



Israel Securities Authority

Annual Report 2004

3rd Nissan 5765
12th April 2005

Mr. Benjamin Netanyahu
Minister of Finance
Ministry of Finance

MK Yakov Litzman
Chairman of the Finance Committee
The Knesset

Dear Minister of Finance,

Dear Knesset Member and Chairman,

Re: Report on the activities of the Securities Authority

In accordance with section 14 of the Securities Act, 5728-1968 (hereinafter: the Securities Act), I have the honor of submitting to you a report on the activities of the Securities Authority for 2004.

The year 2004 was characterized by an expansion of activity in the capital market. This expansion can be seen in the growth in the number of public offerings of securities, growth in the number of mutual funds, and growth in the number of investment advisers and portfolio managers active in the market. Expansion of activity this year was also characterized by the issue of new types of investment instruments – some of them complex since their financial analysis require the use of more advanced tools – and also by increased activity of new investors, including pension funds and foreign investors.

The year was dominated by the recommendations of the Inter-Ministerial Team, led by the Director General of the Ministry of Finance, Dr. Yossi Bechar, for structural changes in the capital market in Israel. The Authority was a full partner in drawing up these recommendations, and considers their full implementation of prime importance to contribute to refining the capital market and reinforcing competition in it.

2004 was also characterized by an expansion in the scope of the Authority's activity. This expansion was due to the growth in activity already mentioned, but above all to the new initiatives adopted by the Authority in the framework of implementing and executing the long term strategy defined at the end of 2002, as described below.

The strategy defined two objectives. One objective was to increase and refine activity in the capital market, while the second objective was to strengthen the public's trust in the reports of corporations by strengthening the control mechanisms operating in the market, and by the Authority's enforcement activity. The strategic plan was designed, first and foremost, to integrate the Israeli capital market in the globalization process of capital markets worldwide, including by adapting its regulation standard to the standard accepted in capital markets worldwide

The actions taken by the Authority this year to achieve the first objective continued to focus on strengthening competition, improving liquidity, and the aspiration to increase the market's total value. To that end, barriers hindering the access of corporations to the primary market were located and removed. This year two proposals for amendments to the Securities Act initiated by the Authority were approved. They concerned a fundamental reform of the ongoing reporting format of corporations and of the format of disclosure when offering securities by a prospectus. In the first stage of the reform, which began with publication of the periodic reports for 2004, comprehensive and thorough improvements were made in the scope and quality of monetary and non-monetary reporting of the corporations, in order to make them continuously available to the public. In the second stage of the reform, which is expected to start in 2005 together with the institution of regulations based on this Act, offerings of securities to the public based on a "shelf prospectus"

which relies on the ongoing reporting will be permitted. The shelf prospectus should encourage corporations to raise money in the capital market and make it a real alternative to raising funds from the banking system. I am convinced that competition over sources of money is the life blood of a properly ordered money market.

In 2004 exchange traded funds (Index linked certificates) with a total value of NIS397 million were issued. The exchange traded funds led to increased competition in the capital market, as they are an alternative to investing in mutual funds that follow the indices of similar securities, and contributed to a growth in liquidity in the market, and to a reduction in its fluctuations. In addition, structured bonds with a value of NIS3.914 billion were issued this year.

The Authority identified the complexity of these new instruments in the early stages, and therefore reinforced its supervision of disclosure in the prospectuses offering these exchange traded funds and bonds, and of the ongoing reporting of the corporations offering them to the public. These investment instruments are particularly complex, and the risks associated with investing in them are not always clearly visible. For this reason, the Authority worked hard this year to define a special disclosure format, particularly for the structured bonds, with the aim of reflecting the risks inherent in these investments more clearly.

Moreover, to broaden the supply of funding sources in the market and the range of investment instruments, the Authority submitted a number of proposals for amendments to the Joint Investment Trust Law, 5754-1994 which were designed to allow the establishment of mutual funds of new types, such as unique funds, which will be permitted to invest in hedge funds, and in a range of investment products in a growing market. The Authority also proposed making it easier for foreign trust funds to operate in Israel.

This year the Authority also worked on strengthening the trading infrastructures of the secondary market. A proposal to amend the Securities Act that was approved this year ensures the stability of the stock exchange clearing houses in the event of a member of a clearing house failing to meet its obligations towards it. This arrangement reflects the public interest in preferring market stability in the event of a fear for the stability of a member of a clearing house, in order to ensure public trust in the operation of the market.

The actions taken by the Authority to achieve its second objective, of ensuring public trust in the market and in corporate reporting, focused this year mainly on strengthening the control mechanisms operating in the market. Improving the Authority's powers of deterrence does not, in itself, secure the public's trust, and therefore the Authority must strengthen control mechanisms in the market and get involved where these powers are insufficient to secure the public interest. So, for example, in 2004 the Authority worked to improve disclosure of the activities of the boards of directors of the corporations, to the extent that they concern the monetary and non monetary reporting of those corporations. In this context, the Authority published guidelines concerning the disclosure requirements in the directors' reports regarding critical accounting estimates in their financial statements, and regarding the existence of directors with financial and accounting skill.

Increased supervision of the activities of control mechanisms in the market is compatible with the trends currently widespread in western capital markets, and fits in well with the Authority's view, which regards the integration of the Israeli capital market in the global capital market as very important. In view of this, a public committee has been appointed to examine the proper structure and format of a Code of Corporate Governance, for public corporations in Israel. Such a code means a collection of principles and rules that define how public corporations should conduct their affairs in terms of control and supervision ("Best Practice").

The year 2004 also marked a turning point in the enforcement of the provisions of the Regulation of Investment Advice and Portfolio Management Law, 5755-1995. This year the Authority devoted special resources to enforcing the provisions of this Law, in general, and in particular to enforcing the

provisions of the Law concerning investment advisers working in the banking system. The findings obtained show that actions taken to enforce the provisions of the Law have considerably increased the awareness of investment advisers to the duties imposed on them by this law to act solely for the good of their clients. In addition, the Authority initiated an amendment to the Regulations promulgated under this Law, stipulating that the structured deposits offered to the public, mainly by the banks, would be deemed for the purposes of this Law as a financial asset, and therefore they would be offered only by investment advisers.

In conclusion, in 2004 considerable resources were invested in regulating the market, including by setting new reporting rules and relaxing existing rules that acted as barriers to market activity, in particular with a view of integration in the globalization process of the capital markets.

In 2005, the Authority expects to invest a great deal of resources in continuing to implement its strategy of openness and globalization, and in enforcing the arrangements laid down by the securities laws to ensure public trust in the capital market. In particular, the authority will carry out broad and intensified enforcement activities to ensure that trustees are independent of the owners of bonds, and also to ensure the proper functioning of underwriters, trustees, auditing accountants, managers of mutual funds, corporate directors and so on.

The operation of these “doormen” is essential for securing public trust in the capital market, and if this exists, the market can continue growing and integrating with the global capital markets.

Yours truly,

Moshe Tery

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Chapter 1 - Functions of the Authority

Israel Securities Authority was established under the Securities Law, 5728-1968 ["Securities Law"], and its function, as stated in the law, is to protect the interests of the investing public. Under the framework of its mandate, the Authority deals, inter alia, with the following areas:

1. Granting permits to publish prospectuses in which companies offer securities to the public, and prospectuses in which mutual funds offer units to the public,
2. Checking the following reports filed by reporting bodies:
 - a. Immediate current reports, quarterly and periodic financial statements;
 - b. Reports on transactions between a company and a controlling shareholder therein;
 - c. Reports on private offerings in a company;
 - d. Specifications of purchase offers;
 - e. Current reports of mutual funds.
3. Regulating and supervising the activities of the mutual fund sector,
4. Supervision of the proper and fair management of the stock exchange,
5. Licensing portfolio managers and investment advisors, supervising compliance with responsibilities, and dealing with disciplinary violations,
6. Conducting investigations with regard to violations under the Securities Law, the Joint Investment Trust Law, 5754-1994 ["Joint Investment Trust Law"], Regulation of Investment Advice and Investment Portfolio Management Law, 5755-1995 ["Regulations of Investment Advice Law"] and violations of other laws where related to violations of said laws;
7. Supervision over compliance with responsibilities of portfolio managers and members of the stock exchange that are not banks, according to the Prohibition of Money Laundering Law, 5760-2000.
8. The Authority is a partner with the Institute of Certified Public Accountants in Israel, in the financing and operations of the Israel Accounting Standards Board. In accordance with instructions of the Government legal advisor, the Authority transferred its membership in the limited company, which is the administrative body for operations of the Accounting Standards Board, to a trust held by the Accountant General of the Ministry of Finance.

In accordance with Securities Law, the Minister of Finance appoints the Chairman of the Authority and its members. Some of the members are appointed from the public and some are civil servants; one of them is an employee of the Bank of Israel. The Authority employs accountants, lawyers, economists and administrative employees.

Chapter 2 - The Authority and its Employees

The members of the Authority at the end of December 2004 [Tevet 5765] were:

Mr. Moshe Tery, Chairman,
Ms. Michal Abadi-Boyanjo, Adv. [CPA],
Mr. Yehiel Gutman, Adv.,
Mr. Yossi Dolan, Adv.,
Dr. Moshe Druker, Adv. [CPA],
Ms. Daniella Yaron-Zoller, Adv.,
Ms. Drora Lifshitz, Adv.,
Mr. Moran Meiri, Adv.,
Dr. Meir Sokoler,
Mr. Tamir Forrer, Adv. [CPA],
Ms. Michaela Shamir-Chertoff, Adv.,
Mr. Sammy Tallawi, Adv.

The plenum of the Authority meets usually once a month. The Authority acts also through committees that deal with applications for permission to publish prospectuses, giving exemptions and extensions, stock exchange issues, issues relating to the Authority's finances and budget, the independence of auditors in companies subject to the Securities Law, issues relating to the licensing of investment advisors and investment portfolio managers, issues relating to civil fines for managers of mutual funds and other issues, as needed.

In 2004, the Authority held 11 meetings of the plenum - the committee for giving permits for the publication of prospectuses - 66 meetings; committees for giving exemptions - 25 meetings; the committee for stock exchange issues - 11 meetings; the finance committee – five meetings; the audit committee – three meetings; the committee for licensing investment advisors and investment portfolio managers – four meetings; a special committee authorized under section 117[b] of the Joint Investment Trust Law to consider not imposing civil fines under section 114 of the law – five meetings; the committee for the independence of auditors of companies subject to the Securities Law – one meeting.

Senior employees of the authority at the end of December 2004 [Tevet 5765] were:

Ms. Atalia Arad, Director of Investigations Department,
Mr. Meir Bacaleinic, Authority Secretary,
Daniella Gorny, Adv., General Counsel,
Pnina Guy, Adv., Director of Enforcement,
Mr. Aviezer Dannon, Director of the Intelligence Department,
Prof. Shmuel Hauser, Chief Economist,
Mr. Natan Hershkovitz, Director of Information Systems Department,
Lisa Haimovitz, Adv., Director of International Division Department and Senior Advisor to the Chairman,
Dr. Eyal Sulgenik, Director of Corporation Finance Department,
Ms. Sarah Parush, Director of Mutual Funds Supervision Department,
Mr. Ori Katzir, Spokesman,
Ms. Ita Shochat, Director of Licensing and Supervision over Investment Advisors and Portfolio Managers Department.

At the end of December 2004 [Tevet 5765] 125 positions were filled, as follows:

| | | | |
|---|---|------|------------|
| The Chairman's office | - | 4 | positions, |
| General Counsel | - | 2 | positions, |
| Corporation Finance Department | - | 27.8 | positions, |
| Mutual Funds Supervision Department | - | 10.5 | positions, |
| Licensing and Supervision of Investment Advisors and Investment Portfolio Managers | - | 8.5 | positions, |
| Enforcement ¹ | - | 24.6 | positions, |
| Investigations, Intelligence | - | 28.3 | positions, |
| Economic Department | - | 3 | positions, |
| Information systems | - | 4 | positions, |
| Secretarial and Administrative | - | 12.3 | positions, |

The maximum manpower approved at the end of December 2004 was 130 positions.

The maximum manpower approved also includes lawyers who are employed by the Authority in order to assist the State Attorney's office in carrying out its functions in matters relating to the Securities Authority. In this respect, the Authority funds 14 lawyers, and five articulated clerks in the various departments of the State Attorney's office.

The budget of the Authority is funded by annual fees payable by companies that are subject to the Securities Law and the Joint Investment Trust Law, by fees payable for applications to receive a permit to publish prospectuses and private offerings, by the licensing fees of investment advisors and investment portfolio managers, and by fees charged to the Tel Aviv Stock Exchange. The budget is approved by the Minister of Finance and the Finance Committee of the Knesset.

¹ Including lawyers employed by the Authority

Chapter 3 - Departments of the Authority

Intelligence

The function of the department is to locate and expose criminal activity in the capital markets in order to forestall it, in so far as possible, or in order to adopt enforcement measures. In addition, the department channels information, when this is needed, to various departments of the Authority. This information assists the other departments in carrying out their duties.

The department carries out ongoing activity of collecting information from various different sources relating to the capital markets. The information is examined, analyzed and assessed by members of the department, using computer systems and databases in Israel and abroad. As a result of the initial assessment, further intelligence actions are taken, if necessary, to corroborate, authenticate or refute the information that was examined, while ensuring the secrecy of the investigation and its nature.

The collection, analysis and assessment of data is done in order to determine if there is a prima facie suspicion of a breach of provisions of the laws that the Authority is responsible to enforce, and in order to identify the parties who are suspected of the breach. If evidence is found to support such a suspicion, the facts and the legal basis for supporting the suspicion are presented to the Authority's chairman, together with a recommendation to refer the handling of the suspicions to the investigations department, or, alternatively, to adopt other enforcement measures.

Enforcement

The task of the department is to examine events and cases that are discovered in the course of the Authority's current work, or from other sources, which justify the Authority taking enforcement measures.

The department also deals with giving legal guidance for the work of the Investigations Department, coordinating between the departments of the Authority on matters where enforcement is required, maintaining contact between the Authority and the State Attorney's office regarding investigations and filing indictments, assisting in the criminal proceedings until their completion, and maintaining contact and assisting also in other legal proceedings in which the Authority is a party that are being handled by the Tel-Aviv District-Attorney [Civil] or by the State Attorney.

In addition, the personnel of the enforcement department take part in meetings on legislation in the field of enforcement, mainly criminal enforcement, both in the Ministry of Justice and in the Knesset; they participate in various economic enforcement forums - meetings and activities of senior personnel in the bodies that investigate economic violations, whose purpose is to discuss joint issues and to solve joint problems. The enforcement department assists securities authorities abroad in providing information, in so far as possible, under the laws of the State.

The Director of Enforcement has the main responsibility for supervision and coordination of all the enforcement activities at the Authority. In addition, two additional areas of activity are subject to his supervision: monitoring trade control and class actions.

The function of monitoring trading is to detect unusual activities that adversely affect orderly trading and that may indicate the commission of violations under the Securities Law. Monitoring of trading is done by means of the use of computerized audit systems that were developed by the Authority and also by means of other audits. The examination process includes the examination of explanations for

unusual activity in securities, and in those instances where unusual activity occurs during the trading day, in view of the circumstances of the case and inter alia the company's reports, is inexplicable, the matter is referred to the Reporting Center for clarification with the companies. In cases where there is a prima facie suspicion that a violation has been committed, the case is referred to the Intelligence Department for consideration of further proceedings. In addition, the monitoring of trading provides information and professional assistance for other departments at the Authority.

The sphere of class actions involves formulating fundamental recommendations to the plenum of the Authority, with regard to applications to finance class actions and to finance specific expenses relating thereto, monitoring the proceedings of the actions and examining the necessity for the attendance of the State's Attorney-General's office in the class action cases that have ramifications for the efficiency and the contribution of the class action process.-

International

This department was established at the beginning of 2005 as part of the strategic goals of the Authority to integrate the Israeli capital markets in the process of globalization, in general, and in particular, to integrate the Authority in the process of undergoing cooperation with other world wide supervisory bodies.

The duties of the department are to coordinate and manage all international facets of the Authority's work. The department will be responsible for contact with international supervisory bodies and with foreign security authorities, including approval of memorandums of understanding for cooperation with those authorities.

Investigations

The purpose of the Investigations Department is to investigate any suspicion of a violation under the Securities Law, the Joint Investment Trust Law, or the Regulation of the Occupation of Investment Counseling Law. The Authority's investigators are also authorized to investigate certain offenses under the Penal Law, 5737-1977 ["Penal Law"].

An investigation is begun on the instructions of the Authority's chairman, and is completed when the investigation file is sent to the State Attorney, together with a recommendation to file an indictment or to close the file. The recommendation is made by the Authority's chairman, after consulting with the Director of the Investigations Department and with the Director of the Enforcement Department.

The Department also conducts legal investigations under Chapter 12 of the Securities Law, and under the International Legal Assistance Law, 5758-1998.

General Counsel

The General Counsel is charged with all the Authority's ongoing legal activities. The legal staff is grouped into various departments. They follow up on all specific tasks of Authority and engage in drafting legislation and regulations. The Authority's attorneys engage in examining prospectuses and financial statements of companies and mutual funds. They check the various current reports according to regulations on conflicts of interest, regulations on private offerings, and regulations on purchase offers. The Authority's lawyers participate in regulating the stock exchange's activities and in supervising and regulating the activities of investment advisors and investment portfolio managers. They also take part in the advisory process conducted by organs of the State with the Authority in

those areas where this is required by law. In addition, the general counsel represents the Authority in all other matters regarding internal management, including representations before the courts in certain matters and provides support for civil proceedings in which the Authority is a party and which are handled by the State Attorney's Office or by other legal counsel.

Economics

The Economic Department's job is to give economic advice to the chairman of the Authority and to the various departments of the Authority on matter of an economic nature.

The department coordinates the work of the committee on the capital markets, and is a regular partner in discussions and recommendations of the Authority's staff that are presented for the approval of the Stock Exchange Committee and it takes part in various tasks of the Authority's committee's on many subjects including orderly trading on the stock exchange, the stock exchange by-laws, new financial instruments, the Authority's budget, etc.. In addition, the department provides assistance, when needed, for the investigations department on matters relating to trading on the stock exchange, and advice to the lawyers in the State Attorney's Office on matters related to trading on the stock exchange, including preparing economic opinions that are presented in court.

The department is also involved in the development and maintenance of the databases and computerized indices that are connected with the trading in securities and are used by the Authority for continuous monitoring activity and empirical assessment of the possible ramifications of the Authority's decisions or various events on the stock exchange. The department is responsible for the development, operation and supervision of the computerized systems for identifying unusual activity in securities trading, and it is continually monitoring the system in order to examine its effectiveness and its suitability for new financial instruments, new trading technologies, and the sophisticated trading methods of the investors. In addition, one of the important tasks of the department is practical research focusing on an analysis of developments in the capital market, in general, and the stock exchange in particular. The research work is used, inter alia, for supervising the capital market and it forms, sometimes, a basis for legislative initiatives in the field of the capital markets and the supervision thereof. The research concerns a number of issues in the capital markets and focuses mainly on assessing the effect of various important factors on the proper course of trading on the stock exchange. The research issues include, inter alia, an examination of the efficiency of the capital market vis-à-vis the publication of information to the public; the effectiveness of the methods of trading on the stock exchange; the effect of the control structure in companies on the share prices and business results, etc.

Information Systems

The functions of the Department include the development and maintenance of the information systems, and the computing and communications infrastructures for the Authority, for supporting the directors and employees in their responsibilities, and in accordance with the approved annual work plans. The Department is a partner in determining and implementing the Authority's computing strategy. In some cases, the Department acts in response to a request of the other departments, and in some cases, by virtue of its knowledge of the other departments, the Department itself identifies the needs and initiates projects that are designed to respond to these needs and provide a computing solution to them.

The Department is responsible for developing and maintaining the following computer systems: the computerized archive system, electronic mail, task management, meetings management, and

address books; the Authority's Internet site; Information Systems for managing investigations ["AGATHA"] which is used by the Enforcement Department; the electronic reporting system ["MAGNA"] which is used by all those reporting in the capital markets, the general public and the employees of the Authority; the operating system which includes most of the information on the various subjects handled by the Authority - information on companies, mutual funds, investment advisors and portfolio managers, trading figures, trading supervision and identifying unusual events [in the course of developing the interface for receiving information from the stock exchange], data which is used for economic research and accounting information; additional systems for special assignments.

Another field which is handled by the Department is infrastructures and infrastructure software: the purchase and maintenance of personal computers and relevant commercial software, the purchase and maintenance of servers, the internal communications network and external lines of communication, including lines for internet suppliers and a line that connects the offices in Jerusalem and Tel-Aviv, and allows full sharing of information in all systems between the offices at the different sites; data security of all the systems; telephone communications, telephone lines and exchanges; operating and providing service for printers; the supply and installation of short life equipment of all kinds, etc..

The Department includes four employees of the Authority; some of the activities are carried out by means of outsourcing.

Supervision of mutual funds

The law that governs the activity of mutual funds is the Joint Investment Trust law, which prescribes that in carrying out their duties under this law, the fund manager and its trustee will be subject to the Authority's supervision.

The supervisory methods of the Department are:

- a. Examining prospectuses that are filed with the Authority in order to receive a permit for publication;
- b. A computerized warning system that identifies, on a monthly basis, digressions from the provisions of the law;
- c. A computerized warning system that examines, on a daily basis, the reasonableness of the daily changes in unit prices;
- d. Examination of the immediate reports filed with the Authority;
- e. Initiating legislation that regulates mutual fund activity;
- f. Imposing civil fines on account of breaches of instructions.

The computerized warning system is based on monthly reports that are filed with the Authority by mutual fund managers for each fund that they manage and on additional data in the possession of the Authority.

The monthly reports include data about the assets held by the funds on the last trading day of each month and about their activity during the month.

The employees of the Department, with the assistance of the legal department, prepare the infrastructure for changes in legislation that regulates the activity of the funds. The need for these changes arises from changes that take place in the capital markets - the integration of the Israeli

capital market in the global capital markets, the introduction of new financial instruments into trading on the stock exchange, a change in the trading methods on the stock exchange, etc.

Licensing and supervision of investment advisors and investment portfolio managers

The Department deals with licensing and supervising investment advisors and investment portfolio managers, pursuant to regulations on investment counsel and the law on the prohibition of money laundering. In the licensing context, the department arranges professional examinations, handles requests for exemptions from examinations, and coordinates the registration of apprentices. In the context of supervising licensees, the department arranges inspections under the investment counsel law and the law on the prohibition of money laundering, supervises the reporting of licensees to the Authority, and deals with suspicions of breaches of the law.

The department initiates and deals with draft amendments to the law on investment counseling and the regulations enacted thereunder.

In addition, the department is involved in counseling and assisting proceedings related to legislation, enforcement and absorption of the war against money laundering, and within this framework the Department cooperates fully with other supervisory bodies [Bank of Israel, Ministry of Justice, the Ministry of Finance and the Police] and assists the Ministry of Justice in preparing documents that are sent to international bodies [FATF and the IMF] for the purpose of examining Israel's compliance with international standards on the question of the war against money laundering. The department also took part in the meetings that were held with the representations of the various organizations.

Corporation Finance

The Corporation Finance department deals with all reporting by companies reporting under the Securities Law and by dual listed companies. The work of the department unites the work of three departments that existed in the past at the Authority - Accounting and Reporting Department, Legal Department and the Reporting Center.

The department's staff, which includes accountants and lawyers, follows up, in real time, on current reports of companies filed with the Authority, including immediate reports, interim reports, and periodic reports. This follow up includes an assessment and examination of the reports with an emphasis on the level of disclosure in the reports, compliance with the requirements of the law and its regulations, enforcement of generally accepted accounting policies and an examination of the legal, accounting and economic aspects involved therein. While carrying out its responsibilities, the department's staff encounters complex legal and accounting issues, which are interrelated, and locates market failures that require the intervention of the Authority. A special effort is devoted to preventative action, on the basis of intelligence information, together with the Intelligence Department of the Authority.

The department is a central partner in setting up the electronic reporting project including the identifying the characteristics of the system, its legal regulation and providing ongoing support for companies. By means of the department's monitoring tools, the enforcement measures it has at its disposal and its cooperation with the Intelligence Department and the Investigations Department, the Corporation Finance Department is responsible for an ever-increasing improvement in the level and quality of reporting, and in the protection given to investors.

Among its other activities, the department is involved in examining prospectuses of companies and bodies that offer securities to the public, in order to ascertain, inter alia, whether the level of

disclosure therein is fair. In addition, the department examines reports on transactions with controlling shareholders and private offerings, purchase offers, debt arrangements and merger reports. While dealing with these reports the department's staff are required to deal with complex valuation reports, and it examines the economic models underlying the reports, the degree of disclosure as to the facts, the assumptions used for the purpose of the valuation and the reasonableness thereof, and it is constantly on guard to ensure fair disclosure.

The department, under the guidance of the Authority's general counsel, provides support for legislative action and initiates primary and secondary legislation in the field of securities and financial reporting, in coordination with the other departments at the Authority. In addition the department is involved in providing support for civil proceedings in which the Authority is a party and which are handled by the State Attorney's Office ,or by other representation.

The department also takes part in the standardization procedure carried out by the Israel Accounting Standards Board and presents the positions of the Authority on various issues.

As part of the service to the reporting community, the department allows reporting bodies and their accountants and lawyers to contact it, under a certain framework, on matters relating to reporting in order to ascertain the position of the department's staff before the accountant and/or advocate begins his work.

Chapter 4 Companies

1. Prospectuses

In 2004, the business sector¹ raised NIS4,699 million through the issue of shares and convertible securities, compared with NIS1,105 million in 2003. During 2004, the business sector raised NIS 6,504 million through the issue of bonds, compared with NIS3,715 million in 2003. In addition, the business sector also raised NIS1,064 million through the exercise of options², compared with NIS308 million in 2003.

In total, in 2004, the business sector raised³ NIS12,267 million, compared with NIS5,128 million in 2003. During 2004, the Government raised NIS 40 billion [gross], through the issue of bonds, compared with NIS 57 billion [gross] in 2003.

The raising of capital through issues of shares and convertible securities, by sectors⁴, NIS millions, in current prices, is as follows: Industry companies - 1078.8 [40%], compared with 222.0 [20%] in 2003; Trade and services companies - 469.8 [17%], compared with 220.3 [20%] in 2003; Real estate, building and agriculture - 304.0 [11%], compared with 355.2 [32%] in 2003; Insurance companies - 166.4 [6%], compared with 0 in 2003; Investment companies - 139.2 [5%], compared with 166.5 [15%] in 2003; Oil exploration companies - 93.8 [4%], compared with 141.3 [13%] in 2003; Other sectors - 447.4 [17%], compared with 0 in 2003⁵.

| Table 1: Capital raised by the business sector through shares, convertible securities ⁶ and bonds, 2000 - 2004 | | | | | | | | | |
|---|--------|---|--------|---------------|------------------------------|-------------------------------------|---------|----------|--|
| NIS millions, in current prices | | | | | | | | | |
| Year | Public | | Rights | Employe es | Institutional ; investors | Other investor s ⁷ | Bonds | Total | Total, in December 2004 prices |
| | Shares | Convertible bonds and options ⁸ | | | | | | | |
| 2000 | 864.5 | 1,923.3 | 477.1 | 389.2 | 1,324.8 | 205.5 | 267.4 | 5,451.9 | 5,853.6 |
| 2001 | 2.5 | 2,000.6 | 399.7 | 15.6 | 271.6 | 153.5 | 2,666.1 | 5,509.7 | 5,812.7 |
| 2002 | 27.4 | 445.7 | 206.6 | 34.4 | 539.8 | 155.8 | 2,206.8 | 3,616.5 | 3,652.4 |
| 2003 | 154.2 | 394.1 | 172.2 | 2.0 | 325.8 | 57.0 | 3,715.4 | 4,820.7 | 4,835.4 |
| 2004 | 776.1 | 2,036.1 | 55.4 | 0.0 | 1,747.7 | 84.1 | 6,503.6 | 11,203.0 | 11,246.8 |
| 2004, By quarters | | | | | | | | | |
| I | 169.1 | 1,252.2 | 10.2 | 0.0 | 484.1 | 0.0 | 1,992.4 | 3,908.0 | 3,959.2 |
| II | 451.1 | 382.1 | 45.2 | 0.0 | 476.3 | 84.1 | 2,308.6 | 3,747.4 | 3,740.0 |
| III | 108.9 | 264.5 | 0.0 | 0.0 | 566.2 | 0.0 | 2,074.5 | 3,014.1 | 3,014.1 |

¹ The figures in this chapter relating to amounts raised are taken from Bank of Israel reports, and as of the date of the report, is only estimation.

² Including the exercise of options by subsidiaries.

³ In shares, convertible securities, debentures and the exercise options.

⁴ The sectors presented separately are those whose share of issues in 2004, or in 2003, was significant.

⁵ The figures in brackets represent the share, in percentage, of the total issues this year and in 2003, respectively.

⁶ Does not include the exercise of options.

⁷ Includes subsidiaries.

⁸ And others.

| | | | | | | | | | |
|----|------|-------|-----|-----|-------|-----|-------|-------|-------|
| IV | 47.0 | 137.3 | 0.0 | 0.0 | 221.1 | 0.0 | 128.1 | 533.5 | 533.5 |
|----|------|-------|-----|-----|-------|-----|-------|-------|-------|

During 2004 137 applications of corporations were submitted to the Authority for a permit to publish a prospectus⁹. In total, 103 permits were given, including 10 permits for applications that were submitted in 2003, and 31 permits for companies offering securities to the public for the first time [for a comparison with previous years, see table 2 below]. Details of the applications that were processed by the Authority in 2004 appear in appendices A and B of this report.

| Year | Number of applications submitted | Number of permits given ¹⁰ | First time issue |
|------|----------------------------------|---------------------------------------|------------------|
| 2000 | 184 ¹¹ | 104 ¹² | 41 |
| 2001 | 52 ¹³ | 33 | 6 |
| 2002 | 59 ¹⁴ | 45 | 7 |
| 2003 | 55 ¹⁵ | 38 ¹⁶ | 12 |
| 2004 | 137 ¹⁷ | 103 ¹⁸ | 31 |

Handling of applications to grant a permit for a prospectus is done by a team of accountants and lawyers. According to the accepted procedure for full examinations, the draft prospectus is examined by the team and meetings are held with the offeror's representatives, at which time the team's comments are presented. A recent change is that the examination is now also done through correspondence with representatives of the offeror, as opposed to face to face meetings. After the examination of the draft by the team, the draft is referred for consideration by one of the prospectus committees of the Authority. This committee, which is composed of members of the Authority and which meets as needed, is authorized to grant a permit for publication of the prospectus. On the basis of the committee's decisions, the offeror may be asked to file an additional draft, which includes the subjects with regard to which, in the committee's opinion, there is a need to expand or amend the disclosure or the accounting treatment in the prospectus before the permit is granted. When necessary, additional meetings of the team with the offeror's representatives are held and additional drafts are submitted. When the requirements stipulated by the committee are fulfilled, a permit to publish the prospectus is given.

In 2004, there was an increase of 250% in the number of applications for permits to publish a prospectus, compared with 2003. A significant increase was also evident in the number of permits granted for prospectuses in 2004 compared with 2003. The number of issues of companies offering securities to the public for the first time [IPO], as part of the total number of issues, also increased significantly, compared with 2003.

2. Private Issues

⁹ Of these, 5 applications were withdrawn by the applicants, 1 issue was canceled after the tender stage, and 15 applications expired.

¹⁰ Does not include corporations that published prospectuses abroad, after receiving an exemption from receiving a permit from the Authority [according to section 40[c] of the law, this section was cancelled in 2000].

¹¹ In 34 cases, the Authority decided to implement the partial or abbreviated checking procedure for the draft prospectus.

¹² Includes 4 cases where the corporation canceled the issues after receiving permission to publish.

¹³ In 34 cases, the Authority decided to implement the partial or abbreviated checking procedure for the draft prospectus.

¹⁴ In 16 cases, the Authority decided to implement the partial or abbreviated checking procedure for the draft prospectus.

¹⁵ In 21 cases, the Authority decided to implement the partial or abbreviated checking procedure for the draft prospectus.

¹⁶ Includes 1 case where the corporation canceled the issues after receiving permission to publish.

¹⁷ In 32 cases, the Authority decided to implement the partial or abbreviated checking procedure for the draft prospectus.

¹⁸ Includes 1 case where the corporation canceled the issues after receiving permission to publish.

The Securities [Private Offering of Securities in a Listed Company] Regulations, 5760-2000 ["Private Offering Regulations"], which came into force in August 2000, stipulated three levels of disclosure: an exceptional issue, which includes the most extensive disclosure, a substantial issue, and an insubstantial issue.

An exceptional issue is an issue of securities granting 20% or more of the voting rights in a company before issue, or an allocation to a director or the managing director of 5% or more of the issued share capital, or that afterwards they will hold 5% or more of the company's issued share capital or voting rights therein, or an issue the result of which the beneficiary will become a controlling shareholder of the company. A substantial issue is an issue to a party who holds 5% or more of the issued share capital or voting rights in the company or a party who holds this amount after issue, and any issue to a director or managing director which is not an exceptional issue.

