

**Oil Refineries Ltd.**



**Condensed Consolidated Interim Financial Statements  
as of 31 March 2009  
(Unaudited)**

This translation of the financial statement is for convenience purposes only. The only binding version of the financial statement is the Hebrew version.

# Oil Refineries Ltd.

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(Unaudited)

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**Directors' Report on the State of the Company's Affairs**  
**for the period ended March 31, 2009**

The board of directors is pleased to present the Directors' Report on the state of the Company's affairs for the period ended March 31, 2009 ("the reporting period").

**1. Description of the Company and its Business Environment**

**1.1 General**

Oil Refineries Ltd. ("the Company" or "ORL") and its subsidiaries are industrial companies involved in three synergetic fields of operations organized in three segments: refinery, petrochemicals and trade. The Company's primary operations are the production of oil products, feedstock for the petrochemical industry and materials for the plastics industry. In addition, the Company is involved in the trading of crude oil and its products and distillates other than for operational purposes, logistics and infrastructure services, and the supply of electricity and steam to neighboring plants. The Company's petrochemicals operations are made up of two operations: aromatics, through Gadiv Petrochemical Industries Ltd. ("Gadiv") (100%) and polymers, through Carmel Olefins Ltd. ("Carmel Olefins") (50%). The plants of these companies are downstream facilities of the Company and they receive the required feedstock entirely or mostly from the Company on an ongoing basis through pipelines and return all or part of products of their facilities to the Company, as well as the feedstock not used in their operations. The Company's refinery operations are integrated with its petrochemical operations.

In the Company's opinion, the integration and synergy between the various fields of operations leads to an increase in aggregate margins flowing to the Company from all of its fields of operation and a reduction in fluctuations of the Company's profits, over time, since business turnover in the areas of the Company's operations and those of its subsidiaries do not necessarily overlap. In addition, the joint management of the Company and Gadiv streamlines the operations of the companies and reduces expenses.

The Company, Carmel Olefins and Gadiv have no significant dependency on customers or suppliers, except for the dependency of the subsidiaries on the supply of feedstocks from the Company. The Company has an operating dependency on government companies – Petroleum and Energy Infrastructures Ltd. ("PEI") and Eilat Ashkelon Pipeline Company Ltd. ("EAPC") which provide it with crude oil transportation services at terminals and in pipelines. The Company has holdings in other companies, each which are not on a scope that is material for the Company.

The Company's strategic plan, which was launched in September 2007 in a scope of \$1.1 billion, focuses on achieving growth and increasing in the competitive capacity of the Company in the coming years, as well as expanding the share of high added-value products in the Company's product mix and emphasizing environmental quality. The blueprint of the strategic plan includes the following: (1) accelerated investments in refining, mainly in increasing the complexity and efficiency of the refinery and in synergetic areas. The investment is estimated at \$850 million, of which \$600 million is for the expansion of the cracking capacity of oil products with high added value; (2) identification of business opportunities relating to refineries and petrochemicals in Israel and abroad; (3) expansion of petrochemical operations, by focusing on high added-value products, in Israel and abroad; (4) expansion of trade and logistics operations for oil products; (5) investment of an estimated \$270 million in environmental quality, safety and security and in enhancing operational reliability; (6) reorganization, with a division into three segments: refining, trade and petrochemicals.

**1.2 Business environment and Company profitability**

The refining margin is the major factor affecting the results of operations in the refining segment. This margin is the difference between the revenue from the sale of the basket of products sold by the Company and the ex-refinery cost of the raw materials purchased by the Company (mainly crude oil). The level of the margin is based on the index of the products and their prices in the reporting period, compared to the composition of the crude oil index and its prices in the same period, depending on different market forces.

Global prices of crude oil and distillates are highly volatile and are set, inter alia, by global supply and demand. Prices are also affected by geopolitical events which are not directly connected to oil

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production, but which are viewed by the markets as having a potential impact on future production. The level of the refining margin is a result of the market forces active on two different planes: one, supply and demand of crude oil and the other, supply and demand of end products.

The factors affecting the supply and demand of crude oil and oil products, as described above, generate fluctuations and seasonality in the profitability level of the refining industry.

In the reporting period, the average price of crude oil and its distillates was \$45/barrel compared to an average of \$97/ton in the corresponding period last year, and compared to \$37/barrel on December 31, 2008. Concurrently, there was also a decrease in the prices of oil products that the Company produces from crude oil and sells.

Accordingly, the accounting results of the Company's operations and refining margins were primarily affected by: (1) a loss of \$36 million due to timing differences between purchase and selling prices and unhedged basic inventory of 600,000 tons, for which changes its value do not generate cash flow exposure for the Company; (2) net profit of \$86 million due to the provision of \$183 million for impairment of the Company's inventory made at the end of 2008, following the decrease in prices at the end of 2008, offset by the actual loss of \$97 million from the sale of this inventory; (3) the effect of changes in fair value of derivatives on prices of goods, due to the transition to international financial reporting standards (IFRS) in the amount of \$0.2 million (profit).

In the refining segment, operating profit, EBITDA and the refining margin after neutralizing these three impacts is \$22 million, \$32 million and \$32.4 per ton, respectively.

The operating loss, EBITDA and refining margin, as reflected in the financial statements (without neutralizing these impacts) is \$72 million, \$82 million and \$56.9 per ton, respectively.

In the reporting period, neutralized refining margins increased to \$32.4 per ton, compared to \$17.7 per ton in the corresponding period last year. The margins publicized by Reuters for an example of a Mediterranean refinery having the capability of cracking Ural-type crude oil (Reuters margin), amounted to \$24.8 per ton in the reporting period compared to \$27.1 per ton in the corresponding period last year. See section 3.1.2 for further information.

It is noted that there are differences in a number of parameters between the refining margin of the Company and the Reuters margin. These include the composition of the crude oil (the Company also refines crude oil types that are not Ural), the composition and quality of the products produced by the refineries and the difference generated as result of the fact that the quote takes into account purchase and sale on the same day, while in practice, there is a gap between the purchase date of the crude and the selling date of distillates produced from the crude oil. Accordingly, the comparison to the Reuters' margin is likely to provide insight in relation to the trends of the development of the Company's refining margin, and does not constitute an exact criterion for estimating the Company's refining margin in the short term.

The following table summarizes the comparison of the refining margins with the refining margin in the Mediterranean.

	<u>31.3.2009</u>	<u>31.3.2008</u>	<u>3.12.2008</u>
<b>Ural margin in the Mediterranean (dollar/barrel)</b>	<u>3.4</u>	<u>3.7</u>	<u>5.5</u>
<b>Neutralized margin (dollar/barrel)</b>	<u>4.4</u>	<u>2.4</u>	<u>5.7</u>
<b>Neutralized margin (dollar/ton)</b>	<b>32.4</b>	<b>17.7</b>	<b>41.4</b>
Neutralization of the impact of the accounting method for derivatives according to IFRS	(0.1)	(5.9)	0.7
Buying and selling timing differences	(18.1)	15.3	(9.9)
Provision for impairment of inventory as of the balance sheet date	<u>42.7</u>	<u>-</u>	<u>(22.3)</u>
<b>Accounting margin (dollar/ton)</b>	<u><b>56.9</b></u>	<u><b>27.1</b></u>	<u><b>9.9</b></u>

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Consolidated operating profit amounted to \$80 million in the reporting period, compared to operating profit of \$16 million in the corresponding period last year, an increase of \$64 million.

The following table presents a description of the main reasons for the changes in consolidated operating profit in the period (in USD million).

	<b>1-3.2009 compared to 1-3.2008</b>
Increase in sales turnover	2
Decrease in other revenue	(9)
Decrease in profit from the trade segment	(2)
Decrease in losses for derivative transactions	12
Provision for impairment of inventory	86
Buying and selling timing differences – in the refining segment	(66)
Decrease in margins and buying and selling timing differences – in the petrochemicals segment	(10)
Increase in margins in the refining segment	29
Decrease in production expenses, mainly energy	18
Increase in selling and administrative expenses	4
	64

Consolidated EBITDA amounted to a profit of \$98 million in the reporting period, compared to a profit of \$34 million in the corresponding period last year, an increase of \$64 million.

For further details on the results of operations, including a breakdown by segment, see section 3.

### Production volumes

The refining volume in the Company amounted to 1,967,000 metric tons (in 2008 – 8,245,000 metric tons) with usage of 88.7%.

The following table presents the breakdown of the Company's output (ORL) by the main product groups in the refinery segment (in thousands of tons).

	<b>1-3.2009</b>	<b>1-3.2008</b>	<b>2008</b>
Diesel fuel	634	584	2,367
Gasoline	365	423	1,664
Kerosene	151	169	831
Fuel oil	330	338	1,367
Vacuum diesel	198	173	738
Others	133	159	624
Total	1,811	1,846	7,591

The following table presents the breakdown of the output of the consolidated companies (in thousands of tons).

	<b>1-3.2009</b>	<b>1-3.2008</b>	<b>2008</b>
Gadiv Petrochemical Industries Ltd.	109	129	430
Carmel Olefins Ltd. (the Company's share – 50%)	81	67	307

### **1.3 Summary of Company developments during and subsequent to the reporting year**

#### **1.3.1 Corporate developments**

##### **1.3.1.1. Strategic plan**

On October 12, 2008 the Company's board of directors decided, as part of the strategic plan it adopted in November 2007, to establish a hydrocracker in the Haifa refinery. The hydrocracker, which is expected to be operational at the end of 2011-beginning of 2012, will produce middle distillates (diesel oil and kerosene), following an investment of \$670 million (including an investment of \$37 million approved by the board of directors in November 2007 to advance the project). Upon activation, the hydrocracker will allow production of higher added-value products with each barrel of oil, substantially increasing the complexity of the Haifa refinery. In addition, the plant will increase the flexibility of the refinery in terms of ability to select the raw materials and product mix, adapting them to the changing markets.

The Company's board of directors instructed management to complete the long-term credit arrangements to finance the project. Accordingly, the Company is taking steps to complete arrangements for the credit facility through Export Credit Agency to finance the purchase of equipment from foreign suppliers, and to receive the additional long-term credit from various sources, which is vital for completion of the project. It is noted that the Company raised part of the sum required to finance the strategic plan in December 2007, pursuant to a prospectus published by the Company on November 28, 2007.

In view of the global economic crisis, the board of directors of the Company gave instructions to reduce the cost of the hydrocracker. The board of directors also asked to reassess the balance of financial investments.

Planning of the first stage (feed) was completed in the reporting period. As of the date of the report, the Company is in the advanced stages of negotiations with major equipment suppliers for final proposals and formation of a financing package for the project is underway, for presentation to the board of directors.

As of the approval date of the financial statements, the Company has no financial liabilities for the purchase of fixed assets that are not covered by secured financial financing.

##### **1.3.1.2. Implementation of the strategic plan by segment**

- 1. Refining:** In 2008, organization and staffing the segment was completed. An internal compliance plan was adopted for environmental quality, health and safety. In addition, the following investments are made as part of the strategic plan:
  - A.** Increased flexibility of refining at crude refining terminal 4 is in process. Operation is expected to be renewed after shutdown for renovation in the third quarter of 2009. The upgrade will allow refining of a very wide range of crude oil types common in the region, such that utilization of the plant will increase and it will be possible to take advantage of more opportunities of good margins
  - B.** Conversion of the desulfurization facility from heavy vacuum gas oil (HVGO) to moderate catalytic hydrosulfurization is in process. Stage A is being conducted in the second quarter of 2009 and stage B will be conducted in the third quarter of 2010. Operation of stage A is expected to produce an additional 1.5% of diesel fuel for refining output. Stage B

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is expected to produce a similar additional output. The Company is acting to advance the implementation of stage B.

