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Bank of Jerusalem

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Contents

Translation: "Globus-Translations"
Design: Studio "Shahar Shoshana"
from the "Scorpio 88" Group
Printed by the Old City Printer, Jerusalem

Statement by the CEO

Part One
Description of the banking corporation's general business development

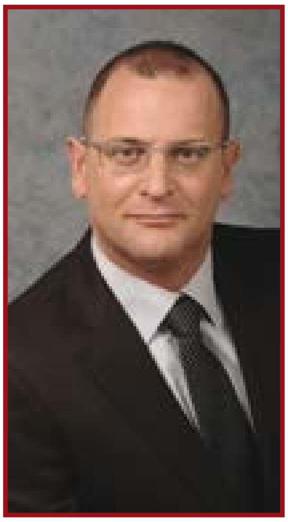
Part Two
Other information

Part Three
Description of the banking corporation's business by activity sectors

Part Four
Matters related to the banking corporation's overall activities

Management review, financial and periodic reports and the corporate governance questionnaire

Statement by the CEO



The year 2012 continued to be one of increasing economic uncertainty around the world and in Israel. Although sales in the real estate market have recovered, the macro economic parameters have worsened and Bank of Israel interest rates are continuing to decline.

Bank of Jerusalem continued with the implementation of its strategic plan in various areas:

In the retail sector, the Bank continued to implement its competitive retail strategy in a number of levels, largely in an innovative and different manner than its competitors.

1. Entry into the Current Account sector in the last quarter of 2012, the Bank launched a large-scale campaign to enter the current accounts sector and attract new customers, at the center of which is an extremely attractive value offer that includes management of the current account for private customers in shekels without a current account fees, without preconditions and for an unlimited period of time. The move is unique in the world of Israeli banking and resulted in over 3,000 new customers by the balance sheet date.

   The Bank of Jerusalem views this move as part of its implementation of its long-term retail expansion strategy.
2. Increased marketing of short-term deposits (up to one year) at extremely attractive prices in relation to the competition, through both the branches and through the closed system. This is a significant move in terms of competitiveness in this field. Standard practice in the banking system is that the Banks' table prices are approximately 20% of the Bank of Israel's interest rate while the Bank of Jerusalem offers at least 80% of the Bank of Israel's interest rate and for any sum of deposit.
3. The Bank presented a profile of its future branches – the video branches. Two video branches have already opened while two more are scheduled to open in ensuing days.

   The video branch provides services to customers 10-12 consecutive hours a day, five-and-a-half days a week. The branch occupies a small space and service is provided via video by a banker at the call center. The level of service involved is extremely high and the cost is extremely low – a fact that allows the Bank to stand behind its value offer of no current account fees as well as offer high interest rates on deposits and current accounts.
4. Deepening consumer credit activity based on a working model that combines examination of each and every customer under a supporting decision model, as well as detailed examination by a branch banker.

   This year, as a result of the continued growth of the consumer credit portfolio, expenses for credit losses significantly increased.

   The Bank continued to draw conclusions and improve its underwriting models and treatment of problem debts, to improve the quality of the credit portfolio.

   On the one hand, the Bank's entry into the consumer credit sector significantly improves, income from financing and the margin. On the other hand, the level of expenses for credit losses will be higher than in the past.

5. Continuation of sales of the Bank's traditional products. Mortgages, deposits, Securities, credit cards and credit for vehicles, with the emphasis on the second-hand vehicle market.
6. Extensive upgrade of work procedures and regulatory entities in the bank, primarily in the retail sector.
7. Continuing the upgrading project for the computer systems while strengthening the the Bank's core system, and adopting a multi-channel environment. This year, the telephone call center operated at full capacity and expanded during the year. In addition, the customer relations management (CRM) system was launched, as well as the digital archives. The Bank's new website is currently being launched. Over the next several months, the Bank is planning a gradual deployment of ATM machines.

Furthermore, concerning oversight of construction projects, the Bank continued to grow although at lower rates than last year.

This year, there was a material increase in the Bank's revenue from financing of its core business sectors. As a result of this expansion and correspondingly, there was an increase in expenses, as direct consequence from the deployment of this activity.

In 2013, the Bank is planning to continue its efforts and further expand the retail sector.

Part of the above-mentioned information is information facing the future. The bank's actual conduct may be essentially differ from the above-mentioned description as result from a large number of factors, including, among others, as a result of unexpected political/security events, changes in customer preferences and regulations, changes in legislative instructions, or instructions from supervisory factors.

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Uriel Paz
Chief Executive Officer

Report of the Board of Directors

For the general assembly of Shareholders

Financial Statement for 2012

Bank of Jerusalem Ltd. and its consolidated companies

Report of the Board of Directors for the General Assembly of Shareholders

At the meeting of the Board of Directors held on February 28, 2013, the decision was made to approve and publish the consolidated financial statements of Bank of Jerusalem Ltd. (hereinafter: "the Bank" or "Bank of Jerusalem") and its subsidiaries for the year 2012 (hereinafter "the book year"). The financial statements were prepared in conformity with the instructions of the Supervisor of Banks, and data presented in reported amounts.

Part One – Description of The General Development of The Business of The Banking Corporation

Activity of the banking corporation and description of business developments

The Bank

Bank of Jerusalem was founded in 1963, as a public company, in accordance with the definition in the Companies Ordinance, New Version, 5743 – 1983, in the name of Bank of Jerusalem for Development and Mortgages Ltd. Bank issued its shares to the public for the first time in 1992, thereby becoming a company whose shares are traded on the Tel Aviv Stock Exchange. In 1996, the Bank's name was changed to its current name, the Bank of Jerusalem Ltd. Mrs. Kena Shoval is a controlling shareholder of the Bank conforming to the control permit from the Bank of Israel.

The Bank is a banking corporation, with a banking license according to the Banking Law (permit), 5741 – 1981, and operates as a commercial bank as of 1998. The Bank is based on an extensive homeowner customer base, Israeli and foreign residents, and operates in mortgage sector, consumer credit, savings and deposits, financing of constructions for residential purposes, financing vehicle purchase, other commercial credit and capital market activity.

The Bank's management is located at Airport City. The Bank operates through 18 branches located across the country.

Objectives and Business Strategy

At the center of the Bank's strategic plans is the extensive growth of the retail sector while increasing the customer base and the product packages, as well as services to households, while diversifying and dispersing its retail activity areas. For example: consumer credit and deposits (hereinafter in this report: "the Plans" or "the Strategic Plans").

According to the Plan, strategic growth will be accompanied by offering differentiated value while developing the Bank's retail expertise. At the base of the the Strategic Plans, is a decrease in the Bank's systematic risks by diversifying and customer deficit and minimum revenue resources, as well as public deposits with emphasis on households, and from well-dispersed consumer credit.

The Strategic Plan is supported by competitive environment analysis that indicates the positive potential for customer recruitment from households. This, in view of the centralization in banking systems on one hand, and on the other hand, the increase in customer awareness and readiness to improve his situation.

In order to achieve the plan's aforementioned goals, the Bank is operating in several areas of operation that were defined in the strategic plan as follows:

- Expansion of the Bank's current activity with emphasis on expansion of activity in current accounts and consumer credit sectors.

- Opening 3-5 branches in 2013 as well as the expansion of the branch system in 2014-2015 by opening technology-based video branches.

- Transition to a widespread use of technological means for communication with customers including multi-channel banking, enabling opening a deposit certificate via the Internet, while reducing the dependency on activity in the physical branches.

- Continuation of the upgrade of the Bank's IT system including assimilation of the CRM system, continuation of assimilation of the advanced telephony service center, which would allow for most banking transactions to be carried out without having to arrive at the branch, and is characterized by state-of-the-art technological capabilities. The project further includes infrastructure for the service stations and ATMs as well as an upgrade of the Bank's website. The total investment is estimated at tens of millions of shekels, and is being implemented gradually and in a controlled manner.

- Offering better financial value to the customer, in the savings and deposits sector, as well as in additional consumer areas. The value offer does not come only at the expense of costumer profitability, but is based on diverting the operating model to the Internet. This model will allow for lower costs without affecting the quality of the service provided to the customer, and without the Bank having to compromise on the quality of risk management.

- Increasing consumer awareness to the Bank's image as a competitive and creative bank.

In October 2012, the bank began a gradual process for recruiting household current accounts (private accounts). During 2013, the bank wishes to recruit thousands of new accounts from among both new and existing customers. In order to accomplish this, the Bank formulated a value offer with a sweeping exemption from current account fees for individual Israeli residents.

A current account is considered an anchor product and as such, expansions in current accounts significantly contribute to reducing credit risks by broadening the connection with customers and by diversifying banking products. Furthermore, it allows the bank to expand its customer base over time. Increased profitability will be achieved as a result of the sale of the accompanying products.

The bank aims to serve customers while maintaining a narrow and optimal cost base. As a result, the concept of the extremely small branch that can serve about 3000 customers was developed. The branch, staffed by one or two employees per shift, relies on technology that enables video conferencing between the customer and the banker at a call center. It should be noted that a gradual and controlled deployment of these branches is planned while maintaining the existing branch system.

As part of the continued planning and review of retail expansion, the Bank is exploring the expansion of several contact points with the customer through cooperation with external retail partners. The Bank views such collaborations as a strategic solution for the relative lack of branches. This of course, is subject to an in-depth review of risk management and allocation of capital required, as well as the required regulatory approval.

In the consumer credit sector, the Bank 's Strategic Plan continues the procedure that had already begun during the fourth quarter of 2010, to provide consumer credit to the Bank's customers, as well as to new customers who are members of the household sector. This procedure gradually brings diversification of the Bank's credit portfolio, which is concentrated in mortgages. Since the fourth quarter of 2010, an extensive volume of consumer credit has been provided to customers. At the same time, expenses for credit losses in this credit sector, which provides the highest margins, increased. It should be noted that most of the increase in the provision in the fourth quarter is attributed to the update of the provision coefficients on a group basis following Bank of Israel directives. The Board of Directors and Management continued to follow up the conclusions and improve the underwriting models as well as work processes to improve the quality of the consumer credit portfolio.

Additionally, the Bank places much emphasis on strengthening its supervision and control array. Within these confines, the functions of the first control level were strengthened, and a retail accounts management and operations department were established, supervision has been established in the branch banking department, with focusing on close supervision of branch work as its role. In addition, the functions of the second control and third control level were strengthened – For information, see details in the chapter on "Risks and Risk Management Methods."

Furthermore, the Bank continues with business activity in project oversight, and this while conservatively reviewing business profitability, and integrating institutional entities in syndicates for dispersal of credit risk in large transactions and regularly monitoring the real estate market situation.

The change in definition of the Bank's core activity and the massive expansion of contact points with the customers and the supply of retail services are accompanied by the Bank's meticulous examination for changes in the risk profile derived from new activity characteristics and the allocation of required capital suitable for the aforementioned risks.

The Bank work plan for 2013, which is based on the principles of the Strategic Plans, relies on, among others, capital ratios (total capital ratios and core capital ratios) as defined in theICAAP for 2012. The planning was submitted to the Bank of Israel with the Bank receiving a first reference from the Bank of Israel for this plan and for the ICAAP document. For additional information, please see the "Risk and Risk Management Methods" chapter.

The Bank's plans and assessments, as specified above, are future facing information, as well as based upon assumptions and different forecasts presented to the Bank's Board of Directors. This information may not be realized because of changes that may be applied for various factors that are not controlled by the Bank only. Influencing factors include forecasts and assessment concerning economic development in Israel and globally, especially concerning the economic situation, including the influence of macro-economic and geopolitical conditions, changes in capital markets, as well as other additional factors influencing risk exposure: public preference, instruction by supervisory factors and others, aspects related to the Bank's image, technological developments and the subject of human resources.

The Bank's activity during 2012

In 2012, the Bank of Jerusalem operated in a challenging environment, against the background of the local market's recovery with the increasing economic uncertainty and attempts to recover from the global financial crisis that broke out during 2008.

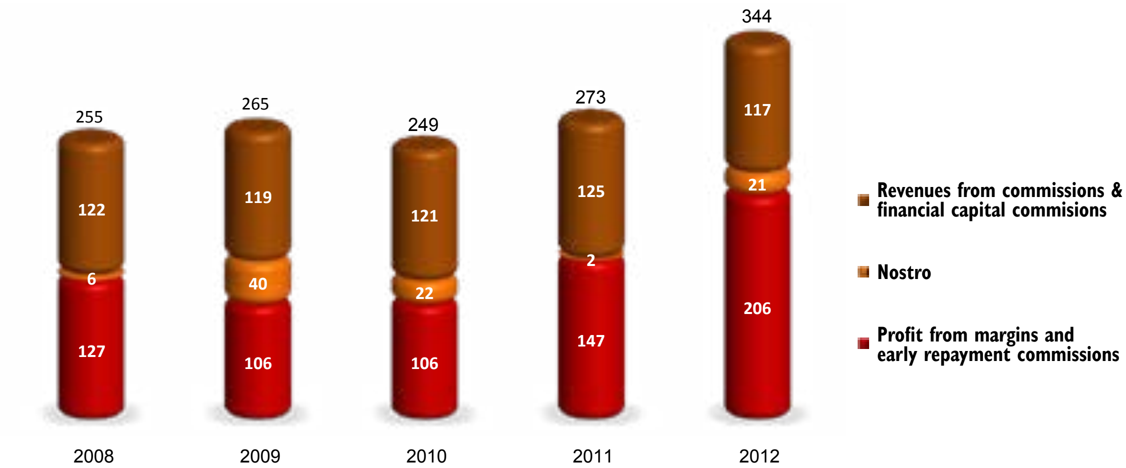
Developments in Profit and Loss items

In accordance with the Bank of Israel's instructions, as of the report to the public for the first quarter of 2012, the manner of presenting the Profit and Loss Statement has been changed. For more information, see Note 2 – Accounting Policies for the Financial Statements.

Net income for the report year amounted to NIS 36.1 million, compared to NIS 24.7 million in the previous year (neutralized by the profit from the sale of the administration building for NIS 20.8 million in 2011), an increase of 46%. Most of the growth can be attributed to increased net income from interest and from increased financing income not from interest.

The net yield on average equity was 5.4% compared to 4.0% for the same period previous year (and in contrast with 7.3% without neutralization of the profit from last year's sale of the administration building).

Listed below is the composition of the bank's total income in millions of NIS:



Net income from interest in the report year totaled NIS 230.9 million, in contrast with NIS 174.8 million in 2011 – a 32% increase. Most of the growth of approximately NIS 43 million is attributed to a sharp increase in the bank's core businesses – from the continued improvement in mortgage profits, and from increased consumer credit and business credit balances. In addition, an increase of NIS 16 million was recorded that is attributed to the lowering of cost of raising resources, inter alia, through expansion of recruitment channels, as well as through the "closed system" (For information about the "closed system", see below Chapter on Recruitment of Financing Sources). In contrast, a decrease of approximately NIS 3 million was recorded in income due to a lower interest rate environment.

Expenses for credit losses during the report year totaled NIS 36.0, compared to NIS 15.1 million for the same period last year. The reviewed period included an increase in the group provision attributed to an increase in consumer credit portfolio as well as an update of the group provision rate in accordance with Bank of Israel directives.

The ratio of expenses for credit losses for the period reviewed on an annual basis for the total net public credit (including off-balance-sheet credit risk) is 0.37%.

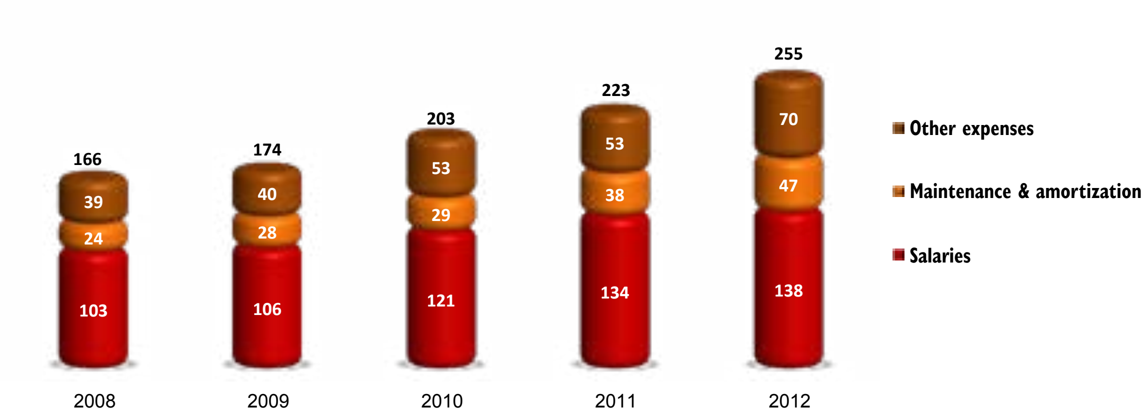
Non-interest financing income for the report year totaled NIS 22.6 million, compared to NIS 6.1 million for the same period last year. The main increase is attributed to an increase in Nostro earnings.

Fees for the report year totaled NIS 90.2 million, compared to NIS 91.9 million for the same period last year. The decrease is attributed to a decline in revenue from securities activity totaling NIS 2.0 million; a decline in revenue from life and property insurance for a sum of NIS 1.6 million; and from a decline in revenue from fees based on the degree of collection (loans to payables from government money) of NIS 1.4 million; against a recorded increase of approximately NIS 3.6 million in revenue from project oversight.

Operating and other expenses for the report year amounted to NIS 254.5 million, compared to NIS 223.1 million in the previous year; an increase of 14%. The main increase is derived from a rise in building and equipment maintenance expenses resulting from moving from an owned property to a rented one, increased payroll and advertising, computerization, depreciation, and consulting expenses, all of which are based on implementing the Bank's strategic plan.

Payroll expenses for the report year totaled NIS 137.8 million, compared to NIS 134.1 million for the same period last year. Despite the continued growth and development of the bank, the increase in this Section is moderate.

Listed below is the composition of the bank's total income in millions of NIS:



The provision for taxes on profits from regular activity in 2012 amounted to a total of NIS 17.7 million. The effective tax rate for 2012 reached 32.9%, compared to the statuary tax rate of 35.5%. For additional information see Note 29 of the Financial Statements.

Below are details of net earnings per share during the last three years:

Net Earnings per Share (in NIS)

	2012	2011	2010
Net Earning Per Share	0.51	0.35*	0.48

* In 2011, the net Earnings per Share does not include the profit from the sale of the administration building, without neutralization of this profit, the Earnings per Share for 2011 would have been NIS 0.65.

Developments in Balance Sheet Items

The total of the Balance Sheet as at December 31, 2012, amounted to NIS 12,291 million, compared to NIS 11,483 million at the end of 2011; an increase of about 7%. The increase derives from an increase in credit balances for the public, as detailed below.

The balance of liquid assets (cash, deposits in banks and securities) at December 31, 2012, totaled NIS 2,524 million, compared to NIS 2,283 million at the end of 2011; a decrease of about 11%.

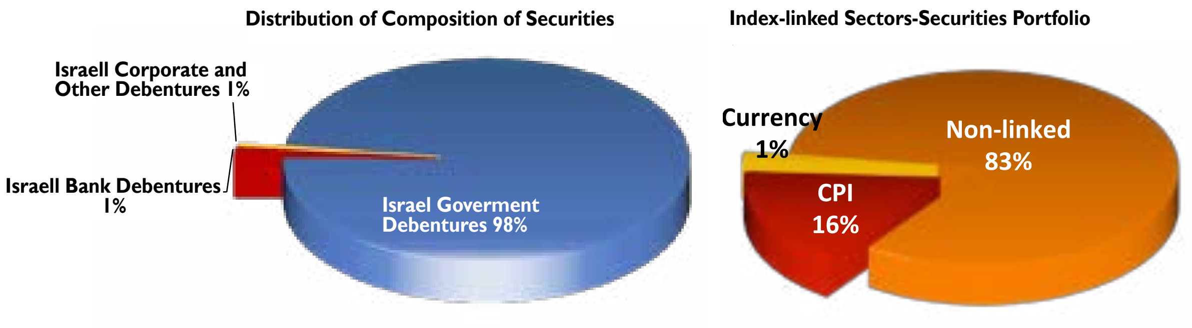
The cash and deposits balances at the banks as at December 31, 2012, amounted to NIS 1,361 million, compared to NIS 792 million at the end of 2011; an increase of about 72%.

The Balance of Securities for December 31, 2012, amounted to NIS 1,163 million, compared to NIS 1,491 million at the end of 2011; a decrease of about 22%.

Below is the composition of the securities portfolio:

	Balance for December 31		Percentage of Securities Portfolio on December 31, 2012
	2012	2011	
	Millions of NIS		
Israeli government debentures	**1,140**	1,245	98.0%
Israeli bank debentures	**17**	120	1.5%
Israeli Corporate & Other Debentures	**6**	126	0.5%
Total securities	**1,163**	**1,491**	**100%**

Listed below is the composition of the nostro portfolio:

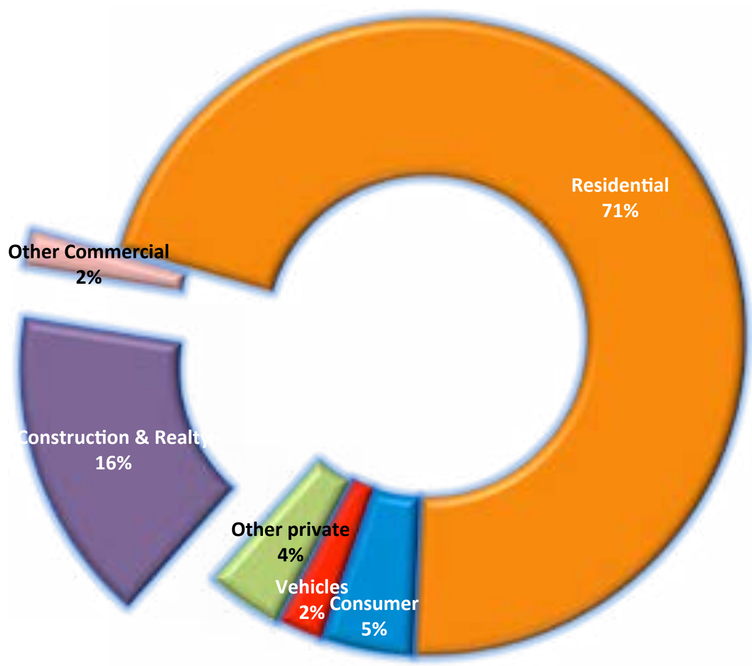


Balance of Public's Credit, net as at December 31, 2012, amounted to NIS 9,581 million, compared to NIS 9,058 million at the end of 2011; an increase of about 6%. The increase derives from an increase in the housing credit portfolio and an increase in consumer credit portfolio.

Below is the composition of the public's credit balance:

	Balance for December 31		
	2012	2011	
	Millions of NIS		Changes in %
Credit for Individuals			
Housing credit	**6,822**	6,558	4%
Consumer credit	**450**	300	51%
Credit for vehicle purchase	**226**	307	-26%
Individuals – Other	**367**	275	33%
Total credit for individuals	**7,865**	**7,440**	**6%**
Commercial credit			
Construction and real estate – Construction (including projects, buyers groups and solar energy)	**1,159**	967	20%
Construction and real estate – Real estate activity (particularly commercial assets)	**377**	392	-4%
Commerce – Other	**180**	259	-31%
Total commercial credit	**1,716**	**1,618**	**6%**
Total credit for the public	**9,581**	**9,058**	**6%**

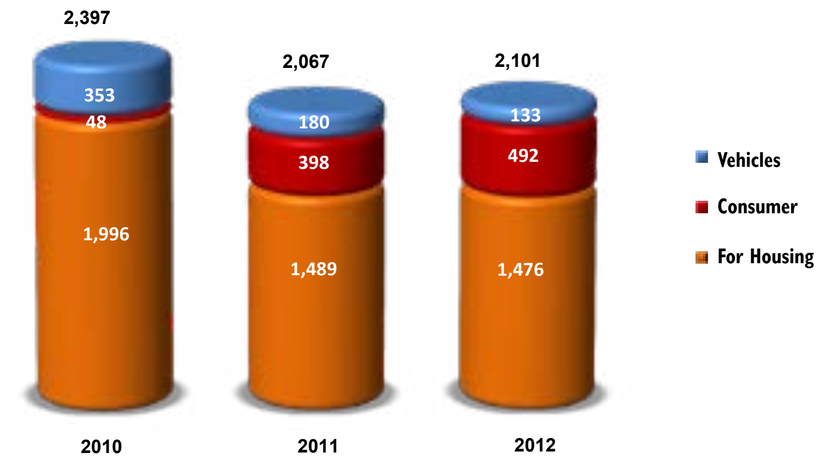
Listed below is the composition of the credit portfolio:



Below is a table with the retail credit performance data:

	For the year ending on December 31		
	2012	**2011**	
	Millions of NIS		Changes in %
Housing credit performances	**1,340**	1,402	-4%
Recycling housing loans	**136**	87	56%
Total housing credit (including recycling)	**1,476**	**1,489**	**-1%**
Consumer credit performance (including credit cards and current*)	**492**	398	24%
Vehicle credit performance	**133**	180	-26%
Total retail credit	**2,101**	**2,067**	**2%**

(*)Net accumulation of the balances of current account and credit cards during the period.



Balance of public deposits Balance of public deposits as at December 31, 2012 totaled NIS 9,814 million, compared to NIS 9,065 million at the end of 2011; an increase of about 8%. The main increase is attributed to an increase in the balance of household deposits to the amount of NIS 930 million as specified below in the Recruitment of Financing Resources chapter.

Balance of debentures and deferred liability notes as at December 31, 2012 totaled NIS 1,581 million (from this – balance of deferred liability notes for a total of NIS 490 million), compared to NIS 1,612 million at the end of 2011 (from this – deferred liability notes for a total of NIS 518 million). On December 24, 2012 the Bank issued deferred liability notes through its subsidiary Jerusalem Financing, and debenture issuances for a total amount of approximately NIS 122 million. Also, deferred liability notes for a total sum of about NIS 72 million. (For more information, see "Events during the Report Year" chapter below).

Total balance of public deposits, debentures and deferred liability notes as at December 31, 2012, amounted to NIS 11,395 million, compared to NIS 10,677 million at the end of 2011; an increase of about 7%.

Developments in off-balance-sheet items

The balance of loans from deposits by collection level (loans to entitled from government money) as at December 31, 2012, totaled NIS 1,997 million, compared to NIS 2,308 million at the end of 2011; a decrease of about 13%. The main decrease derives from an ongoing curtailment of performance volume of loans to entitled in the general market, and from the low-interest environment that caused low economical profitability for utilizing these loans. The income from collection fees by collection level, amounted to NIS 17.0 million in 2012, compared to NIS 18.5 million in 2011.

The balance of security portfolios held in the Bank's custody was about 4,400 customers as at December 31, 2012 amounted to about NIS 2,116 million compared to NIS 1,829 million, held by 4,100 customers at the end of 2011. The income from securities activity amounted to NIS 8.1 million during 2012, compared to NIS 11.4 million during 2011.

The Trust Company of Bank of Jerusalem Ltd (a subsidiary fully owned and controlled by the Bank) handles the trust accounts and financial assets of foreign residents and others. Balance of assets at the Trust Company as at December 31, 2012, amounted to NIS 2 million (compared to a total of NIS 3.5 million during 2011). In 2012, the Company's income totaled about NIS 2 thousand, compared to NIS 28 thousand during 2011.

Developments in revenue and expense rates

Below are the interest disparity (the difference between revenue rate on assets and expense rate on liabilities) in various linked sectors (including derivative influence):

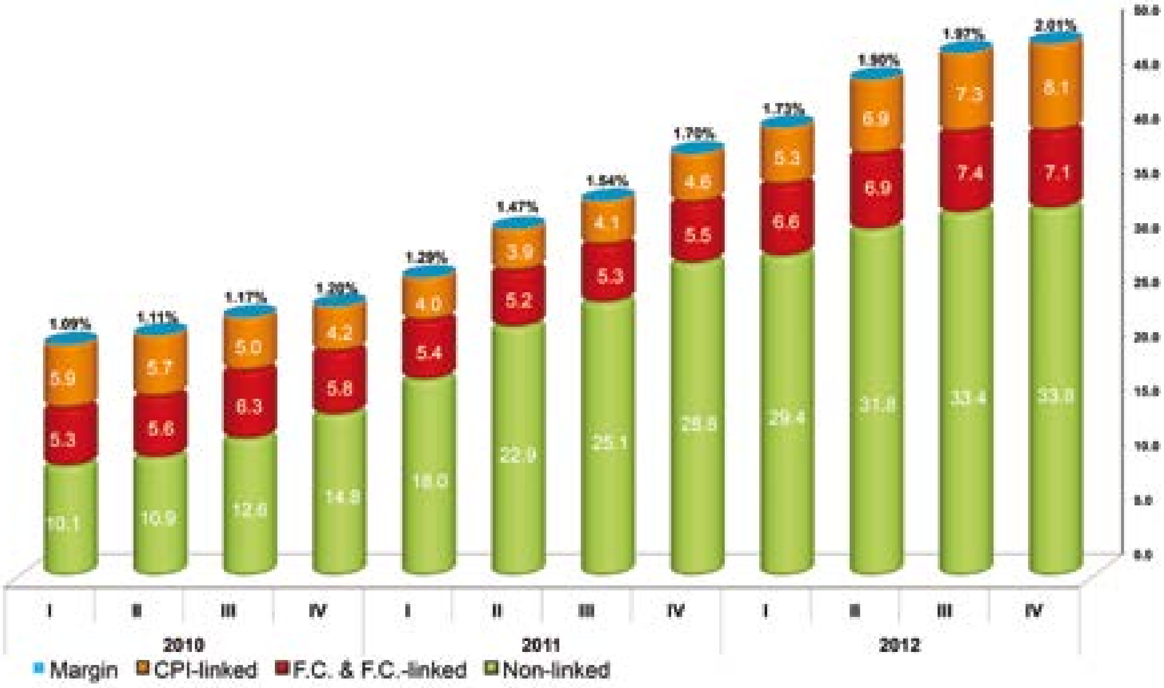
	Average for the year 2012	Average for the year 2011
Un-linked	1.98%	1.76%
Index linked	0.75%	0.15%
In foreign currency and linked to foreign currency	2.47%	1.65%
Total including influence of derivatives	**1.70%**	**1.17%**

The widening of the interest gaps in the non-linked sector derives mainly from improvement in housing credit profitability, as well as a change in the mix in the credit portfolio as detailed above.

The widening of the interest gaps in the linked sector mainly attributed to the improvement in housing credit profitability, as well as a decrease in recruitment costs of index resources.

The widening of the interest gaps in the foreign currency sector is primarily attributed to improved profitability in housing credit.

Listed below is the credit margin data – quarterly average for the years 2010-2012 (in millions of NIS)



For more extensive information, See Appendix C for the Management Review.

Events during the report year

In January 2012, the Bank made an announcement on a change in the deposit pricing model, including an undertaking, according to which the Shekel interest rate on one-year deposits will not be less than 80% interest from the Bank of Israel, except for deposits with fixed interest for a period longer than three months, whose interest rate will not be reduced from 80% of the yield rate for the relevant short-term loan. On deposits for periods of one year or more, the Bank undertakes that the interest rate will not be less than 80% of the yield rate on government debentures or the price of cash, whichever is higher. This undertaking does not depend on the size of the deposit or on opening a checking account. Since the announcement, and during 2012, there has been a significant increase in the recruitment of new deposits under this framework. For more information, see the "Recruiting Financial Resources" chapter.

On April 22, 2012, Standard & Poor's Maalot (hereinafter: Maalot) announced that in continuation of the monitoring of the Bank's rating under Maalot's updated bank-rating methodology (as published on November 9, 2011), it was removing the bank's rating from [1]CreditWatch (with negative repercussions) entered on June 2, 2011, and is leaving the Bank's rating ilA+ (negative rating forecast) intact[2]. For details, please see the Immediate Report dated April 22, 2012, (reference number 2012-01-106239).

1 CreditWatch emphasizes the probable immediate direction of the Diroog change particularly due to identifiable events and short-term trends.

2 The Diroog forecast assesses the potential direction of long-term credit rating (rangung from six months to two years)

On May 15, 2012, an arrangement was signed with the Bank's former CEO Mr. Avi Bazura, concerning the end of his employment. For more information, please see the Immediate Report from May 16, 2012 (reference number 2012-01-126258).

On June 30, 2012, the Israeli government approved economic measures to reduce the deficit, including increasing the Value Added Tax to 17% (instead of 16%). The amendment became applicable as of September 1, 2012.

Accordingly, the statutory tax rate (Companies Tax and Profit Tax) that applied to financial institutions in 2012 will be 35.53% and from 2013 onwards, 35.9%. (instead of the tax rates before this increase – 35.34% in 2012, and 35.06% effective from 2013).

In July 2012, the bank sold all its holdings to the public in debentures of series B of "Jerusalem Financing and Issuance (2005) Ltd." (a bank subsidiary) at n.v. totaling NIS 79,545 thousand.

In July 2012, the recommendations of the Zaken Committee were published to increase competition in the banking system. A significant percentage of the Committee recommendations focused on small businesses. The Bank believes that the Committee recommendations in this area does not materially affect the bank's expected profits since the activity of small and middle-sized businesses in the Bank is not material.

In addition, the Committee published several recommendations that pertained to private household accounts (an individual account that is not a corporation) whose main business is expanding the information available concerning customers. The Bank believes that the Committee recommendations will increase competition in the retail credit sector and can serve as an opportunity for banks that are the size of the Bank of Jerusalem.

The Bank's assessments, as specified above, are future facing information, as well as based upon assumptions, and different forecasts presented to the Bank's Board of Directors. This information may not be realized because of changes that may be applied for various factors that are not controlled by the Bank only. Influencing factors include forecasts and assessment concerning economic development in Israel and globally, especially concerning the economic situation, including the influence of macro-economic and geopolitical conditions, changes in capital markets, as well as other additional factors influencing risk exposure: public preference, instruction by supervisory factors and others, aspects related to the Bank's image, technological developments and the subject of human resources.

In October 2012, the bank began a gradual process for recruiting household current accounts (private accounts). During 2013, the bank wishes to recruit thousands of new accounts from among both new and existing customers. In order to accomplish this, the Bank formulated a value offer with a sweeping exemption from current account fees for individual Israeli residents.

On December 24, 2012, the Jerusalem Financing and Issuances Company issued, according to the shelf offering report as at December 24, 2012, that was published based on the prospectus dated August 31, 2011, debentures (Series H) in n.v. totaling NIS 122,421 thousand. Debentures in consideration for NIS 122,421 and NIS 71,761 thousand n.v., deferred liability notes (Series 10) in consideration for a sum of NIS 71,761 thousand.

Events After the Balance Sheet Date

On January 7, 2013, Jerusalem Investment Portfolio Management Ltd., a wholly owned subsidiary, entered into an agreement with a third party not related to the Bank, for the sale of its portfolio management activity, as defined in the Regulation of Investment Advice, Investment Marketing and Portfolio Management Law 5755-1995 that is managed by it. The transaction is expected to be completed within several months in accordance with the mechanisms established in the agreement between the parties.

It should be noted that the resulting income for the subsidiary from the activities being sold, as well as the consideration for said sale, is not material for the bank.

On February 19, 2013, the Supervisor of Banks published draft directives concerning residential credit and realty, on the allocation of capital and provision for doubtful debts for housing loans and a change in the risk weight of guarantee in accordance with the Sales Law. For more information, see the sub-chapter on Standard Legislative Restrictions, Directives and Contracts from the Supervisor of Banks, and special constraints in the "Household Sectors Chapter" in this statement.

Details of the Main Consolidated Companies

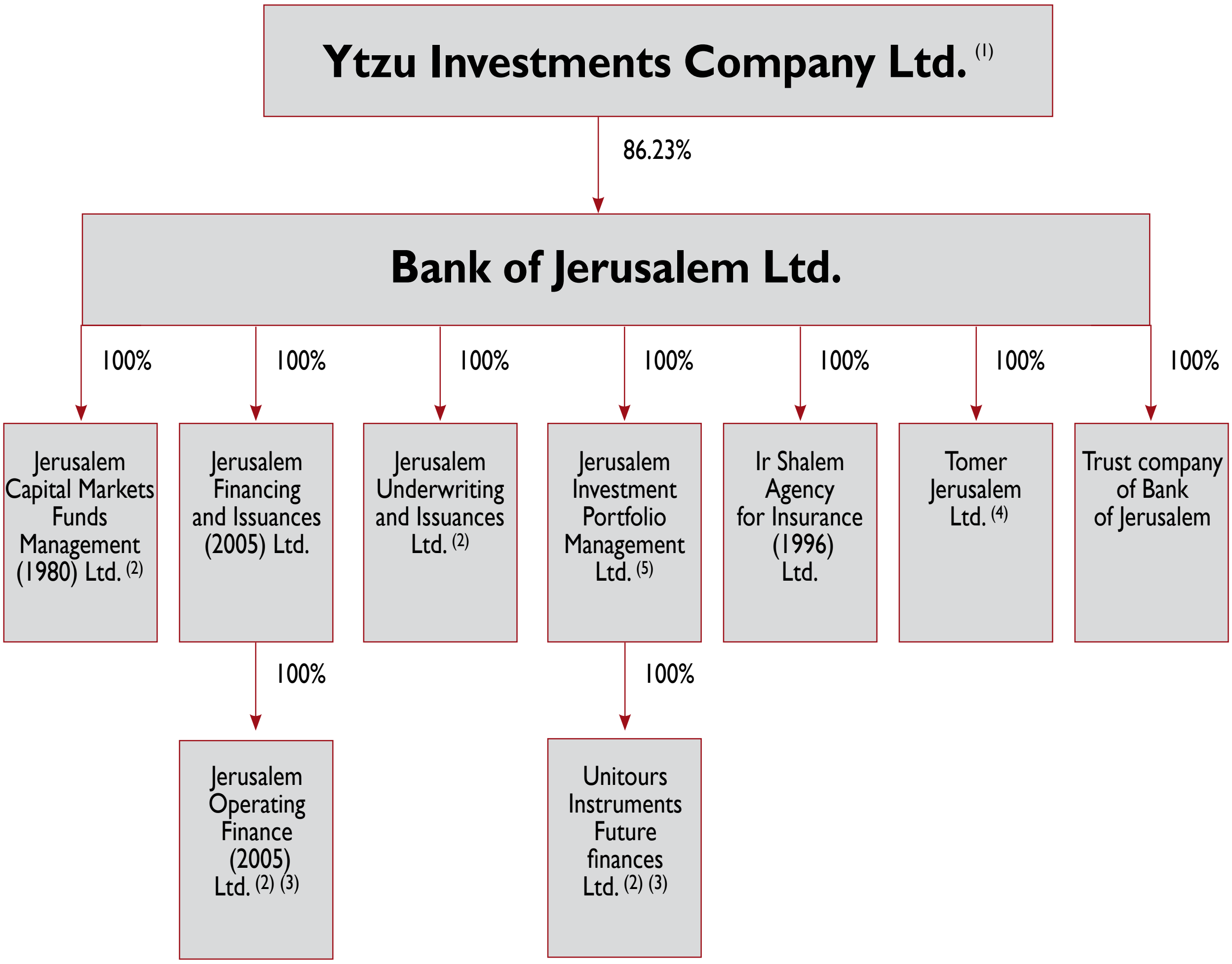
For details about the main consolidated companies, please see note 7 of the Financial Statements.

Main Data from the Financial Statements

Main data from the annual report of the Bank are attached in Appendix A of the Board of Directors' report.

Structural Diagram of the Bank's Holdings

Below is a structural diagram of the Bank's holdings in subsidiaries and in associated companies as at December 31, 2012. Concerning details of the activity sectors of the subsidiaries and associated companies see note 7c.



(1) For details concerning the Bank's controlling shareholders, please see below.

(2) Not active

(3) Company in voluntary liquidation.

(4) Mr. Zalman Shoval has negligible holdings in the company as specified in the regulations 11-13 of the periodical report.

(5) The Company's portfolio management activities were sold to a third party on January 7, 2013.

The Bank's Controlling Shareholders

Mrs. Kena Shoval is a controlling shareholder in the bank, holding 74.30% of the issued and paid-up share capital of Yitzu Investments Ltd., which is a public company whose shares are listed on the Tel Aviv Stock Exchange (Hereinafter: "Yitzu"). Yitzu holds 86.23% of the Bank's issued and paid-up share capital. In addition, Mrs. Shoval holds 0.33% of the Bank's issued and paid capital securities through the companies: H. Shoval Holdings Ltd.; I.C.C. Israel Capital Corporation Ltd.; Financial Trust Corporation Ltd.; which are privately owned companies controlled by Mrs. Kena Shoval.

According to the legal opinion presented to the Bank, Mr. Zalman Shoval (Mrs. Kena Shoval's spouse and a Bank director), Mr. Gideon Shoval (Mrs. Kena Shoval's son and a Bank director), may also be considered a controlling shareholders of the Bank under the provisions of the Banking Licensing Law.

Mr. Zalman Shoval is considered to be controlling shareholder even according to the instructions of the Securities Law.

Forward-looking Information

Part of the information included in the Board of Directors' Report, which does not relate to known information, constitutes forward-looking information, as defined by the Securities Law, 5728 – 1968.

The actual Bank results may materially differ from those included; and if included under forward-looking information, due to a large number of factors, including, among others, as results of deviating economic events, such as: extreme changes in interest rates, depreciation/appreciation of currency and inflation, and also unexpected political/security events that may change the conduct of the public from the aspect of credit taking volume, early repayment, return of current repayment difficulties in all activity sectors of the Bank as well as from aspects of capability for raising resources. Also, regulatory or legislative changes, instructions issued by supervisory authorities and behavior of competitors may affect the bank's activity.

Forward-looking information is characterized by expressions including: "in the Bank's estimate", "the Bank intends …", "is expected to …", "may …", "might possibly …", "estimates that …", and similar expressions.

Such forward-looking expressions include risks and uncertainties since they are based on management's evaluations concerning future events that include, among others:

- Mergers and acquisitions in the banking system and their influence on the sector's competitive structure.

- Influence of changes in regulatory instructions on customer preferences and/or on the banking system's scope of activity, the competitive structure therein, and/or the Bank's profitability.

- Ability to realize the Bank's plans according to the objectives determined in accordance with its strategies.

- Unexpected responses of additional factors (customers, competitors, etc) operating in the bank's business environment.

- Future realization of sector estimates and macro-economic forecasts according to the bank's preliminary estimates.

- Possible results of legal procedures.

- Changes in consumer preferences and/or behavior.

The following information is based on professional evaluations of the bank, on macro-economic forecasts concerning the status of the economy and the business environment, publications and estimates of factors active in the sector, and statistical analysis prepared by the bank concerning its customer's behavior.

The aforementioned reflects the the Bank subsidiaries' point of view at time of editing the Financial Statements concerning future events, based on uncertain assessments. The evaluation of the Bank and its subsidiaries and its business plans is derived from these data and assessments. As mentioned above, the actual results may differ significantly and influence the implementation of business plans or bring about a change in those plans.

Summarized description of activity sectors

The Bank of Jerusalem Group operates through the Bank's headquarters, its branches and subsidiaries. The Bank's activity sectors are classified according to the guide lines from the Supervisor of Banks according to the type of customers included in each of these sectors and do not necessarily match the Bank's organizational structure.

The Bank operates and provides various banking services in four main activity sectors. Below are details on the reported activity sectors:

- **The household sector** – household customers and small business with characteristics similar to that of households.
- **Private banking sector** – This sector includes customers with a medium to high level of financial wealth, and services are provided through a branch specializing in private banking, mainly for foreign residents (mostly from North America, England and France).
- **Business sector** – Customers in this sector are construction and real estate companies, business customers, corporations, and associations.
- **Financial management sector** – This sector includes the Bank's available financial capital and positions, management of the Bank's nostro portfolio, activity vis-a-vis banks in Israel and abroad, and implementation of transactions in derivative financial instruments.

The Bank's activity in recruiting of resources from the public is concentrated in the Financial Division. Due to the fact that this activity concerns all of the Bank's sectors and has unique characteristics differing from other sectors; this activity will be concisely described in the chapter "Recruitment of Financial Sources" rather than in each sector individually.

Attribution of the income and expenses to the activity sectors in the bank was implemented as follows:

Income from Interest, net

From the profit obtained from the provision between the credit interest provided to the sector's customers and the price of cash (economic transfer price adjusted to the linked sector and the average credit duration).

This profit includes financial expenses between the sectors – debt of the sector providing the loan and credit of the sector raises the deposit in the transfer prices (the income will be increased accordingly in the sector, which raises the deposits, and on the other hand, it decreases the income for the sector using the credit).

Expenses for Credit Losses

The provision was attributed to the activity sector in which the customer's activity is classified for which the provision was implemented. In a similar way, collection from implemented provision or reduction is also attributed to the sector for which the customer's activity is classified.

Non-Interest Income

Income not from interest was directly attributed to the sector in which the customers' activity is classified.

Operating and Other Expenses

Direct identifiable expenses are specifically attributed to the activity sector. The balance of indirect or direct expenses that are not accurately identifiable, are attributed according to model by which these expenses are attributed in compliance to the relative part of the direct service in that sector of the Bank's total service to each of the activity's sectors.

Taxes on Income

Taxes are calculated according to the effective tax rate and attributed accordingly to each sector.

Yield on Capital

The allocated capital for the yield calculation to capital in each of the activity sectors is based on the average risk assets in each sector. Calculation of the yield for each sector was made according to the equity, as aforementioned, that is attributed to the sector.

Investment in The Capital of The Banking Corporation and Transactions of Its Shares

Equity

As at December 31, 2012, the Bank's equity totaled NIS 694 million, compared to NIS 645 million at the end of 2011.

Most of the increase in earnings is attributed to the Bank's earnings over the past three months the sum of NIS 36.1 million; to the adjustments for presentation of available for sale securities based on a fair value of NIS 12.7 million; and an increase of NIS 0.7 million that is attributed to the issuance of options to the Bank's CEO (For more information, see Note 22a of the Financial Statements).

As at December 31, 2012, the balance of deferred liability notes issued to the public, deferred deposits raised from households, and institutional customers, which were included in the capital for the purpose of calculating the ratio of capital to risk components, totaled NIS 337 million, compared to NIS 319 million at the end of 2011.

For data concerning decrease in value of debentures available for sale (government and corporate) recorded to capital reserve by period of time, and the rate of impairment, please see data in the Financial Management Sector.

For details concerning changes in equity, see the "Statement of Changes in Equity" in the Financial Statement.

Concerning the capital objectives under the Basel II instructions, please see the "Risk and Risk Management" chapter.

The Bank examines its capital needs under the Bank's annual work plan, in accordance with Bank of Israel directives concerning implementation of the Basel III instructions, and according to current business developments The Bank cannot assess the types of capital instruments that will develop in accordance with the Bank of Israel instructions. On December 24, 2012 the Bank issued deferred liability notes totaling NIS 71,761 million through a subsidiary.

Dividend Distribution

In 2012, the Bank did not distribute dividends.

On March 31, 2011, it was decided to pay dividends to the Bank's shareholders totaling NIS 25 million, namely, NIS 0.35 per ordinary share of NIS 1 n.v. The date for determining dividend distribution was April 12, 2011, the X-Day was April 13, 2011, and the actual date of payment was April 27, 2011.

On February 27, 2011, it was decided to approve stage A of the Bank's Strategic Plan. Among the Plan's objectives is striving to create higher and continuous value for the Bank's shareholders, including continuous annual dividend distributions in the range of 25%-40% of the net profit during the coming years. Nevertheless, the considerations for distribution of dividend and the actual distribution, if there will be one, will be affected by the requirement to comply with the updated capital objective as determined by the Board of Directors (see below the sub-chapter "Capital Adequacy" in the "Risks and Risk Management" chapter), and subject to the instructions of the Supervisor of Banks, as are determined from time to time.

The aforementioned information concerning the distribution of dividend is forward-looking information, that may not be realized in whole or in part, or that may be realized differently from expectations. This information is based on the assessments and various forecasts presented to the Bank's Board of Directors. This information may not be realized because of changes that may occur because of various factors that are not solely controlled by the Bank. The influencing factors include forecasts and assessments concerning changes in the situation of the economic situation, legislation, instructions from supervising factors and others, and changes in the Bank's Strategic Plans and work plan.

The dividend distribution is implemented subject to the instructions of the Corporate Law, 5759 – 1999 and instructions of Proper Banking Management number 331, which discusses dividend distribution by banking corporations. On June 30, 2010, the Supervisor of Banks notified the banks that in addition to the Proper Banking Management instruction № 331, a bank that fails to comply with the capital objective of 7.5% or whose dividend distribution will not cause it to meet the objective is not allowed to distribute dividends, except after obtaining the Supervisor of Banks' approval.

Nothing stated above concerning the distribution of dividend creates any liabilities towards any third party (including on the issue of payment dates and/or rates of dividend).

Part Two – Other Information

Financial information concerning the banking corporation's activity sectors

Details of the banks activity according to sectors are presented in Note 30 in the Financial Statements. Developments that took place in activity sectors are presented below in the descriptive part of the corporation's business by activity sectors. Activity and other expenses related to the activity sector resulting from transactions between sectors, are not recorded in the Bank's activity sectors.

Material Developments in the Business Environment

General

In 2012, the Israeli market grew by 3.3% (according to preliminary estimates of the Central Bureau of Statistics). Throughout 2012, the growth rate suffered a slowdown, when in the second half of the year, according to Bank of Israel estimates, growth is expected to be less than 3%. The main factor underlying the growth slowdown is the decrease in exports due to global circumstances. During the last quarter of 2012, export of goods decreased by more than 3% in contrast with the previous quarter. Furthermore, the growth rate in private consumption and in investments has moderate. The Procurement Managers Index for December 2012 indicated shrinking industrial activity for the seventh consecutive month. A similar trend can be seen in the review of business trends issued by the Central Bureau of Statistics, in which the balance sheet of total business activity in the fourth quarter of 2012 was at the lowest level since the start of the review.

The unemployment rate in Israel remains stable, at 6.9% in 2012. The number of people employed in 2012 increased by 3.5%, most of whom were employed in the public sector: education and health services.

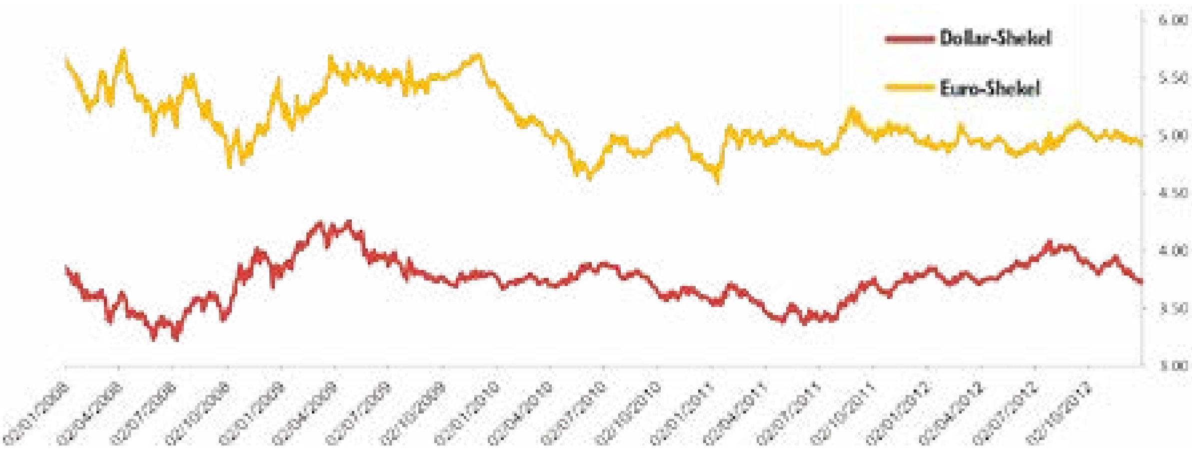
The global economy also recorded a slowdown in annual growth rate in 2012 to 3.3%. The slowdown was recorded due to a recession in Europe, a slowdown in growth of awakening markets, and in contrast improvement in the US economy. The industrialized economies grew at a limited rate of 1.3%. Most of the global growth could be attributed to developing economies, which grew at a rate of 5%. The debt crisis in Europe continued to be at the center of the world's attention, accompanied by high unemployment. In the United States, the crisis surrounding fiscal problems clouded economic recovery. The central banks around the world acted to encourage growth and maintained expansive monetary policies that was also made possible by low inflation, which was affected, inter alia, by a decline in the price of commercial goods.

Inflation and Exchange Rate

In 2012, the Consumer Price Index rose by 1.6%, the Index without Vegetables and Fruit increased by 1.7%, the Index without housing increased by 1.2%, and the Index without energy by 1.3%. Inflation in 2012 was relatively lower than projected despite the Bank of Israels expansive monetary policies. In contrast, the government's measures such as expansion of Free Mandatory Education Law from the age of three and the reform in the cellular market led to a decline in prices. The main contributing factor to inflation in 2012 was housing and energy prices, which rose by 3.3% and 6.5%, respectively.

Inflation forecast for 2013, according to analysts' expectations and projections based on futures contracts of banks, is projected to be between 1.8%-1.9%.

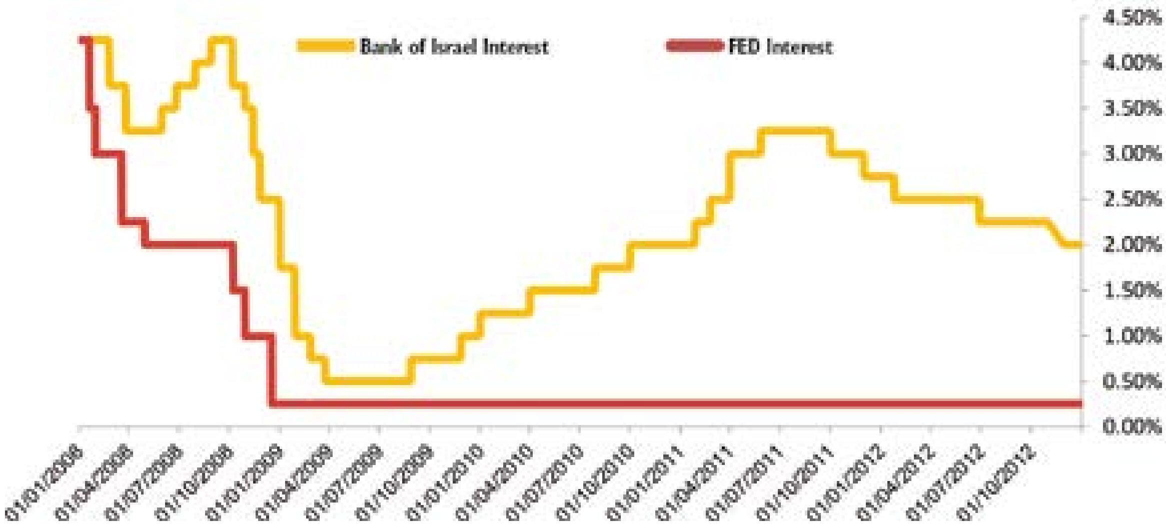
In 2012, the dollar exchange rate dropped by 2.3%, and during the first eight months of the year, rose by 5.4% but subsequently dropped by 7.3%. Among the explanations for the latest decline in the dollar rate are the dissipating concerns of a strike on Iran and expectations of a change in Israel's payment balance with the start of the flow of natural gas in 2013. The Euro exchange rate dropped by 0.4%.



The Fiscal and Monetary Policy

In 2012, the Bank of Israel interest gradually declined from 2.75% at the start of the year, to 1.75% in January 2013. The decisions to lower the Bank of Israel's interest rates came in light of the need for additional support for economic activity and the lack of inflationary pressures, as noted in the notices on the Bank's interest rate decisions. The market expects Bank of Israel interest rates at the end of 2013 to be between 1.6%-1.7%.

The total government deficit for 2012 totaled approximately NIS 39 billion, or 4.2% of the product, in comparison with 3.4% that was projected at the start of 2012. The deviation is attributed to revenue that was lower by NIS 6.9 billion (of which revenue from taxes was lower by NIS 3 billion than forecasts) and expense higher by NIS 2.2 billion than the original budget.



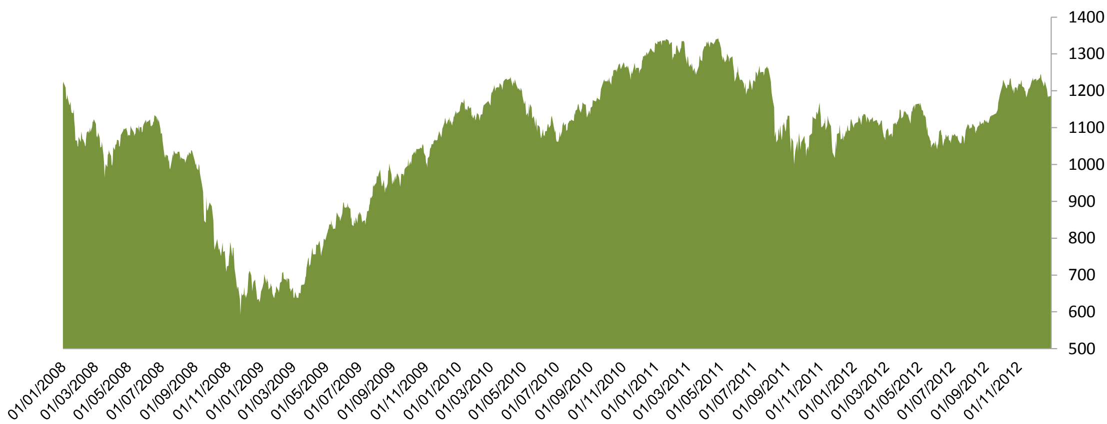
The Capital and Monetary Markets

Israel's stock market was characterized by tremendous fluctuations in 2012, with the year ending with a positive yield in the main shares indexes. Another prominent trend in 2012 is shrinking trade turnover. In 2010, the average trade turnover totaled approximately NIS 2 billion per day. In 2011, this number declined to NIS 1.5 billion per day, and in 2012, daily trade volume stood at only about NIS 1 billion.

Israel's debenture market was characterized by increases in rates in all debenture indexes, government and concern. The low inflation environment and the drop in Bank of Israel interest rates in the year contributed to this trend.

In 2012, the TA-25 and the TA100 rose by 9.4% and 7.2% respectively. The government debenture index in 2012 rose by 7.2%.

Tel Aviv 25 Index



The Construction Sector

In 2012, 21,517 new apartments were sold in Israel – an 11% increase in comparison with 2011. Despite the trend data, the consecutive increase recorded in new apartment sales between October 2011 until September 2012 (approximately an average of 2.4% per month) became moderate, and since October 2012, an average 0.5% decline per month has been recorded.

By district-based sectoration, an increase was recorded during 2012 in the number of new apartments sold, in comparison with 2012: in the Jerusalem district – approximately 49%, in the northern district – approximately 35%, in the southern district – approximately 12% and in the central district – approximately 6%. In contrast, an 8% decline was recorded in the Tel-Aviv district.

The number of new apartments remaining for sale at the end of December 2012 is estimated at 20,400 apartments – a 2.7% decline in comparison with the end of 2011. The number of supply months in accordance with the average number of new apartments sold between October-December 2012 was at the end of December 2012, for 11 months.

The Automotive Sector

In 2012, approximately 205 thousand new vehicles were sold, a 9.3% decline in contrast with 2011. In December 2012, 10 thousand vehicles were delivered – the lowest monthly number in 2012.

Accounting Policies on Critical Issues

The Bank's Financial Statements are prepared in accordance with generally accepted accounting principles in Israel (Israeli GAAP), and according to the instructions by the Supervisor of Banks and the guidelines concerning preparing a bank's Financial Statement. The principle accounting policies are specified in note № 2 of the Financial Statements. Implementation of the accounting policies by the Bank's management when preparing the Financial Statements involves assumptions, estimates and forecasts, which affect the Bank's reported amounts of assets and liabilities (including contingent liabilities) and its reported business results. Utilization of estimates involves extensive uncertainties and changes, which may significantly affect results presented in the Financial Statements. Part of the assessments and estimates are critical for the financial situation and the activity results reflected by the Financial Statements because of the subject's essence, complex calculations, or the planning level of realization of events for which an uncertainty exists. These forecasts are important and are called "critical subjects". A possibility exists that future realization of estimates and forecasts will differ from their presentation in the Financial Statements.

Provision for Credit Losses

The bank determines provisions for credit losses on loans against mortgage of a residential housing according to the depth of arrears as determined in Appropriate Banking Management Instructions № 314 of the Supervisor of Banks. In addition, conforming to the Supervisor of Banks' guidelines, the group provision for credit losses of 0.75% is calculated for housing loans balance provided as of the beginning of 2009 and onwards, while the ratio between debt and the mortgaged asset value at the time of provided loan, (LTV) is greater than 60%.

With the other retail credit, as well as business credit, the Bank determined that its provisions conform to the Supervisor of Banks' circular: "The measurement and disclosure of defective debts, credit risks, and provision for credit losses," as published on December 31, 2007. The circular is based, among others, on American Accounting Standards and on regulatory instructions of supervision institutions of banks, and on the American SEC (Securities and Exchange Commission}. This instruction is implemented in the Financial Statements of banking corporations and credit card companies as of January 1, 2011 (by original instruction – from January 2010). The instruction is not to be implemented retroactively in Financial Statements from previous periods. This influence of this circular on the Bank is expressed in the following subjects:

Detailed examination – The Bank recognizes the necessity of detailed examination of each borrower (except for housing loans) whose contract balance is NIS 1 million or more, as well as other debts identified by the Bank (such as fraud and bankruptcy). Each borrower that has been individually examined, and concerning him there are signs of probable problems in repayment capability for the credit provided; the Bank will assess the collectible amount from this borrower according to the expected cash flow from his business activity, realization value of his assets, third-party guarantees, and realization date. Since this information is based on estimates and forecasts, there is no certainty that the actual amounts received will be identical to the forecast. Concerning fraud and bankruptcies

– these debts are immediately written off. Concerning the other debts that are individually examined – impairments are written off no later than two years from the date of the individual provision.

Debt classification – Five main classifications were determined, creating hierarchy in severity problem of the debt, and determining provisions for it: Proper debt, debt under special supervision, inferior debt, defective debt, and debt that does not accumulate interest.

Provision for credit losses – A distinction is made between provision on individual basis for debts that have been examined individually and identified as damaged, and between group provision for all debts that are not classified as defective. The group provision rates for credit losses of balance sheets and off-balance sheets based on historical loss rates in the various market branches (some from retail credit based on sector historical loss rates in various activity sectors) as divided between non-problematic credit and problematic credit between 2008 and 2012, as well as for actual recorded net write-offs rates. Conforming to the Supervisor of Banks' transitional order, the validation and update of these provision rates will be implemented quarterly.

Write-offs – for debts that have been examined individually and are recognized as non-collectible debts. The Bank's policy is to write-off all specific provisions whose duration exceeds two years. Furthermore, write-offs are implemented on debts for which group provisions have been made and are passed due for more than 150 days. Furthermore, the bank's policy is to write-off housing loan debts that were provided for loss but as a result of collection proceedings, there are no collateral balance to realize the debt against it.

The group provision for credit losses due to non-defective credit risks, cancels the additional and general provision because of problematic debts and risk characteristics determined by the Supervisor of Banks' instructions. Among the included risk characteristics: debt classification, credit to individuals linked to the bank, lack of borrower financial data, credit to a borrower or to a group of borrowers deviating from the liability limitations of an "individual borrower". In 2011, in conformity conformity with Supervisor of Banks' instructions, the Bank continued to calculate the additional gross provision from taxes for the purpose of comparison for group credit losses provision, while the provision recorded in the balance sheet is the higher one of the two.

In general, the implementation of the instruction on the subject "Measurement of Defective Debts Provisions for Credit Losses" that has been implemented as of January 1, 2011, brought a material change in the examination and classification method for debts, as well as a method for calculating the provisions for credit losses and performing write-offs. In the Profit and Loss Statement for the year 2012, one can notice that the expenses for credit losses were NIS 36.0 million in contrast with NSI 15.1 million in 2011, while in note 30 of the Financial Statements (on the subject of activity sectors) one can notice that the increase resulted mainly from credit provided to household sector that was mostly included in the provision on a group basis, as well asfrom the update of group provision percentage in accordance with Bank of Israel directives. The increase in this sector is also explained by the Bank's strategy to expand retail credit performances.

For additional details concerning the quantitative influence, please see note 5 of the Financial Statements and appendix E on Management Review.

Deferred Taxes

Deferred taxes are calculated for temporary differences between the value of assets and liabilities in the financial reports, and the amounts taken into consideration for tax purposes. Deferred taxes are calculated according to tax rates expected to be applicable when such taxes are imputed to Profit and Loss, as such rates are known near the approval date of the financial reports. Deferred taxes receivable are calculated for temporary differences for which a tax saving is expected to be created as of the reversal date.

At the time the deferred taxes are entered, the bank utilizes estimates and forecasts concerning the possibility of future realization of deferred taxes receivable.

For information on quantitative effect – please see Note 29 of the Financial Statements.

Derivative instruments

In conformity with the Supervisor of Banks' instructions, the derivative instruments at the Bank are presented in the balance sheet according to fair value. The fair value of the derivatives is determined according to quoted market prices in active markets or by estimated fair value that is determined according to prices of similar assets or similar liabilities (Mark to model). The estimation method includes various parameter; e.g., interest curves, currency exchange rates, and standard deviations. The estimate includes considering assumptions concerning various factors such as the other party's credit risk for transactions and its liquidity. There are no instances in which the revaluation of the derivatives and fair value were not established based on the model but based on price quotes received from third parties.

For information on quantitative affect – please see Note 20 of the Financial Statements.

Measurement of Fair Value of Financial Instruments

On December 31, 2009, the Supervisor of Banks published a circular applying Standard ASC 820-10 FAS 157, concerning fair value measurement, on the banking system. Under implementation of this standard, the Bank uses appraisal techniques that utilizes to the maximum the observed relevant data, and minimizes the use of unobserved data. Observed data is data reflecting the assumptions that market participants would use for pricing the assets of liabilities, developed based on market data presented from resources that are independent of the Bank. The unobserved data is data reflecting the assumptions of the Bank itself concerning assumptions that market participants would use for pricing the assets or liabilities, developed based on the best data available under these circumstances.

Measuring the fair value is based on the assumption that the transaction will take place in the principal market for that asset or liability, or for lack of principal market, at the most useful one.

The Bank classifies fair value while using a fair value hierarchy reflecting the significance of the data used for implementing the measurement. Hierarchy of fair value consists of the following levels:

Level 1 - Measurement based on quoted prices (unadjusted) in active markets for identical assets or liabilities. Quoted prices in active markets are the most reliable evidence for fair value, and are used as fair value measurement so long as they are available.

Level 2 - Measurement based on observed data for the asset or liability, directly or indirectly, that are not quoted prices, including: quoted prices for similar assets and liabilities in active markets; quoted prices for similar or identical assets or liabilities in non-active markets; data derived mainly from observed market data, or supported by observed market data through correlation or other means.

Level 3 - Measurement based on data concerning assets or liabilities that are not based on market data may be observed and are significant for measuring the overall fair value.

This hierarchy requires that the Bank use observed market data, when this information exists. Whenever possible, the Bank considers observed and relevant market data within the confines of its assessment. The scope and frequency of transactions, the margin and reconciliation required when comparing similar transactions are factors that are taken into account when determining the relevance of prices observed in those markets.

Establishment of the fair value of financial instruments that belong to Tier 2 and Tier 3 are based on the assessment and assumptions that rely on, inter alia, subjective discretion.

In general, the Bank has negligible balances that rely on inactive market data, and in any case, the measurement is reasonably and adequately reviewed by external experts and appraisers.

The Bank acted to implement Standard ASC 820-10 in 2011, according the Bank of Israel's directives. However, there was no material change in the method for measuring fair value and in forecasts on which they were based prior to the implementation of this standard.

For additional details concerning the quantitative effect for implementing the measurement of fair value – please see Note 21 of the Financial Statement and Appendix D in the Management Review.

Impairment of securities that is not of temporary nature

Changes in fair value of securities available for sale are imputed to equity after deducting the tax influence, unless a non-temporary decrease is evident. In such circumstances, the impairment is included in the Profit and Loss report.

Periodically the bank examines the need to record a provision for an impairment that is not of a temporary nature. The bank has defined criteria for tracking securities and the aforementioned examination. These criteria are based, among others, on the following factors:

- Change in classification of securities by classification agencies.
- The length of time during which the security is traded at high yield.
- Exceptional cases such as irregular impairment.

In addition, criteria were set for implementation of the provision for impairment because of impairment that is not of a temporary nature pursuant to two accrued conditions:

1. A 40% decline in the value of the security in contrast with the depreciated cost.
2. Decrease for nine consecutive months.These criteria are discussed by the directors' credit committee and approved by it, and are reported to the Supervisor of Banks at the Bank of Israel.

During 2012, the Bank performed a provision for impairment that was not temporary for the amount of NIS 1.5 million (in 2011, no provision for impairment was provided)

Contingent Liabilities

The Bank is a party in legal processes filed against the Bank by its customers, former customers, and other third parties who considered themselves injured or damaged by the Bank's activity. Estimation of the risk inherent in legal processes is based on the opinion of the Bank's internal lawyers or on the opinion of external legal advisers, which is examined by the Bank's internal lawyers. Such estimates are based on the best judgment of the relevant legal advisers, taking into consideration the stage of the legal proceedings and accumulated legal experience in various issues in Israel.

Estimates concerning chances of class actions involves greater difficulty because of the minimum accumulated legal experience concerning the realization of such claims in Israel. Moreover, chances of certain class actions cannot be estimated because of the stage of the proceedings they are at.

It should be taken into consideration that results of legal proceedings may differ from the determined estimate because in certain legal sectors it is not possible give such estimations.

For additional information concerning the contingent liabilities - please see note 19 of the Financial Statements.

Part three - Description of The Banking Corporation's Business Activities by Activity Sectors:

Below is a summary of average balances of assets and liabilities according to the activity sector:

	Assets			Liabilities		
	2012	2011	Change	2012	2011	Change
Sectors	Millions of NIS		%	Millions of NIS		%
Households	7,028.7	6,608.9	6	6,292.4	5,505.7	14
Private Banking	1,192.6	982.7	21	1,119.7	835.0	34
Business	1,311.9	1,165.8	13	3,405.1	3,728.9	(9)
Financial Management	1,955.2	2,015.8	(10)	70.2	81.2	(14)
Total	11,488.4	10,773.2	7	10,887.4	10,150.8	7

Below are detailed the profits from regular activities, and profit yield from regular activities on capital by activity sectors:

	Net Profit		Yield on Capital	
	2012	2011	2012	2011
Sectors	Millions of NIS		%	
Households	3.7	14.2	1.0	4.3
Private Banking	2.8	3.9	4.3	7.4
Business	15.0	14.0	10.2	7.4
Financial Management	14.6	(7.4)	30.1	(19.8)
Total (not including non-allocated amounts)	36.1	24.7	5.4	4.0

During 2012, the net profit from household and private banking sectors declined, and on the other hand, an increase in profitability was recorded for the business sector and financial management sector. For details, please see profitability data for each sector.

Household Sector

General

In the household sector, the Bank provides a variety of services and financial products. The main products that the Bank provides to its customers under this activity sector are: current account, deposits and savings, current frameworks, consumer loans and credit cards, loans for purchasing residential housing and for vehicles, loans for any purpose, and activities in the capital market in securities and investment consultation.

Most of the Bank's customers belonging to this activity sector, receive banking services from the Bank through its branches.

Objectives and Business Strategy

One of the main objectives placed at the basis of the strategic plans of the Bank (as described above), is development and expansion of the household sector, while materially increasing the customer volume of this sector, and simultaneously expanding the range of services and products that are offered to this sector's customers, and increase the embedded profitability. The Bank has the intention to offer products in this activity area that include unique characteristics embodying added value compared to products currently existing in the Israeli banking system.

Below are the Bank's principles for the Strategic Plan in this activity sector:

— Significant increase in existing customer base through:

- Expanding branch activity and opening new branches.

- Increase in the number of customers who manage their current account in the Bank (activity that began in October 2012).

- Increasing recruitment of deposits from households, through the Bank's branches, Internet, and cooperating with retail partners (such as the Postal Bank).

- Providing consumer credit to existing and new customers, and additionally by marketing credit cards and cooperating with retail partners.

- Developing unique mortgages adjusted to the customer's needs and personal preferences, while focusing on channels with high profitability.

— Increasing marketing and sales efforts, including by means of continuous improvement of customer service level; among others, by:

- Continued expansion of the telephone call center that was established at the end of 2011, expanded in 2012, and is designed to provide a solution for most banking services.

- Integrating a CRM system and upgrading the Internet website while turning it into a site enabling implementing transactions.

- Operating an advanced credit underwriting system as a supporting decision tool, allowing for quick and proper customer service.

The Bank’s plans and assessments, as specified above, are forward-looking information, and are based on assumptions and on various forecasts presented to the Bank. This information may not be realized because of changes that may be applied for various factors that are not controlled by the Bank only. Influencing factors include forecasts and assessment concerning economic development in Israel and globally, especially concerning the economic situation, including the influence of macro-economic and geopolitical conditions, changes in capital markets, as well as other additional factors influencing risk exposure: public preference, instruction by supervisory factors and others, aspects related to the Bank's image, technological developments and the subject of human resources.

Structure of the Activity Sector

Below is a description of the products and main services offered under this activity sector:

Mortgages:

- Providing loans for housing against a lien on the residential housing for individual Israeli residents and for buyers groups for long periods, based on different linkages and according to a variety of interest tracks determined by the type of loan, customer preferences, and borrower’s repayment capability.

- The activity in the mortgages area includes also providing services related to life insurance and property insurance through the mortgage, provided they conform with the Supervisor of Insurance and the Supervisor of Banks’ instruction by means of: Ir Shalem Insurance Agency (1996) Ltd., the Bank's wholly owned and controlled subsidiary (hereinafter: "Ir Shalem").

Banking and Finance:

- Full current account management.

- Providing fixed-time credit for single-name household consumers for households.

- Mobilization of deposits and savings from households.

- Issuing credit cards to Bank costumers.

- Credit facilities and activity for checking accounts determined by the customer’s requirements and income level.

- Assistance in financing vehicle purchase – The activity in this area is implemented, among others, cooperating with companies and car lots for second-hand car sales.

- Providing credit for fixed-time against collateral.

The Capital Market:

- Providing services for securities – Implementing purchases, sales, operating in securities transactions, in derivatives at the Bank's branches in Israel and abroad.

- Investment consultancy – Providing securities consultancy to customers at all of the bank's branches through authorized consultants.

- Investment Portfolio Management – managing financial assets for customers through Jerusalem Management Portfolios Ltd., the Bank's fully owned subsidiary (hereinafter: "Jerusalem Management Portfolios Ltd."). On January 7, 2013, Jerusalem Investment Portfolio Management sold its portfolio management activity and from the date of completion of the transaction, the Bank (through its subsidiary) will not manage the portfolios (See Chapter on Events after the Balance Sheet Date above).

Legislative restrictions, standard, guidelines and circulars from the Supervisor of Banks, and special constraints

The Bank in general, and the household sector in particular, operates within the framework of laws, standards, regulatory guidelines and instructions imposed on the banks by legislative and supervising entities, including the Supervisor of Banks, the Securities Authority, and the Commissioner for the Capital Market, Insurance and Savings at the Ministry of Finance.

Below are details concerning updated and proposed legislation on matters concerning providing banking services to households:

Memorandum from the Supervisor of Banks on the subject of housing loans at variable interest

On May 3, 2011, the Supervisor of Banks issued a letter to the banks in which was mentioned that, due to the continuing increase of loan performances at variable interest and the possible implications on this issue of increase in the market's interest rate, the banks are required to approve and provide housing loans only if the ratio between the "housing loan at variable interest" part and between the total "housing loan" part will not be higher than 33.3%. The banks are allowed not to impose the aforementioned limitation on housing loans in foreign currency for foreign residents, on bridging loans and on loans for any purpose in small amounts, and only if the ratio between the total housing loan at variable interest and between the total housing loan, that have been provided during calendar quarters, is not higher than 33.3%. Moreover, the banks are required to bring to the attention of the existing borrowers whose loan does not meet the above mentioned determined relation, the embedded risk in the composition of the loan, including an example for illustration. Concerning the housing loans for which in principle approval is applied, the letter is effective as of May 5, 2011.