In 2004, 177 immediate reports were submitted for private issues [of which 137 dealt with substantial issues and 40 dealt with exceptional issues], compared with 77 reports in 2003.

The reports are checked on a sample basis, in accordance with a July 1999 decision of the Authority [see the 1999 Annual Report, page 6] by the staff of the Corporation Finance department.

In accordance with that stated in the Private Issues Regulations, the Authority may ask for explanations, details, information and documents, and if necessary, order a change to an immediate report. The Authority exercises its power in cases where, in its opinion, all the details required by holders of the company's shares have not been given, or when there is a need to clarify details given in the immediate report. In such cases, the company issues an amended immediate report, and the shareholders are given an amended notice with regard to the private issue, which includes the clarifications and details that are required. In certain cases, and subject to that stated in the regulations, the Authority may order the shareholders' meeting to be deferred by not less than three business days and not more than twenty-one days, after the date of publishing the corrected report.

3. Transactions between the Company and a Controlling Shareholder

On February 28, 2002 [16 Adar 5762] the Securities [Transaction between a Company and a Controlling Shareholder therein] Regulations, 5761-2001 ["Controlling Shareholder Regulations"] came into effect. These regulations replaced the Securities [Restricting Conflicts of Interest between a Listed Company and a Controlling Shareholder therein] Regulations, 5754-1994. The new regulations, unlike the regulations that were repealed, stipulate disclosure requirements only for transactions with controlling shareholders. The approval mechanisms are now stipulated in the Companies Law, 5759-1999 ["Companies Law"] whereas in the past they were prescribed by regulations under the Securities Law. The controlling shareholder regulations stipulate disclosure requirements for a listed company that wants to carry out an exceptional transaction with a controlling shareholder, or an exceptional transaction with another party, in which the controlling shareholder has a personal interest, or approval of terms of office and employment of a controlling shareholder.

In 2004, 426 immediate reports were filed, prepared according to the conflicts of interest regulations, as compared with 279 reports in 2003 [321 reports in 2002]. In January 2002 an amendment to the Companies [Concessions in Transactions with Interested Parties]

Regulations, 5760-2000, came into effect. This amendment reduces the duty to file reports with regard to transactions with controlling shareholders, since it provides that when the conditions stated therein are fulfilled, the transaction does not require the approval of a general meeting, and therefore, the company is exempt from submitting a detailed report on the transaction with the controlling shareholder, but rather a short report on the main points of the transaction, and the rationale for approval. However, it should be noted that shareholders holding at least one percent of the issued share capital or voting rights of the company are entitled to request, in this situation, a shareholders' meeting. Accordingly, a report on the transaction with controlling shareholders will also be issued.

The types of contacts that are the subjects of the said reports are many and varied. Most of the reports deal with approval of employment terms and conditions, indemnification and management fees. Some of the reports refer to the purchase of business activity from the controlling shareholder, or the purchase of shares in another corporation belonging to the controlling shareholder, some refer to the sale of one of the company's assets to the controlling shareholder, and some refer to guarantees, deposits, loans, providing various services, insurance arrangements, purchase of knowledge, etc.

The Authority's staff invests much effort in examining the various issues relating to transactions with controlling shareholders, such as defining transactions as exceptional transactions, classifying the company shareholders as interested parties having a personal interest in transactions, etc.

Another matter that was also emphasized this year was the results of voting at general meetings. Within the framework of dealing with this matter, the Authority's staff contacted companies and asked for details on voters who were defined as those persons who are not interest parties having a personal interest in the vote. These details included, inter alia, details of the connections of those voters with the company. In some cases, the companies were required to issue immediate reports that included this additional information.

The reports are examined by the Authority's staff in the same manner as reports submitted under the private issue regulations. In addition, the Authority's staff examines immediate reports that deal with transactions between the company and its controlling shareholders, and in some cases, the companies are obligated to issue a report in accordance with the controlling shareholder regulations.

4. Purchase Offers

In February 2000 [Adar I, 5760], the Securities [Purchase Offer] Regulations, 5760-2000 ["Purchase Offer Regulations"] were issued and came into force. These regulations require the filing of a purchase offer statement under the regulations in three cases: an ordinary purchase offer, which is an act of an offeror designed to induce those members of the public holding securities of a listed company to sell a security to the offeror; a full purchase offer, as defined in section 336 of the Companies Law, and a special purchase offer, as defined in section 328 of the Companies Law. Someone who wishes to make a purchase offer to the shareholders of a listed company must do so by means of a written statement and subject to the conditions prescribed in the regulations.

In August 2004, the Finance Committee of the Knesset approved an amendment, proposed by the Authority, to the regulations. The subject of the amendment – scope of disclosure in the

purchase offer, a timetable to undertake the purchase offer, and the submission of various reports. Under the amendment, various provisions on disclosure were added requiring detailing the sources of financing for the purchase offer, and disclosure provisions where the offeror is the company itself [self purchase offer]. Regarding deadlines, provisions were added to prevent an overlap in the dates of receipt of a competing purchase offer, more flexible deadlines for issuing the directors' opinion in the case of substantial purchase offer, and an easing of the last deadline for the receipt of an additional purchase offer by the offeror. The amendment to the regulations became effective at the end of 2004.

In 2004, 41 statements relating to purchase offers to shareholders of listed companies were published, compared with 58 statements in 2003 [63 in 2002]. Six purchase offers were substantial purchase offers, [one of which was unsuccessful], 12 offers were ordinary purchase offers, of which two were from the same company [Tempo] and the remainder were full purchase offers.

Twenty three purchase offers were issued for 21 companies. Those companies requested to de-list their shares from trade on the stock exchange and to become private companies. These purchase offers were submitted by controlling shareholders of the listed companies involved, by the companies themselves or by a subsidiary company. Fourteen of the offers were successful and shares of those companies were de-listed from trading on the stock exchange. The purchase offers of two companies were still open by the end of 2004.

Under the provisions of the regulations, the Authority has the power to demand explanations, details, information and documents, with regard to the details included in the purchase offer statement, and it may even order that the statement be corrected. In accordance with this right, various offerors were required to give additional details, such as details of the last transactions in the company's shares, shareholders' equity per share [in order to compare it to the offered purchase price in the purchase offer], etc.

5. Current Reports

Companies whose securities have been offered to the public by means of a prospectus have reporting requirements from the time that their securities were offered to the public, and so long as the public still holds them. These obligations include filing immediate reports, periodic reports and interim financial statements.

In the context of the Authority's monitoring of said reports, in various manners, it constantly samples reports filed by companies that are subject to the Securities Law, in order to examine the extent to which they comply with the Securities Law, the regulations thereunder, and generally accepted accounting and reporting principles that seek to implement the principle of fair disclosure. In so far as is necessary, these companies are instructed to correct their financial statements, and in other cases they are instructed to disclose additional information to the public.

During 2004, the process of examining financial reports of all reporting entities continued, and towards year end an internal change in the Corporation Finance department was undertaken, the goal of which was the upgrading of the department's ability to examine financial statements. Under this framework, more involved and extensive examinations will be carried out, which will include all reports issued by reporting entities, the sector in which the company operates, and the group of companies to which it belongs. In addition, during 2005 the Authority intends to complete the examination of financial statements of reporting entities which were not examined

during 2004, and to regularly examine all financial reports of all reporting entities. Moreover, the "Red Flags" system which became operative during the last quarter of 2004, gave the department an additional tool to locate areas of weakness in financial reports or in the situations of reporting entities.

The examination strategy of the Authority also takes into account economic developments and developments in accounting standards. The Authority's staff monitors developments in the global capital markets, and tests the regulation relating to the various financial instruments that have been recently introduced in Israel, including structured products, "BOT" projects, and the issue of asset - backed securities. Regarding same, the Authority appointed a joint committee with the office of the Income Tax Commissioner to examine the implications of the issue of asset - backed securities. The committee is to issue its conclusions during March 2005. As a general rule, the Authority has decided to be the first to study these new instruments, in order to help develop the capital markets while maintaining a high level of supervision.

A. The Periodic Report and Interim Financial Statements

During the examinations of statements that were carried out during the year, various instances were found of entities which did not comply with, at the level required, the principles of fair disclosure and generally accepted accounting principles.

The main subjects for which sufficient attention was not paid: presentation of assets at a sum which does not exceed its recoverable value, and the treatment of provisions for write - offs; recognition of income not according to principles; classification and presentation of income and expenses in the statement of income; accounting treatment of investments on the equity basis and in consolidated financial statements, taking into account cases of companies that avoided consolidation and from recording the investments on the equity basis, a situation which is required, and against this, cases where statements were consolidated even in the absence of control; absence of fair disclosure and correct measurement of contingent liabilities, mainly for legal claims; no implementation of regulations on presentation of transactions between a company and a controlling shareholder therein; improper presentation in the financial statements in order to exclude certain deviations in financial ratios which the company committed itself to banks to maintain; disclosure of policy on the recognition of discounts from suppliers; incorrect classification of leasing and the treatment of sales and leasebacks; writing off of liabilities from the balance sheet; an unwarranted change in the term used for depreciating assets, etc..

Further to discussions that were held with companies and their accountants, a significant number of the companies from which the staff of the Authority requested additional explanations, decided to correct or to justify their statements, without being requested to do so by the Authority. Regarding the other companies, in some cases the staff was convinced of the companies' stands, and in other cases the treatment of the case has not yet been completed. The Authority uses its power to order the change in statements, from time to time, in cases where the companies do not undertake the change on their own.

Following the increase in the last few years in the volume of checks and promptness, the tendency continued also this year, of increasing requests by companies and their accountants for early consultation with the Authority's staff and sometimes a request for early guidance from the Authority's plenum. Among the subjects that were brought up by the companies: accounting treatment for reverse purchases and the pooling of activities, signs of control at the entity,

effective control of the company, debenturization of assets, currency translations in the financial statements and implementation of Accounting Standard 13, recognition of income, accounting treatment of complicated financial instruments, distribution of options to employees, accounting treatment of BOT projects, and statements using realization values for a company in liquidation.

During the year, the Authority concentrated on the operations of the board of directors, in so far as it was related to financial reporting and the systems of control at the company. In this framework, the Authority sent out general letters to various boards of reporting companies and published its position on the findings of this examination. In addition it began to send out specific requests to various boards in order to identify weak points in their operations.

As part of the tendency to increase transparency in operations of the various "gate keepers", the Authority published its guidelines which require the boards to relate to the system of internal audit at the company and to the functioning of the internal auditor, and issued additional guidance dealing with the relation of the board to critical accounting estimates which are used in the financial reporting. In addition, the Authority's guidelines on disclosure of the accounting and financial expertise of the board of directors members was extended by one year,

The subject of independence of accountants was stressed this year by following up on the going-ons at companies. Save for a request to reporting companies at the time of changing accountants, the Authority also sent out letters to all accountants who audit public companies. In accordance with the findings, the Authority has started to draw up a plan, during the last quarter of 2004, which is intended to increase the consciousness of accountants that audit reporting companies on the subject of independence and to increase their knowledge in this field.

Besides the directors' report and the financial statements, the periodic report also includes additional information on the company, its subsidiaries, and its officers. Some of this is checked by department, in order to test the degree of compliance with the regulations, and to the information that is reported by the entity during the year. According to need, entities are required to correct deficiencies that are found. In addition, each report is checked against a computerized check list, and if a deficiency is discovered, the matter is brought to the attention of the company and it is required to correct it [see table 3 below].

| Reporting year | Number of companies required to report | Number of companies which did not report by the end of the reporting period | | Of which number of companies which did not report 7 days after the required period | | Of which number of companies which did not report 14 days after the required period | | Of which number of companies which did not report 30 days after the required period | | Of which number of companies which did not report 60 days after the required period | |
|--------------------|--|---|------|--|------|---|------|---|------|---|------|
| | | # | % | # | % | # | % | # | % | # | % |
| 1999 | 707 | 150 ²⁰ | 21.2 | 70 | 9.9 | 46 | 6.5 | 33 | 4.7 | 22 | 3.1 |
| 2000 | 725 | 90 ²¹ | 12.4 | 44 | 6.1 | 36 | 5.0 | 33 | 4.5 | 31 | 4.3 |
| 2001 | 716 | 140 ²² | 19.5 | 74 | 10.3 | 56 | 7.8 | 47 | 6.6 | 41 | 5.7 |
| 2002 | 687 | 161 ²³ | 23.4 | 52 | 7.5 | 47 | 6.8 | 42 | 6.1 | 38 | 5.5 |
| 2003 ²⁴ | 659 | 155 ²⁵ | 23.5 | 122 | 18.5 | 115 | 17.4 | 108 | 16.3 | 91 | 13.8 |

¹⁹ The last date to submit periodic statements is three months after the balance sheet date [or three days from the auditors' opinion date to the financial statements], and in any event, at least 14 days before the annual general meeting called for the financial statements, the earliest of all]. This table does not include reports for which the Authority granted extensions dates. [see table 5 below regarding extensions].

²⁰ Including 12 entities that are in the process of liquidation, temporary liquidation, receivership, etc.

| Table 4: Interim financial statements – companies that did not report on time ²⁶ | | | | | | | | | | | | |
|---|-----|--|---|------|--|------|---|------|---|------|---|------|
| | | Number of companies required to report ²⁷ | Number of companies which did not report by the end of the reporting period | | Of which number of companies which did not report 7 days after the required period | | Of which number of companies which did not report 14 days after the required period | | Of which number of companies which did not report 30 days after the required period | | Of which number of companies which did not report 60 days after the required period | |
| | | | # | % | # | % | # | % | # | % | # | % |
| 00 | I | 672 | 179 ²⁸ | 26.8 | 91 | 13.5 | 60 | 8.9 | 27 | 4.0 | 16 | 2.4 |
| 00 | II | 714 | 89 ²⁹ | 12.5 | 24 | 3.4 | 23 | 3.2 | 19 | 2.7 | 18 | 2.5 |
| 00 | III | 721 | 154 ³⁰ | 21.3 | 25 | 3.5 | 22 | 3.0 | 20 | 2.8 | 18 | 2.5 |
| 01 | I | 705 | 136 ³¹ | 19.3 | 28 | 4.0 | 28 | 4.0 | 25 | 3.5 | 21 | 3.0 |
| 01 | II | 703 | 106 ³² | 15.1 | 39 | 5.5 | 35 | 5.0 | 26 | 3.7 | 24 | 3.4 |
| 01 | III | 694 | 115 ³³ | 16.6 | 35 | 5.0 | 31 | 4.5 | 29 | 4.2 | 27 | 3.9 |
| 02 | I | 682 | 103 ³⁴ | 15.1 | 34 | 5.0 | 31 | 4.5 | 27 | 4.0 | 27 | 4.0 |
| 02 | II | 678 | 148 ³⁵ | 21.8 | 47 | 6.9 | 46 | 6.8 | 44 | 6.5 | 41 | 6.0 |
| 02 | III | 672 | 188 ³⁶ | 28.0 | 39 | 5.8 | 36 | 5.3 | 33 | 4.9 | 27 | 4.0 |
| 03 | I | 678 | 145 ³⁷ | 21.3 | 51 | 7.5 | 44 | 6.4 | 41 | 6.0 | 37 | 5.4 |
| 03 | II | 673 | 125 ³⁸ | 18.5 | 47 | 6.9 | 46 | 6.8 | 45 | 6.6 | 42 | 6.2 |
| 03 | III | 666 | 49 ³⁹ | 7.3 | 48 | 7.2 | 48 | 7.2 | 47 | 7.0 | 47 | 7.0 |
| 04 | I | 636 | 109 ⁴⁰ | 17.1 | 81 | 12.7 | 77 | 12.1 | 68 | 10.7 | 64 | 10.1 |
| 04 | II | 646 | 88 ⁴¹ | 13.6 | 68 | 10.5 | 64 | 9.9 | 60 | 9.2 | 59 | 9.1 |
| 04 | III | 651 | 93 ⁴² | 14.2 | 65 | 9.9 | 63 | 9.6 | 61 | 9.3 | 61 | 9.3 |

B. Dual Listings

In November 2000, the Securities Law was amended to add chapter 3, which deals with dual listings. Pursuant to the amendment, companies that are traded on the NASDAQ, the NYSE or AMEX may list their securities that are traded on the said markets for trading also on the stock exchange in Israel, relying on the identical reports that the company files in the United States. Companies that had dual listings when the law came into effect ["dual companies"] or those that will be listed for trading on the stock exchange in Israel in the future, and choose to be listed for trading afterwards also on one of said exchanges, will be able, under the amendment, to change over to reporting under chapter 3, under condition that most of the company's shareholders who are not considered as controlling shareholders, agree.

²¹ Including 18 entities that are in the process of liquidation, temporary liquidation, receivership, etc.

²² Including 24 entities that are in the process of liquidation, temporary liquidation, receivership, etc.

²³ Including 36 entities that are in the process of liquidation, temporary liquidation, receivership, etc.

²⁴ The periodic report for 2003 is the first report that was submitted through MAGNA and the increase in companies which did not submit on time relates, apparently, to the long amount of time taken to correct technical problems in sending the reports by the companies, and which delayed their receipt.

²⁵ Including 56 entities that are in the process of liquidation, temporary liquidation, receivership, etc.

²⁶ This tables includes only delays because of non submission under the time framework granted for submission, and takes into account extensions that were granted

²⁷ Entities reporting according to chapter 3[dual listed entities] are not required by law in the United States to submit interim statements and accordingly are not included herein

²⁸ Including 12 entities that are in the process of liquidation, temporary liquidation, receivership, etc

²⁹ Including 12 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁰ Including 12 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³¹ Including 18 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³² Including 20 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³³ Including 20 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁴ Including 32 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁵ Including 35 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁶ Including 42 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁷ Including 32 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁸ Including 40 entities that are in the process of liquidation, temporary liquidation, receivership, etc

³⁹ Including 44 entities that are in the process of liquidation, temporary liquidation, receivership, etc

⁴⁰ Including 58 entities that are in the process of liquidation, temporary liquidation, receivership, etc

⁴¹ Including 59 entities that are in the process of liquidation, temporary liquidation, receivership, etc

⁴² Including 59 entities that are in the process of liquidation, temporary liquidation, receivership, etc

In 2004, five companies were listed on the stock exchange in Israel with dual listing. No company was de-listed. One dual listed company changed over to reporting under chapter 3-reporting in the format that applies under the law in the United States. In 2003, two companies were listed on the stock exchange in Israel with dual listing, and one was de-listed. One dual listed company changed over to the reporting under chapter 3.

It should be noted that as a rule, the provisions of the Securities Law apply to reports under chapter 3, both in the civil and criminal spheres. However, the Authority's position takes into account the fact that these companies are already regulated by the American regulator [SEC], whose standard of regulation is among the highest in the world. Of course, this state of affairs was the main reason for the decision to grant concessions under chapter 3, and therefore the Authority exercises its powers while taking account of this fact. In addition, chapter 3 provides that in those cases where the Authority concludes that that it should consider exercising its powers, it may first contact the SEC before exercising its powers against the reporting company.

6. Extensions and Requests for Exemption

A. Extensions

The Authority may extend the time that is prescribed in the regulations for filing reports ["granting extensions"]; if it is convinced that the company was unable to file its report on time [see Table 5 below]. The Authority places emphasis on the timeliness of the reports and not merely on the disclosure included therein. As a result, the Authority exercises its power to grant extensions only in very exceptional cases. In addition, and in order to minimize the number of instances in which interim financial statements and periodic reports are filed late, the Authority submitted to the Minister of Finance a proposed amendment to the Securities Law, according to which a civil fine will be imposed on companies that report late.

B. Requests for Exemption

Pursuant to the powers granted it under the Securities Law, the Authority is entitled to exempt companies from certain reporting obligations. During 2004, 93 exemption requests were filed with the Authority, of which 10 requests were filed together with applications for permits to publish prospectuses. Seventy six of the aforesaid requests were approved in full, there were no approvals of partial requests, 14 requests were cancelled or withdrawn by the company and no requests were rejected⁴³. By comparison: in 2003, 100 exemption requests were submitted to the Authority, of which five were filed together with applications for permits to publish prospectuses. Ninety four of these requests were approved in full, there were no approvals of partial requests, five requests were cancelled or withdrawn by the company, and one request was rejected.

A breakdown of aforesaid exemption requests shows that of the requests filed in 2004, 29 concerned the publishing of a prospectus for employees, 40 exemption requests were filed in connection with reporting transactions between a corporation and its subsidiaries and its interested party shareholders, two requests dealt with the attachment of the financial statements of invested companies; 19 requests dealt with an exemption from disclosing a trade or security secret in a prospectus or in current reports, there were no requests concerning a private offering, and three requests were filed with regard to a prospectus of companies with dual listing.

⁴³ As of this date, 3 requests are still pending.

| Report | Year | Number of requests submitted ⁴⁴ | Requests rejected | | Extension granted for up to 30 days | Extension granted for 31-60 days | Extension granted for more than 60 days |
|-------------|------|--|-------------------|-------|-------------------------------------|----------------------------------|---|
| | | | # | % | | | |
| | | | | | | | - |
| Periodic | 1999 | 20 | 7 | 35.0 | 14 | - | - |
| 1st quarter | 2000 | 7 | 5 | 71.4 | 2 | - | - |
| 2nd quarter | 2000 | 3 | - | -0 | 3 | - | - |
| 3rd quarter | 2000 | 4 | 3 | 75.0 | - | 1 | - |
| Periodic | | 15 | 10 | 66.7 | 5 | - | - |
| 1st quarter | 2001 | 10 | 7 | 70.0 | 3 | - | - |
| 2nd quarter | 2001 | 11 | 8 | 72.7 | 3 | - | - |
| 3rd quarter | 2001 | 8 | 3 | 37.5 | 5 | - | - |
| Periodic | 2001 | 22 | 12 | 54.5 | 10 | - | - |
| 1st quarter | 2002 | 8 | 2 | 25.0 | 3 | - | 3 |
| 2nd quarter | 2002 | 18 | 10 | 55.5 | 5 | - | 3 |
| 3rd quarter | 2002 | 11 | 5 | 45.5 | 6 | - | - |
| Periodic | 2002 | 30 ⁴⁵ | 11 | 36.6 | 5 | - | 14 |
| 1st quarter | 2003 | 23 | 4 | 17.3 | 4 | 1 | 14 |
| 2nd quarter | 2003 | 23 | 2 | 8.6 | 5 | 2 | 14 |
| 3rd quarter | 2003 | 21 | 4 | 19.0 | 2 | - | 15 |
| Periodic | 2003 | 7 | 6 | 85.7 | 1 | - | - |
| 1st quarter | 2004 | 2 | 2 | 100.0 | - | - | - |
| 2nd quarter | 2004 | 2 | 0 | 0.00 | 2 | - | - |
| 3rd quarter | 2004 | 1 | 1 | 100.0 | - | - | - |

By comparison, in 2003 51 requests for exemption dealt with publishing a prospectus to employees; 34 exemption requests were filed in connection with the reporting of transactions between a corporation and its subsidiaries and its interested parties, five requests dealt with the attachment of the financial statements of investee companies; nine requests dealt with an exemption from disclosing a trade or security secret in a prospectus or in current reports, there were no requests dealing with a private issue, and one request concerned a prospectus issued by dual listed companies.

7. Reports by Underwriters

Underwriters are required, *inter alia*, to file reports of various kinds under the Securities [Underwriting] Regulations, 5753-1993, such as a report of an issue which is filed within seven days of the end of the period for submitting orders under the prospectus, three quarterly reports and an annual report.

⁴⁴ In instances where a company made several requests with regard to a certain report, all of the requests were counted as one request. The request was categorized according to the last approved date.

⁴⁵ Companies that received permanent liquidation injunctions, received extensions to submit their annual and quarterly financial statements that were not yet submitted. The extension is granted until completion of the liquidation proceedings, such that if that in the end the company finally liquidates, it will not have any further responsibility to file. On the other hand, if the liquidation proceedings end in reorganization of the company or in the use of a "stock exchange shell company", it will be required to meet its reporting obligations, and to submit all missing financial statements, that were not submitted, for the period before the liquidation order, and for the period after. It should be noted that the extension does not exempt companies which received liquidation injunctions, from the responsibility of filing regarding immediate reports in accordance with Securities Law and regulation issued there under.

| Table 6: Results of examining quarterly and annual reports for the reporting years 1999-2003 | | | | | |
|---|-------------|-------------|---------------|---------------|---------------|
| | 1999 | 2000 | 2001 | 2002 | 2003 |
| Number of reports submitted and checked | 249 | 236 | 230 | 230 | 221 |
| Number of reports in which deficiencies were found | 40 [16%] | 44 [19%] | 53 [23%] | 55 [24%] | 33 [14.9%] |
| Number of items checked | 2,980 | 2,836 | 2,769 | 2,734 | 2,588 |
| Number of deficiencies | | 88 [3%] | 135 [4.9%] | 148 [5.4%] | 75 [2.9%] |

8. Reform in Service

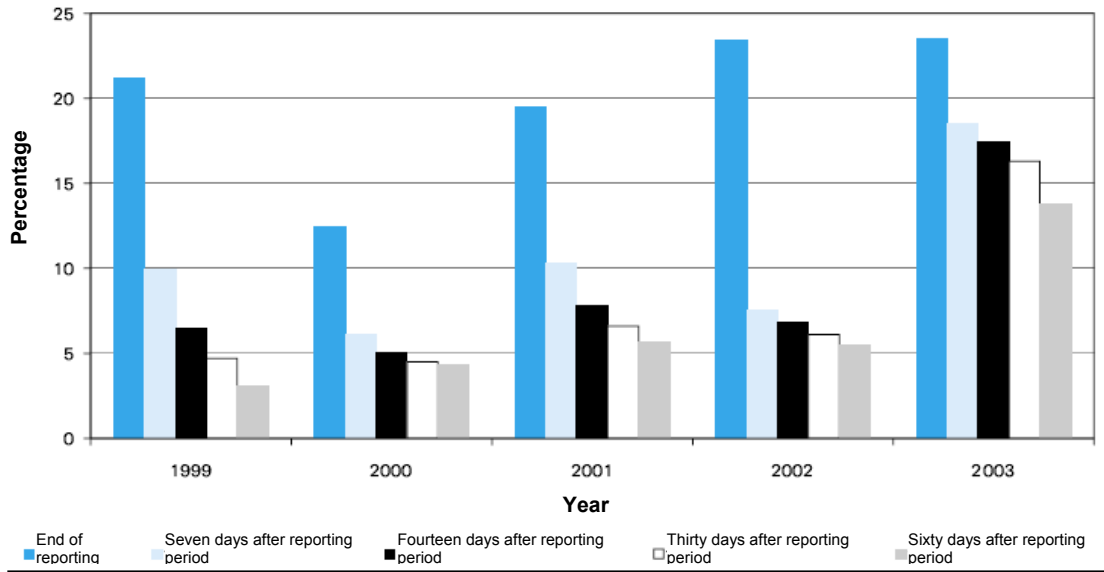
During December 2004, the Corporation Finance department formulated a reform of the organizational structure of the department, work methods, and the Authority's contact with reporting companies. Operations under the new framework started at the beginning of 2005. According to the reform, the department's work will be based on a system of autonomous teams. Each team will have accountants and lawyers who are staff members of the Authority and each team member will be a contact point for a defined group of companies. A deputy head of the Corporation Finance department will be in charge of the team. The legal and accounting departments have been assigned to provide the teams with professional support and will deal with requests for preliminary guidance. In addition, the reform will allocate generalists for various subjects, whose purpose is to monitor the operations of the team on legal and accounting matters and to give advice and support.

The objective of the move is to achieve results on both external and internal fronts. On the external front, the reform ties in with the overhaul in service which the Authority is carrying out vis a vis public companies. Following the start of the "pre-ruling" service for various fields, and the publication of staff decisions on various subjects, the reform is intended to provide a full battery of services to public companies with the setting up of contact personnel for every company drawn from the department's members. The model of operations will encourage a more professional service, faster, and more focused, because of the ability of the service team to maintain on-going contact with the companies and as a accordingly, gain experience in dealing with their issues.

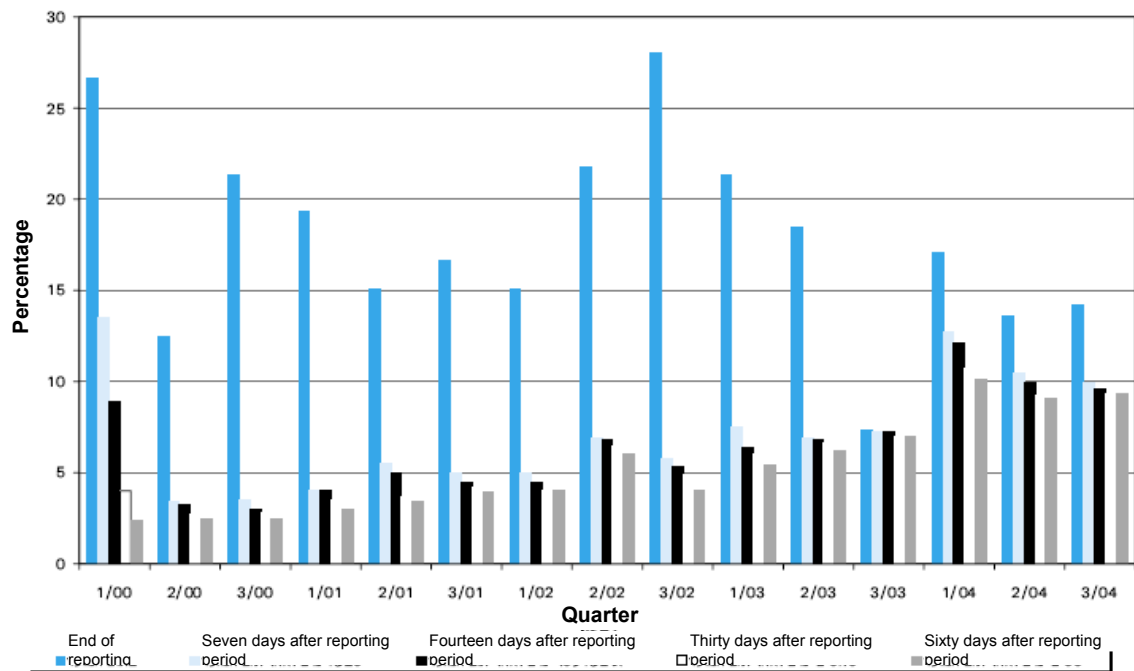
Regarding objectives on the internal front, the reform will permit the department to become more efficient, and to improve the Authority's speed of response to events in the capital markets. Making decisions at the level of the team, while maintaining a possibility for consultation with generalists, will permit an immediate professional response to reports. In addition, because of the continuity of contact and total involvement with the companies, the contacts will gain experience in both width and breadth -exposure to a number of subjects, and will follow all events at the company over time. It should be noted that this organizational change will help the department meet the new objectives which it set for itself regarding coverage and review of all reports that are issued by public companies.

In addition to that said above, the Authority began a far-reaching plan to publish the staff's accounting and legal decisions, which have cardinal importance for the investing public and reporting companies, on its internet site. In this manner, the Authority requests to contribute to increased transparency and to reduce uncertainty among reporting companies.

Graph 1—Percentage of Companies That Did Not Report on Time – Periodic Reports



Graph 2—Percentage of Companies That Did Not Report on Time – Interim Reports



Chapter 5 - Supervising the Mutual Fund Sector

1. General

At the end of 2004 [Tevet 5765], the number of mutual funds totaled 795. One fund was close - end, and the remaining funds were open - end [two open - end funds are in liquidation]. During the year, 143 new open - end mutual funds were added.

At the end of the reporting year 41 mutual fund managers were operating. During the year, three new mutual fund managers were added. Three managers stopped managing funds, and the funds under their management were transferred to other fund managers. There were nine active mutual fund trustees at the end of the year.

The value of assets¹ held in mutual funds as of the end of December 2004 [Tevet 5765] totaled NIS100.9 billion, the highest amount ever, this for the second consecutive year running, compared with NIS82.8 billion at the end of 2003 [Tevet 5764] Most of the increase in assets stems from the excess of inflows over outflows [NIS13.9 billion]. The year was especially characterized by an increase of 58% in the share of investment managers who do not belong to bank groups, in assets managed in the sector [see table 7 below].

| Table 7: Mutual funds, according to managers and asset values 2000 -2004² | | | | | |
|---|-------|-----------------|------------|-----------------|------------|
| Number of mutual funds | | | | | |
| | | Bank groups | | Others | |
| Year | Total | Number of funds | Percentage | Number of funds | Percentage |
| 2000 | 453 | 244 | 54 | 209 | 46 |
| 2001 | 529 | 280 | 53 | 249 | 47 |
| 2002 | 587 | 326 | 56 | 261 | 44 |
| 2003 | 652 | 400 | 61 | 252 | 39 |
| 2004 | 795 | 472 | 59 | 323 | 41 |
| Asset value [NIS Billion] | | | | | |
| | | Bank groups | | Others | |
| Year | Total | Asset value | Percentage | Asset value | Percentage |
| 2000 | 49.2 | 41.3 | 84 | 7.9 | 16 |
| 2001 | 66.7 | 59.4 | 89 | 7.3 | 11 |
| 2002 | 45.5 | 39.6 | 87 | 5.9 | 13 |
| 2003 | 83.8 | 75.8 | 90.5 | 8 | 9.5 |
| 2004 | 100.9 | 85.9 | 85 | 15 | 15 |

¹ In current prices.