- C. See section 3.1.1 above for establishment of the hydrocracker.
- D. Projects related to environmental quality in the scope of \$50 million were implemented in 2008.
- E. Establishment of a power station: The configuration testing stage has been completed.

2. **Trade:** In 2008, a modern commercial center was established and the information system for managing trade in oil products was implemented.

### **3. Petrochemicals**

- A. Agreement for the purchase of the remaining Carmel Olefins shares

On June 24, 2008, the Company signed an agreement with Israel Petrochemical Enterprises Ltd. (IPE) for the acquisition of the remaining 50% of Carmel Olefins shares in return for the allotment of 20.53% of the Company's shares (after the allotment). This transaction is part of the Company's business strategy, which aims, inter alia, to realize the full synergy potential in the refinery, polymers and aromatics segments. It was also agreed that the Company would sell IPE all of the Company's shares in IPE ("the acquired IPE shares"), representing 12.29% of the share capital of IPE, in consideration for \$40 million.

On December 31, 2008, the agreement for the purchase of Carmel Olefins expired, without the fulfillment of all the preconditions defined in the agreement and therefore the transaction was not completed.

However, as the main reasons underlying the decision of the board of directors to approve the merger of Carmel Olefins with the Company are still valid today, the Company and IPE agreed to continue to cooperate in an attempt to complete the merger, and if the conditions ripen, the issue will be brought to the organs of the Company.

- B. Increased production capacity of paraxylene and benzene: completion is expected in the fourth quarter of 2009.
- C. Increased production capacity of phthalic anhydride is expected in the fourth quarter of 2009.

#### **D. Acquisition of a company by Carmel Olefins**

On April 25, 2008, Carmel Olefins acquired, through Colland Polymers B.V. ("Colland"), Domo Chemicals N.V. ("Domo") pursuant to an agreement entered into on January 23, 2008. Colland is a wholly-owned subsidiary of Carmel Olefins. Domo is a petrochemical company incorporated in the Netherlands that manufactures and markets polypropylene used as raw material in the plastics industry for a range of uses and products.

The main terms of the agreement are as follows: Carmel Olefins purchased 49% of the shares of Domo for €20 million. In addition, commencing from 2013, the shareholders of Domo who sold Carmel Olefins the Company's shares ("the sellers") could be entitled to additional compensation, not to exceed an amount of €1 million a year for a five-year period, in accordance with the terms set out in the agreement. Carmel Olefins, through Colland, has a call option from the

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purchase date until December 31, 2016, for the purchase of the balance of the shares for an additional €10 million, net of the dividends to be distributed to Domo, plus interest at a rate of 5% per annum. The sellers have a put option, exercisable commencing on July 1, 2011 for the sale of the remaining 51% in Domo to Carmel Olefins at the same terms.

Commencing May 1, 2008 Carmel Olefins fully consolidates Domo results due to the options, and the minority interests for the shareholders' balance in Domo are not included.

### **E. TMA project**

On September 25, 2007, Gadiv signed a memorandum of intent ("the memorandum of intent") for the purchase of 50% of the registered share capital of a Chinese company ("the acquired company") which benefits in China from the status of a wholly-foreign owed company (WFOE) and which will manufacture Trimellitic Anhydride (TMA), a product used mainly as a softener in the polymer industry and as a component in powder colors, and Para Diethyl Benzene (PDEB), a product used mainly in the production of paraxylene.

On November 25, 2007 the validity of the memorandum of understanding expired, and the negotiations conducted by the Company on this matter ended without the parties reaching the required agreements for consummation of a binding transaction. At the reporting date, the parties are in the advanced stages of negotiations.

### **4. Company headquarters**

- A.** The Company is examining ways to take advantage of business opportunities outside of Israel, primarily in Mediterranean countries.
- B.** In 2008, internal enforcement plans for antitrust issues, securities laws and environmental quality and safety issues were adopted and assimilated.

### **5. Environmental quality**

Alongside the implementation of environmental, reliability and safety projects in the scope of \$50 million in 2008, out of the comprehensive investment plan in these issues, which was included in the strategic plan, and the assimilation of an internal compliance plan for environmental quality and safety, the Company invested effort to raise public awareness of its activity in these areas. This included the investment of great effort in contact with representatives of green organizations and the media, and in deepening their knowledge of the Company's plants, presentation of environmental activities and the planned investments in the subject.

See section 15 below for details of the hearing held for the Company in respect of the personal order under which it operates.

#### **1.3.1.3. The Company's preparation for 2009 and organizational changes**

As part of the 2009 work plan, which was approved by the board of directors, the Company is implementing efficiency measures in a number of areas, including production, logistics, purchasing, contractual work and human resources, with the aim of ensuring the realization of its strategic plan and its long-term strength and prosperity, against the background of the global economic crisis and its implications on the Israeli economy.

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As part of these measures, there were organizational changes at the beginning of 2009, which included incorporation of the activities of the business development unit into other units in the Company. In this context, the Company's vice president for business development and capital market ended his employment at the Company. In addition, the Company appointed a vice president for administration and human resource development.

1. In this context, the chairman of the board, CEO and other officers in the Company have announced their intention to take a 10% reduction on the salary due to them in 2009 (with the exception of provisions and incidental conditions).
2. In addition, the Company's directors, including the outside directors, announced their intention to take a 10% reduction on the directors' remuneration due to them in 2009.
3. On January 6, 2009, CFO Jacob Hirsh announced his resignation. Igal Salhov, who had served as CFO at Carmel Olefins (held 50% by the Company) until this date, was appointed in his place.

Subsequent to the reporting period, a special collective agreement was signed between the Company and the workers union. Under the agreement, in 2009 only, the Company's employees will not receive certain payments due to them under the special collective agreements between the Company and its employees. However, if the Company presents a net profit, after deducting taxes, in its financial statements for 2009, each employee shall be paid, in the month after publication of the financial statements, the amounts that were not paid in 2009, provided this payment, had it been made in 2009, would not have resulted in a net loss after taxes in 2009.

### **1.3.2 Developments in the economic environment and in financial markets and their impact on the Company**

In the first quarter of 2009, oil prices rose from \$37/ton at the end of 2008 to \$50/ton at the end of the quarter, after great fluctuation in the price of crude oil and its products in 2008, which was \$90/barrel at the beginning of 2008, rose to \$140/barrel in the middle of the year and fell to \$37/barrel as aforesaid.

In the reporting period, compared with the corresponding period last year, there was also a decrease in the prices of fuel products produced by the Company from crude oil and sold by the Company. There was no full correlation between the dates of the changes in product prices and the scope of these changes and the dates of the changes in the prices of crude oil and the scope of changes, which resulted in fluctuation in the refining margin.

A rise in the price of crude oil leads to an increase in the volume of working capital required by the Company to finance its purchases and to an increase in the inventory value in the Company's books. On the other hand, a drop in the price of crude oil leads to a reduction in the volume of working capital required by the Company to finance its operations and an impairment of inventory in the Company's books. The Company's exposure to changes in the price of crude oil is hedged in the futures and derivatives markets.

The increase in the price of crude oil and its products in the reporting period has a material impact on the first quarter results, as described in the section below describing the main factors for the increase in gross profit. It is noted that the Company does not hedge against the basic inventory value of 600,000 ton. Change in the inventory value has no economical and cash flow impact, therefore, the Company reports its operating results after removing these effects and other effects in respect of changes in the value of derivatives in accordance with IFRS.

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In the first quarter of 2009, there was significant fluctuation in the dollar-shekel exchange rate. Although the Company's functional currency is the dollar, the Company has assets and liabilities denominated in the shekel (mainly due to salaries, payments to suppliers and subcontractors in Israel and payments to institutions and authorities. From the beginning of 2009 and until the end of the first quarter, there was a depreciation of 10%. The impact of the change in exchange rates on the business results in the reporting period amounts to an expense of \$6 million

In the reporting period, the CPI fell by 0.1%. The Company finances its operations, inter alia, through a public placement of CPI-linked debentures. To reduce the Company's exposure to changes in the rate of inflation, the Company entered into a currency swap, converting most of its long-term index-linked shekel debentures into dollar loans (see section 6.1.8 below). Parallel to the Company's index-linked liabilities for which there were no currency swap transactions, the Company holds assets linked to this index.

As a result of the crisis in the financial markets in the first quarter, the fair value of the financial derivatives held by the Company decreased by \$31 million, which was recognized in the Company's financing expenses.

In view of the crisis in the financial markets and in order to reduce the exposure to financial assets, at the end of the first quarter, the Company decided to update its investment policy to further reduce the risks in most of the components of the investment portfolio.

See section 16 below for the implications of the changes in the financial markets subsequent to the balance sheet date and the implications of the economic crisis on the Company's financial position.

## **2. Financial position**

### **2.1 Current assets**

On March 31, 2009, consolidated current assets amounted to \$1,253 million, representing 49% of the total assets, compared to \$1,104 million, representing 46% of total assets on December 31, 2008. The change in current assets is mainly due to an increase of \$148 million in the inventory balance in the Group, mainly due to an increase in quantity, reduction in trade receivables (after offsetting the discount of \$91 million on March 31, 2009 and \$108 million at December 31, 2008), of \$17 million, and an increase of \$39 million in deposits for derivatives. This was due to an increase in inventory prices and an increase in the volume of transactions following an increase in the volume of inventory.

### **2.2 Investments and long-term loans**

At March 31, 2009, investments and long-term loans amounted to \$140 million, representing 6% of the assets, compared to \$193 million, representing 8% of the assets at December 31, 2008. The increase is mainly due to a decrease of \$37 million in financial derivatives in the reporting period, mainly due to the impact of the depreciation on the fair value of derivatives for hedging on debentures, offset by the impact of the change in interest and the impairment of the value of the investment in Haifa Early Pensions of \$14 million, due to the impact of the depreciation offset by the increase in fair value and due to the increase in current maturities for the loans fund and the interest of \$11 million recognized in other payables.

### **2.3 Current liabilities**

Consolidated current liabilities at March 31, 2009 amounted to \$884 million, representing 46% of total liabilities, compared to \$737 million, representing 40% of total liabilities at December 31, 2008. The increase is mainly due to the increase in trade payables of \$56 million, mainly owing to an increase in the amount of inventory and an increase in prices, as well as an increase in credit of \$96 million, which is mainly due to an increase in short-term credit of \$29 million taken by Carmel Olefins and credit in the Company due to an increase in the price of inventory and the amount of inventory of \$72 million, offset by a decrease in current maturities.

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### **2.4 Long term financial liabilities**

Consolidated long-term liabilities amounted to \$860 million at March 31, 2009, compared to \$960 million at December 31, 2008. The decrease of \$100 million is due to repayment of loans and debentures and the erosion of shekel debentures due to the depreciation in the reporting period.

### **2.5 Shareholders' equity**

Equity at March 31, 2009 amounted to \$622 million, representing 25% of the balance sheet, compared to \$552 million, representing 23% of the balance sheet at December 31, 2008. The increase in equity is mainly due to the profit of \$74 million in the reporting period.