As result of the above described limitation a change was applied on the customers' credit implementation mix.

The Bank received relief from the Bank of Israel according to which it is allowed to impose the aforementioned limitation of the aforementioned loans (foreign currency loans, bridging loans and loans for all purpose) and only if the ratio will not be higher than 40% (in contrast to the aforementioned 33.3% rate). The aforementioned relief is valid until June 30, 2014. In the event that the Bank of Israel will not extend the validity of the relief provided to the Bank, the Bank will adjust the customers' credit implementation so that it complies with the original limitation without this relief. By the Bank's assessment, not extending the relief will probably materially influence the Bank's revenue derived from providing housing loans.

On November 1, 2012, the Supervisor of Banks issued a letter to banks that stated that due to the significant increase in housing prices in recent years, some of which can be attributed to investor activities that was intensified by housing loans at high financing rates, limitations were imposed on the percentage of financing that a banking corporation may approve. The directive set forth that a banking corporation may not approve or perform a housing loan at a financing rate (LTV) that exceeds the following percentages:

— Housing loan for purchase of the right to land for a single apartment – 75%.

— Housing loan for purchase of the right to land for an investment apartment – 50%.

— Housing loan that is not included in the aforementioned sections – 70%.

The stipulation in the directive will apply to housing loans that were approved in principle beginning on November 1, 2012.

The Bank believes that the directive will not materially affect bank performances.

The Bank's assessments, as specified above, are future facing information, as well as based upon assumptions and different forecasts. This information may not be realized because of changes that may be applied for various factors that are not controlled by the Bank only. Influencing factors include forecasts and assessment concerning economic developments in Israel and around the world, especially concerning the economic situation in the market, such as a sharp decline in demand to purchase housing for residential and/or investment purposes, including effect of macro-economic conditions, as well as other additional factors that affect exposure to risks and instructions of supervising factors and others.

On February 19, 2013, in light of the banking system's accelerated growth in residential credit in recent years (a 76% increase over the past five years), in parallel with an increase in housing prices, the Supervisor of Banks published a draft directive concerning housing credit and real estate, on the allocation of capital, provision for doubtful debts for housing loans, and change in the scale of the risk weight guarantee in accordance with the Sales Law.

Listed below are the main guidelines that were included in the new Draft:

a. In accordance with the new Draft directive, capital for housing loans will be allocated based on the following weighted rates:

   - Housing loans in which the financing rate is up to 45% will be weighted at 35% – remains unchanged.

   - Housing loans whose financing rate is higher than 45% and up to 60%, will be weighted at 50% instead of 35%.

   - Housing loans whose financing rate is higher than 60% will be weighted at 75% for capital requirement purposes instead of 35% or at 100% (see the following point).

   - Simultaneously, the requirement (from October 2010) to weight 100% loans whose financing rate exceeds 60% and for a sum exceeding NIS 800 thousand and whose variable interest rate exceeds 25%, will be replaced, as previously mentioned, by a weighted rate of 75%.

b. The Draft directives set forth a requirement to increase the provision for doubtful debts for housing loans – so that the ratio between the balance of the group provision and the balance of the housing loan will be at a minimal rate of 0.35%. On average, at the end of third quarter of 2012, this ratio stood at 0.22%.

c. In addition, the Draft directives establish a reduction in the allocation of capital required for Sales Law guarantees in the event that the apartment had already been delivered to the tenant. These guarantees will be weighted with a credit conversion coefficient of 10% instead of 20%. This move constitutes a relief in the capital allocation requirements and may increase the supply of bank credit in the construction and real estate industry.

The purpose of the directives is to increase the capital cushions and provision required for increased risks embodied in the housing credit portfolio. Correspondingly, the move eases the capital requirements for the Sales Law guarantees after delivery of the apartment to the tenant, due to a relatively low level of risk they entail.

The new directives will take effect beginning on January 1, 2013. The immediate affect will be increased provision for credit losses for debts that were reviewed on a group basis of NIS 17-20 million gross before tax (a 0.2% decrease in the Tier 1 capital ratio (for risk components). In relation to the long-term effect, the bank is examining the effect of the instruction on the housing credit component, as well as on its future profitability.

Changes in the Sector's Activity Markets in Customer Characteristics

After the last quarter of 2011, banking system activity, and particularly the Bank's, activity, declined in the mortgage area that was primarily attributed to the Bank of Israel's limitations for providing housing loans with variable interest and of the social protests that influenced, inter alia, the demand for housing acquisitions, the scope of activity in this area returned to their average levels prior to said decline.

The Supervisor of Banks directive on limiting the financing percentage in housing loans as of November 1, 2012 did not materially affect the scope of activity in the mortgage area, while apartment demand in the sector did not significantly decline. It should be noted that since publication of said directive, only several months passed that were needed to continue monitoring the impact of the directive, if any, on the mortgage industry.

During 2012, there were no changes in the characteristics of the Bank's customers in this activity sector.

Critical Success Factors in the Activity Sector and Their Applied Changes

- Building a variety of products adjusted to the needs of the existing and potential costumers that will have innovative and unique characteristics.

- The Bank uses its knowledge and extensive experience accumulated in the mortgage sector to help it understand the various relevant variables that affect real estate values used as collateral against loans provided to customers; high capability of credit underwriting, and high profitability channels.

- Exposure and availability of the distribution array (branches) across the country.

- Intensive marketing activity, inter alia, through cooperation, which helps reach main centers where vehicles are sold. This is in combination with fast response capability for integrating a flexible financing plan, adjusted to the marketing plans and requirements of importers and/or vehicle sales lots, on the one one hand, and the needs of potential customers on the other.

- Providing professional and reliable service to Bank customers, providing a solution to their needs and personal preferences.

- Expanding the Bank's existing customer base in this activity area, as well as expanding the variety of products and services offered to this sector's customers.

- Flexibility and sensitivity to changes taking place in the market, including high response capability and access to new activity areas.

- Developing systems and computerized infrastructure that will enable to provide various and advanced products for the Bank's customers while maintaining low-risk levels.

The Main Entry and Exit Barriers of the Sector's Activity

The sector's entry barriers include human capital in service that is professional and experienced, customer habits, advanced computer systems and their maintenance, and minimum capital requirements. Entry barriers for the area of credit provision for second-hand cars are credit price, the ability to quickly close a credit transaction resulting from a competition-saturated market to quickly provide finance services by non-bank companies, and subsidized finance transactions with the large banks.

Moreover, the exit from mortgages area falls within a range of years, because of the long life of the loans, granted for a period of up to 30 years. Or, alternatively, sales of a mortgage portfolio to another financial institute.

Alternatives to Products and Services of the Activity Sector of and Occurring Changes

Alternative to products and services offered by the Bank to the sector's customers, are the same services and products offered by the non-banking system, including providing loans for vehicle acquisitions also offered by various leasing companies and capital market services, and also provided by investment houses having an Internet trade platform. As for the consumer credit, more financial non-banking entities and institutional entities (credit card and insurance companies) can be seen turning to relevant population sectors with credit provision offers. In addition, the food retail chains in cooperation with credit card companies issue credit cards for customer, not by means of the banking system.

Competition in the Activity Sector

- In current accounts, the competition is increasing. After years in which only medium-sized banks competed with the large banks, recent years have also witnessed increased competition by small banks. The small banks offer household current accounts that are attractive in terms of fees and financial margin and therefore try to compensate for their shortages in retail coverage.

- In recent years, there has been aggressive competition between the banks over the mortgage market. According to the Financial Statements by the banks over the last years – the four large banks have a market share of over 85% of the industry's total mortgage implementation. The other banks and insurance companies operating in this field share the remainder part. In the Bank's assessment, its share in the mortgage market is about 2%. In general, it should be mentioned that mortgage products offered by various banks are similar and therefore the competition focuses on the quality of the service, financing rate, credit prices, and fees paid by customers.

- The Bank deals with competition in the mortgage field through its expertise in examining collateral and the high and fast service level granted to customers even for complicated transactions.

- In the field of related mortgage services, banks face additional competition from insurance companies that offer bank customers their life and property insurance policies.

- In the finance sector credit for vehicles purchase, most the financing credit in previous years was granted by financing by non-bank companies. During the past years, with the entry of the large banks into the area, the profitability in financing new vehicles has been reduced, and with the purpose to strengthen the loyalty of its customers, the banks (including the Bank) lowered prices, and in subsidizing campaigns with various importers.

- Nevertheless, in the finance market for acquisition of second-hand vehicles, significant presence of the large banks is still not felt and the competition level is still low. This enables the Bank to finance acquisition of second-hand vehicles with higher margins in relation to the area of new-car acquisition. The competitors in this area are credit-card companies who established mutual ventures in the vehicle area and non-banking financing companies such as: "Pama," "Direct Financing," and "Clal Financing" providing financing services enabling the customer to complete the acquisition and a method of financing in one place.

- In addition to competition among the banks, the credit card and consumer credit sector, accelerated effort by the credit card companies in cooperation with retail and other chains is felt in households by issuing credit cards directly to the customer without bank intervention, including granting credit.

- The capital market is characterized by fierce competition between banking factors, private brokers and institutional entities. A large number of players is active in the sector and the strength of the large banks plays a very significant part. As a result of the Bachar Committee, many customers now manage their capital market activity through institutional entities and investment houses, which try to attract customers for all their capital market activities. Competition in this area focuses mainly on long hours of service, advanced Internet platforms, and competitive prices.

Customers

The sector's customers are private customers, households, and Israeli residents. The Bank's proposed value in current accounts appeals to all sectors and all socioeconomic classes. Sector activity is characterized by tremendous spread of customers. In terms of credit, it should be noted that the focus on households while the credit provided to each of them is at a relatively low volume, and therefore the Bank is not significantly dependent on an individual customer or a limited number of customers while their loss may significantly influence the activity sector. Moreover, this sector has a great deal of weight in the Bank's recruitment of resources in various channels.

Out of 18 branches, 3 of the Bank's branches are located in areas characterized by a population of mostly Ultra-Orthodox and 2 in areas with a mostly Arab population.

Marketing and Distribution

The Bank's marketing activity in the household sector is based on a distribution array of bank branches, direct banking (Internet and call center), and direct mailing to customers. From time to time, the Bank holds advertisement campaigns through various media.

In financing credit area for vehicle purchasing, the bank also operates by cooperating with importers, car agencies and vehicle sale lots, which have mutual advertisement campaigns with the bank for customers to purchase vehicles with financing provided by the bank.

The Bank is not dependent on the marketing and distribution channels in the framework of this activity sector.

Human Capital

In 2012, the average number of direct positions in the sector totaled 189 positions vs. 163 positions in 2011.

In the mortgage field -an average of 61 positions vs. 59 in 2011. In the banking and financing area – an average of 102 positions vs. 76; in 2011, 34 – a 34% increase primarily due to expansion of retail activity. In the capital market field – an average of 26 positions vs. 28 in 2011. Moreover, head office and management personnel were loaded onto this sector.

Below is a summary of the operating results of the household sector:

	For the year ending December 31, 2012				For the year ending on December 31, 2011*			
	Mortgages	Banking and Finance	Capital market	Total	Mortgages	Banking and Finance	Capital market	Total
	Millions of NIS							
Income from Interest, net								
From externals	107.7	80.3	-	**188.0**	102.6	59.0	-	161.6
Inter-sectorial	(6.6)	(8.0)	-	**(14.6)**	(10.2)	(10.5)	-	(20.7)
Total Income from Interest, net	101.1	72.3	-	**173.4**	92.4	48.5	-	140.9
Income that is not from External Interest	40.9	7.9	8.0	**56.8**	43.6	7.4	10.8	61.8
Total Income	142.0	80.2	8.0	**230.2**	136.0	55.9	10.8	202.7
Expenses for Credit Losses	2.0	(35.4)	-	**(33.4)**	(2.8)	(17.6)	-	(20.4)
Operating and other expenses with the exception of depreciation and amortization	(58.9)	(92.0)	(26.7)	**(177.6)**	(59.9)	(63.0)	(29.7)	(152.6)
Depreciation and Amortization	(4.2)	(7.2)	(1.9)	**(13.3)**	(3.5)	(4.5)	(1.7)	(9.7)
Profit (Loss) before Taxes	80.9	(54.4)	(20.6)	**5.9**	69.8	(29.2)	(20.6)	20.0
Provision for Taxes on Profit	(26.8)	17.8	6.8	**(2.2)**	(20.0)	8.3	5.9	(5.8)
Net profit (loss)	54.1	(36.6)	(13.8)	**3.7**	49.8	(20.9)	(14.7)	14.2
Capital yield (net profit rate from equity)	16.7%	-40.4%	-	**1.0%**	18.4%	-30.1%	-	4.3%
Average balance of assets	6,059.0	969.7	-	**7,028.7**	5,818.9	790.0	-	6,608.9
Average balance of liabilities	-	6,292.4	-	**6,292.4**	-	5,505.7	-	5,505.7
Average balance of risk assets	3,428.3	951.9	-	**4,380.2**	2,834.4	718.0	-	3,552.4
Average balance of securities	-	-	1,476.0	**1,476.0**	-	-	1,539.0	1,539.0
Average balance of other assets under management	2,118.3	-	191.7	**2,310.0**	2,426.3	-	175.3	2,601.6
From margin from activity of providing credit	81.9	53.8	-	**135.7**	71.2	30.1	-	101.3
Margin from deposit receipt activity	-	17.9	-	**17.9**	-	17.7	-	17.7
Other	19.2	0.6	-	**19.8**	21.2	0.7	-	21.9
Total Income from Interest, net	101.1	72.3	-	**173.4**	92.4	48.5	-	140.9

* Reclassification.

Changes in the sector activity scope and its profitability

The revenue rate in this sector is about 67% of the Bank's total revenue, compared to 68% for 2011.

The total revenue in the sector totaled NIS 230.2 million in comparison with NIS 202.7 million; an increase of about 14% that is primarily attributed to increased revenue in the mortgage area as a result of increased margin as well as increased revenue in the banking and finance are, and as a result of a rise in the consumer credit balance.

Total expenses for credit losses totaled NIS 33.4 million, in comparison with NIS 20.4 million; a 64% increase attributed to a rise in the write-off rate in consumer credit and vehicle credit, an increase in group provision resulting from an increase in consumer credit portfolio, as well as an update of the group provision rate in accordance with Bank of Israel directives.

Total operating and other expenses totaled NIS 190.9 million, in comparison with NIS 162.3 million, an 18% increase that is primarily attributed to the lending Bank's expansion in the retail area as part of its strategic plan that is accompanied by expansion of branches, advanced telephone call center, and advertising campaigns. For more information, see the paragraph on Business Strategy and Goals.

The net profit in this sector this year totaled NIS 3.7 million, compared to NIS 14.2 million in 2011.

The majority of the profit decline is attributed to increased expenses for credit losses, and in operating and other expenses as stipulated above.

The net profit from mortgage activity in this sector amounted this year to NIS 54.1 million as compared to NIS 49.8 million in 2011. The majority of the growth in profit is attributed to increased revenue as a result of an increased margin.

Loss from banking and finance activity in this sector amounted this year to NIS 36.6 million as compared to NIS 20.9 million in 2011. The majority of the growth in loss is attributed to increased expenses due to credit losses and in other operating expenses as said above.

The loss from capital market activity in this sector this year totaled NIS 13.8 million, compared to NIS 14.7 million in 2011.

Material and Cooperative Agreements

Below are details on material and cooperative agreements in which the Bank is a relevant party for the household sector:

Agreements with Government of Israel for Granting Loans

The Bank has framework agreements with the Government of Israel to grant loans with government guarantees (including arrangement for implementing loans and their collection) to entitled Ministry of Housing borrowers. The agreements determine that the Bank is entitled to receive commissions at different rates as determined in the aforementioned agreements and participation in collection expenses. The last framework agreement was signed in July 2004, for a period of two years, and is renewed automatically for additional periods of one year each, unless either party terminates the agreement 4 months prior to its termination date.

Additionally, during May 2008, the bank signed an agreement with the Government of Israel concerning loans to entitled Ministry of Housing borrowers from the date of signing the agreement and onward. Loans that will be granted to entitled borrowers according to this agreement are mostly from bank funds and are under the bank's warranty, and only a small part from Government funds and are under the Government's warranty. The Bank is entitled to receive a subsidy from the Government for loans granted from bank funds, and commissions at various rates for loans granted from state funds. The agreement is in effect for one year and is renewed automatically for additional periods of one year each, unless either party terminates the agreement 3 months prior to its termination date.

The Bank has committed to the Bank of Israel that by providing the services according to the aforementioned agreements, it operations conform to the government's letter of instructions and that it will reimburse the State of Israel if it did not. The Bank's operations conform to the government's letter of instructions on the issue of loans for eligibles, and therefore it estimates that the indemnification commitments will not create material exposure to the Bank.

Borrowers Life Insurance Agreement

The Bank is a party in agreements from 1992 (as periodically updated) with several insurance companies, Ir Shalem Insurance Agency, and other insurance agencies. According to the agreements, the insurance companies are committed to insure the lives of the borrowers, subject to conditions determined in the agreements and in the insurance policies. The insurance companies are entitled to a premium, and the Bank and the aforementioned insurance agencies are entitled to payments from the insurance companies in accordance with their services. The bank is the policy owner and beneficiary in accordance therewith. The aforementioned agreements apply only to life insurance of borrowers made up until December 31, 2005.

Borrowers Property Insurance Agreement

On April 1, 2007 agreements were signed between the Bank, Ir Shalem, and several insurance companies, according to which the insurance companies committed to insure property mortgaged in favor of the Bank, subject to conditions determined in the agreements and in the insurance policies, and to payment of commissions to Ir Shalem. The agreements were renewed at the end of March 2012, and were extended until March 31, 2013, and will be renewed yearly. These agreements apply only to property insurance because of loans granted until December 31, 2005.

Framework Agreement – Life Assurance and Property Insurance in Respect of Housing Loans

On April 10, 2006, an agreement was signed, and effective from January 1, 2006, between Ir Shalem and an insurance company, according to which the insurer will issue life assurance and property insurance policies (including water damage), in respect of housing loans granted by the Bank to its customers, which will be marketed by Ir Shalem through a subsidiary of the insuring corporation.

Agreement with Bank Leumi of Israel Ltd.

The Bank has an agreement with Bank Leumi of Israel Ltd, ("Bank Leumi") as of November 15, 1998, according to which the Bank receives from Bank Leumi clearing services for transfers presented at the Bank and relays drawn at the Bank through Bank Leumi clearing, commission compensated as determined in the agreement.

Agreements with Credit Card Companies

As of August 8, 2002, the Bank has agreement with Israel Credit Cards Ltd. and as of February 25, 2010, with Poalim Express Ltd. These agreements reflect the relationship in the cooperating framework between the Bank and the aforementioned credit card companies, including the issue of dividing responsibility between the credit card companies and the Bank, and the commercial terms between the parties.

Private Banking Sector

General

Activity in the private banking sector provides banking services and products granted under the household sector, to customers with medium to high financial status; mainly for foreign residents. The sector's services are provided through a bank branch specializing in providing these services and products to foreign residents. Under this activity sector, greater emphasis has been made on providing personal and highly professional service.

Objectives and Business Strategy

The Bank sees this activity sector as an important tier for its business activities, and accordingly operates, among others:

- To maintain the status and reputation that the Bank has created among Jewish communities abroad.

- To expand the range of financial services and products relevant to this market sector.

The Bank's assessments, as specified above, are future facing information, as well as based upon assumptions and different forecasts presented to the Bank's Board of Directors. This information may not be realized because of changes that may be applied for various factors that are not controlled by the Bank only. Influencing factors include forecasts and assessment concerning economic development in Israel and globally, especially concerning the economic situation, including the influence of macro-economic and geopolitical conditions, changes in capital markets, as well as other additional factors influencing risk exposure: public preference, instruction by supervisory factors and others, aspects related to the Bank's image, technological developments and the subject of human resources.

Structure of the Activity Sector

In recent years, there is more and more evidence of a trend for most banks operating in Israel, in developing and promoting services and products provided by private banking services

The activity in this sector mainly consists of services and products as specified below:

Mortgages – Providing loans for financing acquisition of housing in Israel, as well as providing credit for other purposes backed by pledging other collateral.

Banking and Finance –Variety of products and services in this area including providing credit, activity in checking accounts, recruiting deposits in foreign currency and others, while the emphasis is on providing advanced professional service and adjusted to the personal and specific needs of the customer.

The capital market – Providing customer securities services, including implementing and operating transactions in securities and in derivatives in Israel and abroad; investment advice by consultants who specialize in investment areas that are relevant for foreign residents, with special expertise in markets abroad.

Legislative Restrictions, Standards and Special Constraints

In addition to the details provided on this issue in relation to the above household sector and the relevance also concerning this activity area; the provided services are also subject, in the framework of this sector, to specific limitations of the applicable laws in the various countries of the customers' residence from this sector.

In 2011, in the United States the Fatca Bill has been enacted, according to which the world's financial institutions are required to identify all their American customers and reports of these customers' transfer data to the U.S. Income Tax (IRS). In January 2013, standards regulating this issue were published and will probably go into effect at the start of 2014. As of the date of this report, the Bank is not capable of assessing the aforementioned legislative influence on its activity.

Moreover, in view of the existing enactment in the United States, the financial institutions not having a suitable American permit, are prevented from providing a variety of securities services to customers who are residents of the United States. Therefore, Bank of Jerusalem is prevented from providing securities services to its customers who are residents of the United States.

Critical Success Factors in the Activity Sector

The unique success factors include, a system of widespread connections with Jewish communities in various countries around the world, and providing professional and personal services to sector customers in private banking areas, and this in addition to success factors that are extensively detailed in the household sector and also relevant to this sector.

The Main Entry and Exit Barriers of the Sector's Activity

Customer habits, regulatory limitations, training of professional and skilled human resources and technological infrastructure may be the entry barriers to this activity sector. The exit from mortgages area falls within a range of years, because of the loans' long life.

Alternatives to Products and Services of the Sector of Activity

The majority of the products and services of the sector have no substitute, although there is competition between banking and financial institutions in Israel and around the world.

Customers

The customers of this sector are mainly foreign residents with a great attraction to the State of Israel as well as a medium to high financial status. Most of these customers are residents of the United States and Western Europe. The bank does not have significant dependency on any individual customer. Activity in this sector is characterized by dispersion of credit risk and widely spread recruitment of resources. The services are provided through the private banking branch, while most of the assets purchased in the this sector are financed by the Bank and are in the Jerusalem area.

Marketing and Distribution

Most of the marketing is implemented by a personal request from potential customers during conferences and events in which the Bank participates, as well as through request of customers by professionals involved in the aforementioned communities abroad; among them, lawyers, consultants, accountants with whom the Bank has current contacts.

Competition

All the banks compete for this market sector. The Bank cannot assess its relative part in the banking system concerning this activity area. In order to deal with the competition, the Bank invests a great deal of efforts in unique professional training of the employees for the private banking branch. Another of the Bank's advantage in this activity sector is the service level and the availability of bankers at the Bank speaking various languages and capable of creating personal contact with the sector's customers.

Human Capital

In 2012, the average number of direct positions in the sector totaled 31 positions vs. 24 positions in 2011. In the mortgage field – an average of 11 positions vs. 9 in 2011.

In the banking and financing area – an average of 19 positions vs. 14 in 2011, a 36% increase. In the capital market – an average of one position, similar to 2011. Moreover, head office and management personnel were loaded onto this sector. The sector's personnel includes tenured employees trained to provide appropriate service adapted to the sector's customers.

Below is a summary of the operating results for the private banking sector:

	For the year ending December 31, 2012				For the year ending on December 31, 2011*			
	Mortgages	Banking and Finance	Capital market	Total	Mortgages	Banking and Finance	Capital market	Total
	Millions of NIS							
Income from Interest, net								
From externals	13.3	8.2	-	**21.5**	10.3	7.4	-	17.7
Inter-sectorial	(1.2)	(1.2)	-	**(2.4)**	(1.6)	(1.4)	-	(3.0)
Total Income from Interest, net	12.1	7.0	-	**19.1**	8.7	6.0	-	14.7
Income that is not from External Interest	0.7	7.3	3.6	**11.6**	1.9	6.3	1.8	10.0
Total Income	12.8	14.3	3.6	**30.7**	10.6	12.3	1.8	24.7
Expenses for Credit Losses	(0.2)	(0.4)	-	**(0.6)**	2.7	-	-	2.7
Operating and other expenses with the exception of depreciation and amortization	(8.3)	(14.7)	(1.0)	**(24.0)**	(6.8)	(12.8)	(1.0)	(20.6)
Depreciation and Amortization	(0.8)	(1.2)	(0.1)	**(2.1)**	(0.5)	(0.7)	(0.1)	(1.3)
Profit (Loss) before Taxes	**3.5**	**(2.0)**	**2.5**	**4.0**	6.0	(1.2)	0.7	5.5
Provision for Taxes on Profit	(1.1)	0.7	(0.8)	**(1.2)**	(1.7)	0.3	(0.2)	(1.6)
Net profit (loss)	2.4	(1.3)	1.7	**2.8**	4.3	(0.9)	0.5	3.9
Capital yield (net profit rate from equity)	4.1%	(26.8%)	-	**4.3%**	8.4%	(25.0%)	-	7.4%
Average balance of assets	1,164.9	27.7	-	**1,192.6**	958.7	24.0	-	982.7
Average balance of liabilities	-	1,119.7	-	**1,119.7**	-	835.0	-	835.0
Average balance of risk assets	599.5	53.6	-	**653.1**	522.6	33.4	-	556.0
Average balance of securities	-	-	263.7	**263.7**	-	-	227.9	227.9
Average balance of other assets under management	-	-	-	**-**	-	-	-	-
From margin from activity of providing credit	12.1	1.0	-	**13.1**	8.7	0.6	-	9.3
Margin from deposit receipt activity	-	6.0	-	**6.0**	-	5.4	-	5.4
Other	-	-	-	**-**	-	-	-	-
Total Income from Interest, net	12.1	7.0	-	**19.1**	8.7	6.0	-	14.7

* Reclassification.

Changes in the sector activity scope and its profitability

The revenue rate in this sector is about 9% of the Bank's total revenue, compared to 8% for 2011.

The total revenue in the sector amounted NIS 30.7 million in comparison with NIS 24.7 million, an increase of about 24% that is primarily attributed to increased revenue in the mortgage area as a result of increased margin, as well as a rise in balance.

Total expenses for credit losses totaled NIS 0.6 million in comparison with revenue of NIS 2.7 million. Most of the change is attributed to recovery (cancellation of the provision) that was recorded in 2011 in the mortgage field.

Total expenses in the operating and other expenses totaled NIS 26.1 million in comparison with NIS 21.9 million, an increase of about 19% that is primarily attributed to a higher allocation of employees to this sector.

The net profit in this sector this year totaled NIS 2.8 million compared to NIS 3.9 million in 2011.

The majority of the decline in profit is stems frm increased expenses for credit losses and in operating and other expenses.

The net profit from mortgage activity in this sector this year totaled NIS 2.4 million compared to NIS 4.3 million in 2011. The majority of the growth in profit is stems from recovery (cancellation of the provision) recorded in 2011.

The loss from banking and financing activity in this sector this year totaled NIS 1.3 million compared to NIS 0.9 million in 2011.

The profit from capital market activity in this sector this year totaled NIS 1.7 million compared to NIS 0.5 million in 2011.

Business Sector

General

The business sector provides banking services to business customers, corporations, and associations. These services are provided to the Bank's customers, mainly through the business division and the business department specializing in providing these services and located in the Bank branches in Jerusalem and Tel Aviv, as well as in private banking branches. The sector includes activity in the real estate sector, overseeing housing construction projects mainly by the financial oversight method, among others, project financing according to NOP 38 and buyers group financing. In addition, the Bank provides financing for companies implementing solar energy projects, as well as commercial mortgages.

Objectives and Business Strategy

Under its Strategic Plans (as described above), the Bank works to implement a policy in selective sectors in this realm by providing credit to construction companies and residential real estate, with the emphasis on potential growth and without increasing the existing risk level. For this purpose, the Bank works to create cooperation with insurance companies and other institutions for providing project credit loans (operating model) and issuing guarantees according the Sales Act (Apartments) and other guarantees. This strategy enables the bank to increase the scope of projects it handles, and with adjustment to the Bank's policy, using its accumulated expertise, entering large and complicated transactions, dispersion risk and, respectively, increases the yield of allocated capital deriving from this activity while reducing risk.

Moreover, the Bank works to shift risk and inputs, for financing transactions (escorting resident construction) or financing transactions requiring allocated capital as low as possible, and this while reducing, as far as possible, the scope of commercial credit for financing current activity of small companies and business, .

In addition, the Bank operates to expend the financing of transactions in the solar energy branch, which have a long-term agreement with the Electric Company, among others, by cooperating between the Bank and insurance companies, as well as other institutional entities for providing credit. Such cooperation, similar to the aforesaid for financing projects (operator model), enables entry into large transactions and risk dispersion.

The Bank's plans and assessments, as specified above, are future facing information, as well as based upon assumptions and different forecasts presented to the Board of Directors. This information may not be realized because of changes that may be applied for various factors that are not controlled by the Bank only. Influencing factors include forecasts and assessment concerning economic development in Israel and globally, especially concerning the economic situation, including the influence of macro-economic and geopolitical conditions, changes in capital markets, as well as other additional factors influencing risk exposure: public preference, instruction by supervisory factors and others, aspects related to the Bank's image, technological developments and the subject of human resources.

Structure of the Activity Sector

The activity in this sector mainly includes:

Construction and Real Estate – The bank finances the acquisition of land and establishment of housing projects, as well as providing various types of guarantees according to the transaction's requirements. Financing for erecting housing projects is mostly provided by the accompanied financing method conforming to the specific requirements of the project and its characteristics. In the accompanied financing method, the project is separated from the customer's remaining activity. A special account is opened for the project, only for that project's purposes, into which proceeds from housing unit acquisitions, equity, and bank credit are deposited. The proceeds are used for implementing the project and are released as per the construction's rate of progress according to reports from the expert inspector. Under financing the construction project, the Bank grants implementation, financial, and Sales Law guarantees for purchasers of project units. Realty and receivables mortgaged to the bank. Sales Law guarantees are issued for most of the transactions by the insurance company with whom the Bank has a cooperative agreement.

The Bank cooperates with financial entities for the purpose of expanding the scope of its activity and maximizing profitability, while dispersing credit risks, and complying with the required regulatory limitations.

The difference between the types of cooperation with institutional entities, is expressed in the type of credit or collateral provided by the institutional entity: providing guarantees according to Sales Law; providing guarantees to the land owners in combination transactions; and providing financial credit according to the operator model.

Operator model in the construction and real estate area, is implemented according to the principles below:

The project is examined and approved by the financial partner institutions; the collaterals in the project will be pari-passu, when the ratio of distribution in case of collateral realization is determined in advance between the Bank and the financial partner; the volume ratio of the provided credit will remain during the project life. Release of surplus obtained for the project developer, is implemented by the Bank according to the Bank's approved surplus release formula and is included in the cooperation agreement.

Management of the project according to this model, is implemented by the Bank at its discretion and according to accepted banking standards; monitored project reports are transferred by the supervisor to the Bank and to an additional entity, while the Bank reports to the additional entity about irregular events in the project.

Banking and Finance

Credit provided on behalf of the financing of current activity of companies – The Bank made a decision for reducing the credit volume provided under this activity area for 2012, with the credit provided during previous years, and this due to the large capital allocation and required current operations. Financing of commercial activity including financing of income-producing assets and current activity, is generally implemented against material collateral. Current activity of the companies is also financed, among others, against liens on the current assets.

Credit for the solar energy branch – financing acquisition, installation, and operating solar energy systems is implemented against a contract with the Electricity Company for a period of 20 years at a defined electricity purchasing rate and fixed for the whole operating period. Additionally, the bank mortgages the system equipment and the total arrangement of transaction contracts, as required, accumulating various reserve funds during the financing period. In this area, the Bank cooperates with financial entities, similar to the real estate area, according to the operator model.

Operator model in the construction and real estate area is implemented according to the principles below:

The cooperation agreement between the Bank and financial entities is formed and generally signed before the project's setup stage. The solar project's establishing stage is mostly financed only by the Bank. The mutual financing starts in the operating stage of the project, when the credit provided until then by the Bank in the framework of the establishing stage, is paid in full through the mutual credit provided by the Bank and the financial partner under the operating stage; the collateral in the project will be pari-passu, when the ratio of distribution in case collateral realization is determined in advance between the Bank and the financial partner; the volume ratio of the provided credit will remain during the project life.

Management of the project according to this model, is implemented by the Bank at its discretion and according to the accepted financing agreements;, and cooperation agreement between the Bank and a financial entity, and based on accepted banking standards; engineering reports for the project are transferred by the supervisor to the Bank and the additional entity before financing is made available. During the life of the project, the Bank reports to another entity the project's current data and extraordinary events in the project.

Legislative Restrictions, Standards and Special Constraints

The Bank in general, and the business sector in particular, operates within the framework of laws, directives, regulatory guidelines and instructions imposed on the banks by legislative and supervising entities, including the Supervisor of Banks, the Securities Authority, and the Commissioner for the Capital Market, Insurance and Savings at the Ministry of Finance.

Below are updates on the legislative instructions applicable on this sector:

The Draft Amendment of the Companies Law on Company Recovery.

On July 17, 2012, Amendment No. 19 of the Companies Law on Companies Recovery was published. Below are the principles of the amendment:

- Granting of authority to the courts to bind a creditors arrangement on type of creditors that opposed it; arrangement of an efficient and speedy approval process by the court for a creditors settlement that was formulated outside the court; arrangement of tools to operate the company as part of the recovery proceedings until the formulation of the arrangement, including granting authority to the court to prevent suppliers of the essential products or services to discontinue supplying said product or service due to non-payment of past debts. As well as authority to the court to bind the parties to an agreement with the Company concerning continued implementation of the agreement.

In addition, in light of the importance of new credit to the company's recovery, the amendment arranges the court's authorities to approve new credit to the Company and the preferred status of this credit over past debts.

Furthermore, in order to enable the Company's current operation, the amendment arranges the authorities of the officers to use the Company's liened assets, pursuant to the creditors being given adequate protection. The amendment to the law defines for the first time what adequate protection is and under what circumstances it is required.

- Preventing the owners of the asset by virtue of the retention of title clause to receive possession of the asset required for current operation of the Company – the memorandum includes a proposal to consider stipulating that the procedure freeze order will prevent owners of the asset by virtue of retention of title stipulation to receive possession of the asset required for the Company's operation, pursuant to them being granted adequate protection; i.e., granting of securities for payment of the value of the asset at the end of the procedure freeze order.

Changes in the Sector's Activity Markets in Customer Characteristics

The real estate branch has been characterized by price increases over the past few years and by tremendous demand for housing accompanied by a lack of available land for building. The year 2012 was characterized by significantly higher sales rate of housing units than expected at the start of the year, and price levels that were similar to 2011 prices, despite the expectation of a decline in prices following the social protests that took place in the summer of 2011. This expectation did not materialize in light of the shortage of land available for construction, shortage of personnel in the construction industry, and regulatory restrictions that affected the banking system (most banks reached the industry limitation level for the construction branch). Therefore, there still in uncertainty in the real estate market concerning price levels, influenced among others by the lack of available land for construction and decrease in the volume of construction starts in desired areas (marketing of the land of the Ministry of Housing and the Israel Lands Administration is mostly centralized in the periphery areas), and a burden on mortgagers alongside expectations of government intervention that will result in declining prices.

In addition, some of the banks exhausted the existing branch limitation in compliance with the Proper Banking Management instructions № 315: Additional Provision for Doubtful Debts, and because of that, the Bank is exposed to additional customers that are not the "home customers" of these banks.

Nevertheless, in light of the government decision from August 16, 2012, to establish a fund for VAT reimbursement for Sales Law guarantees (within the confines of the financial oversight agreements that were signed and/or that will be signed between September 1, 2012 and December 31, 2015), there is an expectation that some banks that had been blocked due to industry restriction will return to be active players in project financing.

Critical Success Factors in the Activity Sector and Occurred Changes:

- Professional training of manpower with experience and skills.
- Intelligent risk management, while establishing proper credit control systems for locating and minimizing risk.
- Providing qualitative and quick service.

In the real estate area:

Specific professional knowledge in this area, including understanding and ability to analyze the relevant variables affecting the risk level in real estate projects, such as demand areas, construction in stages, land ready for construction, and so forth.

– Locating opportunities through connections with experienced entrepreneurs operating in this branch.

– High credit underwriting ability expressed in correct choice of the accompanied project as a derivative of the project's location and its marketing possibilities in accordance with market needs.

– Defining a financing structure for the transaction according to project and customer requirements.

– Control and supervision of project income and expenses until completion.

– Ability to manage credit in crisis conditions.

– Appropriate assessment of the customer's repayment ability.

Banking and Finance:

– Careful management of credit, while implementing diligent control.

– Thorough comprehensive analysis of new transactions, including understanding of risks inherent in financing.

- Defining a loan structure and adapting the of amount of financing to cash flows in respect of corporate transactions and activity.

- Reliable current assessment of the Bank's existing collateral and following the company's current reports.

- Development of expertise in the financing area of the solar energy branch and access to operating factors in the branch.

- Legal examination concerning providing financing for solar energy transaction including examining the rights of the assets on which the solar systems are installed, examination of rental contract between the entrepreneur and the owner of the asset (as far as it concerns a transaction on this type), examination if the financial model of the transaction, etc.

The Main Entry and Exit Barriers of the Sector's Activity and the changes applied to them

- Regulatory limits on banking corporations, including limitation on borrower debts or group of borrowers, as well as also other regulatory limits; as for example, non-bank factors have limited independent access to the real estate branch as result of mandatory Sales Law, in certain conditions, issuance of bank guarantees for buyers of construction project units.

- Requirements for minimum capital.

- Long-term relationship with factors operating in areas under the business sector.

- Knowledge and accumulated experience working at financing under the accompanied financing method.

Alternatives to Products and Services of the Activity Sector of and Occurred Changes

As an alternative to banking credit, alternative financing products have been developed and provided by non-banking entities. An alternative credit including mobilization on the capital market, among others, by issuing debentures to real estate companies, which may be backed by specific cash flows, including direct credit granted to these bodies. This credit alternative and its availability is influenced by the capital market situation. Therefore, there exists a decline in the issuance scope.

Customers

In the construction and real estate sector, the bank oversees about 180 projects with an average size of 58 residential units per project. More than half of the accompanied residential units are located in high-demand areas – Greater Jerusalem, Central, and Sharon areas.

The bank's credit portfolio is spread and the bank does not have dependency on any individual customer or limited group of customers. The credit balance of bank customers is not dependent on any single borrower. Scatter of the portfolio is also enabled through the bank's strategic cooperation with insurance companies that generally issue policies according to the Sales Law (Apartments) to buyers in projects accompanied by the bank. Also, there are also several joint projects with an insurance company to provide financial credit for accompanied projects (on the operator model).

In the area of credit for commercial activity in the solar energy branch – the customer portfolio is spread among a large number of customers across the country. In financing the solar energy branch there are two types of customers: Asset owners that install solar systems on roofs owned by them, and a second; entrepreneurs that rent roofs for installing solar systems.

Marketing and Distribution

The marketing and the distribution are performed through managers and employees of the real estate sector of the Bank and in the commercial departments in the Bank's branches in Tel Aviv, Jerusalem, and in the private banking branch.

The bank mobilizes customers and expands its activity in the realty branch, among others, by collecting data concerning tenders for land acquisitions intended for construction; analyzing the tenders, and then initiating contact with the tender winners through its wide familiarity with those operating in this branch. Additionally, the Bank works to expand its activity using its existing customer base.

The bank initiates exposure to the target public by sponsoring events organized by the association of contractors and builders and by local contractors' organizations, through participation in various meetings, including speakers and/or panelists from the bank at these events.

In the solar energy sector the bank markets itself among installation companies and potential customers as well as initiating contact with these factors.

Competition

The competition among the banks to attract quality real estate customers is expressed on equity rates of invested in the project, transaction structure, commission size, interest on transactions, and the level of customer service. During 2013, insurance companies also intend to enter the project financing area. The Bank's principle methods for dealing with competition, is based on the connections that it has been accumulating over the years, as well as its existing customer base, which constitute a lever for continuing its activity. Also, the bank sometimes utilizes excess sources in existing projects to leverage future activity by its customers' new projects. The bank operates a mechanism to determine the amount of equity required for the project, derived form the rate of project implementation, as well as sales. The aforementioned mechanism constitutes an incentive for promoting project sales and therefore reduces the projects' risk levels.

Most of the banks in the banking system participate in financing the solar energy branch. Moreover, at transactions with high volumes, institutional entities and insurance companies are also taking part in the financing. The level of professionalism, the knowledge and extensive familiarity with the branch enables the Bank to expand it activity with existing and new customers.

The Bank has no ability to assess its share of this area's credit balance of the entire banking system. Nevertheless, by the Bank's assessment for 2011, its relative portion in overseeing new housing units, stood at about 12% of all the housing units starts during 2011. Furthermore, the Bank assesses that its part in the solar energy branch is greater than the Bank's share in the banking system.

Cooperative Agreements

The bank has cooperative agreements with several insurance companies for providing credit and/or for issuance of insurance policies to buyers of apartments in residential projects financed by the bank according to the accompanied financing method (the policies are issued by the insurance companies as required in accordance with the Sales Law (Apartments). The agreements with insurance companies include arrangement of cooperation between the bank and the insurance companies concerning the following: responsibility for current management of the project, submission of reports, receipt and release of collateral, and following procedures for realizing liens and creditor arrangements between the parties.

Human Capital

In 2012, the average number of direct positions in the sector totaled 30 positions vs. 31 positions in 2011. In the construction and real estate field – an average of 18 positions, in comparison with an average 17 positions in 2011.

In the banking and financing area - an average of 10 positions vs. 12 in 2011, a 17% decrease attributed to organizational changes. In the capital market area – average of 2 positions, similar to 2011. Moreover, head office and management personnel were loaded onto this sector.

Below is a summary of the operating results of the business sector:

	For the year ending December 31, 2012				For the year ending on December 31, 2011*			
	Construction and real estate	Banking and Finance	Capital market	Total	Construction and real estate	Banking and Finance	Capital market	Total
	Millions of NIS							
Income from Interest, net								
From externals	21.9	16.6	-	**38.5**	17.7	21.9	-	39.6
Inter-sectorial	(1.1)	(3.9)	-	**(5.0)**	(1.5)	(6.8)	-	(8.3)
Total Income from Interest, net	20.8	12.7	-	**33.5**	16.2	15.1	-	31.3
Income that is not from External Interest	16.3	5.0	1.1	**22.4**	13.9	4.7	1.5	20.1
Total Income	37.1	17.7	1.1	**55.9**	30.1	19.8	1.5	51.4
Expenses for Credit Losses	0.6	(2.6)	-	**(2.0)**	3.7	(1.1)	-	2.6
Operating and other expenses with the exception of depreciation and amortization	(15.8)	(11.8)	(2.0)	**(29.6)**	(16.0)	(14.0)	(2.5)	(32.5)
Depreciation and Amortization	(1.3)	(0.7)	(0.1)	**(2.1)**	(1.0)	(0.8)	(0.1)	(1.9)
Profit (Loss) before Taxes	20.6	2.6	(1.0)	**22.2**	16.8	3.9	(1.1)	19.6
Provision for Taxes on Profit	(6.7)	(0.8)	0.3	**(7.2)**	(4.8)	(1.1)	0.3	(5.6)
Net profit (loss)	13.9	1.8	(0.7)	**15.0**	12.0	2.8	(0.8)	14.0
Capital yield (average net profit rate from capital)	13.2%	4.2%	-	**10.2%**	10.4%	3.7%	-	7.4%
Average balance of assets	810.4	501.5	-	**1,311.9**	687.8	478.0	-	1,165.8
Average balance of liabilities	239.5	3,165.6	-	**3,405.1**	222.4	3,506.5	-	3,728.9
Average balance of risk assets	1,101.7	425.7	-	**1,527.4**	1,194.5	774.7	-	1,969.2
Average balance of securities	-	-	247.8	**247.8**	-	-	318.9	318.9
Average balance of other assets under management	-	-	72.7	**72.7**	-	-	125.9	125.9
From margin from activity of providing credit	20.3	8.5	-	**28.8**	16.1	8.1	-	24.2
Margin from deposit receipt activity	2.4	3.2	-	**5.6**	2.7	4.4	-	7.1
Other	(1.9)	1.0	-	**(0.9)**	(2.6)	2.6	-	-
Total Income from Interest, net	20.8	12.7	-	**33.5**	16.2	15.1	-	31.3

* Reclassification.

Changes in the sector activity scope and its profitability

The revenue rate in this sector is about 16% of the Bank's total revenue, compared to 17% for 2011.

The total revenue in the sector totaled NIS 55.9 million compared to NIS 51.4 million, an increase of about 9% that stems primarily from increased revenue as a result of an increase in credit balances primarily in the construction and real estate area.

Total expenses for credit losses totaled NIS 2.0 million compared to revenue of NIS 2.6 million. Most of the change is attributed to recovery (cancellation of the provision) that was recorded in 2011 in the construction and real estate area.

Total expenses in the operating and other expenses totaled NIS 31.7 million compared to NIS 34.4 million, a decrease of about 8% that is primarily attributed to a decrease in the number of employees in the banking and finance area.

The net profit in this sector amounted this year to NIS 15.0 million as compared to NIS 14.0 million in 2011.

The net profit from construction and real estate activity in this sector amounted this year to NIS 13.9 million as compared to NIS 12.0 million in 2011. The majority of the growth in profit stems from net increased income from interest, as a result of increased credit balances.

The net profit from banking and financing activity in this sector amounted this year to NIS 1.8 million as compared to NIS 2.8 million in 2011. The main decrease is attributed to a decline in inter-sector income attributed to this activity.

The loss from capital market activity in this sector amounted this year to NIS 0.7 million, similar to that in 2011.

Financial Management Sector

General

The activities in this sector are not with customers, including the bank's financial management, and include:

- Managing the bank's available financial capital.
- Managing the bank's nostro portfolio.
- Managing exposure to market risks, including basis, interest, and liquidity exposure.
- Activity relative to banks in Israel and abroad.

Objectives and Business Strategy

The purpose of this activity is to increase the yield on excess liquidity while maintaining appropriate risk levels.

Structure of the Activity Sector

This sector's activity is concentrated in the Financial Division. The bank currently manages the positions in the various linkage sectors through a variety of financial instruments available to it. This management is implemented in accordance with the risk management policy as defined by the Board of Directors, and taking into account changes in relevant economic data and current supervision of risks resulting from such exposure.

The nostro portfolio is divided into the following types of activity:

- Activity for commercial purposes characterized by short-term investments primarily in government securities both in the primary market and in the secondary market.
- Activity used as protection for short-term, medium-term and long-term deposits with the Bank, as well as investments against the Bank's equity.
- Investment activity in debentures mainly for the purpose of reaching surplus yield on the Bank's liquidity balances.
- Investment activity in non-government securities, mainly bank or corporate debentures, according to the banks credit policy.

The investment portfolio and the financial products are examined currently, taking into account macro-economic forecasts on the issues of exchange rates, short-term and long-term interest rates, inflation, economic growth, and yield curves. Such analysis is required in order to arrive at correct costing of financial products and investment decisions relating to the nostro portfolio.

As part of managing the surplus liquidity, and in consideration of the limitations determined by the Bank's Board of Directors, surplus liquidity is deposited at the Bank of Israel and banks in Israel and abroad. For details concerning the liquidity model and limitations of the management and the Board of Directors, please see the "Risks and Risk Management" chapter.

The Bank has credit frameworks from banks in Israel, which it uses from time to time in accordance with its regular needs.

Legislative Restrictions, Standards and Special Constraints

The Bank, and the financial management sector in particular, operates in the framework of laws, regulations and instructions from the authorities, imposed on the banks by the Supervisor of Banks, the Securities Authority, and the Commissioner for the Capital Market, Insurance and Savings.

Critical Success Factors in the Activity Sector

The critical success factors in this sector may correctly recognize the market conditions and the expected timing for a change in these conditions, the ability yo understand and analyze the possible influence of macroeconomic factors on market condition and to predict their power, and the ability to operate quickly, to changes in positions, and exposure according to the market conditions. An additional factor is the professionalism of the employees relied upon to manage the financial sector in general, and the nostro portfolio in particular.

Human Capital

In 2012, the number of direct positions in this sector amounted to 2 positions, similar to 2011.

Moreover, head office and management personnel were loaded onto this sector.

Below is a summary of the operating results of the financial management sector:

	For the year ending December 31, 2012	For the year ending on December 31, 2011*
	Millions of NIS	
Income from Interest, net		
From externals	**(17.1)**	(44.1)
Inter-sectorial	**22.0**	32.0
Total Income from Interest, net	**4.9**	(12.1)
Income that is not from External Interest	**22.6**	6.2
Total Income	**27.5**	(5.9)
Expenses for Credit Losses	**-**	-
Operating and other expenses with the exception of depreciation and amortization	**(5.6)**	(4.4)
Depreciation and Amortization	**(0.2)**	(0.1)
Profit (Loss) before Taxes	**21.7**	(10.4)
Provision for Taxes on Profit	**(7.1)**	3.0
Net profit (loss)	**14.6**	(7.4)
Capital yield (net profit rate from equity)	**30.1%**	(19.8%)
Average balance of assets	**1,955.2**	2,015.8
Average balance of liabilities	**70.2**	81.2
Average balance of risk assets	**509.2**	389.2
Average balance of securities	**-**	-
Average balance of other assets under management	**-**	-
Margin from activity of providing credit	**(14.5)**	(33.1)
Margin from deposit receipt activity	**-**	-
Other	**19.4**	21.0
Total Income from Interest, net	**4.9**	(12.1)

* Reclassification.

Changes in the sector activity scope and its profitability

The net profit in this sector amounted this year to NIS 14.6 million as compared to a loss of NIS 7.4 million in 2011.

The main change is attributed to an increase in profits from nostro activity (realization of securities and adjustment to fair value of negotiable securities) of NIS 22.6 million, of NIS 6.2 million in the parallel period last year (gross before tax).

As at December 31, 2012, the Bank holds NIS 226.5 million in n.v. in liability certificates its subsidiary issued (Jerusalem Financing and Issuances). Due to purchasing these liability certificates the Bank recorded gains totaling NIS 0.3 million, that have been reflected in this sector (during 2011 – NIS 3.9 million).

Below is data concerning the decrease in value of debentures available for sale (government and corporate) recorded under capital reserve by time periods and the impairment rate:

Impairment rate on the date of the financial statement	Impairment amounts (in NIS millions)					
	Period of time in which fair value of asset was less than its cost				Total impairment for December 31	
	up to 6 months	6-9 months	9-12 months	Over 12 months	2012	2011
up to 20%	-	-	-	1.7	1.7	16.0
40%-20%	-	-	-	-	-	5.4
Over 40%	-	-	-	-	-	-
Total	**-**	**-**	**-**	**1.7**	**1.7**	**21.4**
From Israeli government debentures	-	-	-	1.7	1.7	15.2

Note: It should be emphasized that the rate of impairment and the period of time of impairment relates to different periods – The period of time is measured from the date on which the fair value of the asset was materially lower than its cost price, while the rate of impairment is stated as at a specific point in time, December 31, 2012 and December 31, 2011.

Fourth part - Matters related to the activities of the overall banking corporation

Attracting financial resources

General Information

Over the years, the Bank has adopted a policy committed to expanding activities with households for the purpose of expanding the resource recruitment base. During these years, the policy added a significant increase to the weight of the households in the total public deposits and this corresponding with the decrease in weight of the deposits from institutional entities. The balance of public deposits as at December 31, 2012, amounted to NIS 9,814 million, compared to NIS 9,065 million at the end of 2011. The percentage of public deposits from households from the balance of public deposits on December 31, 2012, totaled about 82%, in contrast with 79% at the end of 2011.

The Bank's activity in the mobilization of financing sources from the public is managed by the financial divisions.

Objectives and Business Strategy

The Bank set a long-term policy for itself to expand mobilization of sources, increasing the weight of household resources out of the total deposits by the public while maintaining the ability to mobilize sources from institutional customers. Long-term deposits are mobilized according to the volume of new long-term credit granted. In addition, the Bank, through the "Jerusalem Financing and Issuances Ltd." subsidiary, mobilizes deferred liability notes according to the bank's capital requirements.

Bank management determines specific branch objectives and for the head office in all sectors of activity and manages current monitoring for meeting these objectives.

The bank acts to perform the strategy and objectives through a variety of products and their adaptation to customer requirements and variable market conditions. Also, the bank holds campaigns to the depositor public and through the media and online means to existing and potential customers. The bank offers closed circuit banking services that enable mobilization of funds from customers of all banks, as listed below. Moreover, the bank attributes importance to strengthening cooperation with institutional customers, including the monetary funds.

Structure of the Activity Sector

The financing sources in the banking system, in shekels and in foreign currency, are mainly deposits from households, companies, institutional entities, banks in Israel and abroad, and by mobilization of marketable debentures on the capital market.

The sources include, inter alia, deposits in all linkage sectors, bearing fixed interest or variable interest, deposited for various periods from one day to eighteen years.

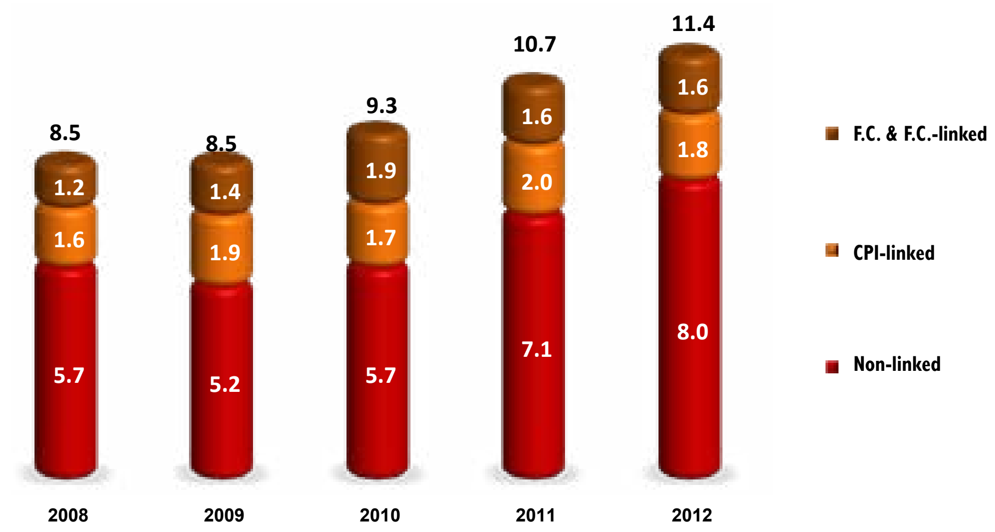
During 2012, there was a net accumulation in the households deposits for a total of about NIS 930 million, compared to net accumulation of a total of about NIS 1,400 million in the previous year. The net accumulation from households in recent years is attributed to improved work processes in the branches, management of the ad campaigns that resulted in the recruitment of new customers in the branches, through the closed system, and changes in the deposit pricing model.

Below is the composition of the bank's financing sources including deposits by the public, liability certificates and deferred liability notes:

		Balance for December 31		
		2012	2011	Change in percentages
		Millions of NIS		
.1	NIS deposits and current accounts	**5,367**	4,962	8%
.2	Index-linked Savings Plans & Deposits	**3,012**	2,764	9%
.3	Deposits in foreign currency and linked to foreign currency	**1,435**	1,339	7%
	Total Public Deposits	**9,814**	9,065	8%
.4	Debentures and deferred liability notes	**1,581**	1,612	-2%
	Total financing resources	**11,395**	10,677	7%

The average balance of liabilities in 2012 totaled NIS 10,887 million, compared to NIS 10,151 million in 2011. This balance includes an average balance of liabilities for households totaling NIS 6,292.4 million (household sector), an average balance of liabilities to private banking entities for the amount of NIS 1,119.7 million, an average balance of liabilities to companies and institutional entities amounting to NIS 3,405.1 million (business sector), and an average balance of liabilities to banks for the amount of NIS 70 million (financial management sector).

Listed below is The Bank's Resource Mix in NIS Billions:



The bank has credit frameworks from banks in Israel, which it uses from time to time in accordance with its current needs. The height of the credit lines is determined by other banks and is unknown to the Bank. As of the balance sheet date, the Bank did not exploit any credit lines from Israeli banks.

Legislative restrictions, standard, guidelines and circulars from the Supervisor of Banks, and special constraints

The Bank operates in the framework of laws, regulations, and directives from the authorities, imposed on the banks by the Supervisor of Banks, the Securities Authority, and the Commissioner for the Capital Market, Insurance and Savings.

Competition Structure

Competition structure in the banking system is such that most customers in the banking system deposit their funds with the commercial bank in which their checking account is maintained and these customers are generally indifferent to interest offers on various investment products in other banks. Accordingly, only part of the customers in the banking system compare prices between banks in order to obtain the maximum interest on their investment.

In 2011, the Bank launched a unique venture for recruiting deposits from households called "Closed System". The system enables customers to deposit money in deposit notes at the Bank through the Internet without the bother involved in opening a full account at a bank branch, and thus increasing the Bank's access to potential customers. The venture is built according to Proper Banking Management Instruction № 417 of the Bank of Israel.

At the start of 2012, the Bank changed the deposit pricing model, including an undertaking, according to which the interest rate on one-year NIS deposits will not be less than 80% of the interest from the Bank of Israel, except for deposits with fixed interest for a period longer than three months, whose interest rate will not be reduced from 80% of the yield rate for the relevant short-term loan. On deposits for periods of one year or more, the Bank undertakes that the interest rate will not be less than 80% of the yield rate on government debentures or the cost of cash, whichever is higher. This undertaking does not depend on the size of the deposit or on opening a checking account.

This combination of the new pricing policy alongside the existing access within the closed system, contributed to the competition in the deposits sector of the banking system.

The success of the process resulted in an increase of the Bank's customer base, dispersal of resources, diminished reliance on capital markets, and an improvement in the Bank's profitability.

The bank acts to recruit resources also through the capital market by issuance of debentures and deferred liability notes. The issuance is performed by fully controlled subsidiary, Jerusalem Financing and Issuances that is the recruitment force of the Bank, and therefore, the Bank undertook to comply with all the conditions of the liability certificates, to bear the payment of full amounts that will be required for the payment of the liability certificates to their holders and their interest, conform the conditions determined in the issuance prospect that has been published by Jerusalem Financing and Issuances.

On December 24, 2012, the Jerusalem Financing and Issuances Company issued, according to the shelf offering report as of December 24, 2012, that was published based on the prospectus dated August 31, 2011, debentures (Series H) in n.v. totaling NIS 122,421 thousand. Debentures in consideration for NIS 122,421 and NIS 71,761 thousand n.v., deferred liability notes (Series 10) in consideration for a sum of NIS 71,761 thousand.

Customers

During recent years the bank placed emphasis on expanding the depositor base and increasing deposits from households, in order to reduce the reliance on large depositors. The bank's deposits portfolio is spread among many customers, thereby decreasing the liquidity risk and providing a low level of sensitivity in the bank in respect of individual depositors. The bank does not have any customer or group of customers whose deposit balance exceeds 5% of the total deposits by the public.

Marketing and Distribution

The recruitment of households is implemented through 18 Bank branches spread throughout the country, as well as through the closed system enabling recruitment of deposits without opening an account at the Bank's branch Recruitment of institutional customers is generally implemented directly by the deposits department.

During 2011, the bank joined with the Postal Bank, which has a larger nationwide deployment, in a cooperative agreement, under which the Bank of Jerusalem's deposit notes would be sold at Postal Bank branches. For details please see the "Material and Cooperative Agreements" section. This agreement enables the Bank to market deposit notes to customers of the Postal Bank living all over the country, and will expose these customers to the Bank of Jerusalem. As of the end of 2012, Bank of Jerusalem deposits are offered at dozens of Postal Bank branches at which over 2000 deposit certificates were opened. In 2013, the plan is to offer Bank of Jerusalem deposits in other Postal Bank branches.

This information in relation to expanding activity with the Postal Bank is future facing information, that may not be realized, in whole or in part, or that may be realized differently from expectations. This information is based on the Bank's assessment and might not be realized in the event that the Postal Bank will be allowed to perform this activity by itself, other regulatory changes in relation to the Postal Bank or the Bank, customer preferences, unsuccessful and unpredicted business responses in the Bank's business environment.

Competition and Alternatives to Products and Services of the Activity Sector

The competition in the resource recruitment area is strong and includes all the banks. Competition focuses mainly on that sector of customers that is sensitive to changes in interest rates. The Bank deals with the competition, among others, by attractive campaigns for customers and developing new products to vary the product basket. Moreover, various capital market products are alternative investments for deposit notes offered by the Bank.

Bank of Israel

The Bank of Israel acts as a central agent for financing and short-term absorption of money for the banking system, including for the Bank. It should be mentioned that, every bank that borrows money from the Bank of Israel requires collateral, this fact is taken into consideration in current liquidity management. An additional channel for recruiting short-term resources is the interbank money market.

The scope of deposits and their types in the banking system are influenced, among others, by the Bank of Israel's monetary policies. Below is a review of monetary tools activated by the Bank of Israel for the purpose of implementing its monetary policy:

Interest – Each month the Bank of Israel publishes the prevailing interest rate for the following month. This interest comprises the basic interest of loan and deposit centers provided to the banking system as specified below.

Liquidity obligation – The Bank of Israel's instructions require banks to keep balances by means of liquidity for public deposits, at different rates according to the deposit period. Current liquidity obligation rates are 6% on deposits for a period longer than one day and up to 6 days; and 3% on time limited deposits from one week up to one year. There is no liquidity obligation for deposits with a period of one year and more.

As of the end of January 2011, the Bank of Israel imposed new liquidity obligation for currency swap and future Shekel – foreign-currency transactions for foreign residents, including foreign banks.

Deposits for absorbing surplus liquidity – The Bank of Israel provides deposit tenders for the banking system as an absorption tool for system liquidity surplus. The deposit tenders are for the following time periods: day, week, and month. The maximum interest in these tenders is the interest announced by the Bank of Israel. Additionally, there is a window for depositing daily deposits at the Bank of Israel without limit, at an interest rate of 0.5% lower than the Bank of Israel's interest rate.

Short-term loans – The main financial instrument for absorbing Shekels surplus are short-term loans, by means of current issuances to the public and the Bank of Israel's secondary market activity.

Bank of Israel loan tenders at the – The Bank of Israel provides short-term loan tenders (up to one week) for the banking system as instrument for the system's liquidity flow. The minimum interest in these tenders is the Bank of Israel interest rate. Moreover, there is a daily credit window at the Bank of Israel at an interest that is 0.5% higher than the Bank of Israel interest rate. Obtaining credit from the Bank of Israel, through tenders as well as a credit window, is limited according to the amount of collateral each bank has at the Bank of Israel.

Material and Cooperative Agreements

Agreement with the Postal Bank

As of September 25, 2011, the Bank has an agreement with the Israel Postal Company Ltd. (on its behalf and on the behalf of the Postal Bank Ltd.), under which cooperation between the Bank and the Postal Bank is agreed, to offer its customers the use of the postal services for the purpose of opening deposit certificates at the Bank. According to the terms of the agreement, Postal Bank customers may request to open a deposit certificate and make a deposit at the Bank of Jerusalem, to transfer funds from their Postal Bank accounts to the deposit certificate at the Bank of Jerusalem, and to manage the deposit certificate in the Bank of Jerusalem.

Ranking of Bank's Liabilities by Standard & Poor's Maalot

E. On April 22, 2012, Standard & Poor's Maalot (hereinafter: Maalot) announced that in continuation of the monitoring of the Bank's rating under Maalot's updated methodology for rating banks (as published on November 9, 2011), it was removing the bank's rating from CreditWatch (with negative repercussions) that it had entered in June 2, 2011, and is leaving the the Bank's rating ilA+ (negative rating forecast) intact. For details, please see the Immediate Report dated April 22, 2012, (reference number 2012-01-106239).

This rating is also the rating for the liability notes (except for the deferred liability notes as listed below) that were issued by Jerusalem Financing and Issuance, the Bank's fully owned and controlled subsidiary, that is ilA+. Deferred liability notes that were issued by Jerusalem Financing and Issuance are rated at one rating level lower than the Bank's rating in accordance with the rating company's methodology. Therefore, the rating is ilA.

On December 13, 2012, Maalot announced that it had set a rating of ilA+ for the debentures (Series H) and a rating of ilA for the deferred liability notes (Series 10).

Fixed Assets and Installations

As at December 31, 2012, the amortized cost of the bank's buildings and equipment amounted to NIS 117.9 million, compared to NIS 79.7 million for December 31, 2011. The growth is largely attributed to investments in software costs.

Most of the premises in which the Bank conducts its business are rented ones. As at December 31, 2012, the Bank had a total area of about 11 thousand sq.m. at its disposal, as compared to 9.6 thousand sq.m. for December 31, 2011.

As of the end of 2012, the head quarters area extended over a total of 4.9 thousand sq.m. The balance of area was used by the Bank's branches.

On April 7, 2011, the Bank's headquarters were transferred to Airport City according to the rental agreement from December 19, 2010. The rental agreement is for a period of 7 years (until 2018) with an option for extending it an additional 7 years (until 2025, and an additional option for 7 years (until 2032). At the beginning of the year 2012, the bank rented additional 878 sq.m. in the headquarters building.

Other fixed assets are equipment, furniture, and vehicles (mainly computer systems, see below chapter Computers) that are utilized by the bank for its current activity.

For additional information see Note 8 of the Financial Statements.

It is the Bank's policy to only hold actually required real estate assets or that is expected to be required in the future. The Bank continually examines their scope, characteristics and location of the areas needed by it, based on its business plans and nationwide distribution of branches and makes the required adjustments.

Intangible Assets

Trademarks and Domain names - The Bank has the following intellectual property rights, registered in its name at the Registrar of Trademarks: "Bank of Jerusalem", "BANK OF JERUSALEM", "Bank of Jerusalem a Capital Bank", "BANKAOOT LEMADRIN". Furthermore, the Bank is the registered owner of the domain names bankofjerusalem.co.il www.bankofjerusalem.co.il, www.bank-jerusalem.co.il.

Databases – The Bank and companies in its group are the owners of registered databases containing data concerning the Bank's business and its customers.

Information Systems and Computerization

The Bank 's computer department handles all of the Bank's computer activity through the Tomer Company and works to develop advanced technological systems for continuously improving the Bank's systems and computer infrastructure.

Computer Centers

The Bank's main computer center is at the Head Office in Airport City, Lod.

The Bank operates a backup site (DR) located in Jerusalem.

The Bank's branches are connected through a TCP/IP network with the computer center, through a route at each branch. In total, about 450 work stations are operated by the Bank's communication network.

Information Systems

The support of the Bank's business activities implemented on the basis of 3 core systems:

Commercial system (BankWare) – For management of commercial activities and the ledger. The package is installed on a platform – with AIX/Unix as the operating system, and Oracle for database.

Mortgages system – for management of mortgage activities. The software program is installed on a LINUX platform and Cache as a database.

Securities trade system – for managing the activities in the capital market, the package is run on IBM AS/400 computers.

In addition to the core systems, the Bank operates about 60 software/hardware systems. The additional software programs are characterized by 3 categories:

1. Accompanying banking systems.
2. Accompanying managing systems.
3. Infrastructure, communication, and storage systems.

Backup and Disaster Recovery (DR)

The Bank's disaster recovery policy is based on operating the systems defined as essential, conforming to the time period as set by the policy.

For this purpose, a backup site (DR) has been established in Jerusalem including the systems defined by a high critical rating.

In 2012, the site's expansion continued as did the establishment of backup systems for additional and new systems that have been defined as critical ones, and this according to priorities as will be determined by the Bank.

In the first quarter of 2012, a drill was carried out that tested several systems that will be operated from the backup site.

During the year, a mapping was implemented of the critical processes that are required for business continuity in the event of a disaster / emergency and accordingly, a mapping was made of the support systems of these business processes.

Software was built to respond to the aforementioned requirements through the existing information systems in the bank. In the last quarter, this software was launched after it was validated by Bank management and is scheduled to be finished during the first half of 2013.

Information Security

The Bank invests vast resources for the assimilation of new products and the continuous improvement of the level of information security. In view of the high importance the Bank places on this issue, the Bank's information security policy is determined by the Bank's Board of Directors, which oversees actual policy implementation. The policy is implemented by the Information Security Manager and the Bank's computer department.

Projects

1. CRM

The process of setting up infrastructure and components in the manufacturing environment was completed in May 2012. The soft-launch stage began on October 15, 2012.

Deployment of use in telephone call centers and in branches is taking place in stages based on the rate at which solutions for system malfunctions are provided.

2. Internet

The Bank plans on upgrading the website so that customers will be able, in the first stage, to obtain information and in the later stage, perform bank transactions.

3. Mail and Distribution

The mail and distribution system infrastructure setup was completed, which allows mail and distribution of notices to bank customers. Some of the notices to customers were already sent through the system. In 2013, use of the new system will expand.

4. Automated Teller Machines (ATM)

The Bank is in advanced stages of setting up an ATM system across the country that will enable cash withdrawals, cash deposits, depositing of checks, implementing additional activities and obtaining information. The deployment of the ATMs will begin in 2013.

5. **Upgrade and expansion of the telephone call center (Contact Center)**

The call center (Contact Center) was set up is based on an advanced technological system for supporting the Contact Center's work processes with customers and with the Bank's business units in terms of telephone response, with the ability to work with video branches in order to serve as a "Central Branch" for the Bank's customers, and enable full support of the Bank's customers in obtaining information and implementing activity, as well as for marketing and sales purposes.

6. **Digital Archive**

A digital archive was established to store customer documents. In 2013, the archive link will be completed for all of the relevant bank systems.

7. **Video Branches**

In order to expand the geographic spread of bank branches and to reduce operating costs, the Bank is setting up video branches in which the customer can conduct video conversations with a bank teller at a sales center. As part of the established infrastructure, a customer self-service system was built in the branch in compliance with information security requirements. Special emphases was placed on user friendliness of the system, system stability and protection of information privacy as required. Avaya video software was used in combination with an application for internal development for customer identification and printout and scan management.

Integration and Connectivity

The Bank will implement project integration of the (Service-Oriented Architecture) SOA" concept, and will integrate software tools that will support the multi-channel concept and realization of customer-focused business activities.

The Bank will integrate software tools (ESB – Enterprise Service Bus) that will enable integration between the core and other systems.

The integration method between systems will be through developing Web services .

Management Information

Producing information for managers will be implemented by an effective method, while providing qualitative information in fast response time – as required by dynamic business reality.

In 2013 and 2014, the DWH data models and the BI system will be upgraded to allow for the provision of a response to a greater range of business questions. Furthermore, the BI system version was upgraded and advanced tools were provided for data review by analysts and end users.

Computing Infrastructure

The Bank's computer infrastructures fully support the bank's developed systems or that are acquired as off-the-shelf products from external suppliers. The Bank performs standardization of uniform infrastructures that provide a response to all systems, standards were set for the setup of databases on which the system relies, broad communications networks were built that enable a fast flow of information without loads even during peak hours. A modular telephony system was built that supports growth of both quantity and in call volume including recordings required by regulation.

The information detailed above in relation to computer plans and planned projects is "future facing information" that may not be realized in whole or in part or may be realized differently from expectations. This information is based on the assessment by the Bank's management, the agreements signed with different suppliers, and the Bank's work plans. These estimates may not be realized, among others, as a result of economic events, political/security-related events, non-compliance with timetables set in the agreements with suppliers, and changes in the Bank's work plans.

Supplier Management

The Bank relies on different systems including the core systems developed and maintained by various companies. The Bank maintains proper connections with all the external suppliers of information technology, in order to ensure system normality, continuous operation, as well as technological and functional upgrading.

Periodically the Bank verifies the situation of the companies and their economic soundness, mainly their essential and central systems.

The Bank's relations are anchored in individual agreements with each supplier specifying the supplier's obligations to the Bank (including SLA) and also the Bank's obligations to the supplier.

The Bank is not materially dependent on suppliers, except forEMC, IBM, Oracle, Matrix, Kav Systems and F.M.R.

Investment Scope

During 2012, the investment scope in software and hardware amounted about NIS 48.8 million. A similar scope is planned for 2013, for the purpose of meeting work plans as approved by the Bank's management.

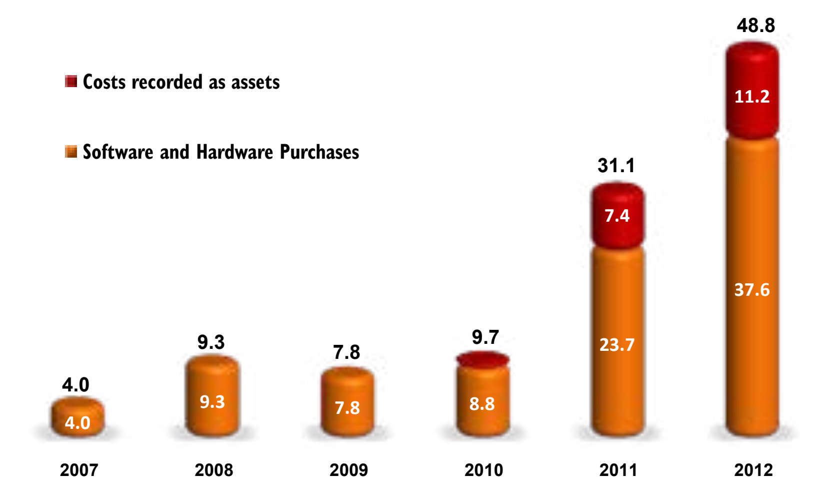
Computerization Costs for 2012

Expenses recorded in the Profit and Loss report (in millions of Shekels)	
Expenses for payroll and accompanying	6.8
Expenses for outsourcing	6.1
Depreciation Expenses	12.9
Other expenses	21.8
Total	47.6

Costs recorded as assets (in millions of Shekels)	
Capitalization for payroll and accompanying	4.9
Capitalization for outsourcing	6.3
Total	11.2

Balance of assets for information technology system (in millions of Shekels)	
Depreciated Cost (Software Costs)	70.8
Depreciated Cost (Computer Equipment)	5.5
Total	76.3

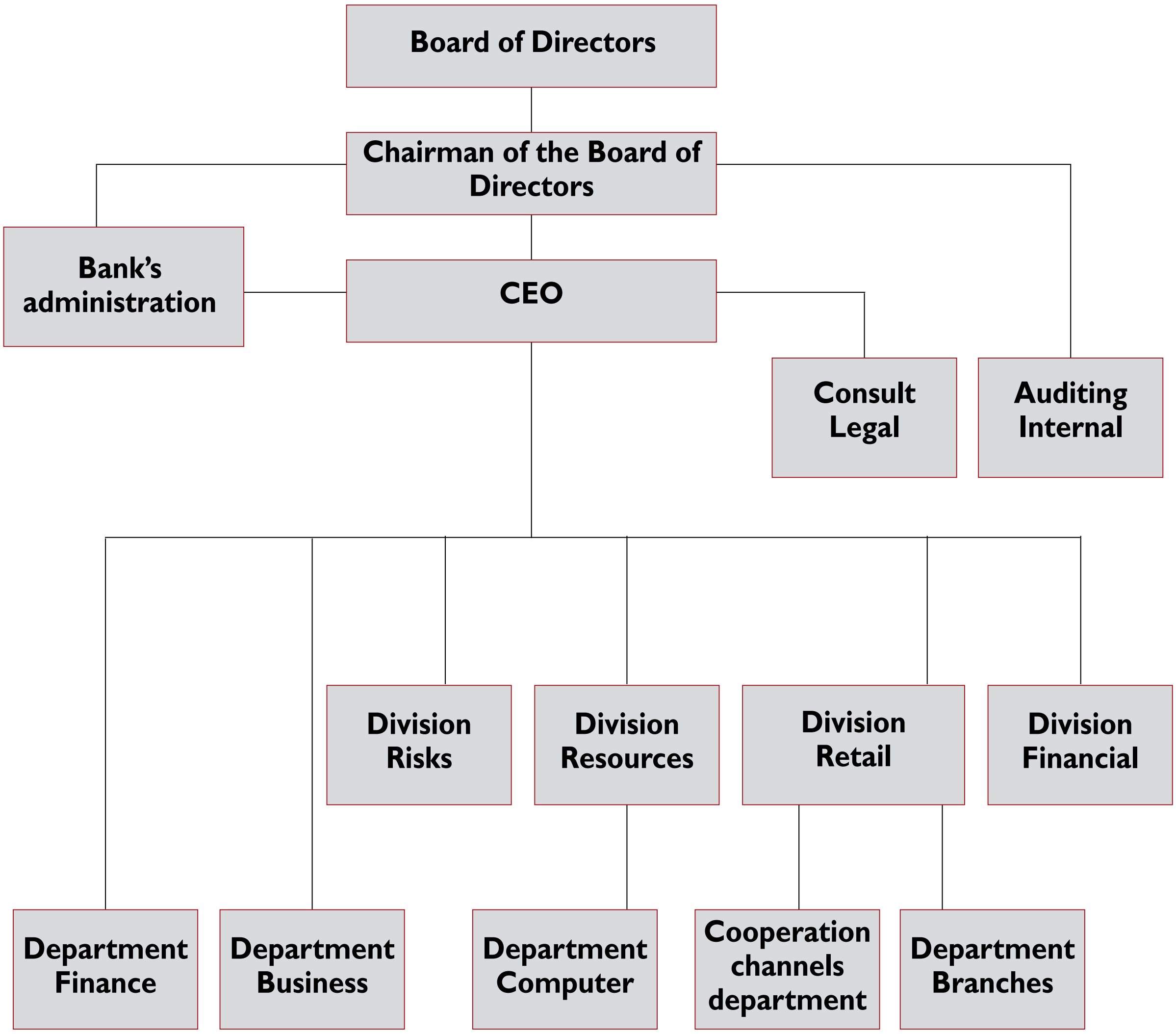
Investment in computerization (in millions of NIS)



Human Capital

Structural Diagram of the Organization Structure

Below is a Diagram of the Bank's Organization Structure:



In 2012, a change was made in the Bank's division structure in which a retail credit division was created under which the Bank's retail credit and commercial activity was centralized. In contrast, the cooperation channels division was canceled, with some of its activities being reassigned to the Sales Furthermore, the real estate sector department was placed under the direct auspices of the CEO. The purpose of the change was to strengthen the Bank's management capability by creating clear specialization lines and more efficient control span in organizational management.