² As at year end, in December 2004 prices.

2. Prospectuses

An open-end mutual fund prospectus remains valid for a period that may not exceed twelve months from the date of publication.

In order to ensure continuity in the offering of mutual fund units to the public, the fund manager must publish a prospectus at least once a year.

In 2004, 810 permits for to publish a prospectuses were granted, including 143 permits for the prospectuses of mutual funds making an initial public offering of units [compared with 659 permits in 2003, of which 79 were permits for prospectuses of mutual funds that were making an initial public offering of units]. Eighteen mutual funds received permits to publish prospectuses twice during 2004.

3. Reports

Mutual fund managers and trustees submit reports to the Authority under the Joint Investment Trust Law. During 2004, fund managers filed 16,794 reports [compared with 13,778 reports in 2003] with the following breakdown:

8,428 Monthly reports on fund assets under their management, on the last trading day of each month, and on the activities of the funds during the month [compared with 7,390 reports in 2003]. The reports are sent to the Authority once a month by electronic mail, and constitute the basis for the computerized system of supervising the funds.

3,991 Reports on participation in general meetings of companies whose securities are held by funds managed under their management [compared with 2,941 reports in 2003]. Based on these reports, the Authority publicly distributes a summary on how the fund managers voted at general meetings [see also paragraph 4 below].

4,375 Reports on events that require the filing of a report under the law and the regulations [compared with 3,447 reports in 2003]. The aforesaid reports are examined, summarized and entered into the computerized database.

4. Fund Managers' Attendance at General Meetings

In 2004, there were 2,192 general meetings of companies that are subject to the Securities Law. According to the reports of fund managers, the fund managers participated in 458 general meetings, including 335 general meetings at which the approval of transactions with, and benefits to, interested parties were discussed. Information showing the breakdown of participation of fund managers who, on the date of said meetings³ held securities of companies whose meetings were called to approve transactions with, and benefits to, interested parties, is presented in table 8.

³ In the absence of figures with regard to the securities held by funds during the month, it has been assumed that holding a security at the end of the month prior to the date of the general meeting and also at the end of the month in which the general meeting took place, means that the security was held on the date of the general meeting.

| Year | Number of meetings | Participation by less than 30% of the managers | | Participation by between 30% and 70% of the managers | | Participation by more than 70% of the managers | |
|------|--------------------|--|----|--|----|--|----|
| | | Number of meetings | % | Number of meetings | % | Number of meetings | % |
| 2000 | 435 | 49 | 11 | 206 | 47 | 180 | 42 |
| 2001 | 330 | 16 | 5 | 141 | 43 | 173 | 52 |
| 2002 | 365 | 13 | 4 | 118 | 32 | 234 | 64 |
| 2003 | 328 | 16 | 5 | 98 | 30 | 214 | 65 |
| 2004 | 335 | 21 | 6 | 102 | 31 | 212 | 63 |

5. Civil Fines

A. Fines imposed

Under section 114 of the Joint Investment Trust Law, anyone who violates any of the provisions of that section is liable to a civil fine. The fines are collected by the Authority and transferred to the Government treasury.

During the year, fines were imposed on ten fund managers and on two fund trustees.

All fines that were imposed were paid, save for one case where an appeal was submitted against the imposition of the fine. The court ordered, at the request of the fund manager, to delay payment of the fine, until the decision on the appeal will be rendered.

Table 9 below specifies the types of violations for which fines were imposed during the year:

| Violation for which a fine was imposed | Section of law under which the fine was imposed | Number of managers/Trustees | Number of violations |
|---|---|-----------------------------|----------------------|
| Non - submission of quarterly reports under section 78[e][1] of the law regarding systems to ensure management of the fund in accordance with the law | 114[b][17] | 1 | 4 |
| Sale and redemption of units on a day which is not a trading date | 114[c][2] | 1 | 1 |
| Publication of notices in a newspaper about receiving a permit to publish a prospectus before the permit was given | 114[b][3] | 1 | 1 |
| Publication in a newspaper not in accordance with provisions of the law regarding publication | 114[b][16] | 3 | 3 |
| Holding a security in a percentage in excess of that permitted, based on the value of the fund's assets | 114[b][12] | 3 | 3 |
| Holding of an asset contrary to the investment policy | 114[c][4][a] | 2 | 2 |
| Holding a security in a percentage in excess of 5% of the amount permitted as part of the value of the assets | 114[c][5] | 2 | 2 |
| Non compliance by a trustee on a fund manager's compliance with the provisions of the law | 114[c][8] | 1 | 1 |

In addition, notices were sent to four fund managers notifying them of the intention to demand a fine for six violations. The managers were given an opportunity to state their case with regard to the demand for the fine, and also to present special reasons that might justify not imposing a fine. Fund managers submitted requests to stay of a fine. The Authority considered the requests and made its decision accordingly [the requests for fines were sent after the end of the reporting year and before the publication of the report. The fines were not included in the totals of fines requested, as reported above].

The following are the violations for which notices were sent to fund managers:

- Three violations of publication of notices in a newspaper or the internet not in accordance with provisions of the law on publication.
- Three violations of the provisions of the law regarding the holding of a security in an amount that exceeds the permitted proportion of the fund assets.

B. Hearings on Requests to Stay the Demand for Fines Based on Special Considerations

The Authority has the power, under section 117[b][2] of the law, to stay the demand for a civil fine if there are special considerations. On the basis of this power, the Authority decided as follows:

1. To stay the demand for a fine for 6 violations:

- Two violations of calculating selling and redemption prices, not as required,
- One violation of holding an asset in an amount in excess of that permitted as a portion of the fund's assets,
- Three violations of undertaking transactions for the fund, using credit

2. To reduce the fines, as following

- A fine for a constantly repeated violation - the fine was reduced and set at an amount for one repeated violation, for the entire period of violation,
- In two cases of a number of similar violations that resulted from the same cause - the fine was reduced and set at the amount for one violation, the more serious of the two,
- One case – the fine was reduced by 25%,
- One case – the fine was reduced by 35%,
- Five cases – the fines were set at 1/2 of the original amounts
- One case – the fine was set at 1/3 of the original amount,
- One case – the fine was reduced to 10% of the original amount.

C. Legal Proceedings Against Fines Imposed

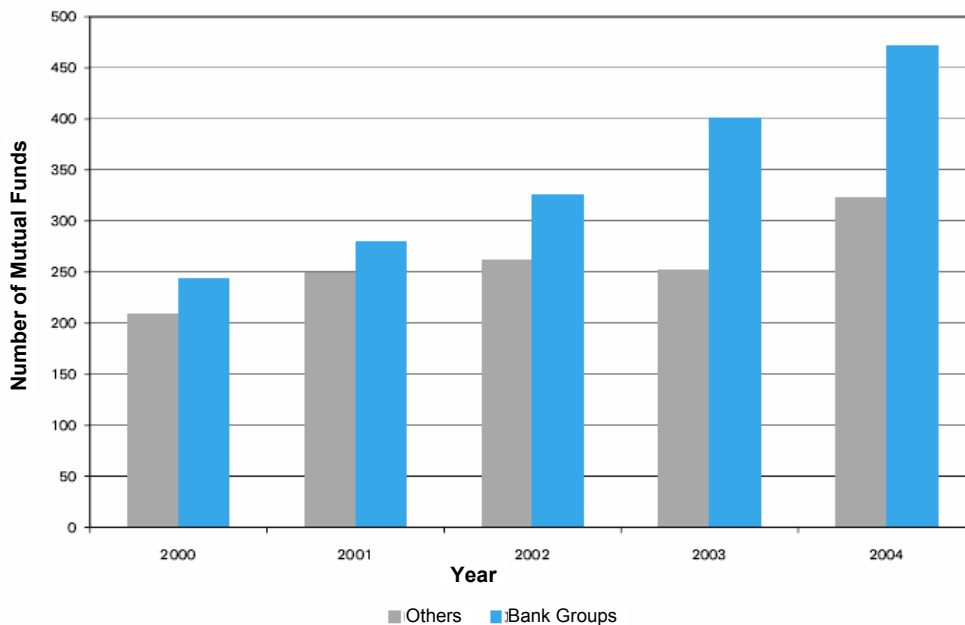
During the year, three appeals against decisions by the Authority to impose fines were submitted:

- a. One case – the District Court passed judgment on 20.7.04. The case regards fines that were imposed on a fund manager in 1999. The appeal against the fine was submitted by the fund manager in 2000. The appeal was rejected by the court, taking into account the Authority's declaration that it intended to consider if special considerations existed which would justify a partial reduction of the fine [see the 2003 annual report, page30, paragraph c[a]. The

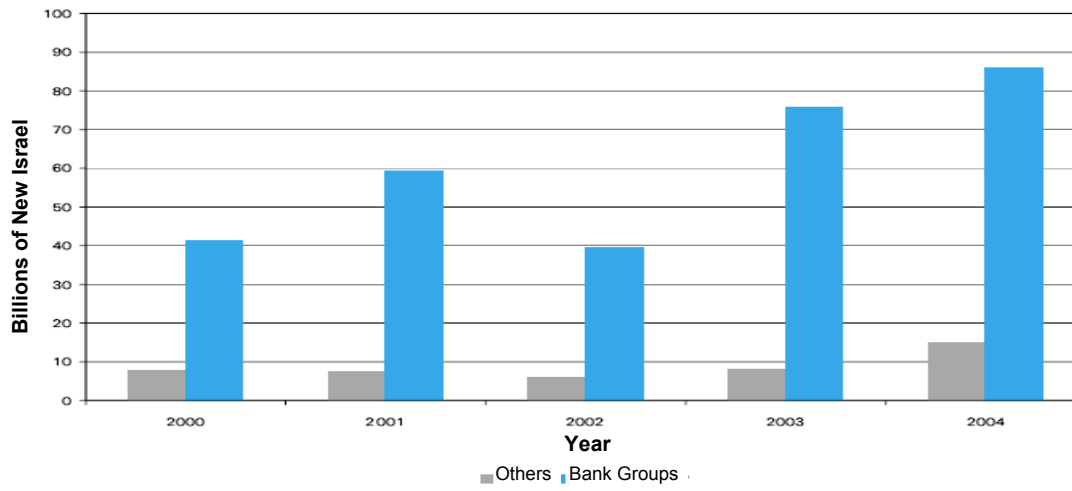
Authority did in fact review the request and decided to partially reduce one of the three fines imposed on the fund manager. The fund manager submitted an additional appeal against this decision. The Court rejected the appeal stating that the fines were legally imposed and that the due concern taken by the Authority, under section 117[b][2] of the law was reasonable and that there was no justification for appeal.—File 3011/04

- b. An appeal by a fund manager against the decision by the Authority to reduce 25% of the total of fine imposed. [and this further to the decision of the Supreme Court in the matter of Afikim, see paragraph b above, and the 2003 Annual report, pages 29-30, paragraphs b and c]. The appeal was cancelled by the fund manager at the recommendation of the Court- File 3015/04.
- c. An additional appeal on the principle of imposing a fine and on the decision not to stay the decision because of special considerations is pending before the Court- File 3055/04

Graph 3: Number of Mutual Funds 2000-2004



Graph 4 – Value of Assets of Mutual Funds - 2000-2004



Chapter 6 - Supervision over the Secondary Market and the Stock Exchange

Under its mandate, the Authority also deals with the subject of supervision over the proper and fair management of the stock exchange. In addition, the Authority operates, on the basis of the provisions of chapter h of the Securities Law. That chapter deals with the Authority's supervisory powers regarding setting provisions of the stock exchange bylaws and regulations, and the duty of supervision over the proper and fair management of the stock exchange. A representative of the Authority follows discussions of the board of directors of the stock exchange and its committees, and serves as an observer in said negotiations.

Within this framework, the Authority also deals with enforcement of the provisions of the Prohibition on Money Laundering Law, 5760-2000, together with the Prohibition on Money Laundering Directives [Requirements for Identification, Reporting, and Record Management of Stock Exchange Members], 5761-2001. In order to carry out this position the Authority checks how members of the stock exchange comply with responsibilities imposed upon them, by the provisions of the Prohibition on Laundering Law and Directives.

In addition, the Authority deals with requests submitted by the public regarding its fields of operations

Changes in the Stock Exchange Bylaws and Directives

Within the framework of the Authority's supervision over the proper and fair management of the stock exchange, the Authority's recommendation to the Minister of Finance is required as a precondition to making any changes in the stock exchange bylaws. In addition, the Authority's approval is also required when the stock exchange proposes to enact rules that include details regarding various items in the bylaws. Accordingly, the Authority considered and approved changes, and recommended the adoption of amendments, that the stock exchange initiated for changing its bylaws, as set out below:

1. On February 24, 2004 [Adar 5764]:

- a. The Authority approved an amendment to the guidelines regarding a reduction in the units of the TA 25 Index for calculating limitations on open positions.
- b. The Authority approved an amendment regarding the linkage of handing fees for the transfer of membership in the stock exchange to the parent company – correction of error.
- c. The Authority approved an amendment to the guidelines regarding the minimum periods of time for keeping documents.

2. On March 2, 2004 [Adar 5764]:

The Authority approved amendments to the guidelines on special open trading in securities included in stock exchange indices.

3. On April 20, 2004 [Nissan 5764]:

- a. The Authority approved a guideline regarding a reduction in the steps for submitting orders for securities and convertible securities.

- b. The Authority recommended that the Minister of Finance amend the bylaws, and also approved an amendment regarding changes in sections dealing with credits and guarantees.
- c. The Authority approved, for a period of one year, temporary measures regarding principles for registering dual listed companies for trading - companies which do not report in accordance with the law on dual listing.
- d. The Authority approved an amendment regarding an issue tender, without setting a maximum price [limitation on amount ordered].

4. On April 28, 2004 [Iyar 5764]:

The Authority approved, for a period of one year, temporary measures regarding the system of trading for institutional investors.

5. On May 23, 2004 [Sivan 5764]:

- a. The Authority approved an amendment regarding the maintenance – change in definition of shareholders' equity.
- b. The Authority approved an amendment regarding an issue to institutional investors.

6. On June 8, 2004 [Sivan 5764]:

The Authority made a recommendation to the Minister of Finance regarding approval of an amendment to the bylaws on trading in matching orders, and an amendment to guidelines.

7. On July 13, 2004 [Av 5764]:

- a. The Authority approved an amendment regarding the request for guarantees from a member who is not a member of the "Maof" clearinghouse.
- b. The Authority made a recommendation to the Minister of Finance regarding an amendment to bylaws on the supervision over credits and guarantees.
- c. The Authority approved an amendment regarding a reduction in commissions that the stock exchange collects.
- d. The Authority approved an amendment regarding increases in fees of members of the stock exchange for foreign clearinghouse activities.
- e. The Authority made a recommendation to the Minister of Finance regarding stock exchange bylaws on futures contracts on "Shahar" certificates.

8. On August 8, 2004 [Av 5764]:

The Authority approved an amendment regarding limitations on the quantity of securities that can be ordered in an issue by a buyer.

9. On September 6, 2004 [Elul 5764]:

- a. The Authority made a recommendation to the Minister of Finance regarding an amendment to the bylaws on the renewal of trading after canceling the reason for the halt in trading.
- b. The Authority approved an amendment regarding procedures on requests for securities licenses, examination and securities registration fees.

- c. The Authority approved an amendment regarding rating companies and the valuation of securities which serve as guarantees, and regarding the classification of the First International Bank in the first tier.
- d. The Authority approved an amendment regarding commissions.
- e. The Authority made a recommendation to the Minister of Finance regarding an amendment of bylaws on broadening the definition of the term "financial assets".
- f. The Authority made a recommendation to the Minister of Finance regarding an amendment of bylaws on guidelines that are binding on a "company under supervision", and approved a change in guidelines on same.
- g. The Authority approved of a change in guidelines regarding proposed changes to stock exchange indices.
- h. The Authority approved a change in guidelines regarding the manner of submitting orders for an issue.
- i. The Authority made a recommendation to the Minister of Finance regarding a change in the bylaws on broadening the field of permissible operations, and in the matter of issue of financial asset - backed securities.
- j. The Authority made a recommendation to the Minister of Finance regarding a change in the bylaws on options on individual shares, and approved changes to guidelines regarding same.
- k. The Authority approved a change in guidelines regarding futures contracts on implicit debt certificates bearing returns based on "Shahar" bond returns.

10. On November 16, 2004 [Kislev 5765]:

The Authority approved, for a period of one year, temporary measures concerning the issue of commodity certificates.

11. On December 12, 2004 [Kislev 5765]:

- a. The Authority made a recommendation to the Minister of Finance regarding a change to the bylaws on updating of the guidelines for dual listings. The Authority also approved amendments on same, and also approved a change and an extension by one year, of temporary measures regarding foreign members of the stock exchange.
- b. The Authority made a recommendation to the Minister of Finance regarding a change to the bylaws on changes to guidelines concerning the issue of index linked certificates on stock exchange indices. The Authority approved changes to these guidelines.
- c. The Authority approved changes to guidelines regarding changes in the steps to issue orders for bonds.
- d. The Authority approved changes to guidelines regarding setting dates for securities delisting from trading
- e. The Authority approved, in principle, a recommendation to the Minister regarding a change in the stock exchange bylaws regarding guidelines on maintenance, and approved guidelines on same.

Chapter 7 - Licensing and Supervision of Investment Advisors and Investment Portfolio Managers

1. Licensing

Within the framework of licensing investment advisors and portfolio managers under the Regulation of Investment Advice and Investment Portfolio Management Law, 5755-1995, ["law regulating advice"] during June and December 2004, examinations were held in the following subjects:

- a. Securities laws and professional ethics;
- b. Accounting;
- c. Statistics and finance;
- d. Economics;
- e. Analysis of securities and financial instruments;
- f. Portfolio management [for those requesting a license to manage investment portfolios].

In total, 4,012 examinations were held, and 3,629 candidates were tested. 2,396 candidates successfully completed the tests [see table 10 below].

The Regulation of Investment Advice and Investment Portfolio Management Law [License Application, Examinations, Apprenticeship and Fees] Regulations, 5757-1997 ["Apprenticeship Regulations"], provide that candidates, who prove that they hold a relevant degree or who prove that they took relevant courses in a recognized institution, as defined in the regulations, are entitled to exemptions from one or several examinations. During 2004, 4,322 applications for exemptions were reviewed, and of these 3,582 were approved.

During the year, 506 apprenticeship applications were approved, of which 363 were in investment advice, and 143 were in portfolio management. In addition, 386 individuals received licenses [see table 11 below].

As of December 31, 2004 [Tevet 5764], there are 4,304 individual licensees, 146 companies with licenses to manage investment portfolios and 25 companies with licenses as investment advisors.

During the reporting year, 184 licensees had their licenses suspended or cancelled; of 181 licensees requested the suspension or cancellation – composed of 48 investment portfolio managers, and 133 investment advisors.

The Authority cancelled three licenses according to the following breakdown: two portfolio managers and one investment advisor. The licenses were cancelled in accordance with the Authority's right under sections 10[a] and 10[c] of the law regulating advice. This law deals with the right of the Authority to cancel the license of someone who ceases to comply with the conditions for granting a license.

In addition, the licenses of 14 companies were suspended or cancelled, at their request: 13 companies which provided investment portfolio management and one company which provided investment advice.

| Examination subject | Number of candidates | Passing percentage |
|---|----------------------|--------------------|
| 1. Professional ethics | 478 | 79.7 |
| 2. Securities laws and professional ethics | 1,104 | 66.8 |
| 3. Accounting | 208 | 73.1 |
| 4. Statistics and finance | 258 | 63.2 |
| 5. Economics | 186 | 53.2 |
| 6. Analysis of securities and financial instruments | 879 | 62.0 |
| 7. Portfolio management | 516 | 61.8 |

| License granted based on Year | Portfolio Managers | | | | | Investment Advisors | | | | |
|--------------------------------------|--|----|--|----|-------|--|----|--|----|-------|
| | Exemption from examinations based on experience ¹ | | Passing examinations or exemption based on studies | | Total | Exemption from examinations based on experience ¹ | | Passing examinations or exemption based on studies | | Total |
| | Total | % | Total | % | | Total | % | Total | % | |
| 1997 | 198 | 56 | 153 | 44 | 351 | 1,578 | 86 | 255 | 14 | 1,833 |
| 1998 | 51 | 60 | 33 | 40 | 84 | 386 | 71 | 154 | 29 | 540 |
| 1999 | 13 | 19 | 56 | 81 | 69 | 171 | 56 | 137 | 44 | 308 |
| 2000 | 35 | 34 | 68 | 66 | 103 | 65 | 28 | 167 | 72 | 232 |
| 2001 | 8 | 7 | 100 | 93 | 108 | 38 | 12 | 274 | 88 | 312 |
| 2002 | 5 | 6 | 72 | 94 | 77 | 25 | 9 | 252 | 91 | 277 |
| 2003 | 6 | 7 | 82 | 93 | 88 | 6 | 2 | 245 | 98 | 251 |
| 2004 | 1 | 1 | 112 | 99 | 113 | 7 | 3 | 266 | 97 | 273 |
| Total licenses | 317 | 32 | 676 | 68 | 993 | 2,276 | 57 | 1,750 | 43 | 4,026 |

2. Supervision

The supervision of investment advisors and portfolio managers is centered on three main areas:

- a. Making inspections under section 28 of the law regulating advice and the Anti Money Laundering Law;
- b. Enforcing the duty of filing reports under section 27 of the law regulating advice, and the examination of reports submitted;
- c. Investigating suspicions of violations, under the law regulating advice.

¹. Experience - experience during the "relevant period" - the period beginning on August 9, 1994 and ending on June 30, 1997, or at least seven years experience out of the ten years prior to January 31, 1997 [see also the 1998 Annual Report, page 23, paragraph 1a].

A. Inspections

During the reporting year, three kinds of inspection were made:

1. Broad inspection — an inspection that examines one issue in a large sample of companies.
2. An inspection of compliance with the provisions of the Anti Money Laundering Law and compliance with the insurance requirements. These inspections were made within the framework of the efforts invested this year in assimilating the provisions of the Anti Money Laundering Law and Directives [Requirements for Identification, Reporting and Record Management by Portfolio Managers], 5762-2001 ["Anti Money Laundering Directives"]
3. In - depth inspections - the inspection of specific issues at companies holding licenses and at investment advisors employed by banking entities.

It should be noted that the inspections were made at the offices of the companies and at bank branches, with the exception of broad inspections, in which the companies were required to submit documents to our office.

Broad inspections:

1. During the reporting year, a broad inspection was completed on the issue of compliance with section 18 of the law regulating advice, regarding the customer's consent, in advance and in writing, to the purchase of special risk assets. Forty-five companies were examined in this regard.
2. During the reporting year, a broad inspection was started regarding compliance of portfolio management companies related to underwriters, with the provisions of section 16 of the law regulating advice, concerning the customer's consent to purchase securities in a company related to the portfolio manager, or in a company related to a company in which the manager is employed, and which served as an underwriter of the issue. Thirty nine companies were examined in this inspection. As of the date of this report, the inspection has not yet been completed.

Compliance with the provisions of the Prohibition on Money Laundering Law and compliance with insurance requirements

During the reporting year, inspections were made at 15 companies, and the following matters were examined:

1. Compliance by companies with the provisions of the Prohibition on Money Laundering Law Directives. In this respect, the following subjects were examined: requirements for identification, authentication of details, declaration of a controlling shareholder and the beneficiary, face – to - face identification, keeping identification documents, reports to the Anti Money Laundering Authority and maintaining a computerized database.
2. Compliance by companies with the provisions of Investment Advice and Investment Portfolio Management Law [Equity and Insurance] Regulations, 5760-2000. In this respect, the fields of insurance coverage and self participation were examined.

Specific inspections:

1. During the reporting year, four specific subject inspections were carried out at four portfolio management companies, in which one or more of the following subjects were examined:
 - a. Agreements with clients;
 - b. Matching service to the customer's needs;
 - c. Fair disclosure to the customer of significant matters concerning a transaction or advice given;
 - d. Investments in special risk cases;
 - e. Ban against taking inducements;
 - f. Compliance by companies with capital requirements.

2. During the reporting year, five specific subject inspections were carried out with bank investment advisors who offered advice on mutual funds of companies related to the banks. In this regard the inspection centered on the advisor's compliance with:
 - a. Fiduciary duty;
 - b. Matching service to the customer's needs;
 - c. Agreements with clients;
 - d. Fair disclosure to the customer of significant matters concerning advice given;
 - e. Notice to clients of conflict of interest.
 - f. Ban on preferential treatment;
 - g. Ban against taking inducements
 - h. Memorandum of advice given.

B. Enforcement of Duty to Report and Examination of Reports

During the reporting year, the following actions were taken to enforce the reporting duty, and the following reports were examined:

1. Regarding annual reports in accordance with section 27[a] of the law regulating advice, and regulation 8 of the regulations on apprenticeships, the following actions were taken:
 - a. In cases where deficiencies were noted in the accountants' opinion letter appended to the annual report – letters were sent to the accountants and to the companies. Following this, the Authority initiated, together with the Institute of Certified Public Accountants, a seminar on this subject [see paragraph 5 below].
 - b. In cases where the accountants' opinion was not in accordance with the recommended terminology, as published by the Institute of Certified Public Accountants, the companies were requested to correct their review or to justify the deviation from said terminology.
 - c. In cases where there was doubt regarding the abilities of some companies to comply with capital requirements, whereas those companies increased their capital through the creation of interested parties debts to the company, they were requested to provide details and explanations to the Authority in this respect, and, if necessary, were requested to increase their capital, in accordance with generally accepted accounting principles.

- d. Companies which did not comply with regulation 5 of the insurance regulations, which decree that self participation will not exceed 5% of the minimum insurance requirements, were requested to correct this deficiency.
2. From a review of the annual reports, it was noted that a number of companies did not submit their reports on non compliance with the conditions for licensing, according to section 27[c] of the law regulating advice, on time.

These companies were served with reprimands advising them that in the future civil fines would be imposed for violations of their reporting requirements.

C. Investigating Suspicions of Violations under the Law Regulating Advice

Among its activities, the licensing and supervision of investment advisors and investment portfolio managers department investigates suspicions of violations of the law regulating advice. The investigations are made following complaints from the public, or as a result of suspicions that arise during the regular work of the department. When a suspicion of a criminal breach or a disciplinary breach arises, the matter is referred for investigation.

In 2004, 53 cases were handled involving initial suspicions of criminal and/or disciplinary breaches, of which 18 cases were carried over from prior years.

Of the 53 cases which were handled:

In 11 cases - it was found that there were suspicions of disciplinary offenses for violations of fiduciary trust, matching of service to the needs of the customer, drawing up of consultation agreements with the customer and the recording of consultations. These cases were referred for disciplinary investigation.

In one case - the complaint was referred to the District Attorney, in addition to the case already under examination. An additional case was forwarded to the attention of Israel Police, and another case was forwarded to another department at the Authority.

Twenty three other cases were investigated and closed for one or more of the following reasons:

- No violation was found of the law regulating advice, or of any other law under the supervision of the Authority,
- Lack of evidence,
- No cooperation by the complainant, a matter which stymied the ability to deal with the complaint,
- Lack of interest to the public because of the time that passed from the original offense until the submission of the complaint, or because of the immateriality of the case.

At the end of the reporting year, seven cases were still open.

3. Disciplinary Proceedings

A. Disciplinary investigations

During the year 17 investigation files were opened, of which 14 dealt with reservations concerning advice given to clients while giving preference to financial assets of an entity related to the entity which employed the advisor, and three other files which dealt with possible violations because of the inappropriateness of service given to clients, the lack of written agreements as required, and lack of caution in giving promises to clients. One file also included the suspicion of a criminal violation of granting advice without a license to do so.

During the year 17 investigation files were closed, as follows

Fourteen files that were opened during the year, but regarding same it was recommended that certain investment advisors be brought before disciplinary action because of the suspicion of offering investment advice while giving preference to financial assets of an entity related to the entity which employed the advisor. Because of that said, the files were referred to the District Attorney.

Two files that were opened in 2002, included a recommendation for disciplinary and criminal action, were referred to the District Attorney. One file dealt with disciplinary violations because of the lack of written agreements with the customer, and the ordering of securities of a related entity which served as underwriter to the issue without receiving the customer's consent in advance and in writing. Another file involved disciplinary violations because of the mis-match of services to the customer's needs and a violation of caution, and for a criminal violation of managing portfolios without a license to do so.

One file from 2002 was closed, because of the lack of proof that an offense was created.

B. Disciplinary complaints

Up to now, nine complaints have been submitted to the disciplinary committee. Six complaints were dealt with by the committee, and five were closed during the year, as follows:

1. Against Moritz and Tuchler Ltd., a complaint was served during 2003. That company did not have some of their clients sign agreements according to section 31[a] of the law regulating advice, and did not include all details necessary in agreements according to section 31[b] of said law for other clients, all this relevant from 1996 until the beginning of 2000. In their plea, which was approved by the disciplinary committee, the company confessed to the facts detailed in the disciplinary complaint. As noted in last year's report [see the 2003 annual report, page 42, paragraph 3], the committee fined the company NIS45,150.

The disciplinary committee noted in its decision that the violations were committed by the company before the control was transferred to Bituah Ya'shir, Financial Assets Ltd. Management of the company was replaced upon transfer of control in 1.9.2003. The company reported to the disciplinary committee that from 2001, it had taken steps to adjust its portfolios to the requirements of the law.

2. Against so and so, who served as mentor to an employee who was apprenticing in investment advice at a bank - during 2003 a disciplinary complaint was submitted because of a misleading report regarding the absence of said apprentice, a matter which constitutes a violation under regulations 19 and 23 of the apprenticeship regulations. According to his statement, the disciplinary committee concluded that he violated all said regulations. In its decision, the committee received the approval of the parties involved and reprimanded the mentor. In its decision, the committee decided that its decision will be published without noting the name of the bank, the name of the apprentice, or the respondent.
3. Against so and so, who served as a mentor to an employee who was apprenticing in investment advice at a bank – during 2003 a disciplinary complaint was submitted because of a misleading report regarding the absence of the apprentice. The mentor reported on the completion of the training period of the apprentice a number of months after he stopped serving under his supervision, even though, according to the regulations he had to do so within seven days. The mentor also did not note that the apprentice was absent from his employment under his supervision for a period of 23 days. Accordingly, the respondent violated regulations 18 and 32 of the apprenticeship regulations. The committee decided to reprimand the respondent. In its decision, the committee decided that its decision will be published without noting the name of the respondent, the name of the apprentice, or the bank.
4. Disciplinary complaints were served in 2003 against Mr. Ze'ev Cohen, a licensed portfolio manager, and against Machshava Consulting and Management Ltd. ["Machshava"] as follows:
 - a. 171 counts of not signing agreements for management, under section 31[a] of the law regulating advice.
 - b. Not receiving the agreement of clients, in advance and in writing, for the purchase of securities, in a company related to Machshava and which served as underwriter to the offer – violation under section 61[b] of the law regulating advice.
 - c. One count of conditioning management fees to the return earned on the customer's investment portfolio – a violation under section 24 to the law regulating advice.

Under the plea bargain that was accepted by the disciplinary committee, Mr. Cohen admitted to carrying out the violations that he and Machshava were accused of, and the following penalties were imposed:

- a. The license of Mr. Cohen was suspended for two years.
- b. The license of Machshava was canceled for 10 years.
- c. A fine of NIS100,000 was levied on Mr. Ze'ev Cohen.

It was further decided that Mr. Cohen would inform his clients in writing of the fact that he was brought before disciplinary committee and that he was punished by the committee.

5. A disciplinary complaint was served in 2003 against Mr. Harry Sapir, a licensed portfolio manager. The disciplinary committee decided to honor the agreement that was signed between the Authority and Mr. Harry Sapir, according to which Mr. Sapir admitted that as an investment portfolio manager he held powers of attorney to manage portfolios of clients at the Israel General Bank Ltd. and at United Mizrahi Bank, and voted in the name of his clients at two general meetings of Arad Investments and Industrial Development Ltd. to approve transactions, while at the same time he was director in the company representing controlling shareholders, without advising his clients of the conflict of interest, between his interests and the interest of his

clients, and without receiving their consent to vote in their name for approval of the transaction, in advance and in writing, and therefore violated regulation 15[a] of the law regulating advice. After approval of the transactions, Mr. Sapir purchased shares on behalf of his clients at a price in excess of the market price on the stock exchange, and thus showed preference for the affairs of the company and its controlling shareholders, both of which were his clients, over the interests of his clients, and thus violated section 11[a] of the law regulating advice. Mr. Sapir also did not draw up agreements in writing with his clients, and thus violated regulation 13[a] of the law regulating advice.

The agreement that was signed between the Authority and Mr. Sapir related to all the open proceedings against him at the time: a criminal proceeding, a disciplinary proceeding and an administrative proceeding. The committee decided to honor the agreement also regarding the punishment and to impose the following penalties on Mr. Sapir:

Suspension of license to manage portfolios and for providing investment advice for a period of one year and a reprimand, this taking into account the fact that for his conviction in the criminal proceeding, the Authority will cancel his license under the administrative proceeding.