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**3. Results of the Group's operations**

**3.1 The following tables present selected information compared to last year**

	Refining		Trade		Petrochemicals				Adjustments to consolidated		Consolidated	
					Polymers		Aromatics					
	31.3.2009	31.3.2008	31.3.2009	31.3.2008	31.3.2009	31.3.2008	31.3.2009	31.3.2008	31.3.2009	31.3.2008	31.3.2009	31.3.2008
	<b>Three months ended</b>											
Revenue	784	1,562	58	79	84	108	58	137	-	-	984	1,886
Inter-company operations	86	186	-	-	-	-	9	12	(95)	(198)	-	-
<b>Total sales</b>	<b>870</b>	<b>1,748</b>	<b>58</b>	<b>79</b>	<b>84</b>	<b>108</b>	<b>67</b>	<b>149</b>	<b>(95)</b>	<b>(198)</b>	<b>984</b>	<b>1,886</b>
Cost of sales	778	1,717	57	77	50	34	(3)	16	-	-	882	1,844
Inter-company operations	9	12	-	-	27	68	58	117	(94)	(197)	-	-
<b>Total cost of sales</b>	<b>787</b>	<b>1,729</b>	<b>57</b>	<b>77</b>	<b>77</b>	<b>102</b>	<b>55</b>	<b>133</b>	<b>(94)</b>	<b>(197)</b>	<b>882</b>	<b>1,844</b>
<b>Gross profit (loss)</b>	<b>83</b>	<b>19</b>	<b>1</b>	<b>2</b>	<b>7</b>	<b>6</b>	<b>12</b>	<b>16</b>	<b>(1)</b>	<b>(1)</b>	<b>102</b>	<b>42</b>
Selling, general and administrative expenses	11	14	1	-	4	5	6	7	-	-	22	26
Inter-company operations	-	-	-	-	1	1	-	-	(1)	(1)	-	-
<b>Operating profit</b>	<b>72</b>	<b>5</b>	<b>-</b>	<b>2</b>	<b>2</b>	<b>-</b>	<b>6</b>	<b>9</b>	<b>-</b>	<b>-</b>	<b>80</b>	<b>16</b>
Financing income (expenses)											14	(17)
Share in the profit (loss) of investees											5	(5)
Profit (loss) before taxes on income											99	(6)
Tax benefits (income tax)											(24)	8
<b>Net profit</b>											<b>75</b>	<b>2</b>

### 3.1.1 Sales turnover

The sales turnover of the **refining segment** (carried out through the Company) amounted to \$870 million in the reporting period, compared to \$1,748 million in the corresponding period last year. The decrease in sales turnover was mainly due to the decrease in the average price of oil products. The average price per ton of the product index in the Mediterranean area, similar to the product index produced by the Company (the Company's product index) amounted, to \$385 in the reporting period, compared to \$795 in the corresponding period last year.

Revenues from the sale of products with a volume of over \$125 million in the reporting period were as follows: gasoline - \$176 million and diesel fuel - \$285 million.

According to publications of the Ministry of National Infrastructures, there was a decrease of 11% in consumption of distillates in the local market compared to the corresponding period last year, which included an increase of 1% in the consumption of gasoline for transportation offset by a decrease of 7% in diesel oil, mainly due to an increase in gasoline-powered vehicles and the slump in operations in the economy. Additionally, there was a decrease of 15% in the consumption of fuel oil compared to the corresponding period last year, due to the conversion of the Israel Electric Corporation's power station to production of electricity using natural gas.

Sales turnover in the **trade segment**, which commenced operations in the corresponding period last year and is carried out through the Company, amounted to \$58 million, compared to \$79 million in the corresponding period last year.

Sales turnover in the petrochemical segment

Sales turnover of **polymer operations** (carried out through Carmel Olefins) decreased by \$24 million in the reporting period compared to the turnover in the corresponding period last year. The decrease is mainly due to a decrease in selling prices of \$62 million, which was offset by an increase in the sales quantities of \$38 million, due to the sale of Domo which was consolidated for the first time commencing from May 1, 2008 for products produced by Carmel Olefins.

Sales turnover of **aromatics operations** (carried out through Gadiv) decreased by \$82 million in the reporting period compared to turnover in the corresponding period last year. The decrease is mainly due to the decrease in selling prices of \$50 million, a decrease in quantities of \$30 million and a decrease in processing fees of \$2 million.

### 3.1.2 Gross profit

The following table presents a description of the main reasons for the increase in gross profit in the **refining and trade segments** in the reporting period, compared to the corresponding period last year (in USD millions):

	<b>31.3.2009 compared to 31.3.2008</b>
Decrease in other revenue	(6)
Decrease in profit from the trade segment	(2)
Increase in profits for derivatives	12
Provision for impairment of inventory	86
Buying and selling timing differences	(66)
Increase in neutralized margin from refining operations	29
Decrease in production expenses	10
	<u>63</u>

The margin from refining operations is the difference between the revenue from sales of the products that the Company sells and the cost of raw materials that it purchases, ex-

refinery (dollars per ton). The cost of raw materials includes the hedging transactions for the inventory of crude oil and distillates, as described below in the section referring to risk management.

The following table describes the Company's refining margins, offset by the impact of impairment of inventory, buying and selling timing differences and recording of derivatives in accordance with IFRS in UDS/ton.

Q1		Year
2009	2008	2008
32.4	17.7	41.4

In the first quarter of 2009, crude oil prices rose from \$37/ton at the beginning of the quarter to \$50/ton at the end of the quarter, while in 2008 there was extreme volatility in the fuel markets in Israel and worldwide. In 2008 oil prices rose from \$90/barrel to \$140/barrel in the second half of 2008, and fell to \$37/barrel at the end of the year. At the end of the first quarter of 2009, refining margins dropped compared to the end of 2008, due to the relative price increase of oil and the end of the winter.

The decrease in other revenue was due to the decrease in the sale of energy and water utilities in the reporting period compared to the corresponding period last year, which was largely caused by the decrease in the selling prices.

The decrease of \$10 million in production expenses in the reporting year compared to the corresponding period last year was mainly due to the impact of the depreciation on shekel expenses, mainly payroll, during the period, a decrease in maintenance expenses for facilities due to the postponement of planned maintenance works and a decrease of periodic maintenance.

Gross profit in **polymers operations** amounted to \$7 million in the reporting period, compared to gross profit of \$6 million in the corresponding period last year.

The following table presents a description of the main reasons for the increase in gross profit (in USD millions).

	<b>31.3.2009 compared to 31.3.2008</b>
Increase in sales turnover	7
Decrease in products index margin and buying and selling timing differences	(8)
Decrease in production and other expenses	2
	<u>1</u>

Gross profit in **aromatics operations** amounted to \$12 million in the reporting period, compared to \$16 million in the corresponding period last year.

The following table presents a description of the main reasons for the decrease in gross profit (in USD millions).

	<b>31.3.2009 compared to 31.3.2008</b>
Decrease in sales quantities	(5)
Decrease in processing fees	(3)
Decrease in products index margin	(3)
*Decrease in production expenses, in particular energy	7
	<u>(4)</u>

### 3.1.3 Selling, general and administrative expenses

Selling, general and administrative expenses include mainly payroll, insurance, taxes and authorization fees.

In the reporting period, consolidated selling, general and administrative expenses amounted to \$22 million, compared to \$26 million the corresponding period last year. The decrease in expenses was mainly due to the decrease in salary expenses as a result of the impact of the depreciation on payroll expenses.

### 3.1.4 Operating profit and EBIDTA (earnings before interest, taxes, depreciation and amortization)

#### Refining and trade segment

The neutralized operating profit in the refining and trade segments amounted to \$23 million in the reporting period, compared to a loss of \$12 million in the corresponding period last year.

The accounting operating loss in the refining and trade segments amounted to \$72 million in the reporting period, compared to a profit of \$7 million in the corresponding period last year. The changes in the accounting operating profit of \$65 million is due to the increase of \$63 million in gross profit as explained above, and a decrease of \$2 million in selling and administrative expenses as described above.

Neutralized EBITDA of the refining and trade segment amounted to \$32 million in the reporting period, compared to a loss of \$2 million in the corresponding period last year, an increase of \$34 million.

Accounting EBITDA amounted to \$82 million in the reporting period, compared to EBITDA of \$17 million in the corresponding period last year, an increase of \$65 million.

#### Petrochemicals segment

Operating profit in the **polymers operations** amounted to \$2 million in the reporting period, compared to a balance in the corresponding period last year. The increase is due to an increase of \$1 million in gross profit, as described above, and a decrease of \$1 million in selling, administrative and general expenses.

EBITDA of the **polymers operations** amounted to \$9 million in the reporting period, compared to \$6 million in the corresponding period last year.

Operating profit of **aromatics operations** amounted to \$6 million in the reporting period, compared to operating profit of \$9 million in the corresponding quarter last year, a decrease of \$3 million.

EBITDA of the **aromatics operations** amounted to \$7 million in the reporting period, compared to \$11 million in the corresponding period last year.

The consolidated accounting operating profit amounted to \$80 million in the reporting period, compared to a profit of \$16 million in the corresponding period last year.

Consolidated accounting EBITDA amounted to \$98 million in the reporting period, compared to \$34 million in the corresponding period last year.

### 3.1.5 Financing expenses

Net consolidated financing income amounted to \$14 million in the reporting period compared to expenses of \$17 million in the corresponding period last year.

The following table presents details of the principal changes in financing expenses (in USD millions).

	<b>31.3.2009 compared to 31.3.2008</b>
Impact of the changes in fair value of derivatives on debentures	1
Decrease in cost of short-term credit mainly due to a decrease in the volume and the decrease in the interest rate	4
Decrease in interest expenses on debentures and long-term loans mainly due to a decrease in the volume of debentures and loans offset by a decrease in the interest rate	8
Impact of the depreciation on financial items, net	13
Increase in the value of the securities portfolio and loans to Haifa Early Pensions including the impact of the depreciation	5
	<b>31</b>

### **3.1.6 Income tax**

In the reporting period, tax expenses in the Group amounted to \$24 million, due to changes in deferred tax reserves resulting from the impact of the depreciation.

### **3.1.7 Company's share in earnings of investees**

The Company's share in the earnings of investees amounted to a profit of \$4.5 million in the reporting period, compared to a loss of \$5 million in the corresponding period last year.

## **4. Liquidity**

Total current assets less current liabilities as of March 31, 2009 amounted to \$369 million compared to \$367 million as of December 31, 2008. The current ratio as of March 31, 2009 is 1.4 compared to 1.5 on December 31, 2008.

Consolidated cash flows from operating activities in the reporting period amounted to \$30 million, mainly due to the accounting profit less adjustments of non-cash activities and an increase in current assets and liabilities, as a result of the increase in the prices of crude oil and its products in the reporting period.

Cash flows used in investment activity in the reporting period amounted to \$83 million, used mainly to finance investments in property, plant and equipment and for investment in a deposit for derivatives on inventory.

Net cash flows from finance activity amounted to \$51 million in the reporting period, mainly from short-term credit received in the amount of \$101 million less repayment of debentures and long-term loans of \$30 million, \$12 million in interest paid, and a decrease in deposits received from customers of \$9 million.

The total cash flows from operating activities less cash used for financing and investment operations led to a decrease of \$2 million in cash balances in the reporting period.