On December 12, 2012, Mr. Asher Ben David, the manager of the Retail Division, and second to the CEO, retired, and as of the date of this report, the CEO of the Bank actually holds this position as well. On December 12, 2012, the Bank's Board of Directors approved the appointment of Mr. Yisrael Boker as deputy managing director and Manager of the Retail Division, subject to Bank of Israel approval. The expected start date of Mr. Boker's term is March 1, 2013, subject to Bank of Israel approval.

For details concerning members of the Bank's management and their functions, please see paragraph "The Bank's Management Members," their functions and the periodic report attached to this report.

Personnel Placement (1)

Below are details of the number of personnel in the bank and in its subsidiaries:

	For the end of the year		Annual average	
	2012	2011	2012	2011
Number of employees:	509	463	479	440
Of this outsourcing	46	49	45	43
Number of positions:				
In normal hours	483	453	468	427
In extra hours			19	16

Below details on the expense levels on salaries (cost of salary for employer:

	Number of positions:(2)		Total Expenses
In thousands of Shekels per Year (3)	**Bank employees**	**Outsourcing**	**in millions of Shekels**
up to 100	7	17	1.6
above 100 until 300	267	12	56.2
Over 300	149	16	81.8
Total salaries	**423**	**45**	**139.6**
With addition of expenses not included in salaries			3.1
Less salaries and accompanying expenses that were capitalized			(4.9)
Total salaries and accompanied expenses			**137.8**

(1) In this report the section on Bank Personnel also includes managers who provide their services through the management company controlled by them. The paragraph "Outsourcing" includes workers employed through employment agencies, software houses, and other companies providing services to the Bank, from whom certain workers for specific positions are hired.

(2) Including employees according to 100% position. Employees in part-time jobs have been merged.

(3) The division into groups was based on the annual cost per employee assuming a 100% position.

For details concerning division of personnel by various sectors of activity, see paragraph "Financial Data by Sectors of Activity" in this report.

During 2012, according to the Bank's Strategic Plans, employee placement increased, mainly in the branches in order to staff new branches and reinforce existing branches. In addition, employee placement in the bank's contact center and front system was increased. During 2013, according to the objectives as set by the work plan, the Bank intends to recruit about 28 new employees. These employees are expected to fill positions in new branches the Bank intends to open during the year, and to increase the existing branches as well as the back-office system that will continue expansion of its activities and its support of business activities.

The information detailed above is "future facing information" that may not be realized in whole or in part or may be realized differently from expectations. This information is based on the assessment by the Bank's management concerning implementing of the Bank's annual work plan. These assessments may not be realized, among others, as result of economical events, political/security-related events, ability to realize the Bank's programs according to the objectives determined in accordance with its strategies, unexpected responses by additional factors (customers, competitors, etc) operating in the bank's business environment.

Rotation

The Bank operates according to the Proper Banking Procedures instructions on the issue of rotation, and considers the rotation of sensitive functionaries an important component in the organization's internal auditing procedures. In the event that mobility between positions does not exist, the Bank implements compensating controls.

Training

The Bank provides regular guidance and professional training to its employees in accordance with the employee's position and the Bank's requirements. The year 2012 was characterized by professional strengthening of the existing system and training activity in the current accounts and consumer credit areas, while accepting and training new employees.

In preparation of the launch of the CRM system in 2013, training of the headquarters representatives and branch arrays has started.

In 2012, the Bank's training focused on training the branch arrays, the call center, and backup system for the support of new business objectives issued by the Bank's management. The training in the core area includes, inter alia, current account training and consumer credit, training for credit officers. Furthermore, the Bank began training for video conference bankers while acquiring knowledge in various professional subjects and individual skills in services and sales. In addition to the aforementioned, training is given in the risk management channel (money laundering, operating risks, arrears controls management, compliance and administrative enforcement).

In the area of soft skills, comprehensive training was given to improve the sales skills of banker operations with customers (branch arrays, representatives in call centers). Branch managers received personal training and exercise with an emphasis on sales management. We note that in 2012, a comprehensive training program was provided for management of select employees.

During 2012 the bank provided 2,364 training days at a cost of NIS 964 thousand (NIS 741 thousand of which for instruction and sales training) compared to 2,588 training days at a cost of NIS 937 thousand in 2011.

Employee Compensation Policy

In 2010, the Bank 's Board of Directors approved a compensation plan for employees and management members (except for the CEO) that establishes parameters and threshold criteria for receiving annual bonuses (hereinafter: "the Plan"). The Plan was accepted in accordance with Bank of Israel instructions on employee compensation.

Should the Bank meet the threshold for bonus payments, as set by the Plan, the employees, including management members, will be entitled to annual bonus payments according to rating, as follows (data in thousands of Shekels):

Yield calculated	Bonus sum for employees		Bonus sum for management members		Total Bonus sum for employees and members of Management	
(as defined below)	starting with	until	starting with	until	starting with	until
8.5%-9%	1,200	1,200	-	-	1,200	1,200
9%-10%	2,900	4,500	400	700	3,300	5,200
10%-11%	4,500	6,000	700	950	5,200	6,950
11%-12%	6,000	7,250	950	1,500	6,950	8,750
12%-13%	7,250	8,500	1,500	2,000	8,750	10,500
13%-14%	8,500	11,000	2,000	2,700	10,500	13,700
14%-15%	11,000	13,000	2,700	3,300	13,700	16,300
15%-16%	13,000	15,000	3,300	4,500	16,300	19,500

It should be mentioned that in the event the Bank will, in a certain year, not comply with the established threshold, a sum of NIS 800 thousand will be allocated for paying bonuses to select employees.

The threshold for receiving the bonus, two situation have been defined:

a. Before the Bank's Board of Directors approved the project (as determined below) or after the Board of Directors determined that the project becomes accounting profit – the minimum reporting yield (as determined below) shall be higher than 8.5%.

b. After the Board of Directors approved the project and before the Board of Directors determined that the project becomes an accounting profit – The minimum reporting yield that will be higher than 5% (in case the reporting yield was higher that 5% but did not reach 8.5% only the relative part of the bonus will be distributed derived from the above table).

“Calculated Yield” is defined as the “Reported Yield” (as defined below), neutralized by the capital share that is tied up by the project activity (as stipulated below) (for this purpose, capital tie-up is defined as the required capital based on the capital adequacy requirements for risk assets that are managed as part of the project) and neutralized by (1) project expenses and income (as defined below); (2) tax shelter that will be formed as a result of the project; as will be recorded in the bank’s books. The mode of neutralizing the project’s income and expenses and tax shelter that will be formed as a result of the project, will be examined and approved by the Bank’s Board of Directors or its committee based on the opinion that will be submitted, every year, by an independent outside auditor whose identity was defined in the Plan.

“Reported yield" means the average between the annual yield (net) on equity as reported in the Bank’s annual audited Financial Statements and between the growth rate in the Bank’s equity as reported in the Bank’s annual audited Financial Statements. A dividend announced and paid during the year and capital issuances if there were any, will be neutralized for the purpose of growth calculation in equity (meaning, it will not be taken into account for the purpose of calculating the equity growth rate). In light of the Reported Yield calculation, the effects of non-recurring profits will be neutralized (it is clarified that the activity that is in the financial characteristics, such as the nostro account, will not be considered a one-time activity) and capital gains (with the exception of profit that may derive from the sale of a certain land asset). To remove any and all doubt, the Reported Yield will be after taking into account the expenses for payment of grants to the CEO, to members of management and to employees, and after taking into account the expenses for options to the CEO and to management members (and to any other party, if any), as will be recorded in the Bank’s books. The mode of neutralizing said components will be examined and approved by the Bank’s Board of Directors or its committee based on the opinion that will be submitted, every year, by an independent outside auditor whose identity was defined in the Plan.

In the Plan, “project” was defined for the setup and operation of new retail banking for the Bank; further defined was “Project Expenses and Income”, which will be in accordance with the project’s activity expenses in the grant year, so that at least 75% of said expenses and income, according to the matter, is derived or related, directly or indirectly, to the project. It is hereby emphasized that if at least 75% of said expenses or income is derived from or related to, directly or indirectly, the project, 100% of these expenses or income will be attributed to the project.

It is noted that the bonus calculation conforms to the aforementioned, will be done in a linear manner and pro-rata, between the above specified ratings, within the set boundaries of these ratings. Furthermore, the bonus level is limited to 8 salaries for bank employees and 12 salaries for Management.

The bonus will be paid on dates and terms as determined by the plan. It should be mentioned that, according to the plan, the bonus for management members will be paid in stages over three years from the eligible date (60% per eligible year and 20% for one and two years after the eligible date), while the payment of each part of the annual bonus depends on continuous compliance with the objectives in the year determined for payment.

The actual payment of the annual bonus depends therefore on the year in which the payment should be implemented, that there will be no regulatory limitation and/or capital adequacy limit on dividend distribution at a rate of at least 33% from the net profit in the payment year for the Bank's shareholders. As far as the aforementioned limitation is applied on dividend distribution, the bonus payment will be deferred, in whole or in part, to a date on which the aforementioned limitation is removed. In the event of partial payment capability of dividend, the dividend will be paid pro-rata to the shareholders and the bonus, for the aforementioned limitation rate, and the payment of the bonus balance will be deferred to a date on which the regulatory and/or capital adequacy limitation is removed.

It should be noted that in accordance with the compensation plan for Management, at this stage, in accordance with the regulatory instructions for banks, this section will not be implemented.

The payment of the bonus according to the plan is conditional for at least six months of employment at the Bank, and actual employment on the day of bonus payment. Nevertheless, the Bank's CEO in relation to the employees, and the Bank's Board of Directors in relation to management members, have exclusive discretion to approve bonus payments also in the event in which the employer employee relation is terminated, prior to the bonus payment date and to stipulate conditions, as seen fit.

The Bank’s Board of Directors will examine whether to increase the bonus ceiling while paying attention to the labor force, total profit, profitability, risk profile, and so forth.

On November 12, 2012, the Knesset passed Amendment No. 20 of the Companies Law 5773-2012 in which public companies were required to appoint a compensations committee and establish compensation policies for officers. The Bank has a compensations committee whose composition complies with the provisions of said Amendment. In addition, the Bank is examining its compensation policies and will act in accordance to comply with the provisions of the Law.

For details concerning the CEO’s compensation and the Board of Directors, see Note 22 of the Financial Statements.

Description of Employment Agreements

About 50% of the Bank's employees are employed under personal employment agreements, that arrange the employment terms at the Bank. Once a year the update of their terms of employment are examined according to the employee’s differential contribution to the bank, as well as recommendations by his managers. The personal employment agreements are signed separately with each employee, according to the salary and social benefits arrangements as individually agreed with them at the time of recruitment.

The employment terms of about 50% of the Bank's employees are arranged under an agreement signed with the Bank’s Employees Committee for arranging the employment terms and their salary increments (hierarchical employee agreement). This agreement has the status of a collective agreement. Every two years the agreement is updated with the consent of the employees committee through an additional letter signed by the management and the Employees Committee. This update includes salary increases in respect of the basic salary and related expenses, and takes into consideration the increase of Consumer Price Index for the update period. In addition, the bank also holds annual personal rating negotiations with the aforementioned employees. The aforementioned arrangement is also applied on part of the employees who are the Bank's approved signatories and are included in the population of rank employees, except for the fact that salary due to their signing authority, they are eligible for an additional increment.

Retirement arrangements – retirement terms for employees with personal agreements are included in their employment agreement.

Employees of subsidiaries are employed according to the Bank's employment terms.

In addition, the Bank and its subsidiaries purchase services from employment agencies and software houses (for details see "Outsourcing Workers" in the above table).

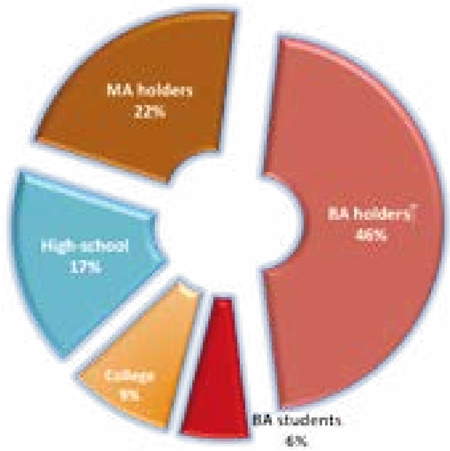
Development of Human Resources

The Bank places emphasis on value investment in its personnel, concurrent with developing employees and human resources.

In addition to specific integral training dealing with the Bank's core business and risk management, the bank encourages its employees to participate in academic studies and external training in the areas that touch upon their activity areas. Moreover, the Bank sends its employees to courses, seminars and professional conferences that touch upon banking industry.

During the last quarter of 2011, candidates for a management training course were identified following a meticulous screening process. During 2012, the course took place and combined workshops for developing personal skills, professional instructions and personal training by an external moderator.

At present, the Bank recruits mainly academic personnel. As of the end of 2012, 68% of the Bank's employees possess an academic degree, of them, 22% have a master's degree and 7% are studying towards a master's degree. A total of 83% of the Bank's employees possess a high school education or higher, and 6% are studying towards their bachelors degree.



The Bank also encourages mutual support between its employees, and established a mutual fund between the Bank and its employees for supporting employees in financial distress.

Senior Officers and Approved Signatories

As at December 31, 2012, 12 officers serve in the Bank. Of these, 11 are employed under personal agreements, and another one is under a service provision agreement through management companies controlled by them and with approval of the Bank of Israel, and 175 authorized signatories, 92 in branches and 80 in headquarters.

Taxation

General

The bank is defined as a "financial institute" for purposes of the Value Added Tax Law - 1975, and as such is subject to payroll tax and profit tax on its activities according to the rates determined in the VAT Act.

According to the VAT Order (Tax Rate on Non-Profit Organizations and Financial Institutions) (temporary order), 5769 - 2009, which was approved by the Knesset in December 2010, the Income Tax Rate applied on the financial institutions will be 16% between 2012-2010.

In August 2012, the VAT Order (Tax Rate on Non-Profit Organizations and Financial Institutions) (Amendment), 5772 - 2012, which was approved by the Knesset in December 2010, determined that the Income Tax Rate that applied to financial institutions will be 17% of the generated profit. The provision concerning tax on profit in 2012 will apply to one-third of the products in that year. The said order canceled the temporary order.

On December 5, 2011 the Knesset enacted a change in the law of the tax burden (Legislative), 5771 - 2011 (hereinafter: the Law). As of 2012, as part of the law, among others, the outlining of the decrease in corporate tax rate is canceled. As part of the law the corporate tax is also increased to a rate of 25% as of 2012. In view of the increase of corporate tax to 25% as aforementioned, the tax rate of real capital gain and the real credit tax are also gradually increased.

Listed below are the statutory tax rates that apply to financial institutions, including the Bank:

year	Corporate tax rate	Profit tax rate	Total tax rate
		%	
2010	25	16.00	35.34
2011	24	16.00	34.48
2012	25	16.33 *)	35.53
2013 and henceforth	25	17.00	35.90

* Weighted rate

Assessments

The bank issued final assessments until and including the year 2007. For its two subsidiaries, final tax assessments have been issued until and including the fiscal year 2005. The tax assessments for subsidiaries until and including the year 2008 are considered final.

The current and deferred taxes are calculated according to the new tax rates.

Restrictions and supervision of the activity of the banking corporation

The Bank has a bank permit, according to paragraph 10 of the Banking Law (permit) 5741 - 1981. According to the permit, the following limitations are applied on the Bank: the Bank may not control and may not be an interested party in entities of any type, in Israel or abroad, except auxiliary corporations, to a certain corporation or to a type of corporation, without the Supervisor's approval. The aforementioned will not be applicable to corporations held by the Bank according to relevant legislation immediately prior to receipt of the license, and such holding is according to the determined conditions.

Moreover, appointment of the Chairman of the Board of Directors and the Managing Director is subject to advance written approval from the Supervisor of Banks.

It is clarified that license requirements concerning control in auxiliary corporations and approval for appointing Chairman and CEO, are requirements included nowadays in the banking enactment and relate to all the banking corporations.

The Bank of Israel informed the Bank that it may carry out options and spot transactions between currency rates or interest rates solely for the purpose of hedging. Transactions that are not for the purpose of hedging require the prior approval of the Bank of Israel.

According to the announcement submitted by the Bank to the Bank of Israel, the Trust Corporation of Bank of Jerusalem Ltd., a wholly owned subsidiary, implements the customers' instructions without exercising discretion.

Licenses For Activities of Subsidiaries

Ir Shalem Insurance, the Bank's wholly owned and controlled subsidiary, has an corporation insurance agency license according to the Law for Supervision of Financial Services (insurance), 5741 - 1981. In accordance with the relevant instructions by the Supervisor of Insurance and the Supervisor of Banks, Ir Shalem is entitled to engage only in marketing of life and property insurance policies, resulting from housing loans granted by the Bank (this limitation does not apply to insurance made before January 1, 2006).

Jerusalem Investment Portfolio Management Ltd, the Bank's wholly owned and controlled subsidiary, has a license from the Securities Authorities for managing portfolios. The Company's portfolio management activities were sold on January 7, 2013. For more information, see above the Chapter on Events After the Balance Sheet Date

General

The Bank is a commercial bank, a public company whose shares are traded on the Stock Exchange in Tel Aviv Ltd., member of the Stock Exchange in Tel Aviv Ltd., member of the Clearing House and Derivatives Clearing House and thus all the relevant laws apply to it.

The Bank's activities are subject to laws, standards and instructions that are partly unique for the banking system, and partly, even if not unique as mentioned, influence material sections of its activities. Bank deposits, different banking laws, and proper banking management instructions that are periodically published by the Supervisor of Banks, are the legal and central basis of the Bank's activities. These determine, among others, the allowed activity boundaries of the Bank, relationships between the Bank and its customers, usage of the Bank's assets, manner of reporting on the aforementioned activities to the Supervisor of Banks and the public and the allowed activities of the Bank's subsidiaries, and the terms of control and capital ownership.

Besides them, the Bank is subject to extensive legislation that regulates the Bank's activities in the capital market for its customers as well as for itself (e.g. in the area of investment consultancy and managing customer portfolios, Securities Laws, and limitations on activities in the insurance area).

Bank commissions, including those of the Bank of Jerusalem, are supervised by the Bank of Israel. Moreover, the Bank of Israel determined a fees schedule that includes a list of the services for which banks may charge commissions and the method for calculating such commissions.

Additional laws, on unique subjects, imposed of banks, on the Bank included, specific obligations and rules. For example, the enactment in relation to the prohibition of money laundering, the prohibition of financing terror, law for provision of credit, enactment in relation to housing loans, collateral laws, etc.

In addition to these, there is an enactment, that due to its connection to the Bank's activities, has great affect upon its conduct. On this issue, among others, the execution proceeding office law, liquidation and receivership laws, and various tax laws should be mentioned.

The activity of the Bank is under the supervision and control of the Supervisor of Banks, as well as other factors in this specific activity area; for instance, Securities Authorities, Commissioner on Capital Market, Insurance and Savings at the Ministry of Finance, and the Anti-Trust Commissioner.

The Bank and its subsidiaries operate in order to comply with obligations applied on them by provision of law.

In the framework of the legislation, in most of the laws applied on the Bank’s activity is the possibility of imposing financial sanctions due to violations of legal instructions and secondary legislative instructions (including circulars and guidelines) issued for or excluded from enforcement.

Below are, in summary, details of legislative changes (including instructions by the Supervisor of Banks) relevant to the report period that influence or may influence in a material manner the Bank's activity (for relevant legislative changes for the report period that influence or may influence the activity of activity sectors, please see reference for each sector separately):

The Banking Act (Legislative Amendment) 5772-2012

On March 12, 2012, the Knesset approved The Banking Act (Legislative Amendment) 5772-2012 The law includes amendments to the Banking Ordinance (Licensing) and the Banking Ordinance and is primarily designed to supplement the arrangements set forth in these laws in the manner in which candidates are proposed to serve as directors in the banking corporation without a control core, appointments and terms, in order to prevent actual control of a banking corporation without a control permit from the Bank of Israel. Most of these amendments are not relevant on the date of the report to the Bank, in light of the Bank having a control core.

In addition, the law includes several amendments that apply to all banking corporations that are public companies, such as the prohibition of banking corporation directors to appoint directors to the Board of Directors, amendments to the Fit and Proper process, the requirement to publish a preliminary immediate report concerning the intention to publish a convening of the General Assembly concerning appointment of directors, etc.

Proper Banking Management Instruction № 350 on the Issue of Operating Risk

On February 14, 2012, the Supervisor of Banks published Proper Banking Management Instruction № 350 on the issue of Operating Risk Management.

In the instruction the basic principle for Operating Risk Management is determined while referring to corporate governance issues and the risk management environment including reference on the issue of control and decrease in operating risk.

The instruction will be effective from the 1st of January 2013. The bank implements the instruction of the Supervisor.

Legislative Proposals

From time to time, proposals for legislative amendments on various issues are brought before the Knesset. Some of them may affect the business of the banking corporations including the Bank. As of the date of the Financial Statements there are a number of legislative proposals in various stages of enactment. The legislative proposals are designated to increase the supervision and arrangements of customer bank relation, to arrange the work of the directors and more. Nevertheless, as of the date of the Financial Statements, these proposals are in various enactment stages. There may be changes, and there is no certainty when they will be completed and finally become obligatory legislative instructions.

Material Agreements

For a summarized description of the material agreements, not in the regular course of business of the Bank, as well as relevant cooperation agreements for activity sectors, that were signed and/or that are valid for the reporting year, please see details in each of the sectors.

Agreements with suppliers for establishing multi-channel computer infrastructure

In April 2011, Tomer entered an agreement with Teldor Computer Systems (1986) Ltd., according to which Teldor will establish and integrate a multi-channel computer infrastructure for managing the Bank's customer relations. As of the report date, most of the project content was carried out and with the uploading of the website, which is expected to occur in the second quarter of 2013, the project will come to its conclusion. Accordingly, the parties agreed to conclude the agreement concerning the project.

Providing liability for indemnification of senior officers at the Bank and its subsidiaries

In January 2012, the Bank's General Assembly of shareholders approved the decision, according to which the Bank will grant somebody serving from time to time as senior officer at the Bank and its subsidiaries, indemnification liability due to financial debts imposed on someone and for reasonable litigation expenses related to the list of events attached as appendix to the letter of liability. Provision of indemnifications depends on the existence of conditions specified in the liability letter and the maximum indemnification amount per senior officer of the Bank and its subsidiaries, as accumulated and not exceeding 25% of the Bank's equity.

Legal Procedures

For information on the issue of legal procedures see note 19c of the Financial Statements.

Risk and Risk Management Methods

Discussion on Risk Factors

The activity of the Bank as a financial intermediary exposes it to a variety of financial risks, including credit risks, market risks and liquidity risks. Moreover, the Bank is exposed to accompanying risks, that are not financial risks derived mainly from operating risks, from legal and strategic risks. The risk management policy in various areas is used for supporting supervision of business objectives while limiting the risk exposure involved in various activities.

The activity and profitability of the Bank are exposed to changes in the business environment, affected by the economic situation, by developments in real estate and capital markets, and by regulatory changes. An economic slowdown or possible crisis in the real estate market and/or in the capital market may affect the Bank's activity, in general, and its activity in the housing loan and real estate sectors, in particular.

Below are described the main changes in business environment that may affect the Bank's activity and profitability:

1. The development of the financial crisis in Israel, and a deepening of the economic slowdown, may affect the repayment ability of the Bank's borrowers; on increasing the scope of arrears of borrowers due to deterioration of their repayment ability; and on the Bank's ability to raise capital and the margins of its activity.

2. Incorrect forecasts and faulty estimations, unexpected responses from factors (customers, competitors and more) operating in the Bank's business environment , late recognition of market trends, changes in consumer preferences and/or conduct, changes in the banking system and/or its regulation and affect of the above on the branch's competitive structure, lack of monitoring the realization of multi-year objectives – realization of each of the above different than expected being at the base of the Bank's strategic plan, may harm the Bank's margins and expected revenue, and prevent it from implementing the plan.

3. Significant changes in the residential real estate market may affect both the value of collateral for credit provided by the Bank and the increase of provision for credit losses as well as on the credit scope provided to households against a lien on their residence. These changes may even affect the credit provided for projects accompanied by the Bank.

4. Tangible damage in real estate assets used as bank collaterals for provided credit, for example diminished value as result of war or destruction of buildings are result of a natural disaster, may, in case of lack of full insurance coverage, diminish the repayment capability and cause an increase in the extent of problematic debts. Extensive damage as aforementioned may cause the development of economic crisis and deepening of the recession.

5. Change in recovery from the crisis in global financial markets and/or its deepening, may affect the repayment ability of foreign resident borrowers, reducing demand for new credit to finance the purchase of residential property in Israel, and affecting the ability to raise resources to finance foreign currency activity.

6. The slowdown in the capital market might influence the bank's possibilities for raising resources for the bank by means of negotiable issuances. Moreover, the slowdown in this market may affect the bank's activities in the capital market.

7. The increase in interest rates might increase the repayment of the borrowers burdened with loans with variable interest and may therefore affect the insolvency probability of these borrowers.

8. Future realization of the market's macro-economic forecasts in a manner different than the bank's assessments concerning these forecasts (sample of exceptional and unexpected increase of the real interest) may affect the results in the financial management sector and the fair value of the Bank's securities portfolios.

9. Material, sudden and unexpected deviation from the macro data (e.g., explosion of uncontrolled inflation, increase in exchange rate of the dollar at an exceptional rate) may cause an unexpected increase of risk assets, and prevent the Bank from implementing its work plans.

10. Changes in regulatory instructions and also possible results of legal procedures may affect the banking system's scope of activity, the competitive structure therein, and/or the Bank's profitability.

11. Damage to the Bank's image and decline in the Bank's credit rating may damage the Bank's profitability due to curtailment in its activity scope and increase capital recruitment cost and liquidity because of a rating decline.

12. Operating risks, that may be expressed, inter alia, in failure of information systems that do not have proper control, or an embezzlement and fraud event, as well as damage to information security, because of the increase in the scope of electronic business, refinement of financial activity and complexity of products and technologies.

13. Increased threats to information security in relation to computer technology and primarily cybernet incidents that might occur from an intentional attack or unintentional events.

The information detailed above is "future facing information" that may not be realized in whole or in part or may be realized differently from expectations. This information is based on estimates by bank management concerning future realization of industry forecasts and macro-economic forecasts according to the bank's preliminary estimates. These estimates may not be realized, among others, as a result of economic events, political/security-related events, changes in customer preferences, and increased competition.

The Bank's risk management is implemented continuously, according to instructions from the Bank of Israel and according to the rules determined in the second tier instructions of Basel II. In this framework the Bank appointed a Risk Manager for each of the material risks as listed below, and a Chief Risk Manager (CRO), serving as Vice President and Manager of the Risk Division.

The Supervisor of Banks published various directives in the framework of Proper Banking Management on the issue of risk management by banks, including Basel II instructions. The bank integrated a work framework for risk management and control, and adjusts the policy of the bank for managing various risks to the principles appearing in the instructions of Basel II.

Factors involved in risk management

Risk management in the bank is spearheaded by the Chief Risk Director (also a Management member) and the bank's Manager of the Risk Management Control Division. For each of the various risks, a management array is determined, including a supervision circle and three control circles, according to the details of the following entities below:

The supervisory tier contains supervisory entities – Board of Directors, designated Board of Directors committees, and senior management.

Board of Directors – has the responsibility foe determining the Bank's business strategy, including in risk management and securing the Bank's capital. The Board of Directors is responsible for determining the risk tolerance and the Bank's appetite for risk, among others, through defining the scope of the Bank's exposure limitation for risks and risk management. Moreover, the Board of Directors is responsible for verifying the functional adequacy of the Bank's risk management; to approve principle internal methodologies of recognition, valuation and management of risks, and for the calculation of the required capital; performing control and supervision on applying policies determined by it.

Quarterly, the Board of Directors discusses the central risks exposure document presented by the Bank's Chief Risk Manager of the.

The Board of Directors appointed a Board of Directors' Committee for risk management, that has among its functions discussions and recommendations to the Board of Directors on everything related to plotting and approving of the Bank's policy in risk management; examination of risk management procedures, and the level of adjustments to the policy framework approved by the Board of Directors; supervision over implementation of risk management policies determined by the Bank's Board of Directors, including receiving reports on deviations from policies or limitations determined by the Bank's Board of Directors. In addition, the Board of Directors' committee discusses and approves new significant products and/or procedures at the Bank according to the recommendations by the relevant internal forums headed by the Bank's CEO.

The management – committed to manage the risks according to policies, appetite for risk, and the limitations determined by the Board of Directors. The management, headed by the CEO, is responsible for the implementing the risk management policies, realization of controls, supervision over quality of risk management, and adequate risk measurement and assessment. In addition, management is responsible for creating an effective system for risk management and their control. The management operates through designated committees for management of various risks, as well as through the Risk Division headed by the Chief Risk Manager.

Description of Control Circles

First Control Circle – This circle includes the risk-takers and managers, which constitutes the business and operational function, making business decisions involving risk-taking. The controls implemented under the framework of the ongoing activity, by the business factors, include a variety of activities, including: compliance with policies and procedures, complying with limitations, and reporting to the senior management and the Board of Directors.

Below are details of risks and management members and department managers serving as risk managers:

Type of risk	Risk Manager
Credit	Manager of the Retail Credit Division
Business credit in the real estate area:	Manager of the Real Estate Sector
Market	Manager of Financial Division
Liquidity	Manager of Financial Division
Operating	Manager Risk Division
Operating - Information System	Manager Resources Division
Strategy	CEO (*)
Legal	Legal consultant
Regulatory	Legal consultant
Reputation	CEO (*)
Compliance	Compliance Officer
Money Laundering and Terrorism Financing	Party responsible for implementing the Prohibition against Money Laundering and Terrorism Financing Law
Clearance and other party	Manager of Financial Division
Environmental	Manager of the Real Estate Sector
Human Resources	Manager Resources Division
Administrative enforcement	Manager Risk Division

(*) On December 12, 2012, the retail division manager, Mr. Asher Ben David, retired. He served as Strategic Risk Manager and Goodwill Risk Manager until that time. At this stage, the CEO serves as Strategic Risk Manager and Goodwill Risk Manager.

Second control circle – this circle includes the risk management functions used as control factor of the management and is non- contingent on risk creators, as well as the credit and financial risk controls headed by the Chief Risk Officer. The processes involved in this circle of control include, among others: outlining risk management policy (in conjunction with the business function), identification and independent measurement of levels of exposure to risk, examination of the existence of proper work processes, validation of the models, examination of compliance with the limitations set forth in the various policy documents and reporting if levels of exposure, as well as deviations from the policies of the Bank and managers to the relevant parties.

Chief Risk Manager – According to the instructions by the Bank of Israel, and according to the framework outlined in the second tier of Basel II, the Bank appointed a Chief Risk Manager for the Bank (CRO). As of August 1, 2011, Mr. Michael Ben-Ischai serves as manager of the Bank's Risks Division and as Chief Risk Manager. The role of the Risks Management Division is to strengthen the Bank's capability to understand the total risks the Bank faces and ensuring their cautious management. The instructions of the Bank of Israel define the operating principles for the Chief Risk Manager and risk management functions, and specifies their position, their function, and areas of responsibility.

The purpose of the CRO's function is to create a wide and cross-organization view of the overall risks inherent in the Bank's activities, among others, through creating a risk management culture influencing all the Bank's activities.

Under the responsibility of risk management functions and its head, is to provide, directly and indirectly, to the Board of Directors and its senior managers, all the relevant data for the proper supervision of the Bank's risk profile in such a manner that it assists in directing the Bank's activities.

The third control circle – this circle includes, inter alia, the internal audit that examines the validity of the activity and processes that are being carried out by the bank, its subsidiaries and its ancillary corporations, including: A review and assessment of the due diligence and effectiveness of the internal control framework and the manner in which the offices and authorities are performing their roles. A review of transactions as well as a review of the activity and role of specific processes in internal control. A review of implementation and effectiveness of the risk management procedures and risk assessment methodologies. A review of the resources for protecting the Bank's assets. A review of the various information systems, including: business and operating information systems, information systems used for managerial and financial purposes, as well as reporting systems. Electronic information systems and communications banking services. A review of due diligence of internal control frameworks in the financial reporting generation process. A review of the precision and reliability of the accounting records and financial reporting. A review of the reliability and timing of the reports to regulatory authorities and other authorities. A review of the systems to ensure compliance with laws, regulatory requirements and behavioral rules as well as implementation of Bank policies and procedures. An audit of current implementation of the decisions of the Board of Directors and management as well as senior management activity. A review of capital assessment vis-à-vis assessment of the risks entailed in the banking corporation activities. Implementation of tests and special investigations.

Capital Adequacy

General Background

On June 20, 2010, the Bank of Israel published Proper Banking Management instructions dealing with measurement and capital adequacy. The instructions define the method for calculating capital adequacy and are based on the Basel committee recommendations on the issue of international Convergence for Measuring Capital and Capital Regulations (Basel II) that was published June 2006.

The Basel II recommendations are divided into three sectors:

First Tier – Minimum capital requirements for credit risk, market risk and, for the first time, also for operating risk.

Second Tier – The ICAAP process an supervising survey process (SREP).

Third Tier – Market compliance.

The first Tier enables, for purposes of calculating minimum capital requirements, several approaches for measurement of risk components for credit risks, market risks and operating risks: the Standardized Approach or more sophisticated approaches, based on internal models of customer ranking and relevant operating risks. The sophisticated approaches are subject to specific approval by the Supervisor of Banks. In these reports, similar to all banking systems, the capital adequacy data were reported according to standard presentation principles in Basel IIas integrated in the Proper Banking Management instructions 201-211.

The second Tier emphasizes integrated risk management. Under this, the banks are required to determine methodologies, processes, and procedures intended to ensure long-term capital adequacy, including examination of all significant risks to which each bank is exposed. The banks are required to prove implementation of the required methodologies for ensuring capital adequacy. The Supervisor of Banks is required to evaluate these procedures, and to levy supervisory means insofar as required for evaluation results.

Tier Three relates to the level of transparency and requirements for disclosure in reporting to the public by banking corporations, to supplement the second sector. These requirements are intended to assist entities utilizing the financial statements to evaluate the bank's capital adequacy and the addition data concerning the bank's capital, as presented in the reports, the exposure to various risks and the evaluation processes.

In June 2011, the Basel committee published recommendations on the issue of "Framework of Global Supervision to Strengthen the Banking System's Durability" that received the name Basel III. Among others, the recommendations included the requirement to increase the ratio of the minimum equity tier 1 (core capital) from 2% up to 7% (4.5% minimum capital ratio and additional 2.5% cushion of capital preservation) in 2019. The recommendation also included new requirements in the area of liquidity risk management (in January 2013, the Basel committee updated the recommendations on liquidity), defining additional capital cushions (counter-cyclical cushion and specific cushion against systemic risk), requirement for leverage ratio management, and more. The committee further recommended that capital instruments in Tier 1 be required to include a mechanism for absorbing losses, and that instruments than do not comply with the new conditions will be gradually reduced from the capital.

On December 30, 2012, the Bank of Israel published an updated Proper Bank Procedure draft that adopts the BaselII and BaselIII recommendations in Israel's banking system (Proper Banking Procedures 201-211).

The draft banking procedure set forth that banking corporations and credit companies must:

- Comply with the minimum Tier 1 equity ratio (core capital) for weighted risk assets of 9% for the entire banking system beginning on January 1, 2015, and for a banking corporation whose total balance sheet assets on a consolidated basis is equal to or exceeds 20% of the total balance sheet assets in the banking system to comply with a minimum total capital ratio of 10% beginning on January 1, 2017.

- To comply with the minimum equity ratio for weighted risk assets of 12.5% for the entire banking system as of January 1, 2015, and for a banking corporation whose total balance sheet assets on a consolidated basis is equal to or exceeds 20% of the total balance sheet assets in the banking system to comply with a minimum total capital ratio of 13.5% as of January 1, 2017.

In addition, criteria were established for the competency of Tier 1 equity, additional Tier 1 capital and Tier 2 capital. Furthermore, temporary provisions were established that refer to supervisory adjustments and deductions from capital as well as capital instruments that are not suitable for inclusion in the supervisory capital in accordance with the new established criteria.

The Bank conducted a survey of the quantitative effect of the transition to the Basel III protocol. According to the results of this survey, the transition to the Basel III protocol reduces the Tier 1 equity adequacy ratio by 0.2%.

The ICAAP and SREP Procedures.

On May 10, 2012, the Bank's Board of Directors approved the internal process for adequate capital assessment – ICAAP – Internal Capital Assessment Adequacy Process for December 31, 2011. The ICAAPis an ongoing process by which the Bank recognizes and handles risks embedded in its activity, examines the required capital for support of these risks and verifies that the provided capital exceeds this requirement. Building this process at the Bank is a central part in the preparation of the Bank for the requirements of Basel II, and the requirements of the Bank of Israel for implementing the second tier of these instructions.

The Bank's financial statements data, the calculation of the risk assets and capital adequacy ratio for December 31, 2012, are calculated and presented in compliance with the directives required in accordance with standard rules for submission in Basel II. The capital adequacy ratio for risk components at a rate of 14.4% and core capital ratio for risk components of 9.7% (Basel II) that are presented in the statement for December 31, 2012 cover according to bank assessments the capital required for Tier 1 and Tier 2, including extreme scenarios used by the Bank for its internal assessments. This ratio is higher than the minimum capital ratio required by the Supervisor of Banks

Simultaneous to the ICAAP procedure, the Supervisor of Banks performs the review and evaluation process (called SREP – Supervisory Review and Evaluation Process) under which the Supervisor is required to determine the capital adequacy of a banking corporation and the appropriateness of the ICAAP process in relation to risk exposure (risk profile), taking into consideration the Bank's corporate governance framework. This process will assist the Supervisor to formulate an opinion concerning the appropriate level of capital adequacy, the supervisory measures, and additional risk reducing activity in relation to the Bank's capital adequacy.

Within the confines of the ongoing discussions between the Bank of Israel and the Bank in which issues that arise from the ICAAP and the SREP process are discussed, the Bank received on February 19, 2013 an internal review procedure letter (SREP) of the Bank of Israel. The letter refers to the ICAAP document for 2011 in which the Bank of Israel issued its position on the need to make decisions concerning the long-term core capital objective in relation to a higher ration than that proposed by the Board of Directors.

Furthermore, the letter set forth that the aforementioned decision would be made during discussions on the ICAAP process for 2012, which should end by April 30, 2013.

The Supervisor of Banks issued an interim instruction on the application of disclosure requirements of Tier 3 of Basel II. Below is the table of relationships between exposure requirements in the aforementioned instruction and between paragraphs of the report by the Board of Directors or the note on the Financial Statements in which the required information is included except for the requirements that are not relevant to the Bank (such as the securitization issue):

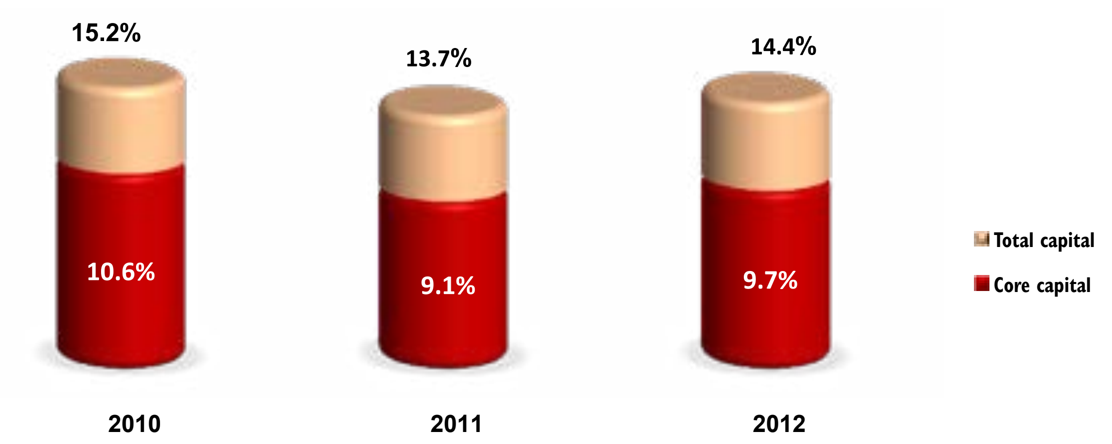
Number of table	Subject	Location	Number of columns
Table 1	Implementation of application	Capital Adequacy	99-102
Table 2	Capital structure	Capital Adequacy Note 16	103 270-271
Table 3	Capital adequacy	Capital Adequacy Note 16 b	103-104 271
Table 4	Credit risk – general disclosure requirement	Credit Risks Appendix E to the Management Review Note 5 Note 18	105-119 190-192 254-259 276-280
Table 5	Credit Risk – Disclosure concerning portfolios handled according to the standard approach	Capital Adequacy Credit exposures to foreign financial institutions	105 118
Table 7	Credit Risk Reduction	Capital Adequacy	105
Table 8	Credit risk of other party	Note 20c Clearance risks and other party risks	289 122-123
Table 10	Market Risk	Market Risks	123-124
Table 12	Operating Risk	Operating Risks	132-135
Table 13	Position of Securities in the Bank's portfolio	Note 4	250-253
Table 14	Interest risk in the Bank's portfolio	Interest Risk	125-127

Below is the calculation for capital ratio according to Basel II instructions:

Capital for the purpose of calculating capital ratio

	December 31	
	2012	**2011**
	Millions of NIS	
Capital Tier 1, after deductions	693.0	644.6
Capital Tier 2, after deductions	338.0	318.6
Total of all capital	**1,031.0**	**963.2**
Average balance from risk assets		
Credit risk	6,452.3	6,395.8
Market risks	148.2	171.6
Operating Risk	553.3	491.1
Total average balance from risk assets	**7,153.8**	**7,058.5**
Capital ratio for risk components		
Capital ratio Tier 1 for risk components	9.7%	9.1%
Total capital ratio for risk components	14.4%	13.7%
Minimum comprehensive capital ratio required by the Supervisor of Banks	13.0%	13.0%

Listed below are the capital ratios for risk components by years:



Below are the balances of the Bank's risk assets in accordance with the first Tier (in millions of Shekels):

Credit risk	Assets risk	Capital requirement
Exposure of sovereignties	5.9	0.5
Exposure of the public sector	0.8	0.1
Exposure of banking corporations	177.1	15.9
Exposure of corporations	1,576.1	141.8
Exposure in collateral commercial real estate	54.0	4.9
Retail exposures for individuals	850.8	76.6
Exposure of small businesses	168.3	15.1
Exposure for housing mortgages	3,452.6	310.7
Exposure for other assets	166.7	15.0
Market Risk	148.2	13.3
Operating risk	553.3	49.8
Total	**7,153.8**	**643.7**

Below is the composition of exposure (according to conversion to credit of off-balance-sheet exposure) by the weight of risks according to the first tier (in millions of Shekels):

Risk Weight	Before Amortization	After Amortization
0%	1,777.0	1,777.0
20%	88.9	88.9
35%	4,485.7	4,484.9
50%	310.7	332.3
75%	3,892.0	3,706.0
100%	2,724.2	2,551.7
150%	89.1	88.6
Total	**13,367.6**	**13,029.4**

Below are the exposure composition and balances covered by collateral and guarantees according to the first tier (in millions of Shekels):

	Gross credit exposure	Risk exposure covered by proper financial guarantee	Risks caused because of guarantees	Additional amounts because of guarantees	Credit exposure net
Debts of sovereignties	1,799.9	-	-	-	1,799.9
Debts of public sector entities	1.6	-	-	-	1.6
Debts of banking corporations	368.5	-	-	21.7	390.2
Debts of securities companies	-	-	-	-	-
Debts of corporations	2,065.1	(151.2)	(21.7)	-	1,892.2
Debts in commercial real estate security	54.0	-	-	-	54.0
Retail exposures for individuals	1,301.1	(46.9)	-	-	1,254.2
Loans for small businesses	369.4	(138.4)	-	-	231.0
Housing mortgages	7,234.7	(1.7)	-	-	7,233.0
Securitization	-	-	-	-	-
Other assets	173.3	-	-	-	173.3
Total	**13,367.6**	**(338.2)**	**(21.7)**	**21.7**	**13,029.4**

Credit Risks

Credit risk is the risk for damaging the Bank's value derived from the potential that a borrower or other party of the Bank fails to meet his liabilities in relation to the agreed terms or due to worsening of borrowers quality and the value of the collaterals provided by them.

The credit risk is the Bank's main risk. The materiality of this risk is compatible with the Bank's core business. The risk is expressed mainly in the activity with retail customers but also with business customers and nostro activity. In order to manage the credit risk, the Bank defined credit risk management policy and credit policy that is approved annually by the Board of Directors.

The credit risk management policy describes the creating factors, managers, and controllers of this risk, the principles of risk management, its decrease, and risk management control tools. Moreover, the process of determining authority, orderly reporting process, and reporting of irregularities are also described in it.

An additional document is the credit policy document approved by the Bank's Board of Directors, outlining the policy for providing Bank credit, and specifies the principles for providing credit, limitations, and collaterals. Under the policy are also determined the principles and rules of credit portfolio management and control on it, that refer to households, as well as to business customers according to the branch classification.

The activity of credit for public is managed in a number of principle sectors differing between them in customer characteristics and their required banking services, as well as the organization unit responsible for handling each of the customer types:

- Household sector and customers operating internationally are under the responsibility of the retail division.

- Business customers, mainly in the area accompanying real estate projects, and commercial customers, are under the responsibility of the business department and subject to the Bank's CEO.

In the credit providing process, transaction data are examined to conform with the criteria that have been determined in the Bank's procedures. The underwriting and credit approval mechanism are hierarchical, from the branch level and up to the level of senior management according to the authority ranking that was approved by the Board of Directors.

The Bank operates in a number of levels in order to monitor and to reduce the credit risk as much as possible, starting from the credit underwriting stage, its approval, the required collaterals are according to the credit policy and relevant procedures, and until the monitoring and continuous control implemented in the business units that are the first control circle and in designated control units. The Bank invests many efforts to improve the professionalism and expertise of those dealing with the credit provision and their management and also in developing automatic tools assisting in effective management.

Measurement and monitoring systems – The Bank uses a number of automatic systems for the purpose of credit risk management and control. Computer systems provide control tools for the first control circle and also for the second and third circle, for credit risk detection.

Among the principle systems the following are the commercial credit system, mortgage management system, and supporting systems for obtaining credit decisions.

The Bank has a number of internal systems for ranking borrowers for supporting the decision for receiving credit: In the accompanied project sector, the system integrates parameters from project exposure reports; e.g., examination of rate of completion, liquidity status, profitability erosion, inventory value, and more. In retail credit the customer is rated according to the Bank’s existing rating mode. The Bank completed the development of the customer ranking system in consumer credit that is incorporated in this credit underwriting system.

The Bank's management continues to improve the measuring, reporting, and control tools for obtaining more comprehensive information for assisting with credit risk management.

Reducing credit risk – For the purpose of reducing credit risk, the Bank operates in accordance with policy, processes, and work procedures for obtaining and managing collateral, reliance rates on collateral, collateral recording, and so forth.

Collaterals – The principal collateral provided to the Bank is a mortgage on rights to a real estate asset. Moreover, the bank receives current liens, project liens and project accounts, liens on deposits and securities, third-party bank guarantees, personal guarantees by debt guarantors, liens on property insurance and contractors' insurance policies, and more. The rules for reliance on each of the types of collateral according the collateral characteristic, its negotiability, realization rate, and the collateral's legal status are determined by the Bank's policy. The collaterals are adjusted to the loan circumstances.

The regulations for management of collaterals and update of their value are determined by the Bank's procedures.

The examining unit in the second control circle, credit control, as well as the internal audit, examine the collateral portfolios, in addition to business factors in the first circle.

In calculating the capital adequacy, the Bank operates according to the 201-211 instructions of the Proper Banking Management instructions from the Supervisor of Banks concerning measurement and capital adequacy, and offsets from credit to the public only deductible collateral according to the mentioned instruction.

In this calculation, according to instruction 203, the bank refers to two central CRM instruments, according to the Basel II guidelines, clarifications by the Bank of Israel, and legal opinions. The first is deposits and savings that were established and managed at the Bank, and the second is third party guarantees to secure the exposure of bank customers.

Deposits and savings that may be used to secure credit are deposits that are marked in the Bank system as mortgaged, where the owner of the deposit is also exposed, as well as deposits that are recorded in the Bank system and mortgaged in favor of the Bank, where the mortgages is recorded in the Register of Mortgages or the Company Register, as applicable. Offsetting of deposits and savings from the total credit for the public is implemented according to compliance of the collateral with the aforementioned instructions.

Description of the active creating factors, managing and controlling the credit risk:

The Bank has adopted a work framework for risk management and control, based on control circle and 3 "control circles."

The Supervising Entities

Board of Directors – The Board of Directors and its committees have the ultimate responsibility for determining the Bank's business strategy, including the risk management area, and securing the Bank's capital. Moreover, the Board of Directors approves the business policy and the Bank's work plan for each year, and examines the risk asset allocation for business factors. The Board of Directors approves the credit risk exposure limitations, credit risk management policy document; establishing periodical follow-up of credit risks exposure developments; discusses the required changes in limitations in order to ensure that the determined limitation enables ongoing operations while complying with the determined risk appetite. The Board of directors examines the embedded credit risk in new relevant activities or products.

Board of Director's committee for risk management – Its role is to examine the Bank's credit risk management procedures and the level of adjustments to the policy framework that was approved by the Board of Directors, and the report systems, lines of responsibility and authority. Their functions and authorities will include, inter alia: discussion on the Bank's exposure policy for various risks, on the exposure document, and recommendations according to the Board of Directors; a discussion of product offers or new activities and accordingly, recommendation to the Board of Directors.

The Board of Directors Credit Committee – The Board of Directors' Credit Committee holds preliminary and individual discussions on subjects of establishment of credit policies in the Bank as well as other issues, according to the Board of Directors' decision, that from time to time, requires delving into, and accordingly makes recommendations to the Board of Directors.

According to the transitional order that has been determined under the new Proper Banking Management instruction 301, the Bank 's Board of Directors approved a plan to reduce the involvement of the Board of Directors in credit approval. The Board of Directors will approve credit requests that are materially of irregular quantities during the Bank's normal business and therefore constitutes a deviation from its policy. The requests will come to the Board of Directors without prior discussion by the Board of Directors' Credit Committee according to the rank of authority and directives as specified in the credit policy for 2012, as was approved on November 22, 2011 by the Board of Directors. It should be noted that the number of transactions that deviate from the credit policies and that are brought before the Board of Directors for approval is extremely limited.

Management – Among others, through its committees, is responsible for establishing effective systems for risk and control management, including: consolidating an annual work program at the Bank and its credit policy, consolidating the Bank's annual risk management policy, defining the credit risk exposure levels and defining the actual requested levels, determining procedures connected to recognition, measurement, neutralization and control of credit risk exposure and ensuring the effectiveness of this risk management procedure through established procedures and through control factors in the risk division.

Risk-takers and Managers – CircleI

Internal Credit Committee – in which senior management having financial and legal skills, are members, some of whom are Bank credit department managers, and is headed by the Bank's CEO. The committee discusses requests for providing/renewing credit to borrowers/group of borrowers in amounts that have been determined according to the collateral mix as has been determined by the Bank's management that has been approved by the Bank of Directors. As part of the program the reduce the involvement of the Board of Directors in credit approval and increase of authority of the internal credit committee, the Chief Risk Manager or representation on his behalf, has been added as an observer at credit committee meetings. The Chief Risk Manager will report at his discretion on a particular credit to the Chairman of the Board of Directors/Chairman of the Risk Managing Committee.

Credit Authorizers – Their function is to approve credit requests according to criteria that have been determined in the approved credit policies by the management and the Board of Directors and Bank's procedures.

Underwriting system – operates at the retail and commercial retail credit department in the business wing, and, after valuation and reexamination, transfers approvals for any credit request deviating from the branch manager's approval authority, for approval by more senior officers.

Retail Credit Division – The Retail Credit Division includes all retail credit activity and commercial credit activity handled by the retail and commercial credit department.

Screening Department – this department is responsible for activities at the branches that create credit risk. The department is responsible for training branches, directing them, sales management, and complying with objectives.

Collection Department – has the function of enforcing the collection of problematic debts. The Collection Department deals with classification, regulation and collection and measurements of provisions for doubtful debts in the retail, business and commercial credit area.

Risk Management Functions – Circle II

Chief Risks Manager – The Chief Risks Manager is responsible for the independent control circles and it is his role to verify the overall effectiveness of the risk managing and control system. Moreover, he verifies the ongoing risk reports, to be reliable and relevant, and periodically examines compliance with the division of authorities and the determined exposure limitations.

Risk Control Unit – The risk control unit serves an independent function, while its role, among others, is to provide information to the management and Board of Directors about credit risks; gives an independent opinion on credit risk exposures, developing models for credit provision (established and statistically validated) and developing tools and methodologies (Best Practice) for credit risk management. This assessment process by the unit is independent of the functions that approve credit, since credit control is not involved in decisions concerning the provision of credit and its terms. A credit controller operates in the unit whose area of responsibility includes a number of realms:

Assessing the quality of specific borrowers and the quality of the Bank's credit portfolio as a whole, coverage of main borrowers, and checking and reviewing these borrowers. Moreover, the unit prepares a quarterly report on credit exposure trends that is submitted to the credit risk management forum, the risk management committee, and the Board of Directors. The report includes review of credit risks measurements, business as well as retail, compared to periods and to other banks (as many as possible).

Credit Risk Management Forum – Its purpose is to review reports received from credit takers and risk managers in relation to the Bank's exposure situation to credit risks, as well as to discuss policy before submitting it for approval. Furthermore, the forum discusses the monthly exposure estimates, the quarterly trend report, and the issues arising during the work of the credit risk management unit or credit control, conclusions of the review, reviewing collection in addition to additional issues according to demand.

Central Examination Unit – Examines the mortgages portfolios according to criteria determined by the management of the Bank prior to actual implementation, as well as reviewing of vehicle loans prior to implementation. The examination system is subject to the Resources division and thus there exists a management separation between the credit approval process and transferring of documents for examination.

Examining and analyzing credit risk unit – The unit was set up under the preparations for Basel II with the purpose of separating between the level that creates the credit risk (that brings the transaction to the Bank), the one that prepares the credit request, and the one that approves it. The unit has two principle roles:

1. Examining credit portfolios and analyzing credit risks. Under the second control circle, the unit deals with examining credit portfolios and borrower collateral (from the real estate sector and from the commercial banking division), prior credit provision, as well as during the current credit life.

2. Receipt of credit application before their transfer for approval, and examines whether the transaction structure as specified in the credit request complies with the Bank's credit policy and risk appetite policy. The credit risk management unit was made subordinate to the the Risks Division manager, and reports directly to him about its activity.

The Manager for credit risk management unit gives his opinion on the credit transaction brought for approval at the Bank's institutions in a separate and independent document (hereinafter – "credit risk management unit document").

Credit application will not be discussed in the credit committee without the credit risk management unit document that is submitted simultaneously.

The credit risk management unit was made subordinate to the the Risks Division manager, and reports directly to him about its activity.

Credit Audit and Guarantees in Securities – is required to supervise compliance with the instructions of the Stock Exchange regulations on the issue of credit provision (as part of Securities activity), securities requirements and short sales, as well as compliance with the instructions by the Board of Directors on these issues. The audit includes examination of barriers and alerts, custodian activity, audit on special accounts, as well as additional checks. In case of irregularities, the auditor will report to the relevant factors at the Bank according to the level of irregularity, and if necessary, will also report to the Chairman of the Board of Directors. In addition, the Bank will continuously monitor credit irregularities, short securities and Securities activities.

Extreme scenarios team – The team determines the various extreme scenarios such as, extreme holistic scenarios, adhesive effects occurring between the markets; and according to Basel II guidelines, examines their results. If necessary the teams will advise the management on required preparedness for realization of extreme scenarios.

Control Entities – Circle III

Internal auditor / internal auditing – The audit is responsible for the examination of activity and procedures implemented by the Bank, and mainly: integrity of activity performed by the Bank and its employees; the Bank's compliance with regulatory instructions and internal procedures; implementing decisions of the Board of Directors and management; management of assets and liabilities; amendment of deficiencies discovered in the auditing reports; and examination of the Bank's risk management procedures.

The Monetary Division – The function of this division is responsibility for accounting registration and subsequently all the financial information used for risk management. In addition, the department provides specific information in relation to capital composition, capital specifications, and capital forecast and risk assets for the coming 3 years. Additionally, the department is responsible for composing reports on Tier 1 issues and on monitoring the ongoing compliance with capital adequacy outline as determined in the annual work plan, including risk assets allocation for the activity area.

Internal Committee for Doubtful and Problematic Debts – In which preliminary discussions are held on borrowers/group borrowers on amounts that are determined by the policy prior to the discussion by the Board of Directors' Committee.

External accountant – perform auditing and accounting review assignments with reference to the Bank's Financial Statements.

Concentration

The risk of concentration is the risk deriving from the lack of dispersion in credit portfolios. With the purpose of reducing centralization deriving from the lack of dispersion of the Bank's credit portfolios, the Bank works to spread its credit portfolio between many borrowers in various sectors of the economy.

The Bank's credit centralization risk has a number of principle aspects:

Borrower Centralization Risk – Risk deriving from credit provided to the borrower or a number of borrowers belonging to the same borrowing group. As the dispersion of the credit portfolio between the various borrowers becomes larger, the borrower centralization risk will become smaller.

Under the preparations of the Bank for changes in the business environment, and with the willingness to reduce the Bank's exposure of the to large borrowers, the Bank's Board of Directors has narrowed, beyond the regulatory limits determined by the Supervisor of Banks, the limitations of the sole borrower, of the framework for group borrowing and of the framework for the six large borrowers.

The Bank continuously monitors large borrowers and meeting the limitations set by the Board of Directors.

On November 8, 2011, the Supervisor of Banks published directives concerning additional disclosure for material exposure of a group borrowers. Since there are no group borrowers at the Bank (as defined in Proper Banking Management instructions № 313) while its debts increase with 15% from the Bank's capital, the Bank is not required to provide additional disclosure according to the aforementioned guideline.

Centralization risk of economic sectors – The risk results from a large volume of credit provided to borrowers in a certain economic sector relative to the credit portfolio.

In order to reduce the credit risk derived from centralization in the construction sector in accompanying projects in which the Bank cooperates with insurance companies issuing sale policies to housing purchasers in projects and share mutual collateral with the bank – "pari passu".

The Bank complies with the limitations of the Bank of Israel concerning the exposure to economic sectors.

Geographical centralization risk – The risk derives from insolvency of the borrower centralized in a certain geographic area or collaterals centralized in a certain geographical area.

It is the Bank's credit policy to set limitations concerning geographic dispersion with the purpose of reducing this risk.

Sector centralization risk – Risk deriving from insolvency of a borrower belonging to the same population sector.

Out of 18 branches, 3 of the Bank's branches are located in areas characterized by population of mostly Ultra-Orthodox and 2 in areas with a mostly Arab population.

The Bank's concentration in the Ultra-Orthodox sector beyond its estimated proportion of the population. The Bank is not centralized in the Arab sector beyond its estimated proportion of the population. The Bank continuously examines its exposure to these populations and performs scenario analysis from which it appears that the Bank is not expected to have irregular losses as result of the Bank's exposure to these sectors.

Each quarter, the Bank examines the its credit centralization, also for extreme scenarios. The examination results are submitted to the Board of Directors in its quarterly Credit Exposure Report.

The Bank's Credit Implementation Procedure

The majority of the Bank's credit portfolio is managed by the Retail Credit Division, the credit in project oversight, and construction financing, is managed by the Real Estate Sector Department that is directly subordinate to the CEO. In both units, there is a clear division of credit authorities: type of credit, type of customer, and amount of credit. The credit underwriting process is also defined. Each credit application is examined and approved by the appropriate level of authority according to principles approved by the Bank's Board of Directors.

The Retail Credit Division includes an underwriting center, that sends each mortgage application exceeding the branch manager's approval authority, for endorsement at the level authorized for approving such credit.

In addition, the Bank has a central system for examining all mortgage portfolios before actual implementation. The examination process focuses on a review of the credit documents and the collateral, compliance with the terms defined when the credit was approved, and all with the purpose of performing a monitoring function of the loan creation process , to reduce exposure to operating risks in mortgage activity, and to ensure that the Bank as a whole, works according to uniform and controlled standards. The examination system is subject to the Resource Division and thus there exists a managerial separation between the credit approval process and document transfer for examination.

In the Real Estate Sector Department, applications for credit are prepared by the division's control and reports team and not by the referents (creating the risks), and are examined by the credit risk management unit (subject to the manager of the Risks Division), before being submitted for approval in the relevant credit committees, in accordance with the specified authority level.

As part of examining the credit and collateral portfolios, the unit even checks the existence of all required documents and collateral, before granting the credit, and approves the provision of credit to the customers by the credit teams. As part of analyzing credit risks, the Credit Risk Management Unit provides an additional and independent opinion on the credit application submitted for approval at the Bank's institutions in a separate and independent document (hereinafter – "the CREA document"). It should be emphasized that credit applications are not discussed in the Bank's institutions without the CREA document that is submitted in parallel with the application. Once quarterly, the CREA unit manager of the reports to the Risk Management Control division on the CREA documents prepared by him.

In the department for project accompaniment, each accompanied project is managed in close accompaniment to the Construction Supervisor, making periodical reports on its progress. The required additional credit needed for completing the construction is approved only after examining the updated exposure report for the project, in considering its progress rate and the conditions, parameters and set milestones, which the borrower needs to meet. In addition, during the project's life, generally once per month (with the receipt of the supervisor's performance report), the financial solidity of the project is examined by the division's referents.

In the business credit area, requests for renewal are submitted at least once a year. The credit portfolio and collateral are examined, as of the credit grant date, and as of the renewal date. Also in this area, examinations are implemented concerning the borrowers' financial stability, as well as the financial statement reports. Moreover, daily controls are being implemented on irregularities in the credit lines and collateral.

Handling and recognition of problematic credit

For the purpose of providing recommendations concerning credit classifications and provisions for credit losses existing once a quarter, an individual review is held quarterly for all customers from the real estate sector, as well as commercial customers under the Retail Credit Department.

As part of the review customers with negative symptoms are located such as: passed due debts, cash flow difficulties expressed in difficulty in paying loan principal and/or interest, worsening of business activity, and so forth. The need for providing a new classification recommendation for the customer or a change in the customer's classification with an existing one is examined.

The recommendations are submitted to the Problematic Debts Committee according to the set authority level, which conducts discussions and make decisions.

When the business department recognizes that a borrower is in trouble or there is suspicion that he may get into trouble, immediate discussions are held with the participation of the main parties handing the customer and immediate decisions are taken whether to transfer handling to the Bank's Collection Department, external legal treatment, imposing receivership, liquidation or arranging for debt settlement.

In Retail Credit – when the loan is in arrears – The branches will handle the collection up to a certain depth of arrears as determined by the procedures. Loans beyond the aforementioned depth of arrears will be passed for handling by the Collection Department. In irregular cases in which there is suspicion of forgery, fraud, or suspicion of flight abroad by the borrowers, and so forth, the portfolio will be transferred immediately to the Collection Department regardless of the sum of the arrears.

The Collection Department centralizes all the procedures in the framework of as part of the Banks collecting activity, and supervises the work of lawyers and subcontractors involved in the collecting process.

The Bank's management strives to settle with the borrower whose debts to the Bank are passed due, and continuing the current monthly payments, but only if there exists sufficient collaterals in the borrower’s portfolio.

In the event, in which the borrowers do not cooperate and/or avoid repaying the debt, receivership proceedings will be initiated as a last resort for clearing the debt.

The Bank has orderly procedures for identification, classification and handling of problematic debts and there is a mutual work relationship between the Credit Managers and the Collection Departments.

Controls of significant events that might affect a group of customers or the Bank's credit portfolios, the Bank examines the effect of the event on the credit portfolio and responds accordingly. The response may be in the form of change in policy or by means of an activity with the existing borrowers.

The Board of Directors and its committees receive periodic reports concerning distribution of credit, distribution by sector, large borrowers, and other parameters measuring the exposure to credit risk.

The Bank has an internal system for ranking borrowers that supports credit decision making. In the Accompanied Project Sector, the system integrates parameters from project exposure reports; e.g., examination of completion rate, liquidity status, erosion of margins, value of inventories, and more. For all extended retail credit, the customer is rated according to the Bank’s existing rating model.

The bank determines provisions for credit losses on loans against mortgage of a residential housing according to the depth of arrears as determined in Appropriate Banking Management Instructions № 314 of the Supervisor of Banks. In addition, conforming to the Supervisor of Banks’ guidelines, the group provision for credit losses is calculated for housing loans balance provided as of the beginning of 2009 and onwards, and while the ratio between debt and the mortgage asset value at the time of loan, providing (LTV) is higher than 60%.

For the remaining retail credit, as well as business credit, the Bank determines its provisions according to the circular from the Supervisor of Banks on the issue: "The measurement and disclosure of defective debts, credit risk and provision for credit losses" as published on December 31, 2007. The circular is based, among others, on American Accounting Standards and on regulatory instructions of supervision institutions of banks, and on the American SEC (Securities and Exchange Commission}.

According to the circular, the Bank sets as separate liability account, the provision at suitable level for coverage of the expected credit losses related to the off-balance-sheet credit instruments, such as agreements for providing credit and collaterals.

The required provision for covering the expected credit losses in relation to the estimated credit portfolio, is in one of two tracks: "individual provision" and "group provision".

Individual provision for credit losses – The Bank identifies for need to examine individually each debt whose contractual balance (without deduction of write-offs that are not involved in accounting waiver, unrecognized interest, provisions for credit losses and collaterals) is NIS 1 million or more. The Bank also identifies the need for individual valuation, other debts (except housing debts concerning to which provision has been calculated according to the depth arrears formula) while the provision for their depreciation is not included in the group provision. The individual provision will be recognized for every debt classified as defective. Debt will be classified as defective when according to the information and updated events the Bank may probably not be able collect all the entitled amounts according to the debt's contractual terms. Debt classified as defective when the debt is passed due for 90 days or more, except if the debt is properly insured and is in collection process.

The individual provision for credit losses is estimated, based upon future cash-flows, discounted by the debt's effective interest rate, or when the debt is backed up with collateral or when the Bank determines that seizure of the asset is probable according to the fair value of the mortgaged collateral to ensure that credit after deducting sales cost.

The provision for credit losses is estimated on a group basis – implemented for depreciation provision of the large groups of small and homogeneous debts (such as: credit card debts, housing loans and loans for the purpose of consumer debts paid by installment), and also for debts that have been individually examined and have been found defective. The specific provision for credit losses for debts estimated on group basis, except for housing loans for which provision has been calculated according to the depths arrears formula, will be calculated according to the regulations determined in the American Accounting Standard FAS 5: Accounting for Contingencies (hereinafter – "FAS 5"), based on the updated estimated past loss rates for each of the homogeneous groups of debts with similar risk characteristics. The formula is based on rates of historical losses in the various market branches as divided between non-problematic credit and problematic credit between 2008 and 2011, as well as for actual recorded net write-off rates.

The required provision in relation to the off-balance-sheet credit instruments are estimated according to the regulations determined in the American Accounting Standard FAS 5.

In addition to this, the instruction established the definitions and various classifications of balance sheet and off-balance-sheet credit risks, recognition rules for entering interest from impaired debts, as well as write-off regulations for problematic debts. Inter alia, the Bank operates to write-off all debts estimated on an item by item basis and is considered uncollectible and has such a low value that the remaining assets is unjustified or debt for which the Bank manages efforts for long-term collecting. Concerning debts estimated on a group basis, write-off regulations have been determined based upon the depth arrears period (in general, when passed due over 150 days) and their collaterals.

This instruction will be implemented in the Financial Statements of banking corporations and credit card companies as of January 1, 2011. The instruction is not to be implemented retroactively in Financial Statements from previous periods.

Listed below is a table of credit risk and non-performing assets:

	Balance as at December 31, 2012			Balance as at December 31, 2011		
	Credit risk [3]			Credit risk [3]		
Credit risk	**Balance sheet**	**Off-Balance-Sheet**	**including**	**Balance sheet**	**Off-Balance-Sheet**	**including**
1. Problematic credit risk [1]						
Defective Credit Risk	78.1	9.7	87.8	35.6	3.0	38.6
Inferior credit risk	28.3	6.3	34.6	75.0	38.1	113.1
Credit risk under special supervision [2]	277.7	0.4	278.1	259.0	6.3	265.3
Total problematic credit risk*	384.1	16.4	400.5	369.6	47.4	417.0
*From this: unimpaired debts, in arrears of 90 or more days [2]	280.3		280.3	310.6		310.6
2. Non-performing assets						
Defective debts that do not accrue interest income [4]	44.1	9.7	53.8	35.6	3.0	38.6
Assets received for cleared credit	-	-	-	-	-	-
Total non-performing assets	44.1	9.7	53.8	35.6	3.0	38.6

1. Credit risk that is defective, inferior, or under special supervision.

2 Including for housing loans for which there is a provision based on the depth of arrears, and housing loans for which there is no provision based on the depth of arrears that is in arrears by 90 or more days.

3. Balance sheet and off-balance-sheet credit risk is represented according to the affect for credit loss provision and before collateral affects allowed for deduction for the purpose of the obligation of the borrower and for groups of borrowers.

4. Not including debts whose recognition of income from interest was based on a cash basis.

Listed below is a table of the provision rates from credit risks for the public:

		December 31, 2012
A.	Defective credit to the public: credit rate balance for the public that does not accumulate interest revenue from public credit balances	0.81%
B.	Credit rate balance for the public that is not defective, which is in arrears for 90 days or more than the public credit balance	2.90%
C.	Rate of balance provision for credit loss for public credit from public credit balances	0.96%
D.	Rate of balance provision for credit loss for public credit from the balance of impaired public credit	118.57%
E.	Problematic credit risk for the public from the public's total credit risk	4.14%
F.	Expenses rate for credit losses for average balances of public credit	0.38%
G.	Net off-writes rate for credit to the public from average public credit balance	0.38%
H.	Net off-write rate for credit for the public from credit loss provision balance for public credit	100.28%

Credit exposures for foreign financial institutions [1] on consolidated basis as at December 31, 2012:

	Total credit exposure in millions of NIS [2]	
	As of December 31	
External credit rank	**2012**	**2011**
AAA until AA-	49	28
A+ until A-	56	27
Unrated	-	25
Total exposure [3]	105	80

1 Banks, the Bank's Maintenance Companies, Banks for Investments and brokers.

2. Deposits and current balances in banks. The bank has off-balance-sheet credit credit risks.

3. There are no financial institutions that are classified as defective debt or debt under special supervision, as well as there is no provision for credit losses.

The balances included in the above table primarily include institutions operating in the United States, Denmark, Switzerland, Germany, Britain and Canada.

With the outburst of the financial crisis in 2008, the Bank reduced its deposits in financial institutions abroad, determined limitation on centralized depositing and determining procedures and examinations required prior depositing funds on foreign banks abroad. The bank relies on the rating by the rating companies "Standard & Poors", "Moody's". The ratings are relevant in relation to deposits that have been deposited at foreign banks only.

Exposure to Environmental Risks

Increase in global and Israeli awareness, expressed in regulatory extensions, for compliance with instructions concerning environmental quality that require the Bank to relate to the functional financial exposure deriving from the environmental risks. The Bank is obligated towards its customers and shareholders to manage its business in a profitable and responsible manner. As part of this obligation, the Bank works to recognize, assess and manage the environmental risks involved in its activity and that of its customers. The appetite of the Bank for risks in this area is lower and therefore the Bank operates according to conservative principles for environmental risk management in its financial activity.

The current activity of the Bank focuses on borrowers in the retail sector who do not have a high exposure to environmental risk. Actually, the Bank's exposure to this risk is not significant. Also, the activity of the Real Estate Sector in providing credit in the construction, real estate and commercial activity areas for corporations and individuals does not expose the Bank to material environmental risks, inter alia, in light of the Bank’s avoidance from providing credit to branches prone to environmental pollution.

Housing Loans

The Bank of Jerusalem has made it its objective to improve the quality of its credit portfolio. This objective is obtained by the activity for improving its new customers. The Bank's activity in the housing loans area is with the mid-decile and above population level and as the main target public. Therefore, the customers with the following characteristics are preferred: Customers living in the center of Israel, an asset mortgaged in loans secured by real estate located in an area defined by the Bank as preferred, the gross family income is not less than the average income in the market. Over the past two years, the financing percentage in housing loans provided by the bank significantly declined. In 2012, approximately 92% of the loans were granted at a financing rate that does not exceed 60% of the value of the asset.

The Bank's Average Financing Rate – The balance of the loan divided by the estimated value of the assets, as examined in relation to the existing credit portfolio at the Bank, is very low and stands at about 31% (value of the estimated assets calculated from the last assessment day, according to the Housing Price Index that the Bureau for Central Statistics publishes, distributed by geographical areas and according to the number of rooms).

The following table presents the developments in the quality of housing credit portfolio:

	2012	2011	2010	2009	2008
Total implementation (millions of NIS)	1,476	1,489	1,996	1,179	937
From this:					
In variable interest at a frequency less than 5 years in millions of NIS	328	731	1,198	743	523
In F.C. in millions of NIS	252	243	482	247	252

General data with mortgages in NIS (according to year of implementation):

	2012	2011	2010	2009	2008
Average loan period in months	221	226	217	203	199
Average income per person (NIS)	4,136	3,740	3,716	3,322	3,082
Distribution in Implementation amount distribution according to percentage of asset financing (LTV)					
0%-60%	92%	87%	60%	61%	58%
61%-75%	7%	12%	37%	36%	38%
Over 75%	1%	1%	3%	3%	4%
Breakdown of several of the sums based on the implementation sum:					
0-500	74%	72%	75%	82%	85%
500-1,000	18%	19%	18%	14%	11%
Over 1,000(*)	8%	9%	7%	4%	4%
Average loan amount (in thousands of NIS)	510	458	447	324	300

(*) In 2012, 113 loans exceeding NIS 2 million were given, for an overall sum of NIS 394 million.