Mr. Sapir was found guilty for his actions to bring about an approval of transactions with controlling shareholders on 16.9.2003 by the District Court of Tel Aviv [Criminal file 40200/99]. See the 2003 annual report, pages 64-65, paragraph m.

4. The Committee to Impose Financial Sanctions in Accordance with the Prohibition on Money Laundering Law

Further to the findings of the audit that was undertaken at portfolio management companies and at members of the stock exchange, 12 cases were brought before the committee. In these cases, the audit found violations of the regulations and directives on anti money laundering procedures, including 11 cases involving investment portfolio managers and one case of a member of the stock exchange, as follows:

Portfolio management companies:

| | Name of company | Section violated² [Anti Money Laundering Prohibition]: | Committee decision |
|----|--|--|---------------------------------|
| 1 | Nessuah-Zannex Investment Management Ltd. [today Excellence Nessuah Brokerage Services Ltd.] | 8[5], 18[a] and [b] | NIS15,000, financial sanctions |
| 2 | Gaim Paragon [Israel] Ltd. | 2,3,4,7 and 15 | NIS15,000, financial sanctions |
| 3 | Pe'elim Portfolio Management Ltd. | 7,6,4,3,2,8[5] and 18[a] | NIS200,000, financial sanctions |
| 4 | Momentum Capital Markets Ltd. | 2,3 and 4 | Reprimand |
| 5 | Proxima Investments Ltd. | 2,3 ,4, 8[1] and 15[a] | Reprimand |
| 6 | Lehava Investments Ltd. | 2,3 and 18 | NIS40,000, financial sanctions |
| 7 | T.I.M. - Performance Ltd. | 2,3,7 and 18 | NIS25,000, financial sanctions |
| 8 | Quattro Investment Portfolio Management Ltd. | 2,3,7,15[a] and 18[a] | NIS10,000, financial sanctions |
| 9 | Simodan Investments [1990] Ltd. | 2,3,7,9,15[a] and 18 [a] | NIS30,000, financial sanctions |
| 10 | Menorah Gaon Investment House Ltd. | 8[5] and 18 | NIS100,000, financial sanctions |
| 11 | Analyst Exchange and Trading Services Ltd. | 8[5] and 18 | NIS10,000, financial sanctions |

Members of the Stock exchange

| | | | |
|----|-------------------------|---|--------------------------------|
| 12 | Moritz and Tuchler Ltd. | 3 | NIS30,000, financial sanctions |
|----|-------------------------|---|--------------------------------|

The financial sanctions [fines] were deposited with the fund set up according to section 36a of the Law for Dangerous Drugs [New Version] 5733-1973.

² Violations:

Paragraph 2 - recording identification details; paragraph 3 - verifying details, paragraph 4 - declaration on controlling shareholder and beneficiary; paragraph 6 - "face to face" identification; paragraph 7 - keeping identification documents; paragraphs 8 and 9 - duty to report to the Authority on money laundering; paragraph 18 - transitional provisions.

5. Briefings

In order to augment the professional knowledge of those concerned, the Authority arranged the following activities:

- a. A seminar on the subject of the law regulating advice. This seminar was held on 29.11.2004, with the participation of the Chairman of the Authority, the Managing Director of the Stock Exchange, the Chairman of the Financial Division of the Federation of Israeli Chambers of Commerce, representatives of the Authority on the Prevention of Money Laundering, and employees of the department for licensing and supervision over investment advisors and investment portfolio managers at the Authority. The seminar day was dedicated to brief the participants on the following subjects:
 1. Implementation of the law in a manner which will fulfill the intentions of the legislator and the changes expected.
 2. The duty of trust of portfolio managers and keeping the interests of the client.
 3. The annual report and the auditors review.
 4. Reports on exceptions, according to the provision against money - laundering.

- b. A seminar evening for accountants was held on 29.12.2004, and dealt with the issue of auditing at companies managing investment portfolios, with the participation of the President of the Institute of Certified Public Accountants and his assistants, senior accountants and members of the Authority's staff. The seminar dealt with the responsibilities of auditors of investment management portfolio companies, and in all aspects on same in the annual report which is submitted to the Authority.

Chapter 8- General Counsel

1. Legislation and Subordinate Legislation that was Enacted or Approved, During the Report Year

A. Securities Law [Amendment no. 23], 5764-2004 [Sefer HaHukkim - Book of Laws 1946, page 427]

The law was published on June 28, 2004 [9 Tamuz 5764] and it is the outcome of the Authority's proposal following adoption of the recommendations of the Barnea Committee for a re-examination of the model for disclosure of a company's operations in a prospectus and in related reports ["the committee"]. [See also the 2002 annual report, page 47]

The principle matters are: setting special norms of responsibility for forward looking information in a prospectus, and in the regular reports of reporting entities, which will provide a safeguard for forecasts, evaluations and estimates, which by their nature may not be fully realized; establishing the responsibility set out in law on misleading items in a prospectus and in the periodic reports, and matching the responsibility of the entity and its advisors for information given to the public in a prospectus and in the current report; establishing the responsibilities of the controlling shareholder and the managing director in an entity for misleading details in a prospectus, and coordinating the written opinion of legal counsel [in the prospectus] such that it will be binding on significant matters for which legal counsel for the prospectus appends his opinion.

The principle recommendations of the committee relating to the disclosure necessary on the entity's operations are presented in the regulations that were published [see paragraphs k, m and n below].

B. Securities Law [Amendment no. 24], 5764-2004-[Sefer HaHukkim - Book of Laws 1955, page 492]

The law was published on August 10, 2004 [23 Av, 5764] and it sets out new procedures for two main subjects: At present, section 15 of the Securities Law states that it is possible to offer securities to the public only after the publication of a prospectus that the Securities Authority gave a permit for. The new procedure will permit the offeror to offer securities to the public already after submitting a draft prospectus to the Authority [road show], and the sale of securities to the public will be conditional upon receiving a permit from the Authority. In addition, at present there is a duty to sell securities intended for trading on the stock exchange in an equitable manner ["the equitable offer"]. This principle will continue to be binding also after approval of the amendment. However the authorization of the Minister of Finance will be added to regulations relating to cases where it will be possible to deviate from the principles of an equitable offer. The agreement will not be binding on the equitable price.

In addition, the amendment permits the non-inclusion of the price of the security and its derivatives in the prospectus, and in the follow up notice. In addition, the amendment sets out limitations on the sale and holding of securities with the intent to prevent conflicts of interest between the underwriter and investors, and limitations on the ability of the company to indemnify the underwriter.

Additional changes that were made in the framework of this amendment include: cancellation of the law regarding the period to submit orders, and its replacement by authorizing the Minister to set the period, as stated in the regulations. In addition, the principle was added that the decision of the Authority is considered as a decision of the State in matters of the payments of taxes and civil damages.

In order to implement the amendment of the law, and to create a new and complete procedures regarding underwriting and underwriters, the Authority is submitting four groups of regulations [see paragraph v below, in the paragraph on draft and subordinate legislation below]. Most of the new procedures will become effective on the date set out in said regulations.

C. Regulation of Investment Advice and Investment Portfolio Management Law [Amendment no. 6], 5765-2004 [Indirect Amendment under Amendment no. 24 to the Securities Law] [Sefer HaHukkim - Book of Laws 1955, page 492]

The law was published on August 10, 2004 [23 Av 5764] as an indirect amendment under the framework of Amendment no. 24 to the Securities Law [see paragraph b above], dealing with the definition of underwriting undertakings, in a manner that ties it into the definition given in the Securities Law.

D. Securities Law [Amendment no. 25], 5764-2004 [Sefer HaHukkim - Book of Laws 1961, page 18]

The law was published on November 17, 2004 [4 Kislev, 5765] and it permits the offer of securities on the basis of a "shelf prospectus" – a prospectus for securities that can be offered a number of times and on different dates over a period of two years, except that a framework for all offerings will be set out already at the date of submitting the prospectus, all this with the intent of easing the burden on issuers who will meet the requirements set out in the regulations to raise capital from the public, and to increase the marketability of their securities.

In addition, the amendment also expands the definition of "marketable security" [eliminating the lack of indexation to the CPI, price and tradability on the stock exchange] in order to ease the burden on the issuer of marketable securities in the capital markets and to encourage the use of these financial instruments.

The proposed amendment was undertaken in the framework of implementing the recommendations of a committee that was set up by the Authority to examine the requirements of disclosure in a prospectuses offering of marketable securities or bonds [non convertible] ["Bachar Committee"]. Implementation of this must be by legislation, taking into account the recommendations of another public committee ["Barnea Committee"], procedures that guarantee comprehensive and detailed current reporting which will enable said amendment [see also paragraphs a, m and n].

Most of the procedures become effective [save for a correction to the definition of marketable security] on the date that the regulation becomes effective [see paragraph m on proposed primary and subordinate legislation].

E. Securities Law [Amendment no. 26], 5764-2004 [Sefer HaHukkim - Book of Laws 1961, page 19]

The law was published on the November 17 2004 [4 Kislev 5765] and its intent is to grant a preferred position to the stock exchange clearinghouses in the matter of liens of marketable securities. The procedures set out guarantee a preferred proprietary position for the clearinghouses regarding marketable securities traded on the stock exchange and to the financial proceeds, and this in order to guarantee the financial stability of the clearinghouses, a stability, which in absence of same, could damage the entire stability of the financial system.

F. Joint Investment Trust Law, [Amendment no. 9], 5765-2004 [Sefer HaHukkim - Book of Laws 1965, page 39]

The law was published on December 15, 2004 [3 Tevet 5765]. Its purpose is to permit the integration of reports by mutual fund managers and their mutual fund trustees into the Authority's electronic reporting system, and the publication of reports on the Authority's internet distribution site. The changes are in the form of amendments to the Securities Law [Amendment no. 22], 5763-2002 [see the 2002 annual report, page 47], as adjusted for necessary changes.

An additional change included in this proposal, and which is not related to the operation of the electronic reporting system, relates to authorizing the Chairman of the Authority to order distributors to send immediate notices to the holders of mutual funds, at their known addresses, if the Chairman is of the opinion that the information included therein has special importance to the holders of the unit certificates.

The change will become effective subject to the publication of notices in accordance with Securities [Electronic Signature and Reporting] Regulations [Amendment], 5765-2004. These regulations were approved by the Finance Committee of the Knesset on November 24, 2004, were signed by the Minister of Finance and are to be published shortly [see paragraph q below].

G. Regulation of Investment Advice and Investment Portfolio Management Law [Amendment no. 7], 5765-2004 [Sefer HaHukkim - Book of Laws 1965, page 41]

The law was published on December 15, 2004 [3 Tevet 5765]. Its purpose is to require electronic reporting by companies managing investment portfolios and companies offering investment advice.

The change will become effective subject to the publication of notices in accordance with Securities [Electronic Signature and Reporting] Regulations [Amendment], 5765-2004. These regulations were approved by the Finance Committee of the Knesset on November 24, 2004, were signed by the Minister of Finance and are to be published shortly [see paragraph q below].

H. Securities [Periodic and Immediate Reports] [Amendment], 5764-2004, Kovetz HaTakanot – Collection of Regulations - 6313, page 488]

The regulations were published on May 6, 2004 [15 Iyar 5764]. They concern reports to the investing public, where a company whose securities are held by the public is a party to a merger [see the 2002 annual report, page 48]. Further to the provisions of the Companies Law regarding mergers of companies, a need was created for this report. The regulations set out the form of the report that is to be submitted, while differentiating between a "significant merger" and a "merger which is not significant". The threshold of significance is 20%, according to criteria of profitability; overall investment, number of shares allocated, and total assets. These disclosure requirements are identical in principle to those existing today in Securities [Offering of Securities

not to the Public] Regulations, 5760-2000, and Securities [Transaction between a Company and Controlling Shareholder therein] Regulations, 5761-2001. A "significant merger" report includes an explanation of the main points of the merger agreement, a description of the target company with financial statements attached, and details of the purchase payments made for this company and a valuation report, if such report was prepared for the transaction. A "non-significant merger" report includes a more condensed and focused explanation of the merger agreement and its consequences. The regulations also refer to a situation where the target company is a reporting company which issued bonds to the public. According to the Companies Law, which states that the results of a merger are a transfer of all liabilities of the target company to the absorbing company, these bonds become bonds of the absorbing company, and accordingly the target company is required to submit a report which includes all details required for a "significant merger". The regulations became effective 30 days after their publication date, that is - on June 6, 2004.

I. Regulations on Foreign Issuers

[1]. Securities [Transaction between a Company and Controlling Shareholder therein] Regulations [Amendment], 5764-2004, Kovetz HaTakanot – Collection of Regulations - 6321, page 657];

[2]. Securities [Preparation of Annual Financial Statements] Regulations [Amendment], 5764-2004, Kovetz HaTakanot – Collection of Regulations - 6325, page 716]

[3]. Securities [Periodic and Immediate Reports] Regulations [Amendment], 5764-2004, Kovetz HaTakanot – Collection of Regulations - 6325, page 718].

The first Kovetz HaTakanot [Collection of Regulations] was published on June 10, 2004 [21 Sivan 5764] and the two others were published on June 21, 2004 [2 Tamuz, 5764]. They state that a foreign issuer may submit financial statements drawn up in accordance with United States generally accepted accounting principles, or in accordance with generally accepted international accounting principles and those statements may be audited according to American auditing standards, or international auditing standards. The regulations became effective upon publication.

J. Securities [Periodic and Immediate Reports] Regulations, 5762-2001 [Amendment], 5764-2004, Kovetz HaTakanot – Collection of Regulations - 6325, page 719].

The regulations were published on June 21, 2004 [2 Tamuz 5764]. They regulate reporting by companies on donations. Further, the temporary measures on donations become permanent regulations, and they became effective upon publication.

K. Securities [Preparation of Annual Financial Statements] Regulations [Amendment no.2], 5764-2004 [Kovetz HaTakanot – Collection of Regulations - 6337, page 954]

The regulations were published on August 31, 2004 [14 Elul 5764]. They are part of three regulations which complement Securities Law [Amendment no. 23] 5764-2004 [see paragraph a above]. Their intent is to implement the principles of disclosure which were recommended by the Barnea Committee ["Barnea Committee Regulations"]. The regulations stipulate that the inclusion of guarantees in financial statements is required also when dealing with guarantees, limited in amounts, which could put in doubt the continuing operations of the entity in its present form, and in any event that the entity gave very material guarantees to cover the liabilities of the controlling shareholder therein [see also paragraphs m and n below].

L. Securities [Annual Fee] Regulations [Temporary Provisions], 5763-2002 [Amendment], 5764-2004 [Kovetz HaTakanot – Collection of Regulations - 6337, page 954]

The regulations were published on August 31, 2004 [14 Elul 5764]. They provide for a reduction in the annual fee for 2004 of 15% because of increased activity in the capital markets and an increase in the number of issues from the beginning of this financial year. A similar reduction is provided against the fee for annual trading which is paid by the stock exchange to the Authority. This reduction is not valid for companies subject to chapter 3 of the Securities Law - companies under dual listing, as they are liable for only half of the annual fee [that is - the full fee before the reduction in 2004].

M. Securities [Details, Structure and Form of Prospectus] Regulations [Amendment], 5764-2004, [Kovetz HaTakanot – Collection of Regulations - 6339, page 975]

The regulations were published on September 14, 2004 [28 Elul 5764] and are part of the Barnea Committee Regulations [see also paragraphs k and n]. The main points of the regulations are: the inclusion in the regulations of - the requirement to provide a description of the entity's operations in the prospectus; regulations which permit the entity to include, in the prospectus, all details required by the regulations by reference to previous reports; the requirement to state the name of the controlling shareholder in the prospectus; setting the details that must be included in the report, professional opinion or certificate included in the prospectus. The amendment becomes effective as noted in paragraph n below.

N. Securities [Periodic and Immediate Reports] Regulations [Amendment no. 3], 5764-2004 [Kovetz HaTakanot – Collection of Regulations - 6339, page 972]

The regulations were published on September 14, 2004 [28 Elul 5764] and are part of the Barnea Committee Regulations [see also paragraphs k and m]. The principle points are – expanded framework for the current report of companies, this in accordance with the recommendations of the Barnea committee [see also the 2002 annual report, page 47]. The main points of the regulations are: setting detailed requirements for describing the entity's operations in its current reports, while permitting reference to the additions to Securities [Details, Structure and Form of Prospectus] Regulations, 5729-1969 [see paragraph m above]; setting requirements that permit an entity to include details which are required to be presented by reference to previous reports; setting the details that must be included in every report, professional opinion or confirmation included in a report by the entity; including the requirement to submit a written quarterly report which will relate mainly to the significant changes that transpired from the last periodic report. The regulation will be binding on financial statements prepared for December 31, 2004 [19 Tevet 5765]. [See also paragraph s below].

O. Securities [Annual Fee] Regulations, [Amendment], 5765-2004 [Kovetz HaTakanot – Collection of Regulations - 6350, page 170]

The regulations were published on November 25, 2004 [12 Kislev 5765]. They prescribe the proportional annual fee for the year that the Securities Law or the Joint Investment Trust Law, became binding on an entity or fund, respectively. The regulations also deal with the matter of changing the rating of the entity or fund. The regulations are binding on the annual fee for 2005 and afterwards.

P. Securities [Purchase Offer] Regulations [Amendment], 5765-2004 [Kovetz HaTakanot – Collection of Regulations - 6352, page 208]

The regulations were published on December 14, 2004 [2 Tevet 5765] and deal with changes to regulations regarding two main concepts of the purchase offer: the amount of disclosure in the purchase offer, and the time framework to carry out the purchase offer and the submission of various reports. Regarding the amount of disclosure, provisions were added regarding mandatory disclosure of the sources of financing the purchase offer, and a specific regulation regarding the requirements for disclosure in the purchase offer which is not financed by external sources [self - financed]. Under the framework of the provisions dealing with timing, for example, provisions were introduced to prevent an overlap of dates for the receipt of the final purchase offers by competitors, more flexible time tables regarding the publication of the board of directors' opinion in a special purchase offer, and an easing of the last date requirement for an additional purchase offer from the offeror.

The regulations came into effect 30 days after their publication, that is - January 14, 2005.

Q. Securities [Electronic Signature and Reporting] Regulations [Amendment], 5764-2004, [MAGNA Regulations]

On November 24, 2004 [11 Kislev 5765] the Finance Committee of the Knesset approved regulations which supplement the changes to primary legislation regarding electronic reporting [see paragraphs f and g above]. These regulations are binding on the reports under the Joint Investment Trust Law and the law regulating advice. As of the date of preparing this report, the regulations have been signed by the Minister of Finance but have not yet been published.

R. Securities [Periodic and Immediate Reports] Regulations [Amendment], 5765-2004

On December 30, 2004 [18 Tevet, 5765] the Finance Committee of the Knesset approved regulations which set out the dates when the reporting responsibilities end for an entity reporting under the Securities Law, and what final reports it must submit. In addition, the regulations set out the first reports which an entity which offered its securities for the first time to the public, must submit.

The regulations will become effective 30 days after their publication. As of the date of preparing this report, the regulations have been signed by the Minister of Finance but have not yet been published.

S. Securities [Periodic and Immediate Reports] Regulations [Amendment no. 3] [Amendment], 5765-2004

On December 30, 2004 [18 Tevet 5765] the Finance Committee of the Knesset approved these regulations, concerning Barnea Committee regulations for periodic and immediate reports [see paragraph n above].

As a rule, the last date for submitting periodic reports for 2004 is, as in every year, three months after the end of the reporting year, that is March 31, 2005. However, the amendment provides, for a one time basis only, that an entity that had special and extraordinary justification, may submit its periodic report for 2004 in the expanded form up to May 31, 2005. However, in such a case, the entity will have to submit its periodic report in the old format by March 31, 2005. It will also have to state and explain the special difficulties that prevented it from submitting its report in the expanded form until March 31, 2005, and to explain the steps taken in order to submit its report in the expanded format on time, and why it was not able to do so.

In addition, provisions were added regarding the duty to submit in the expanded form will not be binding on an entity for which its responsibility to report fell before March 31, 2005, and the periodic report for 2004 is its last report. As of the date of preparing this report, the regulations have been signed by the Minister of Finance but have not yet been published.

2. Draft Legislation and Subordinate Legislation

A. Draft - Regulation of Investment Advice and Investment Portfolio Management Law, [Amendment no. 8], 5765-2005.

On September 7, 2004 [21 Elul, 5764] the Ministerial Committee for Legislation approved the draft legislation.

The proposed amendment is the first comprehensive correction from the time that the law regulating advice came into effect, and is the result of experience that has been earned over the years.

The main points of the proposed amendment are:

[1] on the one hand, limiting the exemption from a license to a portfolio manager or advisor to five clients, such that the exemption will be binding only for individuals and only for five clients in a calendar year, and, on the other hand, imposing the fiduciary duty of trust and caution set out in the law also on someone who is exempt from the license, as said above, and thus making it a duty to inform the clients before beginning the business relationship that he is not a license holder, if he doesn't hold insurance as required by a license holder, and if in the past he had a license - the reasons why he stopped holding a license;

[2] reducing the prohibition on a license holder to purchase securities for himself, such that the prohibition will not be binding on securities issued by the entity which employs a member of the license holder's family, and which were purchased in the framework of a compensation program for employees, on securities of a company traded abroad, save that the value is not less than the amount set out in the regulations, and on index linked certificates;

[3] cancellation of the possibility to receive a license to manage portfolios on the basis of experience of three years as an investment advisor;

[4] setting out the authority to legislate subordinate legislation in fields related to relations between the license holder and the client, including giving the possibility to an investment portfolio manager to manage an account also through financial institutions situated abroad, and the cancellation of the transitional provisions of the law, according to which whoever operated in Israel in portfolio management or investment advice just before the law came into effect, in the period set out in the transitional provisions was exempt from examinations for the purpose of receiving a license.

B. Draft - Securities Law [Amendment no.], [Enforcement Authority] 5765-2005

On March 21, 2004 [30 Nissan 5764] the Ministerial Committee for Legislation approved the draft legislation.

According to the proposed amendment, all enforcement authority of investigators of the Securities Authority will be channeled through the Securities Law, including the authority to incarcerate and release with bond, and there will no longer be any need to request the authorization of the Minister of Justice or the Minister of Internal Security, as is today. The proposed arrangement is in light of the Criminal Law [Enforcement Authority – Incarceration] 1996-5756, as adjusted for the needs of securities violations and investigations in these fields [see also the 2003 annual report of 2003, page 48].

C. Draft - Securities Law [Amendment no.], [Financial Sanctions], 5765-2005

On November 17, 2004 a memorandum of a proposed law was circulated. The law proposes to create an effective and deterring system to enforce the compliance with certain provisions in the law, by financial sanctions. The proposed arrangement is similar to that set out in the Joint Investment Trust Law [see the 2002 annual report, page 42]. The proposed measures can be applied in situations such as - violations of delays in submitting reports, when the main objective of the proposal is the enforcement of timely reporting by entities that report, and creating a system that is easy to operate and is effective and deterring, to deal with late submitters. The amendment is the first step in building a system of non - criminal enforcement of provisions in the Securities Law.

D. Draft - Securities Law [Amendment no.], [Exception for The World Bank], 5765-2005

On November 17, 2004 a memorandum of a proposed law was circulated. The law proposes to permit the International Bank for Reconstruction and Development, because of its international position and reputation, to offer bonds, non convertible, to the public in Israel, by registration for trading on the stock exchange in Israel and through a special arrangement, without requiring the Bank to submit a prospectus and with imposing upon it the duty of regular reporting [which is generally imposed on reporting entities].

According to the proposed arrangement, the Bank will be able to offer, to the public in Israel, said securities , on the basis of an offering document, which differs from a prospectus from the standpoint of content [which will set out in the regulations, and which will be similar to the content of registration documents that are required of entities on the dual listing system which report according to chapter 3 of the Securities Law], and for parties that bear the responsibility for them [only an issuer of special securities, however not a director of the issuer, managing director or controlling shareholder therein.]

It is proposed that the International Bank will be required to submit a series of reports to the stock exchange and to the Authority according to special arrangements, which are similar to the arrangements binding on dual listed entities which report according to chapter 3 of the Securities Law; the contents of which will be set out in the regulations by the Minister of Finance.

In addition, it is proposed to exclude information included in the financial statements [as required by the principles for preparing financial statements] from the overall concept of "forward looking statements", which because of non realization, the entity is exempt from responsibility, under certain conditions, this according to Amendment no. 32 of the Securities Law [see paragraph a above].

E. Draft - Joint Investment Trust Law [Amendment no. 10], 5764-2004

On July 13, 2004 [24 Tamuz 5764] a memorandum of a proposed law was published. The following changes are proposed, taking into account the experience that has been earned. The main subjects include - reducing conflict of interests, eliminating the barriers to operations of the funds, improving protection for the investing public, and improving information that is provided to investors in mutual funds through publication in daily newspaper and through the internet.

Among the proposed changes, the following can be noted: definition of a unique fund; expanding the possibility of fund managers to transfer investment portfolios of funds under their management to the management of outside investment managers; forbidding the payment for purchase of units from the investment portfolio, as this transaction could be considered as not in the best interests of unit holders; limiting the possibility of significant changes in the investment policy of the fund to one time per year; empowering the Minister of Finance to set conditions in the regulation such that the fund manager is permitted to finance redemptions using credits when the redemptions in that fund are especially high; canceling the limitation in the law on the price that the fund manager may pay for a transaction not carried out through the stock exchange. The limitation will be substituted by a provision in the regulations concerning the types of transactions for which the fund manager must submit a report to the Authority and the stock exchange, including transactions not carried out through the stock exchange and matching transactions; forbidding matching transactions, [transaction for which conditions are set between the parties before carrying out the transaction and are similar in nature to transactions carried out off the stock exchange], between the fund and between the investment fund manager, the trustee, controlling shareholder in the one of them and other close parties, similar to the limitation existing on carrying out a transaction off the stock exchange between a fund and parties close to the fund manager, the goal of which is to prevent a situation of conflict of interest; increasing and detailing the duties of supervision imposed on a trustee; authorizing the Minister of Finance to set provisions on the matter of the classifying funds according to groups in publications, including the offer and redemption price of the funds [all or most], including how they are classified; authorizing the Authority to set guidelines for the form of said publication; setting a clause for the prohibition against publication of data by a fund manger on a fund not under his management, on the internet; setting up a provision that when the unit holders do not attend a deferred meeting of the general meeting called to approve the appointment of the external auditor, the appointment of said auditor will be considered as approved; and a provision stating that a violation in calculating the asset value of the fund, and the collection of a fee in excess of the amount stated in the prospectus or report, will be added to the list of violations for which a civil fine will be imposed. In addition, various clarifications are proposed concerning making the fund manger take a position in voting at the general meeting of an entity, and authorizing the Authority to authorize outside parties to carry out audits.

F. Draft - Joint Investment Trust Law [Amendment no. 11], 5765-2005

The plenum of the Authority approved a proposal to change the Joint Investment Trust Law [and regulations and guidelines – see paragraphs y, z, and aa below] in order to regulate the offering of units of a mutual fund in Israel, and accordingly, to improve competition in the mutual funds sector.

Based on the responsibility to maintain the interests of the investing public in Israel, and an awareness of the possibility of supervision over foreign investment managers, and in order to prevent unfair competition with funds managed in Israel, it is proposed to permit the offer of foreign mutual fund units under the following conditions: a foreign fund set up in a country included in the closed list of countries included in the schedule to the law, for which it was found that laws and supervision on the fund manager sufficiently ensure the needs of the investing public in Israel [the Minister of Finance, on the basis of a proposal of the Authority and with consent of the Finance Committee of the Knesset is permitted to add a country to, or subtract a country from, the schedule]; the foreign fund manager has seniority and experience in management; the foreign fund manager will appoint a representative in Israel, who will serve as the contact person between the manager, the Authority and the unit holders in Israel, and he will be required to prepare an addendum to the prospectus for units in the fund, as proposed in the draft proposal, and will confirm to the Authority, by notice, that the prospectus and addendum include all the information required by the regulations; the foreign fund manager and his representatives will be open to class actions by unit holders in Israel, class actions that will be judged in Israel; the responsibilities binding on the foreign fund manager in the home country to home country unit holders will also be binding on him vis a vis unit holders domiciled in Israel; the Authority will be empowered to order the discontinuance of units offerings in Israel if it is proven that any condition under this law is no longer being met, or if the foreign fund manager or his representative did not fulfill their responsibilities under this law, or in the event of the cancellation of the consent by the supervisory body in the home country of the fund; the fund manager will be required to provide unit holders in Israel, at their request, a copy of the prospectus of the fund and its appendices, without payment; the foreign fund manager will be required to provide the Authority and unit holders domiciled in Israel, at their known addresses, all reports that he must provide, according to law, to unit holders in his home country, translated into Hebrew, at a date close to the date when he provides said reports to unit holders in the home country; an appendix will list the places where the foreign fund prices can be obtained; the regulations will require the foreign fund to meet the minimum requirements binding on funds in Israel [spreading of investments, valuation of fund assets at prices set by the stock exchange, redemption of units at the request of the unit holders, the holding of marketable securities only, the duty to prepare financial statements]. It is also proposed that the Authority will not consider an offer of units in a foreign fund under the first schedule under section 51a[b][1] of the Securities Law, that was undertaken without an offering to the public, as an offer of units in the foreign fund to the public.

G. Draft - Securities Law [Amendment no.], [Cooperation with a Foreign Authority] 5765-2005

In January, the plenum of the authority will consider for approval, a proposed change to chapter 2i of the Securities Law. This proposal is the result of the increasing need for cooperation in the field of enforcement of securities laws between the various securities authorities in the world ["foreign authorities"] and the Authority in Israel. This chapter sets out the framework for cooperation between the Authority and foreign authorities which signed a memorandum of

agreement with the Authority. The proposed change seeks to permit the Authority to be a party to international cooperation and to be a signing party of the multi party agreement with IOSCO.

It is also proposed to permit the Authority to provide aid to foreign authorities, even if the request is not considered to be a violation according to the laws of Israel, except that the subject of the request may be a violation of security laws that a foreign authority is charged to carry out and enforce.

In addition it is proposed to expand the list of matters and bodies for which the Authority may aid a foreign authority. The list of matters will be expanded such that it will include all matters and all parties, subject to the supervision of a foreign authority even if the matters and parties are not subject to supervision by the Authority in Israel.

Together with the proposed changes to the law, there is a proposal to change Securities [Cooperation with a Foreign Authority] Regulations, 5760-2000 [see paragraph bb below]

H. Draft - Securities Law [Amendment no.], [Exemption from Prospectus] 5762-2002

The proposed amendment, which has been submitted to the Minister of Finance, is intended to expand the list of exemptions that were set out in Amendment no. 20 to the law, which was published in 2000, for additional exemptions, and to change certain guidelines relating to existing exemptions [see the 2002 annual report, page 47]. This amendment is necessary in order to implement the lessons that have been learnt over time from the last amendment, and, as a result of globalization, which justifies additional relief for foreign entities whose securities are held also by the public in Israel, yet are registered for trading only on stock exchanges abroad. The relief relates only to various proposals regarding said entities, for example the amendments on exchange and amendments regarding rights.

I. Draft - Securities [Periodic and Immediate Reports] Regulations [Amendment], 5764-2004, and Securities [Details, Structure, and Form of Prospectus] Regulations [Amendment], 5764-2004 [Code of Ethics]

A proposal prepared by the Authority for the correction of the two above noted groups of amendments is at present with the Finance Committee of the Knesset.

The regulations require an entity that adopted a code of ethics, as defined in the amendment, to disclose this in the directors' report, in the form specified in the amendment. Under this amendment, there are minimum criteria which are to be included in the overall principles, which the entity adopted for itself, so that it can be classified as a code of ethics. It is also proposed that the entity will be required to state the reasons for its choice not to adopt a code of ethics, where it so chose.

J. Draft - Joint Investment Trust Law [Assets that may be Bought and Held by a Fund and their Maximum Amounts] Regulations [Amendment], 5765-2005

A proposal to amend regulations is at present with the Finance Committee of the Knesset. The proposal includes various changes made necessary because of accumulated experience. The main proposal is intended to permit new classes of funds – funds of funds and money market funds, and a new type of investment vehicle, in which funds will be permitted to invest in - debt certificates that are not listed for trading on the stock exchange. In addition it is proposed to increase the rate of investment permitted by a fund in exchange tracking funds. This proposal

was circulated among members of the relevant public and various replies were received, which were considered and integrated, where relevant, in the proposed amendment.

In the near future, the regulations will be replaced by a new version, which will relate to additional changes that are being prepared at present under Amendment no.10 to the Joint Investment Trust Law [see paragraph e above]

K. Draft - Joint Investment Trust Law [Purchase and Sale Prices of Fund Assets and Value of Fund Assets] Regulations, [Amendment], 5765-2005

A proposal to amend regulations is at present with the Finance Committee of the Knesset. The regulations deal with additional changes to proposed changes to the Joint Investment Trust Law [Assets that may be Bought and Held by a Fund and their Maximum Amounts] Regulations [Amendment], 5765-2005 [see paragraph j above], which provide proper guidance regarding the method of valuing investment vehicles, and the offer and redemption prices for the new types mutual funds which are being offered.

