]	140.0	194.7
Ratio of total capital to risk-adjusted assets[1]	140.0	194.7
Minimum total capital ratio required by the Supervisor of Banks	9.0	9.0

(1) Calculated in accordance with Proper Conduct of Banking Business Directives No. 201-211, “Capital Measurement and Adequacy.”

Note 3B – Capital Adequacy According to the Directives of the Supervisor of Banks[(1)] (cont.)

Capital Adequacy Target

The Company has a policy, which has been approved by the Board of Directors and by Management, of maintaining a capital-adequacy level according to a capital target that is higher than the minimum ratio required by the Supervisor of Banks. In the opinion of the Company, the capital target set by the Board of Directors and Management reflects the appropriate required level of capital given its risk profile and risk appetite. As at the reporting date, the target core capital ratio is 7.5%, and the target total capital ratio is 12.5%.

As part of the gradual process of adoption of the Basel III directives in Israel, on March 28, 2012, the Supervisor of Banks issued a letter entitled, "The Basel III Framework – Minimum Core Capital Ratios." The letter requires banks and credit-card companies to maintain a core capital ratio of 9% (instead of the current 7.5%) by January 1, 2015. The Company is preparing to comply. In addition, a banking corporation whose total consolidated balance-sheet assets constitute at least 20% of the total balance-sheet assets in the banking system will be required to maintain a minimum core capital ratio of 10% by January 1, 2017. For such banking corporations, the core capital ratio of 9% to be implemented by January 1, 2015 will serve as an interim target.

The Company is studying this directive and its expected implications in connection with the formulation of a revised capital plan, with the aim of ensuring the implementation of the directive and compliance with the new core capital ratio requirements; the Company will adapt to the Group policy as necessary.

Note 4 – Contingent Liabilities and Special Agreements

A. Antitrust Issues and Additional Regulation

Antitrust Issues

Most of the Company's activity is performed for the Company and on its behalf by Isracard. In the area of clearing, this activity includes clearing of transactions executed with merchants in Israel in foreign currency using MasterCard cards issued abroad. Isracard clears, for itself, transactions executed with merchants in Israel using MasterCard and Isracard cards issued in Israel, and transactions executed in Israel in Israeli currency using MasterCard cards issued abroad.

Reports by Isracard and by Bank Hapoalim indicate, among other matters, that in October 2006, Isracard and Bank Hapoalim, together with other credit-card companies (not including the Company) and other banks, filed a request with the Antitrust Tribunal to approve a restrictive arrangement under the terms formulated and agreed upon with the Antitrust Commissioner. An amended cross-clearing arrangement, revising the earlier agreements, was submitted to the Tribunal on December 28, 2011; this arrangement is in effect from the date of its approval until December 31, 2018. A ruling handed down by the Antitrust Tribunal on March 7, 2012 approved the amended arrangement, including all of the terms thereof.

A common technical interface for the credit-card companies Isracard, Aminit, Leumi Card, and CAL began to operate in June 2007, for the clearing of transactions executed in Israel using Visa and MasterCard cards issued in Israel. Expansion of the activity of other companies in clearing transactions executed in Israel using MasterCard cards may influence the Company's activity and detract from its revenues, despite the fact that its activity is focused on the clearing of transactions executed using MasterCard cards issued abroad.

Although the Company is not directly associated with the processes described above, the Company estimates that these processes, or part of such processes, may influence the Company's activity and impair its revenues, despite the fact that its activity is focused on clearing transactions in MasterCard cards issued abroad. The Company cannot estimate which of the factors mentioned will materialize, when such factors may materialize, or the extent of their impact.

Additional Regulation

1. A private bill was submitted to the Knesset in March 2010, according to which credit-card companies must note in their statements to cardholders whether a transaction performed by the cardholder constitutes a transaction in a missing document. This bill was passed in a preliminary reading on May 26, 2010, and transferred to the Economics Committee to be prepared for a first reading. On May 23, 2010, a ministerial committee made the decision to promote this bill through regulations, in coordination with the Ministry of Justice.

   In accordance with these decisions, following discussions of this matter with the Ministry of Justice, an agreement was reached regarding the execution of the amendments under both of the aforesaid bills in Proper Conduct of Banking Business Directive No. 470, Charge

Note 4 – Contingent Liabilities and Special Agreements (cont.)

A. Antitrust Issues and Additional Regulation (cont.)

Cards (hereinafter: the "**Directive**"). A draft amendment of the directive was distributed in June 2011.