Customer Quality

The population of mortgage customers are mainly in their upper thirties, from the 6th decile and above, with an income higher than the economy's average income. The return ratio of the average income is materially lower than the minimum requirements as defined in the Bank's credit policy.

The rate of return from fixed income:

The financing rate in housing loans is used as a parameter of the customer's ability to repay the loan it took. In general, the bank ensures that the monthly rate of return of the requested loan does not exceed 35% of the household income. In loans in which the rate of return is higher, the credit granted to the borrower with a high scope of assets, and whose ability to repay the loan is not solely based on the applicants' current income. In 2012, the average rate of return to income ration was 33%, with only 11.4% from housing credit given to customers with a rate of return to income ratio higher than 35%. The average financing rate to these customers was less than 60%.

Distribution of the portfolio according to the financing rate:

In the credit policy of recent years, the Bank decided to reduce the credit risk exposure by the maximum financing rate limitation, in general to 75% of the mortgaged asset's value. Over the past two years, most credit performances focused on financing rates that do not exceed 60% of the value of the mortgaged asset. Following the instructions published by the Supervisor of Banks in the second half of 2010, the Bank significantly reduced the loans provided for a financing rate above 60%. Beginning in November 2012, the Bank began implementing the Supervisor of Banks directive concerning limitation of the financing rate in housing loans in which a significant percentage of loan performances will be limited to a financing rate of 50% of the value of the mortgaged property. For more information, see the Household Sector chapter above.

According to the credit policy, the Bank does not grant loans in which there is an element of deferred payment of principal and interest.

The loan balance secured in secondary mortgages or when the Bank's collateral rights is unsecured, is not significant. There are no housing loans at the Bank on which the information is incomplete.

In general, the bank does not grant loans for a period exceeding 30 years.

In 2012, approximately 14% of all housing credit (NIS 205 million) was granted for a period exceeding 25 years. The original loan period for 90% of the balance of the housing credit portfolio was for less than 25 years.

Breakdown of the portfolio according to geographical areas:

The Bank's housing loans portfolio is distributed between many borrowers, most of whom purchased assets in a centralized manner in the center of Israel. Some 54% of the portfolio is granted to assets in the Gush Dan and Greater Jerusalem area.

Housing credit provision process:

The mortgages activity mainly includes providing loans for housing against a lien on the apartment for Israeli residents with various linkage bases and according to a variety of interest tracks; and to foreign residents in the major foreign currencies (mainly in US dollar, English Pound and Euro).

The loans are divided into two types: loans from the Bank's funds, and loans from government funds and under its responsibility for those entitled by the Ministry of Construction and Housing (hereinafter: the "budget loans"). The Bank has no credit risk on budget loans.

The procedure of assessment and credit approval for residential housing mortgage is a structured and standardized process.

The loan approval is performed by the branch and/or transferred to a more senior approval level, according to the authority level determined by the Bank's Board of Directors.

The procedure required separation of functions (the credit officer is not allowed to approve the application he assesses – the computer system blocks this possibility) thus, also those applications within the branch's authority may not be performed by the same officer.

Applications deviating from the authority of the branch manager are transferred for approval to an underwriting center. The role of the underwriting center is to reexamine the application, to approve or reject it. In case the credit application is under the greater authority than the underwriting center authority; the underwriting center presents its recommendation and transfers it to a senior factor for approval (department manager, CEO or credit committee) according to the relevant authority.

As part of the loan granting process, credit portfolios in the framework activity of mortgages are examined by the Central Examination Unit that examines the completeness of the portfolio after approval, and reception of all the necessary documents and collaterals: The unit is subject to the back operating system in the Resource division and thus there exists a managerial separation between the credit approval process and document transfer for examination prior to implementation.

The retail credit activity is supported in a tight manner with legal guidance of lawyers from the Bank's legal department, that examine, among others, the legal diligence of the documents and kinds of collaterals.

Clearance risks and other party risks

The clearance risk is the risk that the other party does not fulfill its part and does not transfer to the Bank on the fixed date the required amount in the clearance transaction, this although the Bank did transfer its part to the other party. The risk only exists when the exchange for the transaction is not simultaneously transferred. The exposure to clearance risk is for a short period of time and generally for a day.

The other party's risk is a risk when the other party to the transaction is in lapse before the final clearance of the transaction flows. The transaction's market value, which may be positive or negative for any of the parties, actually depends on the fluctuation of the market factors. Only in case the transaction will have a positive fair value for the Bank and the other party will be in lapse – a general loss may be caused to the Bank during the lapse. The risk exposure to the other party may be created during the transaction's entire life time.

Until September 2007, the banking system mainly cleared receivables through the central banking clearance center, in addition to the check clearing system. In addition, as of September 2007, the banking system started to operate RTGS systems (Real Time Gross Settlement), that is a real-time financial transactions clearing system. The transaction amount requiring transfer via RTGS was set by the Bank of Israel at NIS 1 million.

The main source for exposure of the Bank for clearance risk is clearance of derivative transactions (OTC – Over The Counter). The Bank operates with its customers in derivative instruments traded at the various stock exchanges, but does not operate with them in OTC derivatives. The Bank operates in these derivatives for itself and only for risk hedging, and as an additional tool it uses for managing its assets and liabilities. In addition, the Bank 's exposure to clearance risks resulting from trading in foreign securities performed with brokers through clearance NON-DVP (Delivery Versus Payment) type of process.

Therefore, the main exposure of the Bank to other party risk is formed with banks and recognized financial institutions abroad for clearance of derivative transactions (OTC) and with brokers and custodian service provides in securities for transaction clearance of foreign securities. In the framework of the activity with these institutions approved at least once a year by the Board of Directors of the Bank in the credit framework of these same institutions. During the review period, clearance risks or other party risks were not realized at the Bank.

Decrease of risk – the Bank has signed agreements with ISDA and CSA appendixes with some of the banks where derivative activities are implemented. Enabling offsetting of transactions, so that the amount transferred between the transaction parties is only the net exposed amount, and thus reducing the exposure of each of the parties. CSA appendixes regulate the transfers of the finances between the transaction parties whenever the exposure reaches a certain predetermined scope, and thus reducing the other party's exposure.

Market Risks

General

Market risks are a group of risks whose essence is loss exposure as a result of changes in various market parameters (exogenous parameters). In this risk group, several types of specific risks are included, managed at the Bank in similar manner, based on similar work structure and through the same principle factors.

Management market risks

Board of Directors – Carries the ultimate responsibility for management and supervision on market risks and liquidity and creating a proper risk environment. The function of the Board of Directors, as determining the Bank's policy, is to outline the risk management characteristic and the required corporate governing structure.

Board of Director's Committee for Risk Management – Its role is to examine the Bank's credit risk management procedures; the level of adjustments to the policy framework that has been approved by the Board of Directors; the report systems; and lines of responsibility and authority. The committee holds discussions in advance of the discussion by the Board of Directors on everything concerning the exposure policy for market risk and liquidity (including nostro policy). Moreover, the committee discusses the organizational preparedness for management and these risk controls. The committee even discusses every proposal for new financial activity or irregular activity by the Bank and every deliberate investment in new financial instruments, and submits, if necessary, its recommendations to the Board of Directors.

Senior management – convenes very frequently on current issues. On behalf of the senior management, a number of sub-committees have been established, whose members are the relevant senior management members for issues to be discussed, handling among others, the Banks risks management.

The Assets and Liabilities Management Committee – Headed by the CEO, it convenes twice weekly, and reviews reports on all issues related to the Bank's management of assets and liabilities. The committee monitors compliance with the Bank's objectives, as defined by the work plan and after complying with the exposure limitations for market risks, as has been approved by the Board of Directors. The committee makes operative decisions on various issues and determines prices and quantitative objectives for each of the business activities.

At each meeting, the committee reviews the current parameters of the activity including quantities and prices in all sectors. These parameters are central indicators for the exposure and liquidity situation. This review includes data concerning credit implementation and implementation of prices, recruitment in current month and prices of recruitments, balances of liquid assets and their components, activity in the nostro portfolio, index positions and foreign currency, Profit and Loss from index positions and foreign currency, financial forecasts, and more.

It is the responsibility of the committee to continuously monitor all the reports related to risk management and the Bank's liquidity and management of the Bank's nostro portfolio.

Risk Management Forum – Convenes monthly in order to review the reports received from the risk manager in relation to the Bank's market risk exposure situation. Furthermore, the forum discusses the monthly exposure estimates, the exposures document (quarterly), issues arising during the Risk Manager's work, the Risk Management Department or Auditor, and additional issues as required. At each meeting the forum reviews the exposure situation in various risk and liquidity situations, among others, through monitoring all the parameters appearing in the exposure document including the model and extreme scenario results. Moreover, the forum monitors events affecting the Bank's various exposures and liquidity.

Financial Division Manager – Serves as market risk and liquidity manager and responsible for implementation of the Bank's policy and to consolidate work setting including this risk management and its approval by the Bank institutions. In principle, the Division deals with the current management of market risk exposure and guidance of the various units dealing with the management of the Bank's financial instruments, and creating exposure by the various activity sectors. The Finance Division Manager even makes recommendations to management, the Board of Directors and the Board of Directors' committees concerning the feasibility of creating risks through financial instruments allowed for creating and hedging risks, and all the remaining issues connected to exposure creation and management. Moreover, it has the responsibility for managing the nostro portfolio while examining the implication of the nostro activity on its entire exposure.

The Risks Division headed by the Chief Risks Manager – Deals with consolidating models for market risk assessment, exposure and liquidity; development of techniques for risk management; and support current management of market risk exposure. The division also makes recommendations to the Internal Committee on issues related to the feasibility of exposure management, while considering the expected income components from these exposures and costs of exposure hedging, and the feasibility and profitability examination of new and/or existing financial products.

It is the responsibility of the division to implement and currently monitor compliance with the limitations as determined for the various exposures.

The Mode and Scope of Reporting Systems

The Bank manages its risks, among others, with the assistance from the ALM, the system controls the Bank’s cash flows, derived from its various financial activities. This system enables asset and liability management – ALM – (Asset Liability Management) and inter alia, enables quantification of market risks according to the value methodologies provided for the risk – VaR. In addition, the system enables monitoring additional risk parameters such as: interest exposures and Stress Testing. During the first half of 2012, the ALM system underwent validation in accordance with instructions by the Bank of Israel on model validation.

The VaR measures the maximum loss expected to occur at the Bank resulting from realization of market risks in a given period of time and at a predetermined statistical level, according to previous market conditions. The calculation at the Bank is performed monthly, during a period of 10 days and at a significant 99% level. Through this system, the Bank measures the comprehensive risk through the VaR of the total banking portfolio and the portfolio's exposure to market risk. In addition to management and control through the VaR model, the Banks also uses other models for quantifying risks.

The bank determined limitations for given risk value (economic VaR): total VaR – 20 million NIS. As at December 31, 2012, the VaR amounted to NIS 5.8 million, compared to NIS 9.7 million as at December 31, 2011. The maximum economic VaR (month end) amounted to NIS 14.4 million during the reporting period, compared to a maximum value of NIS 13.8 million in 2011.

Hedging Policy and/or Risk Decrease

The Bank’s financial risk management policy is based on exposure management for market risk and liquidity by determining quantitative limitations. The means used for the purpose of complying with the limitations include, among others: purchase and sales of marketable securities (mainly government of Israel debentures), recruitment of non-negotiable deposits (from private and institutional departments), recruitment of negotiable deposits, and activity in derivative financial instruments.

Interest Risk

Interest risk results from the differences between the relative sensitivity of assets and liabilities to unexpected changes in interest rates and between this sensitivity of liability changes – changes that may result in corrosion of the Bank's capital. The Bank’s role as a financial intermediary creates this risk exposure, and the Bank works to reduce it. The Bank’s principal exposure is in the index-linked sector, since this is the sector in which most of the assets and liabilities bear fixed long-term interest rates. Moreover, the exposure in the non-linked NIS sector in concerning the activity scope should be noted, in the credit area as well as in nostro and resource recruitment. This, although the main activity in this sector, except for the activities in the nostro portfolio, is made for the average duration (interest) of up to a year. The Bank monitors the development during the loan’s average duration along with the deposits, for the purpose of taking measurements for minimizing the affect of possible changes in the interest rate upon the value of its net financial flows. To this end, it continuously measures the average duration deriving from the current new activity, and also monitors the extent of early loan repayments that have a significant affect on the effective average duration.

The Bank's policy on management of exposure to interest risk is periodically examined in consideration of expectations concerning the decrease in various interest rates, examining the costs required to reduce exposure to this risk, and taking into consideration the estimated early repayment rates on loans and factors affecting it. Estimates of early repayment rates is implemented by relying on past experience and on the Bank's assumptions concerning a number of factors affecting the early repayment rate, and of them mainly the interest rates. The assumption of early repayments by borrowers serves as in the index-linked sector for calculating the gap between the average duration and the interest risk exposure.

According to the Bank's estimation, considering the extent of early repayments during recent years and the risk exposure in all linked sectors, the risk exposure as result of unexpected change of 1% in the interest rate was smaller, relatively to the value of the Bank's capitalized net flows. This assessment by the Bank is "future facing information" and may be realized differently than expected in view of the fact that it is based on the scope of early repayments in recent years and the exposure in all linked sectors and probably that the actual scope of future repayments may be different.

Moreover, the Bank's exposure to risk resulting from reducing the margins in the mortgages area and that due to the acute competition in this area. One of the objectives of the strategic plan in the Bank is to reduce this risk and to reduce the Bank's dependency in this area.

Below is a summary of various exposures because of unexpected changes in interest (in millions of Shekels before Tax):

	The potential change in economic value				The potential change in annual profit	
	31/12/12		31/12/11		31/12/12	31/12/11
Immediate effect of changes parallel to the yield curve	**increase 1%**	**decrease 1%**	**increase 1%**	**decrease 1%**	**increase 1%**	**increase 1%**
Sector						
Un-linked	(6.0)	7.0	(13.1)	14.3	3.1	1.5
linked	0.8	(0.4)	(5.2)	6.5	(1.7)	(3.5
Foreign Currency	2.1	(2.1)	5.6	(6.0)	5.9	6.7
Total	(3.1)	4.5	(12.7)	14.8	7.2	4.7
Limitation	50.0	50.0	20.0	20.0	12.0	12.0
Maximum during the period	(18.5)	20.8	(12.7)	14.8	9.4	(12.1)
Minimum during the period	(3.1)	4.5	9.8	(9.8)	4.9	7.9

Below is information concerning the effect of hypothetical changes in the interest rate on the fair value of the financial instruments of the Bank and its consolidated companies as at December 31, 2012 (in millions of Shekels):

Fair value of the financial instruments of the bank and its subsidiaries, except for non-financial items (before hypothetical changes in interest rate):

	Israeli currency			
	Un-linked	**Index linked**	**Foreign currency** (2)	**Total**
Financial assets (1)	6,919.0	3,816.1	1,575.3	**12,310.4**
Receivable amounts for derivative financial instruments (3)	259.2	119.6	7.4	**386.2**
Financial liabilities	6,217.4	4,006.6	1,436.3	**11,660.3**
Payable amounts for derivative financial instruments (3)	243.1	50.2	88.4	**381.7**
Fair value net	717.7	(121.1)	58.0	**654.6**

a. The effect of hypothetical changes on interest rates on the fair value of the financial instruments of the bank and its consolidated companies, with the exception of non-financial items:

	Net fair value of financial instruments after the affect of changes in interest rates				Change in fair value	
	Israeli currency		Foreign currency linked to foreign currency index		Millions of NIS	In percent
Change in interest rates	**Un-linked**	**Index linked**	**currency Foreign (2)**	**Total**	**Total**	**Total**
Immediate concurrent increase of one percent	711.7	(120.3)	60.1	651.5	**(3.1)**	**(0.48%)**
Immediate concurrent increase of 0.1 percent	717.1	(121.0)	58.2	654.2	**(0.4)**	**(0.06%)**
Immediate concurrent decrease of 1%	724.7	(121.5)	55.9	659.1	**4.5**	**0.68%**

(1) Not including balance-sheet statements of derivative financial instruments and fair value of off-balance-sheet financial instruments.

(2) Including Israeli currency linked to foreign currency.

(3) Amounts receivable (payable) for derivative financial instruments and for off-balance-sheet financial instruments, capitalized at interest rates utilized to calculate fair value.

Basic Risk

The exposure to basic risk is attributed to changes in the exchange rate and the inflation rate. The policy of the Bank is to manage the risks resulting from basic exposure in a controlled manner, as part of the limitations determined by the Board of Directors.

The Bank currently manages the positions in the various linkage sectors through a variety of financial instruments available to it, in accordance with consideration of changes in relevant economic data and current supervision of risks resulting from such exposure. The limitations were determined while maintaining the Bank's flexibility and its ability to change the various positions in short time according to the economic forecasts. In order to limit this risk exposure, the Bank's Board of Directors determined the maximum rates for each linked sector.

Below are limitations on exposure rates in each linkage sector as determined by the Board of Directors (not necessarily an accounting exposure). The limitations are on the excess amounts (deficit) of assets over liabilities in each sector:

	In percentages of the financial capital (1)		In millions of Shekels as of 31/12/12	
	Maximum amount	Minimum amount	Maximum amount	Minimum amount
Index linked	50%	(50%)	304	(304)
In foreign currency linked to foreign currency index	From $10	From ($10)	37	(37)
Un-linked	150%	50%	912	304

(1) The financial capital is equity less non-financial assets in consolidation.

The Bank measures its positions daily by various linkage bases through its data system. This data reports to responsible units on position management and adjustment to the applicable limitations. The date on the issue of position height is reported in a current manner at the meetings of the Assets and Liabilities Management Committee, as well as at meetings of the other forums operating in risk management.

Below are the economic exposures (that are not necessarily an accounting exposure) active in each linkage sector (in millions of Shekels):

		Exposure during the reviewed period (2)		
	Exposure as at 31/12/12	Maximum	Minimum	Average
	Millions of NIS			
Index linked	(252)	117	(198)	(34)
In foreign currency linked to foreign currency index	(0.2)	18.3	(17.8)	1.0

(2) Exposure for the index linked sector is determined on the 15th of each month.

Below is data about the Bank's capital sensitivity to changes in the Consumer Price Index (the theoretical change in economic value as result of the scenario, that includes the affect of the change on the economic value of the nostro portfolio that was not included in the calculation of the position as a result of the scenario in millions of Shekels):

Scenario	**As at December 31, 2012**	**Maximum for 2012**	**Minimum for 2012**
Increase of 5% of the index	-6.4	-7.3	6.0

Below is data about the Bank's capital sensitivity to changes in the currency exchange rates in millions of NIS (the theoretical change in the economic value as a result of the scenario, when the strengthening scenario means strengthening of the currency in question against the shekel):

	As at 31/12/12		**Maximum for 2012**		**Minimum for 2012**	
	US Dollar	**Other**	**US Dollar**	**Other**	**US Dollar**	**Other**
Scenario						
Strengthening of 10%	2.8	(0.3)	4.2	1.4	(1.6)	(0.4)
Increase of 5%	1.4	(0.1)	2.1	0.7	(0.8)	(0.2)
Weakening of 10%	(2.8)	0.3	1.6	0.3	(4.2)	(1.4)
Weakening of 5%	(1.4)	0.1	0.8	0.1	(2.1)	(0.7)

Part of the Bank's overall strategy for managing the exposure level to market risks, as mentioned above, the Bank implements, among others, transactions in derivative financial instruments for reducing its exposure to these risks. The Bank's activity in derivative financial instruments is as an intermediary, trader or end-user. The Bank has derivative financial instruments such as future transactions for exchange between currencies (Swap), future contracts for protection of currency rates (Forward).

The transactions in derivative financial instruments is recorded according to fair value and changes in the fair value are recorded in a continuous manner in the Profit and Loss Report. Moreover, the Bank enters into contracts that do not actually constitute derivative instruments but that include integrated derivatives.

The policy of the Bank is to prevent, as much as possible, exposure to exchange rate risks between the various foreign currencies. Inter-currency exposure is managed within a restricted framework, and within such limits as have been approved by the Bank's Board of Directors.

Liquidity Risks

Liquidity risk is a profitability risk of the Bank and for the stability deriving from its uncertainty concerning capability of supplying liquidity needs because of uncertainty concerning availability of sources and ability to recruit (without having an unusual affect upon prices) and concerning the ability to realize assets in fixed time and at a reasonable price. The exposure results from providing long-term loans (even if provided with fluctuating interest) financed by short term deposits. Liquidity risk also exists when recruiting short-term deposits suitable for the period of interest changes in loans, if by this the exposure of interest risk is reduced. This risk also exists in relation to the Bank's activity in foreign currency.

The Bank is exposed to liquidity risks and to uncertainty due to a slowdown in its ability to mobilize negotiable debt or from institutional sources because of market changes, legislative changes and/or changes in depositors' preferences. In order to comply with this risk, the Bank implements a policy of enlarging its depositor base and a decreasing reliance on large depositors. Additionally, emphasis is placed on maintaining a high level of liquidity.

The Bank's policy is to adjust, as much as possible, the repayment periods of these resources to those utilizable in each linked sector. The characteristic of credit and rates of early repayment in the various linked sectors and learning the recycling of short-term deposits have a significant affect on estimated exposure to this risk.

The Bank's risk management is managed similar to market risk as described above in the chapter on Market Risks.

In accordance with Bank of Israel's instructions, every banking corporation is required to establish a comprehensive policy to manage liquidity, and to maintain a data system for supervision, control, and reporting of the liquidity position and its measurement. The instruction requires the Bank to establish a minimum ratio of 1 in respect of liquid assets and liabilities for a repayment period of up to one month (hereinafter: "the Liquid Assets Ratio"). Exposure to liquidity risk and the liquid assets ratio may be measured utilizing an internal model.

On January 13, 2013, the Supervisor of Banks published Proper Banking Management Instruction № 342 on Liquidity Risk Management. As part of preparing to implement the Basel III instructions, the Supervisor found it appropriate, for the interim period until the full update of the instruction according to the Basel documents, to clarify and to emphasize a number of aspects liquidity risk estimations. The date of implementation of most instructions was established for July 1, 2013. The Bank has prepared to implement the instruction on said date.

The Bank examines its liquidity status at least once a month through an internal liquidity model (the Bank determined the situations in which it is required to run the model at more frequently). For the purpose of the model, the Bank collected and continues to collect data concerning early repayment rates, timing and rate of renewal of deposits and savings. In addition, the Bank examines its liquidity status through two extreme scenarios expressing: one scenario is system pressure (e.g., failure at all the banking systems) that may affect the Bank. The second scenario is internal pressure occurring only at the Bank. The various scenarios differ from each other mainly in the recycle rate of the deposits and the ability to realize liquid assets. As part of the implementation of the Proper Banking Management Instruction 342, the Bank has prepared to update the liquidity model to the minimum liquidity ratio model that appears in the aforementioned instruction and to the principles of the (Liquidity Coverage Ratio) in the Basel III instructions. In addition, the Bank is preparing to develop a stable financing ratio model based on the principles of the Net Stable Funding Ratio) in the BaselIIIinstructions by the end of 2013, in accordance with the Proper Banking Management 342 instruction.

The Bank's Board of Directors has determined the liquidity management principles, the level of responsibility and authority, and the warning system, and handling of exceptions to predetermined limits. Determination of the aforementioned limitations and restrictions, takes into account expected events at the Bank and in the business environment, and possibilities available to the Bank concerning mobilization of alternative sources insofar as required, as well as the costs of these resources

The Bank's Board of Directors established limitations (according to the internal model) for the ratio of liquid assets to liabilities (for the repayment period of up to one month) that will not be less than 2.2. Moreover, the Board of Directors has determined additional limitation and among them the limitation relating to liquid assets for liabilities (for repayment periods of up to one month) in an extreme scenario, of not less than 1.0.

The aforementioned ratio as at December 31, 2012 was about 2.7 compared to the ratio of 2.3 for December 31, 2011. This average ratio during the period was 2.3, and the lowest rate of this ratio was 2.2.

According to the Bank's estimation, in consideration of the recycling rate of deposits in past years, the aforementioned exposure risk is higher, among others, because the Bank diversifies its financing sources, meticulously expands the depositor base, and reduces the reliance on large depositors, and maintains sufficient liquidity cushion expressed by a higher than required liquid assets ratio.

Below are the capital requirements due to market risks according to the first Tier (in millions of Shekels):

Type of risk	Capital requirement
Interest rate risk	0.8
Exchange rate risk	12.5
Total	**13.3**

Operating Risks

Operating risk is defined as the risk of loss as a result of non-diligence or failure of internal processes, people, systems, or external events. The definition of operating risk includes legal risks but does not include strategic or goodwill risks.

The Bank operates in a range of financial activities and is exposed to operating risks that include, inter alia, risks of embezzlement and fraud, information technology risks, business continuity risks and information security risks.

In December 2012, the Bank approved updated policies for managing operating risks that include a definition of an operating risk management framework in the Bank, the Bank's risk appetite and an organizational framework through which the Bank's units implements the control processes to minimize risks.

Management of operating risks in the Bank relies on three lines of defense:

Responsibility for operating risk management is that of the unit management. They are the first line of defense, which also includes a function for management of information technology, information security, and business continuity. The Operating Risks Management Unit, compliance officer, legal advisor, and the SOX process that takes place in the Monetary Division represents the second line of defense. The third line of defense is the internal audit, which involves an independent review of controls, and challenge of the processes and operating risk management systems in the bank.

Operating Risks Management relies on an ongoing process of identification, assessment, measurement, monitoring, reporting and control / reduction of risks.

The organizational structure for operating risk management:

Board of Directors – Carries the ultimate responsibility for managing and supervising operating risks, outlining and approving operating risks.

Board of Directors Committee for Risk Management – Holds advanced discussions for the deliberations by the Board of Directors on everything concerning operating risks. Discusses the process / product / new activity whose introduction exposes the Bank to material operating risks, risk management policies and limitations, risk assessment, quality of risk management and controls, capital adequacy, and risk appetite.

Bank Management – By means of the Risk Division consistently and regularly examines the operating risks entailed in Bank activity, as well as loss or near-loss events that occurred.

Operating Risks Management Forum – A committee, headed by the Bank's CEO, which discusses the Bank's operating risk management policies before its submittal to Management and the Board of Directors for the approval of new material products and processes, the approval of relevant operating procedures related to operating risk, monitoring implementation of various audit findings concerning embezzlement and fraud, the risk profile, risk appetite, the mode and quality of risk management, as well as controls and capital adequacy.

Information Technology Manager – Manager of the Resources Division defined as the Bank's Information Technology Manager. As part of management of the division, the Division Manager is responsible for managing information systems, human resources, logistics, Back-End System, Organization and Methods.

Business Continuity Manager – Manager of an organization unit and methods defined as Business Continuity Manager.

Information Security – Information security at the Bank is managed by the the Resource Division manager and Information Security Manager, who are responsible for updating policy and control of this issue. Once a year, the Information Security Manager examines the need to update the information security policy and is brought before management and the Board of Directors for approval.

The Operating Risks Management Unit – The unit is part of the Risks Division and constitutes an independent function for operating risks management. The unit is responsible for the formation of a comprehensive operating framework for operating risk management, planning, implementation, and updating operating risk management methodology, formulation of operating procedures to implement the operating risk management framework, recommendations to management and the Board of Directors concerning operating risk appetite, performance of operating risks surveys, defining reporting processes to various management personnel, challenging the mode of operating risk management in Bank units, receiving reports of material and broad malfunctions, creation of a framework for reporting operating risk profile to the Board of Directors and Management, and involvement in the assessment of the operating risk involved in new products and procedures.

The Bank allocates capital for operating risks in accordance with Bank of Israel's directive. The allocation, in accordance with the base indicator approach that calculates the required allocated capital for operational risk, based on the average gross income multiplied by the last three years with a factor of 15%.

In February 2012, the Bank of Israel published an PBM Instruction 350 on operating risk management. The Bank implemented and assimilated the principles of the instruction in operating risk management in the bank.

Lowering the Operating Risk:

The Bank has in recent years been preparing for the creation of a comprehensive framework of processes and methods to lower the exposure to losses resulting from operating risks. This assessment includes, inter alia, the following measures:

- Reducing operating exposure through adoption of continuous control measures, and a requirement for performing dual controls on each process in which a material operating risk exists.

- Implementing broad controls in various areas of activity according to the risk entailed in the procedure, with emphasis on procedures that lack dual control.

- Conducting an operating risk survey and reviewing embezzlement and fraud in addition to formulating plans to lower risks identified in the survey.

- Assimilation of an organizational culture for operating risk management and increase awareness of this issue among employees.

- Implementation of the approval process prior to operation of any new product / activity / process – which requires the conduction of a comprehensive risk survey, formulating a plan that is adjusted to the risk level, and approval of any new material product in the risk management forum headed by the CEO and in the Board of Directors Risk Management Committee.

- Collection of data on loss or near loss events for monitoring, improvement and drawing lessons. The Bank's Management and Board of Directors receive a report of operating events in which a loss was incurred and events that entailed a potential loss, conduct investigations and draw conclusions concerning the loss or near loss events.

- Map of operating risks, plans to lower risk and reports of loss and near loss events – managed by a designated operating risk management system.

The Bank performs a comprehensive operating risk survey under which operating risks are mapped, identified and evaluated, risks levels and effectiveness of controls with reference to the substantial business and operating procedures. Based on the survey, a plan to lower operating risks is prepared. The plan includes, among others, treatment to reduce risks related to embezzlement and fraud risk.

Insurance – In order to reduce the operating risks to which the Bank is exposed, each year the Bank purchases professional responsibility insurance, as well as property insurance. These insurances provide a response to the following principle issues: external and internal fraud risks (embezzlement), cases of theft of money and precious property, financial damage as result of fake documents such as: checks, exchange bills, deposit confirmation, Guarantee certificates, Letters of Credit, mortgage certificates, and more; damage as result of computer crimes including penetration by a hostile factor into the Bank's computer systems, and damage to physical assets. Financial damages caused to customers or a third party following hardware or software failure. The general responsibility limit of the banking policy is up to $22 million.

Business Continuity

In order to maintain business continuity, survivability and operating continuity of the Bank following a disaster or malfunction, and in accordance with Bank of Israel instruction 355 on Business Continuity Management, the Bank is prepared for emergency situations. The Bank's computerization system is based on two computer sites - the main site in the Bank headquarters in Kiryat Sde Teufah and an alternate site in Jerusalem. Bank activity for readiness for recovery in emergency situations is composed of the following activities:

1. Technological infrastructures for information systems backup.

2. Activity and procedural plans – Over the past year, the Bank created a comprehensive procedural infrastructure to cope with and perform activity under various emergency situations including manual work and the possibility of shifting of critical activity.

3. Drills – The Bank participated this year in the TurningPoint 6 Drill, and even conducted internal drills to test the backup sites as well as activity in several areas in accordance with Business Continuity procedures.

Information Technology Risk and Information Security

Information Technology is a central component in the Bank's proper operation and management. Information technology risks are attributed to the regular activity of the Bank's information systems, broad information technology processes and the development of new activities (projects and systems). Information technology risks include also information security risks and banking risks in communications, that may affect the Bank's business and/or operational procedures. The manager of the Resource Division is responsible for the Bank's Information Technology risks.

In February 2012, the Bank's Information Technology Management policy was updated and approved, including the IT Risk Management policy. In addition, Bank procedures defined the methodological infrastructure for operating risk management in IT processes.

In 2012, the OCIO Unit was set up under the Computerization Division Manager, and its main role is to handle project risks and IT risks. Management includes mapping of existing existing risk and monitoring of the performance of the amortization plans.

The Bank is in the advanced stages of implementing its project involving development of its computer infrastructure as part of the project called "New World." These project risks are managed through forums arranged for project risk management and assistance by external consultants guiding the Information Technology department manager and the Chief Risk Officer (CRO). Furthermore, the amortization plan is examined for project risk management. Continuous monitoring is performed after the implementation of the risks reduction plan included in the plan.

Information Security

According to Proper Banking Management Instruction Amendment № 357, the Bank appointed an information security manager, subject to the Resource Division manager. The information security manager is responsible for determining the Bank's information security policy, to develop an information security plan, monitor its implementation, as well as handling irregular events in the information security area.

Information security risk management supports a response to threats and risks as well as protection of the Bank's information assets and information technology systems.

During the past year, the Bank significantly expanded its preparation in information security in light of the increasing threats and worldwide cybernet attacks. The Bank acquired automated information security monitoring tools and even increased the number of employees in the information security unit.

Every new system or new product/process that is relevant for IT is inspected by the information security manager, including hacking reviews – and no product is operated prior to its approval by the information security manager.

Legal Risks

Definition of Legal Risk is – The risk resulting from potential loss and result of a breach of laws, regulations, or regulatory instructions, or as a result of the Bank's rights or debts that were not founded as required; the risk is also effective when there are contracts with no enforcement capability, legal procedures, or mistaken judgment, that may make it harder for realization or harm the Bank's rights.

The legal risk may result from poor legal or faulty infrastructure on which the Bank relied in providing service to the customers, received sufficient service and/or received collateral from customer or from third party such as: connection that is not properly backed up by a contract, collateral that cannot be used as result of a defect in its creation or recording, or because the collateral was stolen or lost its value, etc.

In addition, legal risk at the Bank may be created as result of external factors that are not dependent on the Bank, such as: change in legal instructions, regulations or instructions of the various supervising (instructions of the Supervisor of Banks, instructions from the Securities Authorities, Money Laundering Prohibition Authority, etc.) or new verdict by the courts according to which the Bank is required to operate on a certain issue in a different manner then it used to operate before that verdict.

The legal risks are part of the overall operating risks the Bank is exposed to. The lawyer, Sarit Vistuch, Vice CEO and legal adviser is responsible for the Bank's legal risk management, assisted by employees from the the Bank's legal department. The regulatory legal risk is managed at the Bank in an organized and structural manner, anchored in written procedures and policies for the purpose of minimizing as much as possible the realization of these risks and to minimize the damage caused to the Bank in case this risk was indeed actually realized.

According to the Bank's policy and procedures, any legal issue emerging as part of business management is transferred to the Bank's Legal Department (each in its area of responsibility). Each claim, legal procedure or lawsuit threat due to the Bank's employees are transferred for handling by the legal department. Every contact by a customer to a Bank employee with a legal question is transferred to the legal department or legal assistance for a response.

Goodwill Risk

Goodwill Risk is a risk for loss deriving from damage to the Bank's good name or damage to the external assessment of its banking capabilities or to its financial strength. Such a risk may be caused as result of factors within the Bank such as: operational failure of the Bank's systems, failure in preventing events connected to the capital core, fraud and embezzlement by employees and so forth; or as result of external factors of the Bank such as: economic crisis in Israel or worldwide, failures at other banks, class action, etc.

The Goodwill Risk is characterized by two principle risk factors – first grade risk and second grade risk. A first-grade risk is a pure Goodwill Risk that is attributed to the realization of a risk managed in the Bank and that harms Bank profits. For instance, credit risk, that is a first grade risk, may cause loss from actual realization of the event according to which, a certain borrower does not repay his debts to the Bank. Second grade risk is risk deriving from realization of other risks. For instance, realization of operational risk from theft on a large scale may lead to decline in reputation (and this without connection to the loss from the actual theft) expressed by a decrease in the Bank's profits.

Among the risk factors are also included a number of additional risks such as operational risk, compliance risk and strategic risk.

Management of Goodwill Risk is divided into two: risk prevention, and managing risk after realization of the event or indications for the event's realization.

On the level of risk prevention, the Goodwill Risk takes up a central place in the Bank's management. The risk appetite, procedures, limitations, and activity areas clearly aim to reduce the exposure to Goodwill Risk.

the Board of Directors has the ultimate responsibility for managing and supervising Goodwill Risk and creating a proper risk environment. The senior management is generally responsible for reducing and managing Goodwill Risk. The manager of the Retail Division has been defined as this risk manager.

In addition, various units of the Bank are involved in risk management. The spokesman unit serves as responsible default for handling all crystallizing or potential events, concentrating and reporting to the Retail Division manager. The additional units involved in risk management are: unit for public complaints, legal department, compliance officer responsible for implementing the Money Laundering Prohibition Act, factors involved in risk management, Human Resources.

The Bank's policy for risk management defines three types of events that might be risk events:

1. Expected events that can be prepared for in advance.

2. "Rolling" events that might develop gradually and that might become goodwill risk events.

3. Unexpected events that suddenly occur.

The handling of each risk event is managed and centralized by the Bank's spokesman in cooperation with the Retail Division manager while in relation to each of the types of the aforementioned events, operating methods and identity of additional relevant factors working with them were defined.

Compliance Risk

General

The severity of the compliance risk increased in recent years due to increased regulation in Israel and around the world, in addition to administrative enforcement and American authority requirements. The consumer evidence in managing banking businesses on the part of various legislative parties and authorities as well as the complexity and development of banking activity, requires the Bank to be more strict on the existence of the overall obligations applicable to banking corporations, in its relations with its customers, by virtue of legislation, regulations, orders, permits, and the instructions by the Bank of Israel.

Proper Banking Management Instruction 308 requires banks to comply with consumer directives that apply to the bank's relationship with its customers.

Consumer instructions are laws, regulations and instructions governing the banking activities on every issue covering the relation between the Bank and its customer as part of the obligations applicable to the Bank towards the public and its customers, including the Money Laundering Prohibition Act, 5760 – 2000, prohibition on money laundering (requirements concerning identification, reporting and recording of banking corporations to prevent money laundering and financing terrorism), 5761 – 2001, instructions of the Banking Supervision Order and Securities Authorities guidelines.

Compliance Risk Management

Compliance risk is the risk that a corporation will suffer from a legal or regulatory sanction, significant financial loss or damage to its reputation as a result of failure to comply with consumers instructions, legal directives, directives from the Supervisor of Banks and other relevant regulatory instructions.

Compliance risks are managed in the Bank on all organizational levels from compliance trustees in branches and headquarters to product management departments. Therefore, the Bank bases all its work procedures on the principle of dual control of edits and checks. Furthermore, there is a structured process according to which, each change in consumer instructions affecting the Bank will be integrated into the Bank's procedures, work procedures and forms, and training. The Legal Department and the Organization and Methods Department support this procedure.

The compliance officer is responsible for implementing Bank policy and to formulate a comprehensive work framework for risk management and its approval by the Bank institutions. This framework includes planning, implementation and update of compliance risk management methodologies, conducting regular compliance surveys, defining reporting procedures for various parties in management.

According to Instruction 308, an infrastructure survey will be conduced once every five years during which the consumer instructions, risks of occurrence of irregular events along with the definition of various controls will be mapped. The survey was assimilated in the automated risk management system that enables regular and dynamic monitoring of compliance risks.

The compliance officer conducts symposiums for all compliance trustees and prohibition against money laundering, in conjunction with the party responsible for prohibition of money laundering, convenes a conference for branch managers, training and instruction for all employees as part of the bank courses.

Administrative enforcement risks

General

The Streamlining of ISA Enforcement Procedures Law (Legislative Amendments) 5770-2010 effected several significant changes by adding another track to adopt administrative proceedings for violations of Securities Laws and their subsequent regulations. Possible sanctions against a corporation and/or individual who violates these provisions include significant financial sanctions (up to NIS 5 million for a corporation) without possibility of insurance / indemnity, prohibition of serving as a senior officer, suspension or even revocation of license in accordance with the Advisory Law.

In the meantime, legislation in the administrative enforcement area expanded to other areas: insurance, labor laws, and anti-trust.

The risk to the Bank and to its employees is reflected in exposure to imposition of sanctions by the Securities Authority for violation of the Securities Laws including in cases of negligence and failure to comply with the provisions.

Risk Management Administrative Enforcement

The Bank is preparing to curtail exposure to this risk by formulating an internal enforcement plan based on criteria that were set forth by the Securities Authority in August 2011. As part of the Plan, the Bank, with the assistance of external consultants, conducted a survey to map risks in the securities area (at the same time, a similar survey was being conducted in the insurance area) in the Bank and in its subsidiaries.

Handling of risk management in the Bank and in the subsidiaries is centralized with the Chief Risk Officer – CRO, who is a member of the Bank's management and who was appointed by the Board of Directors to supervise internal enforcement in the Bank and its subsidiaries, and operates via the Internal Enforcement Department that was set up for this purpose in the Risks Division.

In accordance with the principles set forth in the criteria document, the Bank is working to curtail exposure to this risk by way of regular handling of the gaps discovered in the survey, training and assimilation to increase compliance, and regular management including drawing conclusions in reports on events that might be considered as violations of the provisions of the law.

Money Laundering and Terrorism Financing Risks

General

Prohibition of money laundering and financing terror risks (Hereinafter: "Money Laundering") are risks of imposition of significant financial sanctions on the Bank in light of failure to comply with the provisions of the Law concerning the prohibition against money laundering and against financing terrorism as well as the risk of the formation of criminal responsibility of the corporation and its employees. In addition, materialization of a violation of the provisions of the law in the area of the prohibition against money laundering and financing terror may result in materialization of the goodwill risk. As part of its activity, the Bank is exposed to money laundering and terrorism financing risks. This exposure focuses at the account opening stage, as well as in the process of account managing. The Bank may be exposed to parties that are interested in "exploiting" it for the purpose of money laundering which have at their source violations as defined as "predicated offenses" in the Money Laundering Prohibition Act and to finance terrorism through it.

The Bank is subject to various provisions as part of the prevention of money laundering and financing terror that includes, inter alia, the Anti-Money Laundering Law, The Law Prohibiting the Financing of Terrorism, The Injunction Prohibiting Money Laundering, Regulations Prohibiting the Financing of Terror, the provisions of Proper Banking Management 411, various circulars, etc.

Management of the Prohibition of Money Laundering and Terrorism Financing Risk

The concentration of risk management in the Bank is carried out by the party responsible for the prohibition against money laundering and financing terror, who is directly subject to the director of the Risk Management Division - CRO, who is a member of the Bank's management. The Board of Directors and the Bank's management determine the procedures and policies on the issue of Prohibition of Money Laundering. Other instructions are according to and subject to the provisions of the law. His job description includes, inter alia, meticulous monitoring of bank activity in accounts, in order to identify potentially irregular activity that smut be reported to the Anti-Money Laundering Authority, conduct controls of reports based on the type and size of activity, delivery of reports on irregular activity to the Anti-Money Laundering Authority, conduct various controls of activity in various accounts in accordance with their profile, update policies and procedures in accordance with legislative updates and provisions, provide regular advice to branches in this area, and to carry out training adapted to various employees in the bank, based on their positions. The responsible person is updated continuously on renewals of the legislation, the orders and standards linked to the prohibition of money laundering, among others, by participating in meetings and seminars on the issue. It is his responsibility to take care of the implementation of all the implications resulting from the updating of the Bank's activity.

In order to implement the law and assimilate its provisions, the Bank appointed compliance trustees who also serve as anti-money laundering trustees in the branches and in the headquarters (Hereinafter: The Trustee"). The Trustee is selected from among Bank employees upon recommendation of the branch manager / department manager in the headquarters / party responsible for prohibition against money laundering and financing terror. The trustee is a professional party linked to the location where the transactions are implemented and provide an immediate response to questions arising at branches. His role is to help identify problems or difficulties in implementing the provisions concerning the prohibition against money laundering to the extent possible in real time and to serve as the first professional address for branch or unit employees in which they are working to prevent money laundering and financing terror.

The trustee receives increased training and seminars for the purpose of raising its level in the area and is a linking factor between the responsible person on the issue of prohibition of money laundering and the branch.

The party responsible for the prohibition against money laundering conducts symposiums for all compliance trustees and prohibition against money laundering, in conjunction with the compliance officer, convenes a conference for branch managers, regular training and instruction for all employees as part of the bank courses. In addition, in 2012, the Bank created educational software that includes at test on assimilation of the software content among employees that is updated in accordance with the changes and developments in the field and in the provisions of the law. Bank employees are examined in a test and their ability to successfully pass it.

On February 14, 2013, the Bank received a report conducted by the Supervisor of Banks on the prohibition against money laundering, following an audit conducted the Bank that referred to Bank activities between 2007-2010. The report includes a list of findings, as well as requirements to implement measures concerning the prohibition against money laundering and financing terrorism. The Bank was given the right to submit its written response to the report within 30 days from the date of its receipt, while noting the fact that it would consider filing a motion to impose a financial sanction on the bank in accordance with the authorities prescribed by law. The Bank is studying the report's findings and is preparing to submit its written response within the obligatory timetable.

At this stage, the Bank cannot assess whether financial sanctions will be imposed on the Bank as a result of this report and if so, the sum of said sanction.

The Bank believes that improvements made in the bank's performance concerning money laundering following the audit significantly reduces the bank's exposure to the risks of money laundering.

Affect of Risk Factors on the Transactions of the Banking Corporation

The Bank is required, as all the banking corporations, to included a table with risk factors in each of the detailed categories below, and to estimate the affect of the risk factor on its business. As part of these evaluations, the potential exposure or the damage as result of the occurrence of a certain event, as well as the probability that such an event may occur, should be estimated. Moreover, the adequacy of the control of the risk environment, as other activities implemented by the Bank, for purposes of risk management, as it affects the level of risk exposure. Therefore, the risk assessment in the table below are the Bank's subjective evaluation of the affect of the residual risk on its business.

	Risk factor	affect The risk
1	**Total Affect of Credit Risks** The risk derives from the borrower's non-compliance for his liabilities to the Bank according to the agreement. Deterioration of various borrowers' stability and/or ability to repay the credit might negatively affect the value of the Bank's assets and profitability. Risk exposure is managed, among others, through the Bank's credit policy and exposure limitations concerning various types of borrowers in various sectors of activity.	**Medium**
1.1	**Risk due to quality of borrowers and collaterals** Risk stemming from deterioration of the quality of the borrowers and/or the value of the collateral provided as security to the Bank, that might negatively affect the chances of collecting the credit and therefore upon the value of the Bank's assets and its profitability. Risk exposure is managed, among others, through clear definition of credit policies, appropriate underwriting and limitation of activity to specific types of borrowers in the specific sectors of activity and various products.	**Lower**
1.2	**Risk due to branch centralization** The risk results from a large volume of credit provided to borrowers in a certain economic branch relative to the credit portfolio. Deterioration in business activity results in the same branch might harm repayment ability and/or the value of the collateral provided by some of the borrowers in the branch and, as a result, might negatively affect the value of the Bank's assets and its profitability. Risk exposure is managed, among others, through restrictions of the Bank of Israel in this regard, and limitations determined by the Board of Directors concerning maximum exposure in various economic branches. The Bank does not go beyond the aforementioned restrictions.	**Medium**
1.3	**Risk due to centralization of borrowers/group of borrowers** The risk results from deterioration in the situation of a large borrower or a large group of borrowers (relative to the credit portfolio), which may negatively affect the chances for collecting the credit, as well as the value of the Bank's assets and its profitability. Risk exposure is managed, among other, through restrictions by the Bank of Israel in this regard, and limitations determined by the Board of Directors concerning maximum exposure for a borrower and for a group of borrowers. Current controls also exist concerning compliance with these restrictions. The Bank does not go beyond the aforementioned restrictions.	**Lower**

	Risk factor	affect The risk
2	**Total Affect of Market Risks** The risk results from changes in prices or changes in financial market rates or other economical parameters, which affect the value of the Bank's assets or liabilities, and which may result in erosion of its capital or damage to its profitability. Risk exposure is managed separately for each risk as detailed below and also centralized through the VaR model.	**Lower**
2.1	**Interest rate risk** The risk derived from the difference between assets value for unexpected changes in interest rates and between this sensitivity of the liabilities – changes may bring erosion in the Bank's capital. As a result from the exposure to interest the various linkage bases may cause future decrease (during assets' or liabilities' life) of financing income. Risk exposure is managed, among others, according to estimates of market variables and subject to restrictions on sensitivity from net capitalizing financing income of the Bank in a scenario to change in shekel interest curves and index linked interest. The exposure restrictions are being controlled continuously.	**Lower**
2.2	**Inflation risk** The risk results from changes in the rate of inflation that may result in a loss in the value of the economic difference between assets and liabilities (active financial capital) in the index linked sector. Risk exposure is managed, among others, subject to limitations concerning the amount of active financial capital, while considering changes in relevant economic data according to market conditions. The exposure restrictions are being controlled continuously.	**Lower**
2.3	**Exchange rate risk** The risk results from changes in the rate of inflation that may result in a loss in the value of the economic difference between assets and liabilities (active financial capital) in the foreign currency and linked to foreign currency sectors. Risk exposure is managed, among others, subject to limitations concerning the amount of active financial capital, while considering changes in relevant economic data according to market conditions. The policy of the Bank is to prevent, as much as possible, exposure to exchange rate risks between the various foreign currencies. The exposure restrictions are being controlled continuously.	**Lower**
2.4	**Price risk for securities and debentures** The risk results from a decrease in the value of securities and debentures held by the bank. The Bank's securities portfolio includes mostly Government debentures and a small part in corporate debentures. The Bank's policy does not enable significant activity in securities (not for purposes of investment and not for purposes of trading). The percentage of the Bank's holding (including indirect holding) in securities and indexes of securities is negligible. Risk exposure is managed through limitations and restrictions on the amount of investments, characteristics, marketability, average duration of the portfolio, and the amount of expected loss from these investments. The limitations and restrictions are managed through the VaR model and through extreme scenarios	**Lower**
3	**Liquidity risk** Liquidity risk results from uncertainty concerning availability of sources and ability to recruit (without influencing unusual affect on prices), and concerning the ability to realize assets in limited time and at a reasonable price. Extreme "supply and demand" circumstances in financial markets, may create unexpected costs of source mobilization that may affect the financing income. The management for risk exposure is implemented, among others, through expanding the depositor base and decreasing reliance on large depositors, extension of the sources' average duration, and maintaining a high level of liquidity. The Bank has a system of controls based on an internal model that examines a number of scenarios. Moreover, over time, the Bank examines behavior of its customers that may affect exposure to this risk.	**Lower**
4	**Operating Risk** The risk of loss as a result of non-diligence or failure of internal processes, people, systems or external events. Risk exposure is managed, among others, through operating risk survey, procedures writing, implementation of controls, and integration of systems for issues affecting risk exposure; e.g., human resources, information security, processes, etc. The Bank maintains an organized process for approval prior to the operation of any new product / activity / process, including a review of risks and implementation of adequate controls. The Bank monitors loss and near loss operating events in order to draw conclusions and improve control.	**Medium**

	Risk factor	affect The risk
5	**Information Technology Risks** This risk is a business and operating risk stemming from ongoing activity of the Bank's information systems, the complexity of work procedures implemented in the various computer units, or from ongoing activity of infrastructure system and/or from hardware or software components. Including, information technology and banking risks in communications, that may affect the Bank's business and/or operational procedures. The Bank is in the process of project implementation for improving its computer systems as part of the project called "New World." These risks are managed through forums arranged for project risk management and assistance by external consultants guiding the Information Technology department manager and the Chief Risk Officer (CRO). furthermore, the amortization plan is examined for project risk management. Continuous monitoring is performed after the implementation of the risks reduction plan included in the plan.	**Medium**
6	**Information Security Risks** Risk of damaging information that exists in the organization, particularly through harming technological assets and the physical environment of the computerized systems. Information security risk management in the bank supports a response to threats and risks as well as protection of the Bank's information assets and information technology systems. The Bank does not allow its customers to carry out transactions through digital means – website, cell phone. Exposure to risk therefore is not high.	**Medium**
7	**Legal Risk** The risk results from unexpected events, such as legal claims, including class actions, inability to enforce agreements, or judicial rulings against the Bank that may harm the Bank's profitability. The management of risk exposure is performed, among others, through legal controls and internal and external legal consultancy system. Past experience ascertains that the aforementioned events did not expose the Bank to significant losses.	**Lower**
8	**Regulatory risk** Regulatory risk is an existing or prospective risk on the Bank's income and capital that may create regulatory changes or in legislation, which can have significant affect on the bank's activity and obligations imposed upon it. The Bank, as a banking corporation and as a public company, is subject to many regulatory instructions expressed by legislation, secondary legislation, policies and instructions for the implementation of various authorities and supervising entities. Management for risk exposure is implemented, among others, through existence of ongoing monitoring of proposals and legislative memorandums, legislative instructions, and drafts and instructions from the various regulators (the Supervisor of Banks, Securities Authorities, Money Laundering Prohibition Authority, the Authority for Information and Technology, Ministry of Justice, etc.). Moreover, monitoring is implemented after new verdicts by the various legal systems in Israel. In order to verify completeness of the instructions concerning the implementation of the monitoring, the legal department is responsible for current professional publications of a number of leading law firms in the banking area in Israel, capital market, real estate, Labor Law, etc.	**Lower**
9	**Goodwill Risk** The risk stems from damage to the Bank's reputation as a stable and reliable financial institution following publications, correct or incorrect, on customer issues, investments, and various regulatory entities. Damage to reputation may result in transfer of customers' activity to other providers of financial services, harming the Bank's activity and profitability. Management of exposure is divided into two: risk prevention, and managing risk after realization of the event or indications for realization of the event.	**Medium**
10	**Strategic risk** The strategic risk results from mistaken business decisions, improper implementation of decisions or lack of response to sector changes, economical or technological. The risk results also, among others, from income from new areas, expansion of existing services and increase of infrastructure investment for realization of business strategy. This risk has a potential of adjustment between the Bank's strategic objectives, business plans developed for obtaining these objectives, allocating resources to comply with these objectives, and the quality of the implementation. Exposure management for this risk is implemented, among others, through building strategic arrangements, receiving external professional advice in the area, and addition activity for reducing the risk.	**Medium**

	Risk factor	affect The risk
11	**Compliance Risk** Compliance risk is attributed to a failure to comply with consumers instructions, legal directives, directives from the Supervisor of Banks, and other relevant regulatory instructions. Consumer debts that apply to the Bank are cross-organizational debts that pertain to a wide range of activities, processes, and products. Proper Banking Management Instruction 308 requires banks to comply with consumer directives that apply to the bank's relationship with its customers. Management of exposure to risk is managed on all levels of the organization, from compliance officer, compliance trustees in the branches and headquarters to the product management department and is implemented in accordance with a structured process according to which, each change in consumer instructions affecting the Bank will be integrated into the Bank's procedures, work procedures and forms, and training.	**Lower**
12	**Prohibition of Money Laundering and Terrorism Financing Risk** Prohibition of money laundering and financing terror risks are risks of imposition of significant financial sanctions on the Bank in light of failure to comply with the provisions of the Law concerning the prohibition against money laundering and against financing terrorism, as well as the risk of the formation of criminal responsibility of the corporation and its employees. In addition, materialization of a violation of the provisions of the law in the area of the prohibition against money laundering and financing terrorism might result in materialization of the goodwill risk. In order to minimize exposure to the risk, a party responsible for the prohibition against money laundering was appointed to be responsible for implementing the provisions of the law in this area and its assimilation including training to all Bank employees in this area. In addition, the Bank appointed compliance trustees who also serve as anti-money-laundering trustees in the branches and in the headquarters.	**Lower**
13	**Administrative enforcement risk** Administrative enforcement risk is a risk of imposition of significant financial sanctions and/or anti-trust sanctions on any of the Bank's employees for failure to comply with the Securities Laws. The Bank is preparing to reduce the risk by appointing a manager of the Risks Division as Supervisor of Internal Enforcement in the Bank and in its subsidiaries, establishment of an Internal Enforcement Department in the Risks Division, formulation of an internal enforcement plan based on the principles established by the Securities Authority, conducting a survey to map gaps in the area and handling the bridging of the gaps, and ongoing handling of events that might be considered as violations, including drawing the relevant conclusions.	**Medium**

Internal Auditor

Until March 20, 2012, Mr. Motti Gedali served as the Bank's internal auditor. Mr. Motti Gedali has a BA degree in Economics and Political Science and a MA in Business Administration from The Hebrew University in Jerusalem. Has extensive experience in audits. Between 1976-2005, he held various positions in the Bank of Israel at the Supervision on Banks Department as auditor and as manager of the audit unit specializing in supervising and control on the manner of exposure of the banking corporations in Israel to all kinds of financial risks. His appointment was approved by the Audit Committee and the Board of Directors on November 25, 2010. The appointment was approved in view of Mr. Gedali's skills, experience, and education.

On February 22, 2012 (after recommendation of the Audit Committee as of February 9, 2012), the Board of Directors approved the resignation of Mr. Gedali (as predetermined, with his consent, for a set period) and also appointed Mr. Rom Sagy as the Bank's Internal Auditor. The appointment was approved in light of Mr. Sagy's skills, experience and education. This decision went into effect on March 20, 2012, upon approval by the Bank of Israel of the appointment, and from that date, Mr. Ron Sagy has been serving as the Bank's internal auditor. Mr. Ron Sagy has a BA in Economics from The Hebrew University of Jerusalem. Mr. Ron Sagy has banking experience and in his previous position, served as VP, Director of the Banking Infrastructure and Operations Division in the Bank.

The Internal Auditor complies with the conditions determined under paragraph 3 (a) Internal Audit Law; the instructions of section 146 (b) of the Companies Law 5759 – 1999, as well as paragraph 8 of the Internal Audit Law, 5752 - 1992. The Internal Auditor is no family member to any of the senior officers or parties of interest at the Bank; he has no material business relations with the Bank and does not indirectly hold Bank securities. The Internal Auditor is also responsible for the Public Ombudsman Unit, does not serve any additional function besides his position as the Bank's Internal Auditor. In addition, the Internal Auditor does not serve in any function outside the Bank that creates or might create a conflict of interest with his position as Internal Auditor.

The internal auditing employees comply with the instructions of paragraph 8 of Banking Regulations (internal auditing), 5752 – 1992, and are only appointed with the approval of the Internal Auditor.

The person responsible for the Internal Auditor is the Bank's Chairman of the Board of Directors.

The Internal Auditor's scope of employment and and the staff subject to him during 2012, averaged 9.5 positions annually, (including editing the internal audit through external professional factors to an average of 1.5 positions). The scope of the average positions in public inquiries was, in 2012, a single position.

Auditing Program

The internal auditing at the Bank operates according to the annual work plan based on the multi-year auditing work plan, consisting of an ongoing annual work plan and a work plan for the next three years.

The multi-year work plan refers to most of the audit subjects included: the Bank's organizational units, subsidiaries and associated corporations, work processes, products marketed, and computerized systems. Moreover, the internal audit audits the Bank exposure management procedures to the various risks, such as: credit, financial, operating (including fraud and embezzlement risks), compliance risks and so forth. Moreover, the internal audit monitors the correction of significant deficiencies disclosed in the audit work of the Internal Auditor, of the auditing accountant and of the Supervisor of Banks at the Bank of Israel. An annual summary report is submitted once a year to the Chairman of the Board of Directors, the CEO of the Bank, and members of the Audit Committee.

The work plans, annual and multi-year, are arranged according to the Internal Audit Law, 5752 - 1992, according to the Banking on Internal Audit (5752 - 1992) and according to the Proper Banking Management instructions.

The annual and multi-year work plans are derived from the systematic methodology of risk assessment and controls, according to which the audit frequency for each issue are determined. In the second half of 2009, with the assistance of an external company, a comprehensive review of risks was carried out for on all the bank's divisions. In 2011, the internal auditing performed a comprehensive updating of the multi-year work plan of the internal auditing, which will be derived from the annual work plans as of 2012. During the update of the multi-year work plan, the mapping of audited entities of the bank was also updated and the update frequency for examination of these entities was established according to the business and operating developments in accordance with the regulatory directives. The frequency of the audit is determined according to a matrix managed by the Internal Auditor, relating to evaluation of the exposure to financial damage and the evaluation of the quality of the controls intended to reduce risks. These estimates are updated regularly. As result, concerning the issues with higher risks, the audit frequency will be yearly and on issues with a lower risk, the audit frequency is two or three years.

The audit committee and the Board of Directors approved this work plan and because of this the increase of internal auditing resources conform the requirements according to the new multi-year work plan.

As part of the integration process of the ICAAP at the Bank and according to the guidelines of the Supervisor of Banks and also the Basel II instructions, it is required that an independent factor will challenge and examine the Bank's implementation process. The Bank's internal auditing is determined as the independent factor that has the task to prepare the independent review document. The independent review document reviews the risk management system that is implemented by the Bank, the ratio between risk and capital level of the banking corporation, and the methodologies developed for monitoring the compliance with the internal capital policy. The independent review document includes details of the examination procedures and implemented audits, the implementing factor, as well as the main conclusion arising from the review. The document will be presented to the audit committee and the Board of Directors. For the purpose of preparing this review, the internal auditing is assisted by an external professional consultant.

The annual and multi-year work plans were discussed and approved by the audit committee on December 20, 2011, and after that by the Chairman of the Board of Directors and by the assembly of the Board of Directors at their meeting on December 29, 2011.

During 2012, the internal audit operated according to this work plan. However, in light of the changes in business activity and in a number of material procedures at the Bank, and conforming to the recommendations of the internal audit, the internal audit approved, during the year, an update to the work plan. The annual and multi-year work plan leaves to the Internal Auditor's discretion to deviate from them, subject to updating the Chairman of the Board of Directors and the Chairman of the Audit Committee in a current manner and receive their approval.

Also, significant transactions, if any, implemented by the Bank, are reported to the Internal Auditor and are examined by him, including the process for approving these transactions. As part of this examination, a material transaction agreement in the area of information systems were examined, as well as the sales transaction of the Bank of Jerusalem building, was guided by the Internal Auditor.

The Internal Auditor is authorized as part of the approved budget, to be assisted through outsourcing, to perform the auditing work that requires knowledge and special expertise and/or in case of lacking a job opening.

The Internal Auditor prepares the internal audit according to accepted professional standards, and operates according to instructions and guidelines issued by the Supervisor of Banks.

During 2011, an external assessment was performed on the internal auditing activity of the Bank and its compliance in arranging the Financial Statements according to the accepted professional standards was examined. The findings of the examination, that the internal audit the Bank operated according to the accepted professional standards, has been presented to the Audit Committee and the Board of Directors. In 2012, the internal audit performed an internal procedure of assessing the quality of work of the internal audit function whose findings were presented to the Audit Committee.

The Internal Auditor has free and complete access to information and data as stated in section 9 of the Internal Audit Law, 5752 – 1992, including free and complete access to the bank's data systems including financial data derived from these systems and data from subsidiaries.

During December 2011, the Bank of Israel published a new banking management instruction referring to the internal audit's function. The purpose of this instruction is to implement the general principles specified in the Basel II documents concerning the Internal Audit. The instruction defines the functional role of the Internal Audit, the required work method for applying the audit function in order to effectively fulfill it, the reporting format for the audit function, and more. The instruction became valid on July 1, 2012. The Internal Auditor worked in order to implement this instruction.

Reference to corporations that constitute material holdings

The Internal Auditor also serves as Internal Auditor of all the Bank's subsidiaries. The subsidiaries are included in the annual and multi-year work plan and are audited according to the frequency determined according to risk estimates and the existing audit, as specified in the previous paragraph.

Audit Reports and Discussions Thereon

According to the Audit Committee's work procedure and the work Internal Auditor's procedure derived from it; each audit report is submitted in writing to the auditing factor, the CEO, the Chairman of the Board of Directors and to the Chairman of the Audit Committee. For every audit report there is a discussion with those audited and also a concluding discussion is held with the responsible managers and the Bank's CEO on the findings and material recommendations. The audit reports are also presented for discussion to the audit committee and this after receiving suitable reference to the report's findings from the auditing factor and the Bank's CEO.

The summary of the internal auditing activity for the first half of the year 2012 was discussed by the Audit Committee on July 24, 2012. The annual report summarizes the internal auditing activity during all of 2012, also including monitoring implementation of the annual work plan, and was discussed at the meeting by the Audit Committee held on January 29, 2013.

Internal auditing also reports quarterly to the Audit Committee, on the manner and level of implementation of the by the internal auditing's recommendations that arose from the audit reports that were held in the Bank's various activity areas.

The reports on the summary of internal auditing activity and on the manner and level of implementation of the by the internal auditing's recommendations are also submitted to the Chairman of the Board of Directors and the Bank's CEO.

Compensation of the Internal Auditor

As mentioned above, the Internal Auditor has been serving in this position since March 20, 2012. His salary cost amounted in the report year to NIS 992 thousand (this cost includes the total cost of salary for the report year including the cost for his position as deputy internal auditor up to March 20, 2012).

Evaluation of the Board of Directors

Annually, the Audit Committee holds a meeting with only the Internal Auditor. This meeting took place on November 20, 2012.

Based on the current reports submitted by the internal auditor and in accordance with the work procedures of the internal audit function, the Audit Committee expresses its opinion concerning the internal auditor's compliance with professional standards, according to which the audit reports on the bank's various activities were prepared. In addition, the Audit Committee conducted a survey of the function of the internal audit carried out by an external party in accordance with the provisions of Proper Banking Management 307 The Internal Audit.

The audit committee and the Board of Directors believe that the salary and the payments that have been provided to the Internal Auditor have no affect on the Auditor's professional discretion.

The Board of Directors and the audit committee believe that the Internal Auditor's scope, nature, continuity of activity, and work program are reasonable for the existing circumstances, and they address and meet the objectives of the bank's internal audit.

Disclosure Concerning the Process for Approving Financial Statements

The organization at the Bank responsible for the ultimate control (as defined in Proper Banking Management Instruction № 303) is the Bank's Board of Directors, the names of the Board of Directors' members and their accounting and financial skills are specified in chapter "The Board of Directors, the management and the salaries of senior officers" are listed below.

Principle issues related to disclosure are provided in the Financial Statements, discussed in the Disclosure Committee headed by the CEO with the participation of the Chief Accountant, legal advisors, additional management and accounting managers. As part of the discussions, the committee included issues that materially affect the Financial Statements, issues of public interest, developments that must be reported to the public, and any issue the committee finds necessary to discuss before transferring the reports to the Audit Committee.

Prior to approval of the Financial Statement by the Board of Directors, drafts of the financial reports, directors' report, and the annual periodic report are transferred to the Audit Committee. The Bank authorized the Audit Committee to serve also as a committee for examining the Financial Statements. The committee consists of the following members of the Board of Directors: Chairman of the committee, Mr. Shmuel Eshel who is an external director; Mr. Shalom Hochman and Mr. Adiv Baruch, who are external directors, and Mr. Ram Harmelech.

The committee discusses the Financial Statements' format and decisions are made for recommending approval of the Financial Statements for the Board of Directors.

After reaching an agreement concerning such recommendation, drafts of the financial reports, directors' report, annual periodic report are transferred for review by members of the Board of Directors a number of days prior to the date of the meeting fixed for approving the reports.

During the meeting of the Board of Directors, operating results and financial status are reviewed, and information concerning the Bank's activity is presented and the directors' questions are answered.

The Bank's external accountant also participates in the meeting in order to express a professional opinion concerning the financial reports and accounting issues relating to the financial reports. After concluding the discussion, the Board of Directors decides on approving the financial reports.

Miscellaneous

Circular on the issued of "Management Responsibility for Internal Controls on Financial Reporting – SOX Act 404"

On December 5, 2005 the Supervisor of Banks published a circular detailing instructions Application of Requirements of Paragraph 404 of the SOX Act. Section 404 determines regulations of the SEC and the Public Company Accounting Oversight Board (PCAOB) concerning management's responsibility for internal controls over financial reporting.

As part of implementing the instructions, the Bank implemented , in cooperation with an external accountant, recognition of business accounts and procedures relating to financial reporting and appropriate disclosure. In these processes, documentation was prepared and risks and controls were evaluated, including review of existing internal controls and risks at the level of processes, procedures and transactions

Moreover, the Bank completed evaluation of the effectiveness of the controls, including documentation of control effectiveness examinations and analysis of existing differences relative to the internal control model.

The management of the bank, under the supervision of the Board of Directors, evaluated the effectiveness of the bank's internal control over financial reporting as at December 31, 2012, based on the criteria that were established in the internal control model by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment, the management believes that as at December 31,2012, the Bank's internal control over financial reporting is effective.

The effectiveness of the Bank's internal control over financial reporting as at December 31,2012 has been audited by the Bank's visiting accountant from "Kost Forer Gabbay & Kasierer", as was stated in their report on page 202 in which an unqualified opinion has been included concerning the effectiveness of the Bank's internal control over its Financial Reporting as at December 31,2012.

Evaluation of Controls, Processes and Procedures Concerning Financial Statement Disclosure

The Bank's Management, in cooperation with the CEO and Chief Accountant, as of the end of the period covered by the report, evaluated the effectiveness of the Bank's controls, processes and procedures relating to disclosure. Based on this assessment, the Bank's CEO and Chief Accountant concluded that as of the end of this period the Bank's controls, processes and procedures relating to disclosure are effective; in order to record, process, summarize and report on data that the Bank is required to disclose in the interim report according to the public reporting requirements of the Supervisor of Banks, as of the date determined in these requirements.

During the fourth quarter ending on December 31, 2012, no change occurred in the Bank's internal control over Financial Reporting that materially affected, or that might have reasonably materially affected the Bank's internal control over financial reporting.

Ethical Code

The Bank has an ethical code that was approved by the management in 2009 whose purpose is to express the Bank's policy in the area of professional ethics of its employees and determine the level of ethical standards according to which its employees are required to operate.

The Bank insists on the fulfilling the law and the instructions of various authorities, and these are anchored it is procedures. The Bank's ethical code is intended to add a value-based infrastructure to its procedures in order to ensure a valued and qualitative work environment for its employees.

At the base of the ethical code are a number of principles: personal honesty, fairness, reliability, professionalism, responsibility, as well as loyalty to the Bank and its customers.

Donations

The Bank's donation policy is implemented according to management's decision according to the framework of the Bank's budget. This policy includes criteria for the selection of institutions and associations. In the year 2012 the bank donated NIS 537 thousand (2011 – NIS 598 thousand) to help charities and public institutions.

Transactions with a Controlling Shareholder

1.1 According to the Securities Regulations (Periodic and Immediate Reports), 5730 - 1970, a corporation that must report under these regulations will submit in the immediate and in the periodic report details "concerning every transaction entered into by the corporation with the controlling owner or where the controlling owner has a personal interest in its approval." Among others, the reporting corporation is required to include "details of the identity of the parties to the transaction, its content and qualitative and quantitative features, the personal interest of the controlling owner, the date of approval, and details of the entity that approved the transaction."

1.2 The aforementioned will not apply in the case of a "negligible" transaction as the term is defined in Regulation 64(3)(d)(1) of the Securities Regulations (Preparation of Financial Reports), 5753 - 1993; i.e., a transaction answering to "the types and characteristics of the transactions" that the corporation views as negligible. The Association of Banks contacted the Securities Authority in order to determine the reporting format applying to banks in this context. Further to this query by the aforementioned Association of Banks and the discussions between the Bank and the Securities Authorities on this issue, it was determined that the reporting format for the Bank's transactions with its controlling owner or with another person with whom the controlling owner has a personal interest, the division into banking and non-banking transactions, will be as follows:

A. For banking transactions – the Bank will determine criteria for exceptional banking transactions for which the Bank will publish an immediate report upon their occurrence. On the other hand, banking transactions that are not exceptional will be specified cumulatively in the framework of the annual reports (see the table below), even though according to the Securities Regulations

(Periodic and Immediate Reports) 5730 - 1970, the Bank is required to submit an immediate report as well as for transactions that are not exceptional.

B. Concerning non-banking transactions – the Bank will determine criteria for classifying such transactions that are "negligible", and they will be subject to the provisions concerning reporting of transactions with a controlling owner that apply to other reporting corporations (i.e. that are not banks).

Proper Banking Management instructions (312) from the Supervisor of Banks (hereinafter: "PBM 312") determines that as a rule the Bank shall not make a transaction with a "related person" (as this term is defined in the mentioned instructions) on better terms than those under which it makes similar transactions with others, excluding a "related person" that is a corporation fully owned by the Bank and that does not give any credit or other service to anyone outside the bank group.

1.3 Below are details of the criteria defined as mentioned at the meeting of the Board of Directors' Audit Committee of February 18, 2010 in the distribution for banking and non-banking transactions:

1.3.1 "Exceptional" banking transactions:

Banking transactions meeting the following criteria will be deemed exceptional:

A. On the matter of "liability" transactions – A liability transaction will be deemed exceptional if following its implementation the total liability of the controlling owner's group will be more than 5% of the Bank's capital; within the meaning of this term in Appendix A of the Proper Bank Management Instructions (311), as reported in the Financial Statements last published before the transaction date (hereinafter: "regulatory capital"), or if the growth in an individual borrower's liability from the controlling owner's group following the transaction is more than 2% of the regulatory capital at the time of the transaction.

If the Bank learns of liability transactions in which the controlling owner has a personal interest and to which PBM 312 does not apply because they were not made with a "linked person", within the meaning of PBM 312, the Bank shall bring them for approval as determined in the aforementioned PBM 312. Concerning these transactions, the Bank will cumulatively submit information as part of the annual reports in the format shown in the tables below (separate tables for these transactions and for transactions to which PBM 312 applies). In this context it should be clarified that the criteria for an exceptional liability transaction with a controlling owner, or in which a controlling owner has a personal interest, will apply whether or not Instruction 312 applies to it.

In addition, any specific provision for credit losses or write-off of a particular amount due to the liability of a controlling owner or a corporation linked to him shall be considered a significant transaction.

B. Concerning "deposit" transactions – the deposit of money in a certificate of deposit of any type shall be considered an exception transaction if as a result the total deposits of a controlling owner's group is greater than 2% of the total public deposits, as reported in the last financial reports published by the Bank before the transaction date. Receiving a deposit from a company that is a "linked person" to the controlling owner (as the term is defined in PBM 312), which is not one of the companies that are controlled by the controlling owner, shall be considered exceptional if as a result the total deposits of that "linked person" are greater than 2% of the total public deposits, as reported in the last financial reports published by the Bank before the transaction date.

On the issue of securities transaction or foreign currency transaction (that is not a liability transaction or deposit transaction as specified above) – transaction in securities or transaction in foreign currency will be considered as exceptional if the yearly commission collected is equal or exceeds 4% of the annual total of the Bank's operating income (with deduction on income from investment in shares) according to the the Bank's last annual financial reports.

C. Any other banking transaction, of the type that the Bank usually implements with the public, providing that it does not involve granting of credit by the Bank, where the amount of such transaction exceeds 0.1% of the regulatory capital at the transaction date.

A negligible temporary deviation from the extents specified in paragraphs (a) to (d) above, and for a period of no more than 30 days, shall not lead to a change of classification of the transaction as a "transaction that is not exceptional", and such exceptions shall be disclosed in the framework of the annual report. It should be clarified that any change to an exceptional transaction is in itself, an exceptional transaction for which an immediate report shall be submitted.

1.3.2 Non-banking transactions:

The following transactions shall be considered negligible transactions:

A. A transaction to purchase services from a controlling shareholder or where the controlling shareholder has a personal interest, provided that it is not an arrangement with a controlling shareholder or his relative concerning the terms of his service and employment, which is in the normal course of business, and on market conditions, and whose scope does not exceed NIS 250,000, providing that the total number of transactions of this type in one calendar year does not exceed 0.1% of the regulatory capital. The aforementioned total shall not include individual transactions whose value is less than NIS 25,000.

B. Transactions concerning the renting areas from a controlling shareholder or where the controlling shareholder has a personal interest, that were approved in one calendar year, in the normal course of business, and on market terms, and whose scope does not exceed 0.1% of the regulatory capital.

C. Bearing the costs of a controlling shareholder, in the normal course of business, and on market terms, for the purpose of participating in representative events and conferences of customers and subsidiaries of the bank at their invitation – expenses up to a total of NIS 250,000 per year.

D. Any other transaction in the normal course of business, and on market terms, and whose scope is no more than the sum of NIS 250,000, providing that the total of such transactions in one calendar year will not exceed 0.1% of the regulatory capital. The aforementioned total shall not include individual transactions whose value is less than NIS 25,000.

Definitions:

For the purpose of the above mentioned decision, on each of the paragraphs, the following terms will have meaning as specified below:

(1) "Liability" – as this term is defined in Proper Banking Management Instruction number 312 of the Supervisor of Banks.