The proposal also gives guidance on calculating the value of bonds where trading has stopped in advance of expected redemption, and the valuation of a foreign security denominated in foreign currency, on a date when no representative exchange rate is published.

This proposal was circulated among members of the relevant public and various replies were received, which were considered and integrated, where relevant, in the proposed amendment.

L. Draft - Joint Investment Trust Law [Calculation of Yield] Regulations, [Amendment], 5765-2005

This proposal is also with the Finance Committee of the Knesset. The main objective of the proposal is to extend the time period for publishing returns on the internet.

M. Draft – Regulations Further to the Recommendations of the Public Committee Chaired by Advocate Reuven Bachar, and Amendment to the Law Regarding the Possibility to Offer Shares On the Basis of Shelf Prospectus.

As an addition to Securities Law [Amendment no. 25], 5764-2004 [see paragraph d above] the plenum of the Authority approved a proposal to amend the regulations in order to implement the provisions of the law. The proposals concern three groups of new regulations and one correction to an existing regulation, as follows:

[1] Securities Law [Shelf Issue] 5765-2005

These regulations are intended to regulate the manner in which securities will be offered under a shelf prospectus, over the period permissible.

[2] Securities Law [Period to Submit Purchase Orders Under a Prospectus] Regulations, 5765-2005

In light of the cancellation of the provisions of the law regarding the period to submit orders, and its replacement by authorizing the Minister to set the period, as stated in the regulations [see paragraph b above], these regulations propose to formalize the possibility to set various period of time to submit orders under prospectuses and under various other offering documents.

[3] Securities Law [Conditions to Offer, under a Shelf Prospectus] Regulations, 5765-2005

The objective of these regulations is to set out what conditions the issuer must meet in order to offer securities under a shelf prospectus.

[4] Securities [Details, Structure and Form of Prospectus] Regulations, [Amendment] 5765-2005

This proposal is to provide relief for the issue of marketable securities and asset backed securities. In addition the proposed amendment makes various changes to correct the law regarding an issue under a shelf prospectus.

N. Draft - Securities [Fee for Application to Grant a Permit to Publish a Prospectus] Regulations, 5764-2004; Securities [Fee for Processing a Securities Issue in a Listed Company That Was Not Offered to the Public] Regulations, 5764-2004

Further to the creation of a system to issue securities on the basis of a shelf prospectus [see paragraph d in the section on approved legislation]; a proposal is made to create a system to calculate the fee for these offerings. In addition, a proposal is made to provide a temporary exemption from the payment of the fee to request a permit to issue a prospectus to issue shares of a fund that invests in real estate, for a period of two years from the date of the amendment to the Income Tax Ordinance that defines said funds becomes effective.

In addition, various other amendments are proposed dealing with the date of updating the fixed portion of the fee [also for the fee for handling the issue of securities in a registered company which offered shares not to the public], the date of payment after the prospectus, and establishing a minimum fee for payment, cancellation of indexation on a fee refund, and an increase in the payment for late payment of the fee.

O. Draft - Joint Investment Trust Law [Offering Units of a Foreign Fund in Israel], Regulations, 5765-2005

As an additional step to the proposed Amendment No. 11 to the Joint Investment Trust Law [see paragraph f above] the plenum of the Authority proposed amendments that set out the following: conditions regarding the management of the foreign fund; bank guarantees or deposits by the manager of the foreign fund; the representative, his duties and conditions for ending his tenure; conditions regarding the foreign fund, conditions regarding the prospectus and the details included therein; conditions regarding the addendum to a prospectus, and the details therein [see also paragraph q below].

P. Draft - Joint Investment Trust Law [Immediate Report, Monthly Report, Report Concerning Unit Holdings and Report of Voting at a General Meeting] Regulations, [Amendment], 5765-2005

The Authority approved a proposed change to the regulations, to conform the reporting by fund managers to the electronic reporting system, and the addition of events for which the fund manager and the trustee will be required to issue an immediate report [see also paragraphs f and q below, in the section on approved legislation]. During the year, this proposal was circulated among members of the relevant public and various replies were received, which were considered and integrated, where relevant, in the proposed amendment. The regulations are at

present in the final stage of finalization. Consultations are underway with the Ministry of Finance and the Ministry of Justice before submitting them for discussion at the Finance Committee of the Knesset.

Q. Draft - Joint Investment Trust Law [Assets that may be Bought and Held by a Fund and their Maximum Amounts] Regulations, [Amendment], [Temporary Provisions], 5764-2004

Together with the guidelines of the stock exchange based on section 46a of the Securities Law that were submitted to the Finance Committee of the Knesset during last May, another proposed amendment to the regulations was also submitted. According to the proposal, at this stage, and as a temporary provision which will be in force for one year, a fund will not be permitted to hold marketable securities which are traded on the stock exchange in the new institutional market ["Institutional Retzef"]. A discussion on the regulations is still pending, however it is noted that also according to the present situation, taking into account the departure by funds from this guideline, the funds are not permitted to participate, at this point, in the institutional market.

R. Draft - Regulation of Investment Advice and Investment Portfolio Management Law, [Recording Investment Advice], 5765-2005

Section 25[a] of the law set out the duty of a portfolio manager to record every transaction that he undertakes with a client. Section 25[b] of the law states that the investment adviser must record every act of advice that he undertakes. From an audit that was carried out in the past, it was noted that a record is not always prepared as required. Accordingly, the proposed Amendment No. 8 to the Joint Investment Law [see paragraph a above] proposes, inter alia, to give the authority to issue regulations which will detail the recording responsibilities of investment advisors and portfolio managers. In addition, the proposed amendment sets out the responsibilities.

S. Draft - Securities [Preparation of Annual Financial Statements] Regulations, [Amendment], 5765-2005

The plenum of the Authority approved a proposed amendment to the regulations canceling the power of the Authority to grant an exemption from describing a transaction with interested parties in certain circumstances, and the granting of an exemption based on the proposed regulations when certain conditions are met. The objective of the amendment is to create the situation where the decision to make use of said exemption would be the responsibility of the entity reporting. The regulations are at present in the state final stage of finalization, and under consultation with the Ministry of Finance. Afterwards, they will be forwarded for comment to Ministry of Justice, before being submitted for discussion at the Finance Committee of the Knesset.

T. Draft – Joint Investment Trust Law [Classifying a Mutual Fund for the Purpose of Publication] Regulations, 5765-2005 and Guidelines on the Form of Publication of the Offer and Redemption Price of Mutual Funds Units, 5765-2005

As an additional step to consolidate all proposals under Amendment No. 10 to the Joint Investment Trust Law [see paragraph e above], it was proposed to establish guidelines on the form of publishing information on the funds, while classifying the funds under groupings that will be selected from a list of groupings chosen by the Authority.

U. Draft - Securities [Periodic and Immediate Reports] Regulations [Amendment], 5765-2005

During April, the plenum of the Authority approved a proposed amendment to the regulations which imposes the responsibility for immediate reports and comments on the directors' report, when dealing with a plan to repurchase shares of the company, or with a plan by a subsidiary to purchase shares of the parent company.

It was also proposed to give the possibility to issue the immediate report immediately after publication through the electronic reporting system, without the need for waiting 30 minutes, as is practice today.

V. Draft – Supplementary Regulations to Amendment No. 24 to the Securities Law Concerning Underwriting

Further to Securities Law [Amendment no. 24] 5764-2004, [hereinafter – Amendment to the Law; see paragraph b in the section on approved legislation], during the month of August the plenum of the Authority approved the following proposed amendments in order to implement guidelines of the law, as follows:

[1] Securities [Underwriting] Regulations, [Amendment] 5765-2005

The main items dealt with by this amendment are: A registry of underwriters which will include all underwriters who wish to underwrite; qualifications of underwriters; cancellation of the need for equity, but on the other hand an increase in the manner in which the deposit is held by the underwriter which serves as a security blanket for legal claims in the future and the amount of professional insurance needed; setting certain limitations on the underwriter pricing the offering, as defined in the amendment to the law which is intended to deal with possible conflicts of interest as a result of said position; on the one hand, reduction of some of the duties to report and addition of other duties, on the other hand.

[2] Securities [Offering Securities to the Public] Regulations, 5765-2005

The proposed regulations set out the principles to carry out a uniform offer in a tender [guidelines which exist today in the stock exchange by laws], guidelines to carry out an offer which is not uniform and the period to submit orders. It is proposed that the arrangement regarding the proposal which is not uniform will be considered as temporary provisions for a period of five years and that during that period, the success of the provisions will be studied.

[3] Securities Regulations [Additional Information], 5765-2005

In addition to the proposed amendment to the law, inter alia, that it will be possible to receive a permit for a prospectus that will not include different details on the price of securities offered and their quantities, and that this information may be given at a date closer to the actual sale in a notice of additional information. This proposed amendment sets out the information that must be included in the notice.

W. Draft – Various draft regulations on expanding the list of stock exchanges for dual listing
[[1] Draft - Securities Directives [Determining a Stock Exchange under the Third Schedule] 5765-2004; [2] Draft - Securities [Determining the Period of Registering for Trading on a Foreign Stock Exchange] Regulations [Amendment], 5765-2004; [3] Draft - Securities [Details, Structure, Form and Listing Documents], Regulations [Amendment], 5765-2004; [4] Draft - Securities [Periodic and Immediate Reports of a Foreign Corporation] Regulations, [Amendment], 5765-2004]

On August 17, 2004 [30 Av, 5764] the plenum of the Authority approved a number of proposed amendments dealing with broadening the binding of the special arrangements included in chapter 3 of the Securities Law ["dual listing arrangement"]

The main point of the arrangement for dual listing, which was set out in the Securities Law in 2000 - guidelines for special reports binding on entities whose securities are registered for trading on the AMEX, NYSE and NASDAQ National market in the United States [included in schedule 2 of the Law] and authorizing the Minister to add from time to time, additional stock exchanges which will be included in the arrangement, in the same form or according to changes that will be determined.

The proposed amendment is to make use of said authority and to enforce the arrangement for dual listing, subject to some adjustments on entities whose securities are registered for trading on the Small Cap market of the NASDAQ and on the London Stock Exchanges Main Market Primary Listing.

X. Draft – Directives Regulating Investment Advice and Investment Portfolio Management [Determining Financial Assets], 5765-2005 ["Draft Directives- Determining Financial Assets"] and Directives Regulating Investment Advice and Investment Portfolio Management [A Transaction Involving Special Risk], 5765-2005, ["Proposed Directive on Special Risk"]

During August, the plenum of the Authority approved, by a directive under section 1 of the law regulating investment advice, the definition of the term "financial assets" as defined in said law, such that it will also include structured products, such that the law will be binding also on these products, as the risk involved in this investment is not less than the risk involved in an investment in securities or in other financial assets. In addition, a proposal was made [as a directive on special risk], based on section 18 of said law, that a transaction in a structured product is a special risk transaction, and accordingly an investment adviser is required to inform his client of the risk involved in the transaction, and the investment portfolio manager is forbidden to carry out the transaction without receiving consent from his client in advance and in writing to carry of the transaction.

Y. Draft - Joint Investment Trust Law Regulation [Transaction Using Credits and the Maximum Amount of Indebtedness] [Amendment], 5765-2005

On August 17, 2004 [30 Av, 5764] the plenum of the Authority approved a proposed amendment to Amendment no. 10 to the Joint Investment Trust Law [see paragraph e above]. According to the proposal, an investment manager will be permitted to carry out a transaction using credits in foreign currency, if a parallel transaction in a foreign security was also carried out, such that the fund manager will maintain the exchange rate in which he carried out the foreign security transaction, all subject to regulations set out in the proposed regulations.

Z. Draft – Joint Investment Trust Law Regulation [Options, Futures Contracts and Short Sales] [Amendment], 5765-2005

On August 17, 2004, [30 Av, 5764] the plenum of the Authority approved a proposed amendment to the regulations, in order to permit funds to purchase and write options on Euro 1 and options on Dollar 1, further to their trading on the stock exchange, and this without imposing

any restriction on the amounts purchased. In addition, it is proposed to limit the possibility of a fund manager to write options in a manner which will be measured according to the securities required by the stock exchange from its members for operations in derivatives, identical to the operations of the fund manager, this to differentiate from the methods of measurement used today, which are based on the securities that the fund manager was required to actually deposit. In addition it is proposed to eliminate the right to vote at the general meeting of an issuing entity which has withdrawn the rights that are granted to the fund at the time of borrowing its securities, and this in order to prevent a situation that a double right to vote would be created on the basis of those securities.

AA. Draft – Joint Investment Trust Law [Transactions that Could Involve Conflicts of Interest and Significant Transactions] Regulation [Amendment], 5765-2005

As a supplement to proposed Amendment no. 10 to the Joint Investments Trust law [see paragraph e above] which includes a definition of a matching transaction, during August, the plenum of the Authority approved a proposal to amend the regulations such that there will be a syllogism between a transaction off the stock exchange and a matching transaction, for the purpose of receiving the approval of the board of directors of the fund manager to carry out said transaction.

BB. Draft - Securities [Cooperation with a Foreign Authority] Regulations [Amendment], 5765-2005

In addition to the proposed change to the Securities Law regarding cooperation between the authorities [see paragraph g above] the plenum of the Authority also approved a proposed change to the regulations to adjust and simplify the process of a request for help that a foreign authority submits to the Authority in Israel, in two ways: one - as the amendment to the main law proposes to cancel the requirement that the subject of the request be subject of an investigation of a criminal violation in Israel regarding the exercise of certain powers by the Authority, in the main regulations it is proposed that under the framework of the request, an explanation of events which are the basis for the request, and not the facts which are a basis for the suspicion of a violation, as stated in the main regulations; and two - simplification of the procedure for a foreign authority, such that an employee of the foreign authority by himself will be able to submit the request for help and a request by the chairman of the foreign authority will not be necessary [as is the case today]. In the same manner the process regarding the translation of documents from Hebrew to English will also be simplified.

CC. Draft – Joint Investment Trust Law [Details, Structure, and Form of a Prospectus of a Fund] Regulation, 5761-2001

These proposed amendments to the regulations, which are to replace Securities [Details, Structure and Form of a Mutual fund Prospectus], Regulations, 5729-1969 were submitted to the Finance Committee of the Knesset in 2000 [see the 2001 annual report, page 45]. During the year, the Finance Committee did not discuss the proposed regulations. Because of the proposed changes to the proposed law [see proposed Amendment No. 10 to the Joint Investment Trust Law, paragraph e above] and in other regulations to the law [such as regarding a fund of funds, see paragraph j above], and because of tax reform, there will be a need to introduce changes to the proposed amendments. With the finalization of the proposed legislation regarding said changes, an alternative version of the proposed regulations will be submitted to the Minister of Finance, such that they may be submitted to the Finance committee.

DD. Draft Proposals Regarding the Issue of Funds to Invest in Real Estate: Draft - Securities [Details, Structure, and Form of Prospectus] Regulations [Amendment], 5765-2004 and Draft - Securities [Transaction between a Company and Controlling Shareholder in Financial Statements] Regulations [Amendment], 5765-2005.

The plenum of the Authority approved a proposed amendment in accordance with recommendations of the committee regarding funds that invest in real estate, which was chaired by the Chairman of the Authority and the Income Tax Commissioner at that time [Advocate Tali Yaron - Eldar]. The recommendations were submitted in December 2003. In order to implement the recommendations, it is proposed to set out in the Securities [Presentation of Transactions Between a Corporation and a Controlling Shareholder in Financial Statements] Regulations, 5756-1996, that a fund for investment in real estate will be permitted to record assets that were transferred from an interested party, at fair value and not at the book value of the controlling shareholder before the transfer. In addition it is proposed to set out, in schedules to the Securities [Details, Structure and Form of Prospectus] Regulations, 5729-1969, requirements for special disclosure for funds that invest in real estate. Whereas in the periodic report, the entity will be required to provide details, as required, by the regulations on prospectuses [see paragraph m on the section on approved legislation], there will be a new requirement set out to provide this information every year also in the periodic report.

3. Guidance According to Section 36a of the Law

A. New Guidance

During the year and under the power granted it by Section 36a of Securities Law, the Authority published guidance on the following matters:

Disclosure Regarding the Internal Auditor of an Entity

The guidance was published in October 2004, effective January 1, 2005, regarding disclosure in the director's report on the internal auditor of the entity, taking into account the importance of the position as a defender of the interests of the public which holds shares in the reporting entity.

The guidance sets out the responsibility for disclosure of the framework of operations of the internal auditor at the entity without giving details of these operations, as the matter could damage his position and effectiveness of his work. The disclosure will require details regarding the tenure of the internal auditor at the entity, his identity and his qualifications, manner and volume of workload, the professional standards under which he operates, identity of his supervisor at the organization, the manner of establishing the audit work plan, the dates when the board of directors discussed the internal auditor's findings and the board of directors views on the volume of audit work, audit subjects and work plan of the internal auditor, and the access to information on the entity given him.

Guidance in the Director's Report Regarding Critical Accounting Estimates

The guidance was published in December 2004, regarding disclosing information to investors on reporting risks, and significant presentation risks resulting from the use of estimates and valuations in the financial statements. According to the guidance, an entity is required to include, in the director's report, an explanation of critical accounting estimates used, and the methods,

manners and assumptions used as the basis for these estimates. In addition, the report must include a quality discussion on the importance of critical accounting estimates for the investing public and the influence on the financial statements of the company, an analysis of sensitivity that was used with the estimates, information on parameters that a change in any of them brings about a change in the estimates, and a discussion on the changes that were made to the accounting estimates during the last three years.

The guidance stresses that the goal is to eliminate the lack of certainty involving the use of estimates only when they are significant, and it is not intended to be a platform for pro - forma reporting which will undermine the reliability of the information provided in the financial statements, which is based on the estimates used. Accordingly the guidance permits the inclusion of data sensitivity tests only when there is significant uncertainty regarding the estimates.

The guidance is not binding on a banking corporation, as defined by the Banking Law [Licensing], 5741-1981, and on an insurer, as defined by the Law on Supervision of Insurance Activities, 5741-1981.

B. Extensions to Guidance

When the Authority became convinced that the guidance that was published in the last report year was essential and required, it exercised its power under section 36[a][c] of the Securities Law, and with the consent of the Minister of Finance, extended the date of validity of a number of existing guidelines, as will be detailed below. The Authority is considering making the guidelines permanent.

Disclosure on Minimum Disclosure Necessary for a Valuation of Assets, Relation to It and Guideline Regarding Inclusion

The guidance was published in October 2003 [the commencement was deferred to December 31, 2003]. The guidance is in force until the end of 2005. It sets out the duty to attach a valuation report [as defined in the guideline], in situations noted in the guideline, and sets out clear guidelines regarding the minimum disclosure that will be given, and reference to it in the directors report. The background to issuing the guideline is the increasing use by entities of valuation reports in their reports, which in turn, is the result of Accounting Standard no. 15, coming into force. The objective of the guideline is to give the shareholders tools to in order to test the trustworthiness of the valuation reports.

Report on Directors Having Accounting and Financial Expertise

The guidance was published in October 2003, and is valid until October 20, 2005. It sets out the duty to report on directors of the entity who have accounting and financial expertise and the minimum number of directors who have such expertise at the entity. The guideline was published against the background of a crises in trust that hovered over leading capital markets of the world, and which exposed, inter alia, weaknesses in the operations of the board of directors, especially on everything regarding their ability to guarantee fair reporting and disclosure. The objective of the guideline is to supply information to the investors in order to assess the ability of the board of directors to fulfill its duties to check the financial status of the entity and to prepare the financial statements and approve of same.

Reporting Currency of the Reporting Entity

The guidance was published in September 2003, and is valid until the end of 2005. The guidance declares that the Israel Shekel is the currency for reporting financial information in the reports [as defined in the guidance]. The guidance states that entities that choose, in accordance with generally accepted accounting principles, to report in a currency which is not the Shekel, may do so on condition that the financial statements will not include any conversions into Shekels. Publication of the guidance became necessary after it was noted that some of the reporting entities were considering submitting their reports in foreign currency.

4. Legal Proceedings in Which the Authority is Involved

A. Civil Proceedings Handled During the Year

Originating Motion 431/01 [Civil Appeal 3623/03; 3643/03 - Supreme Court

Concerns the Authority's interpretation of the term "investment counseling", as defined in the law regulating investment advice - Regulation of Investment Advice and Investment Portfolio Management Law, 5755-1995 [see the 2002 annual report, page 51]. In April 2003, appeals were submitted by the Authority and by the Bankers' Association on a decision by the District Court of Tel Aviv that was given in October 2002. The oral discussion was held in September 2004. As of the date of writing this report, a decision has not yet been rendered.

Civil Appeal 8812/02 - Supreme Court

An appeal that was submitted by Pacific Cooperative Society for Economic Development Ltd [formerly: Moondragon Cooperative Society Ltd.] against a permanent injunction against it issued by the District Court of Tel Aviv in July 2002, prohibiting it, or anyone acting on its behalf, to offer its shares to the public and/or any other securities not through a prospectus that the Authority authorized for publication [see the 2002 annual report, page 52]. The appellant withdrew his appeal, at the recommendation of the Court and the appeal was cancelled on July 28, 2004.

Originating Motion 609/03 - District Court of Tel Aviv

A claim that was submitted in May 2003 by the Kiryat Ono Academic College, Registered Foundation, for a declaratory judgment that graduates of certain of its courses are exempt from examinations of the Authority for licensing as investment advisors, according to the law regulating advice, and that the decision of the Authority not to recognize these courses as a basis for the exemption according to said regulations is cancelled. In August 2003, 13 graduates of the College's courses joined the motion and submitted a corrected claim, according to which the Court is requested to also declare that those graduates are entitled to exemptions from examinations for licensing, on the basis of courses that they took.

Miscellaneous Civil Appeal 1179/04 - District Court of Tel Aviv

An appeal against a rejection by the Authority of the request by Israel Discount Bank for a third extension to file its financial statements for the second quarter of 2004, this in addition to the two extensions that were already approved. The reasons for the request for extension were that the Controllers Department of the Bank was on strike and did not transfer data on the consolidated

balance sheet of the Bank. The request for extension was rejected after the Authority was not convinced that the Bank was prevented from submitting its statements on time [as required by section 36[a] of Securities Law].

B. Legal Proceedings Concerning Civil Fines under the Joint Investment Trust Law, 5754-1994

For details of these proceedings, see chapter 5 above.

C. Criminal proceedings

For details of indictments, criminal cases and criminal judgments, see chapter 9 below.

Chapter 9 - Criminal Enforcement

1. Indictments

During 2004, further to various investigations that were undertaken by the Authority, eight indictments¹ were issued by the District Attorney of Tel Aviv [Taxation and Economics]:

- a. In March [Adar 5764] an indictment against Mr. Joseph Greenfeld and Mr Yitzhak Grossman was filed with the Magistrate's Court in Tel Aviv on suspicion of the use of insider information by an insider. Mr. Greenfeld was accused of 298 violations under section 52c of the Securities Law. Mr. Grossman was accused of two violations of section 52c of the law and six violations of section 53[b][8] of the law together with section 52i[b] of the law – violations by an employee of a member of the stock exchange. In addition, the indictment includes accusations against Mr. Greenfeld and Mr. Eitan Richter on the suspicion of securities fraud. Mr. Greenfeld was accused of four violations under section 54[a][2] of the law and Mr. Richter was accused of two violations under section 54[a][2] of the law.

Mr. Greenfeld and Mr. Grossman were insiders at Kardan Ltd. ["Kardan"], on the basis of their holdings and positions at the company. Mr. Greenfeld was the Chairman of the Board of Directors and a principal shareholder in Kardan. Mr. Grossman was a director ,who served in senior positions at various companies in the Kardan group and was a principal shareholder in Kardan. At the end of 1997, the management of Kardan began to formulate a re-organization plan with the intent of advancing the company, to enable it to raise capital, to increase its market value, and to increase the marketability of its shares. This important information was sufficient to bring about a significant change in the price of Kardan shares . Mr. Greenfeld and Mr. Grossman increased their holdings and ordered the purchase of Kardan shares for their own accounts, all this before the publication of the information to the public .

Mr. Richter was director, a member of the audit committee and a principal shareholder in Kardan. Mr. Greenfeld and Mr. Richter transacted on 30 - 31.12.98 in shares of Kardan on the stock exchange, and according to the indictment influenced the share price by fraud, with the intent to reduce the tax liability following changes to the Inflationary Tax Law [Amendment No.11] and the consolidation of capital which was to be undertaken under the reorganization of the company.. Criminal file 2617/04.

- b. In May [Sivan 5764] an indictment was submitted to Magistrate's Court of Tel Aviv against Mr. Shimon Mandelman, who was accused of securities fraud, in violation under section 54[a][2] of the Securities Law. Mr. Mandelman, a holder of a license to manage portfolios that was, at his request, suspended before being issued the indictment, during 2002 transacted in securities for his own account and for others through a number of accounts at Central Securities Company Ltd. According to that claimed in the indictment, Mr. Mandelman traded for his own account while influencing the market price by fraud, and manipulating the methods of trading and creating profit on accounts under his control, as detailed below: 11 transactions for his own account in shares of Mini Line Ltd.; six transactions for his own account in shares of Kafrit Industries Ltd.; 27 transactions for his own account in shares of Osif Investments and Development Ltd.; 29 transactions for his own account in shares of Keshet Rent a Car Ltd.; 14 transactions for his own account in Willifood Investments Ltd.; 13 transactions for his own

¹ The number of indictments does not necessary correspond to the number of investigation files that are open. Sometimes, the District Attorney combines a number of investigations into one indictment, or vice versa: submits under one investigation file a number of indictments.

account in shares of Alliance Tire Company Ltd.; and 14 transactions for his own account in shares of Ham-Let [Israel Canada] Ltd. During the year Mr. Mandleman was convicted, see paragraph 3.16 below .Criminal file 4190/04

- c. During May [Iyar 5764] an indictment was submitted in Magistrate's Court of Tel Aviv against Yodpaz Steel Services Ltd., ["Yodpaz"], Mr. David Cohen, Mr Joshua Cohen, and Mr. Meir Shabtai Mazar, on suspicion of violation under section 25 [d] of the Securities Law - a violation under section 53[b][3] of the Law, together with section 25[a] of the Law and suspicion of fraud under aggravated conditions – a violation under section 415 of the Penal Law. Mr. David Cohen served as chairman of the board, joint managing director and was a shareholder of Yodpaz. Mr Joshua Cohen served as joint managing director, and was the principle shareholder of Yodpaz. Mr. Shabtai Mazar served as an outside director, and was a shareholder in Yodpaz. On 28.5.2000 Yodpaz published a prospectus. The accused declared, that interested parties in the company will not submit requests for the purchase of units offered in the prospectus for their own accounts. In addition, the accused undertook not to make arrangements which were not stated in the prospectus regarding the offer of securities, their distribution and dispersion among the public, and undertook not to grant the right to purchasers of securities on the basis of the prospectus to sell the securities that they bought in excess of that stated in the prospectus. Mr. David Cohen, Mr Joshua Cohen, and Mr. Shabtai Mazar who wanted the minimum distribution required by the stock exchange bylaws, ordered debenture units for their own account while hiding the information from the investing public that they purchased the securities for their own account. In addition they did not report to the Authority, the Registrar or to the Stock Exchange on changes in their holdings. Mr. David Cohen even recruited members of his family; his workers and his friends encouraged them to purchase bonds in the prospectus, transferred money to finance the purchases and in some of the instances guaranteed to repurchase the bonds in the future. In addition, Yodpaz is accused of 23 violations under section 53[a][4] of the Securities Law together with section 1 of the Law and Regulation 33 of Securities Law [Periodic and Immediate Reports] Regulations, 5730-1970 - non reporting of changes in holdings of an interested party with the intent to mislead a reasonable investor. Mr. David Cohen was accused of 17 violations under section 53[a] [4] of the Law and section 1 of the Law and regulation 33 of Securities Law [Periodic and Immediate Reports] Regulations, 5730-1970 - non reporting of changes in holdings of an interested party with the intent to mislead a reasonable investor. Mr. Shabtai Mazar was accused also of three violations under section 53[a] [4] of the Law together with section 1 of the Law and regulation 33 of the Securities Law [Periodic and Immediate Reports], 5730-1970 – non reporting of changes in holdings of an interested party with the intent to mislead a reasonable investor. During the year of the report, the Court accepted a plea bargain from the parties – see paragraph 3.8 below .Criminal file 3792/04.
- d. In June [Sivan 5764] an indictment was submitted in Magistrate's Court of Tel Aviv against Mr. Ronen Birenbaum, Bizuiim Ramah Securities and Investments Ltd., ["Bizuiim Ramah"] and Mr. Ohad Berman on suspicion of managing portfolios without a license – a violation under section 39[a] of the law regulating advice together with section 29 of the Penal Law.

Bizuiim Ramah is a company which holds a license to manage investment portfolios and manages portfolios for its clients. Mr. Berman, a holder of a license to manage portfolios, served as a manager and was a controlling shareholder of the company. Mr. Birenbaum was employed by Bizuiim Ramah from July 2000 until October 2001. In the framework of his employment, he managed investment portfolios for 15 clients, all the while without a license to manage investment portfolios. Bizuiim Ramah and Mr. Berman knew that Mr. Birenbaum was operating without a license to manage portfolios, and accordingly they were accused of violating, together

with Mr. Birenbaum, the law requiring the holding of a license in order to manage investment portfolios. Criminal file 4553/04

- e. In August [Av 5764] an indictment was submitted in Magistrate's Court of Tel Aviv against Hatahuf Company Ltd., Mr Yuval Maharshak, and Mr. Gadi Hazut on suspicion of non compliance with section 36 of the Securities Law together with regulation 34 of the Securities [Periodic and Immediate Reports] Regulations, 5730-1970, and nine violations under section 53[c] [8] of the law. Mr. Yuval Maharshak served as director, was a controlling shareholder, and alternatively served as managing director and chairman of the board of directors of Hatahuf Company. His father, Mr. Joseph Maharshak, was a controlling shareholder and chairman of the board of directors of Hatahuf Company. Mr. Hazut was vice president of finance, company secretary and from time to time served as managing director or as acting managing director of Hatahuf Company. In the immediate reports to the stock exchange, to the Authority, and to the Companies Registrar, Hatahuf Company did not report when required to do so, and occasionally did not report at all, on the constant turnovers in senior positions at the company. The indictment includes also the suspicion of 2 violations under section 53[a] [4] of the law by said accused, and by Mr. Joseph Maharshak. Mr. Joseph Maharshak is accused also with non compliance with section 36 and section 37 of the law together with regulation 33 of Securities [Periodic and Immediate Reports], Regulations, 5730-1970 - a violation under section 53[c] [8] of the law. Criminal file 7011/04.
- f. In October [Heshvan 5765] an indictment was submitted in Magistrate's Court of Tel Aviv against Mr. Zeev Cohen and Machshevah Advice and Management Ltd., on suspicion of carrying out a large number of violations according to section 39[b] of the law regulating advice, and section 4 of the law. Mr. Cohen is a holder of a license to manage portfolios [from 17.9.97] and a controlling shareholder and managing director of Machshevah Company. Machshevah also holds a license to manage portfolios. Mr. Cohen held and purchased securities for his own account from the time of receiving his license and at least until 22.3.2004. In addition, Mr. Cohen managed investment portfolios for his mother, for Machshevah Company, and for Innovation Holdings and Projects Ltd., and Anova Hatmiyut Ltd., two companies under his control. All this in millions of shekels through 12 accounts and through the use of Machshevah Company as a conduit for his activities. It should be noted that the license of Mr. Cohen was suspended during the report year, following a decision by the disciplinary committee which operates under the law for regulating advice. Criminal file 8808/04.
- g. In November [Kislev 5765] an indictment was submitted to Magistrate's Court of Tel Aviv against Mr. Chaim Zinger and Mr. Binyamin Gutman on suspicion of violations as follows: the purchase and holding of securities by a holder of a license to manage portfolios - a violation under section 4[a] of the law regulating advice, together with section 39[b] of the law; holding a security of an employee of a member of the stock exchange in an account that is not in his name - violation under section 52i[c] of the Securities Law, together with section 53[b] of the Securities Law; managing investment portfolios for a relative - violation under section 4[b] of the law regulating advice, together with section 39[b] of the law . Fraudulent receipts - violation under section 415 of the Penal Law; deceit and breach of trust in an entity - violation under section 425 of the Penal Law.

Mr. Zinger and Mr. Gutman were employed as investment managers at Ofek Securities and Investments Ltd. ["Ofek"]. The two opened accounts at Ofek for members of their families, and for their own accounts [while masking the details of identification], and operated through them against the law and against Ofek policy. The accused even gave preference to their own accounts over the other accounts which they managed for their clients, and recorded significant

profits, for themselves and for members of their families, compared with profits earned on other accounts of similar risk by other clients. Criminal file 9030/04.