The private bill on reporting of transactions in a missing document passed in the first reading in August 2011. If the matters addressed by the bill are included in the Directive, as noted above, it is likely that the legislation on this matter will not be promoted.

In November 2011, the matters addressed by the aforesaid bills were formulated into binding directives, through amendments to Directive 470, as noted above. The amendment of the Directive has no effect on the Company.

2. A government bill approved by the Knesset plenum and published in the Official Gazette of the Government of Israel in August 2011 concerns, among other matters, the area of discounting, as well as a directive whereby an issuer that issues ten percent or more of the number of charge cards issued in Israel, or an issuer of charge cards used to execute at least ten percent of the amount of transactions executed in Israel, shall be required to contract with a clearer for cross-clearing of transactions in the charge card which it issues. The directives of this law have been in effect beginning on May 15, 2012. This law has a negative effect on the Company; however, at this stage the Company cannot estimate the full actual extent of this effect.

3. Pursuant to an instruction published by the Bank of Israel in November 2011, banking corporations and credit-card companies must provide disclosure in their board of directors' reports of any group of borrowers whose net indebtedness on a consolidated basis (after the permitted deductions) exceeds 15% of the capital of the banking corporation or credit-card company, as detailed in the instruction. This instruction shall apply from the financial statements as at September 30, 2011, to the financial statements as at September 30, 2012. The duration of the instruction was extended to September 2013 in January 2013. As at the date of this report, there is no group of borrowers whose net indebtedness on a consolidated basis exceeds 15% of the capital of the Company (as defined in Directive 313).

4. In December 2011, a government bill was passed in the first reading and transferred to the Constitution, Law, and Justice Committee to be prepared for the second and third readings. The bill sets forth several amendments to the Prohibition of Money Laundering Law and the Prohibition of Terrorism Financing Order, including with regard to reporting duties and the duty to receive identifying information. Discussions are also being conducted by the Constitution, Law, and Justice Committee regarding various amendments to the Money Laundering Prohibition Order applicable to banking corporations.

Note 4 – Contingent Liabilities and Special Agreements

A. Antitrust Issues and Additional Regulation (cont.)

In July 2012, a proposal to amend the Prohibition of Terrorism Financing Law, concerning the procedure for declaring terrorist organizations and terrorist operatives in Israel, was passed in a second and third reading.

5. In February 2012, the Constitution, Law, and Justice Committee approved an amendment to the Charge Card Regulations, pursuant to which the Supervisor will be able to issue directives that differ from the current text of the regulations with regard to the delivery of statements to customers. Directive 470 was amended accordingly in September 2012. The Company estimates that this amendment will have no effect on the Company.

6. In March 2012, the Justice, Technology, and Information Authority issued a draft guideline concerning restrictions on the collection of identification numbers by database owners. If the draft becomes binding in its current format, it is likely to have an impact on the Company; however, the Company cannot estimate the extent of this impact.

7. In May 2012, the Knesset plenum passed a private bill, in a second and third reading, pursuant to which the Governor of the Bank of Israel would have the authority to set rules regarding the minimum font size for notifications sent to senior citizens (as defined in the Senior Citizens Law, 1989). The Company estimates that if such rules are established, they will have no material effect on the Company.

8. In June 2012, the Knesset plenum passed a government bill, in a first reading, which would update the list of causes with regard to conditions considered depriving conditions in uniform contracts, and establish rules with regard to the authority of the Uniform Contracts Court. At this stage, the Company cannot estimate whether the aforesaid bill will result in legislation, and if so, its implications for the Company, if any.

9. In July 2012, the Knesset plenum passed a government bill, in a first reading, for the promotion of competition and reduction of concentration. A discussion on this matter was held on August 29, 2012.

10. In July 2012, a private bill was passed in a second and third reading, according to which a condition in a uniform contract establishing a minimum rate for the CPI shall constitute a depriving condition. This amendment has been in effect beginning on November 12, 2012. The Company has prepared for the implementation of the law. The Company estimates that this law will have no material effect on the Company.

Note 4 – Contingent Liabilities and Special Agreements (cont.)

A. Antitrust Issues and Additional Regulation (cont.)

11. In July 2012, the Economics Committee held a discussion of the recommendations of the Committee for Increased Competition in the Banking Industry. The public was permitted to submit comments on the interim report until August 15, 2012. In addition, on August 14, 2012, the Bank of Israel published a draft of rules issued as a supplementary measure to the publication of the interim report of the Committee for the Examination of Increased Competition in the Banking Industry, in order to promote and improve the efficiency of the formal proceeding, reflecting the main points of the recommendations of the report in the area of fees. Following the completion of the process of consultation with the members of the Advisory Committee on Banking, and the examination of the responses of the parties who submitted their comments on the recommendations of the interim report in writing, a final version of the rules will be formulated. The Banking Rules concerning fees were published in November 2012, and took effect in January 2013. Among other matters, the rules cancel the fee for changing debiting dates of credit cards. In addition, the service provided by a clearer to a discounting service provider was declared a service subject to supervision. The Company estimates that this amendment will have no material effect on the Company.