(2) "Market conditions" – Conditions that are not better than the conditions on which similar transactions of the same type are made by the Bank with people or with corporations that are not controlling shareholders of the Bank or with people with whom the controlling shareholder has no personal interest in the transaction with them. Market terms with respect to banking transactions are examined in comparison to the terms under which transactions of the same type and of similar size are made, as accepted when examining transactions with related people according to Proper Bank Management Instruction 312, with customers of the Bank who are not related people or with entities where the controlling shareholder has a personal interest in the transaction with them; market terms in respect of transactions that are non-banking transactions will be examined in relation to transactions of that type that the Bank enters into with suppliers and/or in relation to offers of other suppliers who were examined before a decision was made about the transaction. In cases where the Bank has no transaction of this type, the market conditions will be examined in relation to transactions of that type made in the economy, on condition that the transaction is in the normal course of business and that the transaction of this type has a market in which similar transactions are made.

(3) “The controlling shareholder's group” – the controlling shareholder together with the private companies related to him within the meaning of the term “related person” in Proper Banking Management Instruction 312, and together with his relatives and private companies related to them, including family members living with him or supported by him. The definition of “relative” according to the provisions of the Banking Act (Licensing) includes brother, parent, issue, spouse's issue, and the spouse of each of these.

Below are details of the balances of the controlling shareholder's group and of others in which the controlling shareholder has a personal interest in their dealings with the Bank, as at December 31, 2012 (in NIS thousands):

	Balance as at December 31, 2012			The highest balance during 2012		
Type of balance	**Controlling group**	**Relatives of controlling shareholders**	**Ytzu Investments Company Ltd.**	**Controlling group**	**Relatives of controlling shareholders**	**Ytzu Investments Company Ltd.**
Credit	49.2	-	0.1	252.0	-	0.1
Unused credit line	107.2	-	-	145.8	-	-
Deposits	(7,685.2)	(637.2)	(196.5)	(13,469.9)	(641.9)	(196.5)

Below are details of income from commissions due to transactions in securities and/or transactions in foreign currency (that are not liability transactions or deposit transactions) paid by the controlling shareholder's group or by others where the controlling shareholder has a personal interest in their dealings with the Bank, for the year ending December 31, 2012 (in NIS thousands):

	Controlling group	Relatives of controlling shareholders	Ytzu Investments Company Ltd.
Revenues from commissions	156.2	1.8	4.1

1.3.3 Below are details of non- banking transactions with a controlling shareholder or where the controlling shareholder has a personal interest, for the year ending December 31, 2012 (in NIS thousands) and where there is no "negligible" transactions as defined above:

(1) Senior Officers Insurance Policy (D&O):

On September 13, 2012, the Bank's the Board of Directors approved (after approval of the Audit Committee as of September 11, 2012), in continuation and according to the decision of the General Assembly of the Bank's shareholders on September 7, 2010, the Bank's agreement with the its directors and senior officers (including subsidiaries), as may be from time to time, according to the matter in regards to the life insurance policies of senior officers (D&O), as specified below:

(a) The limits of liability and policy period will be: US$ 22 million per event and the period, and this for a period of 12 months starting on October 1, 2012 until September 30, 2013.

(b) The yearly premium the Bank will pay for the purchasing of a senior officer policy according to this decision (including the consideration for the insurer's front services) will not exceed the total amount paid in the previous year, that is US$82.1 thousand. The sum of the deductible in the senior officer insurance policy for the bank will not exceed the total amount of US$25 thousand.

The Board of Directors also approved concerning the agreement in the senior officers insurance policy as follows:

(a) The annual premium as aforementioned will be as per market conditions.

(b) The contract of the Bank in the senior officer insurance policy will also apply to senior officers who are related to the controlling shareholders serving at the Bank at the time of this decision, and that the contract terms with them will be identical to the contract terms of other senior officers at the Bank, as per market conditions, and this will not materially affect the profitability of the Bank, its assets and its liabilities.

(c) Transaction agreements of the Bank with the directors and its senior officers (including subsidiaries), from time to time, per issue, concerning senior officer insurance policy (D&O) and the Bank's agreement to purchase banking insurance policy as stipulated in the section above does not damage the Bank's best interest.

(2) Letters of Indemnity

On January 29, 2012 the general assembly of the Bank's shareholders approved providing liability letters for reimbursement of senior officers in the formula as attached to appendix C of the immediate report on invitation of the general assembly from December 22, 2011, as has been amended in the immediate report of January 19, 2012 (hereinafter: "the immediate report"), and this (a) for the senior officers of the Bank serving and/or have served at the bank from time to time and for the senior officers in another company, as defined in the immediate report serving and/or have served from time to time as per request of the Bank, as senior officer at another company, except for senior officers who as controlling shareholders may be considered party of personal interest in providing these liabilities letters for reimbursement. (b) For senior officers whose controlling shareholders may be considered a third party with personal interest in providing them liability letters for reimbursement, serving and/or will serve at the Bank from time to time, and also for senior officers as aforementioned that serve or will serve from time to time per request of the Bank, as senior officers at another company. For details concerning reimbursements, please see the immediate report of the Bank of January 19, 2012 [reference № 2012-01-020319].

Names of the members of the Board of Directors and their occupation*

Director's name	Main occupation
Ze'ev Gutman	Chairman of the Board of Directors of the Bank
Dr. Zalman Shoval	Chairman of the Board of Directors of Ytzu Investments Corporation Ltd. (parent company); Co-chairman of the Faire Foundation.
Shmuel Eshel	Consultant and financial guide
Moshe Bauer	CEO and director of C.F.C. Comprehensive Financing Corporation Ltd.
Oved Ben Ozer	Company Manager.
Adiv Baruch (began serving on 13.9.12)	Partner Manager and Director in Signum Ltd.
Prof. Shalom-Yosef Hochman	Financial lecturer, consultant and member of the Board of Directors.
Ram Harmelech (began serving on 13.9.12)	CEO and owner of Marneg Cranes Ltd. and director in companies
Pinchas Volovelsky	Lawyer, partner in a law firm.
Dr. Efrat Tolkovsky: (served until 3.12.12):	University lecturer, academic manager at the Chaim Katzman Gazit Globe Real Estate Academy
Ira Sobel (began serving on 18.2.13)	CPA, economic advisor to companies and director in public companies.
Jonathan Irony (served until 5.15.12)	Financial consultant; served as Chairman of the Board of Directors of the Bank until 10.27.2011.
Dr. Nurit Kraus (started to serve on 1.29.12)	CEO and founder of Redstar Modeling Services and Consultancy Ltd.
Gideon Shoval	CEO and Deputy Chairman of the Board of Directors of Ytzu Investments Corporation Ltd.

* Additional details on the members of the Bank's Board of Directors, including the dates they started serving, their membership on Board of Director Committees, the terms in other Boards of Directors, whether they are Bank employees, or of its subsidiaries, its consolidated companies or if an interested party and whether they are family of other interested parties, are presented in the periodical report of the Bank for 2012.

Report on directors with accounting and financial expertise

In accordance with the instructions of the Companies Law 5749 - 1999 (hereinafter: "Companies Law") and the Companies Regulations (Conditions and Examination of the Director with Accounting and Financial Expertise), 5765 - 2005, at least two directors will have accounting and financial expertise as the term is defined in the aforementioned Companies Law (hereinafter: "having accounting and financial expertise"). At least two of the external directors will have accounting and financial expertise. According to the Proper Banking Management Instruction 301 at least five of all the members of the Board of Directors will have accounting expertise. According to Instruction 630 of the Public Report instructions from the Supervisor of Banks, the required minimum number of directors with accounting and financial expertise will be specified in the report of the Board of Directors, as determined by the Board of Directors, and the reasons of the Board of Directors for its decision as specified in the aforementioned instruction. In addition, the minimum number of directors with accounting and financial expertise should be specified, as determined by the Bank what will be appropriate for the Board of Directors' Audit Committee as well as in each of the other committees of the Board of Directors, that are authorized to discuss the Financial Statement. In addition, the above mentioned instruction 630 determines that the Board of Directors' report will list the number of directors that "have no accounting and financial expertise" as of the report date.

In accordance with the decision of the Bank's Board of Directors (which is anchored in the Board of Directors work procedure), the minimum number of directors with accounting and financial expertise will be as determined in the Proper Banking Management Instruction 301 and Companies Law, that is: (a) at least five of all of the members of the Board of Directors will have accounting and financial expertise, provided that at least two of the directors will have accounting and financial expertise and at least two from the external directors will have accounting and financial expertise; (b) at least two members of the Audit Committee will have accounting and financial expertise.

This is for the reasons specified below: (a) By the Board of Directors' assessment, the above minimum number will enable the Board of Directors and the Audit Committee to comply with the obligations imposed on them according to the provisions of law and the corporate documents; in particular for their responsibility to examine the Bank's financial status and the evaluate the Financial Statements; (b) the above minimum number considers the size of the Bank, the complexity of its activity, and variety of involved risks.

At the time of reporting, all the members of the Board of Directors of the Bank have accounting and financial expertise according to their education, skills and experience, as detailed below:

Ze'ev Gutman:

Education: Accounting Studies, College of Management (non-degree), MBA, Herriot - Watt Adnivoro.

Skills and Experience:

- Current occupation – Chairman of the Board of Directors at the Bank; director, manager and controlling shareholder in Ze'ev Gutman Management and Consulting Ltd; member of associations as stipulated in the Bank's periodic report for 2012.

- Served in various management positions at the Bein-Leumi HaRishon Bank Ltd., member of management, Vice CEO, as follows: Chief Group Risk Officer CRO), head of Risk Management Division [from October 2010 until August 18, 2011)] Chief Financial Risk Officer, head of Division of Financial Management and Risk Management. [From March 2007 to October 2010]; Department head of Capital Market and Foreign Currency Market [from 2000 until March 2007]; served as director in the following Board of Directors: Magal Issuance Ltd.; Panka Ltd.) FIBI Bank Ltd)Switzerland; First International Underwriting Ltd.; Stokopin (Israel) Ltd.;HIGHTRADE; Tel-Aviv Stock Exchange Ltd.; Maof Clearing House; Chairman of the Board of Directors at Bank Otsar Hahayal; Maalot; Bein-Leumi Insurance Agencies (2005) Ltd.; U-Bank Ltd.

Dr. Zalman Shoval:

Education: B.A. in International Relations from University of California, Berkeley; M.A.. M.A. in international relations, economics and political science from the University of Geneva; and a Ph. D. in International Relations and Political Science from Pacific University.

Skills and Experience:

- Current occupation – Chairman of the Board of Directors of Ytzu Investments Corporation Ltd.; co-Chairman of the Faire Foundation; Chairman or director in the Board of Directors listed in the Bank's Periodic Report for 2012.

- In the past, served as CEO of Bank of Israel's exports, Israel's ambassador to the U.S., Chairman of the Bank of Jerusalem, member of the Knesset Finance Committee, member of the Knesset Foreign Affairs and Defense Committee.

Shmuel Eshel:

Education: B.A. in Political Science and Labor Studies, Tel-Aviv University.

Skills and Experience:

- Current occupation – Business advisor and consultant

- Served as Vice CEO at the Union Bank in the mortgages area (2009-2004); member of management at the Union Bank, Vice CEO, head of Business Department at the Union Bank (1998 - 2004); additional positions at the Union Bank starting from 1977. Until June 2009 served as director at Liblov Insurance Agency and at Carmel - Union for Mortgages and Investments Ltd. In addition, served as Chairman of the Union Leasing Corporation Ltd, and director in the Planus Loans Fund (1998 - 2004).

Moshe Bauer:

Education: High school education.

Skills and Experience:

- Current occupation – CEO and director of C.F.C. Comprehensive Financing Corporation Ltd. Comprehensive Financing Corporation Ltd. Deputy Chairman of the Board of Directors of Ytzu Investments Corporation Ltd., and director in the corporations listed in the Bank's periodic report for 2012.

- Former Manager of the Foreign Currency Department in Bank Elran, Secretary General of Bank Elran, and afterwards Secretary General of the Export Bank.

Ben-Ozer Oved:

Education: B.A. and M.A. in political science from Paddington School of Political Science.

Skills and Experience:

- Current occupation – Manager of Companies. Director in the corporations listed in the Bank's periodic report for 2012.

- Served as CEO of Unitrust Investment Company Ltd. and as Chairman of the Association of Members of the Stock Exchange in Tel Aviv. Served as a member of the Board of Directors of Maalot and its Rating Committee, and until 2010, as director of Jerusalem Portfolio Management Limited.

Adiv Baruch (has been serving since 13.9.2012)

Education: Bachelors Degree in Industrial Engineering and Management, Technion Haifa.

Skills and experience:

- Current occupation - partner manager and director in Signum Ltd., a company that specializes in investment management and recovery of companies in: information systems, communications, software, internet and civilian protection technology systems; director in corporations listed in the Bank's periodic report for 2012.

  Formerly served as Venture partner in Infinity-I-China; served as president and CEO of BOS; served as senior VP of Business Development and president of Ness Ventures in Ness Technologies Ltd.

Prof. Shalom-Yosef Hochman

Education: B.A. in Economics from The Hebrew University, Jerusalem; M.B.A. in Finance from The Hebrew University of Jerusalem Ph.D. in Finance from the University of Toronto.

Skills and experience:

- Current occupation – lecturer on financing; Associate Professor (external lecturer) at Interdisciplinary Center Herzliya; advisor and member of the Board of Directors listed in the Bank's periodic report for 2012.

- Served as CEO of the Mercantile Discount Bank (until 2006); served as associate professor at Houston University, USA and as an external lecturer at Tel-Aviv University (between 2000-2011);

Ram Harmelech (has been serving since 13.9.2012)

Education: B.A. in Statistics and Geography from Tel-Aviv University; M.B.A.. in Business Administration from Tel-Aviv University.

Skills and experience:

- Current occupation – CEO of Marneg Cranes Ltd. and director in the companies listed in the Bank's periodic report for 2012.

- Served as deputy to the CEO, director of the Business Division and Director of Credit Risk in Mercantile Discount Bank (between 1998-5/2012); served as CEO of Maalot The Israel Securities Ratings Company between 1994-1998.

Dr. Pinchas Volovelsky:

Education: B.A. in Economics and International Relations from The Hebrew University of Jerusalem, M.Jur. from The Hebrew University of Jerusalem.

Skills and experience:

- Current occupation – lawyer, partner in a law firm. Member of the Board of Directors as listed in the Bank's periodic report for 2012.

- Formerly Chairman of the Board of Directors of the Bank.

Dr. Efrat Tolkovsky: (served until 3.12.12):

Education: (B.A.) in Electronic Engineering from Tel-Aviv; M.A.. in Finance and Accounting from Tel-Aviv, Ph.D. in Finance and Accounting from Tel - Aviv University.

Skills and experience:

- Current occupation – University lecturer, academic manager of the Chaim Katzman Gazit Globe Institute for Real Estate. Member of the Board of Directors as listed in the Bank's periodic report for 2012.
- Between 2002-2004, served as member of the Faculty of Industrial Engineering and Management at the Technion, Haifa.

Accountant Ira Sobel (has been serving since 18.2.2013)

Education: B.A. in Business Administration / Accounting , College of Management, Rishon Le-Zion Zion; M.B.A. in Business Administration for Executives, Tel-Aviv University and Northwestern University, Chicago, USA.

Skills and experience:

- Current occupation: CPA, economic advisor to companies and director in public companies. Member of the Board of Directors as listed in the Bank's periodic report for 2012.
- Between 1994-2002, senior audit manager in banking at KPMGSomekh-Chaikin; assistant to the firm's CEO.

Jonathan Irony (served until 15.5.2012):**Education** B.A.. in Economics from the Hebrew University, Jerusalem.

Skills and experience:

- Current occupation – Financial consultant Director in corporations as listed in the Bank's periodic report for 2012;
- Served as Chairman of the Board of Directors of the Bank until the end of October 2011; CEO and Director of Investec Bank of Israel Ltd. (currently UBank Ltd.) between the years 1998 to 2005.

Dr. Nurit Kraus: (has been serving since 29.1.12):

Education: B.Sc., Aerospace Engineering, Technion, Haifa; degree M.Sc., Physics, Technion, Haifa; degree D.Sc., Physics, Technion, Haifa.

Skills and experience:

- Current occupation – Director and Founder of Redstart Services for Modeling And Consulting Ltd. dealing in consulting and development of models.

- Former Head of Model Validation and Head of Risk, including at Bank Leumi (between 2006-2011); Director of Trading Algorithms – Schonfeld Securities, USA (between 2000 - 2006).

Gideon Shoval:

Education: L.L.B. Law, University of Buckingham; L.L.M. in Law, Columbia University; M.B.A. in Business Administration, Harvard Business School IMD.

Skills and experience:

Current occupation – Managing Director and Acting Chairman of the Board of Directors of Ytzu Investments Company Ltd.

The Board of Directors

During 2012, and until the report's publication date, the following changes were made to the composition of the Board of Directors:

In a special general assembly that convened on January 29, 2012, Mrs. Nurit Kraus was appointed external director according to instruction 301 of the Proper Banking Management instructions and as an independent director in accordance with the Companies Law for a period of three years.

On May 15, 2012, Mr. Jonathan Irony ceased serving as director in the Bank once his notice of resignation became valid (retirement was not under circumstances that should be brought to the attention of shareholders).

On September 13, 2012, Mr. Ram Harmelech began serving as director in the Bank in accordance with the Board of Directors decision from June 28, 2012 to appoint him and following Bank of Israel approval of his appointment.

In the special general assembly that convened on September 13, 2012, the decision was made to appoint Mr. Adiv Baruch as external director in the Bank in accordance with the Companies Law 5759-1999; (On February 18, 2013, the special general assembly ratified Mr. Baruch's term as external director in accordance with the ratification procedure set forth in Section 5 of the Companies Regulations (Matters that do not constitute Linkage) 5756-2006.

In the annual general assembly that convened on December 3, 2012 the decision was made to chose and appoint the directors (that are not external directors) serving at the Bank for an additional period – Ze'ev Gutman (Chairman); Zalman Shoval; Gideon Shoval; Pinchas Volovelsky; Moshe Bauer; Ben-Ozer Oved and Ram Harmelech. It was further decided in the aforementioned general assembly to appoint to an additional three-year term Shmuel Eshel as external director in accordance with the Companies Law.

On December 3, 2012, Dr. Efrat Tolkovsky ended her term (second) as external director in the Bank in accordance with the Companies Law.

In a special general assembly that convened on January 18, 2013, Mrs. Nurit Kraus was appointed external director according to instruction 301 of the Proper Banking Management instructions and as an independent director in accordance with the Companies Law for a period of three years.

As of the publication of the report, the Bank's Board of Directors appointed 12 directors, 5 of them external directors), 3 external directors according to the Companies Law, and one external director according to instruction 301 of the Proper Banking Management instruction amendment).

It should be mentioned that on October 14, 2010, the Supervisor of Banks contacted the Bank's Board of Directors, as part of examining the functioning of the Bank's Board of Directors and its structure, to establish regulations concerning the composition of the Board of Directors and the relation between external directors and other directors.

As an extension, the composition of the Bank's Board of Directors in the ratio between external directors and other directors complies with the agreement with the Supervisor of Banks (5 external directors of the 12-13 directors).

During 2012, and until the report's publication date, the following changes were made to the composition of the Board of Directors' committees:

On February 6, 2012, Ms. Kraus was appointed member in the Capital Planning and Strategy Committee and Ms. Efrat Tolkovsky as director in the Compensation Committee.

On May 15, 2012, Ms. Kraus was appointed member of the Risk Management Committee;

On September 13, 2012, Mr. Baruch was appointed member of the Audit Committee;

On September 25, 2012, Mr. Harmelech was appointed member of the Audit Committee, the Risk Management Committee and the Capital Planning and Strategy Committee; on said date, Mr. Eshel concluded his term as member of the Risk Management Committee and Mr. Ben Ozer concluded his term as member of the Audit Committee;

On November 27, 2012, the composition of the Compensation Committee was updated in accordance with the provisions of Amendment 20 of the Companies Law whose members are in accordance with the list below:

On February 18, 2013, Ms. Sobel began serving as member of the Audit Committee with her appointment as external director in the Bank.

As of the report's publication date, the committees and the Board of Directors operate as follows:

Audit Committee: Shmuel Eshel (Chairman) (external director), Adiv Rhubarb (external director), Shalom Hochman (external director), Ram Harmelech and Ira Sobel (external director in accordance with instruction 301).

Risks Management Committee: Ze'ev Gutman (Chairman), Shalom Hochman (external director), Nurit Kraus (external director in accordance with instruction 301), and Ram Harmelech.

Capital Planning and Strategy Committee: Gideon Shoval (Chairman), Ze'ev Gutman, Shalom Hochman (external director), Jonathan Irony, Nurit Kraus (external director according to instruction 301), and Ram Harmelech.

Compensation Committee: Adiv Baruch (Chairman) (external director), Shmuel Eshel (external director), Shalom Hochman (external director), and Oved Ben Ozer.

Credit Committee of the Board of Directors: Moshe Bauer (Chairman), Oved Ben Ozer, Pinchas Volovelsky, Shalom Hochman (external director), and Shmuel Eshel (external director).

In 2012, there were 20 meetings of the plenum of the Board of Directors and 40 meetings of its committees.

Members of the Bank's Board of Directors as at the 31st of December 2012 (1) (2)

Uriel Paz	CEO
Michael Tier	Vice CEO, Resource Division Manager
Nissan Levi	Vice CEO, Manager of the Financial Division
Michael Ben-Ischai	Vice CEO, Manager of Human Risks Division (C.R.O.)
Sarit Weisstof	Vice CEO, legal consultant
Arik Zwilli	Vice CEO, Manager Retail Credit Department
Arnon Zayit	Vice CEO, Manager Of Financial Department
Dinah Promovitz	Vice CEO, Manager Screening Department
Ron Sagy(3)	Internal auditor, Deputy CEO, member of Management

Senior officers who are not members of Management

Carmel Florentz	Secretary of the bank
Dani Nachum(4)	Manager of the Information Systems Division
Ayelet Rusk(5)	Manager of the Real Estate Sector Department

Salaries of senior officers	See below in appendix A.
Salary of auditing accountant	See below in appendix A.

The Bank's Board of Directors thanks the management of the Bank and it employees for their dedicated work and contribution for the Bank's business advancement.

Zeev Gutman	**Uriel Paz**
Chairman of the Board of Directors	**Chief Executive Officer**

February 28, 2013

(1) Additional information on senior officers at the Bank are presented in the Bank's periodical report for 2012, and on the Magna website from the Securities Authority at the address http//www.magna.isa.gov.il

(2) Mr. Asher Ben David served as Vice CEO, Retail Division Manager until December 12, 2012.

(3) Mr. Motti Gedali concluded his position as the Bank's internal auditor on March 20, 2012, and Mr. Ron Sagy began serving in this position on said date.

(4) Mr. Danny Nahum ceased serving in this position on February 15, 2013; Mr. Michael Tier is currently serving in the position of Information Technology Manager (ITM) instead of Mr. Nahum as well.

(5) Ms. Ayelet Rusk has been serving in this position since May 30, 2012.

Principal data on the Bank and on its consolidated companies for the year ending on December 31, 2012

Appendix A. to the Report of the Board of Directors

	Rate Changes in %	For the year ending on the day December 31 2012	2011
A. Profit and Profitability (1)			
		In percentages	
1. Net profit yield for average capital		**5.4%**	7.3% *
		Reported amounts in millions of Shekels	
2. Income from Interest, net	32%	**230.9**	174.8
3. Expenses for Credit Losses	138%	**(36.0)**	(15.1)
4. Income from Interest Net after Expenses for Credit Losses	22%	**194.9**	159.7
5. Non-Interest Income	-8%	**113.4**	123.5 *
6. Operating and Other Expenses	14%	**(254.5)**	(223.1)
7. Profit before tax	-10%	**53.8**	60.1 *
8. Provision for tax	21%	**(17.7)**	(14.6)*
9. Net profit	-21%	**36.1**	45.5 *

	Change rate	As of December 31 2012	2011
B. Main financial relations			
		In percentages	
10. Expenses for Credit Losses for the period of total credit for the public – Net (Including weighted off-balance-sheet credit risk)		**0.37%**	0.17%
11. Core capital ratio to risk components (Basel II).		**9.7%**	9.1%
12. Capital ratio for risk components (Basel II)		**14.4%**	13.7%
		Reported amounts in millions of Shekels	
C. Balance sheet - main paragraphs			
13. Total balance sheet	7%	**12,292**	11,483
14. Cash and deposits at the Bank	72%	**1,361**	792
15. Securities	-22%	**1,163**	1,491
16. Credit for the public	6%	**9,581**	9,058
17. Public deposits	8%	**9,814**	9,065
18. Debentures and deferred liability notes	-2%	**1,581**	1,612
19. Equity	8%	**694**	645
20. Capital for the purpose of capital ratio for risk components (Basel II)	7%	**1,031**	963
D. Off-balance-sheet paragraphs			
21. Loan balance from deposits according to collection level	-13%	**1,997**	2,308
22. Collateral balance	-43%	**195**	339

* Comparison numbers include profit from the sale of the administrative building for a sum of NIS 20.8 million after tax. For more information, see Note 8 of the Financial Statements.

(1) The comparison numbers in this Statement were reclassified following the instruction issued by the Supervisor of Banks concerning adoption of the new format for the Profit and Loss Statement. For more information, see Note 2 of the Financial Statements.

Principal data on the Bank and on its consolidated companies for the year ending on December 31, 2012

Appendix A (continuation) to the report of the Board of Directors

E. Specifications of benefits for senior officers (thousands of NIS)

For the year ending December 31, 2012										
Details of the benefits receiver				Benefits for services				Other benefits		Total
Name	Function	Position scope	Holding rate in capital of corporation	Salary(1)	Management fee(2)	Bonus(3)	Benefit for share-based payment(4)	Interest(5)	Other(6)	
Ze'ev Gutman(7)	Chairman of the Board of Directors	Partly	-	-	1,397	-	-	-	-	1,397
Uriel Paz(8)	CEO	Full	-	-	2,059	-	711	3	-	2,773
Asher Ben David(9)	Vice CEO, Manager of the Retail Division	Full	-	-	1,176	30	(10)	4	-	1,200
Nissan Levi(10)	Replacement and Vice CEO, Manager of the Financial Division	Full	-	1,112	-	-	24	3	-	1,139
Michael Tier (11)	Vice CEO, Manager of the Resources Division	Full	-	1,083	-	-	24	-	-	1,107
Michael Ben Ischai(12)	Vice CEO, Manager of Risks Division	Full	-	1,043	-	-	-	4	-	1,047

For the year ending December 31, 2011										
	Details of the benefits receiver			Benefits for services				Other benefits		Total
Name	Function	Position scope	Holding rate in capital of corporation	Salary(1)	Management fee(2)	Bonus(3)	Benefit for share-based payment(4)	Interest(5)	Other(6)	
Ze'ev Gutman(7)	Chairman of the Board of Directors	Partly	-	-	283	-	-	-	-	283
Jonathan Irony(13)	Chairman of the Board of Directors	Partly	-	-	622	310	-	-	-	932
Ze'ev Bezura(11)	Former CEO	-	-	-	-	1,015	-	-	110	1,125
Uriel Paz(8)	CEO	Full	-	-	2,049	-	781	2	-	2,832
Bentzi Adiri(15)	Vice CEO, Manager of Business Department	Full	-	282	766	171	-	-	-	1,219
Asher Ben David(9)	Vice CEO, Manager of the Retail Division	Full	-	-	1,194	-	9	2	-	1,205
Nissan Levi(10)	Replacement and Vice CEO, Manager of the Financial Division	Full	-	1,053	-	-	2	4	-	1,059
Arnon Zayit(16)	Vice CEO, Manager of Finance Department	Full	-	1,047	-	-	2	4	-	1,053

Appendix A (continuation) to the report of the Board of Directors

E. Details of the benefits of the senior officers (in thousands of Shekels) – (continuation)

(1) Including provisions for compensation, royalties, education funds, national insurance, and holidays as well as attendant conditions to the salary, but not including payroll tax. Included in the profit report in paragraph Salaries and Accompanying Expenses.

(2) Includes monthly management fees and accompanying benefits but does not include VAT. Included in the profit report in paragraph Salaries and Accompanying Expenses.

(3) Includes bonus for which was set aside in the report year but not yet paid (without payroll tax). Included in the Statement of Profit and Loss in the section Salaries and Accompanying Expenses

(4) For details: see note 22a of the Financial Statements. Included in the profit report in paragraph Salaries and Accompanying Expenses

(5) Including interest benefit for loans provided with benefit conditions. Included in the profit report in paragraph Profit from financing activity before expenses for credit losses

(6) Including car value benefit. Included in the profit report in paragraph Other Expenses.

(7) Mr. Ze'ev Gutman - Chairman of the Board of Directors of the Bank – Provides managerial services to the bank and is employed for an average of 4 days per week as of October 18, 2011, according to the agreement from November 6, 2011 through the company controlled by him, "Ze'ev Gutman Management and Consultancy Ltd.", for an unlimited period. For additional information see Note 22.

The monthly management fees of Mr. Ze'ev Gutman are linked to the Consumer Price Index.

Each of the parties may terminate the agreement while giving advance announcement of three months in advance and subject to the terms set forth in the agreement. For more information, see Note 22.

(8) Mr. Uriel Paz - The Bank CEO, has been providing management services to the Bank since April 8, 2010 in accordance with the agreement to provide management services through the company controlled by him "Uriel Pal Consultancy Ltd." for a period of 4 years. The monthly management fees of Mr. Ze'ev Gutman are linked to the Consumer Price Index. For additional information see note 22 and also note 22a of the Financial Statements.

Mr. Uriel Paz has a credit balance with benefit terms as at December 31, 2012 totaling NIS 29 thousand.

(9) Mr. Asher Ben David - served as manager of the Retail Division, beginning on May 1, 2010 and until December 12, 2012, in accordance with an agreement to provide management services through the company controlled by him "Yak Asset Management Ltd.". In accordance with the addendum to this Agreement, Mr. Asher Ben David will provide consulting services to the Bank beginning on December 12, 2012 and until March 20, 2013, on which date the management agreement will end. The monthly management fees of Mr. Asher Ben David are linked to the Consumer Price Index. In addition, in accordance with the management agreement, the Bank must pay full management fees during the 3 month adjustment period from the end of the management agreement. Mr. Nissan Levi was allocated under an options program for senior managers 564,142 option units of type A, as well as 282,070 option units of type B. These options were assessed on the balance sheet date at zero value due to their expected expiration of these options upon conclusion of the service provision agreement as stipulated above. For details concerning the options program for senior managers, see Note 22a. For details concerning the compensation program, see the "Human Capital" chapter in the Financial Statement.

Mr. Asher Ben David has a credit balance with benefit terms as at December 31, 2012 totaling NIS 57 thousand.

Appendix A (continuation) to the report of the Board of Directors

E. Details of the benefits of the senior officers (in thousands of Shekels) – (continuation)

(10) Mr. Nissan Levi – Manager of the Financial Division, employed at the Bank as of June 1, 1999, in accordance with a personal agreement, for an unlimited period. The monthly salary of Mr. Nissan Levi is linked to the Consumer Price Index. Each of the parties may terminate the agreement while giving advance announcement of three months in advance. Moreover, when his employment will be terminated, Mr. Nissan Levi will be entitled to all the accumulated amounts the Bank will release on his behalf that are accumulated in his favor over various periods. Mr. Nissan Levi was allocated a framework of options plan for senior managers 155,139 option units of the type of A, as well as 77,569 option units of the type B. For information concerning the options plan for senior managers see Note 22a. For details concerning compensation program see chapter the "Human Capital" in the report of the Financial Statement.
Mr. Nissan Levi has a credit balance with benefit conditions as at December 31, 2012, totaling NIS 45 thousand.

(11) Mr. Michael Tier – Manager of Resources Division, has been employed at the Bank since June 18, 2011, in accordance with a personal agreement, for an unlimited period. The monthly salary of Mr. Michael Tier is linked to the CPI. Each of the parties may terminate the agreement while giving advance announcement of three months in advance. Furthermore, when his employment will be terminated, Mr. Michael Tier will be entitled to all the accumulated amounts the Bank will release on his behalf that are accumulated in his favor over various periods. Mr. Michael Tier was allocated a framework of options plan for senior managers 155,139 option units of the type of A, as well as 77,569 option units of the type B. For information concerning the options plan for senior managers see Note 22a. For details concerning compensation program see chapter the "Human Capital" in the report of the Financial Statement.
Mr. Michael Tier has a credit balance with benefit conditions as at December 31, 2012, totaling NIS one thousand.

(12) Mr. Michael Ben Ischai – Manager of Risks Division, has been employed at the Bank since January 1, 1998, in accordance with a personal agreement, for an unlimited period. The monthly salary of Mr. Michael Ben Ischai is linked to the Consumer Price Index. Each of the parties may terminate the agreement while giving advance announcement of three months in advance. Furthermore, when his employment will be terminated, Mr. Michael Ben Ischai will be entitled to all the accumulated amounts the Bank will release on his behalf that are accumulated in his favor over various periods.
Mr. Michael Ben Ischai has a credit balance with benefit terms as at December 31, 2012 totaling NIS 77 thousand.

(13) Mr. Jonathan Irony served as Chairman of the Board of Directors of the Bank from March 30, 2006, and until October 27, 2011 (but continued to serve as director until May 15, 2012). According to the employment agreement, of March 30, 2006, Mr. Irony will grant services to the Bank as Chairman of the Board of Directors at a scope of about 1.5 to 2 days per week. The services will be provided to the Bank in a standard agreement between the ordering party and the independent contractor and this through the company controlled by Mr. Irony ("Jonathan Irony Holdings Ltd."). The compensation for these services are determined for a monthly total of NIS 41,666 with addition of VAT, linked to the CPI. Furthermore, the managing company is entitled to a monthly payment for return of fixed expenses (telephone, car, petrol, etc.) for a total of NIS 4,065 with addition of VAT and reimbursement of current expenses involved in the granting of the services (such as: travel expenses abroad, entertainment, and so forth), according to the Bank's policy, and against receipts. The Chairman will be entitled to an annual bonus according to and subject to the recommendations of the Bank's Board of Directors and approval of the General Assembly, without this being a liability to pay annual bonus. The agreement period is for one year, and at the end of each year is will be automatically renewed for an additional year. Each party may terminate the agreement at any time, with a written announcement 3 months in advance. On January 29, 2012, the General Assembly of the Bank's shareholders approved the payment of a retirement bonus to Mr. Irony totaling NIS 360 thousand including VAT.

Appendix A (continuation) to the report of the Board of Directors

E. Details of the benefits of the senior officers (in thousands of Shekels) – (continuation)

(14) Mr.Avi Bazuri served as CEO as of December 5, 2007, and ended his tenure on April 13, 2010. With the termination of his employment, Mr. Avi Bazuri was paid amounts due to advance announcement of 6 months and adjustment period of 3 months, according to the employment agreement (period of in advance announcement and adjustments period ended on December 31, 2010). In accordance with the agreement signed with him on May 15, 2012, Mr.Avi Bazura was paid in 2012 an additional adjustment bonus beyond that set forth in his employment agreement of NIS 1.0 million. This bonus was provided for in the 2011 Financial Statements.

(15) Mr. Benzi Adiri – Served as manager of business division, between April 2, 2007 and until December 22, 2011, (as of April 1, 2011, Mr. Benzi Adiri has provided management services in accordance with a management service provision agreement through the company controlled by him "Benzi Adiri Management Services Ltd."). Mr. Benzi Adiri's monthly salary is linked to the CPI. In November 2011, the payment of the retirement bonus for the amount of NIS 171 thousand for Mr. Bentzi Adiri was approved.

(16) Mr.Arnon Zayit – Manager of Finance Division, was employed at the Bank as of April 2, 2000, in accordance with a personal agreement for an unlimited period. The monthly salary of Mr. Arnon Zayit is linked to the CPI. Each of the parties may terminate the agreement while giving advance announcement of three months in advance, moreover, Mr. Arnon Zayit will be entitled to, when his employment will be terminated, all the accumulated amounts the Bank will release on his behalf that are accumulated in his favor in various periods. Mr. Arnon Zayit was allocated in the framework of options plan for senior managers 103,426 option units of the type of A, as well as 51,713 option units of the type B. For information concerning the options plan for senior managers see Note 22a. For details concerning compensation program see chapter the "Human Capital" in the report of the Financial Statement. Mr. Arnon Zayit has a credit balance with benefit conditions as at December 31, 2012, totaling NIS 156 thousand.

Principal data on the Bank and on its consolidated companies for the year ending on December 31, 2012

Appendix A (continuation) to the report of the Board of Directors

E. Details of the benefits of the senior officers (in thousands of Shekels) – (continuation)

	For the year ending on the day December 31	
	2012	**2011**
F. Data of organization structure		
1. Number of Bank branches(1)	**17**	16
2. Number of employees including subsidiaries (including employees from employment agencies and outsourcing)	**509**	463
3. Number of positions with overtime (monthly average)	**19**	16
4. Number of meetings of the Board of Directors assembly	**20**	15
5. Number of meeting of the Board of Directors' committees	**40**	61

G. Salary of Auditing Accountant (2,3,4) in thousands of New Shekels

	Consolidated		The Bank	
	For the year ending on December 31			
	2012	**2011**	**2012**	**2011**
For auditing activity: (5)				
Auditing accountant	**1,185**	1,168	**989**	954
For tax services (6)				
Auditing accountant	**95**	240	**95**	240
For other services				
Auditing accountant	**106**	325	**106**	325
Total salary of Auditing Accountant	**1,386**	1,733	**1,190**	1,519

(1) After the balance sheet date, another branch was opened. As of the date of publication of the balance sheet, the number of Bank branches totaled 18.

(2) Report of the Board of Directors for the annual general assembly on salary of the Auditing Accountant for auditing activities for additional services during the audit, according to paragraphs 165 and 167 of the Companies Law, 5759 - 1999.

(3) The salary of the Auditing Accountant includes payments to to partnerships and corporations under their control, and includes payments based on VAT Law.

(4) Including paid salary and accumulated salary.

(5) Auditing annual Financial Statements and review of the interim reports.

(6) Current tax services and preparation of the reports for the tax authorities.

Management Review

Financial Statement for 2012

Bank of Jerusalem Ltd. and its consolidated companies

Below are multi-period information and various details of Financial Statements that could provide a broad picture on the Bank's financial situation and its activity results, and are present in the addition below:

Consolidated balance sheets for the years 2008-2012

Reported amounts

Appendix A

	December 31				
	2012	**2011**	**2010**	**2009**	**2008**
	Millions of NIS				
Assets					
Cash and deposits at the Bank	**1,360.6**	792.3	652.3	765.1	350.7
Securities	**1,163.0**	1,490.7	1,314.9	1,083.2	1,291.7
Credit for the public *	**9,672.1**	9,148.8	8,158.4	7,481.1	7,652.3
Provision for credit losses *	**(90.7)**	(91.0)	(121.5)	(131.8)	(142.2)
Net credit for the public	**9,581.4**	9,057.8	8,036.9	7,349.3	7,510.1
Buildings and equipment	**117.9**	79.7	56.7	52.4	51.8
Assets for derivative instruments	**20.9**	7.2	23.9 **	23.6 **	9.9 **
Other assets	**47.7**	54.9	41.0 **	27.8 **	37.1 **
Total assets	**12,291.5**	11,482.6	10,125.7	9,301.4	9,251.3
Liabilities and capital					
Public deposits	**9,813.7**	9,064.6	7,407.8	7,115.7	7,279.3
Deposits from banks	**63.3**	76.2	86.5	103.9	139.5
Government deposits	**-**	0.8	4.9	5.4	3.7
Securities that have been loaned or sold as part of the return purchasing agreement	**-**	-	-	-	50.0
Liability certificates and deferred liability notes	**1,581.0**	1,611.9	1,921.1	1,391.8	1,188.3
Liabilities for derivative instruments	**16.4**	15.0	10.7 **	11.0 **	17.2 **
Other liabilities	**123.0**	69.5	61.5 **	67.7 **	53.4 **
Total liabilities	**11,597.4**	10,838.0	9,492.5	8,695.5	8,731.4
Equity	**694.1**	644.6	633.2	605.9	519.9
Total liabilities and capital	**12,291.5**	11,482.6	10,125.7	9,301.4	9,251.3

* On 1.1.2011, the Bank adopted for the first time the instructions from the Supervisor of Banks concerning "measurement and disclosure of defective debts, credit risk and provision for credit losses". The comparison numbers from the previous periods were not presented again. Therefore, the data for the period ending on December 31, 2012 and December 31, 2011 are not comparable to the data of the previous years. For additional explanations concerning the effect of the instruction's first adoption, see Note 2 of the Financial Statements.

** Reclassified

Consolidated Profit and Loss Statements– multi-period information for the years 2008 - 2012

Reported amounts

Appendix B

	For the year ending on December 31				
	2012	**2011***	**2010***	**2009***	**2008***
	Millions of NIS				
Income from Interest	555.7	559.0	426.7	486.2	632.7
Interest expenses	324.8	384.2	302.1	370.1	500.5
Income from Interest, net	230.9	174.8	124.6	116.1	132.2
Expenses for Credit Losses**	36.0	15.1 ***	(2.6)	(1.3)	6.8
Income from Interest Net after Expenses for Credit Losses	**194.9**	**159.7**	**127.2**	**117.4**	**125.4**
Non-Interest Income					
Non-Interest Financing Income	22.6	6.1	24.5	50.5	23.1
Fees	90.2	91.9	98.9	97.9	98.5
Other revenues	0.6	25.5	0.6	0.1	0.8
Total Non-Interest Income	**113.4**	**123.5**	**124.0**	**148.5**	**122.4**
Operating and Other Expenses					
Salaries and accompanying expenses	137.8	134.1	120.7	105.8	102.6
Maintenance and depreciation of buildings and equipment	46.9	37.6	29.4	27.9	24.4
Other expenses	69.8	51.4 ***	53.0	39.9	39.2
Total Operating and Other Expenses	**254.5**	**223.1**	**203.1**	**173.6**	**166.2**
Profit before tax	53.8	60.1	48.1	92.3	81.6
Provision for tax	17.7	14.6	14.0	33.6	29.9
Net profit	**36.1**	**45.5**	**34.1**	**58.7**	**51.7**
Earnings per Share (in NIS)					
Basic and Diluted Earnings Per Share (NIS)	**0.51**	**0.65**	**0.48**	**0.83**	**0.73**

* The comparison numbers in this Statement were reclassified following the instruction issued by the Supervisor of Banks regarding adoption of the new format for the Profit and Loss Statement. For more information, see Note 2 of the Financial Statements. It should be noted that in 2011, the Other Revenues item included profit from the sale of the Bank's administrative building for NIS 25.4 million, and, in the tax expense item a sum of NIS 4.6 million. For more information, see Note 8 of the Financial Statements.

** On 1.1.2011, the Bank adopted for the first time, the instructions of the Supervisor of Banks concerning "measurement and disclosure of defective debts, credit risk and provision for credit losses". The comparison numbers from the previous periods were not presented again. Therefore, the data for the period ending on December 31, 2012 and December 31, 2011 are not comparable to the data of the previous years. For additional explanations concerning the effect of the instruction's first adoption, see Note 2 of the Financial Statements.

*** Reclassified.

Rates of income and expenses – of the Bank and its consolidated companies[1]

Reported amounts

Appendix C

	2012			
			Revenue (expense) rate[5]	
	Balance Average for the period[2]	Revenue (expenses) Financing	without effect derivatives	Total Effect of derivatives
	Millions of NIS		In percentages	
Non-linked Israeli currency				
Assets (7)	6,502.7	312.4	4.80	
Effect of ALM (8)	76.0	(1.0)		
Total assets	6,578.7	311.4		4.73
Liabilities	5,935.2	(159.0)	(2.68)	
Effect of ALM (8)	77.3	(6.4)		
Total liabilities	6,012.5	(165.4)		(2.75)
Interest gap			**2.12**	**1.98**
Israeli currency index linked				
Assets (7)	3,466.7	184.0	5.31	
Effect of ALM (8)	77.3	(0.1)		
Total assets	3,544.0	183.9		5.19
Liabilities (7)	3,481.0	(154.5)	(4.44)	
Total liabilities	3,481.0	(154.5)		(4.44)
Interest gap			**0.87**	**0.75**
Foreign currency – local activity (3)				
Assets (7)	1,551.0	42.1	2.71	
Effect of ALM (8)	405.0	1.1		
Effect of hedging derivatives	14.0	0.3		
Total assets	1,970.0	43.5		2.21
Liabilities (7)	1,423.1	(11.3)	(0.79)	
Effect of ALM (8)	481.0	16.8		
Effect of hedging derivatives	14.0	(0.6)		
Total liabilities	1,918.1	4.9		0.26
Interest gap			**1.92**	**2.47**
Total				
Financial assets that generated financing revenue (7)	11,520.4	538.5	4.67	
Effect of ALM (8)	558.3	-		
Effect of hedging derivatives	14.0	0.3		
Total assets	12,092.7	538.8		4.46
Financial liabilities that caused financing expenses (7)	10,839.3	(324.8)	(3.00)	
Effect of ALM (8)	558.3	10.4		
Effect of hedging derivatives	14.0	(0.6)		
Total liabilities	11,411.6	(315.0)		(2.76)
Interest gap			**1.67**	**1.70**

Notes: at the end of Appendix C.

Rates of income and expenses – of the Bank and its consolidated companies[1] (continuation)

Appendix C (continuation)

	2012	
	Balance Average for the period [2]	Revenue (expenses) financing
	Millions of NIS	
For other derivative instruments		1.0
Commission from financing business and revenue from other financing [4]		42.7
Profit from financing activity before expenses for credit losses		257.4
Expenses for Credit Losses		(36.0)
Revenue from other financing activity after expenses due to credit losses		**221.4**
Financial assets generating financing revenue	11,520.4	
Assets deriving from derivative instruments [6]	8.9	
Other financial assets [7]	45.0	
Provision for Credit Losses	(85.9)	
Total financial assets	**11,488.4**	
Financial liabilities that caused financing expenses	10,839.3	
Liabilities deriving from derivative instruments [6]	12.7	
Other financial liabilities [7]	35.4	
Total financial liabilities	**0,887.4**	
Total surplus financial assets on financial liabilities	601.0	
Non-financial assets	105.1	
Non-financial liabilities	(34.0)	
Total capitalized means	**672.1**	

Notes: at the end of Appendix C.

Rates of income and expenses – of the Bank and its consolidated companies[1] (continuation)

Reported amounts

Appendix C (continuation)

	2011			
			Revenue (expense) rate[5]	
	Balance Average for the period[2]	Revenue (expenses) Financing	without effect derivatives	Total Effect of derivatives
	Millions of NIS		In percentages	
Non-linked Israeli currency				
Assets [7]	6,124.9	300.5	4.91	4.91
Liabilities [7]	5,413.6	(164.5)	(3.04)	
Effect of ALM [8]	145.6	(10.4)		
Total liabilities	5,559.2	(174.9)		(3.15)
Interest gap			**1.87**	**1.76**
Israeli currency index linked				
Assets [7]	3,282.6	205.1	6.25	
Effect of ALM [8]	256.8	8.1		
Total assets	3,539.4	213.2		6.02
Liabilities [7]	3,590.5	(210.8)	(5.87)	(5.87)
Total liabilities	3,590.5	(210.8)		
Interest gap			**0.38**	**0.15**
Foreign currency – local activity [3]				
Assets [7]	1,281.0	131.1	10.23	
Effect of ALM [8]	341.3	26.5		
Total assets	1,622.3	157.6		9.71
Liabilities [7]	1,114.0	(86.5)	(7.76)	
Effect of ALM [8]	452.6	(39.8)		
Total liabilities	1,566.6	(126.3)		(8.06)
Interest gap			**2.47**	**1.65**
Total				
Financial assets that generated financing revenue [7]	10,688.5	636.7	5.96	
Effect of ALM [8]	598.1	34.6		
Total assets	11,286.6	671.3		5.95
Financial liabilities that caused financing expenses [7]	10,118.1	(461.8)	(4.56)	
Effect of ALM [8]	598.2	(50.2)		
Total liabilities	10,716.3	(512.0)		(4.78)
Interest gap			**1.39**	**1.17**

Notes: at the end of Appendix C.

Rates of income and expenses – of the Bank and its consolidated companies[1] (continuation)

Appendix C (continuation)

	2011	
	Balance Average for the period [2]	Revenue (expenses) financing
	Millions of NIS	
For other derivative instruments		1.4
Commission from financing business and revenue from other financing [4]		34.7
Profit from financing activity before expenses for credit losses		195.4
Expenses for Credit Losses		(13.4)
Profit from other financing activity after expenses due to credit losses		**182.0**
Financial assets that generated financing revenue	10,688.5	
Assets deriving from derivative instruments [6]	19.6	
Other financial assets [7]	153.1	
Provision for Credit Losses	(88.0)	
Total financial assets	**10,773.2**	
Financial liabilities that caused financing expenses	10,118.1	
Liabilities deriving from derivative instruments [6]	7.4	
Other financial liabilities [7]	25.3	
Total financial liabilities	**10,150.8**	
Total surplus financial assets on financial liabilities	622.4	
Non-financial assets	35.3	
Non-financial liabilities	(34.9)	
Total capitalized means	**622.8**	

Notes: at the end of Appendix C.

Rates of income and expenses – of the Bank and its consolidated companies[(1)] (continuation)

Appendix C (continuation)

Foreign currency – nominal in US dollar

		2012			
				Revenue (expense) rate[(5)]	
		Balance Average for the period[(2)]	Revenue (expenses) Financing	without effect derivatives	Total effect derivatives
		Millions of US$		In percentages	
Local activity [(3)]					
Assets [(7)]		403.2	10.7	2.65	
Effect of ALM	(8)	195.4	0.6		
Total assets		598.6	11.3		1.89
Liabilities (7)		368.9	(2.9)	(0.79)	
Effect of ALM	(8)	59.6	(0.5)		
Total liabilities		428.5	(3.4)		(0.81)
Interest gap				**1.86**	**1.08**

		2011			
				Revenue (expense) rate[(5)]	
		Balance Average for the period[(2)]	Revenue (expenses) Financing	without effect derivatives	Total effect derivatives
		Millions of US$		In percentages	
Local activity [(3)]					
Assets [(7)]		362.3	9.7	2.68	
Effect of ALM	(8)	108.1	0.8		
Total assets		470.4	10.5		2.23
Liabilities (7)		316.4	(2.4)	(0.76)	
Effect of ALM	(8)	145.0	(0.5)		
Total liabilities		461.4	(2.9)		(0.63)
Interest gap				**1.92**	**1.60**

Rates of income and expenses – of the Bank and its consolidated companies[1] (continuation)

Appendix C (continuation)

Notes:

(1) The data provided in this table is data before and after the effect of derivative instruments (including off-balance-sheet effect of derivative instruments)

(2) On the basis of the monthly opening balance, except for the non-linked Israeli currency sector where the average balance is calculated on basis of daily data, and after deduction the average balance-sheet balance of specific provisions for doubtful debts.

(3) Including Israeli currency linked to foreign currency.

(4) Including profits and losses from investment sales in debentures and fair value adjustments of negotiable debentures.

(5) The percentages are calculated on the basis of data in thousands of Shekels.

(6) The average balance-sheet balance of derivative instruments (not including average off-balance-sheet balance of derivative instruments).

(7) Except for derivative instruments

(8) ALM – Derivatives that are part of the Bank's assets and liability management system (with the exception of options), that concerning them is possible to ascribe the income (expense) to the linked segment.

Complete data on revenue and expense rates in each segment, according to various balance sheet sections, will be provided upon request.

Exposure of the Bank and its consolidated companies for changes in interest rates as of December 31

Appendix D

	December 31				
	2012				
	with Requirement until month	Over month until 3 months	Over 3 months until year	Over year until 3 years	Over 3 years until 5 years
	Millions of NIS				
Non-linked Israeli currency					
Financial assets	4,491.7	863.2	1,059.0	134.6	85.6
Derivative financial instruments (except options)	72.9	18.8	77.9	89.6	-
Total fair value	4,564.6	882.0	1,136.9	224.2	85.6
Financial liabilities	(3,822.8)	(1,175.7)	(537.8)	(626.7)	(42.4)
Derivative financial instruments (except options)	(144.7)	-	(42.6)	(50.9)	(4.9)
Total fair value	(3,967.5)	(1,175.7)	(580.4)	(677.6)	(47.3)
Financial instruments, net					
Exposure to changes in segment interest rates	597.1	(293.7)	556.5	(453.4)	38.3
Accumulated segment exposure	**597.1**	**303.4**	**859.9**	**406.5**	**444.8**
Israeli currency index – linked					
Financial assets	86.6	160.6	735.3	987.4	1,235.6
Derivative financial instruments (except options)	69.5	-	-	50.1	-
Total fair value	156.1	160.6	735.3	1,037.5	1,235.6
Financial liabilities	(62.0)	(236.6)	(1,133.9)	(1,138.5)	(997.7)
Derivative financial instruments (except options)	-	-	-	(50.2)	-
Total fair value	(62.0)	(236.6)	(1,133.9)	(1,188.7)	(997.7)
Financial instruments, net					
Exposure to changes in segment interest rates	94.1	(76.0)	(398.7)	(151.2)	237.9
Accumulated segment exposure	**94.1**	**18.0**	**(380.6)**	**(531.8)**	**(293.9)**
Foreign currency (2)					
Financial assets	1,293.7	37.7	86.0	39.7	74.9
Derivative financial instruments (except options)	7.4	-	-	-	-
Total fair value	1,301.1	37.7	86.0	39.7	74.9
Financial liabilities	(935.5)	(227.1)	(268.1)	(5.4)	(0.2)
Derivative financial instruments (except options)	-	(17.4)	(31.8)	(37.8)	(1.4)
Total fair value	(935.5)	(244.5)	(299.9)	(43.2)	(1.6)
Financial instruments, net					
Exposure to changes in segment interest rates	365.6	(206.8)	(213.9)	(3.4)	73.2
Accumulated segment exposure	**365.6**	**158.8**	**(55.1)**	**(58.6)**	**14.6**
Total exposure to changes in interest rates					
Total assets	5,871.9	1,061.5	1,880.3	1,161.7	1,396.1
Derivative financial instruments (except options)	149.8	18.8	77.9	139.7	-
Total fair value	6,021.7	1,080.3	1,958.2	1,301.4	1,396.1
Total liabilities	(4,820.3)	(1,639.5)	(1,939.9)	(1,770.5)	(1,040.4)
Derivative financial instruments (except options)	(144.7)	(17.4)	(74.4)	(138.9)	(6.3)
Total fair value	(4,965.0)	(1,656.9)	(2,014.3)	(1,909.4)	(1,046.7)
Financial instruments, net					
Exposure to changes in segment interest rates	1,056.7	(576.5)	(56.0)	(608.0)	349.4
Accumulated exposure	**1,056.7**	**480.1**	**424.1**	**(183.9)**	**165.6**

Exposure of the Bank and its consolidated companies to changes in interest rates as of December 31 (continuation)

December 31								
2012							2011	
Over 5 years Up to 10 years	Over 10 years Up to 20 years	Over 20 years	without period Repayment (1)	Total	Rate Yield Internal	during life Average	Rate Yield Internal	during life Average
Millions of NIS					%	years	%	years
232.0	23.2	(0.2)	29.9	6,919.0	3.70	0.38	4.26	0.62
-	-	-	-	259.2	-	0.44		0.05
232.0	23.2	(0.2)	29.9	7,178.2	3.70	0.38		0.61
(12.0)	-	-	-	(6,217.3)	2.13	0.29	3.27	0.31
-	-	-	-	(243.1)	-	0.61		0.28
(12.0)	-	-	-	(6,460.4)	2.13	0.30		0.31
220.0	23.2	(0.2)	29.9	717.8	1.57	0.08	7.53	0.93
664.8	**688.0**	**687.8**	**717.8**	**717.8**				
450.8	155.2	4.6	-	3,816.1	3.13	3.00	3.68	3.16
-	-	-	-	119.6	-	0.58		0.22
450.8	155.2	4.6	-	3,935.7	3.13	2.93	3.68	3.08
(423.3)	(14.5)	-	-	(4,006.6)	1.50	2.47	2.75	2.33
-	-	-	-	(50.2)	-	1.62		-
(423.3)	(14.5)	-	-	(4,056.8)	1.50	2.46		2.33
27.5	140.7	4.6	-	(121.1)	1.63	0.47	0.93	0.83
(266.5)	**(125.7)**	**(121.2)**	**(121.2)**	**(121.1)**				
27.0	11.8	-	4.6	1,575.3	3.82	0.44	3.81	0.23
-	-	-	-	7.4	-	-	-	-
27.0	11.8	-	4.6	1,582.7	3.82	0.44	3.81	0.23
-	-	-	-	(1,436.3)	0.90	0.18	1.33	0.23
-	-	-	-	(88.4)	-	-		0.23
-	-	-	-	(1,524.7)	0.90	0.17	1.33	0.23
27.0	11.8	-	4.6	58.0	2.92	0.28	2.48	-
41.7	**53.5**	**53.5**	**-**	**-**				
709.7	190.2	4.4	34.5	12,310.3	**3.14**	1.20	3.83	1.35
-	-	-	-	386.2		0.47		0.11
709.7	190.2	4.4	34.5	12,696.5	**3.14**	1.18		1.33
(435.3)	(14.5)	-	-	(11,660.3)	**1.85**	1.02	2.81	0.96
-	-	-	-	(381.7)	**-**	0.60		0.25
(435.3)	(14.5)	-	-	(12,042.0)	**1.85**	1.01	2.81	0.95
274.5	175.7	4.4	34.5	654.6	**1.29**	0.17	1.02	0.38
440.0	**615.8**	**620.2**	**654.6**	**654.6**				

(1) The balance sheet balances are presented in the column "without repayment period."

(2) Local activity, including Israeli currency linked to foreign currency.

Notes:

A. Additional details of exposure to changes in the interest rates in each segment, according to various balance sheet sections, will be provided upon request.

B. In this table, the data are by periods presenting the current value of the future flows when they are capitalized according to the interest rate that is deducted from them to the included fair value for the financial instrument in Note 21 of the Financial Statement, following the discounts according to which the fair value of the financial instrument is calculated. For additional information concerning discounts used to calculate the fair value, see Note 21 of the Financial Statement.

C. The internal yield rate; that is, the interest rate deducted from the expected cash flows of the financial instrument to the fair value included for it, in Note 21 of the Financial Statement.

D. The average effective life time of financial instruments group approximates the percent of change in fair value that will be caused as result of a small change in the internal yield rate of each of the financial instruments.

Comprehensive credit risk for the public according to market branches – consolidated

Appendix E

	December 31, 2012								
	Total credit risk[1]		Debts [2] and off-balance-sheet credit risk (with the exception of derivatives) [3]						
				From this:			Credit Losses[4]		
	Total	Problematic [5]	Total	Debts [2]	Problematic [5]	Defective	Expenses for Credit Losses	Write offs Net write-offs	Balance of provision for credit losses
	Millions of NIS								
Public – commerce									
Agriculture	5.1	-	5.1	2.7	-	-	(0.1)	0.1	- [6]
Industry	22.1	0.7	22.1	16.0	0.7	-	0.2	0.2	0.1
Construction and real estate – construction	1,798.7	79.7	1,798.7	1,167.0	79.7	57.2	1.8	1.1	7.9
Construction and real estate – Real Estate Activities	421.1	19.5	421.1	377.1	19.5	13.0	0.1	-	0.1
Electricity and water	0.9	-	0.9	0.9	-	-	- [6]	-	- [6]
Commerce	30.9	4.7	30.9	26.8	4.7	4.6	0.8	0.5	0.6
Hotels, food, and accommodation services	2.6	0.1	2.6	2.1	0.1	-	(0.2)	0.2	- [6]
Transport and storage	52.6	0.5	52.6	51.9	0.5	-	0.2	0.3	0.4
Communications and computer services	4.2	-	1.1	1.0	-	-	- [6]	-	- [6]
Financial services	45.8	-	45.4	38.0	-	-	0.2	-	0.2
Business services and others	36.6	1.1	35.3	31.3	0.1	-	0.3	0.2	0.2
Public and community services	14.7	0.2	13.3	10.4	0.2	0.2	- [6]	-	0.1
Total commerce	**2,435.3**	**106.5**	**2,429.1**	**1,725.2**	**105.5**	**75.0**	**3.3**	**2.6**	**9.6**
Individuals – housing loans	**7,389.9**	**261.6**	**7,389.9**	**6,882.7**	**261.6**	**-**	**(1.8)**	**7.6**	**60.5**
Individuals – other	**1,315.6**	**33.3**	**1,315.6**	**1,064.2**	**33.3**	**3.1**	**34.5**	**25.9**	**22.5**
Total Public - Activity in Israel	**11,140.8**	**401.4**	**11,134.6**	**9,672.1**	**400.4**	**78.1**	**36.0**	**36.1**	**92.6**
Banks in Israel	**177.9**	**-**	**141.8**	**141.8**	**-**	**-**	**- [6]**	**-**	**- [6]**
The Israeli Government	**223.8**	**-**	**223.8**	**223.8**	**-**	**-**	**- [6]**	**-**	**- [6]**
Total Activity in Israel	**1,542.5**	**401.4**	**11,500.2**	**0,037.7**	**400.4**	**78.1**	**36.0**	**36.1**	**92.6**
Banks abroad	**24.5**	**-**	**23.1**	**23.1**	**-**	**-**	**-**	**-**	**-**
Total	**11,567.0**	**401.4**	**11,523.3**	**10,060.8**	**400.4**	**78.1**	**36.0**	**36.1**	**92.6**

Exposure of the Bank and its consolidated companies to changes in interest rates as of December 31 (continuation)

Appendix E (continuation)

(1) Balance sheet credit risk and off-balance-sheet credit risk, including derivative instruments. Including: Debts – NIS 10,060.8 million, Debentures – NIS 22.8 million, Assets for derivative instruments – NIS 20.9 million and credit risks in off-balance-sheet financial instruments as calculated for the purpose of the borrower's liability limitations – NIS 1,462.5 million (in 2011 including: Debts – NSI 9,148.8 million, Debentures – NIS 133.7 million, Assets for derivative instruments – NIS 7.2 million and credit risk in off-balance-sheet financial instruments as calculated for the purposes of the borrower's liability limitation – NIS 1,210.9 million).

(2) Credit for the public, credit for the government, deposits, banks and other debts, with the exception of debentures and securities that were borrowed or purchased as part of the return purchase agreements.

(3) Credit risk in off-balance-sheet financial instruments as calculated for the purpose of borrower's liability limitation, with the exception of derivative instruments.

(4) Including for off-balance-sheet credit instruments (presented in the balance sheet in the section on Other Liabilities).

(5) Balance sheet and off-balance-sheet credit risk that is defective, inferior or under special supervision, including for housing loans for which there is a provision based on the depth of the arrears and housing loans for which there is no provision based on the depth of the arrears that is in arrears by 90 or more days.

(6) Balance less than NIS 0.1 million.

Total credit risk for the public according to market branches – consolidated (continued)

Reported amounts

Appendix E (continuation)

	December 31, 2011								
	Total credit risk(1)		Debts (2) and off-balance-sheet credit risk (with the exception of derivatives) (3)						
				From this:			Credit Losses(4)		
	Total	Problematic (5)	Total	Debts (2)	Problematic (5)	Defective	Expenses for Credit Losses	Write offs Net write-offs	Balance of provision for credit losses
	Millions of NIS								
Public – commerce									
Agriculture	7.7	0.2	7.7	7.0	0.2	-	(0.2)	-	0.2
Industry	28.6	0.5	28.6	25.3	0.5	-	(0.3)	-	0.1
Construction and real estate – construction	1,574.3	98.7	1,570.0	973.7	96.1	33.5	-	1.7	7.2
Construction and real estate – Real Estate Activities	391.7	9.7	391.7	391.7	9.7	2.1	-	-	-
Electricity and water	0.9	-	0.9	0.9	-	-	-	-	-
Commerce	32.0	1.4	32.0	29.4	1.4	-	(2.0)	0.1	0.3
Hotels, food, and accommodation services	15.3	-	15.3	14.8	-	-	0.6	0.3	0.4
Transport and storage	68.2	2.0	68.2	66.8	2.0	-	0.5	0.5	0.5
Communications and computer services	12.8	-	1.8	1.6	-	-	0.1	0.1	-
Financial services	159.2	-	63.4	44.3	-	-	-	-	-
Business services and others	75.0	1.3	53.6	47.7	1.3	-	-	-	0.1
Public and community services	43.4	0.2	42.2	22.9	0.2	-	-	0.1	0.1
Total commerce	**2,409.1**	**114.0**	**2,275.4**	**1,626.1**	**111.4**	**35.6**	**(1.3)**	**2.8**	**8.9**
Individuals – housing loans	**6,987.4**	**253.5**	**6,987.4**	**6,627.9**	**253.5**	**-**	**1.2**	**8.3**	**69.9**
Individuals – other	**1,096.9**	**52.1**	**1,096.9**	**894.8**	**52.1**	**-**	**15.2**	**8.2**	**13.9**
Total Public - Activity in Israel	**10,493.4**	**419.6**	**10,359.7**	**9,148.8**	**417.0**	**35.6**	**15.1**	**19.3**	**92.7**
Banks in Israel	**7.2**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
The Israeli Government	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Total Activity in Israel	**10,500.6**	**419.6**	**10,359.7**	**9,148.8**	**417.0**	**35.6**	**15.1**	**19.3**	**92.7**
Banks abroad	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Total	**10,500.6**	**419.6**	**10,359.7**	**9,148.8**	**417.0**	**35.6**	**15.1**	**19.3**	**92.7**

* Presented again

Consolidated balance sheet – multi quarter information for the end of each quarter for the years 2011 and 2012

Reported amounts

Appendix F

	2012				2011			
	Quarter 4	Quarter 3	Quarter 2	Quarter 1	Quarter 4	Quarter 3	Quarter 2	Quarter 1
	Millions of NIS							
Assets								
Cash and deposits at the Bank	1,360.6	1,054.4	762.5	433.7	792.3	1,272.9	509.9	530.2
Securities	1,163.0	1,150.1	1,390.2	1,883.9	1,490.7	1,557.3	1,351.8	1,192.3
Net credit for the public	9,581.4	9,487.9	9,441.4	9,166.7	9,057.8	8,798.8	8,562.3	8,327.8
Buildings and equipment	117.9	102.3	93.7	83.7	79.7	68.0	62.7	63.2
Assets for derivative instruments	20.9	12.3	4.9	11.4	7.2	14.1	21.6	22.3
Other assets	47.7	41.6	45.3	54.0	54.9	57.6	60.3	53.4
Total assets	**12,291.5**	**11,848.6**	**11,738.0**	**11,633.4**	11,482.6	11,768.7	10,568.6	10,189.2
Liabilities and capital								
Public deposits	9,813.7	9,605.2	9,533.5	9,283.5	9,064.6	9,195.0	7,875.4	7,522.6
Deposits from banks	63.3	71.1	72.8	73.5	76.2	82.4	82.5	84.0
Government deposits	-	-	1.3	1.9	0.8	31.0	-	5.3
Liability certificates and deferred liability notes	1,581.0	1,400.8	1,369.4	1,538.2	1,611.9	1,752.8	1,917.5	1,885.3
Liabilities for derivative instruments	16.4	13.1	19.2	5.0	15.0	10.3	7.1	-
Other liabilities	123.0	72.2	67.7	71.4	69.5	66.1	62.6	90.5
Total liabilities	**11,597.4**	**11,162.4**	**11,063.9**	**10,973.5**	10,838.0	11,137.6	9,945.1	9,587.7
Equity	694.1	686.2	674.1	659.9	644.6	631.1	623.5	601.5
Total liabilities and capital	**12,291.5**	**11,848.6**	**11,738.0**	**11,633.4**	11,482.6	11,768.7	10,568.6	10,189.2

Consolidated Profit and Loss Statements – multiple quarter information for the years 2011 and 2012

Reported amounts

Appendix G

	2012				2011*			
	Quarter 4	Quarter 3	Quarter 2	Quarter 1	Quarter 4	Quarter 3	Quarter 2	Quarter 1
	Millions of NIS							
Income from Interest	**102.7**	**154.7**	**170.4**	**127.9**	123.2	148.1	156.5	131.2
Interest expenses	**42.9**	**95.6**	**112.7**	**73.6**	70.0	102.3	117.4	94.5
Income from Interest, net	**59.8**	**59.1**	**57.7**	**54.3**	53.2	45.8	39.1	36.7
Expenses for Credit Losses**	**15.8**	**10.7**	**6.3**	**3.2**	7.1	4.8	2.4	0.8
Income from Interest Net after Expenses for Credit Losses	**44.0**	**48.4**	**51.4**	**51.1**	46.1	41.0	36.7	35.9
Non-Interest Income								
Non-Interest Financing Income	**5.4**	**3.2**	**10.2**	**3.8**	3.3	5.8	(4.0)	1.0
Fees	**21.9**	**22.3**	**22.7**	**23.3**	23.1	22.3	22.7	23.8
Other revenues	**0.2**	**0.2**	**0.1**	**0.1**	-	-	25.5	-
Total Non-Interest Income	**27.5**	**25.7**	**33.0**	**27.2**	26.4	28.1	44.2	24.8
Operating and Other Expenses								
Salaries and accompanying expenses	**36.1**	**33.9**	**35.4**	**32.4**	37.5	33.3	32.3	31.0
Maintenance and depreciation of buildings and equipment	**12.9**	**11.6**	**11.6**	**10.8**	10.5	9.7	9.9	7.5
Other expenses**	**20.0**	**15.3**	**16.7**	**17.8**	13.2	12.5	12.2	13.5
Total Operating and Other Expenses	**69.0**	**60.8**	**63.7**	**61.0**	61.2	55.5	54.4	52.0
Profit before tax	**2.5**	**13.3**	**20.7**	**17.3**	11.3	13.6	26.5	8.7
Provision for tax	**(0.1)**	**5.1**	**6.6**	**6.1**	1.8	2.9	6.5	3.4
Net profit	**2.6**	**8.2**	**14.1**	**11.2**	9.5	10.7	20.0	5.3
Earnings per Share (in NIS)								
Basic and Diluted Earnings Per Share (NIS)	0.04	0.12	0.20	0.16	0.12	0.13	0.31	0.09

* The comparison numbers in this Statement were reclassified following the instruction issued by the Supervisor of Banks regarding adoption of the new format for the Profit and Loss Statement. For more information, see Note 2 of the Financial Statements. It should be noted that in the second quarter of 2011, the Other Revenues item included profit from the sale of the Bank's administrative building for NIS 25.4 million, and in the tax expense item for a sum of NIS 4.6 million. For more information, see Note 8 of the Financial Statements.

** Reclassified

Statement (Certification)

I, Uriel Paz, hereby declare that:

1. I have reviewed the annual report of the Bank of Jerusalem (hereinafter: "the Bank") for the year 2012 (hereinafter: "the Report").

2. Based on my knowledge, the report does not include any incorrect presentation of material facts and does not lack presentation of material facts required for the presentation therein. In view of the circumstances in which the same presentation have been included, they will not be misleading in relation to the period covered by the report.

3. Based on my knowledge, the Financial Statements and the other financial information included in the report reflect in a proper manner, from any material aspect, the financial status, financial performance, changes in equity, and cash flows of the bank for the days and periods presented in the report.

4. I and others at the bank declaring this statement are responsible for their determination and compliance of controls and procedures concerning the disclosure and internal auditing of the Bank on financial reporting. And also:

   A. We determined these controls and procedures, or caused their determination under our supervision of these controls and procedures, designated to ensure that the material information referring to the Bank, including its consolidated corporations, is brought to our attention by others at the Bank and in those corporations, particularly during the preparation period of the report;

   B. We determined internal auditing of these financial reporting, or caused its determination under our supervision of the internal auditing for such a financial report, designated to provide a reasonable level of security concerning the reliability of the financial report and that the Financial Statements for external purposes are edited according to accepted accounting regulations and the instructions of the Supervisor of Banks and his guidelines;

   C. We assessed the effectiveness of the controls and procedures concerning the the Bank's disclosure and we presented our conclusions in the report concerning the effectiveness of the controls and procedures concerning disclosure, for the end of the period covered in the report based on our assessment; as well as

   D. We did not discover in the report any change in internal auditing of the Bank on the Financial Statement that materially affected, or that could reasonably be expected to significantly affect the Bank's internal auditing of the Financial Statements; as well as

5. I and others at the Bank declaring this statement disclosed to the auditing accountant, the Board of Directors and the Audit Committee of the Board of Directors of the Bank, based on our most updated assessment concerning the internal audit of the financial report:

A. All the material deficiencies and essential weaknesses determined in the operating of the internal auditing of the financial report, that may reasonably be expected to damage the capability of the Bank to record, work, summarize, and report the financial information; as well as

B. Any fraud, whether material or not, in which the management is involved or other employees are involved having a significant function in the internal auditing of the Bank of the financial reports.

The aforesaid shall not detract from my or anyone else's responsibility, by law.

Uriel Paz

Chief Executive Officer

February 28, 2013

Statement (Certification)

I, Arnon Zayit, hereby declare that:

1. I have reviewed the annual report of the Bank of Jerusalem (hereinafter: "the Bank") for the year 2012 (hereinafter: "the Report").

2. Based on my knowledge, the report does not include any incorrect presentation of material facts and does not lack presentation of material facts required for the presentation therein. In view of the circumstances in which the same presentation have been included, they will not be misleading in relation to the period covered by the report.

3. Based on my knowledge, the Financial Statements and the other financial information included in the report reflect in a proper manner, from any material aspect, the financial status, financial performance, changes in equity, and cash flows of the bank for the days and periods presented in the report.

4. I and others at the bank declaring this statement are responsible for their determination and compliance of controls and procedures concerning the disclosure and internal auditing of the Bank on financial reporting. And also:

   A. We determined these controls and procedures, or caused their determination under our supervision of these controls and procedures, designated to ensure that the material information referring to the Bank, including its consolidated corporations, is brought to our attention by others at the Bank and in those corporations, particularly during the preparation period of the report;

   B. We determined internal auditing on this financial report, or caused its determination under our supervision of internal auditing on such financial reporting, designated to provide reasonable level of security concerning the reliability of the financial report and that the Financial Statements for external purposes are edited according to the accepted accounting regulations and instructions from the Supervisor of Banks and his guidelines;

   C. We assessed the effectiveness of the controls and procedures concerning the Bank's disclosure, and we presented our conclusions in the report concerning the effectiveness of the controls and procedures concerning disclosure, for the end of the period covered by the report based on our assessment; and also

   D. We did not discover in the report any change in internal auditing of the Bank on the Financial Statement that materially affected, or that could reasonably expect to significantly affect the Bank's internal auditing of the Financial Statements; and also

5. I and others at the Bank declaring this statement disclosed to the auditing accountant, the Board of Directors and the Audit Committee of the Board of Directors of the Bank, based on our most updated assessment concerning the internal audit of the financial report:

   A. All the material deficiencies and essential weaknesses determined in the operating of the internal auditing of the financial report, that may reasonably be expected to damage the capability of the Bank to record, work, summarize, and report the financial information; as well as

   B. Any fraud, whether material or not, in which the management is involved or other employees are involved having a significant function in the internal auditing of the Bank of the financial reports.

The aforesaid shall not detract from my or anyone else's responsibility, by law.

Arnon Zait

Vice CEO, Manager of Finance Department
and Chief Accountant

February 28, 2013

Report of the Board of Directors and the management concerning the internal audit of the financial report

The Board of Directors and the management of the Bank of Jerusalem Ltd. (hereinafter – the Bank) are responsible for the establishment and existence of proper internal audit of the financial report (as defined in the instructions for reporting to the public concerning "Report of the Board of Directors"). The internal auditing system of the Bank was programmed in order to provide a reasonable level of confidence to the Board of Directors and the management of the Bank concerning the proper preparation and presentation of the published Financial Statements according to generally accepted accounting principles and instructions of the Supervisor of Banks and his guidelines. Independent of their program's quality level, all the internal control systems have understandable limitations. Therefore, even if it was determined that these systems are effective, they can only provide a reasonable level of confidence in relation to the preparation and presentation of the financial statement.