- h. In December [Tevet 5765] an indictment was submitted to Magistrate's Court in Tel Aviv against Mr. Abraham Aufrichter on suspicion of fraudulent influence on the prices of shares of public companies traded on stock exchange, and the suspicion of encouraging investors to join the trading in securities which he held, while carrying out transactions for his own account, and exposing the public to false trading information, which created a false impression of an active and acceptable trading situation. Mr. Aufrichter earned his living by trading in securities through accounts at Solomon Portfolio Management and Capital Markets Ltd. Mr. Aufrichter, during 2002 apparently committed many violations under section 54[a] [2] of the Securities Law and section 54[a][1] of the Securities Law in the following shares:
Yuval Industrial Engineering [1999] Ltd. - 14 violations; Ishpro Israel Company for Rental Buildings Ltd. - 11 violations; Kafrit Industries Ltd. - 11 violations; Yaakov Engel Building Company Enterprises Ltd. - 15 violations; M.T.I. Computers and Software Services Ltd. - 59 violations; Mehadrin Ltd. - 9 violations; Shemen Industries Ltd. - 2 violations . Criminal file 10332/04.

2. Criminal Files Pending in the Courts

At year-end, various files were pending in the courts, as follows:

- a. 20 criminal files at trial court level, of which 15 were for indictments submitted in previous years.
- b. Nine criminal files under appeal, of which two criminal appeals [one was submitted during the year] were submitted to the Supreme Court regarding conviction and regarding sentence [two by the accused], and seven were submitted this year to the District Court of Tel Aviv. Three appeals were submitted by the accused, regarding convictions and regarding sentence [two of them this year], two appeals were submitted this year by the accused only against the sentence. During the year, the District Attorney submitted an appeal against an acquittal in one file, and submitted an appeal against the light sentence and counter appeal of an accused on the severity of the sentence in one file.
- c. In one criminal appeal, the District Attorney submitted a request for appeal to the Supreme Court after the District Court accepted the appeals of the appellants, exonerated them, and thus, on the basis of a majority, overturned a decision of a lower court. On one criminal appeal, the appellant submitted a request to appeal, after the court rejected his appeal, unanimously, and thus left, as is, the decision of the lower court.

3. Criminal Judgments in Trial Court

During the year, 17 judgments were given in trial court²

- a. In February [Shvat 5764] the Magistrate's Court of Tel Aviv sentenced Mr. Haim Navon to five months of imprisonment, suspended, on condition that, during the next three years, he will not commit any violations of the laws regulating advice, and a fine of NIS10,000, or 100 days of imprisonment in lieu. Mr. Navon was convicted, on his admission, of a violation under section 39[b] of the law regulating advice. Mr. Navon, a holder of a license to manage investment portfolios and an investment manager at Sie Ram Capital Markets Ltd. managed investment

² The number of decisions does not necessarily correspond to the number of indictments that are open, as sometimes indictments having more than one accused are sometimes the subject of separate judgments, and vice versa - separate indictments are sometimes combined into one file.

portfolios of NIS200,000 for members of his family. Mr Navon transacted in shares and financial assets in said accounts, over a period of six months. Criminal file 11306/03 [see also the 2003 annual report for 2003, page 59, paragraph h].

- b. In February [Shvat 5764] the District Court sentenced Mr Shlomo Eisenberg to 18 months imprisonment, to be served, and 18 months imprisonment suspended, on condition that during a period of three years from the end of serving his sentence, he will not commit similar violations of which he was convicted in the file, and a fine of NIS1million, or 1 year of imprisonment, in lieu. The Court also sentenced Mr. Harry Sapir, to six months of imprisonment, suspended, on condition that during the next three years, he will not commit similar violations of which he was convicted of in the file, and a fine of NIS200, 000 or three months of imprisonment, in lieu. In addition the Court also imposed a fine of NIS100,000 on Arad Investments and Industrial Development Ltd.

The decision was rendered in September 2003 [Elul 5763], and according to which Mr. Eisenberg was convicted of all the violations which were attributed to him in the indictment, the main points of which are:

three violations of fraud under aggravated conditions - violation under section 415 of the Penal Law; including misleading information in a report or notice - violation under section 53[a] [4] of Securities Law together with section 36[e] and [f] of the same law, including misleading information in a prospectus – violation under section 53[a] [2] of Securities Law together with section 16[b] of the same law. Mr. Sapir was convicted of all the violations which were attributed to him in the indictment – three violations of fraud under aggravated conditions, and the inclusion of the misleading information in a prospectus .Arad was also convicted of all the violations that were attributed to it in the indictment, which overlap the violations, noted above, of Mr. Eisenberg, except for a violation of fraud under aggravated conditions. [see also the 2003 annual report, pages 64-65, paragraph m]. Criminal file 40200/99. In April [Iyar 5764], Mr. Eisenberg submitted an appeal against the decision to the Supreme Court. Criminal appeal 3896/04.

- c. In March [Adar 5764] the Magistrate's Court of Tel Aviv convicted Mr Arie Weksler of five counts of fraudulent influence under section 54[a][2] of Securities Laws an attempt to fraudulently influence under section 25 of the Penal Law , together with section 54[a][2] of the Securities Laws .Mr Weksler, an independent accountant by profession, transacted as a private investor on the Tel Aviv Stock Exchange, through a bank account of his late mother. His bank transactions were undertaken through a computer at his home. Mr. Weksler transacted during August through October 1998 in shares of Benny Cohen Ltd., which at the time was characterized by low trading volumes.

During July [Tamuz 5764], the Court sentenced Mr. Wexler to 18 months imprisonment, of which six months were to be served in community work, and the remaining 12 months were suspended for a period of three years for violations for which he was convicted of, and on all violations, according to the Securities Law. In addition the Court imposed a fine of NIS 30,000, or eight months imprisonment, in lieu. The Supervisor of Community Service found Mr. Wexler unfit for community service because of medical reasons .It was agreed to defer the imprisonment because of Mr. Wexler's intentions to submit an appeal. .Criminal file 8806/00 .

In October [Heshvan 5765] Mr Wexler submitted an appeal against the decision, including a decision on the acceptance of his confession in the lower court [on 18.3.2003], and on the sentence. Criminal appeal 71785/04

- d. In April [Iyar 5764] the Magistrate's Court of Tel Aviv convicted Mr. Amos Lev Levy, of violations under section 54[a][1] of the Securities Law - fraud relating to securities and violations under section 25[d] of the law. The Court exonerated Mr Levy of violations under section 415 of the Penal Law [fraud under aggravated conditions], and attempted fraud. Mr. Levy held 1/3 of the shares of Ha'Namel B.Z.L. Ltd. ["Company"] and served as a joint managing director, together with Mr. Zelig Yehosua. On 30.11.1994 the Company issued a prospectus and offered its shares to the public, in a tender offer that would be undertaken in two stages. The prospectus stated that no special arrangements related to the shares and their distribution among the public would be undertaken, unless so disclosed in the prospectus. After the failure of stage one of the tender, the accused made an agreement with Mr. Avihu Horowitz, who was at that time was Chairman of the Board of Yishtak Industries and Technologies Ltd. [companies that were affiliated at that time – Mentor Dinami Investments Ltd., Kopel Nehiga Atzmit Ltd., and Lebo Finance and Investments Ltd.], according to which Mr. Horowitz would order , in the second stage of the tender, shares of NIS2 million, with a distribution of 15 different accounts, and as compensation Mr. Levy would make a payment of 20% of the order volume, and purchase 490,000 shares of Mentor Dinami Investments Ltd. Mr. Levy was required to report on the agreement to the Securities Authority and to the investing public, and accordingly violated his duty according to the prospectus. Mr. Zelig Yehosua was exonerated after the State retracted its claims against him. Whereas the company was under liquidation and was to be bought by a party who had no contact with the said violations, the State reached a plea bargain in July 1997, and Mr. Levy was convicted of the violations attributed to him in the indictment and fined NIS36,000.

In May [Iyar 5764] the Court sentenced Mr. Amos Levy to 12 months imprisonment, suspended for a period of three years, on condition that he will not commit the same violations for which he was indicted, and a fine of NIS20,000, or seven months imprisonment, in lieu Criminal file 8071/96.

- e. In May [Sivan 5764] Mr Naftaly Mendelovitch, confessed under a plea bargain in Magistrate's Court to two violations under section 39[a] of the law regulating advice without having a license. Between 1999 and 2001, Mendelovitch transacted in shares, at his discretion, in 20 accounts whose owners granted him power of attorney to act on their behalf. In addition, Mendelovitch managed, during said period, an investment club and gave advice regarding the advisability of investments, their holding, selling and buying. The Court sentenced Naftaly Mendelovitch to three months imprisonment, which would be converted into community service, and seven months suspended imprisonment, on condition that during a period of three years, he would not commit violations under the law regulating advice, and a fine of NIS40,000, or one month imprisonment. Criminal file 4580/02.

The State submitted an appeal on the light sentence in August [Elul 5764] criminal appeal 71580/04. In September [Elul 5764] Mr Mendelovitch submitted an appeal on the severity of the punishment criminal appeal 71614/04.

- f. In June [Tamuz 5764] the Magistrate's Court of Tel Aviv convicted Mr. Raphael [Abraham] Elimelech of three violations under section 54[a] [2] of the Securities Law, together with section 25 of the Penal Law, following a plea bargain between the parties, according to which the accused confessed to all violations attributed to him, and agreed to a review by the Probationary Service. Mr. Elimelech invested, during the months of November and December, 2000 as a private investor in the shares of Brill Shoe Industries Ltd. and Topper Fashion Industries 1977 Ltd. On a number of occasions, Mr. Elimelech gave orders to purchase shares of said companies in order to influence the share price and to increase their real value. In his actions, he acted frauduantly, influenced the share price and created a false impression, as if the trading

in said shares was orderly and fair. These violations were calculated, planned and premeditated. [see also the 2003 annual report, page 57, paragraph a].

The Court sentenced Mr Elimelech to 15 months imprisonment, three months of which to be served in community service and 12 months suspended, on condition that during a period of three years, that he not commit any of the violations for which he was convicted. The Court also imposed a fine of NIS10,000, or 50 days of imprisonment, in lieu. *Criminal file 1128/03.*

In October [Heshvan 5765] Mr. Elimelech submitted an appeal to the District Court of Tel Aviv against the punishment and against the severity of the punishment. *Criminal appeal 71784/04.* The State submitted an appeal on the conviction and on the lightness of the penalty. *Criminal appeal 71775/04.*

- g. In June [Sivan 5764] Magistrate's Court canceled the conviction of Mr. Ehud Amir for committing five violations under section 52c the law, [the use of insider information, garnered from an insider], and sentenced him to probationary service for 18 months, community service of 250 hours and a fine of NIS15,000, or 50 days of imprisonment, in lieu, all this is in accordance with section 71a[b] of the Penal Law. [see also the 2003 annual report, page 66, section p]. *Criminal file 10083/00.*
- h. During July [Tamuz 5764] Magistrate's Court of Tel Aviv convicted Yodpaz Steel Services Ltd., ["Company"], Mr. David Cohen, Mr Joshua Cohen, and Mr. Meir Shabtai Mazar, who confessed, under plea bargain, to violations of the Securities Law and the Penal Law, violations concerning the non correction of a prospectus, non reporting of changes in shareholdings of interested parties with the intent of misleading a reasonable investor, and fraud. The penalties imposed were as follows: on Yodpaz Ltd. – a fine of NIS400,000. Mr. David Cohen, a shareholder in the company, chairman of the board and joint managing director, was sentenced to six months in prison which will be served in community service, a sentence of 12 months, suspended on condition that during a period of three years, he does not commit any of the violations for which he was convicted, and a fine of NIS250,000 or 120 days imprisonment, in lieu. Mr. Joshua Cohen, a shareholder of the company, chairman of the board and joint managing director, was sentenced to nine months in prison, suspended, on condition that during a period of three years, he does not commit any of the violations for which he was convicted, and a fine of NIS100,000, or 90 days imprisonment, in lieu. Mr. Mazar, a shareholder of the company and an outside director therein, was sentenced to six months in prison, suspended on condition that during a period of three years, he does not commit any of the violations for which he was convicted, a fine of NIS50,000 or 30 days imprisonment, in lieu, and a written commitment that he will not serve as a director of a public company for a period of ten years, or 20 days of imprisonment for not signing the commitment. *Criminal file 3792/04.*
- i. In September [Elul 5764] Magistrates Court of Tel Aviv convicted Mr. Stephan Mandel and Mr. Amos Doron of violations under section 53[a][1] of the Securities Law and exonerated Pacific Cooperative Society for Economic Development Ltd., of said violations. The accused worked in order to convince the public to join the Moondragon Group, which is a group of companies holding - Pacific Cooperative Society for Economic Development Ltd., Z.N.K. Company, [a private company of which 30% of its shares were owned by Mr. Mandel, who served also as chairman of the board and managing director of the company. Mr. Dolan also held shares in the company and served as director], Veneto Marketing Ltd., [a private company established by Mr. Doron, who was a controlling shareholder therein and Mr. Mandel, who also served as director], and EDCI Company [a private company established by Pacific Cooperative Society, Z.N.K. and Veneto Marketing]. The public joined the group through a financial investment, and as compensation they received [Pacific Cooperative Society] three

dunams on Santo Spirito Island in the State of Venice, and three shares in EDCI The Court concluded that this was an offer of securities to the public, as defined in the Securities Law, and that the accused were aware of this, taking into account their efforts to deal with the problem through circumventing the responsibilities imposed upon them according to law: Mr. Mandel and Mr. Doron decided not to issue a prospectus in order to mislead the investing public. In addition the Court convicted Mr. Mandel of a violation under section 257 of the Penal Law, as on 21.2.2002 he escaped from legal custody at the time of his investigation at the offices of the Securities Authority [see the 2003 annual report, page 58, paragraph e].

In October [Tishrei 5765], the Court imposed the following sentences: Mr. Mandel was sentenced to 20 months imprisonment, of which 10 months were to be served, and 10 months were suspended on condition that during a period of three years he does not violate any sections of the Securities Law and section 257 of the Penal Law, and a fine of NIS100,000, or 200 days imprisonment, in lieu. Mr. Doron was sentenced to 10 months imprisonment – 4 months of actual imprisonment, and the rest suspended on condition that during a period of three years he does not violate any section of the Securities Law, and a fine of NIS20,000, or 50 days imprisonment, in lieu. *Criminal file 4709/03.*

- j. In September [Elul 5764] Magistrate's Court of Tel Aviv convicted Mr Alon Naor of 265 counts of fraudulent influence on the fluctuation of the market price of securities under section 54[a][2] of the Securities Law, and two violations of influence to purchase securities while withholding significant information under section 54[a][1] of the Securities Law. Mr. Naor earned his living by investing in securities for his own account and carried out his transactions through a number of bank accounts. He carried out 49 transactions for his own account in shares Yacobinsky-Lerrer Civil Engineering Contractors Ltd. ["Yacobinsky"], 31 transactions for his own account in shares of Europe Israel [M.M.S.] Ltd., 91 transaction for his own account in shares of A.M.L.D. Investment Company [1981] Ltd., ["AMLD"] and 94 transactions for his own account in the shares of Lipman Electronic Engineering Ltd. In addition, Mr. Naor influenced Mr. Yitzhak Ben Bassat, who consulted with him on the capital markets and operated according to his recommendations, to purchase shares of Yacobinsky and AMLD , concealing from him the fact that his [Ben Bassat] purchase enabled him [Naor] to immediately sell his block of shares at the price that he wanted. *Criminal fine of 10532/01*
- k. In September [Elul 5764] Magistrate's Court of Tel Aviv convicted Mr Avinoam Finkleman and Delek, The Israel Fuel Company Ltd., ["Delek"] of violations under section 53[c][8] of the Securities Law and exonerated them from violations under section 53[a][4] of the law, that is, the inclusion of misleading information in order to mislead a reasonable investor. On 7.01.1999 Delek Investments and Assets Ltd., ["Delek Investments"], a company under the control of Delek, issued a purchase offer. From mid 1998, Delek Automobile Systems Ltd. ["Delek Motors"], a subsidiary of Delek Investments, conducted negotiations with Ford International with the intent of receiving the franchise of Ford in Israel, and to replace the then importer – The Israel Automobile Company ["Hil"]. Close to the end of the period to receive purchase offers, an agreement was signed between Delek Motors and Hil on the transfer of the franchise. On 28.1.1999 the accused submitted an immediate report that explained initial contacts between the company, the importer and the sole distributor of Ford automobiles in Israel, noting the intent to sign an agreement that will permit Delek Motors to receive the sole franchise to import and distribute Ford automobiles in Israel, and other possibilities for cooperation. The Court decided that the reports were misleading and that the accused were required to submit correct and proper reports on contacts and events, with proper explanations. However, it

was decided that there was no criminal intent to mislead a reasonable investor. [See also the 2002 annual report, page 57, paragraph c].

The Court fined Mr. Finkleman and Delek, NIS30,000 each. *Criminal file 3794/02.*

- I. In October [Tishrei 5765] Magistrate's Court of Tel Aviv convicted Tradekal Ltd. ["Tradekal"] of 30 violations under section 53[a][4] of the Securities Law - default of section 36 of the Securities Law, together with regulation 33 of Securities Law Regulations. The Court also convicted Tradekal of nine violations under section 53[a][4] of the Securities Law together with section 36 of the Securities Law and regulation 33 of the Security [Periodic and Immediate Reports] Regulations, 5730-1970, and exonerated it from ten additional violations under the same sections. Tradekal was also convicted of three violations under section 53[a] [4] of the Securities Law together regulations 4, 5 and 6 of the regulations regulating the issue of securities. The Court also convicted Mrs. Ayelet Dravsky of three violations under section 53[a] [4] of the Securities Law, together regulations 4, 5, and 6 of the regulations regulating the issue of securities. Mrs. Dravsky was exonerated of all other accusations that she was charged with in the indictment - violations under section 53[a] [4] of the Securities Law. Originally, an indictment was also issued against Mr. Ronen Rashal, who was a manager and shareholder in Tradekal and who fled the country during the hearings [proceedings against him were suspended], and against Mr. Amit Etinger, who reached a plea bargain with the prosecutor, and was convicted of violations regarding aide to Mr. Rashal to carry out fraud related to securities. He was charged accordingly [see the 2003 annual report for 2003, page 63, paragraph g and page 66, paragraph q]. Tradekal is a public company, whose shares are traded on the stock exchange. Mrs. Dravsky, a dentist and wife of Mr. Rashal, between 1997 and 2002, alternately, was an interested party in Tradekal and served as a director of Tradekal, from 28. 4.1998. Tradekal issued false reports to the public and the authorities, enabling it to earn points in the share market. Mrs. Dravsky together with Mr. Rashal submitted misleading reports that were intended to hide from the investing public the fact that Mr. Rashal was the real interested party in Tradekal, that he in reality, held the shares, that he was the beneficiary of the issue, and that he stood behind all the activity in the shares and changes in volume of holdings therein. Mrs. Dravsky signed most of the reports, fully aware that Tradekal was not presenting a full and correct picture to the public.

In November [Kislev 5765] the Magistrate's Court convicted Mrs. Dravsky and sentenced her to imprisonment, suspended for four months, for a period of three years, on condition that she not commit any violations under section 53[a] [4] of the Securities Law, a fine of NIS15,000, or 30 days of imprisonment, in lieu, and a written undertaking for NIS30,000 for a period of two years, not to commit any of the violations in the file, or 30 days improvements, in lieu. Tradekal was fined NIS100,000. *Criminal file 8226/00.*

- m. In October [Heshvan 5765] Magistrate's Court exonerated, because of doubt, Mr Jonathan Kay and Mr. Nir Hora., of violations that were attributed to them in the indictment, that is 49 violations under section 54[a][2] of the Securities Law and section 25 of the Penal Law. Mr. Kay and Mr. Hora were employed by Ilanot Bitucha Investment House. On 28.5.1998 Mr. Hora gave two offsetting orders [sale and purchase] for 24 shares on the "Maof", for NIS40 million, coincidentally, in order to close an open position that was created with the expiration of a synthetic contract [short] in one of the nostro accounts of Ilanot Bitucha that was a "Maof" arbitrage account. *Criminal file 8241/01.* In January, 2005 [Shvat 5765] the State appealed to the District Court of Tel Aviv against the exoneration of Mr. Kay and Mr. Hora. *Criminal appeal 20143/05*

- n. In October [Heshvan 5765] Magistrate's Court of Tel Aviv convicted Orsis Ltd. [a public company, [from 1995] which develops computer software systems for medical laboratories] ["Orsis"], Dr. Moshe ben - Shaul [a controlling shareholder in Orsis and chairman of its board of directors], Leaders Securities Issues Ltd. [a public company which deals with investments, securities and underwriting, and which served as manager of the consortium of underwriters in the issue of Orsis ["Leader"], Mr. Ohad Libman [responsible for underwriting at Leader], Luxembourg Underwriters Ltd., [a private company which deals with investments, securities and underwriting, and which served as one of the companies underwriting the issue of Orsis] ["Luxembourg"], Mr. Yakov Luxembourg [a controlling shareholder of Luxembourg, and a manager therein], Mr. Asher Ya'ari [a shareholder in Luxembourg, a manager therein, and responsible for underwriting at the company], Ziv – Tal Underwriting and Investments [1993] Ltd. [a private company which deals with investments in securities, and which served as one of the underwriting companies in the issue of Orsis] ["Ziv-Tal"], Mr. Arie Fogelman [a controlling shareholder in Ziv – Tal], Bechora Ltd. [a private company which deals with investments in securities, and which served as one of the underwriting companies in the issue of Orsis ["Bechora"], and Mr. Yakov Danziger [a shareholder of Bechora and a manager therein] of violating, by fraud under aggravated circumstances [confirmation of the stock exchange to register shares of Orsis for trading] under Section 415 [last part] of the Penal Law and a violation of fraudulent influence to purchase securities under section 54[a][1] of the Securities Law. Mr. Yishai Wein [financial manager of Elex] was exonerated of a violation under section 415 [end] of the Penal Law, but was found guilty of a violation under section 54[a] [1] of the Securities Law, relating to a plan of support of the market price only. In addition, the Court convicted all said accused, and Elex [Israel] Ltd. [a subsidiary, under full ownership of Orsis] ["Elex"] of a violation of fraudulently influencing the price movements of a security, under section 54[a] [2] of the Securities Law. As for Mr. Wein, this indictment relates only to the plan of support of the market price.

The Court exonerated the accused of violations of including a misleading item in a prospectus with the intent of misleading a reasonable investor, under sections 16[b] and 53[a] [2] of the Securities Law, and from a breach of duty to advise the Authority of an arrangement that is not included in the prospectus, under section 25[d] of the Securities Law together with section 286 of the Penal Law. The Court exonerated Mr. Yakov Luxembourg, Mr. Asher Ya'ari, Ziv – Tal, Mr. Arie Fogelman, Bechora, and Mr. Yakov Danziger of violations of fraud under aggravated circumstances [from clients], under section 415 [end] of the Penal Law.

Orsis, controlled by Dr. ben – Shaul, requested to issue its shares already in 1993 and secured the services of Leader for this purpose, as lead underwriter of the issue. After the prospectus was deferred a number of times, Dr. ben – Shaul and Mr. Libman decided to issue a new prospectus at the beginning of 1995. Because of the difficult position of the capital market at the time, and against the background of failure of the issue because of the public's lack of interest in the prospectus, and on the background of a fear of failure of the issue following the non response of the public to the offer in the prospectus, the underwriters undertook to order, for their own accounts and for the accounts of entities related to them, shares according to their underwriting commitments, thus creating an impression of a successful issue. At the same time and against a background of the underwriters' fears that the share price of Orsis was expected to fall after the issue, Dr. ben – Shaul made a commitment to the underwriters that he would prevent, by himself and through Elex, employees and members of his family, a drop in the share price during the first days of trading, such that each underwriter will be able to sell on the stock market, in the first few days of trading, some 40% of the shares that he ordered for himself and for accounts related to him, in the issue. Through this action the accused created an impression

that the issue was successful and that the shares were fully bought up by the public, and this contrary to the actual results of the issue. In addition, during the first few days of trading after the issue, the underwriters gave large sell orders for Orsis shares [which they bought in the issue], and Dr. ben – Shaul and Mr. Wein purchased all shares that were offered, without any change in the market price, through their own accounts and accounts of Elex, family members and employees. Consequently, the accused affected the movements in the market price of Orsis through fraud, by creating a misleading impression of stable trading in the share.

In December [Tevet 5765], the Court imposed the following sentences: on Orsis and Elex [known today as Elex Medical Ltd., after their merger] a fine of NIS250,000. Dr. ben – Shaul was sentenced to six months imprisonment, which he can serve out in community service work, 12 months imprisonment, suspended on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS 500,000 or six months imprisonment, in lieu. Mr. Wein was sentenced to eight months imprisonment, suspended on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS25,000, or two months imprisonment, in lieu. Leader was fined NIS250,000. Mr Libman was sentenced to 12 months imprisonment, an additional 12 months, suspended on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS500,000, or six months imprisonment, in lieu. Luxembourg was fined NIS 250,000. Mr. Luxembourg was sentenced to six months imprisonment, which he can serve out in community service work, 12 months imprisonment, suspended on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS500,000 or six months imprisonment, in lieu. Ziv – Tal was fined NIS 250,000. Mr. Fogelman was sentenced to six months imprisonment, which he can serve out in community service work, and 12 months imprisonment, suspended on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS100,000 or six months imprisonment, in lieu. Bechora was fined NIS 250,000. Mr. Danziger was sentenced to six months imprisonment, which he can serve out in community service work, 12 months imprisonment, suspended on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS500,000 or six months imprisonment, in lieu. The decision on Mr. Ya'ari has not yet been given. Criminal file 1349/98.

- o. In December [Tevet 5765] Magistrate's Court to Tel Aviv sentenced Mr. Ben Zion Heller for violations concerning fraudulent influence on the market price of a security - violations under section 54[a] [2] of the Securities Law, as he carried out four matching transactions on the stock exchange in shares of MMD Israel Technologies [1983] Ltd., and 17 matching transactions on the stock exchange in shares of Tom Holdings Ltd., during 1998 - 1999. Thus, Mr. Heller created false trading turnovers, false impressions and influenced the trading in the shares. The Court exonerated Mr. Heller, on the basis of doubt, of carrying out a matching transaction on 13.5.1999. In February, 2005 [Adar 5765] the Court sentenced Mr. Heller to 12 months imprisonment, suspended, on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS 150,000 or six months imprisonment, in lieu. Criminal file 4402/01.
- p. In December [Kislev 5765] Magistrate's Court of Tel Aviv convicted Mr. Shimon Mandelman of carrying out 114 violations of influence by fraud on the movement in the market price of a security under section 54[a] [2] of Securities Law. Mr. Mandelman who holds a license to manage portfolios and who operated in the stock exchange for 25 years, operated in the shares of seven different companies, while trading for his own account. He made 114 transactions for

his own account over a period of eight months, while fraudulently influencing the market price, creating false trading turnovers, false impression of normal arm's length activities between parties, and creating profits in accounts under his control.

The Court sentenced him to 21 months imprisonment, eight months imprisonment, suspended on condition that for a period of three years after his release, he does not commit any violation of the Securities Law. The Court also imposed a fine of NIS100,000, or five months imprisonment. *Criminal file 4190/04.*

- q. In December [Kislev 5765], Magistrate's Court of Tel Aviv, decided to honor the plea bargain, under which Man Food Industries Company Ltd., ["Man Company"] and Mr. Meir Kahtan, managing director and chairman of the board of Man Company, were convicted, on the basis of their confession, in that they did comply with the requirements of the Authority and did not submit an immediate report, on time, to the Authority, Companies Registrar, or to the stock exchange, of changes in senior officers at the end of the tenure of Mr Yakov Shai Mizrahi as an outside director, and this with the intent to mislead a reasonable investor. Man Company and Mr. Kahtan were also convicted of the fact that they did not submit an immediate report to the Authority, the Companies Registrar, and to the stock exchange, giving details of a transaction with a controlling shareholder regarding coordination of voting at the general meeting of Man Company, and that they did not convene the general meeting to approve the voting agreement, this with the intent of deceiving a reasonable investor. Mr. Mizrahi was convicted, on the basis of his confession, in that as an interested party he did not advise the Authority, Companies Registrar, and the stock exchange when required to do so, of ending his tenure as an outside director. Man Company was also convicted in that it did not submit an immediate report, when required to do so, on the resignation of the company's manager director – Mr. Baruch Kotelresky. Later on, Man Company published a misleading report on the termination of the managing director, noting an incorrect date of resignation, and did so in order to mislead a reasonable investor [see the 2002 annual report, page 59, paragraph i].

The Court-imposed a light fine of NIS7,500 on Man Company, taking into account its financial situation. The court sentenced Mr. Kahtan to six months imprisonment, suspended, on condition that he does not commit any of the violations for which he was accused of during a period of three years, and a fine of NIS100,000, or 10 months imprisonment, in lieu. Mr. Mizrahi was fined NIS10,000, or 100 days of imprisonment, in lieu.

In March [Adar 5764], Mr. Kotelresky reached a plea bargain with the State and was convicted on the basis of his confession, of not submitting an immediate report, on time, and not complying with the requirements of the Authority, with the intent to mislead a reasonable investor. Mr Kotelresky was sentenced to four months imprisonment suspended and a fine of NIS20,000 or 200 days of imprisonment, in lieu. *Criminal file 11225/03.*

4. Judgments in Criminal Appeals

During the year, the District Court of Tel-Aviv gave six judgments in criminal appeals and the Supreme Court gave one judgment in criminal appeal.

A. Judgments in Criminal Appeals at the District Court of Tel Aviv

1. In January [Tevet 5764] the District Court of Tel-Aviv decided to partially accept the State's appeal on the sentencing of Mr. Hanan Atir, and he was convicted of committing 12 violations under section 54[a] [1] of the Securities Law – frauduantly inducing someone to transact in a security, and 25 violations under section 54[a] [2] of the law – fraudulently influencing fluctuations in the price of the shares. In addition, both the State and Mr. Atir will withdraw their appeals on the punishment. Mr. Atir was convicted in Magistrate's Court of frauduantly aiding Mr. Joseph Pinkus many times, in the shares of Arad. [See the 2002 annual report, page 61, section f] *Criminal appeal 71605/02, Criminal appeal 71672/02.*
2. In March [Adar 5764] the District Court of Tel Aviv rejected the appeal of Mr. Yechezkel Mualem against his conviction of frauduantly influencing the price fluctuations of the bonds of Tal Company's bonds. Yet, the Court reduced the sentence imposed on Mr. Mualem and set the sentence period at 10 months, [in lieu of 15 months]. No other changes were made to the sentence [see the 2003 annual report, page 61, paragraph d].*Criminal appeal 70484/03.*
3. In October [Tishrei 5765] the District Court of Tel Aviv rejected the appeal of Mr. Adi Eyal, regarding his conviction on two violations of the use of inside information by an insider, under section 52c of the Securities Law. In addition, the Court rejected the appeals of Mr. Eyal and the State on the sentence that was imposed on Mr. Eyal [see the 2002 annual report, page 62, paragraph i]. *Criminal Appeal 70403/03, Criminal appeal 70405/93.*
4. In November [Kislev 5765] the State and Mr. Nathan Lichtigstein decided to reciprocally cancel their appeals. *Criminal appeal 7177/03, Criminal appeal 71442/03.* . Mr. Lichtigstein was convicted in Magistrate's Court of conspiracy to commit a crime, securities fraud and reporting violations. [see the 2003 annual report, page 63, paragraph h].
5. In November [Heshvan 5765] the District Court of Tel Aviv decided to accept the appeal of Discount Investments Ltd. ["Discount Investments"] [*criminal appeal 70953/02*], Mr. Dov Tadmor [*criminal appeal 71288/02*], Mr. Shlomo Cohen [*criminal appeal 70956/02*] and Mr. Joseph Buk, [*criminal appeal 70954/02*], ON the issue of limitation, and decided that all violations of non reporting with the intention to mislead because the financial statements that were submitted before August 1993, fell under the concept of limitation, under section 9[a][3] of the Criminal Procedures Law Code [Consolidated Version] 5742-1982. Regarding the violations of non reporting with the intent to mislead in eight financial statements that were submitted commencing 19.8.1993, it was decided by majority vote to accept the appeals of all the appellants and to acquit them of all violations that were attributed to them. Accordingly the Court decided to reject the State's appeal with regards to Mr. Buk [*criminal appeal 70949/02*]. Justice Judith Shizur, in a minority opinion, stated that the appeals of all appellants must be rejected. The appeal was overturned on the conviction of the accused to carry out 18 violations of not reporting with the intent to mislead a reasonable investor, by withholding the financial statements of Iscar Ltd., Tefron Company Ltd., and Lahavim Technologies Ltd., which were investee companies of Discount Investments. Those financial statements were submitted only to the Securities Authority, but not appended to the financial statements that were submitted to the stock exchange. [See the 2002 annual report, page 59, paragraph 3a].

In December [Tevet 5765] the State submitted a request to appeal against the release of said accused, to the Supreme Court. High court of appeals 11476/04.

6. In December [Tevet 5765] the District Court of Tel Aviv decided to cancel the appeal of Mr. Yakov Eshel on the findings and sentencing [Criminal appeal 70950/02] and the appeal by the State against the leniency of sentence [Criminal appeal 70949/02] further to an agreement between the parties. Mr Eshel was convicted of 18 counts of not reporting with the intent to mislead a reasonable investor by withholding the financial statements of Iscar Ltd., Tefron Ltd., and Lahavim Technologies Ltd., which were investee companies of Discount Investments. [See the 2002 annual report, page 59, paragraph 3a].