12. In August 2012, the Knesset plenum approved an increase of the rate of value-added tax by 1 percent starting September 1, 2012.The Knesset plenum also approved an increase of the rate of income tax on individuals and the rate of employers' contributions to National Insurance. For further details, see Note 7 below.

13. In October 2012, the Economics Committee passed a private bill, in a second and third reading, according to which customers should be notified before the immediate repayment of a loan granted to them by a banking corporation is demanded, or before a legal proceeding is initiated, as detailed in the bill. At this stage, the Company cannot estimate whether the aforesaid bill will result in legislation, and if so, its implications for the Company.

    In October 2012, the Knesset plenum passed the bill for dispersal of the 18th Knesset, in a second and third reading. The election recess began on October 16, 2012 and continued until the 19th Knesset took office on February 5, 2013. Legislative proceedings for private bills can continue in the 19th Knesset if they were passed in a first reading by the 18th Knesset, and if the law of continuity has been applied to them.

14. In November 2011, a government bill was passed in a first reading and transferred to the Constitution Committee for preparation for the second and third reading, concerning the establishment of an administrative enforcement mechanism to serve as an alternative to enforcement in a criminal proceeding with regard to violations of the Protection of Privacy Law. The committee discussion scheduled for July 2012 was canceled. In August 2012, a legislative memorandum was issued amending the Protection of Privacy Law, aimed at improving compliance with the provisions of the Protection of Privacy Law and

Note 4 – Contingent Liabilities and Special Agreements

A. Antitrust Issues and Additional Regulation (cont.)

regularizing the protection of information in computerized databases. The public was permitted to submit comments on the memorandum until August 28, 2012.

15. In January 2013, the Supervisor of Banks issued a circular concerning an amendment to Proper Conduct of Banking Business Directive No. 342, "Liquidity Risk Management." The circular was issued as part of the Supervisor of Banks' efforts to strengthen the robustness of the banking system. The amendment of the directive is aimed at strengthening and simplifying liquidity risk management at banking corporations, and constitutes an interim phase in advance of the future adoption in Israel of the Basel III recommendations concerning liquidity.

    The revised directive clarifies the need to maintain a liquidity cushion against predicted liquidity needs under stress scenarios, with a one-month horizon; details the Supervisor's expectations for risk monitoring on a group basis; establishes a requirement to examine the structure of sources of financing in conjunction with financing needs from a long-term perspective; and adds to the qualitative requirements for liquidity risk management.

    The Supervisor of Banks has not established specific rules for credit-card companies with regard to the aforesaid requirements, but mandates the qualitative requirements for risk management and holding of liquid assets to be fulfilled according to the needs of the company, with the necessary adjustments.

    The amendments to Directive 342 will apply beginning in July 2013, with the exception of Section 16 concerning the stable credit ratio, which will take effect at the end of 2013.

16. With regard to new accounting standards and new directives of the Supervisor of Banks in the period prior to implementation, see Note 1G above.

Note 4 – Contingent Liabilities and Special Agreements (cont.)

B. Legal Proceedings and Contingent Liabilities

1. As at the date of this report, several legal claims have been filed against the Company, arising from the ordinary course of its business, in immaterial amounts. Based on the opinion of its legal advisors, the Company estimates that the financial statements include adequate provisions, in accordance with generally accepted accounting principles, to cover possible damages arising from all of the claims, where such provisions are necessary.

2. In July 2010, the Company filed an appeal of its income-tax assessment for 2006. The dispute between the Company and the Tax Authority with regard to the tax assessment for 2006 concerns the sale of the shares of MC. In the opinion of the Company, the sale should be treated as an event requiring capital-gains tax, rather than as an event of redemption of shares, which carries a different taxation rate. Following a preliminary hearing held at the District Court of Tel Aviv, and after the Company submitted its summations, the Company and the Tax Assessment Officer reached a settlement in which the Company will pay a total of NIS 850,000. On December 31, 2012, the District Court approved the settlement and granted it the status of a ruling.