The management, under supervision of the Board of Directors, maintains comprehensive control systems designated to ensure that transactions are performed according to management's authority; the assets are protected, and accounting registration is reliable. In addition, the management, under supervision of the Board of Directors, takes steps in order to ensure that the information and communications channels are effective and (monitored), including the implementation of internal control procedures.

The management of the bank, under the supervision of the Board of Directors, evaluates the effectiveness of the bank's internal auditing of the financial reports as at December 31, 2012, based on the criteria that has been determined in the internal auditing model by the Committee of Sponsoring Organizations of the Treadway Commission COSO). Based on this evaluation, the management believes that as at December 31, 2012, the Bank's internal auditing of financial reports was effective.

The effectiveness of the bank's internal auditing of financial reports as of December 31, 2012, was audited by the bank's auditor: "Kost Forer Gabbay & Kasierer," as has been stated in their report on page 202, in which an unqualified opinion was included on the issue of effectiveness of the internal auditing by the bank for its financial reports as of December 31, 2012.

Zeev Gutman	Uriel Paz	Arnon Zait
Chairman of the Board of Directors	Chief Executive Officer	Vice CEO, Manager of Finance Department and Chief Accountant

February 28, 2013

Financial Statements

Financial Statement for 2012

Bank of Jerusalem Ltd. and its consolidated companies

Financial Statements – contents

Kost Forer Gabbay & Kasierer.
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Independent Auditor's Report to Shareholders of Bank of Jerusalem Ltd. - In accordance with the Instructions from the Supervisor of Banks concerning Internal Auditing of the Financial Reports

We audited the bank's internal control of the financial statements of the Bank of Jerusalem Ltd. and its subsidiaries (hereinafter together: the Bank) for December 31, 2012, based on the criteria that were determined as part of the integrated internal auditing model by the Committee of Sponsoring Organizations of the Treadway Commission (hereinafter: COSO). The Bank's Board of Directors and the management are responsible for implementation of an effective internal control over financial reporting and their assessment of the effectiveness of the internal control over financial reporting that are included in the attached report of the Board of Directors and Management regarding the internal control over financial reporting. Our responsibility is to give our opinion on the Bank's internal control over financial reporting based on our audit.

We conducted our audit according to the standards of the American Public Company Accounting Oversight Board (PCAOB) concerning the audit of the internal control over financial reporting as adopted by the Institute of Certified Public Accountants in Israel. These standards require that we plan and perform the audit to obtain reasonable assurance, in every material respect, of implementation of effective internal control over financial reporting. Our audit included reaching an understanding regarding internal control over financial reporting, assessment of the risk that there exists a material weakness, as well as an examination and assessment of the effectiveness of planning and operation of the internal control based on the assessed risk. Our audit also included the implementation of other procedures we deemed necessary according to the circumstances. We believe that our audit provides a reasonable basis for our opinion.

The Bank's internal control over financial reporting is a process designated to provide reasonable assurance concerning the reliability of financial reporting and the preparation of Financial Statements for external purposes in accordance with generally accepted accounting principles in Israel (Israeli GAAP) and the instructions and directives of the Supervisor of Banks. Internal control over a bank's financial reporting includes those policies and procedures that: (1) Relate to entries that, with reasonable detail, accurately reflect in a suitable manner the Bank's transactions and transfers of its assets (including their removal from their possession); (2) Provide reasonable assurance that the transactions were recorded as required in order to enable preparation of financial reports in accordance with the generally accepted accounting principles in Israel (Israeli GAAP), and in accordance with the instructions and directives of the Supervisor of Banks; and that receipt and outlays of the Bank's monies were made only according to the permits of the Bank's Board of Directors and management; and (3) Provide reasonable assurance for the prevention or disclosure at the time of acquisition, unauthorized use of or transfer (including removal from authority) of the Bank's assets by unauthorized parties that might materially impact the financial statements.

Because of its built-in limitations, internal control over financial reporting might not prevent or uncover a false presentation. Moreover, drawing conclusions concerning the future based on any current effective assessment is exposed to risk that the controls might become unsuitable due to changes in circumstances or a worsening in the degree to which the policies or regulations are enforced.

In our opinion, the Bank fulfilled in all material respects, effective internal control over financial reporting as of December 31, 2012 based on the criteria that were established as part of the integrated internal control published by COSO.

We also audited, in accordance with the accepted auditing principles in Israel, and certain auditing standards whose application in auditing of banking corporations was set forth in the instructions and guidelines of the Supervisor of Banks, the financial statements – of the Bank and its consolidated companies – for the dates of December 31, 2012 and 2011 and for every one of the years of the three-year period that ended on December 31, 2012, and our report from February 28, 2013 included an unqualified opinion of those financial statements.

Kost Forer Gabbay & Kasierer.
Accountants

Tel Aviv,
February 28, 2013

Kost Forer Gabbay & Kasierer.
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Independent Auditor's Report to Shareholders of Bank of Jerusalem Ltd. - Annual Financial Statements

We audited the consolidated balance sheets of the Bank of Jerusalem Ltd. (Hereinafter - The Bank) for December 31, 2012 and 2011, as well as the Profit and Loss Statements, Statements of Changes in Equity, and Statements of Cash Flows – of the Bank and its consolidated companies – for each the three years that ended on December 31, 2012. These financial statements are the responsibility of the Bank's Board of Directors and management. Our responsibility is to express our opinion about the financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Israel, including those prescribed by the Israeli Auditors (Mode of Performance) Regulations 5733-1973 and certain auditing standards used in the auditing of banking corporations prescribed in the instructions and guidelines of the Supervisor of Banks. These standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and information in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Bank's Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the aforementioned financial statements present fairly, and in compliance with generally accepted accounting principles, in all material respects, the financial position of the Bank and its consolidated companies on December 31, 2012 and 2011 and the results of the company's operations and changes in equity and cash flows - of the Bank and its consolidated companies for each of the three years in the period ending on December 31, 2012, in accordance with generally accepted accounting principles in Israel (Israeli GAAP). Moreover, in our opinion, the aforesaid Financial Statements are prepared in compliance with the instructions and guidelines of the Supervisor of Banks.

We conducted our audit according to the standards of the American Public Company Accounting Oversight Board (PCAOB) concerning the audit of the internal control over financial reporting as adopted by the Institute of Certified Public Accountants in Israel, the internal control over financial reporting of the Bank on December 31, 2012, based on criteria that were established in the integrated framework of internal control published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated February 28, 2013 included an unqualified opinion on the effectiveness of the Bank's internal control over financial reporting.

Kost Forer Gabbay & Kasierer.
Accountants

Tel Aviv,
February 28, 2013

Balance sheets

Reported amounts

		consolidated		The Bank	
		December 31			
		2012	2011	2012	2011
	Note	Millions of NIS			
Assets					
Cash and deposits at the Bank	3	**1,360.6**	792.3	**1,359.9**	791.8
Securities(1)	4	**1,163.0**	1,490.7	**1,184.7**	1,573.0
Credit for the public	5	**9,672.1**	9,148.8	**9,672.1**	9,148.8
Provision for Credit Losses	5	**(90.7)**	(91.0)	**(90.7)**	(91.0)
Net credit for the public	5	**9,581.4**	9,057.8	**9,581.4**	9,057.8
Credit for the government	6	**-**	-	**-**	-
Investments in Held Companies	7	**-**	-	**364.7**	343.2
Buildings and equipment	8	**117.9**	79.7	**19.5**	21.8
Assets for derivative instruments	20	**20.9**	7.2	**20.9**	7.2
Other assets	9	**47.7**	54.9	**43.0**	43.2
Total assets		**12,291.5**	11,482.6	**12,574.1**	11,838.0
Liabilities and capital					
Public deposits	10	**9,813.7**	9,064.6	**11,189.2**	10,517.0
Deposits from banks	11	**63.3**	76.2	**63.3**	76.2
Government deposits		**-**	0.8	**-**	0.8
Debentures and deferred liability notes	12	**1,581.0**	1,611.9	**498.0**	517.8
Liabilities for derivative instruments	20	**16.4**	15.0	**16.4**	15.0
Other liabilities (2)	13	**123.0**	69.5	**113.1**	66.6
Total liabilities		**11,597.4**	10,838.0	**11,880.0**	11,193.4
Equity	16a	**694.1**	644.6	**694.1**	644.6
Total liabilities and capital		**12,291.5**	11,482.6	**12,574.1**	11,838.0

Zeev Gutman
Chairman of the Board of Directors

Uriel Paz
Chief Executive Officer

Arnon Zait
Vice CEO, Manager of Finance Department and Chief Accountant

Approval date of the Financial Statements:
February 28, 2013

(1) That were pledged to lenders in the bank and consolidated on December 31, 2012 and December 31, 2011, a sum of NIS 169.5 million and a sum of NIS 354.0 million, respectively. *For details concerning Securities measured in fair value, see Note 4.

(2) That were pledged to lenders in the bank and consolidated on December 31, 2012 and December 31, 2011, a sum of NIS 1.9 million and a sum of NIS 1.7 million, respectively.

The notes to the Financial Statements are an integral part of them.

Profit and Loss Reports

Reported amounts

		consolidated			The Bank		
		For the year ending on December 31					
		2012	2011(1)	2010(1)	2012	2011(1)	2010(1)
	Note	Millions of NIS					
Income from Interest	23	**555.7**	559.0	426.7	**562.0**	564.5	431.2
Interest expenses	23	**324.8**	384.2	302.1	**337.8**	398.2	314.2
Income from Interest, net		**230.9**	174.8	124.6	**224.2**	166.3	117.0
Expenses due to Credit Losses(2)	5	**36.0**	15.1 (3)	(2.6)	**36.0**	15.1 (3)	(2.6)
Income from Interest Net after Expenses for Credit Losses		**194.9**	159.7	127.2	**188.2**	151.2	119.6
Non-Interest Income							
Non-Interest Financing Income	24	**22.6**	6.1	24.5	**22.1**	6.8	22.7
Fees	25	**90.2**	91.9	98.9	**81.3**	81.9	86.7
Other revenues	26	**0.6**	25.5	0.6	**0.1**	0.1	0.6
Total Non-Interest Income		**113.4**	123.5	124.0	**103.5**	88.8	110.0
Operating and Other Expenses							
Salaries and accompanying expenses	27	**137.8**	134.1	120.7	**123.2**	122.6	110.9
Maintenance and depreciation of buildings and equipment		**46.9**	37.6	29.4	**33.6**	27.4	22.3
Other expenses	28	**69.8**	51.4 (3)	53.0	**98.8**	67.8 (3)	66.7
Total Operating and Other Expenses		**254.5**	223.1	203.1	**255.6**	217.8	199.9
Profit before tax		**53.8**	60.1	48.1	**36.1**	22.2	29.7
Provision for tax	29	**17.7**	14.6	14.0	**15.0**	8.0	10.4
Profit after tax		**36.1**	45.5	34.1	**21.1**	14.2	19.3
The Bank's portion of profit from regular operations of held companies after the tax effect		**-**	-	-	**15.0**	31.3	14.8
Net profit		**36.1**	45.5	34.1	**36.1**	45.5	34.1
Earnings per Share (in NIS)							
Basic and Diluted Earnings Per Share (NIS)		**0.51**	0.65	0.48	**0.51**	0.65	0.48

* The comparison numbers in this Statement were reclassified following the instruction issued by the Supervisor of Banks regarding adoption of the new format for the Profit and Loss Statement. For more information, see Note 2 of the Financial Statements. It should be noted that in 2011, the Other Revenues item included profit from the sale of the Bank's administrative building for NIS 25.4 million, and, in the tax expense item a sum of NIS 4.6 million. For more information, see Note 8 of the Financial Statements.

(2) On January 1, 2011, the Bank adopted for the first time the instructions of the Supervisor of Banks concerning "Measurement and disclosure of defective debts, credit risk and provision for credit losses". The comparison numbers from the previous periods were not presented again. Therefore, the data for the period ending on December 31, 2012 and December 31, 2011 are not comparable to the data of the previous years. For additional explanations concerning the effect of the instruction's first adoption, see Note 2 of the Financial Statements.

(3) Reclassified.

The notes on the Financial Statements are an integral part of them.

Statements on Changes in Equity

Reported amounts

		Capital funds			Comprehensive Profit (Loss) after accumulation		
	Capital Shares Paid	From premium	From benefit For transactions payment based on Shares	Total Capital Shares Paid and capital funds	reconciliations for presentation of available securities for sale according to value fair	Retained earnings	Total Capital Equity
				Millions of NIS			
Balance as at January 1, 2010	127.3	95.3	-	222.6	(2.1)	385.4	605.9
Net profit	-	-	-	-	-	34.1	34.1
Reconciliation for securities							
Available for sale at fair value	-	-	-	-	7.0	-	7.0
Reconciliations for presentation of for securities							
available for sale that have been reclassified for the Statement of Profit and Loss	-	-	-	-	(17.6)	-	(17.6)
Effect of the referring tax	-	-	-	-	3.8	-	3.8
Balance as at January 1, 2011	127.3	95.3	-	222.6	(8.9)	419.5	633.2
Accumulated net effect from the tax for the first-time adoption as at January 1, 2011, of the instruction concerning measurement of defective debts and provision for credit losses	-	-	-	-	-	(9.5)	(9.5)
Net profit	-	-	-	-	-	45.5	45.5
Paid dividend	-	-	-	-	-	(25.0)	(25.0)
Benefit due to share-based payment transactions	-	-	3.1	3.1	-	-	3.1
Reconciliation for securities							
Available for sale at fair value	-	-	-	-	(6.2)	-	(6.2)
Reconciliations for presentation of for securities							
available for sale that have been reclassified for the Statement of Profit and Loss	-	-	-	-	1.9	-	1.9
Effect of the referring tax	-	-	-	-	1.6	-	1.6
Balance as at January 1, 2012	**127.3**	**95.3**	**3.1**	**225.7**	**(11.6)**	**430.5**	**644.6**
Net profit	**-**	**-**	**-**	**-**	**-**	**36.1**	**36.1**
Benefit due to share-based payment transactions	**-**	**-**	**0.7**	**0.7**	**-**	**-**	**0.7**
Reconciliation for securities							
Available for sale at fair value	**-**	**-**	**-**	**-**	**29.6**	**-**	**29.6**
Reconciliations for presentation of for securities							
available for sale that have been reclassified for the Statement of Profit and Loss	**-**	**-**	**-**	**-**	**(10.3)**	**-**	**(10.3)**
Effect of the referring tax	**-**	**-**	**-**	**-**	**(6.6)**	**-**	**(6.6)**
Balance as at December 31, 2012	**127.3**	**95.3**	**3.8**	**226.4**	**1.1**	**466.6**	**694.1**

The notes on the Financial Statements are an integral part of them.

Statements of Cash Flows

Reported amounts

	consolidated			The Bank		
	For the year ending on December 31					
	2012	2011	2010	2012	2011	2010
	Millions of NIS					
Cash flows from current activity						
Net profit for the year	**36.1**	45.5	34.1	**36.1**	45.5	34.1
Reconciliations:						
The Banking Corporation's share of undistributed profits of the held companies	**-**	-	-	**(15.0)**	(31.3)	(14.8)
Depreciation of buildings and equipment	**17.7**	13.0	10.3	**2.3**	2.4	2.8
Expenses for Credit Losses	**36.0**	15.1 *	(2.6)	**36.0**	15.1 *	(2.6)
Loss (profit) from sale of available for sale securities	**(41.3)**	(36.8)	(24.9)	**2.2**	(46.3)	(23.7)
Profits realized from fair value reconciliations for fair value of negotiable securities	**(20.2)**	(7.7)	(3.2)	**(21.8)**	(7.7)	(3.2)
Profit from realization of buildings and equipment	**-**	(20.8)	-	**-**	-	-
Expenses derived from share-based payment transactions	**0.7**	0.8	-	**0.7**	0.8	-
Deferred taxes, net	**(18.4)**	(4.0) *	1.6	**(17.6)**	(4.4) *	0.5
Severance Pay – increase in surplus reserve for purpose (increase in surplus reserve for purpose)	**(5.7)**	4.7	(6.3)	**(5.8)**	5.0	(6.3)
Net change in current assets:						
Deposits in banks	**-**	-	0.9	**-**	-	0.9
Credit for the public	**(559.6)**	(1,052.1)	(685.0)	**(559.6)**	(1,052.1)	(685.0)
Assets for derivative instruments	**(13.7)**	16.7	(0.3)	**(13.7)**	16.7	(0.3)
Negotiable securities	**(72.0)**	(181.9)	(17.1)	**(72.0)**	(184.1)	(20.6)
Other assets	**19.0**	(6.3)	(11.0)	**5.9**	(5.2)	(4.7)
Net change in current liabilities:						
Deposits from banks	**(12.9)**	(10.3)	(17.4)	**(12.9)**	(10.3)	(17.4)
Public deposits	**749.1**	1,656.8	292.1	**672.2**	1,429.6	741.9
Government deposits	**(0.8)**	(4.1)	(0.5)	**(0.8)**	(4.1)	(0.5)
Liabilities for derivative instruments	**1.4**	4.3	(0.3)	**1.4**	4.3	(0.3)
Other liabilities	**92.2**	102.7	90.0	**37.1**	30.8	41.9
Net cash from current activities	**207.6**	535.6	(339.6)	**74.7**	204.7	42.7

* Reclassification.

The notes to the Financial Statements are an integral part of them.

Statements of Cash Flows (continuation)

Reported amounts

	consolidated			The Bank		
	For the year ending on December 31					
	2012	2011	2010	2012	2011	2010
	Millions of NIS					
Cash flow from activity in liabilities and capital						
Purchase of available for-sale securities	**(2,423.4)**	(1,260.3)	(1,585.7)	**(2,205.0)**	(1,372.3)	(1,287.6)
The consideration from the sale of available for-sale securities	**2,877.3**	1,190.3	1,265.9	**2,676.4**	1,148.0	1,043.3
Consideration from the redemption of available for-sale securities	**26.6**	116.3	122.8	**26.6**	144.1	130.9
Acquisition buildings and equipment	**(48.7)**	(45.3)	(14.6)	**-**	(1.2)	(0.4)
Consideration from the realization of buildings and equipment	**-**	34.7	-	**-**	-	-
Net cash from investment activities	**431.8**	35.7	(211.6)	**498.0**	(81.4)	(113.8)
Cash frlows from financing activity						
Offering of debentures and deferred liability notes	**296.9**	104.3	667.0	**78.7**	104.3	-
Redemption of debentures and deferred liability notes	**(368.0)**	(510.6)	(227.7)	**(83.3)**	(62.7)	(41.0)
Dividend paid to shareholders	**-**	(25.0)	-	**-**	(25.0)	-
Net cash from financing activity	**(71.1)**	(431.3)	439.3	**(4.6)**	16.6	(41.0)
Effect of movement in the exchange rates on cash balances	**(7.4)**	0.9	(4.8)	**(7.4)**	0.9	(4.8)
Increase (decrease) in cash and deposits in banks	**575.7**	139.1	(107.1)	**575.5**	139.0	(107.3)
Balance of cash and deposits in banks for the beginning of the year	**792.3**	652.3	764.2	**791.8**	651.9	764.0
Balance from cash and deposits in banks at the end of the year	**1,360.6**	792.3	652.3	**1,359.9**	791.8	651.9
Interest and taxes paid and/or received:						
Interest received	**833.4**	797.8	708.0	**833.4**	797.8	708.0
Interest paid	**329.2**	346.7	299.6	**329.2**	346.7	299.6
Taxes on income that were paid	**10.3**	25.4	11.8	**10.3**	25.4	11.8
Taxes that were received	**7.7**	5.1	20.1	**7.7**	5.1	20.1
Non-cash activity:						
Acquisition of property, plant and equipment with credit	**7.2**	-	-	**-**	-	-
Realization of property, plant and equipment with credit	**-**	-	-	**-**	-	-

The notes to the Financial Statements are an integral part of them.

Notes on Financial Statements

Financial Statement for 2012

Bank of Jerusalem Ltd. and its consolidated companies

Notes to Financial Statements

Note 1 – General

Bank of Jerusalem Ltd. (Hereinafter: The Bank) is a commercial bank that engages in granting housing credit and other retail credit, financing construction concerns for housing, as well as enlisting allotted time deposits, activity in the capital market, current account management, and provision of private banking services to foreign residents.

The Bank is a subsidiary of "Ytzu" Investment Company Ltd. (hereinafter - "Ytzu") and its securities are listed on the Tel Aviv Stock Exchange.

The Bank's Financial Statements are prepared according to generally accepted accounting principles in Israel (Israeli GAAP), as well as according to the Supervisor of Bank's instructions and guidelines concerning preparing a bank's annual Financial Statement.

Note 2 – Accounting Policy

The principle accounting policies that are implemented during the the preparation of the Financial Statements in a consistent manner, and are compatible with the instructions of the Supervisor of Banks and his guidelines, which are:

A. Reporting Base of the Financial Statements

1. In the past, the Bank edited its Financial Statements on basis of historical cost adjusted to the CPI. The adjusted amounts, as aforementioned, which are included in the Financial Statements as at December 31, 2003, were used as a starting point for nominal financial reporting effective as of January 1, 2004. Additions implemented after the transition date are included in nominal values. According to Accounting Standard Number 12 concerning "Discontinuance of Adjustment of Financial Statements," the adjustments of the Financial Statements for inflation was discontinued as of December 31, 2003, and effective from the same date when the Bank started to publish reported amounts. The non-banking financial asset amounts do not necessarily represent the realization value or updated economic value, but only the reported amounts for the same assets.

   In the Financial Statements, the meaning of "cost" is cost in reported amounts.

   Summary of the Bank's data in historical nominal values for tax purposes are provided in Note 31.

2. General consolidation

The Bank's consolidated Financial Statements include the reports from the companies over which the Bank has control. The advantages and mutual transactions between the Bank and its subsidiaries were canceled in the consolidated Financial Statements. In the Bank's separate reports, investments in consolidated companies are presented according to the equity method.

3. Functional currency and presentation currency

The functional and presentation currency of the Bank and of its subsidiaries is the New Israel Shekel (NIS).

B. Foreign currency and linkage

Assets and liabilities in foreign currency or linked to them, and those linked to the CPI, are included in the Financial Statements as follows:

1. Those linked to the CPI are presented according to the known index as of the balance sheet date.

2. Those in foreign currency or linked to it are presented according to the representative exchange rate published by the Bank of Israel on the balance sheet date, except for cases in which the terms of agreement are determined differently.

Below are details on the CPI and representative exchange rates of the US Dollar and their rates of increase (decrease):

	As at December 31			Increase (Decrease) rate in the year		
	2012	2011	2010	2012	2011	2010
				In percentages		
Exchange rate for US dollar (in NIS)	3.733	3.821	3.549	(2.3)	7.7	(6.0)
CPI-basis 1993 (points):						
Month of November	219.8	216.3	210.9	1.6	2.5	2.3
Month of December	219.4	216.3	211.7	1.4	2.2	2.7

Note 2 – Accounting policy (continuation)

C. Principles for The preparation Financial Statements:

Accounting Standard Number 29 – "Adoption of International Financial Reporting Standards IFRS"

In June 2009, the Supervisor of Banks published a circular on the subject of "Reporting of Banking Corporations and Credit Card Companies in Israel according to International Financial Reporting Standards (IFRS)" that determines the manner of expected adoption of the International Financial Reporting Standards (IFRS) by banking corporations and credit card companies.

According to the circular, the designated date for reporting of banking corporations and credit card companies according to the IFRS standards is:

1. On issues that are not core banking business issues, as of January 1, 2011, the Bank implements the following IFRS standards, subject to the instructions of the Supervisor regarding the manner of their implementation:

The Subject	Reporting Standard
Share-based Payment	IFRS 2
Business Combinations	IFRS 3
Non-current Assets Held for Sale and Discontinued Operations	IFRS 5
Accounting Policies, Changes in Accounting Estimates and Errors	IAS 8
Events After the Balance Sheet Date	IAS 10
Property, Plant and Equipment	IAS 16
Leases	IAS 17
Accounting for Government Grants and Disclosure of Government Assistance	IAS 20
The Affects of Changes in Foreign Exchange Rates	IAS 21
Consolidated and Separate Financial Statements	IAS 27
Investments in Associated Companies	IAS 28
Financial Reporting in Hyper-inflationary Economies	IAS 29
Interests in Joint Transactions	IAS 31
Earnings per Share	IAS 33
Financial Reporting for Interim Periods	IAS 34
Impairment of Assets	IAS 36
Intangible Assets	IAS 38
Investment Property	IAS 40

See Section Z below – First-time adoption of Accounting Standards, Accounting Standards

Update and Instructions from the Supervisor of the Banks. In addition, International Financial Reporting Standard IAS 19, which discusses employee benefits, has not yet been adopted. The standard will be adopted in accordance with the directives of the Supervisor of Banks.

2. Regarding matters pertaining to the bank's business core – The final decision will be determined in consideration of the timetables determined in the U.S. and in progress of the convergence process between international and the American's standard entities.

   Furthermore, it was clarified in the circular that after completing the adjustment process of the international standards instruction, the banks' supervising authorities will remain in control for determining obligatory clarifications concerning the manner of implementation of the international standards requirements, as well as to determine additional instructions in cases in which it is obligated by the requirements of the supervising authorities in the world's developed countries or on subjects for which there is no reference in the international standards. In addition, the Supervisor of Banks will maintain his authority for determining requirements for disclosure and reporting.

3. The International Financial Reporting Standards, as specified above, will be adopted according to the following principles (except if otherwise determined by the Supervisor of Banks):

   - In cases in which there is no specific reference in the standards or in the interpretation of material subjects or there are a number of alternative handling on the material subject, the banking corporation will operate according to the specific implementation guidance that has been determined by the Supervisor;

   - In cases in which the material issue is raised while not receiving response in the international standards or in the implementation instructions of the Supervisor, the banking corporation will handle the issue according to generally accepted accounting principles in banks in the U.S. that specifically apply to these issues;

   - In places in which there is a reference in the international standard to another international standard that has been adopted in the Public Reporting Standards, the banking corporation will operate according to the international standard instructions;

   - In places in which there is a reference in the international standard to another international standard that has not been adopted in the Public Reporting Standards, the banking corporation will operate according to the reporting instructions and according to the generally accepted accounting principles in Israel;

- In places in which the international standards refers to definition of defined term in the Public Reporting Instructions, the reference of the term in the standards will replace the original reference.

As of January 1, 2011 and henceforth, the Bank updates continuously the accounting process on the subjects dealt with in the circular according to the new International Financial Reporting Standards that have been published on these issues and according to the principles adopted by and with the clarifications of the Supervisor of Banks.

D. Offsetting Financial Assets and Liabilities

1. Assets and liabilities that are derived from the identical contra side are presented in the balance sheet in a net sum pursuant to the following accrued conditions:

    - For said liabilities, there is a legally enforceable right to offset the liabilities from the assets;

    - There is an intent to pay the liabilities and to realize the assets on a net basis and/or simultaneously.

2. Assets and liabilities with two different opposing parties are presented in the balance sheet based on a net sum pursuant to the existence of two aforementioned conditions, and pursuant to the existence of an agreement between the three parties that clearly anchors the Bank's right to offset said liabilities.

3. Deposits whose payment to the depositor depends on the degree to which collection from the credit was offset from the credit obtained from these deposits, when the Bank is at no risk of credit loss. The margin in the aforementioned activities was included in the "Fees" item.

E. Securities

1. Debentures held for redemption are presented according to their reduced cost as at the reporting day.

2. Available for sale securities are presented in the balance sheet according to fair value. The fair value is based on the quoted prices for securities that have quoted prices or revaluation data received from external sources regarding non-banking negotiable debentures. The profit or loss concerning them with deduction of the reserve suitable for tax is presented in a separate section as part of equity, called: "Reconciliations for presentation for available for sale securities according to fair value".

Note 2 – Accounting policy (continuation)

3. Negotiable securities are presented in the balance sheet according to fair value. Profits or losses from reconciliation for fair value are credited to the Profit and Loss Statement in the Section on Financing Income Not from Interest

4. The Bank examines at each reporting period the need to record a provision for an impairment of securities that is not of a temporary nature. The Bank has defined criteria for tracking securities and the aforementioned examination. These criteria are based, among others, on the following factors:

   - Change in securities rating by rating agencies.
   - The length of time during which the security is traded at high yield.
   - Exceptional cases such as irregular impairment.

   Furthermore, the bank has determined additional criteria according to which immediate provision for impairment will be implemented. These criteria are based, among others, on the following factors:

   - The current rating of the securities by the rating agencies.
   - The current exceptional yield at which the securities were traded.
   - The length of time during which the securities were traded at exceptional yield.
   - Significant negative indications within the Financial Statements.

   In addition, criteria were set for implementation of the provision for impairment for impairment that is not of a temporary nature pursuant to two accrued conditions:

   1. 40% decline in the value of the security in contrast with the depreciated cost.
   2. Decrease for nine consecutive months.

F. Transfer and service of financial assets and clearance of liabilities

The Bank implements the measurement and disclosure regulations as determined by the American accounting standards ASC 860-10 (FAS 140), the transfer and service of financial assets and clearance of liabilities, as amended by ASC 860-10, transfer and service of financial assets (FAS 166), for the purpose of handling transfers of financial assets and clearance of liabilities. According to these regulations, the financial assets will be accounted as sales, if and only if, all of the following conditions exist: (1) the financial asset that has been transferred isolated from the transferring factor, also in a bankruptcy situation or other receivership; (2) each receiver (or, if the received is an entity whose sole designation is to deal in securitization or in limited financing activity it received, each third party holding rights of the beneficiary) may mortgage or exchange the assets (or the beneficiary rights) it received, and there are no conditions that also limit the receiver (or third party that holds the benefit rights) from exploiting the right to mortgage or replace, and also grant the transferor a larger benefit than a trivial benefit; (3) the transferor, or consolidated companies included in the Financial Statements, or its agents, do not preserve active control in the financial assets or the beneficiary rights referring to these transferred assets.

In addition, in order for a transfer of part of the financial assets be considered a sale, the transferred part must comply with the definition of participating rights. Participating rights must comply with the following criteria: the right must present proportional rights in relation to the full financial asset; all the cash flow received from the assets are divided between the participating rights in a manner proportional to their part in ownership; the rights are not inferior rights (subordinated) in relation to other rights; there is no return right to the transferor of others holding the participating rights (except in case of violation of presentation or liabilities, current contractual liabilities for service at the financial asset in whole and management of contact in transfer and contractual liabilities for dividing of offset of any benefit that has been received by any holder of participating rights); and the transferrer and the holder of participating rights have no right to mortgage or replace the financial asset as whole, except if all the holders of participating rights agree to mortgage or replace the financial asses in whole.

In case the transaction complies with the conditions for handling the transaction as a sale, the financial assets being transferred are deducted from the Bank's balance sheet. In case not all the sales conditions exist, the transfer is considered a secured debt. The sale of part of the financial assets that has no participating rights is handled as secured debt, that is, the transferred assets continue to be registered in the Bank's balance sheet and the exchange from sale will be recognized as the Bank's liability.

Securities that have been sold are not deducted from the balance sheets and are presented in section "Securities," and against them the deposit for securing restoration for which securities are presented in the section "Securities that have been loaned or sold as part of return purchasing agreements". Purchase securities are recorded according the value on the implementation day of the transaction in section "Securities that have been loaned of purchased as part of return sales agreements".

The Bank monitors the fair value of securities that have been loaned or were loaned, as well as securities that have been transferred in return purchase and sales agreements on a daily basis and security requirements implemented in suitable cases. Interest received or paid for the aforementioned securities is reported as income or expenses, respectively.

According to instructions of the Supervisor, securities loan transactions are performed as "regular" credit transactions in which the bank loans securities against a collateral portfolio and the lender does not transfer to the banking corporation a safety margin specifically referring to the securities loan transaction, presented as credit to the public according to market value and are attached to the loaner liability. The changes in value of the aforementioned accrual based securities are credited in the Profit and Loss Statement in the section "Revenue from credit for the public," and reconciliation to market value is imputed for available for sale securities based on fair value.

The Bank deducts liability if and only if the liability was cleared, meaning one of the following conditions existed: (a) the Bank paid the lender and is released from its obligation because of the liability, or (b) the Bank legally was released through legal proceedings or in agreement with the lender from being the main debtor because of the liabilities.

ASU 2011-03 – The existing conditions of effective control in return purchasing agreements (hereinafter: "the Amendment"):

In April 2011 the FASB published an amendment whose objective is to improve and simplify the accounting process in return purchasing transactions from repo type and similar transactions. The change applies transversely to financial assets that have been transferred as part of repo transactions and for other agreements that also provide and require the transferor to purchasing anew or redeeming the financial assets before the contractual maturity date.

According to the update, the manner in which existing effective control is assessed effectively by the transferor of return purchasing transactions must be changed. Assessment of existence of effective control will focus on the transferor's contractual rights and contractual liabilities, and therefore (1) criterion that requires that the transferor will have the ability to purchase papers that have been transferred, as well as in case of failure by the transferor, will not be considered; and also, (2) guidelines on the subject of security requirements in relation to this criterion. Additional criteria for examining the existence of effective control have not been changed by the ASU.

Note 2 – Accounting policy (continuation)

The amendment will be applied as of January 1, 2012, on transfer of assets that are valid after that, or on existing transactions in which a change was applied after the starting date.

Implementation of the amendment had no significant influence.

G. Measurements and disclosure of impaired debts, credit risk, provision for credit losses

According to the new instruction from the Supervisor of Banks on the subject of measurement and disclosure of defective debts, credit risk and provision for credit losses; the Bank implements, as of January 1, 2011, the American Accounting Standards on the subject (ASC 310) and the positions of the bank supervisory authorities in the US and the American SEC (Securities and Exchange Commission), as adopted in the Public Reporting Instructions.

The main changes in the accounting policies following the instruction are:

A banking corporation is required to maintain provision for credit loss at the suitable level in order to cover the expected credit loss relating to its credit portfolio, including for off-balance-sheet credit risk. Provisions for credit losses will include:

- The individual provision for credit losses - The provision is implemented based on measurement of impairment of the debt based on the current value of expected future cash flows, capitalized by the debt's effective interest rate, or when the debt is contingent upon collateral, or when the Bank determines that seizure of the asset is probable according to the fair value of the collateral pledged in order to ensure that credit (after deducting sales cost). The need for individual provision is examined for each debt whose contractual balance (without deduction: write-offs that do not involve a legal waiver, unrecognized interest, provisions for credit losses, and collaterals) is NIS 1 million or more and for any other debt that has been recognized for the purpose of individual examination by the banking corporation.

- The group provision for credit losses – are applied for large groups of small and homogeneous debts, as well as for debts that have been individually examined and have not been found defective. Measurement of credit losses, because of credit balance sheets and off-balance-sheet credit instruments, is based on an estimation of past credit loss rates for each of the homogeneous groups of debts with similar risk characteristics. The group provision rates for credit losses are based on historical loss rates between 2008 and 2010, and the rate of net write-offs that were actually recorded in the various market branches from 2011, as divided between non-problematic credit and problematic credit between 2008 and 2012. The assessed provision on a group basis for off-balance-sheet credit instruments is based on provision rates that have been determined for balance-sheet credit, while considering the realization rate of the expected credit of off-balance-sheet credit risk. The realization rate for credit is calculated by the Bank based on conversion factors for credit as specified in the Proper Banking Management instructions number 203, Measurement and capital adequacy – credit risk – the standard approach, with certain adjustments in cases in which the Bank has prior experience indicating the credit realization rate.

New types of problematic debts have been determined, of which:

- Impaired debt – credit that the banking corporation expects that it might not collect all the amounts, according to contractual conditions of the debt agreement, and the provision for credit losses for which they are measured in the individual provision track. The aforementioned classification should be applied, also on credit found in arrears for over 90 days except if it is well secured and is in collection stages, and on problematic debts that have been reorganized which as part of the reorganization the Bank granted the debtor waiver (Concession), while in other conditions it would not have considered to grant it. Debt that is classified as defective debt will be assessed on an item by item basis for the purpose of implementing credit loss provisions or write-offs. In view of the fact that the debt for which re-organization of the problematic debt has been implemented, will not be repaid according to the original contractual condition; the debt will continue to be classified as an defective debt even after the debtor returns to the repayment track according to the new conditions. Despite the aforementioned, the problematic debits in re-organization will return to accrue interest as the debt is being paid in accordance with the terms of the arrangement for a period of at least 6 consecutive months. The projected credit payment is supported by an established credit assessment. Classification of problematic debt as "defective" will be canceled if the cumulative terms are fulfilled: (a) the debt is well secured and in collection proceedings. (b) The debt does not include "arrears components" (including write-offs) and the Bank believes that the original balance will be paid in full.

- Inferior credit risk – is defined as insufficiently protected credit by current established value and the payment capability of the debtor or of the guaranteed collateral; and is so characterized as there is a clear possibility that the bank corporation will absorb a certain loss if the deficiencies will not be amended.

No interest revenue is to be recorded for defective debts. Regarding debts that are examined and allocated on a group basis while in arrears for 90 days or more, the Bank continues to accumulate interest income. During collection of a cash-based defective debt, if there is any doubt regarding collection of the remaining recorded balance of the debt – the receipt will be used to reduce the recorded balance to the degree required to remove this doubt. If there is no doubt about the collection of the remaining recorded balance of the debt – the receipt will be recognized as cash-based income from interest.

The instructions for write-offs of problematic debts became more stringent. Among others, it was determined by this instruction that:

- Write-offs should be made for all debts that are considered impossible to collect or debts for which management of collection efforts of the Bank are long-term.
- Write-offs should be done immediately against credit loss provision of each part of surplus debt on collateral value that has been recognized as non-collectible.
- Write-offs of debt that has been assessed for individual provision of credit loss should not be deferred. Debts should be written off within two years.
- Problematic debts for which the provision is measured based on group provision for credit loss should be written off when the arrears period is more than 150 days.
- At the first time of implementation, the Bank was, among others, required to:
- Write-off each debt which at this date had met write-off conditions.
- To classify by classification for special supervision, inferior, or defective; each debt that meets the aforementioned classification conditions.
- To cancel all interest income accumulated at the implementation date of the instruction and not yet actually collected for each debt which at this date meet the referred conditions.
- The differences accumulated at the date of first application of the new guidelines, between the balance of the provision for credit losses, according to the existing guidelines, and their calculated balance according to the new guidelines, are reflected in Section “Surplus in Equity.”
- The additional provision is only used as a marker concerning the group provision so that in case the total group provision is lower than the additional and general provision, provision should be implemented according to the highest of the two calculations.

The additional provision rate applied on all different types of problematic debts will be as follows:

- Credit risk "under special supervision" – 1%.

- Credit risk "inferior" – 2%.
- Credit risk "defective" – 4%.

Additionally, according to to the Supervisor of Banks' guideline, the group provision for credit losses is calculated for housing loans provided, as of the beginning of 2009 and onwards, and while the ratio between debt and the mortgaged asset value at the time of setting up loan, providing Loan To Value Ratio (LTV) is greater than 60%.

Furthermore, the Bank is implementing Accounting Standard ASU 2011-02 on the subject of decision by the credit provider whether re-organization of debt is a re-organization of problematic debt:

During April 2011, the FASB published an update of Accounting Standard ASU 2011-02, on the subject of a decision by the credit provider whether re-organization of debt is a re-organization of problematic debt. According to the American standard on this subject (ASC 310), debt re-organized as problematic debt is a debt that was formally transferred to re-organization, as part of: economic or legal circumstances related to financial difficulties of the debt – The Bank granted a concession to the borrower. The update provides additional guidelines to the Bank clarifying when the re-organized debt will be considered as re-organization of problematic debt as part of the concession that was granted by the credit provider. In particular, clarifications have been included relating to the manner in which examination of the concession in effective interest is implemented. Furthermore, guidelines have been included for determining whether a concession has been granted in re-organization of a debt as part of the contractual interest is greater according to the new conditions of the original contractual interest, but still less in comparison to the market interest for loans with similar risk characteristics and in consideration of the total conditions determined as part of the re-organization. Furthermore, it is clarified that in situations in which the debtor has no capability to recruit debt with similar risk characteristics in market conditions, the Bank will be required to examine the composite of other conditions of re-organization to determine whether to grant the concession. Additionally, according to the existing standard, an insignificant postponement of payments will not be a concession. The ASU provides a list of characteristics that may indicate that the delay is not significant, such as: the amount of the payment that has been re-organized is insignificant in relation to the balance of the debt that has not been paid, or in relation to the security value, as well as the postponement is not significant in relation to the payment frequency (monthly, quarterly, and so forth), the original contractual repayment date and the original expected duration of the debt. According to ASU, the credit provider is required to consider the accumulative affect of the debt re-organization that was implemented in the past during implementation of an assessment whether the postponement is significant.

In addition, the ASU determines a list of disclosure requirements concerning re-organization activity of problematic debt.

G. Provision for credit losses for housing loans

As of January 1, 2006, the Bank implements the guidelines from the Supervisor of Banks for implementing Proper Banking Management instructions on the issue of "provisions for doubtful debts for housing loans" (hereinafter – "Supervisor's Guidelines"). The Supervisor's guidelines refer to the number of principle types of topics in relation to the manner of calculating provisions for doubtful debs for housing loans, including the general calculation for individuals for determining the minimum provision for housing loans, while the depths arrear in them increases over six months (the provision is calculated at a rate between 8% to 80% from the passed-due debt balance, according to depths arrears), that were implemented by the Bank in the past, except for those listed below:

Provision for loans in new arrangements and reorganization:

A. Loans in arrangements – The loan where an arrangement is implemented without change in the clearance timetable for the loan balance. Calculation of arrears depth is performed while considering the arrears balance and before the original monthly charge. Cancellation of provision will be implemented if the loan still meets the loan repayments during the period of two years as of the arrangement date or if half of the remaining period of the loan has passed during which arrears have been created, whatever comes first.

B. Loan in reorganization – A loan whose clearance table has changed. For these losses, the provision will be frozen according to the arrears depth and an idealistic arrears balance will be recorded comparing the arrears balance and all by the arrangement date. Freezing of the provision and the balance of the notional arrears will be for a period of half a year while at its end the Bank will be entitled to reduce the notional arrears balance during two years in a straight line. Additionally, conforming to the Supervisor of Banks' guidelines (Letters from the Supervisor dated July 11, 2010 and from May 1, 2011), the group provision for credit losses is calculated at 0.75% for housing loans balance provided as of the beginning of 2009 and onwards, and while the ratio between debt and the mortgage asset value at the time of loan, (LTV) is higher than 60%.

Furthermore, the bank's policy for housing loan debt write-offs that were provided for loss but as a result of collection proceedings, there are no collateral balance to realize the debt against it.

I. Property, Plant and Equipment

- Recognition and measurement

Note 2 – Accounting policy (continuation)

Buildings and equipment are presented according to cost, less accumulated depreciation and losses from impairment. The cost includes costs that can be directly attributed to fixed assets and that brings it to a position and condition necessary for its operation.

When material parts of the fixed assets have different duration, they are handled as separate items of fixed assets. Buildings for sale are presented by cost or their realizable value, whatever is lower.

- Subsequent costs

Cost for replacing part of the fixed asset item is recognized as part of the value on the books for the same item if it is expected that the future embedded economic benefits in the replaced part will flow to the Bank and if their costs can be measured in a reliable manner. The value of the replaced part in the books – deducted. The current maintenance costs for fixed asset items are reflected in Profit and Loss with their occurrence.

- Software costs

Purchased software is measured according to cost, less accumulated depreciation and losses from impairment.

Costs related to development of computer programs or adjustments for the purpose for personal use are capitalized only if: the depreciation cost can be measured in a reliable manner; the program can be implemented from a technical and commercial aspect; future economic benefits are expected; the Bank intends and has sufficient resources to complete the development and to use or sell the program. Capitalized costs including direct costs and overhead expenses that may relate directly to preparing the program for its designated use. These costs are measured according to cost, less accumulated depreciation and losses from impairment. Other costs of fixed asset items are reflected in Profit and Loss with their occurrence.

Subsequent costs are recognized as intangible assets only if they increase the embedded future economic benefits of the asset for which they have been expended. Other costs are reflected in Profit and Loss with their occurrence.

- Depreciation

Depreciation is calculated from the cost, according to the estimated usage period, according to straight-line method applied from the date the asset was ready for use in relation to original costs. Improvements in the rented are depreciated for the duration of the lease contract including the option that it reasonably will be realized, or throughout their useful duration according to the shortest period. The estimates concerning the duration of usage and remaining value are reexamined from time to time.

Amortization of intangible assets is reflected in the Profit and Loss Statement according to straight-line method over the useful life estimate of intangible assets, including program assets, applied from the date on which assets are available for use.

Intangible assets that are created at the Bank (such as: software under development) are not systematically amortized as long as they are not available for use according to management's decision. Therefore, impairment for these intangible assets are examined at least once a year, until the date they become available for use according to management's decision.

- Derogation

The book value of fixed assets was deducted during realization or when no realization of future economic benefits were expected or realized. The difference between the net exchange from the realization, if any, and between the book value of the subtracted asset, is reflected in the Profit and Loss Statement in the section "Other Income".

For detailed reference on the subject, see Note 8 below.

J. Impairment of Non-financial Assets

The Bank examines, at each reporting date, the need for recording the provision for impairment of non-financial assets (such as: buildings and equipment and non-tangible assets including goodwill) when there are still signs, as result of events or circumstantial changes, indicating that its assets in the balance sheets are presented in amounts greater than their recoverable amount.

The recoverable amount of the cash-generating asset or unit is higher from between the net sales price and the usage value. The usage value is the current value of the future cash flow estimate, capitalized at the interest rate before tax, that is expected to be generated from use of the asset and its realization. For the purpose of examining the impairment, the assets that cannot be examined individually are grouped together into the smallest assets group that generates cash flow from continuous use, while independent in principle from assets and from other groups ("Generating Cash Unit"). When the book value of the assets exceeds the recoverable amount, the Bank recognizes the impairment at the gap height between the book value of the asset and the recoverable value. The aforementioned recognized loss will be canceled only if changes are applied to the estimates used for recoverable amount of the asset from the date of recognition of last loss of impairment, except for loss from impairment of goodwill that is not insignificant.

J. Segment Reporting

An activity segment is a line of business in the banking corporation that is involved in activities from which it may generate income and bear expenses. Its activity results are regularly examined by the management and the Board of Directors for the purpose of decision-making concerning the allocation of resources and to assess their implementation, as well as maintaining separate financial information on it. The format for reporting the Bank's activity segments is determined by the Supervisor of Banks' instructions.

For detailed reference on the subject, see Note 30 below.

L. Issue Expenses

Issue expenses of debentures and directly attributable transaction costs, liability notes and deferred liability notes are depreciated relative to the principal's balance in the turnover according to the effective interest rate method.

M. Deferred Expenses

Issuance and distribution expenses of debentures and expenses for recruitment of deposits are presented based on the cost and are depreciated during the maturity period of the liabilities according to the effective interest method.

N. Taxes on Income

Taxes on income in the Profit and Loss Statement include current and deferred taxes. Current and deferred taxes are reflected in the Profit and Loss Statement, but only if the tax derives from the transaction or event that is directly recognized in equity. In these events, tax expenses on assets are reflected in equity. The current tax is the amount of tax expected to be paid (or received) on taxable income per annum, that is calculated according to tax rate applicable under the enacted law or in fact is being enacted on the balance sheet date, including changes in tax payments relating to previous years.

The provision for taxes on the Bank's income and its consolidated companies that are financial institutions for the purpose of VAT, including profit tax imposed on the income according to the VAT Law. VAT imposed on salary in financial institutions is included in the Profit and Loss Statement in Section "Salaries and Accompanying Expenses."

Deferred taxes are calculated for provisions when including income and expenses in the time between the financial reporting and recognition for the purpose of tax income, as well as for reconciliation of non-financial assets (except for buildings) for gaps between the adjusted value and between the highest value for deduction purposes of tax income. Deferred taxes are calculated according to tax rates expected to be applied when using the reserve or realizing the tax benefit, based upon the tax law that is valid at the date of the balance sheet.

The calculation of the deferred tax does not take into account the taxes that would have been applied in the realization of investments in the held companies so long as there is an assumption of continuous holding of these investments. The dividend distribution policy in the held companies will not cause an additional tax charge in the Bank.

For detailed reference on the subject, see Note 29 below.

O. Derivative Financial Instruments

In accordance with the instructions of the Supervisor of Banks, the banking corporation should recognize all the derivative instruments, including certain derivative instruments embedded in other contracts as assets or liabilities in balance sheets and measure them according to fair value. The change in fair value of derivative instrument is reported in the Profit and Loss Statement, according to the manner in which the derivative instrument is designated. Changes in the fair value of derivatives, that determine the exposure to change in fair value of an asset, liability or a firm agreement, will be regularly recognized in the Profit and Loss Statement, as well as changes in fair value of a defined item, that may be attributed to the defined risk.

The accounting process for a change in the fair value of derivatives, which determines the exposure to changes of cash flow from an asset, from liabilities or from a forecast transaction depends on the effectiveness of the hedging ratios.

The effective part of the change in fair value of the derivative, designated for hedging cash flow is initially reported in equity and after that, when the forecast transaction affects the Profit and Loss Statement, it is reclassified for the Profit and Loss Statement.

The non-effective part of the change in fair value of the designated derivative as aforementioned, is immediately recognized in the Profit and Loss Statement.

The Bank enters into contracts that do not entirely meet the definition of a derivative instrument – these contracts may include embedded derivative instruments. An embedded derivative instrument will be separated from the host contract and handled as a derivative instrument if the following three conditions exist – jointly: the economic characteristics of the embedded derivative are not clearly related and close to those of the host contact; the involved instrument is not remeasured according to fair value conform according to accepted accounting regulations, while reporting on changes in fair value in the Profit and Loss Statement during their creation, and the separate instrument with the same failure conditions as an embedded instrument would maintain the definition of the derivative instrument. Being identified as the embedded derivative, it is separated from the host contract and handled as a derivative on its own. An embedded derivative that has been separated is presented in balance sheets together with the host contract. The separated embedded derivatives in the Bank are derived from granting credit linked to foreign currency including a floor for linkage basis and recruitment of savings plans with identical characteristics.

Profit or loss from a derivative that is not designated as a hedging instrument is regularly recognized in the Profit and Loss Statement. The transactions in derivative instruments are part of the Bank's management system of assets and liabilities. The fair value of derivative instruments is presented in the balance sheets as assets for derivatives or other liabilities, according to the matter, and the transaction results in derivative instruments deriving from their recording based on fair value are included in the Profit and Loss Statement as part of the Section "Financing Income Not from Interest."

P. Basis for Recognition of Income and Expenses

Income and expenses are recognized on an accrual basis, including income for off-balance-sheet financial instruments, with the exception of:

1. Completion of interest arriving at the Bank from the government for certain housing loans, is reflected in the Profit and Loss Statement according the effective interest embedded in cash flows deriving from the loan agreement and from the interest completion agreement.

2. Commissions from early repayment of housing loans are reflected in the Profit and Loss Statement at equal rates for three years, except for the part related to the financial capital that is reflected in the Profit and Loss Statement upon its receipt.

3. Management fees due to loans that were sold are reflected in the Profit and Loss Statement over the remainder of the loan and repayment period relative to their balance.

4. Interest arrears for housing loans are reflected in the Profit and Loss Statement only upon collection.

5. Income from dividend is reflected in the Profit and Loss Statement on the eligibility date for

their receipt.

Q. Employee Rights

1. Because of all the liabilities of employer-employee relations, there are appropriate reserves by law, agreement, management's custom and expectation. Future liabilities for jubilee grants are calculated by an actuarial expert in evaluating methods of accrued benefits and considering the probabilities based on past experience when the salary increase rate is based on past experience and varies according to the age of the employee.

2. The reserve for severance pay is calculated on the basis of their last salary and the employee's work period, and, in accordance with the law, the terms of the employment agreement, as well as managerial practice and expectations. The amount for severance pay included in the balance sheet includes accrued profits.

For detailed reference on the subject, see Note 14 below.

R. Contingent Liabilities

According to the guidelines of the Supervisor of Banks, American Accounting Standard ASC 450 has been adopted with their accompanying instructions concerning the accounting process issue of pending legal claims; except for rare cases, such as class action suits in which there is no possibility by the Bank and its legal advisers to assess their results. Based on its legal advisers concerning the probability of realization of exposure to risks from claims, the Bank management's assessment is determined on the basis of three areas of probability, as follows:

1. Expected Risk – The probability of realization of the exposure to risk is more than 70%. Because of claims included in this risk group, suitable provisions are included in the Financial Statements.

2. Probable Risk – The probability of realization of the exposure to risk is between 20% and 70%. Because of claims included in this risk group, no provisions are included in the Financial Statements but only disclosure is given.

3. Weak Risk – The probability of realization of the exposure to risk is less than or equal to 20%. Because of claims included in this risk group no provisions are included in the Financial Statements and no disclosure is given.

When the expected exposure is realized, a provision is included in the Financial Statements for the full exposure amount, as estimated by the Bank's management. In case of probable exposure, a provision is not included in the Financial Statements but disclosure is given for the amount of exposure. In case of weak exposure, there is no need to implement the provisions and/or provide disclosure. Due to claims for which the exposure to them is weak but the liability or maximum possible loss might place the continuing activity of the Bank in doubt, disclosure is provided.

For detailed reference on the subject, see Note 19 below.

S. Share-based Payment Transactions

The Bank recognizes share-based payment transactions according to International Financing Report Standard IFRS2 as adopted by the Supervisor of Banks. A benefit due to share-based payment transactions that are cleared in capitalized instruments, are measured on the date the benefit (grant day) is of provided, based on an acceptable options pricing model. The value of the benefit is regularly attributed to expenses against capital fund, over the maturity period.

The cost of a transaction cleared in cash is measured according to fair value on the grant date through use of an acceptable options pricing model. See additional details in Note 22a. Fair value is recognized as expense over the maturity period and correspondingly, is recognized as liability . Liabilities are measured again in each reporting period according to the fair value until clearance, while changes in fair value are reflected in Profit and Loss.

When the company performs changes in the conditions of the grant cleared in capitalized instruments, the additional expense is recognized beyond the original expense that was calculated for every change that increases the total fair value of the granted benefit or that it benefits with the employer/the other service provider according to fair value at the time of the change.

When changes are being implemented in a share-based payment plan, the banking corporation recognizes the influence of the changes that increase the total fair value of the plan during the remaining maturity period, and in addition to the affects on changes that change the nature of the plan from liability to capital, or vice versa.

19. Use of Estimates in the Preparation of Financial Statements

Preparation of the Financial Statements, in accordance with GAAP in Israel and the Supervisor of Banks' instructions and directives; requires use of estimates, assessments and discretion by the management, that affect the reported amounts of the assets and liabilities, on disclosure referring to contingent assets and contingent liabilities, as well as on income and expenses amounts for the reporting period. It should be clarified that the actual results might differ from these estimations.

During the implementation of the accounting estimates used in the preparation of the Bank's Financial Statements, the Bank's management is required to make assumptions for such circumstances and events involving significant uncertainty. In its discretion in determining the estimates, Bank management relies on past experience, various facts, external factors and on reasonable assumptions according to the suitable circumstances for each estimation.

The estimations and assumptions that are based on ongoing reviews. Changes in the accounting estimates are recognized in the period in which the estimates are amended and in future periods that are affected.

U. Earnings per Share

Earnings per share are calculated by dividing the net profit attributable to shareholders of the company by the weighted number of ordinary shares in existence during the period.

The basic earnings per share includes only shares that actually exist during the period.

Potential ordinary shares (convertible securities as an example of convertible debentures, option notes and options for employees) are only included in the calculation of diluted earnings per share whose affect dilutes the earning per share so that the conversion reduces the per share earning or increases the per share loss from continuing operations. In addition, potential ordinary shares that were converted during the period were included in diluted earning per share only until the conversion date, and from that moment are included in the basic earning per share.

V. Comparison numbers

A number of comparison numbers that were reclassified were mentioned in the Financial Statements. For this matter, see also Section Z below.

W. Statement of Cash Flows

The statement was prepared in accordance with the instruction of the Supervisor of Banks and International Accounting Standard 7 (IAS7) regarding Statement of Cash Flows. Cash flows from assets and liabilities are presented net, except for housing credit activity, non-monetary items in motion, non-negotiable securities and debentures and deferred liability notes. Cash also includes deposits in banks whose original period from their deposit date is up to three months.

X. Directives and clarifications concerning strengthening of internal auditing on financial reporting on the subject of employee rights

Note 2 – Accounting policy (continuation)

On March 27, 2011, directives from the Supervisor of Banks were published concerning strengthening of internal auditing on financial reporting on the subject of employee rights. The directives set forth several clarifications concerning the assessment of liability for employee rights and directives concerning internal auditing of the financial reporting process on the subject of employee rights while requiring the collaboration of a certified actuary, identification and screening of liabilities for employee rights, existence of internal auditing for the purpose of relying on the actuary's assessment and validation in addition to certain disclosure requirements. On May 23, 2011, the Supervisor of Banks published a clarification according to which the first time application of the above mentioned directive was postponed to April 1, 2011.

The directives sets forth, inter alia, that a banking corporation that expects that it will have to pay its employees, upon their leaving, benefits for contractual terms, will take into consideration the number of employees expected to leave and the benefits the Banks expects that it will be required to pay for the benefits beyond the contractual terms, for early retirement of employees.

The circular's implications on measuring liabilities and on the internal auditing process on the subject of employees rights are not material.

Y. Fair value and alternative for fair value

1. On April 28, 2011, the Supervisor of Banks published a circular on the subject of measurements of fair value and alternative fair value. The circular adopts, inter alia,:

   1.1. Measurement of Fair Value – American Accounting Standard (FAS 157 ASC 820-10) hereinafter FAS "157".

   ASC 820-10 defines fair value and establishes a consistent work framework for measurement of fair value by defining the techniques for fair value appraisal concerning assets and liabilities and determining the level of fair value and specified implementation directives.

   The circular distinguishes between two types of data that are used to determine fair value:

   Observable inputs represents information available in the market that is obtained from independent resources and data for unobservable inputs reflecting the assumptions of the banking corporation. These types of data create a hierarchy of fair value as specified below:

   Level 1 Inputs: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

   Level 2 Data: Quoted prices for similar assets and liabilities in active markets; quoted prices for identical assets or liabilities in non-active markets; prices that are derived from assessment models where all the data is material (significant inputs) that are observable in the market or are supported by observable market data.

Level 3 Data: Unobservable data for assets of liabilities derived from assessment models where one or more material data (significant inputs) in them are unobservable.

Furthermore, ASC 820-10 expands the disclosure requirements for measurement of fair value. Implementation of the regulations set forth in ASC 821-10 requires discontinuation of the usage of the Blockage Factor in the calculation of the fair value, as well as replacing the directives that prohibit recognition in day one profits and requires the determination of fair value of non-negotiable derivative instruments in the active market based on the transaction price. In addition, ASC820-10 requires the banking corporation to reflect the Bank's credit risk and other risks through fair value measurements of debt, including derivatives, that were issued by it and that were measured according to fair value.

ASC 820-10 became valid as of January 1, 2011 and henceforth, except for a number of financial instruments for which implementation is in the limited format of retrospective application on the date of the first-time adoption date. The difference between the balance-sheet balances of certain financial instruments and the values of the fair value of the same instruments is recognized as an accrued influence for the opening balance of surpluses on January 1, 2011, that is presented separately.

The banking corporation is required to re-examine the assessment method it implements to assess the fair value in consideration of the relevant circumstances for different transactions, including the latest transaction prices in the market, indicative prices for evaluation services, and results of backwards examination (back-testing) of similar types of transactions.

In January 2010, the FASB published an update of the accounting standard on the subject of improving disclosure for measurement of fair value. According to the update, amounts of material transitions from measurement of fair value according to level 2 to measurement according to level 1, and vice versa; require disclosure, as well as including explanations for these transitions. It is required to provide disclosure concerning the gross amounts of changes in measurement of fair value according to level 3 deriving from acquisition, sales, issuance, and repayment.

1.2 Alternative fair value for financial assets and financial liabilities – American Accounting Standard ASC 825-10)FAS 159) hereinafter "ASC 825-10".

The purpose of ASC 825-10 is to enable a reduction of the fluctuations in reported profits that are derived from measurement of hedged assets and liabilities, and hedged derivative instruments according to various measurement bases.

ASC 825-10 enables the banking corporation to select defined dates, for measuring fair value of financial instruments and certain other items (valid items), that according to the Public Reporting Instructions do not require measurement in their fair value. The profits and losses that have not yet been realized for changes in fair value of items for which an alternative fair value is chosen, are reported in the Profit and Loss Statement in each consecutive reporting date. In addition, costs and prepaid fees related to items for which an alternative fair value is chosen are recognized in Profit and Loss at the time of their formation and are not deferred. The choice for implementation of alternative fair value as aforementioned is implemented separately for each instrument (instrument-by-instrument) and cannot be canceled. In addition, ASC 825-10 sets forth a requirement for presentation and disclosure that are designed to facilitate a comparison between the banking corporations that choose different measurement bases for similar types of assets and liabilities. Despite the aforementioned, it is clarified by the Supervisor of Banks that the banking corporation will not chose an alternative to fair value, except if the banking corporation developed in advance knowledge, systems, procedures, and controls at a high level that would allow it to measure the item with a high level of reliability. Therefore, a banking corporation will not chose an alternative to fair value concerning any asset suitable for classification at level 2 or level 3 in the hierarchy of fair value, or regarding any liability, except if it received advanced approval from the Supervisor of Banks. The standard is effective as of January 1, 2011 and henceforth.

2 ASU 2011-04 – Measuring Fair Value (hereinafter: 'the Amendment"):

- In May 2011, the FASB published an amendment concerning ASC 820 Measurement and Disclosure of Fair Value. The new disclosure does not change the existing requirements considerably, but clarifies them. The amendment presents several changes. Among them, the main market in which the measurement will be implemented will be considered the market with the main volume and level of activity for said asset or liability, and not the market perceived by the entity that reflects the said volume or level. Use of the holding size factor is prohibited not only for negotiable instruments classified as Level 1 fair value, as currently determined, but also concerning the remaining instruments in Levels 2 and 3, with the exception of situations in which the premium or discount were taken into account when calculating the measurement of the fair value by participants in the market in the absence of Level 1 data. The amendment provides guidelines for measuring fair value in portfolios of financial instruments. Furthermore, the amendment establishes new disclosure requirements, including classification for levels in the fair value hierarchy for items that are not measured according to fair value in the balance sheet but within the confines of the Notes, disclosure concerning fair value is required. Regarding items included in Level 3, information regarding assessment that is implemented by the reporting entity and disclosure regarding sensitivity analysis of the measurement of fair value for changes in material unobservable data and the mutual relationship between unobservable data, if there exists any transition of measurement of fair value from Level 2 to Level 1 or vice versa, including a listing of the reasons for the transition.

The amendment will become valid as of January 1, 2012 from hereon in. These Financial Statements did not include comparison numbers for new disclosures. First-time adoption did not have any material affect on the Bank's financial statements, with the exception of a representative change of the new disclosure requirements.

For detailed reference on the subject, see Note 21 below.

Z. First-time adoption of Accounting Standards, Accounting Standards Update and Instructions from the Supervisor of the Banks:

Beginning from the reporting periods that begin on January 1, 2012, for the first time, the Bank is implementing the accounting standards and instructions as detailed below:

1. Instructions regarding the format of the Profit and Loss Statement for a banking corporation and adoption of GAAP in banks in the United States on measurement of income from interest.

2. Certain International Financial Reporting Standards (IFRS) and interpretations of International Financial Reporting Interpretations Committee (IFRIC) referring to the implementation of these standards, as stipulated below:

   - International Accounting Standard 7 (IAS) Statement of Cash Flows.

   - International Accounting Standard 12 (IAS) Income Taxes.

   - International Accounting Standard 23 (IAS) Credit Costs.

   - International Accounting Standard 24 (IAS) Related Party Disclosures.

3. The instructions of the Supervisor of Banks on actions between a banking corporation and controlling shareholder and between a company controlled by the banking corporation.

Note 2 – Accounting policy (continuation)

4. Update of the disclosure instructions on credit quality of debts and provision for credit losses (Hereinafter -"The Instruction").

Listed below is a description of the nature of the changes adopted in the accounting policies in the summary of consolidated interim financial statements and the effect of first-time adoption:

1. **Instructions regarding the format of the Profit and Loss Statement for a banking corporation and adoption of GAAP in banks in the United States on measurement of income from interest.**

In December 2011, the Supervisor of Banks issued an instruction regarding adoption of a new format for the Profit and Loss Statement designed to adapt the manner of presentation of the Profit and Loss Statement to the standard presentation of banking corporations around the world and in the United States, while maintaining the level of specification that exists in the instructions for reporting to the public.

As result of the adoption of the new format for the Profit and Loss Statement, the section "Profit from Financing Activity" was replaced by three sections: "Income from Interest", "Interest Expenses" and "Income from Financing that is not from Interest". Moreover, the section "Profit from Extraordinary Operations After Tax" was canceled.

In addition, in accordance with the Supervisor's instructions, the definition of the term interest was amended to clarify that interest will also include index-linked differences for the fund.

On the issue of implementing the instruction on the subject of "measurement and disclosure of impaired debts, credit risk and the provision for credit losses," the banking corporation is required to cancel the index-linked differentials that accumulated from January 1, 2012, for the debt inventory and not yet been paid for the principal, only for debts that have been classified as defective as of January 1, 2012.

The bank implemented the instructions regarding the format for the Profit and Loss Statement beginning on January 1, 2012 retroactively. The first-time adoption had no effect other than a representative change.

Listed below is a list of reclassifications that were carried out:

a. The financing profit components listed below were classified for the section on Financing Income that is Not From Interest for activities that are not for commercial purposes:

Note 2 – Accounting policy (continuation)

* Profits or Losses from the sale of available for sale debentures.

* Income/expenses for derivative instruments used for ALM activity.

* Rate differences with the exception of rate differences on interest that were included as part of the Interest Income or Expenses.

b. The financing profit components listed below were classified for the section on Financing Income that is Not From Interest for activities that are for commercial purposes:

* Profits or losses realized from fair value reconciliations for fair value of negotiable securities

* Dividends for Shares Held For Trade.

* Income / Expenses for other derivative instruments.

c. The financing profit components listed below were classified for the Fees section:

* Income from conversion fees

* Income from Maof fees

* Income from guarantee fees

As a result of the change in classifications as stipulated above, income (expenses) that were included in the profit from financing activity totaled NIS 22.1 million, and NIS 22.6 million in the bank and consolidated, respectively, for the year ending on December 31, 2012. In addition, sums of NIS 6.8 million, and NIS 6.1 million in the bank and consolidated, respectively, for the year ending December 31, 2011 as well as sums of NIS 22.7 million and NIS 24.5 million in the bank and consolidated, respectively, for the year ending December 31, 2010, as said.

Income (expenses) that were included in the profit from financing activity totaled NIS 13.3 million, NIS 14.5 million and NIS 14.6 million in the bank and consolidated, respectively, for the years ending December 31, 2012, December 31, 2011 and December 31, 2010, respectively, were classified in the "Fees" section.

d. Profits (losses) that were included in the past as part of the "Profits (Losses) from Net Investment in Shares section were reclassified and included as part of the Financing Income Not from Interest section. The sums that were classified are not material.

The section, "Profit from Irregular Activity" was canceled and the approach used in the US was adopted regarding classification of an event or transaction as a special item, in which a special item is an item that is "irregular" and "uncommon". In light of this, the banking corporation will be entitled to classify an event or transaction as a special item only with the approval of the Supervisor of Banks.

Profits (losses) that were included in the past as part of the "Profit (Loss) from Irregular Activity, after Taxes" section were reclassified as follows:

Profits (Losses) from Realization of Buildings and Equipment were classified for the "Other Income" section.

As a result of said change in classification, "Profit from Irregular Activity after Taxes" that was derived from realization of buildings and equipment totaling NIS 20.9 million in the year ending December 31, 2011, was recognized in the "Other Income" section at a sum of NIS 25.5 million, and in the Provision for Taxes section at a sum of NIS 4.5 million.

2. Certain International Financial Reporting Standards (IFRS) and interpretations of International Financial Reporting Interpretations Committee (IFRIC) referring to the implementation of these standards.

In accordance with the Supervisor of Bank's circular dated November 30, 2011, on the adoption of certain International Financial Reporting Standards (IFRS), the Bank is implementing the International Financial Reporting Standards (IFRS) listed below:

IAS 7, Cash Flow Statements;

The standard provides information through cash flow statements on changes that have been applied in the cash flow statement period and in cash value classified as cash flows during the period from current activities, from investment activities and financing activities. The cash flow statement will be made while using the indirect method, and based on after tax profit. Nevertheless, a banking corporation may present the cash flow from current activities according to the direct method.

Cash flows resulting from transactions in foreign currency are recorded in the corporation's functional currency by multiplying the sum in the foreign currency at the exchange rate between the functional currency and the foreign currency on the cash flow date. The affect of changes in the exchange rate on cash and cash equivalents held in foreign currency or that are to be paid in foreign currency are presented separately from the other changes in cash and cash equivalents.

For cash flows from interest and dividends that were received for paid as well as cash flows resulting from taxes on income, a separate disclosure will be given. It was further determined that transactions that do not require the use of cash and cash equivalents are not included in the Statement of Cash Flows but in the Appendix.

The bank retroactively implemented the instructions set forth in the standard as of January 1, 2012. The first-time adoption had no affect other than a representative change.

Listed below is a list of reclassifications that were carried out:

Net changes in flows for current assets (such as deposits in banks, negotiable securities, assets for derivative instruments, credit for the public and credit for the government) that were included in the past as part of asset activity totaling NIS 620.8 million in the bank and in consolidation, for the year ending December 31, 2012, were classified as current activity. Furthermore, sums of NIS 982.5 million, and NIS 980.4 million in the bank and consolidated, respectively, for the year ending December 31, 2011, as well as sums of NIS 701.5 million and NIS 705 million in the bank and consolidated, respectively, for the year ending December 31, 2010, were classified as stipulated.

Net changes in flows for liabilities (such as deposits from the public, deposits from banks, deposits from the government, net liabilities for derivative instruments and other liabilities) that were included in the past as part of liability and capital activity totaling NIS 659.9 million and NIS 736.8 million in the bank and consolidated, for the year ending December 31, 2012, were classified as current activity. In addition, sums of NIS 1,419.5 million, and NIS 1,646.7 million in the bank and consolidated, respectively, for the year ending December 31, 2011, respectively, as well as sums of NIS 363.9 million and NIS 766.1 million in the bank and consolidated, respectively, for the year ending December 31, 2010, were classified as stipulated.

IAS 12 – Income Tax;

The standard, in the adoption format, is similar in its instructions to Israeli Accounting Standard 19 concerning income tax that had been implemented until now by the Bank. Nevertheless, alongside the adoption of the international standard, the specific instructions that were determined by the Supervisor of Banks, have been changed.

In general, deferred tax assets will be recognized in the books for transferred losses, tax credits and available provisions granted for credits while it is expected that in the future the income will be taxable, against which it may be exploited. According to the guideline of the Supervisor of Banks the definition of the term "expected" (probable) will be applied in a consistent manner for the term "More likely than not" as part of accounting regulations accepted at banks in the U.S.

In addition, the terms required for a bank corporation to be able to determine temporary provision that can be deducted for a certain investment will be reversed in the near future through a sales transaction. The terms were designed to increase security in that the sale will be expected and based on an example that was included in GAAP in the USA in this matter.

Furthermore, in situations that involve uncertainty in income taxes, banking corporations implement the rules set forth in clarification FIN48 regarding uncertainty in taxes on income, as long as these do not conflict with the International Financial Reporting Standards, via establishment of policies, procedures and application of requirements for documentation of all matters related to tax positions in varying degrees of uncertainty.

The bank retroactively implemented the regulations set forth in the standard beginning on January 1, 2012. The first-time adoption had no effect on the Bank's statements.

IAS 23 – Credit costs;

The standard determines that a company is to capitalize credit costs that refer directly to the acquisition and establishment or creation of a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale, and includes fixed assets, real estate for investment, and inventory required for a prolonged period of time in order to bring it to a state ready for sale. Nevertheless, it should be emphasized that for the banking corporation it will not constitute credit costs, without determining policies, procedures and clear controls concerning the recognition criteria in assets as qualifying assets, and concerning capitalized credit costs.

The first-time adoption had no effect on the Bank's statements.

IAS 24 – Related Party Disclosures

The standard establishes the disclosure requirements that the entity must provide regarding its relationship with a related party, as well as transactions and balances that have yet to be paid with the related party. In addition, disclosure on compensation to key management personnel is required. Key management personnel are defined as individuals who have the authority and responsibility to plan the entity's activities, to orient and control it directly or indirectly, including any director of this entity. The amendment to IAS 24 (hereinafter: the "amendment") clarifies the definition of a related party in order to simplify the recognition of connections with

Note 2 – Accounting policy (continuation)

a related party and to prevent lack of consistency in implementing this definition. Additionally, as part of the amendment, companies connected to the government are provided partial relief in providing disclosure concerning transactions with government and with other companies as aforementioned. As part of the adoption of the standard by the Supervisor of Banks, the format for the required disclosure in the financial statements were adjusted in order to comply with the disclosure requirements of IAS 24 and the disclosures required by virtue of the Securities Regulations 5770-2010. A banking corporation will be required to implement the generally accepted accounting principles of banks in the U.S in this matter. In case, as aforementioned, no reference is found, the banking corporation will be required to implement the regulations that were set forth in Standard 23, and in particular for transactions providing loans or recruitment of deposits between companies within the banking group.

The first-time adoption had no material effect on the Bank's statements. Disclosures were added when necessary.

3. **The Supervisor of Banks' instructions on actions between a banking corporation and controlling shareholder, and between a company controlled by the banking corporation.**

In December 2006, the Israeli Institute published accounting Standard Number 23 concerning "Accounting Treatment for Transactions Between an Entity and its Controlling Shareholder" (hereinafter. "Standard 23"). According to Standard 23, assets and liabilities for which a transaction is performed between the entity and the controlling shareholder will be measured on the transaction date according to the transaction's fair value, while the provision between fair value and the exchange will be imputed to equity. The difference in liability is in essence the dividend and therefore it will be recognized as a reduction in the surplus balance. The difference in credit is in fact the investment of owners and therefore it will be presented in a separate section in equity called capital reserve from a transaction between an entity and a controlling shareholder. The standard discusses three issues pertaining to transactions between an entity and its controlling shareholder, as follows:

- Transfer of an asset to an entity from the controlling shareholder or, alternatively, transfer of an asset from the entity to the controlling shareholder.

- Assumption of the entity's liability of a third party, in full or in part, by the controlling shareholder; indemnity of the entity by the controlling shareholder for an expense; waiver by the controlling shareholder of all or part of a debt owed to it by the entity.

- Loans granted to the controlling shareholder or loans received from the controlling shareholder.

In addition, the Standard sets forth the disclosure that must be provided in the financial statements regarding transactions between the entity and its controlling shareholder. Therefore, the treatment instructions as determined in Public Reporting Instructions on the issue of transactions with controlling shareholders or with a company controlled by a banking corporation were canceled. Nevertheless, the guideline concerning continuous agreement with a different consideration was left intact.

4. **Update of the disclosure instructions on credit quality of debts and provision for credit losses (Hereinafter: "The Instruction")**

- On March 25, 2012, the Supervisor of Banks published an instruction regarding an update of disclosure of credit quality of debts and a provision for credit losses based on the 10-2010 update of the FASB for disclosure requirements in the United States regarding credit quality of debts and for the provision for credit quality losses. The instructions in this matter are based on disclosure requirements of the FASB (Article 310-10 in the Codification), the disclosure requirement that exists in call report and the disclosure actually provided by banks in the USA. In light of the aforementioned, the instructions for reporting to the public were updated and the phrases "Credit Sector", "Groups of Debts", and "Indication for Credit Quality" were defined.

The requirements expand the quantitative and qualitative disclosure for every Group of Debts as defined in the instruction, on quality of its debts to the banking corporation, including:

- Description of the indication for credit quality.
- The registered balance due of debts, in accordance with the indication for credit quality.
- For every indication for credit quality, the date or range of dates on which the information was updated regarding this indication.
- Movement in the Provision for Credit Losses.