B. Judgments and Criminal Appeals at the Supreme Court.

In September [Elul 5764] the Supreme Court rejected the appeals of Mr. Joseph Maharshak and Mr. Yuval Maharshak on the decision of the District Court which convicted them of violations of the use of inside information. The permission to appeal was given only regarding the need of a discussion on the question of factual relationship between the inside information and the use of it, and if there was any need for a factual relationship, if proven that it exists. The Court came to the conclusion, based on the definition of the violation under section 52c of the Securities Law there is no need to prove any factual relationship between the insider information and use of it, however, the accused may and is entitled to prove any one of the defense stands, listed in section 52g of the law, which negates factual relationships. In the case at hand, the appellants did not prove the existence of any one of the defense stands. High court of appeals 8472/01.

Chapter 10 - Investigations

The following is a breakdown of investigation files that were forwarded to the investigations department, investigation files that were forwarded to the District Attorney, indictments, and the number of investigation files that were open at the investigations department and the District Attorney's office on December 31, 2004. Where the classification is by violation, the classification is according to the main violation in the file, or in the indictment [where relevant], under discussion.

| Type of Violation | 2000 | 2001 | 2002 | 2003 | 2004 | Total |
|--|-------------|-------------|-------------|-------------|-------------|--------------|
| Securities fraud | 7 | 5 | 3 | 4 | 5 | 24 |
| Use of insider information | 3 | 4 | - | 1 | 2 | 10 |
| Misleading item [in prospectus, financial statement or immediate report] | - | 4 | 4 | 2 | - | 10 |
| Lateness and failure to report | - | 4 | 3 | 2 | 2 | 11 |
| Unlicensed investment portfolio management or investment counseling | 1 | 4 | - | 1 | 1 | 7 |
| Failure to file annual notice by portfolio management or investment counseling companies | - | - | - | - | - | - |
| Failure to report promptly about preparations for resolving the "Bug 2000" problem | - | - | - | - | - | - |
| Conflict of interest between a listed company and its controlling shareholder regulations | - | - | 1 | - | - | 1 |
| Legal investigation | 1 | 2 | 4 | - | 1 | 8 |
| Breach of provisions of purchase offer regulations | 1 | - | - | - | - | 1 |
| Offering securities to the public other than by prospectus | 1 | - | - | - | - | 1 |
| No written agreement made between portfolio manager and his client | 1 | - | - | - | - | 1 |
| Violations by an employee of a stock exchange member and activity forbidden to a licensed investment portfolio manager | - | - | 1 | - | - | 1 |
| Violations under the Joint Investment Trust Law | - | - | 2 | - | 1 | 3 |
| Total | 15 | 23 | 18 | 10 | 12 | 78 |

| Year | Files which had sufficient evidence that there wasn't apparent evidence of a violation in the last five years | Files which had sufficient evidence that there was apparent evidence of a violation in the last five years | Total |
|--------------|---|--|-----------------|
| 2000 | 4 | 12 | 16 ¹ |
| 2001 | 7 | 10 | 17 ² |
| 2002 | 4 | 12 | 16 ³ |
| 2003 | 4 | 8 | 12 ⁴ |
| 2004 | 3 | 11 | 14 ⁵ |
| Total | 22 | 53 | 75 |

| Type of Violation | 2000 | 2001 | 2002 | 2003 | 2004 | Total |
|---|-----------------------|-----------|-----------------------|-----------|-----------|-----------|
| Securities fraud | 2 | 10 | 6 | 2 | 4 | 24 |
| Use of insider information | 3 | 3 | 3 | - | 1 | 10 |
| Misleading item [in prospectus, financial statement or immediate report] | 8 | 2 | 1 | 4 | 2 | 17 |
| Violations by employee of stock exchange member | - | - | - | - | - | - |
| Lateness and failure to report | - | - | 3 | - | 3 | 6 |
| Fraudulent receipt | - | - | - | - | - | - |
| Unlicensed investment portfolio management or investment counseling | 1 | 2 | 1 | 6 | 1 | 11 |
| Failure to file annual notice by portfolio management or investment counseling companies | - | - | - | - | - | - |
| Failure to draw up a written agreement between the portfolio manager and the client | 1 | - | - | - | - | 1 |
| Conflict of interest between a listed company and its controlling shareholder regulations | 1 | - | - | - | - | 1 |
| Violations under the Joint Investment Trust Law | - | - | 1 | - | - | 1 |
| Offering securities to the public other than by prospectus | - | - | 1 | - | - | 1 |
| Total | 16⁶ | 17 | 16⁷ | 12 | 11 | 72 |

* According to principle violation

- ¹. Does not include one file of a legal investigation, the investigation of which ended in 2000 and whose findings were sent to the foreign authority.
- ². Does not include two files of a legal investigation that were received from a foreign country, and whose findings were sent to the foreign authority.
- ³. Does not include three files of a legal investigation that were received from a foreign country and whose findings were sent to the foreign authority.
- ⁴. Six additional files were forwarded to the Supervisor of Enforcement, to be sent to the District General.
- ⁵. Does not include three files of a legal investigation that were received from a foreign country.
- ⁶. Does not include three files of a legal investigation which were received from a foreign country and whose findings were sent to the foreign authority.
- ⁷. Does not include one file of a legal investigation, the investigation of which ended in 2000 and whose findings were sent to the foreign authority.

| Type of Violation | 2000 | 2001 | 2002 | 2003 | 2004 | Total |
|--|-----------|-----------------------|----------|----------|----------|-----------|
| Securities fraud | 6 | 5 | 5 | 1 | 2 | 19 |
| Use of insider information | 3 | 1 | 1 | - | 1 | 6 |
| Misleading item [in prospectus, financial statement or immediate report] | 3 | 1 ⁹ | 2 | 3 | 2 | 11 |
| Fraudulent receipt | - | | - | - | - | - |
| Accepting bribery | - | | - | - | - | - |
| Unlicensed investment portfolio management or investment counseling | - | | 1 | 4 | 3 | 8 |
| Violations under the Joint Investment Trust Law | - | | - | - | - | - |
| Total | 12 | 7¹⁰ | 9 | 8 | 8 | 44 |

At the end of 2004, 12 uncompleted investigation files remained with the Investigations Department. At the District Attorney's office, no decision had yet been made whether to file an indictment or not [see tables 16 and 17] in 11 files. The Chairman of the Authority recommended indictments for all files

| Year | Number of files |
|--------------|-----------------|
| 2001 | 1 |
| 2002 | 1 |
| 2003 | 1 |
| 2004 | 8 |
| Total | 11 |

| Violation | Number of files |
|---|-----------------|
| Securities fraud | 4 |
| Use of insider information | 1 |
| Misleading item [in prospectus, financial statement or immediate report] | 6 |
| Conflict of interest between listed company and its controlling shareholder regulations | - |
| Unlicensed investment portfolio management or investment counseling | - |
| Total | 11 |

⁸ The number of indictments does not necessarily match the number of investigation files that are sent to the District Attorney's office, as sometimes the District Attorney's office combines a number of investigation files into one indictment, or vice versa, it files several indictments under one investigation file.

⁹ Correction of a year 2000 indictment.

¹⁰ This figure includes an indictment that was filed in 2000 and was re-filed after it was amended in 2001.

Chapter 11 - Research, Development and Economic Advice

1. Economic Advice

During 2004 economic advice on various current issues was given to the Chairman of the Authority and to various departments of the Authority.

During the year, the economics department was a partner in groups which dealt with the following matters: a capital markets group, advice to the Corporation Finance department, to the investment advisors committee, to the investigations committee, to the District Attorney on matters related to trading on the stock exchange, participation in discussions of the committee to reform the capital markets ["Bachar Committee"], coordinated the workings of the committee to study supervision over alternative electronic trading systems ["ATS"], coordinated the coordination team between the Authority and the stock exchange. In addition, the department took part in the group that examined the issue of prospectuses and current reports of "structured securities" and "index linked certificates", and was involved in the development of the economic model which is incorporated in the system that identifies financial risks of companies listed for trading on the Tel Aviv Stock Exchange ["Red Flags System"].

In addition, the department prepared a professional paper at the request of the Tel Aviv Office of the District Attorney [Taxation and Economics]. The department was also a partner in the tender to choose an investment portfolio manager for the Authority, in addition to the regular follow up on the investment portfolio.

2. Capital Markets Group

During the year the department, which is headed by Prof. Shmuel Hauser, coordinated the workings of the capital markets group. That group is charged with the responsibility to eliminate limitations on the development of the capital markets in all fields related to trade development, and to develop and increase investor trust in the capital markets.

3. Management of Systems for Identifying Unusual Trading Patterns in Securities

During the year, development, management, and operations of the computerized system which, on a daily basis, scans activity on the stock exchange in order to identify unusual trading in securities. The system identifies unusual activity in trading, while relying on economic – financial criteria and other criteria, which are based on the practical experience accumulated at the Authority in recent years.

4. Development of Databases

During the year, development of the computerized database continued. The following reports were developed: a report on "Rezev" orders, according to period, update, development and improvement of the report on "Rezev" orders report; a weekly report on interested party shareholders and a report on open positions.

5. Research Projects

a. In October 2004 a paper was published on the contribution of market makers to the efficiency of trading in options on electronic stock exchanges. At the end of 2002 the Hauser Committee recommended to permit, inter alia, operations of market makers in options, under the electronic trading system of the Tel Aviv Stock Exchange ["TASE"]. Further to this recommendation, the stock exchange decided to encourage market makers in Shekel-Euro options by direct compensation to the market makers against their undertakings. The undertakings include the responsibility to quote prices at all times for buy and sell. Market makers started operating in March, 2004. The beginning of their operations permits examining, under empirical conditions, the contribution of the market makers to the liquidity of said options and of the efficiency of trading in options on the stock exchange, where the trading is electronic and the market conditions of the market makers are identical to those of other players in the trading.

The main results are: [1] increased liquidity - volume of trading in options increased by 60% and the spreads between buy and sell prices decreased by 35%; [2] as a result, the efficiency in trading of Shekel - Euro options increased – we found that the deviation from equality ratio between call options and put options decreased significantly by 12% and the skewness in option prices, which is common in option trading, decreased by 30%. These improvements in trading occurred notwithstanding the fact that the volume of the market traders compared with market makers was only 15% of the overall market. The main conclusion from these findings is that the market makers presence has a stronger influence than the volume of their transactions, as they stimulate trading activities even without their intervention. All this points to the need to encourage their integration in the Tel Aviv Stock Exchange, in trading of securities which have relatively low trading volumes.

b. In December 2000 a paper was published dealing with the subject - is publishing the market price in the pre-opening phase of trading informative or manipulative. The phase before trade opening is intended to make the act of publishing the price at the beginning of the trading day using information garnered from buy and sell orders more efficient. The paper examined the question of to what degree is the act of publishing the price informative or manipulative. The paper was based on a sample of data from the Tel Aviv Stock Exchange, data that permits a differentiation between manipulation and information on the process of publishing the market price. The main finding is that publishing the share price before market opening is mainly informative, but also involves a manipulation of information, by buy and sell orders, either partial or actual, or through timing orders in a manner which limits the possibility of other investors to respond accordingly. Setting the opening price, random – timed, reduced the possibility of manipulation. It was found that on expiration days and in the period when opening market prices were not randomly set, fluctuations in market prices increased, and the information included in the demand and supply curve decreased, compared to other days. In addition, it was found that the market prices at the opening phase are influenced sometimes by the manipulative orders during the pre-opening phase.

In addition various other papers and lectures were delivered, on the following subjects:

[1] the "Euronext" stock market; [2] the advantages and disadvantages of an actual clearinghouse as opposed to a financial clearinghouse; [3] issues of debt certificates by local authorities in Israel; [4] considerations for and against the "Box" system; [5] participation in writing a paper on the subject of "Structured Notes" in the capital markets; [6] memo on the subject of models to supervise foreign securities authorities; [7] memo on the subject of are fluctuations in the share prices of shares traded on the Tel Aviv Stock Exchange too volatile; [8] a document dealing with the subject of is it proper to let banks participate in share trading; [9] a rejoinder to the Israel Democracy Institute on the issue of the capital markets; [10] a memo on the subject of supervision over provident funds; [11] alternatives to raising capital through innovative financial instruments; [12] registering securities for trading in Israel of companies that are traded in the United States; [13] participation in writing an offer to examine the influence of "Maof" players on trading in the stock exchange; [14] importance of non-banking financial markets, and the elimination of limitations to their development; [15] aid in implementing the recommendations of the real estate investment trusts committee ["REIT"]; [16] participation in drafting regulations on the subject of purchasing shares for one's own account; [17] participation in filling out a questionnaire to IOSCO on corporate governance; [18] a questionnaire of the World Bank on the subject of short sales.

Chapter 12 - Class Action Lawsuits

1. Financing of Class Action Lawsuits in 2004

According to section 209 of the Companies Law, the Authority may pay the expenses of a class action lawsuit, if it is convinced that it is in the public interest, and that there is a reasonable chance that the court will certify it as a class action.

During 2004, the Authority continued its ongoing financing of class actions, whose financing was approved in previous years. The Authority also approved two application for financing with regard to which applications were filed with the court to approve them as class actions. Two requests for additional financing, one of which was submitted to the Authority last year, were withdrawn at the request of the applicants, after it was made clear to them, following an examination of the indictment and additional documents that were submitted to the court, that their chances for additional financing were not good. The following is a summary of the lawsuits for which the Authority decided to grant the application for financing:

A. Class action against M.P.I. Mediterranean Assets and investments Ltd., and Mishor Ha'Hof Building and Asset Company Ltd.

This class action is submitted to the court further to a request for assistance in accordance with section 338 of the Companies Law, and deals the calculation of fair value, by the court, of compensation for shares which were the subject of a forced sale according to section 337 of the Companies Law. Section 337[a] of the Companies Law requires a forced sale of shares held by the shareholders who did not respond to a purchase offer, where their shareholdings do not exceed 5% of all shares of the public company.

The file concerns a purchase offer for all shares of M.P.I. Mediterranean Assets and Investments Ltd. ["Company"], according to a detailed schedule dated 31.12.2003 by Mishor Ha'Hof Building and Asset Company Ltd. ["the offeror"] for the purchase of shares of the company held by the public ["purchase offer"]. The offeror, a controlling shareholder in the Company, held 87.55% of the Company's shares. Up to June, 2003 the offeror and Trefoil Israel CIM L.P., part of the Shamrock Group ["Shamrock Group"] each held 43.77% of the shares of the Company, and together 87.55% of the shares of the Company. An agreement existed between the two companies on joint control, which granted each of the companies the right to veto decisions that the other group wanted to pass.

At the time of the purchase offer, the Company was a public company, whose shares were registered for trading on the Tel Aviv Stock Exchange. The average share price of a share in the six months preceding the detailed schedule was NIS1.23 per share. In the purchase offer, the offeror set a price of NIS1.38 per share ["offer price"].

Shareholders' equity per share, according to the Company's financial statements as at 30.9.2003 was NIS2.14.

The purchase offer was preceded by another purchase offer, dated 9.12.2003, which also offered NIS1.38 per share. That purchase offer failed.

On 26.6.2003 the offeror noted that it entered into an agreement with the Shamrock Group, according to which the offeror undertook to purchase Shamrock Group's entire holding in

the Company, for \$10.2 million. The transaction reflected a price of NIS2.28 per share. The transaction was carried out, and by the eve of the purchase offer the offeror held 87.55% of the company's shares.

Further to acceptance of the purchase offer, and as required by section 337[a] of the Companies Law, a forced sale of the remaining shares was to be carried out, and the Company was to become a private company.

The applicant, a private individual, did not respond to the purchase offer and his shares were forcibly sold, after he had held them for three years.

The applicant claimed that the purchase price offer was not fair, and requested assistance from the Court, in accordance with section 338 of Companies Law. The applicant claims that the fair value that the offeror had to pay had to be NIS2.28 per share, at least, that is, the same price that Shamrock Group received on the sale of its shares to the offeror. The applicant submitted his request to the Court, within the period of three months as set out in section 338 of the Companies Law, and submitted his request as a class action in the name of all participants in the purchase offer. Civil file 1498/04

B. Class Action in the Matter of Gibor Real Estate, Gibor Sport Holdings Ltd., and Others

The action relates to damage caused to the shareholders of the Gibor Real Estate Ltd., ["Gibor Real Estate"], as a result of the issue of shares of Gibor Real Estate to Gibor Sport Holdings Ltd. ["Gibor Holdings"]. The issue was approved on 7.7.2002 and was carried out on 21.8.2002 ["issue of shares"]. Both companies are public companies whose shares are traded today on the maintenance list of the Tel Aviv Stock Exchange. At the date of issue, Gibor Holdings was the controlling shareholder of Gibor Real Estate, and held 61.48% of its shares. After the issue, it held 90% of Gibor Real Estate's shares.

The issue of shares was undertaken against the transfer of shares that Gibor Holdings held in a number of companies. The value of the remuneration was estimated, by a valuation report, at NIS43 million.

The plaintiff claimed that the valuation report was incorrect and negligent, and that actually the company's value was negative. The meeting of shareholders called for the purpose of approving the issue of shares was told that there was great potential in the transferred companies, and that the public was given a benefit, but in fact Gibor Real Estate started to deteriorate immediately after the issue.

The annual financial statements of Gibor Real Estate as at 31.12.2002 showed that the company had losses of NIS28.6 million and a shareholders' deficit of NIS14.5 million. In addition, the public auditors noted that these facts and others raise significant doubt concerning the existence of the company as a viable enterprise.

On the basis of the above-said, the claimant claims that the damage to shareholders is the dilution following the issue of shares, together with the unwarranted increase in Gibor Holdings' share of Gibor Real Estate.

The action was submitted against the controlling shareholders and officeholders of Gibor Real Estate and against the valuator [who prepared the valuation report for the issue]. The

main grounds are: violation under section 52a of the Securities Law, which deals with damage caused to shareholders as a result of a violation under sections of the Securities Law, discrimination, duty of the shareholders to act in good faith and in a manner acceptable to the Companies Law, negligence, and breach of duty under the Civil Wrongs Ordinance. civil file 1200/04

2. Class Actions that were closed During the Year

A. Class Action against Vitalgo Textile Industries and Others [today Guy 121 Promotion Ltd.]

On 27.1.2004, and after the action was approved as a class action, a compromise agreement was signed between the parties to the action, according to which NIS1,000,000 will be distributed by the defendants to the benefit of the action group, after a deduction for various expenses, including compensation to the lead class action claimant - NIS50,000 plus value added tax, professional fees to the claimant's legal counsel - NIS180,000 plus value added tax, and a refund of expenses to the Authority - NIS56,418. Mr. Yehuda Barlev, CPA, was appointed as trustee. He located the members of the group and was responsible to distribute the funds. At the end of distribution, it was noted that NIS99,000 was not distributed. In accordance with the compromise agreement, this money was donated to the benefit of the community [see also the 2003 annual, page 79, paragraph 3c].

B. Class Action against I.S.I. Consultation and Guidance Ltd., and Others

The action and a request to have the action certified as a class action, was rejected by agreement and with the approval of the Court, without costs, in August, after the claimant became convinced that the probability of proving the claim was low [see the 2003 annual report, page 79, paragraph 3e].

C. Class Action against Discount Investments Ltd., and Others

In September the Supreme Court rejected an appeal against the rejection of the request to recognize an action as a class action in District Court of Tel Aviv. The action concerned a sale of shares of a company controlled by Discount Investments Ltd., and according to the claimant, sold at a very low price, because of the personal interest of the controlling shareholder in the transaction. The Supreme Court accepted the position of the District Court that regulation 5 of Securities [Restrictions on Conflicts of Interest Between a Listed Company and its Controlling Shareholder], Regulation 5754-1994 [this corresponds today to section 281 of the Companies Act] does not grant the right to a personal claim but rather grants the right to claim only against the company. In addition, the Court decided, as a rule, that in order that a justification for claim exist according to section 52a of the Securities Law, it should be proven that damage was caused to the holders of securities, and that the damage caused is included under a class of damage for which responsibility can be claimed, and that the pretext [section 52a[a] of the Securities Law states: "...an issuer is liable to a security holder, for damages caused to the holders of the issue, as a result of the issuer's violations of any provisions of the law or any regulation issued there under...". In the case at hand, the damage that the claimant claims, is the decrease in the value of his holdings in the defendant as a result of the sale of shares of the investee company, this damage was caused primarily to the company, and the right to reduce the

damage is in the hands of the company only [see also the 2003 annual report, page 79 section 3]. Civil appeal 3051/98; civil file 1064/97

3. Class Actions that were settled Before the End of the Report Year

A. Class action Against Ephraim Lahav and Others

After approval of the compromise agreement, most of the compensation funds were distributed by the trustee, Advocate Raphael Amiad, to members of the represented class. The trustee is now preparing his final report to the Court. [see also the 2003 annual report, page 78, paragraph 2a] Civil file 496/95, Leave for Civil Appeal 6561/99.

B. Class Action against Reichert Industries Ltd and Others

During 1999-2002 a compromise agreement was signed between the claimants and most of the defendants, except for Mr. Menashe Cohen, who held office as assistant managing director and controller of the company, and Mr. Dan Reichert, who held shares in Reichert. Towards the end of 2002, a decision was reached establishing the responsibility of the two last defendants, and they were found liable to pay NIS3 million and NIS400 thousand respectively. These amounts are supposed to be added to the NIS10.4 million which has been accumulated up to now within the framework of settlements with the other defendants and which is being held in trust for the members of the class. Mr. Reichart transferred the full amount of his liability, and it is deposited at this stage in a trust fund for the members of the class. The amount charged to Mr. Cohen has not yet been deposited. The appeal that Mr. Cohen submitted was rejected because he did not make the deposit guarantee during the report year. A decision on the appeal and the counter appeal by Mr. Reichart, and the appeal by the representative plaintiff against Mr. Cohen, has not yet been rendered. It should be noted that the representative plaintiff, Moshe Shemesh, of blessed memory, passed away, and that the Supreme Court ordered that heirs of the late Mr. Shemesh replace him in the appeal. Legal counsel of the representative plaintiff, Ardinest Ben - Natan & Co., is acting in order to locate the members of the represented class who are entitled to the distribution of the settlement and judgment funds. Because of the appeal process, the District Court decided that the distribution of funds to those entitled will be done only after rendering judgment on the appeals [see also the 2003 annual report, pages 78-79, paragraph 2b]. Civil file 1134/95, Leave for civil appeal 8268/96; 8377/96; and 8332/96.

4. Pending Class Actions

A. Class Action against Elscint Ltd. and Others

As at the date of writing this report, no decision on the appeal has been rendered [see also the 2003 annual report, page 79 paragraph 3b] Civil file 1318/99; Leave for civil appeal 7028/00

B. Class Action against Snowy Israel Ltd and Mirage Development Israel Ltd.

A request to confirm the action as a class action is underway, summations have been submitted and the parties are awaiting the decision of the Court [see also the 2003 annual report, page 79, paragraph 3d]. civil file 1004/02.

C. Class Action against Ofmat Investments and Others

The District Court of Tel Aviv rejected the request to cancel the action. The defendants submitted a request to appeal to the Supreme Court against the decision to reject the request to cancel. At this stage, the claimant submitted his reply to the request to appeal to the Supreme Court. The District Court has not yet rendered judgment on the request to recognize the action as a class action [see also the 2003 annual report, page 79, paragraph 3f]. civil file 1203/02.

D. Class Action Regarding Yiskal

As noted, the District Court rejected the request to recognize the action as a class action. Under the framework of the appeal to the Supreme Court, summations were submitted and a date to complete the oral presentation was set for March 2005 [see the 2003 annual report, page 78, paragraph 1b]. civil file 1981/02, civil appeal 9014/03.

E. Class Action against Bolos Tourism and Hotels Ltd. and Others

The action is in an advance stage and deliberations were set for May 2005. Requests to stay proceedings in the action based on the position that the Court must wait until the end of the proceedings on liquidation of the plaintiff company has been submitted. The claimant submitted his objection to the request to stay. In addition, a request to delete the company from the action is pending before the Court [see the 2003 annual report, page 79, paragraph 3g]. civil file 1934/02.

F. Class Action against Kaytal International Holdings and Development Ltd. and Levi Kushnir

The file is set for giving testimony in March 2005, under the framework of deliberations on the request to recognize the action as a class action [see also the 2003 annual report, page 79, paragraph 3h] civil file 2338/02.

G. Class Action against Commerce Bank Ltd and Others

As noted, the District Court of Tel Aviv rejected the request to confirm the action as a class action. An appeal to the Supreme Court by the representative plaintiff was submitted against the decision of the District Court. The deliberations have been postponed until May 2005 [see also the 2003 annual report, page 80, paragraph 3i] civil file 1521/02. Civil appeal 10927/02.

H. Action |Against A.Z. Baranowitz Assets and Rentals Ltd., and Armogad Holdings Ltd.

The hearing on the action has not started as A.Z. Baranowitz – Assets and Rentals Ltd. is under procedural freezing. In addition, the company is formulating plans to settle creditors' debts. ["creditors' arrangements"] [see also the 2003 annual report, page 77, paragraph 1a]. civil file 1606/03.

5. Additional Proceedings

After year end, on 2.1.2005, the legal advisor to the government and to the Authority submitted his position paper on the request of 28.10.2004 [file 22082/04], which concerns a request, by agreement to cancel an action [civil file 2314/03 – Moshe Levy Against Ha'Shmira Company Ltd., and others], and a request to recognize the action as a class action, all as noted below:

On 2.12.2003 the claimant, Mr. Moshe Levy, submitted a request to certify an action as a class action in accordance with section 210 of the Companies Law, 5759-1999 against Ha'Shmira Company Ltd., a private company [respondent 1] and against Ha'Shmira – Security Technologies [1971] Ltd., a public company, and at the date relevant to the action, its securities were traded on the Tel Aviv Stock Exchange [respondent 2]. The pretext to the action was a request for the Court's assistance in light of the forced purchase of shares by respondent 1 and 2. The claimant claimed that the shares were bought from him at a value less than their fair value.

On 28.10.2004 the claimant submitted the request to cancel the action and the request to recognize the action as a class action ["the request"]. Within the framework of the request the claimant noted, inter alia, that he reached a settlement with the respondents in that they will pay him NIS300,000 as follows: NIS220,000 to the legal counsel of the claimant; NIS70,000 to an expert whose professional opinion supported the claim action and NIS10,000 to cover office costs incurred by the claimant.

In its decision, the Court was requested to state that the claimant and his legal counsel are not entitled to receive from the respondents any fee concerning their withdrawal from the claim action, as the respondents are not allowed to pay such fee. Alternatively, the Court was asked to decide the fee that the claimant and his legal counsel could receive. In addition, the Court was requested to set guidelines regarding publishing the details of the request and details of the claim action, in public, in order to permit potential members of the group to replace the claimant and his legal counsel in managing the claim action, or to submit an alternative claim action.

The following are the main points of the position:

Cancellation of the request to confirm the action as a class action requires the consent of the Court, which differs from a cancellation under normal procedures. A request to cancel will not be automatically cancelled.

A claimant and his legal counsel are not entitled to receive a fee because of their withdrawal from a request to confirm a class action, except with consent of the Court and at an approved amount. This position is drawn from the provisions of the Companies Law regarding settlements of class actions, and from the basic principles of the class action concept, one of the purposes of which is to prevent the use of the power of class actions to make personal gain, without benefit to the public.

A payment of fees to the claimant and his legal counsel for their withdrawal represents a danger of real damage to the class action concept. As a rule, it is suggested not to approve said fee. A fee should be paid only in the exceptional case where the withdrawal is in good faith because of circumstances that were not reasonably expected. A nominal fee should be paid in such circumstances, but the fee paid should be far from the compensation and fee which would be paid if something concrete was achieved for the group in settlement.

On the side of the benefits of preventing inappropriate agreements, one must consider the benefits of encouraging claimants to submit serious claim actions based on information that they have diligently garnered. A danger of loss because of expenses incurred and time invested in the claim could deter worthy claimants who act in good faith from submitting claims. Taking the above said into account, one must balance the factors and permit payments to the claimant and his legal counsel to cover their expenses.

In determining a fee it is reasonable to also consider: the number of hours involved and which were reasonably necessary, a reasonable fee rate taking into account the standing of the legal counsel and a realistic number of hours invested in the claim. The fee – should be nominal; it is not intended to be full compensation for the work undertaken, and should be far from what the claimant and his legal counsel would have received if they would have come to a settlement agreement for the group. If not, there is no incentive to settle for the benefit of the group.

In the case at hand, it is suggested not to approve the compensation agreement, taking into account the excessive amount, which does not reflect the fact that nothing was really achieved for the group.

The position stressed the importance of the class actions concept system and its special importance in the securities field, as this system is almost the only medium to defend the rights of investors from the public. Accordingly it is very important to encourage deserving class actions in this field, and to compensate, as necessary, the claimants who achieve fitting results for the group.

The Attorney General became involved in the proceedings, on the basis of section 1 of the Code of Civil Procedures [Attendance of the Legal Advisor] [New Version] and on the basis of the special status given him by the Companies Law regarding class actions. The Authority is party to the position, on the basis of its position, granted it by the Securities Laws – to defend the interests of the public that invests in securities. In this case, the interests of the public that owns shares in respondent 2 could be hurt together with the interests of the investing public in general, as a result of the improper use and manipulation of the class action concept.

The response was submitted on behalf of the claimant. A date for deliberation on the request has not yet been set.

Chapter 13 – Information Systems

1. Electronic Reporting – MAGNA

The electronic reporting project is an information system for collecting and distributing, through the Internet, the entire gamut of reports that are required of entities subject to the Authority's supervision: corporations, mutual funds, companies providing investment advice, companies providing portfolio management and underwriters. The project is intended to harness the field of electronic communications and the Internet systems to service the investing public and the entities that are supervised by the Authority.

The system handles all types of report including: prospectuses, annual financial statements, interim financial statements, immediate reports, reports of changes in interested parties holdings, reports on private issues, purchase offers reports, and reports of conflicts of interest in corporations. Similarly, the system will handle prospectuses, immediate reports, monthly reports of mutual funds, forms for portfolio management companies, etc.

The project's objectives are: giving immediate access to public information to a wider spectrum of the public, equal dissemination of information, increasing the efficiency of the supervision over the reliability of information, and providing new tools to carry out analyses.

From the first day of full operation [in November, 2003] and up to the end of 2004, thousands of authorized signatories signed up for the system, and about 50,000 various reports were dealt with, including 33,384 reports in 2004 alone. These reports were sent for processing by the Authority's staff, automatically and through the reporting site, and the public reports were distributed automatically through the distribution site. They were also distributed to the stock exchange and to commercial distributors of information. Every day thousands of Internet surfers log on to the distribution site of the system, and they receive various reports on corporations and processed data reports [see also the 2003 annual report, page 81, paragraph 1].

The project is among the most advanced of its type in the world, and is based upon the most up to date and advanced technologies. It provides technological solutions to complex, questions, including single – value identification of reporting entities, and data security. It has even received a number of prestigious awards for excellence in the field of information systems.

During 2004 a long list of improvements were made to the system, including: stabilizing the system and changing the format of forms; many improvements to the two Internet sites; setting up a form site for easy reporting, setting up an improved system for control and monitoring, to predict and identify faults, carrying out a satisfaction reviews regarding the system and implementation of most of the recommendations; setting up an additional distribution site in the event of a crash; strengthening the interface with the stock exchange; strengthening the servers and various other upgrading activities.

At the end of the report year, the legislative phase which permits the operation of the system for other users was completed. Among those users are mutual fund managers, trustees, portfolio management companies, investment counsel companies and underwriters. All preparations for operating the system for said users have been completed and the Authority is getting ready to carry out the operations, training and assimilation phases in 2005.

2. Document Archives and the Computerized Office

The system permits archiving of all types of internal and external documentation, including documents that are received electronically, by fax, or in paper form [which is scanned into the system]. Through the system, it is possible to identify and reconstitute any document, according to type, on the basis of set parameters and free text.

The system represents one of the most essential tools for the Authority's operations, and it also serves the electronic reporting for archiving and retrieving documents that are received from the reporting entities, some of which are also distributed to the public [see paragraph 1 above]. In addition the system includes the standard functions of a computerized office such as - internal and external e-mail, task management, appointments schedules, address book and workflow.

During the year many improvements were made to the system: improvements in the interfaces with the other information systems of the Authority; upgrading computer software programs, upgrading the backup system for central backup; strengthening the existing servers; additional systems to improve availability and reliability; changes and additions to the "warning system" project [see also paragraph 6 below].

The system improves the Authority's operations, and they become more efficient. The need for manual work becomes unnecessary and the load on the staff in carrying out their responsibilities becomes lighter.

3. Computerized Operations System

During the report year, efforts to develop and maintain the central computerized system continued. This system includes most of the information on subjects that are dealt with by the Authority: data on corporations, mutual funds, investment advisors and investment portfolio managers, trading data, supervision over trading, identifying exceptions, and data that serve all employees of the Authority.

During the year additional systems were developed, and the existing systems were expanded, as is necessary because of changes in work procedures and legislation. Inter alia, new developments in the treasury field were carried out [changes in the system of issuing fee requests], advice [centralized collection], the mutual funds [changes in examining the monthly reports of the funds], etc. In addition, the interfaces with the information system of stock exchange for receiving data on trading were improved. New screens and new reports were introduced. Current maintenance for systems was carried out.