## 5. Sources of financing

Composition of the Group's sources of financing

	<u>31.3.2009</u>	<u>31.12.2008</u>
	<u>(Unaudited)</u>	<u>Audited</u>
	<u>USD millions</u>	
<b>Sources</b>		
Decrease in cash flow in the period	2	246
Cash from operating activities (prior to changes in working capital)	92	-
Receipt of short-term credit and deposits from customers	94	129
Decrease in working capital, net	-	307
	<u>188</u>	<u>682</u>
<b>Uses</b>		
Cash used for operating activities (prior to changes in working capital)	-	162
Increase in working capital, net	66	-
Payment of dividend	-	121
Investments in fixed and other assets	55	142
Investment in deposit	37	-
Investment in associates, in negotiable securities	-	40
Repayment of long term loans and debentures	30	217
	<u>188</u>	<u>682</u>

### Long-term loans and debentures

The long term loans and debentures as of March 31, 2009 (after deduction of current maturities) amounted to \$860 million, representing 34% of the balance sheet, compared to \$960 million, representing 40% of the balance sheet at December 31, 2008. The proceeds of the loans are used to finance investments in property, plant and equipment and to finance working capital. Financial leverage (long term loans and debentures for shareholders' equity plus long term loans and debentures) is 58% of the balance sheet at March 31, 2009, compared to 64% at December 31, 2008.

### Total financial liabilities

Current financial liabilities plus long-term loans and debentures amounted to \$1,337 million at March 31, 2009, representing 53% of the balance sheet compared to \$1,340 million, representing 56% of the balance sheet at December 31, 2008. Financial leverage of total financial liabilities to banks and other credit providers is 68% compared to 71% at December 31, 2008.

Long-term financial debt (long-term loans and debentures, including current maturities) amounted to \$990 million in the reporting period: in the Company \$865 million (including \$115 million in current maturities); in Carmel Olefins \$122 million (including \$14 million in current maturities); and in Gadiv \$3 million.

### Average volume of sources of finance in the reporting period

Long term loans (including current maturities) – \$1,041 million; short term credit – \$297 million; trade payables – \$298 million; trade receivables – \$246 million.

## 6. Exposure to market risk and risk management methods

In the reporting period, the risk management policy of the Company and its subsidiaries and the organs responsible for risk management were the same as those set forth in the Directors' Report of December 31, 2008.

### 6.1 Sensitivity analysis of the Company's exposure to market risks

#### 6.1.1 Summary of the differences in fair value in view of the sensitivity analysis of the dollar-shekel exchange rate

	Profit (loss)		Fair value 31.03.2009	Profit (loss)	
	Increase of			Decrease of	
	+10%	+5%		-5%	-10%
<b>Exchange rate fluctuations</b>	<b>4.6068</b>	<b>4.397</b>	<b>4.188</b>	<b>3.979</b>	<b>3.769</b>
USD thousands					
Long-term linked shekel debentures	41,648	21,816	(458,133)	(24,112)	(50,904)
Long-term shekel debentures	11,609	6,081	(127,700)	(6,721)	(14,189)
Trade receivables(NIS)	(9,220)	(4,830)	101,424	5,338	11,269
Trade payables (NIS)	6,522	3,416	(71,742)	(3,776)	(7,971)
Inventory balance (NIS) (*)	(2,800)	(1,467)	30,800	1,621	3,422
Securities (NIS)	(7,639)	(4,001)	84,029	4,423	9,337
Forward contracts	4,862	2,547	(90)	(2,815)	(5,943)
Swapping principal and interest	(48,041)	(25,165)	18,581	27,813	58,717
	<u>(3,059)</u>	<u>(1,603)</u>		<u>1,771</u>	<u>3,738</u>

\* Inventory denominated in NIS

#### 6.1.2 Summary of the differences in fair value in view of the sensitivity analysis of the euro-dollar exchange rate

	Profit (loss)		Fair value 31.03.2009	Profit (loss)	
	Increase of			Decrease of	
	+10%	+5%		-5%	-10%
<b>Exchange rate fluctuations</b>	<b>1.464</b>	<b>1.397</b>	<b>1.331</b>	<b>1.264</b>	<b>1.198</b>
USD thousands					
Forward contract	1,382	690	(1,157)	(690)	(1,380)

### 6.1.3 Summary of the differences in fair value in view of the sensitivity analysis of the dollar interest rate

	Profit (loss)				Fair Value 31.03.2009	Profit (loss)			
	Increase of					Decrease of			
	+10%	+5%	+1%	+0.5%		-0.5%	-1%	-5%	-10%
<b>USD thousands</b>									
Interest rate swaps (IRS)	2,047	1,027	8,040	4,069	(8,339)	(4,174)	(8,461)	(1,033)	(2,072)
Swap hedging	(4)	(22)	(144)	(72)	14,532	72	143	22	4
Dollar-linked securities	(74)	(37)	(7)	(4)	11,398	4	7	37	74
Forward contract	52	26	176	87	(1,247)	(87)	(176)	(26)	(52)
Swapping principal and interest	1,387	697	461	231	18,581	(232)	(465)	(705)	(1,418)
	<u>3,408</u>	<u>1,691</u>	<u>8,526</u>	<u>4,311</u>		<u>(4,417)</u>	<u>(8,952)</u>	<u>(1,705)</u>	<u>(3,464)</u>

### 6.1.4 Summary of the differences in fair value in view of the sensitivity analysis of the price of crude oil and distillates

Change in price	Profit (loss)				Fair Value 31.03.2009	Profit (loss)			
	Increase of					Decrease of			
	+50%	+20%	+10%	+5%		-5%	-10%	-20%	-50%
<b>USD thousands</b>									
Inventory (*)	229,039	91,615	45,808	22,904	458,077	(22,904)	(45,808)	(91,615)	(229,039)
Futures	(130,558)	(52,222)	(26,109)	(13,053)	(3,077)	13,058	26,114	52,227	130,563
Swap hedging (**)	14,118	5,647	2,824	1,412	14,532	(1,412)	(2,824)	(5,647)	(14,118)
	<u>112,599</u>	<u>45,040</u>	<u>22,523</u>	<u>11,263</u>		<u>(11,258)</u>	<u>(22,518)</u>	<u>(45,035)</u>	<u>(112,594)</u>

(\*) Excluding inventory with a fixed price

(\*\*) Assuming product index prices are unchanged

### 6.1.5 Summary of the differences in fair value in view of the sensitivity analysis of shekel interest in real terms:

Change in Interest	Profit (loss)				Fair Value 31.03.2009	Profit (loss)			
	Increase of					Decrease of			
	+10%	+5%	+1%	+0.5%		-0.5%	-1%	-5%	-10%
<b>USD thousands</b>									
CPI-linked securities	(330)	(165)	(33)	(17)	42,390	17	33	165	330
Long-term CPI-linked shekel debentures	8,563	4,315	13,361	6,780	(458,133)	(6,986)	(14,186)	(4,384)	(8,839)
Swapping principal and CPI-linked interest	(3,333)	(1,673)	(20,155)	(10,259)	21,607	10,639	21,675	1,687	3,387
	<u>4,900</u>	<u>2,477</u>	<u>(6,827)</u>	<u>(3,496)</u>		<u>3,670</u>	<u>7,522</u>	<u>(2,532)</u>	<u>5,122</u>

**6.1.6 Summary of the differences in fair value in view of the sensitivity analysis of nominal shekel interest**

<b>Change in Interest</b>	<b>Profit (loss)</b>				<b>Fair Value</b>	<b>Profit (loss)</b>				
	<b>Increase of</b>					<b>31.03.2009</b>	<b>Decrease of</b>			
	<b>+10%</b>	<b>+5%</b>	<b>+1%</b>	<b>+0.5%</b>			<b>-0.5%</b>	<b>-1%</b>	<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>										
Securities (NIS)	(367)	(183)	(36)	(18)	41,637	18	36	183	367	
Forward contracts	-	-	43	22	(90)	(22)	(43)	-	-	
Unlinked shekel debentures	2,139	1,076	3,353	1,695	(127,700)	(1,734)	(3,506)	(1,090)	(2,193)	
Swapping principle and non-linked interest	(2,461)	(1,239)	(6,440)	(3,272)	(3,026)	3,379	6,869	1,255	2,525	
	(689)	(346)	(3,008)	(1,573)		1,641	3,356	348	699	

**6.1.7 Summary of the differences in fair value in view of the sensitivity analysis of euro interest**

<b>Change in Interest</b>	<b>Profit (loss)</b>				<b>Fair Value</b>	<b>Profit (loss)</b>				
	<b>Increase of</b>					<b>31.03.2009</b>	<b>Decrease of</b>			
	<b>+10%</b>	<b>+5%</b>	<b>+1%</b>	<b>+0.5%</b>			<b>-0.5%</b>	<b>-1%</b>	<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>										
Forward contracts	(38)	(19)	(202)	(101)	(1,157)	101	202	19	38	

**6.1.8 Summary of the differences in fair value in view of the sensitivity analysis of the CPI**

<b>Change in the CPI</b>	<b>Profit (loss)</b>		<b>Fair value</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
CPI-linked securities	1,012	506	42,390	(506)	(1,012)
Long-term CPI-linked shekel debentures	(45,813)	(22,907)	(458,133)	22,907	45,813
Swapping principal and interest	38,907	19,453	21,607	(19,453)	(38,907)
	(5,894)	(2,948)		2,948	5,894

**6.1.9 Summary of the differences in fair value in view of the change in price of marketable securities**

	<b>Profit (loss)</b>		<b>Fair value</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
CPI-linked securities	9,543	4,771	95,427	(4,771)	(9,543)

## 6.2 Sensitivity analysis of the exposure to market risks at Carmel Olefins

### 6.2.1 Summary of the differences in fair value in view of the sensitivity analysis of the dollar-shekel exchange rate

	Profit (loss)		Fair value 31.03.2009	Profit (loss)	
	Increase of			Decrease of	
	+10%	+5%		-5%	-10%
<b>Exchange rate fluctuations</b>	<b>4.6068</b>	<b>4.397</b>	<b>4.188</b>	<b>3.979</b>	<b>3.769</b>
<b>USD thousands</b>					
Long-term linked shekel debentures	6,965	3,649	(76,618)	(4,033)	(8,513)
Trade receivables(NIS)	(927)	(486)	10,198	537	1,133
Trade payables (NIS)	1,097	575	(12,063)	(636)	(1,341)
Forward contracts	(137)	(72)	55	79	167
Swapping principal and interest	(7,574)	(3,364)	8,340	5,057	9,268
	(576)	302		1,004	714

### 6.2.2 Summary of the differences in fair value in view of the sensitivity analysis of the euro-dollar exchange rate

	Profit (loss)		Fair value 31.03.2009	Profit (loss)	
	Increase of			Decrease of	
	+10%	+5%		-5%	-10%
<b>Exchange rate fluctuations</b>	<b>1.464</b>	<b>1.397</b>	<b>1.331</b>	<b>1.264</b>	<b>1.198</b>
<b>USD thousands</b>					
Trade receivables- euro	(1,602)	(840)	17,625	928	1,959
Trade payables - euro	983	515	(10,807)	(569)	(1,201)
Other long-term liabilities - euro	664	348	(7,306)	(385)	(812)
Long-term loans - euro	3,239	1,697	(35,624)	(1,875)	(3,958)
Forward contract	(1,650)	(825)	(369)	825	1,650
	1,634	895		(1,076)	(2,362)