Acquisitions and sales of debt and quality of the credit portfolio. Inter alia, the banking corporation will provide quantitative and qualitative disclosure for every Group of Debts as defined in the circular, on the quality of its debts to the banking corporation, including:

a. Description of the indication for credit quality.

b. The registered balance due of the debts, in accordance with the indication for credit quality.

c. For every indication for credit quality, the date or range of dates on which the information was updated regarding this indication.

The instruction went into effect from the 2012 statement. It is hereby clarified that the 2012 report to the public will include balance sheet disclosures only. Beginning from the public report dated March 31, 2013 and onwards, every disclosure required in accordance with this instruction will be provided.

AA. New accounting standards and instructions of the Supervisor of Banks prior to their implementation:

1. In May 2011 the IASB published three new standards:

- IFRS 10 Consolidated Financial Statements
- IFRS 11 Joint Arrangements
- IFRS 12 Disclosure of Interests in Other Entities

The new amendments will be retrospectively applied as of the Financial Statements for annual periods starting January 1, 2013, or later. The standards included transition instructions with certain reliefs during first time application.

Below are the principles of the aforementioned standards:

IFRS 10 – Consolidated Financial Statements

According to IFRS 10 (Hereinafter: Standard 10), in order to establish control, the existence of power is required and exposure or rights to variable returns from the invested bank. Power is the ability to influence and direct the activities of the invested bank, that significantly affect the investor's yield. Standard 10 determines that during the examination of the existence of control, potential voting rights should only be considered if they are veritable.

In addition, Standard 10 determines that the investor can control even if he holds less than the majority of the voting rights in the held company (effective control), and this in contradiction with the existing IAS 27 that allowed a choice between two models for consolidation – the effective control model and the legal control model.

Standard 10 will be applied retrospectively beginning from the Financial Statements for annual periods from January 1, 2013, or later.

By the Bank's assessment, Standard 10 is not expected to materially affect the Financial Statements.

IFRS 11 – Joint Arrangements

IFRS 11 (Hereinafter - Standard 11) replaces IAS 31 concerning the accounting process of rights in joint transactions and SIC 13 regarding interpretation of accounting process in "non-financial" investments by entities in joint control.

Standard 11 defines joint arrangements as contractual arrangements according to which two parties or more have joint control.

Standard 11 divides the mutual settlements into two types:

- Joint transactions (joint ventures), in which the parties to the arrangement have joint control of the rights in net assets of the joint transaction and that will be treated only in accordance with the book value method.

- Joint activities (joint operations), in which the parties to the arrangement have joint control over the rights to the assets of the joint operations and joint obligations for the liabilities of the joint operations, and therefore will be consolidated in the financial statements based on their relative share in this operation as to be determined in the joint arrangement, similar to the currently existing accounting treatment.

Standard 11 will be applied retrospectively beginning with the Financial Statements for annual periods from January 1, 2013, or later. Early adoption is possible subject to disclosure having been given, as well as subject to early adoption of two other standards that were published at the same time - IFRS 10 Consolidated Financial Statements and IFRS 12 Disclosure of Interests in Other Entities.

The Bank's results are not expected to be materially affected by adoption of this Standard.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 (hereinafter - Standard 12) determines the disclosure requirement concerning the Bank's held entities, including subsidiaries, joint arrangements, consolidated companies and structured entities) Standard 12 expands the disclosure requirement concerning considerations and guidelines used by the management in determining the existence of control, joint control or significant influence in held entities, as well as determining the type of joint arrangement. Standard 12 also included disclosure requirements concerning material held entities.

The purpose of the new disclosure requirements is to allow users of the financial statements to understand the nature and risks resulting from the reporting corporation's interests in other entities, as well as to understand the affect of said interest on the reporting corporation's financial status. This purpose is reflected in the expanded and comprehensive disclosure requirements, inter alia: discretion and significant discounts that are reflected in determination of the nature of the entities and in the arrangements, rights in subsidiaries, rights in joint arrangements and in associated companies as well as rights in structured entities.

The suitable disclosures will be included in the Financial Statements of the Bank with the standard's first time adoption on January 1, 2013, or later.

By the Bank's assessment, the adaption of the new International Accounting Reporting Standard will probably not materially affect the Financial Statements.

2. In May 2011, the IASB published an amendment to two existing standards:

   - IAS 27R (amended 2011) – Separate Financial Statements

   - IAS 28R (amended 2011) – Investments in Associates and Joint Transactions.

   IAS 27R – Separate Financial Statements

   IAS 27R replaces IAS 27 and deals only with separate financial statements.

   The existing guidelines concerning separate financial statements remained without changes as part of of the amended Standard 27.

   IAS 28R – Investments in Associates and Joint Transactions

   IAS 28R (hereinafter: amended Standard 28) replaces IAS 28. The main changes included in it, compared to IAS 28, refer to accounting treatment according to the equity method in investments of joint transactions, as a result of publication of IFRS 11 and the transition from implementation of relative consolidation method to equity method in these investments.

Amended Standard 28 will be applied retrospectively beginning from the Financial Statements for annual periods from January 1, 2013, or afterwards. Early adoption is possible. However, if the company chooses to implement , it must adopt IFRS 10, IFRS 11, IFRS 12, and IAS 27R (amended 2011) as a single totality.

By the Bank's assessment, Amended Standards 27 and 28 are not expected to materially affect the Financial Statements.

3. Supervisor of Banks' instructions concerning the Profit and Loss Statement format for a banking corporation, and adoption of GAAP by banks in the USA for measurement of interest:

   Adoption of ASC 310-20 concerning "Non-refundable Fees and Other Costs":

   On December 29, 2011, the Supervisor of Banks published a circular aimed at adjusting the instructions for reporting to the public for the purpose of adopting the rules set forth as part of the accepted accounting standards in the US regarding non-refundable fees and other costs.

   The instructions set forth rules for treating fees from the creation of loans and direct costs in creating of loans. The qualifying fees and costs in accordance with the criteria set forth in the instruction will not be immediately recognized in the Profit and Loss Statement but will be taken into account in calculating the loan's effective interest rate.

   In addition, the instruction changes the treatment of the fees and costs related to the credit allocation liabilities, including credit-card transactions. Furthermore, the instruction sets forth rules pertaining to the treatment of changes in the terms of the debt that do not constitute reorganization of the problematic debt, treatment of early repayment of the debts, as well as treatment of other credit provision transactions such as syndication transactions.

   The amendments related to adoption of the issue of measuring interest incomes will be implemented as of January 1, 2014, and henceforth.

   The banking corporation examines the expected affect of adopting the rules on financial statements. At this stage, it cannot assess its affect.

4. Disclosure on Deposits

   On January 13, 2013, the Bank of Israel published a circular regarding changes in the instructions on reporting to the public on disclosure of deposits.

The amendments to the instructions for reporting to the public were designed to adapt the requirement for disclosure of deposits to the standard disclosure requirements in financial statements of bank corporations in the USA.

The main changes in the instructions for reporting to the public:

- Definitions of phrases were added;
- Disclosure requirements (in activity sectors, and liquidity status) were added;
- Expansion of disclosure of public deposits Addition C for management review;
- A separate disclosure requirement was added for deposits recruited in Israel from deposits recruited overseas, subject to its materialness, in notes on public deposits, deposits from banks and deposits from the government;
- In the Note on Public Deposits: A separate disclosure requirement was added on the balance of interest-bearing deposits, from the balance of non-interest bearing deposits. The disclosure requirement for deposits in savings plans and other deposits was canceled; a requirement for size-based reporting based on brackets was added; a requirement for reporting identity of depositors in Israel was added.
- In Note 17 "Assets and Liabilities based on Linkage-bases and period of payment": A disclosure requirement for contractual dates of payment of credit to the public and public deposits was added; the lines referring to dates of payment for non-cash items were deleted.

The instructions that were set forth in accordance with this contract will be implemented retrospectively beginning from the report to the public in 2013, and thereafter, with the exception of disclosure of balance of deposits from institutional entities that were included in the public deposits that were recruited in Israel, whose application will begin from the public report from March 31, 2013, and thereafter.

5. A draft of the update for directives on residential realty (Hereinafter: "The Draft")

On February 19, 2013, in light of the accelerated growth in the banking system in residential credit in recent years (a 76% increase over the past five years), parallel to an increase in housing prices, the Supervisor of Banks published a draft directive concerning residential credit and realty, on the allocation of capital and provision for doubtful debts for housing loans and change in the risk weight of guarantee in accordance with the Sales Law.

Listed below are the main guidelines that were included in the new Draft:

A. In order to calculate the capital adequacy ratios, the housing loan is weighted at 35%, with the exception of a leverage housing loan that includes a variable interest component, that since October 2010 has been weighted at 100%. In accordance with the new Draft directive, capital for housing loans will be allocated based on the following weighted rates:

   - Housing loans in which the financing rate is up to 45% will be weighted at 35% – remains unchanged.

   - Housing loans whose financing rate is higher than 45% and up to 60%, will be weighted at 50% instead of 35%.

   - Housing loans whose financing rate is higher than 60% will be weighted at 75% for capital requirement purposes instead of 35% or at 100% (see the following point).

   - Simultaneously, the requirement (from October 2010) to weight 100% loans whose financing rate exceeds 60% and a sum that exceeds NIS 800 thoudsand and whose variable interest rate exceeds 25%, will be canceled and will be replaced, as previously mentioned, by a weighted rate of 75%.

B. The Draft directives set forth a requirement to increase the provision for doubtful debts for housing loans – so that the ratio between the balance of the group provision and the balance of the housing loan will be at a minimal rate of 0.35%. On average, at the end of third quarter of 2012, this ratio stood at 0.22%.

C. In addition, the Draft directives establish a reduction in the allocation of capital required for Sales Law guarantees in the event that the apartment had already been delivered to the tenant. These guarantees will be weighted with a conversion coefficient for credit of 10% instead of 20%. This move constitutes a relief in the capital allocation requirements and may increase the supply of bank credit in the construction and real estate industry.

The purpose of the directives is to increase the capital cushions and provision required for increased risks embodied in the housing credit portfolio. At the same time, the move eases the capital requirements for the Sales Law guarantees after delivery of the apartment to the tenant, due to a relatively low level of risk they entail.

The new directives will take effect beginning on January 1, 2013. The immediate affect will be increased provision for credit losses for debts that were reviewed on a group basis of NIS 17-20 million gross before tax (a 0.2% decrease in the Tier 1 capital ratio (for risk components). In relation to the long-term affect, the bank is examining the affect of the instruction on the housing credit component, as well as on its future profitability.

6. Instruction for Statement of Comprehensive Profit

On December 9, 2012, a circular was published concerning the Statement of Comprehensive Profit The purpose of the circular is to adapt the manner of presentation of the Statement of Comprehensive Profit to the GAAP in the USA. The circular changes the manner of presentation of the items in Comprehensive Profit in Financial Statements so that the items of other comprehensive profit will be reported separately in a "Statement of Comprehensive Profit" that will be presented after the Profit and Loss Statement.

In addition, an itemization of the composition and movement of other accrued comprehensive profit will be presented in a new note on Other Accrued Comprehensive Profit.

The amendments in this instruction will apply to first quarter reports of 2013 and later, and will be adopted retrospectively.

The first-time adoption is not expected to materially affect the financial statements other than a representative change.

Note 3 – Cash and bank deposits

Reported amounts in millions of New Shekels

	consolidated		The Bank	
	December 31			
	2012	2011	2012	2011
Cash and Deposits in the Bank of Israel	**1,030.6**	206.0	**1,030.5**	206.0
Cash and deposits in commercial banks	**330.0**	586.3	**329.4**	585.8
Total cash and deposits in banks	**1,360.6**	792.3	**1,359.9**	791.8
From this: cash, deposits at banks and deposits in the Bank of Israel For an original period of up to 3 months	**1,360.6**	792.3	**1,359.9**	791.8

Note 4 – Securities – consolidated

Reported amounts in millions of New Shekels

	December 31, 2012				
			Other Comprehensive Profit (Loss) after accumulation		
	The value In the Balance Sheet	Amortized cost (in shares – cost)	Profits	Losses	Fair value(1)
Available for Sale Securities – Debentures					
of the Israeli government	786.2	784.5	3.4	1.7	786.2
of financial institutes in Israel	10.0	10.0	-	-	10.0
of others in Israel	3.0	2.8	0.2	-	3.0
Total debentures	799.2	797.3	3.6	1.7	799.2
Shares	1.1	1.1	-	-	1.1 (2)
Total available for sale securities	**800.3**	**798.4**	**3.6** (3)	**1.7** (3)	**800.3** (2)

	December 31, 2012				
	The value In the Balance Sheet	Amortized cost (in shares – cost)	Profits that have not yet been realized from fair value reconciliations	Losses that have not yet been realized from fair value reconciliations	Fair value(1)
Negotiable securities – Debentures					
of the Israeli government	354.0	345.1	8.9	-	354.0
of financial institutes in Israel	6.6	6.6	-	-	6.6
of others in Israel	2.1	2.2	-	0.1	2.1
Total debentures	362.7	353.9	8.9	0.1	362.7
Total negotiable securities	362.7	353.9	8.9 (4)	0.1 (4)	362.7
Total securities	**1,163.0**	**1,152.3**	**12.5**	**1.8**	**1,163.0**

(1) Fair value data is generally based on stock exchange rates that are not necessarily reflected in the prices obtained from sale of securities on a large scale.

(2) Including shares for which fair value is not available, presented according to cost, for a total of NIS 0.1 million.

(3) Included in equity in section "Reconciliations for presentation for available for sale securities according to fair value".

(4) Reflected in Profit and Loss Statement.

Details of activity results in debentures investments, see Notes 23-24.

Note 4 – Securities (continuation) – consolidated

Reported amounts in millions of New Shekels

	December 31, 2011				
			Other Comprehensive Profit (Loss) after accumulation		
	The value in the Balance Sheet	Amortized cost (in shares – cost)	Profits	Losses	Fair value(1)
Available for Sale Securities –					
Debentures					
of the Israeli government	1,011.8	1,023.7	3.3	15.2	1,011.8
of financial institutes in Israel	115.1	115.3	0.5	0.7	115.1
Asset-backed (ABS) in Israel	13.7	17.7	-	4.0	13.7
of others in Israel	78.6	79.9	0.2	1.5	78.6
Total debentures	1,219.2	1,236.6	4.0	21.4	1,219.2
Shares	1.1	1.1	-	-	1.1
Total available for sale securities	**1,220.3**	**1,237.7**	**4.0** (3)	**21.4** (3)	**1,220.3** (2)

	December 31, 2011				
	The value in the Balance Sheet	Amortized cost (in shares – cost)	Profits that have not yet been realized from fair value reconciliations	Losses that have not yet been realized from fair value reconciliations	Fair value(1)
Negotiable securities –					
Debentures					
of the Israeli government	232.5	229.1	3.4	-	232.5
of financial institutes in Israel	5.0	5.0	-	-	5.0
of others in Israel	7.5	7.9	-	0.4	7.5
of other foreigners	25.4	26.6	-	1.2	25.4
Total debentures	270.4	268.6	3.4	1.6	270.4
Total negotiable securities	270.4	268.6	3.4 (4)	1.6 (4)	270.4
Total securities	**1,490.7**	**1,506.3**	**7.4**	**23.0**	**1,490.7**

(1) Fair value data is generally based on stock exchange rates that are not necessarily reflected in the prices obtained from sale of securities on a large scale.

(2) Including shares for which fair value is not available, presented according to cost, for a total of NIS 0.1 million.

(3) Included in equity in section "Reconciliations for presentation for available for sale securities according to fair value".

(4) Reflected in Profit and Loss Statement.

Details of activity results in debentures investments, see Notes 23-24.

Note 4 – Securities (continuation) – the Bank

Reported amounts in millions of New Shekels

	December 31, 2012				
	The value In the Balance Sheet	Amortized cost (in shares – cost)	Other Comprehensive Profit (Loss) after accumulation		Fair value[1]
			Profits	Losses	
Available for Sale Securities –					
Debentures					
of the Israeli government	587.0	585.5	3.2	1.7	587.0
of financial institutions in Israel [5]	232.9	232.9	-	-	232.9
Asset-backed (ABS) in Israel	-	-	-	-	-
of others in Israel	3.0	2.8	0.2	-	3.0
Total debentures	822.9	821.2	3.4	1.7	822.9
Shares	1.1	1.1	-	-	1.1 [2]
Total available for sale securities	**824.0**	**822.3**	**3.4** [3]	**1.7** [3]	**824.0** [2]

	December 31, 2012				
	The value In the Balance Sheet	Amortized cost (in shares – cost)	Profits that have not yet been realized from fair value reconciliations	Losses that have not yet been realized from fair value reconciliations	Fair value[1]
Negotiable securities –					
Debentures					
of the Israeli government	352.0	343.1	8.9	-	352.0
of financial institutes in Israel	6.6	6.6	-	-	6.6
of others in Israel	2.1	2.1	-	-	2.1
of other foreigners	-	-	-	-	-
Total debentures	360.7	351.8	8.9 [4]	- [4]	360.7
Total negotiable securities	360.7	351.8	8.9 [4]	- [4]	360.7
Total securities	**1,184.7**	**1,174.1**	**12.3**	**1.7**	**1,184.7** [2]

(1) Fair value data is generally based on stock exchange rates that are not necessarily reflected in the prices obtained from sale of securities on a large scale.

(2) Including shares for which fair value is not available, presented according to cost, for a total of NIS 0.1 million.

(3) Included in equity in section "Reconciliations for presentation for available for sale securities according to fair value".

(4) Reflected in Profit and Loss Statement.

(5) From this balance sheet value for the total of NIS 222.9 million (NSS 260.7 million in 2011) for debentures of consolidated companies.

Details of activity results in debentures investments, see Notes 23-24.

Note 4 – Securities (continuation) – the Bank

Reported amounts in millions of New Shekels

	December 31, 2011				
	The value In the Balance Sheet	Amortized cost (in shares – cost)	Profits that have not yet been realized from fair value reconciliations	Losses that have not yet been realized from fair value reconciliations	Fair value[1]
Available for Sale Securities –					
Debentures					
of the Israeli government	865.6	876.2	3.3	13.9	865.6
of financial institutions in Israel [5]	347.2	347.7	0.3	0.8	347.2
Asset-backed (ABS) in Israel	13.7	17.7	-	4.0	13.7
of others in Israel	78.5	79.8	0.2	1.5	78.5
Total debentures	1,305.0	1,321.4	3.8	20.2	1,305.0
Shares	1.1	1.1	-	-	1.1
Total available for sale securities	**1,306.1**	**1,322.5**	**3.8** [3]	**20.2** [3]	**1,306.1** [2]

	December 31, 2011				
	The value In the Balance Sheet	Amortized cost (in shares – cost)	Profits that have not yet been realized from fair value reconciliations	Losses that have not yet been realized from fair value reconciliations	Fair value[1]
Negotiable securities –					
of the Israeli government	229.0	225.6	3.4	-	229.0
of financial institutes in Israel	5.0	5.0	-	-	5.0
of others in Israel	7.5	7.9	-	0.4	7.5
of other foreigners	25.4	26.6	-	1.2	25.4
Total debentures	266.9	265.1	3.4	1.6	266.9
Total negotiable securities	266.9	265.1	3.4 [4]	1.6 [4]	266.9
Total securities	**1,573.0**	**1,587.6**	**7.2**	**21.8**	**1,573.0**

(1) Fair value data is generally based on stock exchange rates that are not necessarily reflected in the prices obtained from sale of securities on a large scale.

(2) Including shares for which fair value is not available, presented according to cost, for a total of NIS 0.1 million.

(3) Included in equity in section "Reconciliations for presentation for available for sale securities according to fair value".

(4) Reflected in Profit and Loss Statement.

(5) From this balance sheet value for the total of NIS 260.7 million (NSS 144.1 million in 2010) for debentures of consolidated companies.

Details of activity results in debentures investments, see Notes 23-24.

Note 5 – Credit risk, credit for the public and credit loss provision on a consolidated basis

Reported amounts in millions of New Shekels

a. debts* and off-balance sheets credit instruments

Provision for Credit Losses:

	2012					
	Provision for Credit Losses					
	Credit for the public					
	Commercial	For Housing	Other details	Total	Banks and governments	Total
1. Movement in balance of provisions for credit losses						
Balance of provision for credit losses for the start of the year	8.9	69.9	13.9	92.7	-	92.7
Expenses for Credit Losses	3.3	(1.8)	34.5	36.0	- ***	36.0
Write-offs	(3.2)	(7.6)	(28.8)	(39.6)	-	(39.6)
Collection of write-off debts from previous years	0.6	-	2.9	3.5	-	3.5
Net write-offs	(2.6)	(7.6)	25.9)	(36.1)	-	(36.1)
Other	-	-	-	-	-	-
Balance of provision for credit losses for the end of the year (1)	9.6	60.5	22.5	92.6	- ***	92.6
(1)Of this: because of off-balance-sheets credit instruments	1.7	-	0.2	1.9	-	1.9
2. Additional information on the method for calculating the provision for credit losses for debts* and for debts* for which it was calculated:						
Recorded balance of debts due*:						
Examined on individual basis	1,190.6	-	374.8	1,565.4	-	1,565.4
that were examined on group basis (2)	534.6	6,882.7	689.4	8,106.7	388.7	8,495.4
(2)For which the provision was not calculated according to the depth of the arrears	-	280.1	-	280.1	-	280.1
Total debts *	1,725.2	6,882.7	1,064.2	9,672.1	388.7	10,060.8
Provision for Credit Losses for Debts*						
Examined on individual basis	7.2	-	1.8	9.0	-	9.0
that were examined on group basis (3)	0.7	60.5	20.5	81.7	- ***	81.7
(3)Of this: For which the provision was calculated according to the depth of the arrears	-	53.1 **	-	53.1	-	53.1
Total Provision for Credit Losses	7.9	60.5	22.3	90.7	- ***	90.7

* Credit for the public, credit for the government, deposits in banks and other debts, with the exception of debentures and securities that were borrowed or purchased as part of the return purchase agreements.

** Including balances of provisions that were calculated on a group basis for a sum of NIS 7.4 million.

*** Balance less than NIS 0.1 million.

Note 5 – Credit risk, credit for the public, and credit loss provision on a consolidated basis (continuation)

Reported amounts in millions of New Shekels

a. debts* and off-balance sheets credit instruments

Provision for Credit Losses:

	2011					
	Provision for Credit Losses					
	Credit for the public					
	Commercial	For Housing	Other details	Total	Banks and governments	Total
1. Movement in balance of provisions for credit losses						
Balance of provision for credit losses for the start of the year	41.8	70.8	10.2	122.8	-	122.8
Recognized net write-offs as of January 1, 2011	(26.4)	(7.4)	(8.2)	(42.0)	-	(42.0)
Other changes in credit loss provision as of January 1, 2011 (reflected in equity)	(2.4)	13.6	4.9	16.1	-	16.1
Expenses for Credit Losses	(1.3)	1.2	15.2	15.1	-	15.1
Write-offs	(3.9)	(9.1)	(10.3)	(23.3)	-	(23.3)
Collection of write-off debts from previous years	1.1	0.8	2.1	4.0	-	4.0
Net write-offs	(2.8)	(8.3)	(8.2)	(19.3)	-	(19.3)
Other	-	-	-	-	-	-
Balance of provision for credit losses for the end of the year (1)	8.9	69.9	13.9	92.7	-	92.7
(1)Of this: because of off-balance-sheets credit instruments	1.4		0.3	1.7	-	1.7
2. Additional information on method for calculating provision for credit losses for debts* and for debts *for which it was calculated:						
Recorded balance of debts due*:						
Examined on individual basis	1,314.7	-	318.6	1,633.3	-	1,633.3
Examined on group basis (2)	295.8	6,627.9	591.8	7,515.5	-	7,515.5
(2)For which the provision was not calculated according to the depth of the arrears	-	6,516.3	-	6,516.3	-	6,516.3
Total debts *	1,610.5	6,627.9	910.4	9,148.8	-	9,148.8
Provision for Credit Losses for Debts*						
Examined on individual basis	6.5	-	0.8	7.3	-	7.3
that were examined on group basis (3)	0.7	69.9	13.1	83.7	-	83.7
(3)Of this: For which the provision was calculated according to the depth of the arrears		61.8 **	-	61.8	-	61.8
Total Provision for Credit Losses	7.2	69.9	13.9	91.0	-	91.0

* Credit for the public, credit for the government, deposits in banks and other debts, with the exception of debentures and securities that were borrowed or purchased as part of return purchase agreements.

** Including balances of provisions beyond what is obligated in accordance with the depth arrear method that was calculated on an individual basis for a sum of NIS 0 million and was calculated on a group basis for a sum of NIS 8.2 million.

Note 5 – Credit risk, credit for the public and credit loss provision on a consolidated basis (continuation)

Reported amounts in millions of New Shekels

b. Debts (1)

	December 31, 2012					
1. Credit quality and arrears		**problematic** (2)			**Non-defective debts – additional information**	
Borrower Activity in Israel Commercial Public	**non-problematic**	**Non-defective**	**Defective**	**Total**	**In arrears of 90 or more days**(4)	**In arrears of 30 to 89 days** (5)
Construction and real estate – Construction	1,099.5	10.3	57.2	1,167.0	5.2	0.7
Construction and real estate – real estate activity	357.6	6.5	13.0	377.1	3.4	-
Financial services	38.0	-	-	38.0	-	-
Commerce – other	137.3	1.0	4.8	143.1	0.3	0.9
Total commerce	**1632.4**	**17.8**	**75.0**	**1,725.2**	**8.9**	**1.6**
Individuals – Housing Loans	**6,621.1**	**261.6** (6)	**-**	**6,882.7**	**261.6**	**62.7**
Individuals – other	**1,034.5**	**26.6**	**3.1**	**1,064.2**	**9.8**	**17.7**
Total Public – Activity in Israel	**9,288.0**	**306.0**	**78.1**	**9,672.1**	**280.3**	**82.0**
Banks in Israel	**141.8**	**-**	**-**	**141.8**	**-**	**-**
The Israeli Government	**223.8**	**-**	**-**	**223.8**	**-**	**-**
Total Activity in Israel	**9,653.6**	**306.0**	**78.1**	**10,037.7**	**280.3**	**82.0**
Banks abroad	**23.1**	**-**	**-**	**23.1**	**-**	**-**
Total	**9,676.7**	**306.0**	**78.1**	**10,060.8**	**280.3**	**82.0**

	December 31, 2011				
				Non-defective debts – additional information	
	Non-defective	**Defective** (3)	**Total**	**In arrears of 90 or more days**(4)	**In arrears of 30 to 89 days** (5)
Credit for the public examined on individual basis	1,597.7	35.6	**1,633.3**	40.3	16.5
Housing loans according to arrears depth	6,516.3	-	**6,516.3**	250.2	63.3
that was examined on another group basis	999.2	-	**999.2**	20.1	25.3
Total public	9,113.2	35.6	**9,148.8**	310.6	105.1
Total banks	-	-	**-**	-	-
Total governments	-	-	**-**	-	-
Total	**9,113.2**	**35.6**	**9,148.8**	**310.6**	**105.1**

1 Credit for the public, credit for the government, deposits in banks and other debts, with the exception of debentures and securities that were borrowed or purchased as part of the return purchase agreements.

2 Credit risk that is defective, inferior or under special supervision, including for housing loans for which there is a provision based on the arrears depth, and housing loans for which there is no provision based on the arrears depth in arrears by 90 or more days.

3 In general, defective debts do not accrue interest income. For information about certain defective debts that were reorganized, in the reorganization of problematic debts, see Note 5.b.2.c. below

4 Classified as problematic debts that are not defective, accumulate interest income.

5 Accumulate Interest Income. Debts in arrear between 30 and up to 89 days, totaling NIS 9.3 million, were classified as problematic debts that are not defective.

6 Including balance of the housing loan of NIS 102.3 million with a provision based on the arrears depth, for which a settlement was signed for the return of arrears from the borrower, when a change in clearance schedule is made for the remaining loan that has not yet reached maturity.

Note 5 – Credit risk, credit for the public and credit loss provision on a consolidated basis (continuation)

Reported amounts in millions of New Shekels

b. debts *

	December 31, 2012				
2. Additional information on defective debts A. of defective debts and individual provision Borrower Activity in Israel	balance** of debts defective for which there is a provision individual***	Balance of provision individual***	balance** of debts defective for which there are no individual provisions***	Total Balance** of defective debts	Balance of fund Contractual of of defective debts
Commercial Public					
Construction and real estate – Construction	29.5	2.5	27.7	57.2	65.5
Construction and real estate – real estate activity	-	-	13.0	13.0	14
Financial services	-	-	-	-	-
Commerce – other	3.0	0.3	1.8	4.8	4.8
Total commerce	**32.5**	**2.8**	**42.5**	**75.0**	**84.3**
Individuals – Housing Loans	-	-	-	-	-
Individuals – other	**3.1**	**0.7**	-	**3.1**	**7.5**
Total Public – Activity in Israel	**35.6**	**3.5**	**42.5**	**78.1**	**91.8**
Banks in Israel	-	-	-	-	-
The Israeli Government	-	-	-	-	-
Total Activity in Israel	**35.6**	**3.5**	**42.5**	**78.1**	**91.8**
Banks abroad	-	-	-	-	-
Total (1)	**35.6**	**3.5**	**42.5**	**78.1**	**91.8**
1) Of this:					
Measured according to present value of cash flows	35.6	3.5	25.3	60.9	70.3
Debts with reorganization of problematic debts	35.6	3.5	10.9	46.5	55.8

	December 31, 2011				
Total public	3.7	3.7	31.9	35.6	56.6
Total banks	-	-	-	-	-
Total governments	-	-	-	-	-
Total (2)	3.7	3.7	31.9	35.6	56.6
2) Of this:					
Measured according to present value of cash flows	3.7	3.7	25.1	28.8	48.8
Debts with reorganization of problematic debts	3.7	3.7	3.1	6.8	23.2

* Credit for the public, credit for the government, deposits banks and other debts, with the exception of debentures and securities that were borrowed or purchased as part of the return purchase agreements.

** Recorded debt balance due.

*** Individual provision for credit losses.

Note 5 – Credit risk, credit for the public and credit loss provision on a consolidated basis (continuation)

Reported amounts in millions of New Shekels

b. Debts *

2. Additional information on impaired debts **B. Average Balance and Income from Interest**	**2012**	**2012**
Recorded average debt balance due from defective credit for the public in reporting periods	54.4	30.8
Total income from interest that was recorded in the reporting period for this credit in the time period in which it was classified was defective*	0.2	0.7
Total income from interest that was recorded in the reporting period for which this debt accumulates interest according to the original conditions	3.1	1.8
*Of this: Income from interest that was recorded on a cash basis accounting method	0.2	0.7

2. Additional information on defective debts	**December 31, 2012**				
	Recorded debt balance due.				
C. Problematic debts in reorganization **Borrower Activity in Israel**	**that does not accumulate income from Interest**	**Accruals** in arrears of 90 or more days**	**Accruals** in arrears of between 30 and up 89 days**	**Accruals** not in arrears**	**Total*****
Commercial Public					
Construction and real estate – Construction	29.5	-	-	7.8	37.3
Construction and real estate – real estate activity	3.1	-	-	-	3.1
Financial services	-	-	-	-	-
Commerce – other	3.0	-	-	-	3.0
Total commerce	**35.6**	**-**	**-**	**7.8**	**43.4**
Individuals – Housing Loans	**-**	**-**	**-**	**-**	**-**
Individuals – other	**3.1**	**-**	**-**	**-**	**3.1**
Total Public – Activity in Israel	**38.7**	**-**	**-**	**7.8**	**46.5**
Banks in Israel	**-**	**-**	**-**	**-**	**-**
The Israeli Government	**-**	**-**	**-**	**-**	**-**
Total Activity in Israel	**38.7**	**-**	**-**	**7.8**	**46.5**
Banks abroad	**-**	**-**	**-**	**-**	**-**
Total	**38.7**	**-**	**-**	**7.8**	**46.5**
	December 31, 2011				
Total public	35.6	-	-	-	35.6
Total banks	-	-	-	-	-
Total governments	-	-	-	-	-
Total	35.6	-	-	-	35.6

* Credit for the public, credit for the government, deposits banks and other debts, with the exception of debentures and securities that were borrowed or purchased as part of the return purchase agreements.

** Accumulated interest income

*** Included in defective debts

Note 5 – Credit for the public and credit loss provision on a consolidated basis (continuation)

Reported amounts in millions of New Shekels

b. Debts *

3. Additional information on housing loans

Balance for the end of the year based on the financing rate (LTV)*, type of reimbursement, and type of interest.

		December 31, 2012			
		Balance of Housing Loans			Credit risk
		Total*	Of this: bullet and balloon*	Of this: Variable Interest *	Off-Balance sheet Total
First lien: Financing rate	up to 60%	5,332.7	123.6	4,352.0	638.6
	Over 60%	1,662.2	20.1	1,483.2	56.9
Secondary lien or no lien		45.6	0.9	20.9	4.5
Total		**7,040.5 ** **	**144.6**	**5,856.1**	**700.0**
					31.12.2011
Total		**6,791.7 ** **	**105.8**	**5,520.8**	**359.5**

* The ratio between the approved credit line during the granting of the credit line and the value of the asset, as approved by the bank when providing the credit line.

** Including housing loans provided to certain acquisition groups that are under construction, for a total of NIS 157.8 million in 2012, and NIS 168 million in 2011.

c. Credit for the public and off-balance-sheets credit risk according to the amount of the borrower's credit.

		December 31, 2012			December 31, 2011		
			Credit (2)	Off-balance-sheet credit risk (2) (3)		Credit (2)	Off-balance-sheet credit risk (2) (3)
Credit ceiling in thousands of New Shekels		Number of borrowers (1)	Millions of NIS		Number of borrowers (1)	Millions of NIS	
	Up to 10	**3,545**	**19.3**	**2.5**	3,120	14.0	3.7
Over 10	Up to 20	**5,554**	**79.7**	**9.9**	4,325	57.4	11.5
Over 20	Up to 40	**9,173**	**265.5**	**21.3**	7,882	228.3	21.0
Over 40	Up to 80	**8,375**	**435.2**	**32.4**	7,829	408.8	32.0
Over 80	Up to 150	**4,827**	**516.4**	**29.0**	5,497	578.7	32.0
Over 150	Up to 300	**5,032**	**1,058.8**	**53.6**	5,433	1,128.2	49.9
Over 300	Up to 600	**4,617**	**1,816.4**	**159.3**	4,327	1,738.9	99.1
Over 600	Up to 1,200	**2,244**	**1,673.5**	**170.4**	2,101	1,617.4	121.8
Over 1,200	Up to 2,000	**695**	**957.2**	**97.1**	635	889.2	77.5
Over 2,000	Up to 4,000	**385**	**880.4**	**169.5**	324	798.8	88.6
Over 4,000	Up to 8,000	**132**	**610.3**	**115.0**	114	500.6	106.0
Over 8,000	Up to 20,000	**78**	**677.5**	**254.0**	71	643.7	204.6
Over 20,000	Up to 40,000	**24**	**460.7**	**183.9**	26	461.1	239.5
Over 40,000	Up to 60,000	**7**	**221.2**	**164.6**	4	83.7	123.7
		44,688	**9,672.1**	**1,462.5**	41,688	9,148.8	1,210.9

(1) The number of borrowers according to the total credit and off-balance sheets credit risk.

(2) Off-balance-sheet credit and credit risk are presented according before the effect of the provision of credit losses and before the collateral effects permitted for deduction for the purpose of the liability of the borrower and for groups of borrowers.

(3) Credit risk in off-balance-sheet financial instruments as calculated for the purpose of the sole borrower's liability limitation.

Note 6 – Credit for the government (in consolidation and at the Bank)

Reported amounts in millions of New Shekels

	December 31	
	2012	**2011**
Credit as part of the interest completion settlement for the entitled of the Ministry of Construction and Housing	**1.4**	1.9
Deduction – in advance interest completion from the government	**(1.4)**	(1.9)
Total credit for the government	**-**	-

(1) According to the agreement between the government of Israel and the Bank, the government undertook to complete for the bank, due to certain housing loans that have been provided to those entitled for support according to the directives of the Ministry of Construction and Housing, the interest gap between the average low interest rate that was custom as the mortgage banks, according to an agreed formula, and between the actual interest rate on aforementioned loans. Completion of interest as mentioned in advance for the whole loan period capitalized according to the annual interest rate of 2%, as a deposit in favor of the Bank with the Accountant General, carrying interest at an identical rate.

Note 7 – Investment in held companies

Reported amounts in millions of New Shekels

a – Investment component

	consolidated		The Bank	
	December 31			
	2012	2011	2012	2011
Consolidated companies				
Investment in shares according to equity method	-	-	**364.7**	343.2
From this: Profits accumulated from acquisition date	-	-	**15.0**	31.3
Sections in which equity accumulated from the acquisition date				
Reconciliations for presentation of for available for sale securities according to fair value, net	-	-	**0.1**	(0.8)

b – The Bank's share in profits or losses of held companies

	consolidated			The Bank		
	2012	2011	2010	2012	2011	2010
The Bank's share of the profits from held companies	-	-	-	**18.6**	38.1	18.8
Provision for tax						
Current taxes	-	-	-	**3.3**	6.9	4.8
Deferred Taxes	-	-	-	**0.3**	(0.1)	(0.8)
Total provision for taxes	-	-	-	**3.6**	6.8	4.0
The Bank's share of profits from held companies after the tax affect	-	-	-	**15.0**	31.3	14.8

Note 7 – Investment in Held Companies (continuation)

Reported amounts in millions of New Shekels

c – Details on Held Companies

Company Name	Details on the Company	Share in capital that entitles the owner to receive profits and voting rights %	Investment in shares according to balance sheet value As at December 31		Contribution for net profit from regular activities On December 31	
			2012	**2011**	**2012**	**2011**
			Millions of NIS			
Tomer Jerusalem Ltd.	(1)	100	**157.4**	150.8	**6.6**	21.5
Ir Shalem Insurance Agency (1996) Ltd.	(2)	100	**148.0**	139.5	**7.7**	8.3
Jerusalem Investment Portfolio Management Ltd.	(3)	100	**34.7**	34.8	**(0.1)**	0.5
Jerusalem Capital Markets Funds Management (1980) Ltd.	(4)	100	**1.5**	1.5	**-**	-
Jerusalem Underwriting and Issuances Ltd.	(5)	100	**6.5**	6.5	**-**	-
The Trust Company of Bank of Jerusalem Ltd.	(6)	100	**0.4**	0.4	**-**	-
Jerusalem Financing and Issuances (2005) Ltd.	(7)	100	**16.2**	9.7	**0.8**	1.0
Jerusalem Financial Operations (2005) Ltd.	(8)	100	**-**	-	**-**	-

(1) The principle activity of Tomer Jerusalem Ltd. (hereinafter: "Tomer") is to serve as the Bank's asset company and to grant computer services to the Bank. For details concerning sales of management building, see Note 8.

(2) Ir Shalem Insurance Agency (1996) Ltd. operates as an insurance agent providing services in relation to asset insurance and life insurance for the Bank's borrowers.

(3) Jerusalem Investment Portfolio Management Ltd. deals with providing consultant services and management of investment portfolios. For sale of company activities, see Note 33.

(4) Jerusalem Capital Markets Funds Management (1980) Ltd., dealt in trust fund management. In 2006, the trust fund activity was sold.

(5) Jerusalem Underwriting and Issuances Ltd., dealt in the area of underwriting and issuances, the company decided to cease its activity as underwriter, and switched its underwriting status registry to "Not active".

(6) The Trust Company of Bank of Jerusalem Ltd., handles the trust accounts and financial assets of foreign residents and others.

(7) Jerusalem Finance and Issuances (2005) Ltd. (a subsidiary fully owned and controlled by the Bank), operates to recruit resources by way of issuing liability certificates and deferred liability notes for the public. In 2012, the company raised NIS 194 million by issuing liability certificates, and in 2011 – NIS 100 million. For details see Note 12b.

(8) Jerusalem Financial Operations (2005) Ltd., serves as an agent for performing activities in the debentures series offered to the public by Jerusalem Financing and Issuances (2005) Ltd.As of 2007, the company is not active.The Bank has begun the company's liquidation process.

d – Purchasing of liability certificates issued by the subsidiary (Jerusalem Financing and Issuances (2005) Ltd.)

As at the balance sheet date, the Bank holds liability certificates of the subsidiary, in nominal value for the total amount of NIS 226,493 million (from Series A, F, G, and H). Concerning series A – The Bank is entitled to receive interest according to the certificates, but may waive its right. Concerning series F, G and H, the Banks not entitled to receive interest.

In July 2012, the Bank sold to outsiders its holdings in Series B for a sum of NIS 79.5 million, n.v. In consideration for NIS 104.4 million.

Note 8 – Buildings and Equipment

Reported amounts in millions of New Shekels

	consolidated				Bank			
	Buildings and property (1)(3)(6)	Equipment, furniture and vehicles	Software Costs(4)(5)	Total	Buildings and land(1)	Equipment, furniture and vehicles	Software Costs	Total
Cost of assets(4) (2)								
Balance as at December 31, 2010	69.9	44.8	53.9	168.6	45.3	28.8	-	74.1
Additions	11.4	8.1	25.8	45.3	0.3	0.9	-	1.2
Derogation	19.7	5.2	5.1	30.0	-	-	-	-
Balance as of December 31, 2011	**61.6**	**47.7**	**74.6**	**183.9**	**45.6**	**29.7**	**-**	**75.3**
Additions	4.9	3.7	47.3	55.9	-	-	-	-
Derogation	0.6	2.7	-	3.3	-	-	-	-
Balance as at December 31, 2012	**65.9**	**48.7**	**121.9**	**236.5**	**45.6**	**29.7**	**-**	**75.3**
Depreciation and losses from impairment								
Balance as at December 31, 2010	39.4	32.8	39.7	111.9	28.0	23.1	-	51.1
Depreciation per year	2.6	3.7	6.7	13.0	1.3	1.1	-	2.4
Derogation	10.4	5.2	5.1	20.7	-	-	-	-
Balance as of December 31, 2011	**31.6**	**31.3**	**41.3**	**104.2**	**29.3**	**24.2**	**-**	**53.5**
Annual Depreciation	3.3	4.6	9.8	17.7	1.3	1.0	-	2.3
Derogation	0.6	2.7	-	3.3	-	-	-	-
Balance as at December 31, 2012	**34.3**	**33.2**	**51.1**	**118.6**	**30.6**	**25.2**	**-**	**55.8**
Amortization balance								
As at the Balance Sheet Date	**31.6**	**15.5**	**70.8**	**117.9**	**15.0**	**4.5**	**-**	**19.5**
At the beginning of the reporting year	30.0	16.4	33.3	79.7	16.3	5.5	-	21.8
Book value								
For 31st of December 2010	30.5	16.2	10.0	56.7	17.3	5.7	-	23.0
For December 31, 2011	30.0	16.4	33.3	79.7	16.3	5.5	-	21.8
For December 31, 2012	**31.6**	**15.5**	**70.8**	**117.9**	**15.0**	**4.5**	**-**	**19.5**
Average weighted depreciation rate in % as at December 31, 2012	8.72	18.15	24.82		5.78	8.93		
Average weighted depreciation rate in % as at December 31, 2011	7.70	15.05	26.04		5.87	8.61		

Reported amounts in millions of New Shekels (continuation)

(1) Including improvements in rented asset.

(2) Bank and subsidiaries owned property that cost NIS 77.2 million consolidated, and NIS 37.2 million at the Bank (2011 – NIS 66.5 million, and NIS 34.9 million respectively) fully amortized and is still in use.

(3) On April 14, 2011, Tomer Jerusalem Ltd. (the Bank's fully owned and controlled subsidiary) signed the sale agreement of the Bank's management building at 2 Herbert Samuel Street, Jerusalem for the exchange of a total of NIS 35 million plus VAT. The profit recognized in the financial statements for 2011 for the building's sale is NIS 20.8 million. As part of the sale, the subsidiary undertook to rent from the purchasers part of the area of the sold asset and to rent out the balance of the asset to third parties, according to a rental lease signed with the purchaser, in such a manner ensuring the purchaser fixed consideration for the asset at an agreed rate for a period of 10 years. On April 7, 2011, the management offices of the Bank moved from Jerusalem to Airport City.

(4) Including capitalized expenses for work wages and outsourcing for a total of NIS 11.2 million (2011 – NIS 7.4 million).

(5) Including costs for consumer materials and services related to software development.

(6) The Bank does not have rights that have not been registered with the Lands Registry Bureau.

Note 9 – Other assets

Reported amounts in millions of New Shekels

	consolidated		Bank	
	December 31			
	2012	2011	2012	2011
Deferred taxes for receivables, net (see note 29)*	**35.0**	23.2	**36.3**	25.0
Balance of issuances expenses for debentures and recruitment of long-term deposits**	**5.4**	6.7	**-**	0.1
Prepaid Expenses	**4.3**	4.4	**4.1**	4.1
Income from Receivables	**0.9**	0.9	**0.1**	0.2
Surplus of advances that are paid to income tax on current reserves*	**-**	15.2	**-**	11.0
Other Accounts Receivable and debit balances	**2.1**	4.5	**2.5**	2.8
Total Other Assets	**47.7**	54.9	**43.0**	43.2

* Reclassification.

** Issue expenses for impaired debentures using the effective interest method.

Note 10 – Public deposits

Reported amounts in millions of New Shekels

	Consolidated		Bank	
	December 31			
	2012	2011	2012	2011
Deposits according to requirement (including current credit deposit)	**777.4**	682.5	**790.6**	731.1
Fixed-term deposits (1)	**6,655.4**	6,334.4	**8,017.7**	7,738.2
Deposits in saving plans(1)	**2,380.9**	2,047.7	**2,380.9**	2,047.7
Total public deposits	**9,813.7**	9,064.6	**11,189.2**	10,517.0

(1) After screening the savings plans for short-term deposits in 2012 for a total of NIS 223.1 billion (2011 – NIS 241.5 billion).

Note 11 – Banking deposits

Reported amounts in millions of New Shekels

	Consolidated		The Bank	
	December 31			
	2012	2011	2012	2011
Fixed-term deposits from commercial banks	**63.3**	76.2	**63.3**	76.2

Note 12 – Liability certificates and Deferred Liability Notes

Reported amounts

a - Composition

	during life average(2)	Rate Yield Internal(2)	consolidated		Bank	
			December 31			
			2012	**2011**	**2012**	**2011**
	years	%	Millions of NIS			
Debentures and deferred liability notes that cannot be converted into shares:						
in non-linked Israeli currency	3.26	2.95%	**746.5**	937.3	120.4	126.7
Israeli currency index linked	3.70	1.67%	**834.0**	669.7	377.1	386.2
in Israeli currency US Dollar linked	2.24	4.84%	**0.5**	4.9	0.5	4.9
Total liability certificates and deferred liability notes			**1,581.0**	1,611.9	498.0	517.8
From this: deferred liability notes			**498.0**	517.8	**498.0**	517.8

b - Additional details

1) A. On May 4, 2011, the Jerusalem Financing and Issuances Company issued, according to the shelf offering report as of May 1, 2011, that was published based on the prospectus dated June 17, 2009, debentures (series D) at n.v. totaling NIS 100 million in consideration for NIS 100 million.

B. On August 30, 2011, Jerusalem Financing and Issuances (2005) Ltd. (a Bank subsidiary) published a shelf offering for issuance of debentures and deferred liability notes.

C. On December 24, 2012, the Jerusalem Financing and Issuances Company issued, according to the shelf offering report as of December 24, 2012, that was published based on the prospectus dated August 31, 2011, debentures (Series H) in n.v. of NIS 122,421 thousand. Debentures in consideration for NIS 122,421 and NIS 71,761 thousand n.v. Deferred liability notes (Series 10) in consideration for a sum of NIS 71,761 thousand.

D. Jerusalem Financing has an agreement with the Bank under which it was determined that the exchange for the issuance of deposit certificates according to the forecast have been deposited at the bank bearing interest that will be, with repayment terms, identical to those of the deposit certificates and interest terms that are identical to terms or preferable than those, as agreed from time to time with the Bank. The deposit will be for the Bank's use, at its discretion, and with a repayment level equal to other deposits at the Bank.

E. On April 22, 2012, Standard & Poor's Maalot (hereinafter: Maalot) announced that in continuation of the monitoring of the Bank's rating under Maalot's updated methodology for rating banks (as published on November 9, 2011), it was removing the bank's rating from CreditWatch (with negative repercussions) that it had entered in June 2, 2011, and is leaving the the Bank's rating ilA+ (negative rating forecast) intact. For details, please see the immediate reports dated April 22, 2012, reference number 2012-01-106239. This rating is also the rating for the liability notes (except for the deferred liability notes as listed below) that have been issued by Jerusalem Financing and Issuance, the Bank's fully owned and controlled subsidiary, that is ilA+. Deferred liability notes that were issued by Jerusalem Financing and Issuance are rated at one rating level

Note 12 – Liability certificates and deferred liability notes (continuation)

lower than the Bank's rating in accordance with the rating company's methodology. Therefore, the rating is ilA.

On December 13, 2012, Maalot announced that it had set a rating of ilA+ for the debentures (Series H) and a rating of ilA for the deferred liability notes (Series 10).

(2) Internal rate of yield, is the interest rate directing the expected payment flows on remaining balance sheets included in the financial report. The average life time, is the average weighted payment periods in discounted cash flows according to internal yield rates.

(3) Concerning the Bank's purchasing of liability certificates issued by Jerusalem Financing and Issuances (2005) Ltd. see Note 7d. As part of the issuances for the public of liability certificates by Financing and Issuances, the Bank committed towards Financing and Issuances and the trustee for those periods, to comply with all the conditions of the liability certificates that were issued by it and that will be held by the public.

Note 13 – Other liabilities

Reported amounts in millions of New Shekels

	consolidated		The Bank	
	December 31			
	2012	**2011**	**2012**	**2011**
Prepaid Income	**35.4**	34.8	**35.4**	34.8
Salaries and accompanying expenses to be paid	**14.6**	15.4	**13.4**	14.5
Surplus current liabilities for income tax on advances that were paid	**16.3**	-	**18.1**	-
Expenses to be paid	**9.0**	7.2	**6.5**	5.6
Payables for Property, Plant and Equipment	**7.2**	-	**-**	-
Credit loss provision for off-balance-sheets sections (see Note 19a)	**1.9**	1.7	**1.9**	1.7
Reserve surplus for severance pay for fund (see Note 14a)	**1.5**	6.9	**1.1**	6.9
Other payables and credit balances	**37.1**	3.5	**36.7**	3.1
Total Other Liabilities	**123.0**	69.5	**113.1**	66.6

Note 14 – Employee rights

Reported amounts in millions of New Shekels

a – Severance Pay

The reserve for severance pay included in the balance sheet, together with payments for insurances policies, covers the liabilities for severance pay payment to employees based on their last salary and the work period at the Bank and its subsidiaries. The amounts deposited by the Bank and its subsidiaries in insurance companies as part of personal program for senior employee insurance are not included in the balance sheet, since they are not controlled by the Bank. Withdrawal of designated funds is subject to the compliance with the provisions of the Severance Pay Law. Below are designated reserve amounts:

	consolidated		The Bank	
	December 31			
	2012	2011	2012	2011
Reserve Amount	**59.3**	59.3	**56.3**	56.6
Sum of the Fund	**57.8**	52.4	**55.2**	49.7
Surplus reserve for severance pay for the fund (included in section "Other Liabilities")	**1.5**	6.9	**1.1**	6.9

b - Reserve for Jubilee Grants

The employees of the Bank and its subsidiaries are entitled, when reaching a certain seniority, to a special grant ("Jubilee Grant"). According to instructions from the Supervisor of Banks, the calculated reserve for this liability is effective since 2007 on an actuarial basis and is presented at its present value. The capitalization rate that was determined by the Supervisor of Banks is 4%, in consideration of future increase in salaries. Provisions for the jubilee grants are included in the Financial Statements and their balance is: Consolidated NIS 2.6 million (For December 31, 2011 – NIS 2.1 million), at the Bank NIS 2.3 million (For December 31, 2011 – NIS 1.9 million), in the "Salaries and accompanying expenses to be paid" as part of "Other Liabilities" section.

c - Vacations

Employees of the Bank and its subsidiaries are entitled, by law and employment agreements, to annual vacation days. The provision for vacation is calculated based on the last salary of the employees and the vacation days accumulated in their favor with addition of accompanying obligatory expenses. Balance of vacation provision as of the balance sheet date amounted to about NIS 6.2 million consolidated, at the Bank NIS 5.5 million (for December 31, 2011 – NIS 6.0 million consolidated and NIS 5.5 million at the Bank), and is included in the Financial Statements in section "Salaries and accompanying expenses to be paid" as part of "Other Liabilities" section.

Note 14 – Employee rights (continuation)

d – Description of employee compensation plans

During 2010, the Bank of Jerusalem has integrated a benefit plan for Bank employees, based on the document published by the Supervisor of Banks on this issue, with the purpose of fixing a clear and known in advance formula connecting the bank's yield with the height of the yearly distributed grant and this while long-term examination of the bank's goals and in consideration of the existing risk level in achieving this yield. Distribution of the grant among bank employees will be differential and will be based on quantitative and qualitative performance indicators and other parameters. Should the Bank meet the threshold for bonus payments, as set by the plan, the employees, included management members, will be entitled to an annual bonus payments according to the grades, as follows (in thousands of Shekels):

Calculated Yield	Bonus sum for employees		Bonus sum for management members		Total bonus sum for employees and management members	
	starting with	until	starting with	until	starting with	until
8.5%-9%	1,200	1,200	-		1,200	1,200
9%-10%	2,900	4,500	400	700	3,300	5,200
10%-11%	4,500	6,000	700	950	5,200	6,950
11%-12%	6,000	7,250	950	1,500	6,950	8,750
12%-13%	7,250	8,500	1,500	2,000	8,750	10,500
13%-14%	8,500	11,000	2,000	2,700	10,500	13,700
14%-15%	11,000	13,000	2,700	3,300	13,700	16,300
15%-16%	13,000	15,000	3,300	4,500	16,300	19,500

e - Other Rights

In general, Bank employees, including members of the Management (with the exception of the CEO) are not entitled to adjustment grants and increased compensation during retirement. For information regarding the terms of employment for the CEO and the Chairman of the Board of Directors, see below Note 22 – Stakeholders and Related Parties (consolidated)

f - Share-based Payment

For information regarding share-based payment transaction, for the Bank's CEO and senior managers in the bank, see below Note 22a, "Share-based Payment Transactions".

Note 15 – Liens and Restricted Terms

A – According to the bylaws of Maof Clearing House Ltd. (hereinafter: the "Maof Clearing House"), as member of the Maof Clearing House, the Bank is required to deposit liquid collaterals for full exposure for activity in derivatives and for its part in the risk fund. For this purpose, the Bank mortgaged in favor of the Maof Clearing House the rights to the following accounts:

1. The account opened at the Stock Exchange Clearing House in name of Maof Clearing House in which the government debentures are deposited at full value to meet the collateral requirement from the Bank's customers and for the Bank's part in risk fund (hereinafter: "Securities Account"). The value of the deposited debentures, as of December 31, 2012, amounts to NIS 49.7 million.

2. The account opened at Bank Leumi of Israel Ltd. under the name of the Moaf Clearing House, where cash is deposited for a value of at least 25% of the Bank's portion in the risk fund, as well as cash deposited in this account that will be paid as profit from securities that have been deposited in the securities account at the Bank. As of December 31, 2012, the Bank deposited NIS 1.3 million in this account.

The accounts specified above are mortgaged in a floating pledge in favor of the Maof Clearing House as well as mortgaged in fixed charge in favor of the Maof Clearing House.

B – As a member of the Stock Exchange, the Bank is required to deposit liquid collateral for securing the existence of the Bank's customer liabilities towards the Stock Exchange for transactions performed in the Stock Exchange Clearing House and for securing its part of the Stock Exchange Clearing House risk fund. For this purpose, the Bank mortgaged in favor of the Maof Clearing House, in fixed charge at first level, the rights to the following accounts:

1. The account opened at the Stock Exchange Clearing House in its name and managed for the Bank in which government debentures are deposited at full value to meet collateral requirement for the Bank's customers and for the Bank's part in the risk fund. The value of the deposited debentures, as of December 31, 2012, amounts to NIS 6 million.

2. The account opened at Bank Leumi of Israel Ltd. under the Stock Exchange Clearing House where cash is deposited for a value of at least 25% of the Bank's portion in the risk fund. Also deposited in this account is cash that will be paid as profit from securities that have been deposited at the Bank's securities. As of December 31, 2012, the Bank deposited NIS 1.7 million in this account.

C – For the purpose of securing credit provided or that will be provided by the Bank of Israel to the Bank as part of the Bank's activity in the RTGS System, the Bank will mortgage in favor of the Bank of Israel, according to debentures as of January 24. 2011, debentures the Bank holds and that are deposited or will be deposited at the designated account managed by the Stock Exchange under the name of the Bank of Israel. The lien amount is unlimited. The value of the deposited debentures as of December 31, 2012, amounts to NIS 169.5 million.

Details of securities that have been mortgaged for lenders

	Consolidated and Bank	
	2012	**2011**
	Millions of NIS	
Available for sale securities	**225.3**	406.9

Note 16a – Equity

A – The Bank's registered share capital as of December 31, 2012, is composed of 100,250,000 ordinary shares at NIS 1 per share (as of December 31, 2011 – identical). The issued and paid-up capital as of December 31, 2012 – 70,517,741 shares listed with the Tel Aviv Stock Exchange (as of December 2011 – identical).

B – In 2012 and 2010, there was no distribution of dividend.

C – On March 31, 2011, the Bank's Board of Directors decided to distribute a dividend totaling NIS 25 million. This dividend was distributed on April 27, 2011.

D – The dividend distribution is implemented subject to the instructions of the Companies Law, 5759 – 1999 and instructions of Proper Banking Management number 331, which discusses dividend distribution by banking corporations. On June 30, 2010, the Supervisor of Banks notified the banks that in addition to the Proper Banking Management instruction № 331, a bank not complying with the capital objective of 7.5% is not allowed to distribute dividends if such a dividend distribution will cause it to not meet the objective, except after obtaining the Supervisor of Banks' approval.

Note 16b – Equity – Capital adequacy according to instructions from the Supervisor of Banks

Reported amounts in millions of New Shekels

Calculated according to the Proper Banking Management Instructions number 201-211 concerning "Measurement and Capital Adequacy".

A. In consolidated data

a – Capital for the purpose of calculating capital ratio

	December 31	
	2012	**2011**
Tier 1 Capital, after deductions	693.0	644.6
Tier 2 Capital, after deductions	338.0	318.6
Total comprehensive capital	1,031.0	963.2
b – Weighted balances of risk assets		
Credit Risk	6,452.3	6,395.8
Market Risks	148.2	171.6
Operating Risk	553.3	491.1
Total weighted balance of risk assets	7,153.8	7,058.5

c - Capital ratio for risk components

	In percentages	
Tier 1 capital ratio for risk components	9.7	9.1
Comprehensive capital ratio for risk components	14.4	13.7
Minimum comprehensive capital ratio required by the Supervisor of Banks	13.0	13.0

B. Capital components for the purpose of calculating capital ratio

a – Tier 1 Capital

	December 31	
	2012	**2011**
Equity	**694.1**	644.6
*Less net profits from reconciliation of fair value of available for sale securities	**(1.1)**	-
Total Tier 1 Capital	**693.0**	644.6
b – Tier 2 Capital		
Upper Tier 2 Capital:		
45% of the net profits, before the referring tax affect for reconciliation of fair value of available for sale securities	**0.9**	-
Bottom Tier 2 Capital:		
Deferred Liability Notes	**337.1**	318.6
Total Tier 2 Capital	**338.0**	318.6

Note 17 – Assets and liabilities according to index linked basis (continuation) – Consolidated

Reported amounts in millions of NIS

	December 31, 2012					
	Israeli Currency		Foreign Currency(1)			
	Unlinked	Linked to Index prices	Dollar of U.S.A.	Other	Items that are not monetary	Total
Assets						
Cash and deposits at the Bank	1,017.3	-	293.0	50.3	-	1,360.6
Securities	969.5	189.7	2.7	-	1.1	1,163.0
Net credit for the public	4,881.9	3,474.7	1,097.4	127.4	-	9,581.4
Buildings and equipment	-	-	-	-	117.9	117.9
Assets for derivative instruments	11.6	-	5.5	3.8	-	20.9
Other assets	40.5	2.5	-	-	4.7	47.7
Total assets	**6,920.8**	**3,666.9**	**1,398.6**	**181.5**	**123.7**	**12,291.5**
Liabilities						
Public deposits	5,367.3	3,011.8	1,065.3	369.3	-	9,813.7
Deposits from banks	-	52.4	10.9	-	-	63.3
Liability certificates and deferred liability notes	746.6	833.9	0.5	-	-	1,581.0
Liabilities for derivative instruments	14.0	-	2.0	0.4	-	16.4
Other liabilities	87.6	-	-	-	35.4	123.0
Total liabilities	**6,215.5**	**3,898.1**	**1,078.7**	**369.7**	**35.4**	**11,597.4**
Difference	705.3	(231.2)	319.9	(188.2)	88.3	694.1
Non-hedging derivative instruments						
Derivative instruments (except for options)	19.2	69.0	(280.8)	192.6	-	-
General total	**724.5**	**(162.2)**	**39.1**	**4.4**	**88.3**	**694.1**

(1) Including linkage to foreign currency

Note 17 – Assets and liabilities according to index basis (continuation) – consolidated

Reported amounts in millions of NIS

	December 31, 2011					
	Israeli Currency		Foreign Currency(1)			
	Unlinked	Linked to Index prices	Dollar of U.S.A.	Other	Items that are not monetary	Total
Assets						
Cash and deposits at the Bank	562.2	-	179.9	50.2	-	792.3
Securities*	997.1	449.9	41.8	-	1.9	1,490.7
Net credit for the public	4,705.0	3,086.3	1,104.3	162.2	-	9,057.8
Buildings and equipment	-	-	-	-	79.7	79.7
Assets for derivative instruments	4.3	0.4	2.0	0.5	-	7.2
Other assets	48.7	1.3	-	-	4.9	54.9
Total assets	**6,317.3**	**3,537.9**	**1,328.0**	**212.9**	**86.5**	**11,482.6**
Liabilities						
Public deposits	4,960.6	2,764.3	1,004.7	335.0	-	9,064.6
Deposits from banks	-	58.6	17.6	-	-	76.2
Government deposits	0.4	0.4	-	-	-	0.8
Liability certificates and deferred liability notes	937.3	669.7	4.9	-	-	1,611.9
Liabilities for derivative instruments	5.0	-	10.0	-	-	15.0
Other liabilities	34.7	-	-	-	34.8	69.5
Total liabilities	**5,938.0**	**3,493.0**	**1,037.2**	**335.0**	**34.8**	**10,838.0**
Difference	379.3	44.9	290.8	(122.1)	51.7	644.6
Non-hedging derivative instruments						
Derivative instruments (except for options)	12.1	105.1	(243.7)	126.5	-	-
General total	**391.4**	**150.0**	**47.1**	**4.4**	**51.7**	**644.6**

(1) Including linkage to foreign currency

* Reclassification.

Note 17 – Assets and liabilities according to index linked basis (continuation) – the Bank

Reported amounts in millions of Shekels

	December 31, 2012					
	Israeli currency		Foreign currency(1)			
	Unlinked	linked to Index prices	Dollar of U.S.A.	Other	Items that are not monetary	Total
Assets						
Cash and deposits at the Bank	1,016.6	-	293.0	50.3	-	1,359.9
Securities	988.2	192.7	2.7	-	1.1	1,184.7
Net credit for the public	4,881.9	3,474.7	1,097.4	127.4	-	9,581.4
Investment in consolidated companies	13.7	-	-	-	351.0	364.7
Buildings and equipment	-	-	-	-	19.5	19.5
Assets for derivative instruments	11.6	-	5.5	3.8	-	20.9
Other assets	38.5	-	-	-	4.5	43.0
Total assets	**6,950.5**	**3,667.4**	**1,398.6**	**181.5**	**376.1**	**12,574.1**
Liabilities						
Public deposits	6,267.9	3,486.7	1,065.3	369.3	-	11,189.2
Deposits from banks	-	52.4	10.9	-	-	63.3
Liability certificates and deferred liability notes	120.4	377.1	0.5	-	-	498.0
Liabilities for derivative instruments	14.0	-	2.0	0.4	-	16.4
Other liabilities	77.7	-	-	-	35.4	113.1
Total liabilities	**6,480.0**	**3,916.2**	**1,078.7**	**369.7**	**35.4**	**11,880.0**
Difference	470.5	(248.8)	319.9	(188.2)	340.7	694.1
Non-hedging derivative instruments						
Derivative instruments (except for options)	19.2	69.0	(280.8)	192.6	-	-
General total	**489.7**	**(179.8)**	**39.1**	**4.4**	**340.7**	**694.1**

(1) Including linkage to foreign currency

Note 17 – Assets and liabilities according to index linked basis (continuation) – the Bank

Reported amounts in millions of Shekels

	December 31, 2011					
	Israeli currency		Foreign currency[1]			
	Unlinked	linked to Index prices	Dollar of U.S.A.	Other	Items that are not monetary	Total
Assets						
Cash and deposits at the Bank	561.7	-	179.9	50.2	-	791.8
Securities*	1,135.2	394.1	41.8	-	1.9	1,573.0
Net credit for the public	4,705.1	3,086.3	1,104.3	162.1	-	9,057.8
Investment in consolidated companies	-	9.3	-	-	333.9	343.2
Buildings and equipment	-	-	-	-	21.8	21.8
Assets for derivative instruments	4.3	0.4	2.0	0.5	-	7.2
Other assets	38.6	-	-	-	4.6	43.2
Total assets	**6,444.9**	**3,490.1**	**1,328.0**	**212.8**	**362.2**	**11,838.0**
Liabilities						
Public deposits	5,992.0	3,185.4	1,004.7	334.9	-	10,517.0
Deposits from banks	-	58.6	17.6	-	-	76.2
Government deposits	0.4	0.4	-	-	-	0.8
Liability certificates and deferred liability notes	126.7	386.2	4.9	-	-	517.8
Liabilities for derivative instruments	5.0	-	10.0		-	15.0
Other liabilities	31.8	-	-	-	34.8	66.6
Total liabilities	**6,155.9**	**3,630.6**	**1,037.2**	**334.9**	**34.8**	**11,193.4**
Difference	289.0	(140.5)	290.8	(122.1)	327.4	644.6
Non-hedging derivative instruments						
Derivative instruments (except for options)	12.1	105.1	(243.7)	126.5	-	-
General total	**301.1**	**(35.4)**	**47.1**	**4.4**	**327.4**	**644.6**

(1) Including linkage to foreign currency

* Reclassification.

Note 18 – Assets and liabilities according to index linked basis and according to repayment period – Consolidated[1]

Contractually expected future cash flows

Reported amounts in millions of New Shekels

	with Requirement and up to month	Over month and up to 3 months	Over 3 months and up to year	Over year and up to two years	Over two years and up to 3 years
For December 31, 2012					
Non-linked Israeli currency					
Assets	1,454.8	543.5	1,162.7	720.0	563.9
Liabilities	2,678.2	575.8	1,220.3	986.3	480.0
Difference	(1,223.4)	(32.3)	(57.6)	(266.3)	83.9
derivatives	(71.7)	18.8	35.3	38.7	
Israeli currency index-linked					
Assets	36.2	69.1	323.5	421.6	388.2
Liabilities	63.3	237.1	1,145.5	685.9	485.5
Difference	(27.0)	(168.0)	(822.0)	(264.3)	(97.3)
derivatives	69.5	-	-	(0.1)	-
Foreign currency – Local activity (3)					
Assets	305.8	2.2	122.6	121.3	120.1
Liabilities	945.6	227.3	269.9	5.4	-
Difference	(639.8)	(225.1)	(147.3)	115.9	120.1
derivatives	7.4	(17.4)	(31.8)	(37.8)	-
Non-financial items					
Assets	-	-	-	-	-
Liabilities	-	-	-	-	-
Difference	-	-	-	-	-
Total					
Assets	**1,795.9**	**614.8**	**1,608.8**	**1,262.9**	**1,072.2**
Liabilities	**3,687.1**	**1,040.2**	**2,635.7**	**1,677.6**	**965.5**
Difference	**(1,890.2)**	**(425.4)**	**(1,026.9)**	**(414.7)**	**106.7**
As at December 31, 2011*					
Total					
Assets	1,179.5	316.6	1,530.5	1,295.3	1,178.8
Liabilities	3,001.1	1,166.5	2,398.5	1,729.3	867.5
Difference	(1,821.6)	(849.9)	(868.0)	(434.0)	311.3

(1) In this note are presented contractually expected future cash flows for the assets and liabilities paragraphs on a linkage basis, according to period remaining for the contractual repayment date of these flows. The data is presented less the affect of write-offs and credit loss provisions.

(2) Assets without a repayment period including assets of NIS 3.7 million whose repayment time has passed.

(3) Including linkage to foreign currency

(4) As included in Note 17, assets and liabilities according to index linked basis, including off-balance-sheets amounts for derivatives.

(5) The contractual yield rate is the interest rate that deducts future contractual and expected cash flows presented in this note for monetary item at its balance-sheet balance.

* Reclassification.

Note 18 – Assets and liabilities according to index linked basis and according to repayment period – Consolidated[1]

Contractually expected future cash flows
Reported amounts in millions of New Shekels

Over 3 years and up to 4 years	Over 4 years and up to 5 years	Over 5 years and up to 10 years	Over 10 years and up to 20 year	Over 20 year	Total Flows The cash	Balance-sheets balance [4] without period of repayment[2]	Balance-sheets balance [4] Total	Contractual rate yield [5]
425.6	360.3	1,797.6	1,232.4	117.3	8,378.1	29.8	6,920.8	4.30%
170.7	65.5	209.9	-	-	6,386.7	-	6,215.5	3.00%
254.9	294.8	1,587.7	1,232.4	117.3	1,991.4	29.8	705.3	1.30%
(1.5)	(3.4)				16.2		19.2	
341.0	346.5	1,385.1	1,279.0	215.1	4,805.4	-	3,666.9	3.83%
501.8	567.0	475.3	18.9	-	4,180.3	-	3,898.1	2.30%
(160.8)	(220.5)	909.8	1,260.1	215.1	625.1	-	(231.2)	1.53%
-	-	-	-	-	69.4	-	69.0	
118.2	114.9	480.3	422.8	1.9	1,810.1	4.6	1,580.1	3.20%
-	0.4	-	-	-	1,448.6	-	1,448.4	1.30%
118.2	114.5	480.3	422.8	1.9	361.5	4.6	131.7	1.90%
	(1.4)				(81.0)		(88.2)	
-	-	-	-	-	-	123.7	123.7	
-	-	-	-	-	-	35.4	35.4	
-	-	-	-	-	-	88.3	88.3	
884.8	**821.7**	**3,663.0**	**2,934.2**	**334.3**	**14,993.6**	**158.1**	**12,291.5**	**3.97%**
672.5	**632.9**	**685.2**	**18.9**	**-**	**12,015.6**	**35.4**	**11,597.4**	**2.53%**
212.3	**188.8**	**2,977.8**	**2,915.3**	**334.3**	**2,978.0**	**122.7**	**694.1**	**1.44%**
802.3	828.4	3,811.7	2,904.8	302.4	14,150.3	149.7	11,482.6	4.45%
632.2	592.6	573.1	131.3	-	11,092.1	34.8	10,838.0	2.92%
170.1	235.8	3,238.6	2,773.5	302.4	3,058.2	114.9	644.6	1.53%

Note 18 – Assets and liabilities according to index linked basis and according to repayment period – (continuation) Bank[(1)]

Contractually expected future cash flows

Reported amounts in millions of New Shekels

	with Requirement and up to month	Over month and up to 3 months	Over 3 months and up to year	Over year and up to two years	Over two years and up to 3 years
For December 31, 2012					
Non-linked Israeli currency					
Assets	1,450.2	487.5	1,187.0	743.6	617.0
Liabilities	2,712.7	578.2	1,249.9	1,004.3	528.5
Difference	(1,263.5)	(90.7)	(62.9)	(260.7)	88.5
derivatives	(71.7)	18.8	35.3	38.7	
Israeli currency index-linked					
Assets	33.7	69.1	323.7	422.4	389.4
Liabilities	62.5	237.5	1,161.2	686.4	487.1
Difference	(28.8)	(168.4)	(837.5)	(264.0)	(97.7)
derivatives	69.5			(0.1)	
Foreign currency – Local activity (3)					
Assets	303.1	2.2	122.6	121.3	120.1
Liabilities	945.5	227.3	269.9	5.4	-
Difference	(642.4)	(225.1)	(147.3)	115.9	120.1
derivatives	7.4	(17.4)	(31.8)	(37.8)	-
Non-financial items					
Assets	-	-	-	-	-
Liabilities	-	-	-	-	-
Difference	-	-	-	-	-
Total					
Assets	**1,787.0**	**558.8**	**1,633.3**	**1,287.3**	**1,126.5**
Liabilities	**3,720.7**	**1,043.0**	**2,681.0**	**1,696.1**	**1,015.6**
Difference	**(1,933.7)**	**(484.2)**	**(1,047.7)**	**(408.8)**	**110.9**
As at December 31, 2011*					
Total					
Assets	1,179.3	318.0	1,534.6	1,316.0	1,208.2
Liabilities	3,081.8	1,234.0	2,393.8	1,861.4	972.6
Difference	(1,902.5)	(916.0)	(859.2)	(545.4)	235.6

Note 18 – Assets and liabilities on an index linked basis and according to repayment period – (continuation) Bank[1]

Contractually expected future cash flows

Reported amounts

Over 3 years and up to 4 years	Over 4 years and up to 5 years	Over 5 years and up to 10 years	Over 10 years and up to 20 year	Over 20 year	Total Flows The cash	Balance-sheet balance [4] without period of repayment[2]	Balance-sheet balance [4] Total	Contractual rate yield [5]
474.2	393.6	1,867.5	1,232.4	117.3	8,570.3	29.9	6,950.5	4.30%
221.9	96.2	267.6	-	-	6,659.3	-	6,480.0	2.94%
252.3	297.4	1,599.9	1,232.4	117.3	1,911.0	29.9	470.5	1.36%
(1.5)	(3.4)				16.2		19.2	
341.1	346.5	1,385.4	1,279.6	217.9	4,808.7	-	3,667.4	3.83%
502.3	567.5	477.3	18.9	-	4,200.7	-	3,916.2	2.74%
(161.2)	(221.0)	908.1	1,260.7	217.9	608.0	-	(248.8)	1.09%
					69.4		69.0	
118.2	114.9	480.3	422.8	1.9	1,807.4	4.6	1,580.1	3.20%
-	0.4	-	-		1,448.5	-	1,448.4	1.30%
118.2	114.5	480.3	422.8	1.9	358.9	4.6	131.7	1.90%
-	(1.4)	-	-	-	(81.0)		(88.2)	
-	-	-	-	-	-	376.1	376.1	-
-	-	-	-	-	-	35.4	35.4	-
-	-	-	-	-	-	340.7	340.7	-
933.4	**855.0**	**3,733.2**	**2,934.8**	**337.1**	**15,186.4**	**410.5**	**12,574.1**	**4.02%**
724.2	**664.1**	**744.9**	**18.9**	**-**	**12,308.5**	**35.4**	**11,880.0**	**2.68%**
209.2	**190.9**	**2,988.3**	**2,915.9**	**337.1**	**2,877.9**	**375.1**	**694.1**	**1.34%**
837.1	851.1	3,866.9	2,904.8	302.4	14,318.4	425.4	11,838.0	4.53%
746.5	694.3	687.7	29.5	-	11,701.6	34.8	11,193.4	3.21%
90.6	156.8	3,179.2	2,875.3	302.4	2,616.8	390.6	644.6	1.32%

Note 18 – Assets and liabilities according to index linked basis and according to repayment period – (continuation) Bank[1] (continuation)

(1) In this note are presented contractually expected future cash flows for the assets and liabilities paragraphs on a linkage basis, according to period remaining for the contractual repayment date of these flows. The data is presented less the affect of write-offs and credit loss provision.