An additional and significant development that was carried out was in the field of automatic entry of all data from the reporting systems, this in anticipation of the MAGNA system coming on – line, for the mutual fund and portfolio management sector [see paragraph 1 above], with the added intent of canceling the need to enter data manually, and the development of additional new applications because of the great amount of information that the reporting system receives.

During 2005, this process of improvements is expected to continue.

4. The ISA Web Site

During the year, the old computer which served the Internet site of the Authority [www.isa.gov.il] for four years was replaced with a new one, and from November the new site is run from the Authority's offices. The site was removed from the offices of the outside supplier who provided services to the Authority up to now. The software that served the site underwent significant improvements - to a new, innovative, and advanced environment. In addition, the site continues to be updated regularly with new and relevant content: information on the Authority, information on laws and regulations that were legislated during the year, news, and publications, updated lists of entities which are under the supervision of the Authority, frequently asked questions and answers that were submitted during the year.

In addition, efforts continue the move, the purpose of which is to provide information on an individual basis and through the Internet site, on the status of registration of applicants to receive a license to become investment advisors and/or investment portfolio managers. In order to improve this service, the interface that updates the site automatically from the internal systems was upgraded. In addition, planning has started on a project to permit license applicants to register and pay by Internet.

5. Information System for Investigations

During the report year, the server which serves the information system to manage investigations was replaced, and the new server provides significantly improved capabilities. New and improved software systems were also introduced, which will increase the effectiveness of the system.

Also, the development of the information system continued, new functions and additional abilities were added, and new interfaces were built.

In addition, during the year an additional phase [which started in 2003] was completed. This phase involves a change in the archives of the system, such that all existing and relevant documents will be stored in standard facilities of the entire system. Today, with completion of the process, all Authority authorized users can access, in a uniform and efficient manner, all existing information, without dependence on the original information system which created and stored the information. [see also the 2003 annual report, page 83, paragraph 5]

6. Warning Systems

Together with the economics department, the Corporation Finance department, and the department for intelligence, the department was partner in identifying and setting up an information system to provide "red flag" warnings.

Based on financial ratios that were developed by the Corporation Finance department, and based on economic models that were developed by the economics department, the department built a system which automatically receives financial data from the financial statements of corporations that is fed through the MAGNA system, on the one hand, and various other data [such as data on trading] on the other hand. After a data check, and after plugging them into the relevant ratio formulas, the system decides if the data are in order or if a "red flag" is to be issued.

Through a sophisticated and innovative system of interfaces, the results of the examination are combined with the original financial statement, and are forwarded together to the Authority's archives. Users at the Authority, whose responsibilities are to examine the reports, receive notices in their e-mail boxes, and they access the information in a simple and immediate manner.

The computerized system saves the Authority's staff many hours and enables the staff that checks the financial statements to give priority and to concentrate on those reports that signal a high level of risk.

7. Infrastructure

During the report year, significant improvements were made in the Authority's computer infrastructure. Among the important issues handled the following can be noted: setting up a video conference system between the two offices in Jerusalem and Tel Aviv, which permits holding meetings and discussions without the need for physical presence and saves time and money; replacement of all outdated personal computers and printers with new computer operating systems and printers; improvement and upgrading of the main computer rooms at the Authority's sites in Jerusalem and Tel Aviv by introducing automatic systems to detect flooding and fire; continued upgrading of the local network servers; upgrading the security system and adding security components for communication between the two offices of the Authority; significant upgrading of the system of control and monitoring which warns of breakdowns and issues reports; upgrading the communication lines between the Authority's sites and between the Authority and the outside world; massive improvements in all phases of back ups and disaster.

These activities will continue in 2005, mainly in upgrading the infrastructure of communication and operating systems at the end user's position.

Chapter 14 - Communications from the Public

1. Handling Communications from the Public

During the report year, the Authority received and processed 441 communications from the public (compared with 131 communications from the public in 2003). Some of the communications came from securities holders asking for information or direction that would assist them in continuing to deal with their affairs. An additional group of communications concerned providing information to the Authority regarding current reports or prospectuses that, in the opinion of the person making the communication, were defective or deficient, or regarding improprieties in the trading of securities on the stock exchange. The information is referred to the various departments at the Authority for processing, according to the subject matter of the communications.

2. Report of the Director for Implementation of the Provisions of the Freedom of Information Law, 5758-1998

During the reporting year, 49 requests for information were made to the Authority (compared with seven requests in 2003). In 36 cases, the information was given in full. In seven cases, the individuals making the request were referred to other parties. Six cases were answered partially or rejected, as they dealt with information that could legally be disclosed or the requested information, if disclosed, could undermine the normal operations of the Authority as a public authority, or its ability to carry out its functions.

It should be noted that most communications from the public to the Authority indirectly involve requests for information, but they do not concern detailed information, but merely requests for direction, clarification, or assistance, or they are complaints. Replies to communications of this kind naturally involve giving information, but they are not included in the Director's report.

All requests for information were answered within 30 days from the date of making the request.

3. Communications

An additional address for contacting the Authority, in addition to its office in Jerusalem, is the address of the Director of Public Communications and the Director for Implementation of the Provisions of the Freedom of Information Law at the Authority's Jerusalem's office:

22 Kanfei Nesharim Street

Jerusalem 95464

Telephone: 02-6556555

Fax: 02-6513646

E-mail: public@isa.gov.il

4. Databases Registered under the Protection of Privacy Law, 5741-1981.

- A. Interested parties - personal details, positions, and holdings** - The database includes data on interested parties, as defined by the Securities Law, who have a duty to report to the Authority under the law and the regulations.
- B. Licensing of investment advisors and investment portfolio managers** - a database designed to assist in implementing the law regulating advice, including inter alia: registration of applicants, their credits based on education, examinations, and apprenticeship and the issue of licenses to those entitled to practice the profession.
- C. Intelligence** - a database designed to collect information for purposes of assisting inspections that are designed to identify violations, with respect to which the Authority has investigative powers.
- D. Salary/personnel** - the Authority's employees - a database designed to make salary payments to the Authority's employees.
- E. Investigations** - a database designed to collect information relating to investigations that the Securities Authority is empowered to conduct.
- F. Payments to suppliers and accounting** - a database designed to make payments to suppliers and providers of services.
- G. MAGNA system** - a database for reporting entities and for authorized electronic data users [reports by corporations subject to the Securities Law].

Chapter 15 – Committees to Encourage Trade in the Capital Markets and to Increase Investor Confidence

The crisis that struck the capital markets in Israel in recent years requires those active in the capital markets in general, and the supervisory authorities in particular, to reconsider everything concerning the encouragement of trading in the capital markets, its development and restoring the confidence of investors in it.

Against this background, the Authority formulated a strategy whose goal was to encourage trade in the capital markets and to increase the trust of investors. This plan already operates for two years, through two interdisciplinary teams, in which some of the staff of the various departments of the Authority take part. At the head of the committees are the Head of the Economics Department at the Authority, Prof. Shmuel Hauser, and the Director of Enforcement at the Authority, Advocate Prina Guy.

A. Committee to Encourage Trade in the Capital Markets

The committee to encourage trade in the capital markets works to develop and improve the capital markets. It looks to isolate impediments that hamper the development of the capital markets, and works to eliminate them. During the year, the following matters were examined:

- **New financial instruments** – the committee examined the possibility of introducing new financial instruments to the Israeli capital markets, based on that accepted in the developed capital markets of the United States and Europe. The following instruments were examined: tracking stocks, money market funds, reverse mortgages, mortgage based securities, options on individual shares, covered warrants, etc.
- **Taxation of the capital markets** – The committee examined together with income tax experts, the issues which are impediments to developing the capital markets.
- **Dual listings** – the committee continued to act to encourage eliminating the impediments to dual listing of companies on the Tel Aviv Stock Exchange and the London Stock Exchange, and relief to stock exchanges in the United States. In addition, the possibility to increase the relief given to other stock exchanges was examined.
- **Supervision of the alternative trading systems [ATS]** – the committee discussed the issue of supervision of the alternative trading systems that wish to operate in Israel. The Chairman of the Authority appointed a committee to examine supervision of the alternative trading systems.
- **Market makers in government bonds** – the committee continued with its efforts to eliminate impediments on the operations of market makers in government bonds, this in accordance with the recommendations of the Hauser Committee. The committee worked together with the Authority, Capital Markets Division, the Accountant General, Bank of Israel and the stock exchange in order to jump start market makers operations. The model to regulate the operations of primary dealers in government bonds was approved by the Finance Committee of the Knesset.

- **Clearing forward contracts on government bonds** – further to the issue of the start of operations of market makers in government bonds, the committee discussed the subject of clearing forward contracts on government bonds with the Ministry of Finance. The main points of the discussion centered on examining the advantages and disadvantages of physical clearing as opposed to monetary clearing. During December 2004, the law on government loans regarding regulating the operations of primary dealers in "Shahar" bonds was approved.
- **Market makers in shares and derivatives** – the committee continued cooperation with the Minister of Finance and the stock exchange in order to eliminate everything concerned with regulating the operations of market makers in shares, derivatives and corporate bonds, in accordance with recommendations of the Hauser Committee. During March 2004, primary dealers began trading in Shekel - Euro options.

The committee also dealt with a number of subjects, including: eliminating the impediments related to agreements for repurchase of securities [REPO]; examining the criteria for and against the "Box" system; revaluation of non-traded assets, together with the Minister of Finance; advancing the possibility of signing multi-lateral agreements [MOU] with countries that are members of "IOSCO"; discussion on index linked certificate and structured products; pension savings in the framework of a closed personal account; supervision over financial middlemen, including analysts; designated securitization, including bonds issued by the Chief Scientist, bonds issued by the health services and municipal bonds; setting conditions for transactions in shares for a personal account; educating the public on the important contribution of the stock exchange to the capital markets, on one hand, and the duty of caution in an investment in shares, on the other hand.

B. The Committee to Increase Investor Trust in the Capital Markets

During the year, the committee dealt with examining additional ways to make enforcement more efficient and more applied, this in addition to criminal and civil enforcement which already today.

Member of the committee, which is comprised of seven members, were chosen from various disciplines and from varied educational backgrounds. The committee includes public accountants, economists, and lawyers from the various departments at the Authority. At the head of the committee is the Director of Enforcement.

In the first phase, the committee was asked to examine how to strengthen the independence of accountants, introduction of auditing standards, formulating of methods of civil enforcement, undertaking audits of corporations, in-house enforcement at entities under supervision, taking enforcement steps against accountants and lawyers, regulating the activities of analysts, advancing the activities of the disciplinary committee of portfolio managers, handling profit warnings and introducing changes to Companies Law. In addition, the committee was asked to propose new and additional ideas, to set out priorities to deal with these subjects and to formulate a work plan for each and every subject.

During the report year, the committee dealt with the following subjects:

- **Levying a civil fine - financial sanctions** – passed by the Ministerial Committee at the beginning of 2005.

- **Internal enforcement among entities under supervision** - After a comprehensive internal document was prepared, a discussion with Authority staff was held and it was decided to adopt it, at first for mutual funds and portfolio managers and afterwards for among companies.
- **Accountants' independence** – letters were sent to accounting offices. Most offices replied. There were no significant violations.
- **Measures for arbitration or reconciliation in portfolio management** – complainers and victims usually do not usually claims. Accordingly, the idea was suggested to create a voluntary mechanism that will have quasi arbitration status, and a reference to arbitration will be included in the agreement with the client. Efforts are being made to come to an agreement with the Federation of Portfolio Managers at the Trade Institute.
- **Supervision body over accountants** – A body was set up by the Institute of Certified Public Accountants in Israel to audit other accountants. Irregular findings will be forwarded to the Institute and the Securities Authority.

During the report year, the enforcement committee dedicated most of its efforts and time to prepare a working paper on methods of enforcement alternatives, and towards the end of the year, a summary document was produced. The paper dealt specifically with the methods of enforcement alternatives. The paper was sent for review to the legal advisor of the Government, to his deputies and to the Attorney General. At this stage, the Government's legal advisor has given his support. Upon receipt of all other comments, the year 2005 will be dedicated to preparing a proposed law to update the Securities Law. The proposal will include a system of enforcement alternatives.

Chapter 16 - Special Committees

A. Establishment of a Committee to Formulate a Code of Ethics to Distribute Information through the Internet

In May 2003, the Chairman of the Authority appointed a committee, charged with the responsibility of formulating a code of ethics to for the dissemination of information through the internet, where the possibility of distributing immediate messages exists. Prof. Asa Kasher was appointed chairman of the committee. Members of the committee include: Mr. Eitan Avriel, editor of The Marker.com internet site; Adv. Aviv Eilon; Prof. Shifra Baruchson-Arbiv, of Bar-Ilan University; Dr. Aviva Geva, of Open University; Mr. Menahem Dolinsky, of Bar-Ilan University; Mr. Baruch Hinoch, of Eshnav Foundation; Dr. Na'amah Carmi, of the International Institute for Ethics at Mishkenot Sha'ananim; Dr. Yotam Luria, of Ben-Gurion University; Mr. Ziv Segal, of "Globes" newspaper; and Adv. Haim Ravia.

The committee's letter of appointment states, inter alia, "... during the last few years, together with advances in technology, we have been witness to situations where internet surfers have published misleading information on internet sites that deal with the capital markets. In most cases, the information was published with the intent to encourage other surfers to transact in securities in a manner that the publishers wanted. An investment on the basis of misleading information could cause serious financial damage and could undermine investor trust in the capital markets. Because of this, a need was created to put together rules of conduct, which could deal with the future distribution of information content provided by internet surfers. Possible solutions include, inter alia, legislation, enforcement, and self-restraint while, at the same time, adopting and working within appropriate norms and ethical principles..."

"...We believe that the proper balance between cost and benefit, justifies taking a position of self regulation. The flow of free information is necessary to formulate a correct position, but exact and trusted information is the first condition so that the internet network will be able to serve as a source of information to users. It should be noted that the purpose of formulating an ethical code and self-regulation does not affect the flow of information through the internet. Just the opposite: freedom of expression is a basic right necessary for the existence of a democratic system. However, freedom of expression does not include the right to mislead, to defraud, and to spread misleading information; accordingly, the freedom of expression is not to be used for these purposes and certainly not by the internet network..."

The committee was asked to define "guidelines for proper conduct of the economic information sites of the internet". The letter of appointment stated, "the ethical code is to serve the needs of formulating rules of appropriate behavior, and to set out normative limits for the distribution of information on sites, which have the possibility of distributing immediate messages. These include: forums, talk - back systems, chats, and any other site through which information which could affect the capital markets, can be easily spread."

The committee's work has not yet been completed.

B. Establishment of a Committee to Examine the Aspects of Bonds Issued by Healthcare Services

In January 2004, the Chairman of the Authority and the assistant managing director - sick funds [healthcare services, health maintenance organizations] at the Ministry of Health, Adv. [CPA] Michal Abadi-Boiyanjo, appointed a committee to examine the aspects of debenture issues by the Healthcare Services. Adv. [CPA] Doron Levi was appointed chairman of the committee. Member of the committee include: CPA Tzachi Havusha, in charge of supervision and monitoring of Healthcare Services at the Ministry of Health; Adv. Nathan Somech, legal department at the Ministry of Health; Adv. Lisa Haimovitz, senior advisor to the Chairman of the Authority; Adv. Iris Tzibulsky-Havilio, assistant head of the Authority's Corporation Finance department; Adv. [CPA] Eran Sa'ar, Corporation Finance department of the Authority; CPA Zvika Halamish, senior assistant to the Accountant General of the Ministry of Finance; Mr. Raviv Sobel, coordinator of health services at the Budget Division of the Ministry of Finance; Mr. Ze'ev Varmbrand, managing director of the "Clalit" Healthcare Services; Prof. Yehosua Shemer, managing director of the "Maccabi" Healthcare Services; Adv. Uzi Salant, managing director of "Meuhedet" Healthcare Services; and Mr. Michael Zoller, Chairman of "Leumit" Healthcare Services.

With the expected shift of the sick funds to financial reporting, [in accordance with the recommendation of the committee chaired by Dr. Eyal Sulgenik to regulate the financial reporting by sick funds], with its intrinsic transparency, and to the publication of full financial statements in accordance with Accounting Standard 18 of the Israel Accounting Standards Board in 2005, the Authority and The Ministry of Health became convinced that the time was ripe to examine alternative sources of financing for the sick funds. The committee was asked to suggest models for the issue of securities backed by assets that generate cash flows from health services. This model will include, inter alia, a reference to the national health law, the legal framework appropriate to implement the model, and the fair disclosure requirements according to Securities Law 5728-1968. In addition, the committee was asked to recommend changes necessary in legislation in order to carry out the model.

The committee's work has not yet been completed.

C. The Committee to Examine the Aspects of Issuing Asset-Backed Securities

In January 2004, the Chairman of the Authority and the Income Tax Commissioner Adv. Tal Yaron-Eldar, appointed a joint committee to study the aspects of issuing asset - backed securities. Adv. Lisa Haimovitz, senior advisor to the Chairman of the Authority and Adv. [CPA] Moshe Asher, consultant to the Income Tax Commission on professional matters, serve as committee head. Members of the committee include: Dr. Eyal Sulgenik, head of the Corporation Finance department of the Authority; Adv. Amir Wasserman, legal department of the Authority; Adv. Ronit Shastial, head of the capital markets department - legal department of the Income Tax Commission; CPA Yuval Cohen, manager of the capital markets department - Income Tax Commission; CPA Motti Spiegel, assistant supervisor of banks - Bank of Israel, Mr. Doron Zaken, supervisor of the anti money laundering sector - Bank of Israel; CPA Dov Sapir, chairman of the Israel Accounting Standards Board; Mr. Meir Capota, supervisor of national income; Mr. Avi Gabbai, assistant accountant general at the Ministry of Finance; Adv. Tarek Bashir, senior assistant to the deputy of the government legal advisor [economics and fiscal] - Ministry of Justice; Mrs. Ronit Harel, senior assistant managing director - Tel Aviv Stock Exchange; Mrs. Hani Shitreet, manager of the public issues department - Tel Aviv Stock Exchange; Mrs. Michal Ohana, economist at the capital markets unit - Bank of Israel; Mr. Ran Mor, sector manager – economic and law - projects division - Inbal Company; and Mr. Ophir Levi, assistant to legal counsel in the state income administration.

In the last few years the number of entities in the Israeli economy that have asked to issue debentures backed by various assets such as mortgages, customer accounts, leasing accounts,

assets of local authorities, financial assets in the capital markets, etc., has increased. This type of debenture can be, for these entities, an alternative to outside bank financing, and under certain circumstances, these assets can be taken off the company's balance sheet. An issue of these debentures raises serious legal, accounting, and tax questions, which have to be settled in order to permit the issue of these debentures, and especially those debentures that are registered for trading on the stock exchange.

The committee was asked to propose recommendations on a plan that will permit the issue of debentures backed by assets.

A draft report of the committee's findings was circulated for comment to various parties in the capital markets.

D. Committee to Examine Reporting Requirements for Exposure to Financial Risks and Their Management

In March 2004, the Chairman of the Authority appointed additional committee to examine reporting requirements for exposure to financial risks and management of same. The recommendations of the original committee were submitted to the Securities Authority on September 1, 1999. The Authority adopted its recommendations and incorporated them in regulations. Professor Dan Gallai of the Hebrew University is head of the new committee. Members of the committee include: CPA Ze'ev Abelles, chairman of the Union Bank; Dr. Ephraim Tu'aff – Bank Hapoalim; CPA Eileen Toledano, partner at the accounting firm - Somech Chaikin; Prof. Yitzhak Su'ari - Tel Aviv University and CPA Eran Charninsky – Migdal Insurance Company. The coordinator of the committee is CPA Yuval Mu'alem of – assistant manager of the Corporation Finance department of the Authority. Adv. [CPA] Eran Sa'ar of the Corporation Finance department of the Authority serves as an observer mainly for the legal aspects of the committee's undertakings.

The letter of appointment stated that the experience that has been reaped over time from the passing into law of the original regulations shows that the contribution to the amount and quality of disclosure given by entities is considerable, and that this helped in strengthening the managerial culture of entities in this field. Market risks can affect the stability of entities and the results of their operations, quickly and in the extreme. Because of this, a requirement to report on these risks is especially important, both to the investing public and to the reporting entities.

The first report of the committee recommended establishing, at first, initial requirements of disclosure, this because of a number of reasons, mainly the readiness of public entities for this reporting. The appointment letter stated "...It seems that sufficient time has passed and it is now time to establish qualitative and advanced disclosure principles, which will be based on advanced models of risk management. From the time of publishing the original recommendations, there have been many developments in the field of reporting and measurement on the subject of market risks including - updates of accounting principles acceptable in Israel and the world, and the Basel 2 guidelines which will become effective in the future..."

The work of the committee has not been completed.

E. The Committee to Examine a Code of Corporate Governance [CG] for Israel

In August 2004, the Chairman and Authority appointed a committee to examine a code of corporate governance for Israel. Professors Zohar Goshen, of the Kiryat Ono Academic College is head of the committee. Members of the committee include: Adv. Moshe Gavish, formerly Income Tax Commissioner; Mr. Yitzhak Dvash, chairman of Bondwix Company; CPA Doron Debby, managing partner at the accounting firm - Somech Chaikin; Mrs. Ronit Harel, senior assistant managing director – Tel Aviv Stock Exchange; Adv. Dr. Ya'ir Friedman, partner at the law firm of Sharir-Shevo-Friedman; Prof. Ephraim Zedaka of Tel Aviv University; Mr. Yossi Rosen, who has served in a number of managerial positions with public companies and who at present is chairman of the Israel Electric Company; Adv. Amir Sharf, secretary and legal advisor – El Al Company; CPA Ram Gav of the Corporation Finance department of the Authority and Adv. Yoram Naveh, assistant manager of the Corporation Finance department at the Authority, who also as committee coordinator.

A CG code is a collection of principles, which define how public companies should, act from the standpoint of "best practice". Acceptance of CG has become a standard in economically developed countries, and accordingly it is important as part of the harmonization and globalization of the capital markets.

In the last few years, these codes have been adopted in developed markets of the world, and especially by the OECD. Already in 1999, the OECD adopted a CG code, the purpose of which was to establish goals for OECD member countries for all matters concerning the proper management of companies. In addition, countries such as the United States, England, Holland, Germany, Australia, Turkey and others have adopted a CG code according to OECD guidelines, and in accordance with local laws.

In the letter of the appointment, the committee was asked to recommend a framework and standards [including possible versions] for a CG code for the capital markets in Israel, taking into account codes that have already been adopted by other countries, and especially the OECD code, and to relate, inter alia, to special the characteristics of the capital markets in Israel, to the relevant laws in Israel, and the manner of implementation of the code.

The work of the committee has not been completed.

F. The Advisory Committee to Examine Supervision over Alternative Trading Systems

In August 2004, the Chairman of the Authority appointed an advisory committee to examine supervision over alternative trading systems [ATS]. Prof. Uriel Procatzia is head of the committee. Professor Shmuel Hauser, chief economist of the Authority serves as committee coordinator. Members of the committee include: Prof. Shmuel Kandel of the Management School of Tel Aviv University; Adv. Tida Shamir, member of the board of directors - Israel Bank Discount; Mr. Dror Nagel, manager of the securities and financial assets division - Bank Hapoalim; Dr. Ziv Reich; Adv. Drora Lifshitz, assistant legal counsel – Ministry of Finance; Mr. Nissim Cohen, assistant to the supervisor of capital markets – Ministry of Finance; Adv. Daniella Gorny, general counsel of the Authority; Adv. Eleazer Amir-Himmel, deputy for stock exchange affairs to the general counsel of the Authority; and Adv. Arie Bubis, Corporation Finance department of the Authority.

The letter of appointment stated "...In the era of electronic communications, computerized methods of trading in securities, have contributed to a development of electronic trading sites. These sites have different characteristics. They undertake transactions that apparently are similar to transactions that are carried out by the Tel Aviv Stock Exchange [alternative trading sites]. The development of these trade sites raises serious questions about the need for regulation and supervision, and the type of regulation and supervision needed. A consideration of these issues requires defining and mapping, separately, the types of alternative trading sites, according to their characteristics..."

The committee was asked to relate, inter alia, to the following questions:

1. What are the characteristics of the alternative trading sites in Israel and the world?
2. What are the characteristics of regulation and supervision on these alternative trading sites in the world?
3. Is there a need to regulate and supervise the alternative trading sites in Israel? If so, what is the acceptable form for regulation and supervision of these sites, and on sites operating in Israel but incorporated abroad [and subject to foreign regulation and supervision]?

The work of the committee has not been completed.

Pages 105 – 116, inclusive

Permits to Issue Prospectuses that were Granted During 2004

Annual Budget for 2004

In New Israel Shekels

| Item no. | Item name | Approved budget 2004 | Revised budget 2004 | Actual budget 2004 |
|----------|--|----------------------|----------------------|----------------------|
| | Expenses: Total | 76,285,000.00 | 76,285,000.00 | 74,285,345.76 |
| | Salaries: Total | 40,055,000.00 | 42,488,000.00 | 42,668,125.48 |
| | | [130] | [130] | [130] |
| 100 | Salaries for Authority Employees | 31,000,000.00 | 33,600,000.00 | 33,723,949.86 |
| 101 | Reserve for Pension and Compensation | 5,000,000.00 | 4,950,000.00 | 4,991,629.62 |
| 102 | Overtime | 3,000,000.00 | 2,830,000.00 | 2,870,253.60 |
| 103 | Employees for Temporary Initiatives | 100,000.00 | 165,000.00 | 167,807.88 |
| 104 | Chairman's Salary | 665,000.00 | 665,000.00 | 661,425.83 |
| 107 | Internal Auditing | 130,000.00 | 100,000.00 | 80,813.01 |
| 108 | Payment of Expenses to Authority Members | 80,000.00 | 98,000.00 | 108,336.68 |
| 109 | Preparing Financial Statement | 80,000.00 | 80,000.00 | 63,909.00 |
| | Incidental Expenses: Total | 4,140,000.00 | 4,250,000.00 | 4,309,030.16 |
| 201 | Instruction and Seminars | 600,000.00 | 600,000.00 | 579,838.79 |
| 202 | Automobile Maintenance | 260,000.00 | 335,000.00 | 340,814.71 |
| 203 | Automobile Leasing | 30,000.00 | 40,000.00 | 35,312.60 |
| 204 | Domestic Travel, Lodging and Moving | 3,100,000.00 | 3,125,000.00 | 3,203,064.06 |
| 205 | Loan Fund | 150,000.00 | 150,000.00 | 150,000.00 |
| | Maintenance: Total | 12,910,000.00 | 12,875,000.00 | 12,752,776.87 |
| 301 | Organizational Expenses | 800,000.00 | 815,000.00 | 854,041.19 |
| 302 | Office Supplies | 600,000.00 | 510,000.00 | 493,577.68 |
| 303 | Building Maintenance and Repairs | 10,000,000.00 | 10,000,000.00 | 9,873,694.72 |
| 304 | Mail and Telephones | 750,000.00 | 830,000.00 | 851,906.21 |
| 305 | Equipment, Machinery and Office Furnishings | 60,000.00 | 60,000.00 | 51,969.07 |
| 306 | Automobiles – Payment to Automobile Registry | 670,000.00 | 630,000.00 | 627,588.00 |
| 307 | Changes in Buildings and Installations | 30,000.00 | 30,000.00 | 0.00 |
| | Professional Activities: Total | 3,920,000.00 | 3,830,000.00 | 3,716,536.54 |
| 401 | External Services — Report Examinations | 150,000.00 | 150,000.00 | 15,681.00 |
| 402 | Licensing Investment Counsel and Portfolio | 860,000.00 | 980,000.00 | 981,272.62 |
| 404 | Legal Expenses | 250,000.00 | 30,000.00 | 7,823.91 |
| 405 | Professional Literature | 380,000.00 | 380,000.00 | 374,327.00 |
| 406 | Participation in International Conferences | 180,000.00 | 180,000.00 | 204,553.03 |
| 407 | Accounting Standards (Participation) | 1,500,000.00 | 1,660,000.00 | 1,660,000.00 |
| 408 | Examination of Corporations | 600,000.00 | 450,000.00 | 472,878.98 |
| | Information Systems: Total | 5,830,000.00 | 4,780,000.00 | 4,787,864.28 |
| 501 | Computer Hardware | 120,000.00 | 120,000.00 | 100,026.91 |
| 502 | Computer Software | 180,000.00 | 80,000.00 | 39,083.98 |
| 503 | Computer Maintenance | 4,850,000.00 | 3,950,000.00 | 4,084,691.55 |
| 504 | Purchasing Computerized Information | 680,000.00 | 630,000.00 | 564,061.84 |
| | Development Budget: Total | 7,000,000.00 | 7,000,000.00 | 6,051,012.43 |

Annual Budget for 2004

In New Israel Shekels

| Item no. | Item name | Approved budget 2004 | Revised budget 2004 | Actual budget 2004 |
|----------|--|----------------------|----------------------|----------------------|
| 601 | Information Systems (Software and Hardware) | 7,000,000.00 | 7,000,000.00 | 6,051,012.43 |
| | Reserve: Total | 2,430,000.00 | 1,062,000.00 | 0 |
| 705 | Salary Reserve | 1,200,000.00 | 100,000.00 | 0 |
| 706 | Inflation Reserve | 630,000.00 | 630,000.00 | 0 |
| 710 | General Reserve | 600,000.00 | 332,000.00 | 0 |
| | Income: Total | 77,000,000.00 | 77,000,000.00 | 87,662,509.25 |
| 900 | Income from Prospectus Permit Fees | 9,500,000.00 | 9,500,000.00 | 23,204,358.02 |
| 901 | Annual Registration Fees | 62,000,000.00 | 62,000,000.00 | 54,381,591.59 |
| 902 | Linkage Differentials (Annual Fee) and Interest | 1,500,000.00 | 1,500,000.00 | 4,647,008.64 |
| 903 | Licensing fees for portfolio managers and investment | 4,000,000.00 | 4,000,000.00 | 5,429,551.00 |

Proposed Budget for 2005

In Thousands of New Israel Shekels

| Item no. | Item name | Proposed Budget for 2005 |
|----------|--|-----------------------------|
| | Expenses: Total | 81,640 |
| | | |
| | Salary: Total | 43,640 |
| | | [135] |
| 100 | Salaries for Authority Employees | 34,000 |
| 101 | Reserve for Pension and Compensation | 5,500 |
| 102 | Overtime | 2,900 |
| 103 | Employees for Temporary Initiatives | 100 |
| | | [2] |
| 103/1 | Apprentices | 100 |
| 104 | Chairman's Salary | 690 |
| 107 | Internal Auditing | 140 |
| 108 | Payment of Expenses to Authority Members | 130 |
| 109 | Preparing Financial Statement | 80 |
| | | |
| | Incidental Expenses: Total | 4,270 |
| | | |
| 201 | Instruction and Seminars | 600 |
| 202 | Automobile Maintenance | 330 |
| 203 | Automobile Leasing | 40 |
| 204 | Domestic Travel, Lodging and Moving | 3,100 |
| 205 | Loan Fund | 200 |
| | | |
| | Maintenance: Total | 13,080 |
| | | |
| 301 | Organizational Expenses | 500 |
| 302 | Office Supplies | 600 |
| 303 | Building Maintenance and Repairs | 10,000 |
| 304 | Mail and Telephones | 800 |
| 305 | Equipment, Machinery and Office Furnishings | 80 |
| 306 | Automobiles - Payment to Automobile Registry | 670 |
| 307 | Changes in Buildings and Installations | 30 |
| 308 | International Relations | 200 |
| 309 | Strategic Advice | 200 |
| | | |
| | Professional Activities: Total | 4,400 |
| | | |
| 401 | External Services — Report Examinations | 150 |
| 402 | Licensing Investment Counsel and Portfolio | 900 |
| 404 | Legal Expenses | 250 |
| 405 | Professional Literature | 400 |
| 406 | Participation in International Conferences | 200 |

Proposed Budget for 2005

In Thousands of New Israel Shekels

| Item no. | Item name | Proposed Budget for 2005 |
|----------|--|-----------------------------|
| 407 | Accounting Standards (Participation) | 1,900 |
| 408 | Examination of Corporations | 600 |
| | | |
| | Information Systems: Total | 6,000 |
| | | |
| 501 | Computer Hardware | 120 |
| 502 | Computer Software | 180 |
| 503 | Computer Maintenance | 5,000 |
| 504 | Purchasing Computerized Information | 700 |
| | | |
| | Development Budget: Total | 7,500 |
| | | |
| 601 | Information Systems (Software and Hardware) | 7,500 |
| | | |
| | Reserve: Total | 2,750 |
| | | |
| 705 | Salary Reserve | 1,500 |
| 706 | Inflation Reserve | 650 |
| 710 | General Reserve | 600 |
| | | |
| | Income: Total | 82,500 |
| | | |
| 900 | Income from Prospectus Permit Fees | 10,000 |
| 901 | Annual Registration Fees | 65,000 |
| 902 | Linkage Differentials (Annual Fee) and Interest | 3,000 |
| 903 | Licensing fees for portfolio managers and investment | 4,500 |