### 6.2.3 Summary of the differences in fair value in view of the sensitivity analysis of the GBP-dollar exchange rate

	Profit (loss)		Fair value 31.03.2009	Profit (loss)	
	Increase of			Decrease of	
	+10%	+5%		-5%	-10%
<b>Exchange rate fluctuations</b>	<b>1.574</b>	<b>1.503</b>	<b>1.431</b>	<b>1.359</b>	<b>1.288</b>
<b>USD thousands</b>					
Trade receivables- GBP	(435)	(228)	4,787	252	532
Forward contracts	236	118	(94)	(118)	(236)
	(199)	(110)		134	296

**6.2.4 Summary of the differences in fair value in view of the sensitivity analysis of euro interest**

<b>Change in interest</b>	<b>Profit (loss)</b>		<b>Fair value</b> <b>31.03.2009</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
Fixed interest euro loan	504	244	(22,308)	(225)	(432)

**6.2.5 Summary of the differences in fair value in view of the sensitivity analysis of dollar interest**

<b>Change in interest</b>	<b>Profit (loss)</b>		<b>Fair value</b> <b>31.03.2009</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
Swapping principal and interest	(2,449)	(1,648)	8,340	(45)	758

**6.2.6 Summary of the differences in fair value in view of the sensitivity analysis of shekel interest in real terms:**

<b>Change in interest</b>	<b>Profit (loss)</b>		<b>Fair value</b> <b>31.03.2009</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
Swapping principal and CPI-linked interest	(2,796)	(1,924)	8,340	251	1,369
Long-term CPI-linked shekel debentures	4,260	2,173	(76,618)	(2,263)	(4,619)
	1,464	249		(2,012)	(3,250)

**6.2.7 Summary of the differences in fair value in view of the sensitivity analysis of the CPI**

<b>Change in interest</b>	<b>Profit (loss)</b>		<b>Fair value</b> <b>31.03.2009</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
Debenture swap transactions	8,408	3,781	8,340	(5,474)	(10,102)
Debentures	(7,662)	(3,831)	(76,618)	3,831	7,662
	746	(50)		(1,643)	(2,440)

**6.2.8 Summary of differences in fair value in view of the changes in polymer prices**

<b>Change in interest</b>	<b>Profit (loss)</b>		<b>Fair value</b> <b>31.03.2009</b>	<b>Profit (loss)</b>	
	<b>Increase of</b>			<b>Decrease of</b>	
	<b>+10%</b>	<b>+5%</b>		<b>-5%</b>	<b>-10%</b>
<b>USD thousands</b>					
Debenture swap transactions	2,501	1,251	25,011	(1,251)	(2,501)

## 6.3 Consolidated linkage-based report

### 6.3.1 Consolidated linkage-based report as of March 31, 2009 (USD thousands)

	Index- linked	Foreign- currency linked (*)	Unlinked	Non- monetary	Total
<b>Assets</b>					
Cash and cash equivalents	-	10,360	2,247	-	12,607
Short-term deposit	-	63,746	-	-	63,746
Derivatives at fair value through profit or loss	-	12,820	-	-	12,820
Future purchase	-	49,504	89,378	-	138,882
Investment in other financial assets at fair value through profit or loss	42,391	11,398	41,638	-	95,427
Trade receivables	-	203,080	33,319	-	236,399
Other receivables	18,777	1,623	23,336	19,783	63,519
Inventory	-	647,666	33,404	36,300	717,370
Current tax assets	39,734	-	-	-	39,734
Investments in equity-accounted investees	-	-	-	35,725	35,725
Loan to Haifa Early Pensions Ltd. (**)	81,849	-	-	-	81,849
Long term loans and debit balances (**)	-	718	2,602	-	3,320
Long-term derivatives at fair value through profit or loss	475,927	-	139,387	-	615,314
Employee benefit plan assets	-	-	4,619	-	4,619
Property, plant and equipment	-	-	-	1,117,021	1,117,021
Intangible assets and deferred expenses, net	-	-	-	24,555	24,555
<b>Total assets</b>	<b>658,678</b>	<b>1,000,915</b>	<b>369,930</b>	<b>1,233,384</b>	<b>3,262,907</b>
<b>Liabilities</b>					
Short-term credit and loans	-	(190,089)	(41,694)	-	(231,783)
Trade payables	-	(282,259)	(44,123)	-	(326,382)
Other payables	-	(23,675)	(35,787)	-	(59,462)
Future sales	-	(104,155)	(36,111)	-	(140,266)
Long-term derivatives at fair value through profit or loss	-	(588,393)	-	-	(588,393)
Provisions	-	(2,113)	(10,072)	-	(12,185)
Debentures (**)	(552,912)	(4,194)	(119,389)	2,917	(673,578)
Bank loans (**)	-	(433,554)	-	1,917	(431,637)
Liabilities for finance lease	(7,656)	-	-	-	(7,656)
Other long-term liabilities	-	(7,306)	-	-	(7,306)
Long-term future sale	-	(8,339)	-	-	(8,339)
Employee benefits	-	(440)	(62,033)	-	(62,473)
Liabilities for deferred taxes	-	-	-	(91,209)	(91,209)
<b>Total liabilities</b>	<b>(560,568)</b>	<b>(1,644,517)</b>	<b>(349,209)</b>	<b>(86,375)</b>	<b>(2,640,669)</b>
<b>Net balance</b>	<b>98,110</b>	<b>(643,602)</b>	<b>20,721</b>	<b>1,147,009</b>	<b>622,238</b>

(\*) Primarily dollar

(\*\*) Including current maturities

The Company's management views the product inventory, consisting of commodities with a turnover of a month, as a financial item. Accordingly, it is included in the table above.

### 6.3.2 Consolidated linkage-based report as of December 31, 2008 (USD thousands)

	Index- linked	Foreign- currency linked (*)	Unlinked	Non- monetary	Total
<b>Assets</b>					
Cash and cash equivalents	-	14,194	646	-	14,840
Short-term deposit	-	25,000	-	-	25,000
Derivatives at fair value through profit or loss	-	15,374	-	-	15,374
Future purchase	-	78,684	-	-	78,684
Investment in other financial assets at fair value through profit or loss	49,612	16,432	35,465	-	101,509
Trade receivables	-	173,759	79,456	-	253,215
Other receivables	20,724	9,729	24,159	25,852	80,464
Inventory	-	494,013	34,298	41,096	569,407
Current tax assets	42,047	-	-	-	42,047
Affiliates	-	-	-	36,005	36,005
Loan to Haifa Early Pensions Ltd. (**)	86,047	-	-	-	86,047
Long term loans and debit balances (**)	-	463	3,014	-	3,477
Long-term derivatives at fair value through profit or loss	499,951	-	150,092	-	650,043
Employee benefit plan assets	-	-	5,007	-	5,007
Property, plant and equipment	-	-	-	1,083,446	1,083,446
Intangible assets and deferred expenses, net	-	-	-	25,170	25,170
<b>Total assets</b>	<b>698,381</b>	<b>827,648</b>	<b>332,137</b>	<b>1,211,569</b>	<b>3,069,735</b>
<b>Liabilities</b>					
Short-term credit and loans	-	(81,645)	(48,774)	-	(130,419)
Trade payables	-	(243,107)	(27,487)	-	(270,594)
Other payables	(1,422)	(31,395)	(33,346)	-	(66,163)
Future sales	-	(18,908)	(61,629)	-	(80,537)
Long-term derivatives at fair value through profit or loss	-	(585,674)	-	-	(585,674)
Provisions	-	(2,201)	(10,748)	-	(12,949)
Debentures (**)	(619,875)	(4,455)	(131,510)	3,270	(752,570)
Bank loans (**)	-	(459,736)	-	2,083	(457,653)
Liabilities for finance lease	(8,448)	-	-	-	(8,448)
Other long-term liabilities	-	(7,394)	-	-	(7,394)
Long-term future sale	-	(6,900)	-	-	(6,900)
Employee benefits	-	(461)	(72,277)	-	(72,738)
Liabilities for deferred taxes	-	-	-	(65,827)	(65,827)
<b>Total liabilities</b>	<b>(629,745)</b>	<b>(1,441,876)</b>	<b>(385,771)</b>	<b>(60,474)</b>	<b>(2,517,866)</b>
<b>Net balance</b>	<b>68,636</b>	<b>(614,228)</b>	<b>(53,634)</b>	<b>1,151,095</b>	<b>551,869</b>

(\*) Primarily dollar

(\*\*) Including current maturities

The Company's management views the product inventory, consisting of commodities with a turnover of a month, as a financial item. Accordingly, it is included in the table above.

## **7. Additional information contained in the auditors' report to shareholders**

Without qualifying their opinion, the auditors of the Company drew attention to:

- 7.1. The contents of Note 7(A) and Note 8(A) to the financial statements, regarding the suits filed against the Company, a subsidiary and a proportionally consolidated company ("the subsidiaries"), the legal proceedings, supervision by government authorities, other contingencies, laws and bills relating to the fuel and gas industry and infrastructure facilities. Based on the opinion of the legal counsels of the Company and its subsidiaries, the Company estimates that, at this stage, it is not possible to assess the aforementioned impact on the financial statements, if any exists, and therefore, no provision regarding this matter was included in the financial statements.
- 7.2. The contents of Note 7(B) regarding the dependency of the Group on services from infrastructure companies.

## **8. Disclosure of the process for approving the Company's financial statements**

The board of directors appointed an audit and balance sheet committee and instructed it, among its other duties, to discuss and make recommendations to the board in connection with the approval of the financial statements. Among the members of the audit committee are Mr. Ori Slonim, Mr. Avisar Paz and Mrs. Daphne Schwartz, the directors having accounting and financial expertise, as well as other directors.

The audit committee discusses the financial statements at its meeting at which senior officers of the Company and the external auditor of the Company are in attendance. The committee hears a detailed presentation made by the senior officers and others at the Company, including the CEO and CFO. The presentation includes the material issues contained in the financial reports, including material transactions not conducted in the normal course of business (if any), the significant assessments and critical estimates applied in the financial statements, the accounting policy applied and changes thereto (if any), and the implementation of the fair disclosure principle in the financial statements and accompanying information.

The committee assesses the various aspects of the control and risk management, both those reflected in the financial statements (for example, reporting on financial risks) and those affecting the reliability of the financial statements. The opinion of the external auditor is also heard at the meeting. The committee presents its recommendations regarding the reports to the board of directors.

After receiving the recommendation of the audit committee regarding the financial statements, the board of directors investigates the material issues included in the financial statements, including material transactions not conducted in the normal course of business (if any), the significant assessments and critical estimates applied in the financial statements, the accounting policy applied and changes thereto (if any), and the implementation of the fair disclosure principle in the financial statements and accompanying information. The board of directors assesses the various aspects of the control and risk management, both those reflected in the financial statements (for example, reporting on financial risks) and those affecting the reliability of the financial statements.

The board of directors also studies the recommendations of the audit committee regarding the financial statements being discussed, hears the opinion of the auditor, and where necessary, requests that other matters be reviewed by the board, at its discretion.

The financial statements are submitted to the members of the audit committee and the board of directors a few days prior to the meeting at which they are discussed for purposes of approval.

During the course of the deliberations of the board of directors, questions are raised by the members of the board on various issues, including issues that arose during the audit. The goal of the entire process is to ensure that the financial statements faithfully present the financial position of the Company.