(2) Assets without a repayment period including assets of NIS 3.7 million whose repayment time has passed.

(3) Including linkage to foreign currency

(4) As included in Note 17, assets and liabilities according to index linked basis, including off-balance-sheets amounts for derivatives.

(5) The contractual yield rate is the interest rate that deducts future contractual and expected cash flows presented in this note for monetary item at its balance-sheet balance.

* Reclassification.

Note 19 – Contingent Liabilities and Special Agreements

Reported amounts in millions of New Shekels

a - Off-balance-sheets financial instruments (consolidated and in the Bank)

(contractual balances or their face amounts for the end of the year)

	Balance of contracts (1)		Balance of provision for credit losses	
	As at December 31			
	2012	2011	2012	2011
Transactions in which the balance represents credit risk:				
Non-returnable liabilities that were approved but still not given	**1,038.5**	821.8	**0.7**	0.3
Guarantees for housing purchasers	**32.9**	178.4	**0.2**	0.8
Guarantees for ensuring credit	**81.4**	76.8	**0.3**	0.2
Other guarantees	**80.5**	84.1	**0.5**	0.2
Credit lines for credit cards that were unexploited	**134.4**	133.7	**0.2**	0.2
Revolving credit account and as part of other credit at accounts according to unexploited requirements	**80.1**	76.7	**-**	-
Total	**1,447.8**	1,371.5	**1.9**	1.7

(1) Contractual balances or their face amounts for the end of the year, before the affect of credit loss provision.

b – Off-balance-sheet agreements for activity according to collection level(1) for the end of the year (consolidated and in the Bank)
Balance of credit from deposits based on the collection level(2)

	As at December 31	
	2012	2011
Non-linked Israeli currency	**1,936.7**	2,242.8
Israeli currency index-linked	**59.7**	61.1
Foreign currency	**0.4**	3.8
Total	**1,996.8**	2,307.7

Information on loan provisions during the year

	for the year ending on December 31	
	2012	2011
Loans from deposits by collection size	**4.8**	0.9
Standing loans	**1.8**	2.6

(1) Credits from deposits whose return to the depositor is subject to credit collection, with margin or with collection fees (instead of margin).
(2) Standing loans and government deposits provided for them, for a total of NIS 301 million (2011 – NIS 390.7 million), are not included in this note.

Note 19 – Contingent liabilities and special agreements (continuation)

Reported amounts in millions of New Shekels

b - Off-balance-sheet agreements for activity according to collection level[1] for the end of the year (continuation)

Flows for collection fees and from interest margins for collection level activity[2]

	December 31						
	2012						2011
	until year	Over a year until 3 years	Over 3 until 5 years	Over 5 Up to 10 years	Over 10 Up to 20 years	Total	Total
Future contractual flows	**15.1**	**28.8**	**27.9**	**54.7**	**10.9**	**137.4**	162.1
Expected capitalized flows[3] [4]	**14.8**	**27.1**	**25.1**	**45.6**	**8.1**	**120.7**	132.9

(1) Credits from deposits whose return to the depositor is subject to credit collection (or deposits), with margin or with collection fees (instead of margin).

(2) Including the foreign currency sector and unlinked NIS sector that does not exceed 10% from the total deposits according to collection level.

(3) Capitalization is performed according to a rate of 2.4% (2011 – 3.26%).

(4) The data does not take into account the assessment of early repayments.

c – Claims

1. General

   During regular course of business, various lawsuits were filed against the Bank. Based on the opinion of the legal advisers concerning risks from claims, including requests for approval of class action suits, proper provisions were included in the Financial Statements in accordance with GAAP, for expected loss resulting from these pending claims against the Bank.

2. Motions for class action suits are pending against the Bank are as detailed below.

   a. In July 1997, a claim was filed against the Bank and against four other mortgages banks at the Tel Aviv District Court for the overall amount of more than NIS 1 billion, as well as a motion that was filed for recognition of this claim as a class action suit. In the claim and motion, it was claimed, inter alia, that the aforementioned banks unlawfully collected from the borrowers life insurance and property insurance fees, and that the borrowers are entitled to restitution of these fees. The claim and the motion did not include the manner of calculation of the aforementioned amount, and did not specify which part is attributed to the Bank.

      In February 2008, this claim was sent for arbitration before the Honorable Vice-President (Judge, Ret.) Theodor Or. The parties signed a settlement that included payment of compensation to needy public bodies, which were approved by the arbitrator and on December 5, 2011, was approved by the Court (which ordered the publication of the settlement agreement). According to the agreement, the bank will pay to the aforementioned entities a total of NIS 644,549 (the

Bank's share – 3.185% of the comprehensive settlement amount of NIS 20,237,000). On March 25, 2012, the Bank of Jerusalem paid a sum of NIS 8 thousand of said sum and on June 5, 2012, the Bank paid the balance of the sum. Thereby bringing this claim to its conclusion.

c. On July 12, 2010, a claim was filed against the Bank in the Jerusalem District Court, as well as a motion to recognize this claim as class action suit for an overall amount of NIS 10,692 thousand for the entire represented group. The claim alleges that the Bank failed to remove all records of liens listed in its name to secure loans already entirely cleared by the borrowers. Therefore, it demanded that the Bank remove these records and compensate customers that removed these records at their own cost. Arbitration on this case is currently being conducted.

   According to the Bank's management, relying on the opinion of the legal advisers, the chances that the Bank will be required to pay this claim is slight.

d – Other contingent liabilities

1. In January 2012, the Bank's General Assembly of shareholders approved the decision, according to which the Bank will grant somebody serving from time to time as senior officer at the Bank and its subsidiaries, indemnification liability due to financial debts imposed on someone and for reasonable litigation expenses related to the list of events attached as an appendix to the liability note. Provision of reimbursement depends on the existence of conditions specified in the liability note and the maximum indemnification amount per senior officer of the Bank and its subsidiaries, as accumulated, and not exceeding 25% of the Bank's equity.
2. As part of establishment of the company, "Jerusalem Financing Issuances (2005) Ltd.", a subsidiary fully controlled by the Bank (hereinafter: "Financing and Issuances"), the Bank undertook to indemnify Financing and Issuances for all its liabilities, and this in order to meet the requirement instructions of the Supervisor of Banks on the subject of minimum capital ratio (Section 4 of Instruction 311 of the Proper Banking Management Instructions).

   As part of the public offering of liability certificates by Financing and Issuances, the Bank undertook towards Financing and Issuances and the trustee for those periods, to comply with all the conditions of the liability certificates that were issued by it and that will be held by the public. As of the report date, the liability balance of the Bank is NIS 45 million n.v. Deposit certificates (Series A), NIS 228 million n.v. Deposit certificates (Series B), NIS 150 million n.v. Deferred liability notes (Series C), NIS 68 million n.v. Debentures (Series F), NIS 420 million n.v. Debentures (Series G), NIS 360 million n.v. Debentures (Series G), NIS 122 million n.v. (Series H) NIS 100 million n.v. Deferred liability notes (Series N) and NIS 72 million deferred liability notes (Series 10) that were issued by Financing and Issuances. In June 2012, the final date for redeeming liability certificates (series E) arrived and thus the balance of the principal was redeemed for a total of NIS 33 million n.v. The aforementioned undertaking of the Bank cannot be canceled or changed since the rights of the deposit certificates depend on them.
3. On February 14, 2013, the Bank was given an audit report conducted by the Supervisor of

Banks regarding the prohibition against money laundering following an audit conducted by the Bank between May-November 2011, and August-December 2012. And that referred to the Bank's activities between 2008-2010. The report includes a listing of findings as well as requirements to implement measures regarding the prohibition against money laundering and financing terrorism. The Bank was given the right to submit its written response to the report within 30 days from the date of its receipt, while noting the fact that it would consider filing a motion to impose a financial sanction on the bank in accordance with the authorities prescribed by law. The Bank is studying the report's findings and is preparing to submit its written response within the obligatory timetable.

At this stage, the Bank cannot assess whether financial sanctions will be imposed on the Bank as a result of this report and if so, the sum of said sanction.

The Bank believes that improvements made in the bank's performance regarding money laundering following the audit significantly reduces the bank's exposure to the risks of money laundering.

4. The Bank undertook to allow the depositors and depositors to receive loans for purchasing an apartment or for purchasing a vehicle at the height of their deposits at a lower interest than the nominal interest that will be customary a the bank when providing the loan. This entitlement will be available to them at the end of the year from the start of the repayment period and on condition that they will comply with the conditions customary at the Bank concerning providing loans; additionally, the funds are deposited at dates determined under the plan's terms.

Note 19 – Contingent liabilities and special agreements (continuation)

Listed below is the composition of the liability sums for providing credit:

	Amortization Rate From Interest Nominal	Maximum Liabilities For Providing Loans As at December 31	
	%	**2012**	2011
Details of Saving			
Savings Plans with Monthly Deposits	0.25%	**2,388.0**	2,088.3
Savings Plans with One-time Deposit	0.4%	**1,028.5**	895.9
Savings Plans (monthly or one-time deposit)	0.5%	**42.8**	45.4
Total		**3,459.3**	3,029.6

It should be noted that the affect of the discounts mentioned above and the actual rate of exploitation is not material.

E – Agreements

1. The Bank and a consolidated company entered into a long term lease contract that includes an extension option. The payable rent for the coming years for the aforementioned agreement is as follows:

	consolidated		The Bank	
	December 31			
	2012	**2011***	**2012**	**2011**
First Year	**14.0**	13.8	**2.4**	2.2
Second Year	**13.2**	13.0	**2.0**	2.0
Third Year	**15.5**	12.8	**1.8**	1.9
Fourth Year	**11.7**	11.4	**1.8**	1.9
Fifth Year and After	**111.9**	101.9	**4.6**	6.3
Total Long Term Lease Contract	**166.3**	152.9	**12.6**	14.3

* Presented again

Note 20 – Activity in Derivative Instruments – Scope, credit risks and repayment dates (consolidated and at the Bank)

a. Implementation of the instructions from the Supervisor concerning derivative instruments and hedging activity

The activity of the Bank as a financial intermediary exposes it to a variety of risks including market risks. Market risks include, inter alia, basic risks, interest risks, exchange rates fluctuation risks, and inflation rate risks. As part of the Bank's overall strategy for managing the exposure level to market risks, as mentioned above, the Bank implements, inter alia, transactions in derivative financial instruments for reducing its exposure to market risks. The Bank's activity in derivative financial instruments is as an intermediary, trader or end-user. The Bank has derivative financial instruments such as future transactions for exchange between currencies as well as interest (Swap), future contracts for protection of currency rates (Future, Forward).

The transactions in derivative financial instruments is recorded according to fair value and changes in the fair value are recorded in a continuous manner in the Profit and Loss Statement.

Note 20 – Activity in Derivative Instruments – Scope, credit risks and repayment dates (consolidated and at the Bank) (continuation)

Reported amounts in millions of New Shekels

b. Activity scope

1. Nominal amount of derivative instruments

	December 31, 2012				
	Interest contracts		Contractual Currency	Contracts for	
	NIS – Index	Other	Foreign	Shares	Total
A. Derivatives ALM (1)(2)					
Forward contracts	-	-	649.0	-	649.0
Swaps	170.0	320.8		-	490.8
Total	**170.0**	**320.8**	**649.0**	**-**	**1,139.8**
B. Other derivatives (1)					
Option contracts listed on the Stock Exchange					
Written options	-	-	32.8	610.7	643.5
Purchased options	-	-	32.8	610.7	643.5
Total	**-**	**-**	**65.6**	**1,221.4**	**1,287.0**
C. Credit derivatives and foreign currency swaps spot.					
Foreign currency swaps spot.	-	-	65.5	-	65.5
Total nominal amount	**170.0**	**320.8**	**780.1**	**1,221.4**	**2,492.3**

2. Gross fair value of derivative instruments

	NIS – Index	Other	Contractual Currency Foreign	Contracts for Shares	Total
A. Derivatives ALM (1)(2)					
Gross positive fair value	0.4	0.1	15.9	-	16.4
Gross negative fair value	2.0	6.4	3.5	-	11.9
B. Other derivatives (1)					
Gross positive fair value	-	-	0.3	4.2	4.5
Gross negative fair value	-	-	0.3	4.2	4.5
Total positive fair value	**0.4**	**0.1**	**16.2**	**4.2**	**20.9**
Total negative fair value	**2.0**	**6.4**	**3.8**	**4.2**	**16.4**

Note 20 – Activity in Derivative Instruments – Scope, credit risks and repayment dates (consolidated and at the Bank) (continuation)

Reported amounts in millions of New Shekels

	December 31, 2011				
	Interest contracts		Contractual Currency Foreign	Contracts for Shares	Total
	NIS – Index	Other			
A. Derivatives ALM [1][2]					
Forward contracts	-	-	624.1	-	624.1
Swaps	100.0	70.0	-	-	170.0
Total	**100.0**	**70.0**	**624.1**	**-**	**794.1**
B. Other derivatives [1]					
Option contracts listed on the Stock Exchange					
Written options	-	-	12.7	224.7	237.4
Purchased options	-	-	12.7	224.7	237.4
Total	**-**	**-**	**25.4**	**449.4**	**474.8**
C. Credit derivatives and foreign currency swaps spot.					
Foreign currency swaps spot.	-	-	15.5	-	15.5
Total nominal amount	**100.0**	**70.0**	**665.0**	**449.4**	**1,284.4**
2. Gross fair value of derivative instruments					
A. Derivatives ALM [1][2]					
Gross positive fair value	0.4	0.8	2.4	-	3.6
Gross negative fair value	-	1.5	9.9	-	11.4
B. Other derivatives [1]					
Gross positive fair value	-	-	0.1	3.5	3.6
Gross negative fair value	-	-	0.1	3.5	3.6
Total positive fair value	**0.4**	**0.8**	**2.5**	**3.5**	**7.2**
Total negative fair value	**-**	**1.5**	**10.0**	**3.5**	**15.0**

Note 20 – Activity in Derivative Instruments – Scope, credit risks and repayment dates (consolidated and at the Bank) (continuation)

Reported amounts in millions of New Shekels

C. Credit risk for derivative instruments according to opposite party of the contract

	Stock Exchanges	Banks	Total
For December 31, 2012			
Gross positive fair value of derivative instruments (3)	4.5	16.4	20.9
Balance-sheet-balance of assets derived from derivative instruments	4.5	16.4	20.9
Off-balance-sheet credit risk for derivative instruments	5.9	55.6	61.5
Total credit risk for derivative instruments	**10.4**	**72.0**	**82.4**
For December 31, 2011			
Gross positive fair value of instruments (3)	3.6	3.6	7.2
Balance-sheet-balance of assets derived from derivative instruments	3.6	3.6	7.2
Off-balance-sheet credit risk for derivative instruments	3.4	80.9	84.3
Total credit risk for derivative instruments	7.0	84.5	91.5

(1) Except for credit derivatives and foreign currency swaps spot.

(2) Derivatives are part of the Bank's management system of assets and liabilities, that are not designated to hedging relations.

(3) From this balance-sheet-balance of derivative instruments standing by themselves for a total of NIS 20.9 million (as at December 31, 2011 – NIS 7.2 million) included in Section Assets for Derivative Instruments.

e. Details of repayment dates (amounts in nominal value)

	until 3 months	Over 3 months and up to one year	Over a year and up to 5 years	Total
As at December 31, 2012				
Interest contract (NIS-Index)	70.0	-	100.0	170.0
Interest contracts (other)	-	-	320.8	320.8
Foreign currency contracts	556.8	186.0	37.3	780.1
Securities contract	1,221.4	-	-	1,221.4
Total	**1,848.2**	**186.0**	**458.1**	**2,492.3**
As at December 31, 2011				
Interest contract (NIS-Index)	100.0	-	-	100.0
Interest contracts (other)	25.0	-	45.0	70.0
Foreign currency contracts	536.9	128.1	-	665.0
Securities contract	449.4	-	-	449.4
Total	**1,111.3**	**128.1**	**45.0**	**1,284.4**

(1) Except for credit derivatives and foreign currency swaps spot .

(2) Derivatives are part of the Bank's management system of assets and liabilities, that are not designated to hedging relations.

Note 21 – Balance and estimates of fair value of financial instruments (consolidated)

a – Fair value of financial instruments

The information included in this note refers to the assessment of fair value of financial instruments

For most of the financial instruments in the bank, a "market price" cannot be quoted because an active market in which they are traded does not exist. Therefore, the fair value is assessed through accepted models for pricing, such as present value of future cash flow capitalized by discount interest at a rate that reflects the embedded risk level in the financial instruments. Estimation of fair value through future cash flow evaluation and determining discounted interest rate is subjective. Therefore, for most of the financial instruments, the aforementioned assessment of fair value is not necessarily an indication of the realization value of the financial instrument on the reporting day. Evaluation of the fair value was carried out according to the valid interest rates on the reporting date and does not take into account the fluctuation of the interest rates. Under the assumption of other interest rates, a fair value is obtained that may be significantly different. Mainly these concern the financial instruments at fixed interest or without interest. In addition, by determining the fair value, the commissions that will be obtained or paid for the business activity were not taken into account, as well as not including the tax affect.

It should be noted that it is plausible that the gap between the balance-sheet-balance and between the fair value balance will not be realized since in most cases the Bank may hold the financial instruments until repayment. For all these, it should be emphasized that the data included in this note do not indicate the value of a banking corporation as a going concern. Furthermore, caution should be adopted when preparing the comparison of values of fair value between various banks because of multiple assessment techniques and the possible estimates and assessments for implementing a fair value assessment.

b – The method and principal directives for estimating the fair value of financial instruments

Deposits in banks, debentures and loans that are not negotiable and credit to the government – method of capitalization of future cash flows is based on the interest rates at which the bank made similar transactions at the report time.

Negotiable securities – According to market value, non-negotiable securities according to data concerning valuation obtained from external resources.

Credit for the public – The fair value of the credit balance for the public is estimated according to the method of present value of future cash flows discounted at suitable discount rates. The credit balance was divided into categories based on the main types of population by division according to linked sectors and credit in fixed and variable interest rates. Cash flows (principal and interest) were capitalized at the interest rates that are identical to the average interest rates at which similar transactions were being

Note 21 – Balance and estimates of fair value of financial instruments (consolidated) (continuation)

made at the bank on the reporting date. The fair value at early credit payoff was not taken into account during the calculation when their influence is unambiguous.

The fair value of the problematic debts is calculated using discount interest rates that reflect the high credit risk embedded in them. These discount rates are not reduced from the highest interest rate the bank uses for its transactions at reporting date. Future cash flows for problematic debts are calculated after deduction of write-offs and provisions for credit loss. The fair value at early credit payoff was not taken into account during the calculation when their affect is unambiguous.

Deposits, debentures and deferred liability notes – in capitalization of future cash flow method according to interest rate in which the Bank recruits similar deposits, or by issuing similar debentures and deferred liability notes, by the Bank on report day, except for debentures registered for trade at the Stock Exchange presented according to market value.

The off-balance-sheet financial instruments at which the balance presents credit risk – the evaluated fair value according to the present evaluation of future cash flows is capitalized at the interest rate reflecting the interest level at which similar transaction has been performed at the reporting date.
Financial instruments for the original period for up to three months and at fluctuating market interest – the balance sheet balance constitutes an approximation to the fair value subject to changes in credit risk and in the bank's margin for transactions with fluctuating interest.

Note 21 – Balance and estimates of fair value of financial instruments (consolidated) (continuation)

Reported amounts in millions of New Shekels

	December 31									
	2012					2011***				
	Balance-Sheet Balance	fair value				Balance-Sheet Balance	fair value			
		Level 1(1)	Level 2(1)	Level 3(1)	Total		Level 1(1)	Level 2(1)	Level 3(1)	Total
Financial assets										
Cash and deposits at the Bank	1,360.6	971.9	-	388.7	1,360.6	792.3	792.3	-	-	792.3
Securities*	1,161.9	1,157.9	4.0	-	1,161.9	1,488.8	1,486.6	2.2	-	1,488.8
Net credit for the public	9,581.4	-	-	9,744.9	9,744.9	9,057.8	-	-	9,263.4	9,263.4
Assets for derivative instruments	20.9	4.5	16.4	-	20.9	7.2	3.6	3.6	-	7.2
Other financial assets	43.0	-	-	43.0	43.0	50.0	-	-	50.0	50.0
Total financial assets	**12,167.8**	**2,134.3**	**20.4**	**10,176.6**	**12,331.3**	**11,396.1**	**2,282.5**	**5.8**	**9,313.4**	**11,601.7**
Financial liabilities										
Public deposits	9,813.7	-	-	9,865.8	9,865.8	9,064.6	-	-	9,159.6	9,159.6
Deposits from banks	63.3	-	-	72.8	72.8	76.2	-	-	80.2	80.2
Government deposits	-	-	-	-	-	0.8	-	-	0.9	0.9
Liability certificates and deferred liability notes	1,581.0	1,208.4	-	425.6	1,634.0	1,611.9	1,294.7	-	338.5	1,633.2
Assets for derivative instruments	16.4	4.5	11.9	-	16.4	15.0	3.6	11.4	-	15.0
Other financial liabilities	87.6	-	-	87.6	87.6	34.7	-	-	34.7	34.7
Total financial liabilities	**11,562.0**	**1,212.9**	**11.9**	**10,451.8**	**11,676.6**	**10,803.2**	**1,298.3**	**11.4**	**9,613.9**	**10,923.6**

(1) Level 1 – Measurement of fair value used in quoted prices in an active market.

Level 2 – Measurement of fair value used in other significant observable inputs.

Level 3 – Measurement of fair value used in other significant unobservable inputs. For more information, see Section B of this note.

* For more information about the balance sheet balance and fair value of securities, see Note 4.

** From this: Assets and liabilities whose balance-sheet balance is identical to the fair value (instruments presented in the balance sheet according to fair value) or constitutes an approximation of the fair value (instruments for the original period of up to 3 months for which use was made of the balance-sheet balance approximating the fair value) as at December 31, 2012, December 31, 2011, sums of NIS 2,172.9 million, NIS 801.1 million, NIS 2,267.5 million, and NIS 631.5 million, respectively. For more information about instruments that were measured at fair value on a recurring basis and on a non-recurring basis, see Note 21a.

*** Presented again

Note 21a – Items measured in fair value on recurring basis (consolidated)

Reported amounts in millions of New Shekels

December 31, 2012				
	Measurement of fair value used in			
	quoted prices in active markets (level 1)*	Other material observable inputs (level 2)*	Non-observable material inputs (level3)	Balance-sheet balance
	Millions of NIS			
Assets				
Available for sale securities				
Israeli government debentures	783.9	2.3	-	786.2
Other corporate debentures	11.3	1.7	1.1	14.1
Total available for sale securities	**795.2**	**4.0**	**1.1**	**800.3**
Securities for trade purposes:				
Debentures for trade	362.7	-	-	362.7
Total negotiable securities	362.7	-	-	362.7
Assets for derivative instruments:				
Interest contracts NIS index	-	0.4	-	0.4
Interest contracts – other		0.1	-	0.1
Foreign currency contracts	0.3	15.9	-	16.2
Securities contract	4.2		-	4.2
Total assets for derivative instruments:	**4.5**	**16.4**	**-**	**20.9**
Total financial assets	**1,162.4**	**20.4**	**1.1**	**1,183.9**
Liabilities				
Liabilities for derivative instruments:				
Interest contracts – NIS index	-	2.0	-	2.0
Interest contracts – other	-	6.4	-	6.4
Foreign currency contracts	0.3	3.5	-	3.8
Securities contract	4.2	-	-	4.2
Total liabilities for derivative instruments	**4.5**	**11.9**	**-**	**16.4**
Total financial liabilities	**4.5**	**11.9**	**-**	**16.4**

* During 2012 and 2011, a sum of NIS 2.3 million and a sum of NIS 2.4 million was transferred from Level 1 to Level 2, respectively.

Note 21a – Items measured in fair value on recurring basis (consolidated)

Reported amounts in millions of New Shekels

December 31, 2011				
	Measurement of fair value used in			
	quoted prices in active markets (level 1)*	Other material observable inputs (level 2)*	Non-observable material inputs (level3)	Balance-sheet balance
	Millions of NIS			
Assets				
Available for sale securities				
Israeli government debentures	1009.4	2.4	-	1011.8
Other corporate debentures	191.5	2.2	-	193.7
Asset-backed debentures	13.7	-	-	13.7
Total available for sale securities	**1,214.6**	**4.6**	**-**	**1,219.2**
Securities for trade purposes:				
Debentures for trade	270.4	-	-	270.4
Total negotiable securities	270.4	-	-	270.4
Assets for derivative instruments:				
Interest contracts NIS index	-	0.4	-	0.4
Interest contracts – other	-	0.8	-	0.8
Foreign currency contracts	0.1	2.4	-	2.5
Securities contract	3.5	-	-	3.5
Total assets for derivative instruments:	**3.6**	**3.6**	**-**	**7.2**
Total financial assets	**1,488.6**	**8.2**	**-**	**1,496.8**
Liabilities				
Liabilities for derivative instruments:				
Interest contracts – other	-	1.5	-	-
Foreign currency contracts	0.1	9.9	-	-
Securities contract	3.5	-	-	-
Total liabilities for derivative instruments	**3.6**	**11.4**	**-**	**15.0**
Total financial liabilities	**3.6**	**11.4**	**-**	**15.0**

* During 2012 and 2011, a sum of NIS 2.3 million and a sum of NIS 2.4 million was transferred from Level 1 to Level 2, respectively.

Note 22 – Stakeholders and Related Parties [(1)] (consolidated)

Reported amounts in millions of Shekels

a – Balances

	Stakeholders								Related parties	
	Shareholders									
	Controlling Shareholders[(4)]		Parties of material influence [(5)]		Others		Key management personnel[(6)]		Others [(7)]	
	2	3	2	3	2	3	2	3	2	3
As at December 31, 2012										
Assets										
Credit for the public	-	**0.2**	-	-	-	-	**0.7**	**5.4**	-	-
Provision for Credit Losses	-	-	-	-	-	-	-	-	-	-
Net credit for the public	-	**0.2**	-	-	-	-	**0.7**	**5.4**	-	-
Liabilities										
Public deposits	7.9	13.6	0.2	0.2	2.0	2.0	2.8	5.1	0.6	0.6
Other liabilities – Other payables and credit balances	-	-	-	-	-	-	0.8	0.8	-	-
Shares (included in equity)[(8)]	600.9	600.9	-	-	34.8	34.8	-	-	-	-
Credit risk in off-balance-sheet financial assets	-	-	-	-	-	-	-	-	-	-
As at December 31, 2011										
Assets										
Credit for the public	-	0.2	-	-	-	-	5.4	5.4	-	-
Provision for Credit Losses	-	-	-	-	-	-	-	-	-	-
Net credit for the public	-	0.2	-	-	-	-	5.4	5.4	-	-
Liabilities										
Public deposits	10.1	13.3	0.2	0.2	1.7	2.5	5.5	6.2	0.5	0.5
Other liabilities – Other payables and credit balances	-	-	-	-	-	-	3.4	3.4	-	-
Shares (included in equity)	558.8	558.8	-	-	34.8	34.8	-	-	-	-
Credit risk in off-balance-sheet financial assets	-	-	-	-	-	-	-	-	-	-

Remarks: At end of Note 22.

Note 22 – Stakeholders and Related Parties (consolidated) [1] (continuation)

Reported amounts in millions of New Shekels

b - Summary of business results

	Stakeholders				Related parties
	Shareholders				
	Controlling Shareholders(4)	Parties of material influence (5)	Others	Key management personnel(6)	Others (7)
For the year ending at December 31, 2012-					
Income from Interest, net*	**(0.1)**	**-**	**-**	**-**	**-**
Expenses for Credit Losses	**-**	**-**	**-**	**-**	**-**
Non-Interest Income	**(0.2)**	**-**	**-**	**-**	**-**
Operating and other expenses**	**0.1**	**0.1**	**0.1**	**15.0**	**0.5**
Total	**(0.2)**	**0.1**	**0.1**	**15.0**	**0.5**
For the year ending at December 31, 2011-					
Income from Interest, net*	(0.2)	-	-	(0.1)	-
Expenses for Credit Losses	-	-	-	-	-
Non-Interest Income	(0.3)	-	-	-	-
Operating and other expenses**	0.1	0.1	0.1	15.4	0.5
Total	**(0.4)**	**0.1**	**0.1**	**15.3**	**0.5**
For the year ending at December 31, 2010-					
Income from Interest, net**	(0.2)	-	0.1	-	-
Expenses for Credit Losses	-	-	-	-	-
Non-Interest Income	0.3	-	-	-	-
Operating and other expenses**	0.1	0.1	0.1	13.6	0.5
Total	**(0.4)**	**0.1**	**-**	**13.6**	**0.5**

* List in Table D Interest Income, Net in Transactions with the Banking Corporation and its Consolidated Companies with Stakeholders and Related Parties.

** List in Table C Compensation and Every Other Benefit for Stakeholders (from the banking corporation and held companies).

Remarks: At end of Note 22.

Note 22 – Stakeholders and Related Parties (consolidated) [1] (continuation)

Reported amounts in millions of Shekels

C - Compensation and Every Other Benefit for Stakeholders (from the banking corporation and held companies).

	Stakeholders							
	Shareholders						Key management personnel(6)	
	Controlling Shareholders(4)		Parties of material influence (5)		Others			
	Total benefit	Number of parties receiving benefits	Total benefit	Number of parties receiving benefits	Total benefit	Number of parties receiving benefits	Total benefit	Number of parties receiving benefits
For the year ending at December 31, 2012-								
Stakeholders employed in or for the corporation	**-**	**-**	**-**	**-**	**-**	**-**	***11.9**	**11**
Director who is not employed in or for the corporation	**0.1**	**1**	**0.1**	**1**	**0.1**	**1**	**3.1**	**13**
Of this: Share-based Payment NIS 0.8 million.								
For the year ending at December 31, 2011-								
Stakeholders employed in or for the corporation	-	-	-	-	-	-	*12.6	11
Director who is not employed in or for the corporation	0.1	1	0.1	1	0.1	1	2.8	13
*Of this: Share-based Payment NIS 0.8 million, Post-employment benefit of NIS 1.1 million.								
For the year ending at December 31, 2010-								
Stakeholders employed in or for the corporation	-	-	-	-	-	-	*11.7	11
Director who is not employed in or for the corporation	0.1	1	0.1	1	0.1	1	1.9	13
*Of this: Share-based Payment NIS 2.3 million, Post-employment benefit of NIS 0.7 million.								

Note 22 – Stakeholders and Related Parties (consolidated) (1) (continuation)

Reported amounts in millions of Shekels

D - Interest Income, Net of Transactions with the Banking Corporation and its Consolidated Companies with Stakeholders and Related Parties.

	Consolidated		
	For the year ending on December 31		
	2012	2011	2010
A. For assets			
from credit for the public	0.2	0.1	0.2
B. For liabilities			
on public deposits	(0.3)	(0.4)	(0.3)
Total Income from Interest, net	(0.1)	(0.3)	(0.1)

* Sums less than NIS 0.1 million are presented in this Note as 0.

(1) Stakeholders and related parties as defined in the Securities Regulations.

Related party – related party that is not a stakeholder as defined in Opinion 29 of the Institute of Certified Public Accountants in Israel.

(2) Balance as at the balance-sheet date.

(3) The highest balance during the year – and this based on balances at the end of each month.

(4) Controlling shareholder – as defined in the Securities Law.

(5) Shareholders in material stakeholders – in accordance with Section 80.d(2) of the Instructions on Reporting to the Public.

(6) Key management personnel – in accordance with Section 80.d(4) of the Instructions on Reporting to the Public

(7) In accordance with Section 80.d(92) of the Instructions on Reporting to the Public.

(8) The holdings of stakeholders and related parties in the banking corporation's capital.

Note 22 – Stakeholders and Related Parties (consolidated) [1] (continuation)

E – CEO employment terms

On April 13th, 2010, Mr. Uriel Paz (hereinafter: "Mr. Paz" or "the CEO") began his tenure as CEO of the bank after receiving approval from the Bank of Israel for his appointment. A detailed immediate report of the Bank in relation to the employment terms of the CEO was issued on March 15, 2010. The CEO's employment terms, as detailed below, has been approved by the Audit Committee and the Bank's Board of Directors on March 14, 2010, as required in relation to extraordinary employment of a senior officer.

Below are the principles of the management service provision agreement between the Bank and Uriel Paz Consultancy Ltd. company owned and fully controlled by the CEO (hereinafter: "Management Company"), as of October 10, 2010 (hereinafter: "Management Agreement") (this agreement replaced the work agreement that was signed with the CEO on April 8, 2010), as follows:

1. The Management Company is entitled to a consideration of NIS 120,000 gross per month ("monthly payment") during the management agreement period linked to the CPI as published on February 15, 2010 for January 2010.

2. The term of the agreement according to the management agreement from April 8, 2010 is for a term of 4 years, but each of the parties may terminate the agreement period by issuing written notice six months in advance. In addition, the Bank will be entitled to bring the agreement to an end, immediately, without compensation, and this in each of the following events: (a) the CEO was convicted of a flagrant offense related to providing services to the bank or other offense of criminal type; (b) the court ruled that the CEO caused a grave betrayal of Bank's trust , or embezzlement of Bank funds or intentionally hurt the Bank or any of its employees by causing significant damage to the Bank and/or any of its employees; and (c) under these circumstances it is possible to deprive the CEO of severance pay, in whole or in part, as if he was employed as a Bank employee.

3. Following the approval of the above employment terms of the CEO and the management agreement as of March 14, 2010, the Board of Directors decided on February 27, 2011, after receiving the approval of the Bank's Audit Committee on February 21, 2011, to adopt the options plan for the allocation of option units to the Management Company at a volume and under such terms as determined by the plan. According to the options plan, 2,115,530 units of type A and 1,410,355 units of type B were allocated in the name of the Management Company. For additional details concerning the options program see the the Bank's Immediate Report dated March 7, 2011 (reference number: 2011-01-071295), and Note 22a of the Financial Statements.

4. One time grants

The plan determines the Management Company entitlement to two one-time bonuses, for a maximum amount of NIS 240 thousand each, and this depending on; for one of the bonuses, in the performance formula of the Bank's shares at the Stock Exchange in the period from the plan's approval until April 13, 2011. Concerning the other one-time bonus, it is dependent upon a capital issuance by the Bank at a price that will reflect a certain premium rate on the equity, as determined in the one-time bonus formula. It should be mentioned that, until April 13, 2011, there were no conditions for the aforementioned, and therefore, the Management Company is not entitled to grants specified in this Section.

5. Yearly bonus

The Management Company will be entitled to a yearly bonus, according to the yearly bonus programs that are an integral part of the management agreement ("Yearly Bonus Plan").

According to the yearly bonus plan, the Management Company will be entitled to a yearly bonus derived from the "calculated yield" as defined below and limited to the maximum of 24 monthly payments gross (that is, NIS 2,880 million) (hereinafter: "Yearly Bonus"). The yearly bonus will start at the height of three monthly gross payments (that is, NIS 360 thousand) (an average calculated yield and increase in capital of 9%) and until the maximum of 24 monthly payments as the aforementioned gross (average of 15%).

It should be mentioned that the bonus is listed in the plan as multiple monthly payment paid to the Management Company Derived from this, since the monthly amounts are linked as specified above, the minimum and maximum amounts of the bonus are linked to the index.

The annual bonus will be paid in stages over 3 years (50% in the first year and 25% in the second and third years), while the payment of each part of the annual bonus is contingent upon continued compliance with the goals during the year determined for payment. The actual payment of the annual bonus depends therefore on the year in which the payment should be implemented, that there will be no regulatory limitation and/or capital adequacy limit on dividend distribution at a rate of at least 33% of the net profit in the payment year to the Bank's shareholders. As far as the aforementioned limitation applies to the dividend distribution, the bonus payment will be deferred, in whole or in part, to a date on which the aforementioned limitation is removed.

In the event of partial payment capability of dividend, the dividend will be paid to the shareholders and the bonus, pro-rata, for the aforementioned limitation rate, and the payment of the balance of the bonus will be deferred to a date on which the regulatory and/or capital adequacy limitation is removed. It should be mentioned that the Bank of Israel expressed its reservations in relation to the aforementioned section that reflects the correlation between inability to pay a dividend due to regulatory limitations and/or capital adequacy and payment of the bonus. The Chairman of the Board of Directors in his letter to the Bank of Israel from August 11, 2011, notified the Bank of Israel that the aforementioned reservations were noted, and that the Board of Directors of the Bank will operate in accordance with the position of the Bank of Israel on this issue, and if necessary will contact them. It is clarified that as aforementioned no actual change was made to the agreement.

“Calculated yield" meaning “reported yield" as per definition below, excluding the affect of the aforementioned venture hereinafter.

“Reported yield" is defined as the average between the annual yield (net) on equity as reported in the Bank’s annual audited Financial Statements and the growth rate in the Bank’s equity as reported in the Bank’s annual audited Financial Statements. A dividend announced and paid during the year and capital issuances, if there were any, will be neutralized for the purpose of calculating the growth in equity (meaning, it will not be taken into account for the purpose of calculating equity growth rate).
In the calculation of the annual yield, one-time profits (financial profits such as nostro will not be considered one-time), as well as capital gains (with the exception of potential capital gain from the sale of certain real estate property defined in the plan, and that did not deviate from the calculation of the yield) will be neutralized. In calculating the growth in capital, the capital issues will be neutralized. The manner in which these elements will be neutralized will be reviewed by an external, independent auditor whose identity was defined in the plan.

A project was defined in the plan for establishing and operating new retail banking for the Bank ("the Project”), and it was decided that during the period between the project’s approval by the Board of Directors and until the date when project activity will be profitable from an accounting aspect; the project implications will be neutralized from the bonus formula components (the captive project capital will be neutralized from the denominator of yield formula for capital; the income and expenses related to the project, such as the tax shield created by it, will be neutralized from the numerator in capital yield calculation for the purpose of determining the bonus amount). Implementation of the formula will be controlled and examined by independent factors as mentioned above.

Note 22 – Stakeholders and Related Parties (consolidated) (1) (continuation)

F – Employment terms of the Chairman of the Board of Directors

On October 3, 2011, the General Assembly approved the appointment of Mr. Ze'ev Gutman (hereinafter: "Mr. Gutman" or the "Chairman") as director at the Bank as well as the employment terms as the Bank's designated Chairman of the Board of Directors, after approval of the terms of the agreement, approval of the Audit Committee in their meeting of June 20, 2011, and later the Board of Directors in their meeting on July 17, 2011, was obtained.

On October 27, 2011, the Board of Directors of the Bank decided to appoint Mr. Gutman as Chairman of the Bank's Board of Directors. An Immediate Report regarding the terms of the agreement with the Chairman of the Board of Directors was given as part of the Immediate Report on the summons of the General Assembly from September 4, 2011, and its amendment from September 26, 2011.

Below are the principle terms of the agreement:

1. The services will be provided to the Bank by the Chairman in a standard agreement between the ordering party and the independent contractor and this through the company controlled by the Chairman. Based on this formula, the consideration is determined for these services to the Bank. There will be no employer-employee relationship between the Chairman and the Bank.

   In the event in which instructions will be given on this issue by the Bank of Israel and/or other authorized authority, prohibiting providing services by management companies, the terms on this agreement will be terminated and at the same time the Chairman will be employed for all purposes as a Bank employee. In this event, the employment terms will be adjusted so that the economic situation of the Chairman will not change positively or negatively following this change. So far as there will not be agreement on this issue, the employment terms of the Bank employee will be determined by an accountant agreed upon by the parties.

2. The consideration for the services will be as follows: a fixed monthly amount of NIS 108,340 (one hundred and eight thousand, three hundred and forty NIS), with addition of VAT by law (hereinafter: "the Monthly Consideration"). The monthly consideration will be updated monthly according to the change in the CPI, as specified in the terms of the agreement.

   Should it be that for a given fiscal year, the Bank's annual net profit according to its annual audited statements, will exceed NIS 61 million, the monthly consideration will increase by 10%. It is clarified that if after the above mentioned update in any tax year, the net annual profit of the Bank will be less than NIS 61 million – the monthly consideration will be reduced by 10%. The increase or decrease of the monthly consideration will be implemented one month after the publication of the audited annual Financial Statements of the Bank, and will be applied from that period onwards, without retroactive application. In any case, the monthly consideration will not be reduced from the fixed monthly consideration in the above section and will not exceed 10% of the updated monthly consideration (for the purpose of clarification – if during two consecutive years the annual net profit of the Bank according to its annual audited statements, will exceed NIS 61 million, the monthly consideration will increase by 10% only once). This update mechanism will be applied starting from the publication of the bank's audited reports for 2012.

3. Vacation extending up to 30 days for the full calendar year, as well as absence due to illness to the extent of up to 30 days during a full calendar year, will not cause a decrease of the monthly consideration.

4. The Bank will bear all current expenses involved in providing the services, and against the presentation of receipts (when they do not come directly to the Bank), including vehicle and telephone.

5. The Chairman will be entitled to be included in the compensation plan for members of Management, which establishes parameters and thresholds for receiving the yearly bonus, that was approved by the Bank's Board of Directors on November 25, 2010 (hereinafter: "the Plan"). In accordance with the terms of the agreement, this Plan will be subject to the provisions of the Plan subject to the parameters and designated grades established for the Chairman, as detailed below.

   Should the Bank comply with the threshold for bonus payments, as established in the plan, the Chairman will be entitled to an annual bonus payments according to grades, as follows:

"Calculated yield" *	Bonus sum (in NIS)
up to 9% (not inclusive)	-
9% and up to 10%	100,000
Over 10% and up to 11% inclusive	120,000
Over 11% and up to 12% inclusive	140,000
Over 12% and up to 13% inclusive	170,000

* As defined above in Section D

Should the Bank comply with the threshold for bonus payments, as determined in the plan, the Chairman will be entitled to annual bonus payments contingent on a calculated minimum yield of 9%. The annual bonus is applied from a level of NIS 100,000 + VAT (with a calculated yield of 9% and higher) and up to a maximum sum of NIS 530,000 + VAT per calendar year, and this also in the event that according to the Bank's business results, the Chairman will be entitled to payment of a greater bonus.

The bonus will be paid on dates and in compliance with the terms established in the plan. It should be mentioned that, according to the plan, the bonus for bank managers will be paid in stages over three years from the date of eligibility(60% per eligible year and 20% for one and two years after the date of eligibility), while the payment of each part of the annual bonus is contingent upon continuous compliance with the goals during the year established for payment.

The actual payment of the annual bonus therefore depends on the year in which the payment should be made, that there will be no regulatory limitation and/or capital adequacy limit on dividend distribution at a rate of at least 33% of the net profit in the payment year for the Bank's shareholders. As far as the aforementioned limitation applies to the dividend distribution, the bonus payment will be deferred, in whole or in part, to a date on which the aforementioned limitation is removed. In the event of partial payment capability of dividend, the dividend will be paid to the shareholders and the bonus, pro-rata, for the aforementioned limitation rate, and the payment of the balance of the bonus will be deferred to a date on which the regulatory and/or capital adequacy limitation is removed.

At this stage, and according to the plan, the instruction of the above section will not be implemented due to objections by the Bank of Israel to the paragraph expressing the relation between incapability to paying a dividend because of regulatory and/or capital adequacy limitation and between paying a bonus given in relation to the terms of employment of the Bank's CEO (see details on the aforementioned objections and the letter from the Chairman of the Board of Directors of August 11, 2010, to the Bank of Israel on August 11, in describing the CEO's employment terms).

6. The Chairman will also be entitled to a special bonus – in addition to the yearly bonus as said in Section (E) above, and without derogating from it, if according to the annual audited statements of the Bank the annual yield (net) of the Bank on equity will be at least 9% – Then accordingly and subject to the required approvals according to the provisions of the law, the Chairman will be paid a special bonus and this in consideration

of his special contribution to the Bank's profitability. The scope of the special bonus is at the sole discretion of the Bank's Board of Directors, and approval of the General Assembly, and will be paid on the date of the yearly bonus payment.

7. Each party may terminate the agreement at any time, pursuant to having issued written notice three months in advance. At the end of the term of the agreement, the Chairman will be subject to various limitations for the periods and terms as specified in the terms of the agreement. Should an announcement of termination of the agreement be given before 12 months have passed from the start of the agreement period, then for two months following the end of the period of the early announcement, the Chairman shall not be employed by an other bank in Israel, pursuant to the Bank continuing to make full payments owed to the Management Company in accordance with the agreement between the parties.

Note 22a – Share-based Payment Transactions

1. CEO

A. The CEO is entitled to two types of options – units from type A and units from type B. The quantity of options units from type A will change according to the yield of the Bank's shares as specified below: starting from 70,518 units for each unit, in case that the yield of the Bank's share from the employment starting date until the option units exercise date, reflect annual yield at a rate of up to and including 6.5% above the basic share price of NIS 8.6 per share, and up to 423,106 units per portion; in the event that the yield of the Bank's shares from the employment starting date until the exercise date of the options units reflect an annual yield at a rate above 9% above the basic share price of NIS 8.6 per share. The quantity of option units from type B will be 282,071 units per portion.

B. The options will mature and will be able to be exercised in 5 yearly increments, with the first one maturing on the employment starting date of the CEO in the Bank and the fifth maturing 4 years after the employment starting date of the CEO at the Bank. The options may be exercised for a period of 72 months from the maturity date of each share, subject to provisions of the agreement.

C. Addition to the exercise of each option unit of type A is in the range between NIS 8.6 for the first unit up to NIS 10.8 for the fifth unit, bearing compound interest at annual rate of 4% from the maturity date and until the fifth date; and additional exercise for each option unit of type B will be in the range between NIS 10.3 for the first unit up to NIS 12.5 for the fifth unit, bearing compound interest at an annual rate of 3% from the maturity date and up to the fifth date, everything subject according to the specified in the agreement.

D. Each option unit provides the CEO the right to receive, after exercise, a consideration that reflects the difference between the average price of the Bank's shares during the 30 business days prior to the exercise date and between the exercise increment.

E. In the event of termination of employer-employee relationship between the Bank and the CEO, the matured options may be exercised within 180 days from the termination date of the employer-employee relation, if not otherwise expired.

F. In the Financial Statements of the Bank from December 31, 2012, receipts for options of the Bank's CEO were recorded for a total of NIS 0.8 million (2011-NIS 0.9 million). The estimated economic value of the options that are calculated by the external assessor while using the binomial model is assessed at approximately NIS 4.2 million. On the bonus date, and until February 27, 2011, the Bank's Board of Directors had not yet decided on the manner for granting the options to the Bank's CEO, whether as part of clearance plan in capital instruments with replacing the clearance in cash and whether as part of a cash clearance plan. As a result thereof, and lacking the capability of the Company's Board of Directors to determine that clearance of the options will be made through capital instruments, the company handled the aforementioned granting as a bonus cleared in cash as defined in the International Financial Reporting Standards number 2. As a result, the company measured in each reporting period the fair value of the liabilities while the changes were reflected in the Profit and Loss Statement and this in consideration of the maturity period.

G. On February 27, 2011 the Bank's Board of Directors decided that the options granted to the CEO of the Bank will be cleared in capital instruments. Therefore, on the same day the Company classified the liabilities for the options of the CEO as capital and this according to the fair value of the same day.

The calculation of the estimated economic value for the aforementioned date was based on the following main parameters:
Standard deviation of annual yield: between 27% to 30%.

Risk-free interest rate: between 4.5% to 5.1%.

Share price: NIS 6.56.

2. Senior managers

A. Senior officers of the Bank for whom, on November 29, 2011, were approved by the Board of Directors of the Bank, an allocation of phantom units (hereinafter: the "Managers") will be entitled to phantom units of two kinds – units of type A and units of type B. The quantity of options units from type A will change according to the yield of the Bank's shares as specified below: starting from 58,765 units for each share, in case the yield of the Bank's share from the employment starting date until the exercise date of the option units reflects annual yield at a rate of up to and including 6.5% above the basic share price of NIS 8.84 per share, and up to 352,589 units per portion, in the event that the yield of the Bank's shares from the employment starting date until the exercise date of the options units reflect a annual yield at a rate above 9% above the basic share price of NIS 8.84 per portion. The quantity of option units from type B will be 176,294 units per portion.

B. The phantom units will mature and can be exercised in 4 yearly portions while the first one will mature at on November 29, 2012 and the fourth will mature 3 years after this date. The phantom units may be exercised for a period of 48 months from the maturity date of each share, subject to instructions of the agreement.

Note 22a – Share-based Payment Transactions (continuation)

C. The increment to the exercise of each phantom unit of type A is in the range between NIS 9.37 for the first portion up to NIS 11.16 for the fourth portion, bearing a compound interest at annual rate of 4% from the maturity date and until additional exercise date for each phantom unit of type B will be in the range between NIS 11.14 for the first portion up to NIS 12.9 for the fourth portion, bearing a compound interest at an annual rate of 3% from the maturity date and up to the exercise date, everything subject according to the specified in the agreement.

D. The units are granted without any consideration.

E. The units may not be transferred, except in case of death or in case of legal incompetency.

F. The options plan provides a protection instruction for the exercise period, in case of distribution of benefit shares, distribution of securities through rights, changes in organizational structure of the Bank, as well as at any time in which a dividend is announced.

G. Each phantom unit provides the managers the right to receive, after exercise, a consideration that reflects the difference between the average price of the Bank's shares during the 30 business days prior to the exercise date and between the exercise increment.

H. In the event of termination of employer-employee relation between the Bank and the managers, the matured options may be exercised within 30 days from the ceasing date of the employer-employee relation, if not so they expire.

I. In the Financial Statements of the Bank for December 31, 2012, expenses for options of the Bank's CEO were recorded for a total of NIS 108 thousand (2011 – NIS 26 thousand). The estimated economic value of the options that was calculated by an external assessor while using the binomial model is assessed for December 31, 2012 at approximately NIS 0.3 million.
The calculation of the estimation of the economic value was based on the following main parameters:

Standard deviation of annual yield: between 24% to 29%.

Risk-free interest rate: between 2.3% to 3.2%.

Share price: NIS 4.96.

Note 23 – Income and Interest Expenses

Reported amounts in millions of New Shekels

	consolidated			The Bank		
	For the year ending on December 31					
	2012	2011	2010	2012	2011	2010
income from Interest						
from credit for the public	**510.1**	495.2	385.5	**510.1**	495.2	385.5
From deposits in the Bank of Israel and from cash	**8.2**	9.8	2.3	**8.2**	9.8	2.3
From deposits in banks	**0.7**	5.2	1.8	**0.7**	5.6	2.1
from debentures	**36.0**	47.8	36.9	**42.5**	52.9	41.2
from other assets	**0.7**	1.0	0.2	**0.5**	0.9	-
Total income from interest	**555.7**	559.0	426.7	**562.0**	564.4	431.1
Interest expenses						
on public deposits	**241.0**	262.3	198.4	**309.8**	357.5	276.2
On deposits from banks	**3.8**	5.0	5.4	**3.8**	5	5.4
For liability certificates and deferred liability notes	**80.0**	116.9	97.8	**24.2**	35.6	32
For other liabilities	**-**	-	0.5	**-**	-	0.5
Total interest expenses	**324.8**	384.2	302.1	**337.8**	398.1	314.1
Total Income from Interest, net	**230.9**	**174.8**	**124.6**	**224.2**	**166.3**	**117.0**
Details of the net effect of derivative instruments on income and expenses from interest						
Interest expenses	**(1.2)**	-	-	**(1.2)**	-	-
Itemization of income from interest based on accrual from debentures						
Available for sale	**29.9**	43.1	36.0	**36.3**	48.4	40
For trade	**6.1**	4.7	0.9	**5.9**	4.7	1.2
Total included in income from interest	**36.0**	47.8	36.9	**42.5**	53.1	41.2

Note 24 – Non-Interest Financing Income

Reported amounts in millions of New Shekels

	consolidated			The Bank		
	For the year ending on December 31					
	2012	**2011**	**2010**	**2012**	**2011**	**2010**
A. Non-interest financing income for activities not for trade purposes						
1. From activities with derivative instruments						
Income net, due to derivative instruments ALM	**15.6**	(15.2)	(3.0)	**15.6**	(15.2)	(3.0)
2. Rate differentials, net (without effect of derivatives)	**(15.3)**	17.4	4.7	**(15.3)**	17.4	4.7
3. From investment in debentures						
Profits from the sale of available for sale debentures.	**20.5**	4.5	22	**19.7**	4.5	19.7
Losses from the sale of available for sale debentures	**(10.2)**	(6.4)	(4.4)	**(9.9)**	(5.7)	(3.6)
Total from investment in debentures	**10.3**	(1.9)	17.6	**9.8**	(1.2)	16.1
4. Other Financing Income	**1.0**	3.9	0.7	**1.0**	3.9	0.4
B. Non-interest financing income for activities for trade purposes						
Net income for other derivative instruments	**(3.8)**	(0.4)	-	**(3.8)**	(0.4)	-
Profits that were realized and that have not yet been realized from reconciliations For fair value of debentures for trade net(2)	**14.8**	2.3	4.5	**14.8**	2.3	4.5
Total from activities for trade	**11.0**	1.9	4.5	**11.0**	1.9	4.5
Total Non-Interest Financing Income	**22.6**	6.1	24.5	**22.1**	6.8	22.7

(1) Derivatives are part of the Bank's management system of assets and liabilities, that are not designated for hedging relations. Of these differences in ALM derivative rate for December 31, 2012, 2011, and 2010, in the Bank and consolidated, NIS 15.6 million, NIS (20.3) million, NIS (5.5) million, respectively.

(2) Of this some of the profits and losses related to debentures for trade that are still being held on the balance sheet date in the Bank and consolidated for December 31, 2012, 2011, and 2010, of NIS 8.8 million, NIS 1.8 million and NIS 0.4 million, respectively.

Note 25 – Commissions

Reported amounts in millions of New Shekels

	consolidated			The Bank		
	For the year ending on December 31					
	2012	**2011**	**2010**	**2012**	**2011**	**2010**
Credit processing	**20.5**	19.5	21.1	**20.5**	19.5	21.1
Net income from credit portfolio service	**17.0**	18.4	20.0	**17.0**	18.4	19.9
Commission from Project Oversight	**13.4**	9.8	7.3	**13.4**	9.8	7.4
Commission from life insurance	**10.5**	11.1	11.8	**6.4**	7.4	8.5
Conversion differences*	**9.4**	9.6	9.2	**9.4**	9.6	9.2
Activity in securities	**7.8**	10.0	15.4	**6.6**	8.2	11.7
Commissions for financing business*	**3.9**	4.9	5.4	**3.9**	4.9	5.4
Commissions from property insurance	**3.5**	4.5	5.2	**-**	-	-
Fees for distribution of financial products*	**1.5**	1.4	1.1	**1.5**	1.4	1.1
Credit cards	**0.7**	0.9	0.8	**0.7**	0.9	0.6
Account management	**0.3**	0.3	0.3	**0.3**	0.3	0.3
Foreign trade activity	**0.1**	0.1	0.1	**0.1**	0.1	0.1
Other commissions*	**1.6**	1.4	1.2	**1.5**	1.4	1.4
Total commissions	**90.2**	91.9	98.9	**81.3**	81.9	86.7

* Reclassification.

Note 26 – Other Income

Reported amounts in millions of New Shekels

	consolidated			The Bank		
	For the year ending on December 31					
	2012	**2011**	**2010**	**2012**	**2011**	**2010**
Capital gain from sales of buildings and equipment(1)	**-**	25.4	-	**-**	-	-
Others	**0.6**	0.1	0.6	**0.1**	0.1	0.6
Total other income	**0.6**	25.5	0.6	**0.1**	0.1	0.6

(1) For more information – see Note 8.

Note 27 – Salaries and Accompanying Expenses

Reported amounts in millions of New Shekels

	consolidated			The Bank		
	For the year ending on December 31					
	2012	2011*	2010*	2012	2011	2010
Salaries*	**95.1**	92.1	81.0	**83.6**	83.8	73.3
National Insurance and Payroll Tax	**21.5**	19.4	19.6	**20.7**	18.6	19.0
Severance pay, benefits, education funds and vacation	**19.7**	21.0	17.1	**17.5**	18.8	16.0
Expenses derived from share-based payment transactions **	**0.8**	0.8	2.3	**0.8**	0.8	2.3
Other accompanying expenses*	**0.7**	0.8	0.7	**0.6**	0.6	0.3
Total salaries and accompanying expenses	**137.8**	134.1	120.7	**123.2**	122.6	110.9

* Reclassification

* From this: NIS 0.8 million in 2012 (2011 – NIS 0.8 million, 2010 – NIS 2.3 million); expense deriving from transactions handled as share-based payment cleared in capital instruments.

Note 28 – Other Expenses

Reported amounts in millions of New Shekels

	consolidated			The Bank		
	For the year ending on December 31					
	2012	2011	2010	2012	2011	2010
Computer*	**21.8**	16.1	15.2	**52.8**	34.8	32.0
Professional Services	**10.1**	8.2	9.7	**9.4**	7.2	7.6
Marketing and Publication	**12.2**	5.9	3.5	**12.2**	5.8	3.4
Vehicle Maintenance*	**4.6**	4.5	3.7	**4.0**	3.9	3.3
Telephone Call Center	**3.4**	-	-	**3.4**	-	-
Training and Training Courses	**3.2**	3.0	2.5	**3.2**	3.0	2.5
Communications	**3.0**	3.1	3.2	**2.8**	3.0	3.1
Fees*	**2.2**	1.8	2.0	**2.0**	1.6	1.8
`Salary of members of the Board of Directors that are not employed by the Bank	**1.9**	1.7	1.8	**1.8**	1.6	1.6
Office Expenses	**1.8**	1.6	1.6	**1.7**	1.6	1.6
Insurance	**1.4**	1.5	1.6	**1.4**	1.4	1.6
Other Expenses*	**4.2**	4.0	8.2	**4.1**	3.9	8.2
Total Other Expenses	**69.8**	51.4	53.0	**98.8**	67.8	66.7

Note 29 – Provision for Taxes on Profit

Reported amounts in millions of New Shekels

a – Composition of provision for taxes on profit

	consolidated			The Bank		
	For the year ending on December 31					
	2012	2011	2010	2012	2011	2010
Current taxes –						
For book year	**35.8**	12.2	11.0	**32.5**	4.7	7.6
For previous years	**(0.1)**	-	(1.9)	**-**	-	(1.9)
Total current taxes	**35.7**	12.2	9.1	**32.5**	4.7	5.7
Deferred Taxes – (deduction) / addition:						
For book year	**(11.7)**	2.4	4.9	**(11.2)**	3.3	4.7
For previous years	**(6.3)**	-	-	**(6.3)**	-	-
Total deferred taxes	**(18.0)**	2.4	4.9	**(17.5)**	3.3	4.7
Provision for income taxes	**17.7**	14.6	14.0	**15.0**	8.0	10.4

Note 29 – Provision for Taxes on Profit (continuation)

Reported amounts in millions of New Shekels

b – Reconciliation between the theoretical tax amount on which regular profit from activities was applied, was charged with tax according to the statutory tax rate applied in Israel on the Bank and between the tax provision on regular profits from activities as reflected in the Profit and Loss Statement.

	consolidated			Bank		
	For the year ending on December 31					
	2012	**2011**	**2010**	**2012**	**2011**	**2010**
Profit before tax	**53.8**	60.1	48.1	**36.1**	22.2	29.7
Statutory tax rate applied on the Bank of Israel	**35.53%**	34.48%	35.34%	**35.53%**	34.48%	35.34%
Tax amount based on the statutory tax rate	**19.1**	20.7	17.0	**12.8**	7.7	10.5
Tax (tax savings) for:						
General provision and addition to credit losses	**-**	(0.5)	(0.4)	**-**	(0.4)	(0.4)
Other unrecognized expenses	**0.9**	0.7	1.3	**0.9**	0.7	1.3
Exempt income and with limited tax rate	**(1.1)**	(4.6)	(0.9)	**-**	-	(0.1)
Taxes for previous years	**(0.1)**	-	(1.9)	**-**	-	(1.9)
Changes in deferred tax balance following change in tax rate	**(0.5)**	(1.5)	(0.1)	**(0.5)**	(1.6)	(0.1)
Income of subsidiaries in Israel	**(1.8)**	(1.1)	(1.7)		-	-
Others provisions	**1.2**	0.9	0.7	**1.8**	1.6	1.1
Provision for income taxes	**17.7**	14.6	14.0	**15.0**	8.0	10.4

Note 29 – Provision for Taxes on Profit (continuation)

Reported amounts in millions of New Shekels

c – Assessments

The bank issued final assessments until and including the year 2007. For its two subsidiaries, final tax assessments have been issued up to and including the 2005 tax year. Tax assessments in subsidiaries up to and including 2008, are considered final.
The current and deferred taxes are calculated according to the new tax rates.

d – Deferred receivable tax balance and reserve for deferred taxes

	consolidated				Bank			
	For the year ending on December 31							
	2012	2011	2012	2011	2012	2011	2012	2011
	in millions of NIS		Average tax rate		in millions of NIS		Average tax rate	
Receivable deferred taxes:								
for timing differences:								
Provision for vacation and jubilee grant	**3.1**	2.8	35.2%	34.6%	**2.8**	2.5	35.9%	35.2%
Surplus reserve for severance pay on fund	**0.6**	2.5	36.1%	35.3%	**0.4**	2.4	35.9%	35.3%
Securities	**-**	-	-	35.4%	**2.2**	3.0	35.9%	35.1%
Liability certificates and deferred liability notes	**0.6**	1.2	35.9%	35.1%	**-**	-	-	-
From Provision for Credit Losses	**25.4**	12.3	35.9%	35.1%	**25.4**	12.3	35.9%	35.1%
from interest that is not reflected in this year income	**0.8**	-	35.9%	35.1%	**0.8**	-	35.9%	35.1%
For reconciliation of non-financial assets and others	**4.5**	4.4	30.4%	35.1%	**4.7**	4.8	35.9%	35.1%
Total receivable deferred taxes	**35.0**	23.2	35.0%	35.3%	**36.3**	25.0	35.9%	35.1%

Remark: Exercising the net receivable deferred taxes is based on the forecast according to which the revenue is charged, in the future, with suitable tax amounts.

Note 29 – Provision for Taxes on Profit (continuation)

Reported amounts in millions of New Shekels

e – Tax rate applied on the Bank and its subsidiaries

The bank is defined as a "financial institution" for purposes of the Value Added Tax Law 5736-1975, and as such is subject to payroll tax and profit tax on its activities according to the rates determined by the VAT Law.

According to the VAT Order (Tax Rate on Non-Profit Organizations and Financial Institutions) (temporary order), 5769 - 2009, which was approved by the Knesset in December 2010, the Income Tax Rate applied on the financial institutions will be 16% between 2010-2012.

In August 2012, the VAT Order (Tax Rate on Non-Profit Organizations and Financial Institutions) (Amendment), 5772 - 2012, which was approved by the Knesset in December 2010, determined that the Income Tax Rate that applied to financial institutions will be 17% of the generated profit. The provision regarding tax on profit in 2012 will apply to one-third of the products in that year. Said order canceled the temporary order.

On December 5, 2011, the Knesset Passed the Law for Changing the Tax Burden (Legislative Amendments), 5772 - 2011 (hereinafter: the Law). As part of the law, inter alia, beginning from 2012, outlining the reduction in corporate tax rate was canceled. As part of the law, the corporate tax was also increased to a rate of 25% as of 2012. In view of the increase of the corporate tax to 25%, as aforementioned, the tax rate of real capital gain and the real credit tax were also correspondingly increased.

Listed below are the statutory tax rates that apply to financial institutions, including the Bank:

year	Tax rate Companies	Tax rate Profit	Tax rate Total
2010	25%	16.00%	35.34%
2011	24%	16.00%	34.48%
2012	25%	16.33%*	35.53%
2013 and henceforth	25%	17.00%	35.90%

* Weighted rate

The effect of the mentioned changes on the deferred tax balance, resulted in an increase in the deferred tax balance by NIS 0.4 million. Updating of the deferred tax balance, resulted in an increase in net profit in 2012, of approximately NIS 0.5 million and a decrease in total profit after 2012, of approximately NIS 0.1 million.

* Reclassification.

Note 30 – Activity Sectors (consolidated)

A. General

The Bank of Jerusalem Group operates through the Bank's headquarters, its branches and subsidiaries. The Bank's activity sectors are classified according to the directives from the Supervisor of Banks according to the type of customers included in each of these sectors and do not necessarily match the Bank's organizational structure.

The Bank operates and provides various banking services in four main activity sectors. Below are details on the reported activity sectors:

Household sector

Sector customers are households and small businesses with characteristics similar to that of households.

Private Banking Sector

This segment includes customers with a medium to high level of financial wealth, and services are provided through a branch specializing in private banking, mainly for foreign residents (mostly from North America, England and France).

Business Sector

Customers in this sector are construction and real estate companies, business customers, corporations, and associations.

Financial Management Sector

This sector includes the Bank's available financial capital and positions, management of the Bank's nostro portfolio, activity vis-a-vis banks in Israel and abroad, as well as implementation of transactions in derivative financial instruments.

Non-allocated amounts and reconciliations

Including investment in trust funds and capital gain from sales of Property, Plant and Equipment, if there was any. Furthermore, the sector includes impairment provision for Property, Plant and Equipment, is there was any. In 2011, capital gain from the sale of structure was recorded for the total of NIS 20.8 million.

B. The principle regulations implemented in distribution of activity results between the various sectors:

Income from Interest, net

From the profit obtained from the provision between the credit interest provided to the sector's customers and the price of cash (economic transfer price adjusted to the linked sector and the average credit duration).

This profit includes financial expenses between the sectors – debt of the sector providing the loan and credit of the sector raises the deposit in the transfer prices (the income will be increased accordingly in the sector, which raises the deposits, and on the other hand, it decreases the income for the sector using the credit).

Non-Interest Income

Income not from interest was directly attributed to the sector in which the customers' activity is classified.

Expenses for Credit Losses

The provision was attributed to the activity sector in which the customer's activity is classified for which the provision was implemented. In a similar way, collection from implemented provision or reduction is also attributed to the sector for which the customer's activity is classified.

Operating and Other Expenses

Direct identifiable expenses are specifically attributed to the activity sector. The balance of indirect or direct expenses that are not accurately identifiable, are attributed according to model by which these expenses are attributed in compliance to the relative part of the direct service in that sector of the Bank's total service to each of the activity's sectors.

Taxes on Income

Taxes are calculated according to the effective tax rate and attributed accordingly to each sector.

Yield on Capital

The allocated capital to calculate the capital yield in each of the activity sectors was based on the average risk assets in each sector. Calculation of the yield for each sector was made according to the equity, as aforementioned, that is attributed to the sector.

Note 30 – Activity Sectors (consolidated) (continuation)

Reported amounts in millions of NIS

	For the year ending December 31, 2012					
	Households	Private Banking	Business	Financial Management	Non-allocated amounts and reconciliations	Total
	Millions of NIS					
Income from Interest, net:						
From Externals	188.0	21.5	38.5	(17.1)	-	230.9
Inter-sectoral	(14.6)	(2.4)	(5.0)	22.0	-	-
Income that is not from External Interest	56.8	11.6	22.4	22.6	-	113.4
Total Income	**230.2**	**30.7**	**55.9**	**27.5**	**-**	**344.3**
Expenses for Credit Losses	(33.4)	(0.6)	(2.0)	-	-	(36.0)
Operational and other expenses with the exception of depreciation and amortization:	(177.6)	(24.0)	(29.6)	(5.6)	-	(236.8)
Depreciation and Amortization	(13.3)	(2.1)	(2.1)	(0.2)	-	(17.7)
Profit before tax	**5.9**	**4.0**	**22.2**	**21.7**	**-**	**53.8**
Provision for taxes on profit	(2.2)	(1.2)	(7.2)	(7.1)	-	(17.7)
Net profit	**3.7**	**2.8**	**15.0**	**14.6**	**-**	**36.1**
Capital yield (average net profit rate from equity)	**1.0%**	**4.3%**	**10.2%**	**30.1%**	**-**	**5.4%**
Average balance from assets	7,028.7	1,192.6	1,311.9	1,955.2	-	11,488.4
Average balance of liabilities	6,292.4	1,119.7	3,405.1	70.2	-	10,887.4
Average balance of risk assets	4,380.2	653.1	1,527.4	509.2	-	7,069.9
Average balance of securities	1,476.0	263.7	247.8	-	-	1,987.5
Average balance of other assets under management	2,310.0	-	72.7	-	-	2,382.7
From profit from credit provision activities	135.7	13.1	28.8	(14.5)	-	163.1
From profit from the activity of receiving deposits	17.9	6.0	5.6	-	-	29.5
Other	19.8	-	(0.9)	19.4	-	38.3
Total income from interest	**173.4**	**19.1**	**33.5**	**4.9**	**-**	**230.9**

Note 30 – Activity Segments (consolidated) (continuation)

Reported amounts in millions of New Shekels

	For the year ending on December 31, 2011 *					
	Households	Private Banking	Business	Financial Management	Non-allocated amounts and reconciliations	Total
	Millions of NIS					
Income from Interest, net						
From Externals	161.6	17.7	39.6	(44.1)	-	174.8
Inter-sectoral	(20.7)	(3.0)	(8.3)	32.0	-	-
Income that is not from External Interest	61.8	10.0	20.1	6.2	25.4	123.5
Total Income	**202.7**	**24.7**	**51.4**	**(5.9)**	**25.4**	**298.3**
Expenses for Credit Losses	(20.4)	2.7	2.6	-	-	(15.1)
Operating and other expenses with the exception of depreciation and amortization	(152.6)	(20.6)	(32.5)	(4.4)	-	(210.1)
Depreciation and Amortization	(9.7)	(1.3)	(1.9)	(0.1)	-	(13.0)
Profit before tax	**20.0**	**5.5**	**19.6**	**(10.4)**	**25.4**	**60.1**
Provision for taxes on profit	(5.8)	(1.6)	(5.6)	3.0	(4.6)	(14.6)
Net profit	**14.2**	**3.9**	**14.0**	**(7.4)**	**20.8**	**45.5**
Capital yield (average net profit rate from equity)	**4.3%**	**7.4%**	**7.4%**	**(19.8%)**	**-**	**7.3%**
Average balance from assets	6,608.9	982.7	1,165.8	2,015.8	-	10,773.2
Average balance of liabilities	5,505.7	835.0	3,728.9	81.2	-	10,150.8
Average balance of risk assets	3,552.4	556.0	1,969.2	389.2	-	6,466.8
Average balance of securities	1,539.0	227.9	318.9	-	-	2,085.8
Average balance of other assets under management	2,601.6	-	125.9	-	-	2,727.5
From profit from credit provision activities	101.3	9.3	24.2	(33.1)	-	101.7
From profit from the activity of receiving deposits	17.7	5.4	7.1	-	-	30.2
Other	21.9	-	-	21.0	-	42.9
Total income from interest	**140.9**	**14.7**	**31.3**	**(12.1)**	**-**	**174.8**

* Reclassification.

Note 30 – Activity Sectors (consolidated) (continuation)

Reported amounts in millions of NIS

	For the year ending on December 31, 2010					
	Households	Private Banking	Business	Financial Management	Non-allocated amounts and reconciliations	Total
	Millions of NIS					
Income from Interest, net:						
From Externals	111.2	13.7	37.9	(38.2)	-	124.6
Inter-sectoral	(18.9)	(2.8)	(8.1)	29.8	-	-
Income that is not from External Interest	72.2	11.1	21.9	18.3	0.5	124.0
Total Income	**164.5**	**22.0**	**51.7**	**9.9**	**0.5**	**248.6**
Expenses for Credit Losses	(1.4)	-	4.0	-	-	2.6
Operating and other expenses with the exception of depreciation and amortization	(136.8)	(18.3)	(33.7)	(4.0)	-	(192.8)
Depreciation and Amortization	(7.5)	(1.1)	(1.5)	(0.2)	-	(10.3)
Profit before tax	**18.8**	**2.6**	**20.5**	**5.7**	**0.5**	**48.1**
Provision for taxes on profit	(5.4)	(0.7)	(6.0)	(1.7)	(0.2)	(14.0)
Net profit	**13.4**	**1.9**	**14.5**	**4.0**	**0.3**	**34.1**
Capital yield (average net profit rate from equity)	**4.0%**	**2.8%**	**7.3%**	**15.2%**	**-**	**5.5%**
Average balance from assets	5,755.4	852.9	1,262.8	1,589.0	-	9,460.1
Average balance of liabilities	4,802.7	729.1	3,279.1	86.0	-	8,896.9
Average balance of risk assets	3,040.8	579.7	1,836.5	244.1	-	5,701.1
Average balance of securities	1,545.0	207.6	265.7	-	-	2,018.3
Average balance of other assets under management	2,862.8	-	252.2	-	-	3,115.0
From profit from credit provision activities	62.7	8.0	22.7	(22.5)	-	70.9
From profit from the activity of receiving deposits	15.2	3.4	3.9	-	-	22.5
Other	14.4	(0.5)	3.2	14.1		31.2
Total income from interest	**92.3**	**10.9**	**29.8**	**(8.4)**	**-**	**124.6**

Note 31 – Information based on the Bank's Nominal Data

Reported amounts in millions of New Shekels

	December 31	
	2012	**2011**
Total assets	**12,572.9**	11,836.6
Total liabilities	**11,880.0**	11,193.5
Equity	**692.9**	643.1

	For the year ending on December 31	
	on December 31	
	2012	**2011**
Net profit	**36.3**	45.5

Note 32 – Significant Events during the Report Period

1. On May 15, 2012, an arrangement was signed with the Bank's former CEO Mr. Avi Bazura, regarding the termination of his employment. For more information, please see the Immediate Report from May 16, 2012 (reference number 2012-01-126258).

Note 33 – Events After the Balance Sheet Date

1. On January 7, 2013, Jerusalem Investment Portfolio Management Ltd., a wholly owned subsidiary, entered into an agreement with a third party not related to the Bank, for the sale of its portfolio management activity, as defined in the Regulation of Investment Advice, Investment Marketing and Portfolio Management Law 5755-1995 that is managed by it. The transaction is expected to be completed within several months in accordance with the mechanisms established in the agreement between the parties. It should be noted that the resulting income for the subsidiary from the activities being sold, as well as the consideration for said sale, is not material for the bank. (Reference 2013-01-008226).

Bank Branches and subsidiaries

Central Management
2 HaNegev Street, Airport City
Postal address: 2 Herbert Samuel Street, Jerusalem 91022

Business Department
HaNegev Street, Airport City

Private banking branch
18 Keren HaYesod Street , Jerusalem 992149

Jerusalem branch
2 Herbert Samuel Street, Jerusalem 91022

Geula branch
10 Yacov Meir Street, Jerusalem 95513

Tel Aviv branch
21 Ehad Ha'Am Street, Tel Aviv 65251

Be'er Sheva branch
90 Hadassah Street, Be'er Sheva 84221

Haifa branch
9 Pal-Yam Street (Zim House), Haifa 33095

Bnei Barak branch
2 Hazon Ish Street, Bnei Barak 51512

Ashkelon branch
5 Herzl Street, Ashkelon 78601

Ashdod branch
118 Shavi Zion Street, Ashdod 77273

Rishon LeZion branch
63 Herzl Street, Rishon LeZion 75267

Holon Branch
28 Sokolov Street, Holon 58256

Petah Tikwah branch
10 HaHaganah Street, Petah Tikwah 49591

Netanya branch
45 Herzl Street, Netanya 42401

Mode'in Elite branch
18 Avnei Nezer, Mode'in Elite

Pisgat Zeev branch
Moshe Dayan Blvd. 164, Jerusalem

Kiryon branch
195 Dereh Akko, Kiryat Bialik 27000

Nazareth branch
6092/50 El Riad Center, Nazareth 16000

Sakhnin branch
Sakhnin Mole Shopping Center, Sahknin Main Road

The Trust company of Bank of Jerusalem Ltd.
18 Keren HaYesod Street, Jerusalem 91079

Jerusalem Investment Portfolio Management Ltd.
21 Ehad Ha'Am Street, Tel Aviv 65251

Jerusalem Underwriting and Issuances Ltd.
2 Herbert Samuel Street, Jerusalem 91022

Jerusalem Financing and Issuances (2005) Ltd.
2 Herbert Samuel Street, Jerusalem 91022

Bank of Jerusalem

www.bankjerusalem.co.il