C. Indemnification of Directors and Other Officers

The Company has undertaken a commitment to indemnify directors and other officers of the Company, as they may be from time to time. The indemnification letter approved by the general assembly on February 12, 2012, with the approval of the Audit Committee and the Board of Directors, was adjusted to changes in legislation. The amount of the indemnification to be provided by the Company under this commitment to all insured parties of the Company in aggregate in respect of one or more indemnity events shall not exceed 30% of its equity, according to the most recent (annual or quarterly) financial statements known before the actual payment.

D. Agreement with Isracard (the Parent Company)

An agreement is in place between the Company and Isracard to formalize the joint activities of the parties. Account settlement between the companies is performed in accordance with this agreement.

Transactions executed in Israel in Israeli currency or foreign currency and paid to the supplier in Israeli currency are cleared by Isracard. Transactions executed in Israel in foreign currency and paid to the supplier in foreign currency are cleared by the Company.

Note 5 – Net Operating Income (Expenses) Under the Agreement with Isracard Ltd.

Reported amounts

In NIS millions

	For the year ended December 31		
	2012	**2011**	**2010**
Income			
Income in respect of merchants	15	15	14
The Company's share of royalties from Banks Under Arrangement	4	3	3
Total income	**19**	**18**	**17**
Expenses			
Operating expenses	20	18	17
Payments for operation and management of the arrangement	5	4	4
Total expenses	**25**	**22**	**21**
Total	**(6)**	**(4)**	**(4)**

Note 6 – Interested and Related Parties

Reported amounts

In NIS millions

A. Balances

	December 31, 2012		December 31, 2011	
	Interested parties		Interested parties	
	Controlling shareholders		Controlling shareholders	
	Year-end balance	Highest balance during the year	Year-end balance	Highest balance during the year
Isracard Ltd.	**7**	**185**	**185**	**185**

B. Summary of Results of Business with Interested and Related Parties[1]

	For the year ended December 31		
	2012	2011	2010
Net operating expenses according to the agreement with Isracard	(6)	(4)	(4)
Net interest income	2	6	4
Total	**(4)**	**2**	**(*-)**

(1) See Note 5 above.

* Amount lower than NIS 0.5 million.

Note 7 – Provision for Taxes on Profit

Reported amounts

In NIS millions

1. Item Composition

	For the year ended December 31		
	2012	**2011**	**2010**
Current taxes for the accounting year	-	*-	*-
Taxes for previous years	*-	-	-
Provision for taxes on income	***-**	***-**	***-**

2. Adjustment of the theoretical amount of tax that would apply if operating profits were taxed at the statutory tax rate applicable to the Company in Israel, to the provision for taxes on operating profit as allocated to the statement of profit and loss:

	For the year ended December 31		
	2012	**2011**	**2010**
Tax rate applicable to the Company in Israel	25%	24%	25%
Tax amount based on statutory rate	(1)	*-	*-
Timing difference for which there are no deferred taxes	1	-	-
Provision for taxes on income	***-**	***-**	***-**

* Amount lower than NIS 0.5 million.

3. Final tax assessments have been issued to the Company up to and including the tax year 2005, including tax assessments considered to be final under the Income Tax Ordinance, up to and including 2007.

4. Changes in Tax Rates

On July 14, 2009, the Knesset passed the Economic Efficiency Law (Legislative Amendments for the Implementation of the Economic Plan for 2009 and 2010), 2009, which among other matters set forth an additional gradual reduction of the corporation tax rate, to 18% from the tax year 2016 forward. In accordance with the aforesaid amendments, the corporation tax rates applicable in the tax years 2010 and 2011 were 25% and 24%, respectively.

The Law for Change in the Tax Burden (Legislative Amendments), 2011 was passed by Knesset on December 5, 2011. Pursuant to this law, the tax reduction established in the Economic Efficiency Law will be canceled, as noted above, and the rate of corporation tax will stand at 25% from 2012 forward.

The Value Added Tax Order (Rate of Tax on Non-Profit Associations and Financial Institutions) (Amendment), 2012, was published in the Official Gazette of the Government of Israel on August 30, 2012. The amendment adjusts the rate of value-added tax to 17% beginning on September 1, 2012. The change in the rate of tax had an immaterial effect.

Current taxes for the periods reported in these financial statements are calculated according to the tax rates established in the laws as noted above.

Note 8 – Information Based on Historical Nominal Data for Tax Purposes

In NIS millions

	December 31	
	2012	2011
Total assets	7	185
Total liabilities	*-	*-
Equity	7	185
Nominal net profit (loss)	(4)	2

* Amount lower than NIS 0.5 million.