The questions and issues raised are addressed when necessary by both Company management through the CEO or CFO and by the auditor of the Company. Following a discussion, the chairman of the

board calls for a vote on the approval of the financial statements, after ensuring that members of the board have no further questions and there are no unanswered issues.

The financial statements as of March 31, 2009 were discussed at the audit and balance sheet committee on May 10, 2009 in the presence of the audit and balance sheet committee members – Uri Slonim (chair), Yachin Cohen, Avisar Paz, Nechama Ronen, and Daphne Schwartz, and with the participation of the chairman of the board, Yossi Rosen, and board members – Ron Carol and Uzi Natanel, and were discussed and approved in full at the board of directors of the Company on May 17, 2009, to which all the abovementioned members of the board were invited.

## **9. Disclosure regarding the internal auditor in a reporting corporation**

**9.1.** Name of auditor: Yehuda Meirovitch, in office since 1988

Qualifications: MBA, CIA

**9.2.** The auditor is an employee of the Company.

**9.3.** Scope of employment during the reporting period: full time + two audit employees + the engagement of two outside offices for internal audits in a scope of 4,500 hours in 2009.

**9.4.** The audit plan is based on a multi-year plan to cover the main issues of the Company every two or three years. Other issues once every three or four years and the management's routine audit requirements.

**9.5.** The internal audit plan includes audit issues at Gadiv, which constitutes a material holding of ORL, and refers also to commercial and other connections with companies in which ORL has holdings.

**9.6.** The internal auditor conducts the audit in accordance with professional standards generally accepted in Israel and other countries.

**9.7.** The internal auditor reports directly to the chairman of the board of directors.

**9.8.** The audit reports were presented and discussed at the following meetings of the audit committee:

**9.8.1** The work plan for the 2009 internal audit was approved at the meeting of the audit committee in February 2009. At this meeting, the committee discussed the performance of a comprehensive risk survey for the Company, which will include a separate section for internal audit purposes. The committee decided to convene another meeting as soon as possible to discuss hedging against risks in acquisition of crude oil and distillates and a number of issues that were not discussed at the previous meeting.

**9.8.2** In the meeting held in March 2009, the audit committee discussed a number of issues from the interim internal audit report for 2008. In this meeting, decisions were made to correct faults found in the audit of these issues.

**9.8.3** In the meeting held in April 2009, the audit committee discussed and reported the following:

- The status of implementation of the decisions to correct faults found in the 2006-2007 audits in areas that have not been fully corrected.
- Implementation of the enforcement plan in the Company in various areas.
- Progress in finding an external party to carry out a comprehensive risk survey for the Company.
- The management's method for correcting the faults that were found in two audit reports in the trade segment – trade in crude oil and hedging of transactions for the import and export of fuel products.
- Other audits in accordance with the work plan of the internal audit for 2008.

**9.9.** The nature and continuity of operations and the internal auditor's work plan are reasonable under the circumstances, in the Company's estimation, and will serve to achieve the purposes of the

corporation's internal audit. The internal auditor has free access, as set out in section 9 of the Internal Audit Law - 1992, including constant and direct access to the corporation's information systems, including financial data.

## **10. Debentures of the corporation held by the public**

**10.1.** In the reporting period, there were no significant changes in the three debenture series issued by the Company and offered to the public in a prospectus, the debenture trustees, conditions for the call for immediate redemption of the debentures and the Company's compliance with these conditions and the collateral for the debentures as described in the Directors' Report of December 31, 2008, with the exception of changes in the debenture rating as set forth in section 10.2 below.

### **10.2. Debenture rating**

The table below describes the rating of the debentures in circulation.

<u>Series</u>	<u>Date of issue</u>	<u>Rating proximate to date of issue</u>	<u>Rating on December 31, 2008</u>	<u>Rating company</u>	<u>Date and reference of immediate report on the updated rating<sup>1</sup></u>
Series A	3.12.2007	AA/Stable	A/Negative	S&P Maalot	13.11.2008 Reference 2008-01-316449
Series B	3.12.2007	AA/Stable	A/Negative	S&P Maalot	13.11.2008 Reference 2008-01-316449
Series C	3.12.2007	AA/Stable	A/Negative	S&P Maalot	13.11.2008 Reference 2008-01-316449

On April 23, 2009, Maalot S&P (Maalot) announced that the rating of the Company's debentures (non-negotiable series and negotiable series A-C) has been placed on CreditWatch Negative. This reflects the consequences of the uncertainty in the refining industry in the medium term, the financing of the investments plan and the acquisition of Carmel Olefins and the change in the structure of control in the Company. See section 16.2 below for further information.

## **11. Use of estimates and judgments**

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

When preparing the accounting estimates used to prepare the Group's financial statements, management was required to make assumptions regarding the circumstances and events involving substantial uncertainty and relied on past experience, various facts, external factors and reasonable assumptions according to the circumstances appropriate for each estimate.

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

In the reporting period, there were no material changes in the estimates identified by the Company as critical, the consideration in the assessments and assumptions that affected the application of the policy, as set forth in section 13 of the Directors' Report of December 31, 2008.

## **12. Corporate governance**

In 2008, the board of directors adopted a procedure based on the recommendations of the Goshen Committee and the recommendations regarding their implementation as submitted to the Company by Adv. Dr. Yoram Danziger. On December 30, 2008, the Company added a provision in its regulations

<sup>1</sup> The immediate reports included in this position are presented as a reference.

whereby as long as the Company has a controlling shareholder or a holder of a control block, at least one third of the members of the board of directors will be independent directors, as defined in section 219(E) of the Companies Law. As of the reporting date, the audit committee has not discussed and determined the identity of the independent directors.

### **13. Meetings of the board of directors**

During the reporting period, there were five board meetings and 16 meetings of board committees.

### **14. Salaries of senior officers and considerations on which the board of directors bases such salaries**

Management estimates that the remuneration of the senior officers are appropriate, fair and reasonable, taking into consideration the size of the Company, scope and complexity of its operations and business, the tasks and degree of responsibility of the senior officers who dedicate their effort and time to promote the affairs of the Company and their contribution to the development of the Company's affairs. In determining the salaries of senior officers, as well as bonuses paid to them, the Company takes into consideration achievements in the areas of business and finance, degree of responsibility, specific contribution, and compliance with targets and work plans.

The Company has a policy of granting bonuses to its senior officers, at the discretion of the CEO and the approval of the relevant organs, based, inter alia, on the Company's results.

At the beginning of 2009, the chairman of the board, CEO and other officers in the Company announced their decision to waive 10% of their salary (with the exception of provisions and incidental conditions) in 2009. This is part of the 2009 work plan to ensure implementation of the Company's strategic plan and its long-term strength and prosperity, against the background of the global economic crisis and its implications on the Israeli economy.

### **15. Significant events during the reporting period**

In January 2009, the Company and Gadiv received from the Ministry of Environmental Protection a warning and summons to a hearing relating to violations and alleged defective application of the provisions of the personal order ("the warning"). The warning described the alleged violations which referred, inter alia, to the timetables set forth in the order, the results of the stack samples, the submission of certain plans stipulated in the personal order and to the way information is sent to the Ministry, as stipulated in the order.

Prior to the date of the hearing, the Company and Gadiv submitted their response to the warning it received. In the response, they detailed their arguments and responses to the issues included in the warning. At the conclusion of the hearing, goals and timetables were set for actions to be taken by the Company to reduce the pollution emitted by its facilities. The Company is preparing to implement the mandatory actions under the personal orders and is holding discussions with the Ministry of Environmental Protection regarding additional actions that the Ministry requires.

On January 25, 2009, a hearing was held at the Ministry of Environmental Protection for the Company and PEI regarding two specific sites where, according to the Ministry, soil and groundwater were contaminated by fuel products. After the hearing, the Company and PEI were required to close the two pipelines along which leakage was found; to return them to operation following repair and/or replacement; to test impermeability of all the pipelines and to submit the results to the Ministry of Environmental Protection. In the hearing, the Company and PEI were warned that if the repair and rehabilitation process does not commence within seven days after the hearing, including the removal of the contaminated soil, the Ministry would issue an order for cleanup and removal of the toxic substances. The Ministry gave notice that the Green Police of the Ministry of Environmental Protection would investigate the events, including the Company's failure to act to minimize damage and prevent further contamination of the river and its environs.

On March, 1, 2009, the Company received a removal order for toxic substances, pursuant to section 16(A) of the Hazardous Substances Law - 1993 and a clean-up order, pursuant to section 13(B) of the

Maintenance of Cleanliness Law - 1984, demanding that the Company, PEI and their CEOs submit plans to the Ministry of Environmental Protection for soil gas, soil and groundwater surveys and to fence off the contaminated areas and conduct the survey in accordance with the approved plans. The parties are further required to submit to the Ministry a report of the survey findings, including recommendations for the clean-up and rehabilitation of the contaminated soil and groundwater and the restoration of the river and its banks to their former condition, based on the findings of the survey. The parties will also define a short-term and binding timetable for implementing the recommendations of the survey, until all waste and toxins are removed from the soil and groundwater.

The Company has submitted its plan for the soil gas, soil and groundwater survey to the Ministry of Environmental Protection for approval and it is carrying out the survey in accordance with the plan.

As of the reporting date, the Company is unable to assess the outcome of the survey, the actions required according to the outcome and the expenses arising for the Company when implementing these measures.

At the beginning of 2009, the Company and EAPC were required, under the terms added to their business licenses, to conduct soil surveys along the pipeline corridor and to apply the survey recommendations according to the suggested timetable approved by the Ministry of Environmental Protection. The Company appealed this condition in its business license through the procedure set up by the law. The Ministry of Environmental Protection has not yet responded to the appeal and the Company cannot estimate whether it will be required to implement the additional term and the expense required to implement the term. The Company and the Ministry agreed that until the court hearing, the Company will not carry out the required survey.

## **16. Subsequent events**

### **16.1. Impact of changes in exchange rates and prices of crude oil and distillates**

**Changes in exchange rates:** From the end of the reporting period and up to the approval date of the financial statements, there was an appreciation of 2% in the shekel-dollar exchange rate. The Company, as part of its exposure management policy, uses hedging transactions to neutralize part of this exposure. The effect of the appreciation on the Group's business results, after the results of the hedging transactions, is estimated at \$3 million in financing income.

**Changes in prices of crude oil and its distillates:** As a result of the changes in the economic environment subsequent to the balance sheet date, there were significant fluctuations in the price of crude oil and its distillates. The price of oil, which was \$50 per barrel on the balance sheet date, rose to \$57 per barrel close to the date of approval of the financial statements.

- 16.2.** On April 23, 2009, Maalot S&P (Maalot) announced that the rating of the Company's debentures (non-negotiable series and negotiable series A-C) has been placed on CreditWatch Negative. due to its assessment of the possible consequences of uncertainty regarding the refining industry in the medium term and its impact on the Company's cash flows, uncertainty connected with financing the investment plan and the resulting debt and uncertainty regarding the timing of the acquisition of Carmel Olefins, including the consequences for the Company should Carmel Olefins fail to meet the financial covenants and the changes in the structure of ownership and core control and the possible acquisition of Carmel Olefins.

During the next months, Maalot intends to remove the Company from CreditWatch, after examining the Company's business plans and the expectation of a significant increase in the level of the debt.

Proximate to Maalot's rating announcement, the Company issued an immediate report in which it noted that the reasoning of Maalot in this announcement does not take into account the strength of positive events resulting from the Company's steps and investments, in addition to its ability to take advantage of the changes in its business environment. Among others, these include:

1. The decline in oil prices substantially contributes to the Company's working capital requirements and grants the Company better flexibility in utilizing its available financial resources, as well as reducing finance expenses.

2. Despite the decline in general consumption in 2008, the Company managed to increase both market share and quantities sold.
3. During the past year (2008) the Company increased its unit utilization to an all time record of 92%.
4. The Company has implemented a strategic plan and new organization structure, contributing to lower expenses, while placing emphasis on core competencies.
5. The Company continues to take steps to strengthen its core assets, while increasing refining complexity, unit flexibility, and adding margin drivers and, during 2009, is undertaking several investments geared at increasing profitability and reducing risk over time.
6. The Company continues to implement its investment plan to establish the hydrocracker. The forecasted estimated refining margins of the products produced in this unit are higher than in the past, while the investment is expected to be lower than initially planned when the investment was approved.

The Company wishes to draw attention to the fact that at the date of this report, its traded debentures are trading at similar prices as at the same period last year, prior to Maalot's announcement of the downgrading of the Company's credit rating in November 2008. See Note 16(4) to the financial statements as of December 31, 2008.

- 16.3.** On May 7, 2009, IPE announced that it had received a control permit. On that date, the Company received notice from the Government Companies Authority regarding this control permit. The control permit sets forth the requirements for the operation of IPE and PCH under the control permit, to be fulfilled within 30 days: the validation or the complete fulfillment of the series of agreements signed between Mogdal Ltd. and Mogdal Industries (99) Ltd. and Charabancs Investment N.V; and the validation of the joint control agreement between IPE and PCH and the Israel Corporation Ltd. The Government Companies Authority further announced that it would notify the Company when the conditions exist to allow IPE and PCH to operate under the control permit. On May 7, 2009, IPE issued an immediate report announcing that Modgal Ltd. and Mogdal Industries (99) Ltd. had informed IPE of the validation and complete fulfillment of the series of agreements signed between them and Charabanc N.V. and that all the terms for the validation of the joint control agreement between IPE and PCH and the Israel Corporation Ltd. had been met.

In addition, IPE announced that it had decided that it would not exercise, and would act that PCH would not exercise the call options given to PCH in accordance with the provisions of the joint control agreement.

**16.4. Disclosure of the expected cash flow for financing the repayment of Carmel Olefins liabilities**

As reflected in the financial statements of Carmel Olefins, as of March 31, 2009, Carmel Olefins has an operating capital deficit of \$253 million, mainly due to reclassification of long-term loans of \$230 million to short term, as a result of non-compliance with the financial covenants set with the banks.

The management of Carmel Olefins believes that the results of the first quarter of 2009 indicate that demand has stabilized and margins are no longer eroding. On the other hand, the working capital is expected to continue to be negative until the financial covenants are arranged with the banks. Carmel Olefins is currently negotiating with the banks to reach an arrangement. In view of the progress of the negotiations, Carmel Olefins estimates that, as of the reporting date, it will receive letters of waiver from all the banks. This is forward-looking information and as such may not materialize and is not under the control of Carmel Olefins alone, therefore there is no certainty that it will materialize.

The following table describes the expected cash flow of Carmel Olefins for repayment of its liabilities for its debentures.

	<u>First year</u>	<u>Second year</u>
	<u>USD thousands</u>	
<b>Sources</b>		
Cash flow from operating activities (before interest)	89,320	41,333
Cash flow at the beginning of the period	16,225	41,028
Short-term credit received	-	2,500
Total sources	<u>105,545</u>	<u>84,861</u>
<b>Uses</b>		
Investments in property, plant and equipment	12,000	12,000
Liability for repayment of debentures (interest)	10,197	10,197
Liability for repayment of long-term loans (principle + interest)	42,320	42,320
Dividend	-	20,000
Total uses	<u>64,517</u>	<u>84,517</u>
<b>Cash balance at end of period</b>	<b><u>41,028</u></b>	<b><u>344</u></b>

1. As of the approval date of the financial statements, the board of directors of Carmel Olefins examined the market situation, business forecasts of Carmel Olefins and its cash flow forecast. The board of directors of Carmel Olefins estimates that, based on this information, it is able to repay its liabilities.
2. Carmel Olefins' estimate of its cash flow is based on the forecasted margins, implementation of the planned efficiency measures and reduction of fixed expenses, including the early retirement plan that led to a reduction of human resources, gross payroll expenses and employee benefits.

The cash flow statement of Carmel Olefins is based on its assessments and forecasts of prices and costs. This forecast is forward looking information, the realization of which is not certain and is not under the control of Carmel Olefins alone, Therefore, there is no certainty that the information, assessments or forecasts will materialize, in full or in part, and this could result in a cash flow that differs from the forecast.

- 16.5.** On April 23, 2009, Carmel Olefins signed an agreement for the purchase of feedstocks from ORL. The agreement includes terms for the purchase of 60,000 tons of propylene per year, which ORL undertook to sell to Carmel Olefins under the obligations that were assigned in the split of the refineries, and terms for the purchase of at least 40,500 tons of 4C per year. The agreement is valid for 10 days commencing from January 1, 2009, subject to the rights of the parties to terminate the agreement earlier in accordance with the provisions in the agreement.

The board of directors thanks the managements and employees of the Company and subsidiaries for their efforts and achievements in the reporting period.

\_\_\_\_\_  
Yossi Rosen  
Chairman of the board of directors

\_\_\_\_\_  
Yashar Ben Mordechai  
CEO

May 17, 2009

**Update to the State of the Company's Affairs in the Periodic Report**  
**as of December 31, 2008**

In accordance with Regulation 39A of the Securities Regulations (Periodic and Immediate Reports) -1970.

During the reporting period, there were no significant changes or new events in the Company's affairs, with the exception of those set forth in the Directors' Report.



The Board of Directors Oil Refineries Limited  
HAIFA

## **Auditors Report for the Shareholders of Oil Refineries Limited**

### **Introduction**

We have reviewed the accompanying financial information of Oil Refineries Limited and its subsidiaries ("the Group"), including the condensed consolidated interim statement of financial position as of March 31, 2009 and the condensed consolidated interim statements of comprehensive income, changes in equity and cash flows for the three months then ended. The board of directors and the management are responsible for preparation and presentation of the interim financial information for this period in accordance with IAS 34 - *Interim Financial Reporting*, and are also responsible for preparation of the interim financial information for this period in accordance with Chapter D of the Securities Regulations (Periodic and Immediate Reports) – 1970. Our responsibility is to express an opinion on the interim financial information for the period based on our review.

We did not review the condensed interim financial statements of a proportionally consolidated company, the consolidated assets of which represent approximately 21% of the total consolidated assets as of March 31, 2009, and the consolidated revenue of which represent approximately 9% of the total consolidated revenue for the three months then ended. In addition, we did not review the condensed interim financial statements of equity-accounted investees, the investment in which amounts to \$35,725 thousand as of March 31, 2009, and the share of the Group in their profits is \$4,591 thousand for the three months then ended. The condensed interim financial information of those companies were reviewed by other accountants, whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based on the reviews of the other accountants.

### **Review scope**

We conducted our review in accordance with Accounting Standard no. 1 – *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*, established by the Institute of Certified Public Accountants in Israel. A review of interim financial information consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with accepted accounting principles in Israel and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

### **Conclusion**

Based on our review and the review of other accountants, nothing has come to our attention that causes us to believe that this financial information is not prepared, in all material respects, in accordance with IAS 34.

Additionally, based on our review and the review of other accountants, nothing has come to our attention that causes us to believe that this financial information is not prepared, in all material respects, in accordance with the disclosure provisions in Chapter D of the Securities Regulations (Periodic and Immediate Reports) -1970.

Without qualifying our above opinion, we draw attention to the following:

1. The contents of Note 7(A) and Note 8(A) to the financial statements, regarding the suits filed against the Company, a subsidiary and a proportionally consolidated company ("the subsidiaries"), the legal proceedings, supervision by government authorities, other contingencies, laws and bills relating to the fuel and gas industry and infrastructure facilities. Based on the opinion of the legal counsels of the



Company and its subsidiaries, the Company estimates that, at this stage, it is not possible to assess the aforementioned impact on the financial statements, if any exists, and therefore, no provision regarding this matter was included in the financial statements.

2. The contents of Note 7(B) regarding the dependency of the Group on services from infrastructure companies.

Sincerely,

Somekh Chaikin  
Certified Public Accountants

May 17, 2009

**Oil Refineries Ltd.**

**Condensed Consolidated Interim Statements of Financial Position**  
**USD thousands**

	As at		
	March 31, 2009	March 31, 2008	December 31, 2008
	(Unaudited)		(Audited)
<b><u>Current assets</u></b>			
Cash and cash equivalents	12,607	41,858	14,840
Deposits	63,746	-	25,000
Derivatives at fair value through profit or loss	12,820	10,389	15,374
Investments in other financial assets at fair value through profit or loss	95,427	275,386	101,509
Trade receivables	236,399	469,185	253,215
Other receivables	75,049	121,628	82,642
Inventory	717,370	1,161,466	569,407
Current tax assets	39,734	26,004	42,047
<b>Total current assets</b>	<b>1,253,152</b>	<b>2,105,916</b>	<b>1,104,034</b>
<b><u>Non-current assets</u></b>			
Investments in equity-accounted investees	35,725	44,552	36,005
Loan to Haifa Early Pensions Ltd.	71,117	88,833	84,740
Long term loans and debit balances	2,522	2,039	2,606
Derivatives at fair value through profit or loss	26,921	65,055	64,369
Employee benefit plan assets	4,619	7,397	5,007
Property, plant and equipment	1,117,021	1,005,136	1,083,446
Intangible assets and deferred expenses, net	24,555	22,140	25,170
<b>Total non-current assets</b>	<b>1,282,480</b>	<b>1,235,152</b>	<b>1,301,343</b>
<b>Total assets</b>	<b>2,535,632</b>	<b>3,341,068</b>	<b>2,405,377</b>

**The attached notes are an integral part of the condensed consolidated interim financial statements.**

**Oil Refineries Ltd.**

**Condensed Consolidated Interim Statements of Financial Position**  
**USD thousands**

	<b>As at</b>		
	<b>March 31,</b>	<b>March 31,</b>	<b>December 31,</b>
	<b>2009</b>	<b>2008</b>	<b>2008</b>
	<b>(Unaudited)</b>	<b>(Audited)</b>	
<b><u>Current liabilities</u></b>			
Loans and credit	476,544	282,423	380,339
Trade payables	326,382	698,994	270,594
Other payables	67,319	101,884 (*)	70,971 (*)
Derivatives at fair value through profit or loss	1,384	22,808	1,853
Provisions	12,185	27,309	12,949
<b>Total current liabilities</b>	<b>883,814</b>	<b>1,133,418</b>	<b>736,706</b>
<b><u>Non-current liabilities</u></b>			
Debentures	649,655	772,287	726,554
Bank loans	210,799	437,537	233,749
Liabilities for finance lease	7,656	8,403	8,448
Other long-term liabilities	7,306	-	7,394
Derivatives at fair value through profit or loss	8,339	-	6,900
Employee benefits	54,616	70,417 (*)	67,930 (*)
Liabilities for deferred taxes	91,209	116,363	65,827
<b>Total non-current liabilities</b>	<b>1,029,580</b>	<b>1,405,007</b>	<b>1,116,802</b>
<b>Total liabilities</b>	<b>1,913,394</b>	<b>2,538,425</b>	<b>1,853,508</b>
<b><u>Equity</u></b>			
Share capital	472,478	472,478	472,478
Capital reserves	16,564	29,783	20,953
Retained earnings	133,196	300,382	58,438
<b>Total equity</b>	<b>622,238</b>	<b>802,643</b>	<b>551,869</b>
<b>Total liabilities and capital</b>	<b>2,535,632</b>	<b>3,341,068</b>	<b>2,405,377</b>

(\*) Reclassified, see Note 2(D)(1)

**Yossi Rosen**  
**Chairman of the Board**

**Yashar Ben Mordechai**  
**CEO**

**Igal Salhov**  
**CFO**

Date of approval: May 17, 2009

**The attached notes are an integral part of the condensed consolidated interim financial statements.**

**Oil Refineries Ltd.**

**Condensed Consolidated Interim Statements of Comprehensive Income**  
**USD thousands**

	<b>Three months ended</b>		<b>Year ended</b>
	<b>March 31,</b>	<b>March 31,</b>	<b>December 31,</b>
	<b>2009</b>	<b>2008</b>	<b>2008</b>
	<b>(Unaudited)</b>		<b>(Audited)</b>
Revenue	984,358	1,885,696	8,257,458
Cost of sales, refinery and services	880,977	1,824,174 (*)	8,324,149
Revaluation of open transactions in derivatives on prices of goods and margins, net	1,245	20,487 (*)	(7,465)
<b>Total cost of sales</b>	<b>882,222</b>	<b>1,844,661</b>	<b>8,316,684</b>
<b>Gross profit (loss)</b>	<b>102,136</b>	<b>41,035</b>	<b>(59,226)</b>
Selling expenses	8,773	10,468	40,582
General and administrative expenses	13,121	14,732	67,061
Negative goodwill created upon acquisition	-	-	(14,535)
<b>Operating profit (loss)</b>	<b>80,242</b>	<b>15,835</b>	<b>(152,334)</b>
Financing revenue	58,772	31,412 (*)	64,979
Financing expenses	(44,407)	(48,084) (*)	(126,034)
Financing income (expenses), net	14,365	(16,672)	(61,055)
Company's share in profits (losses) of associates (net of tax)	4,591	(5,070)	(3,111)
<b>Profit (loss) before taxes on income</b>	<b>99,198</b>	<b>(5,907)</b>	<b>(216,500)</b>
Tax benefits (taxes on income)	(24,607)	8,000	107,292
<b>Net profit (loss) for the period</b>	<b>74,591</b>	<b>2,093</b>	<b>(109,208)</b>
<b>Other components of comprehensive income</b>			
Actuarial gains (losses) from a defined benefit plan, net	167	-	(9,318)
Capital reserve for translation differentials	(254)	-	(1,078)
Group's share of other comprehensive income of an equity accounted investee	(4,799)	-	(10,433)
<b>Other comprehensive income for the period, net of tax</b>	<b>(4,886)</b>	<b>-</b>	<b>(20,829)</b>
<b>Comprehensive income for the period</b>	<b>69,705</b>	<b>2,093</b>	<b>(130,037)</b>
<b>Earnings (loss) per share</b>			
Net basic and diluted earnings (losses) per ordinary share (in USD)	0.037	0.001	(0.055)

(\*) Reclassified, see Note 2(D)(2)

Due to first-time adoption of the revised IAS 1 in these financial statements, the presentation format of the statement of comprehensive income was changed. See also Note 3(1)(A) for a description of first-time adoption of the new standards.

**The attached notes are an integral part of the condensed consolidated interim financial statements.**

**Oil Refineries Ltd.**

**Condensed Consolidated Interim Statements of Changes in Equity**  
**USD thousands**

	<b>Capital reserve</b>	<b>Capital reserve for share- based payment</b>	<b>Capital reserve for translation differentials</b>	<b>Capital reserve for financial assets available for sale</b>	<b>Capital reserve</b>	<b>Retained earnings</b>	<b>Total</b>
<b>Three months ended March 31, 2009</b> <b>(Unaudited)</b>							
<b>Balance as of January 1, 2009 (audited)</b>	472,478	3,986	(1,078)	(10,433)	28,478	58,438	551,869
Comprehensive income for the period	-	-	(254)	(4,799)	-	74,758	69,705
Options issued to employees	-	664	-	-	-	-	664
<b>Balance as of March 31, 2009 (Unaudited)</b>	<b>472,478</b>	<b>4,650</b>	<b>(1,332)</b>	<b>(15,232)</b>	<b>28,478</b>	<b>133,196</b>	<b>622,238</b>
<b>Three months ended March 31, 2008</b> <b>(Unaudited)</b>							
<b>Balance on January 1, 2008 (audited)</b>	472,478	558	-	-	28,478	298,289	799,803
Comprehensive income for the period	-	-	-	-	-	2,093	2,093
Options issued to employees	-	747	-	-	-	-	747
<b>Balance as of March 31, 2008 (Unaudited)</b>	<b>472,478</b>	<b>1,305</b>	<b>-</b>	<b>-</b>	<b>28,478</b>	<b>300,382</b>	<b>802,643</b>
<b>Year ended December 31, 2008</b> <b>(Audited)</b>							
<b>Balance on January 1, 2008 (Audited)</b>	472,478	558	-	-	28,478	298,289	799,803
Comprehensive income for the period	-	-	(1,078)	(10,433)	-	(118,526)	(130,037)
Dividend declared and paid	-	-	-	-	-	(121,325)	(121,325)
Options issued to employees	-	3,428	-	-	-	-	3,428
<b>Balance as of December 31, 2008 (audited)</b>	<b>472,478</b>	<b>3,986</b>	<b>(1,078)</b>	<b>(10,433)</b>	<b>28,478</b>	<b>58,438</b>	<b>551,869</b>

Due to first-time adoption of the revised IAS 1 in these financial statements, the presentation format of the interim statement of changes in equity was changed. See also Note 3(1)(A) for a description of first-time adoption of the new standards.

**The attached notes are an integral part of the condensed consolidated interim financial statements.**

**Oil Refineries Ltd.**

**Condensed Consolidated Interim Statement of Cash Flows**  
**USD thousands**

	<b>Three months ended</b>	<b>Year ended</b>
	<b>March 31, 2009</b>	<b>March 31, 2008(*)</b>
	<b>(Unaudited)</b>	<b>December 31, 2008</b>
		<b>(Audited)</b>
<b>Cash flows from operating activities</b>		
Profit (loss) for the period	74,591	(109,208)
<b>Adjustments required to present the cash flows from operating activities:</b>		
Revenue and expenses not involving cash flows (Appendix A – section A)	21,411	19,061
	96,002	(90,147)
Changes in assets and liabilities (Appendix A – section B)	(65,475)	298,052
Income tax received (paid), net	(431)	15,212
<b>Net cash provided by (used in) current activities</b>	<b>30,096</b>	<b>223,117</b>
<b>Cash flow for investing activities</b>		
Interest received	6,631	1,867
Investment in deposits	(36,828)	(25,000)
Acquisition of a subsidiary consolidated for the first time	-	(14,462)
Investment in investees	-	(796)
Repayment (granting) of long-term loans from others, net	1,698	41
Purchase of securities held for trading	-	(150,000)
Sale of securities held for trading	-	148,362
Purchase of property, plant and equipment	(54,750)	(140,221)
Purchase of intangible assets and deferred expenses	-	(1,789)
<b>Net cash used for investing activities</b>	<b>(83,249)</b>	<b>(181,998)</b>
<b>Cash flow from financing activities</b>		
Short-term credit received, net	101,390	127,668
Receipt (repayment) of deposits from customers, net	(8,589)	989
Interest paid	(11,607)	(85,162)
Proceeds from transactions in derivatives	-	9,259
Repayment of debentures	(5,796)	(104,421)
Repayment of bank loans	(24,650)	(113,825)
Dividends paid	-	(121,325)
<b>Net cash from (used for) financing activities</b>	<b>50,748</b>	<b>(286,817)</b>
Net decrease in cash and cash equivalents	(2,405)	(245,698)
Effect of fluctuations in exchange rate on cash and cash equivalents	172	1,213
Cash and cash equivalents at the beginning of the year	14,840	259,325
<b>Cash and cash equivalents at the end of the year</b>	<b>12,607</b>	<b>14,840</b>

(\*) Reclassified, see Note 2(D)(3)

**The attached notes are an integral part of the condensed consolidated interim financial statements.**

**Oil Refineries Ltd.**

**Condensed Consolidated Interim Statement of Cash Flows (contd.)**  
**USD thousands**

**Appendix A: Adjustments required to present the cash flows from operating activities**

	Three months ended		Year ended
	March 31, 2009	March 31, 2008(*)	December 31, 2008
	(Unaudited)		(Audited)
<b>A. Income and expenses not included in the cash flow:</b>			
Depreciation and amortization	17,842	17,982	75,699
Negative goodwill created upon acquisition	-	-	(14,535)
Financial Expenses, net	(31,307)	46,859	60,998
Changes in fair value of derivatives	2,690	19,315	(10,456)
Changes in the fair value of the loan to Haifa Early Pensions Ltd.	2,891	(8,795)	(6,009)
Share in (profits) losses of equity accounted investees, net of dividends received from investees	(139)	5,070	4,064
Earnings (losses) from deposits and securities held for trading	4,163	(12,350)	13,164
Share-based payment expenses	664	747	3,428
Income tax benefit expenses (revenue)	24,607	(8,000)	(107,292)
	21,411	60,828	19,061
<b>B. Changes in assets and liabilities</b>			
Decrease (increase) in inventory, net	(148,299)	(118,910)	485,795
Decrease (increase) in trade and other receivables	32,020	(96,762)	156,575
Increase (decrease) in trade and other payables, net	60,170	129,426	(335,758)
Increase (decrease) in employee benefits, net	(9,366)	4,081	(8,560)
	(65,475)	(82,165)	298,052

(\*) Reclassified, see Note 2(D)(3)

**The attached notes are an integral part of the condensed consolidated interim financial statements.**

Notes to the Financial Statements  
As of March 31, 2009

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**NOTE 1 – GENERAL**

**A. Reporting entity**

1. Oil Refineries Ltd. (“the Company” or “ORL”) is a company domiciled and incorporated in Israel. The Company is located in the Haifa Bay and its official address is PO Box 4, Haifa 31000, Israel. The Company and its subsidiaries are industrial companies which operate in Israel and are engaged primarily in the production of oil products, feedstock for the petrochemical industry and materials for the plastics industry. The facilities of the subsidiaries are integrated with those of the Company. In addition, the Company provides water treatment and power generation services (primarily electricity and steam) to a number of industries adjacent to the Haifa refinery.
2. Until the date of sale of the Ashdod Oil Refinery, the Company had two operational sites: one in the Haifa Bay area and the other in Ashdod. On September 28, 2006, the Company sold all of its shares in Ashdod Oil Refinery (“ORA”). On February 21, 2007, as part of implementation of the privatization that was decided upon on December 26, 2004, the State sold all the shares it held in Company in a private and public offering. The Israel Corporation Ltd. acquired 36.8% of the Company’s shares and Petroleum Capital Holdings Ltd. (“PCH”) acquired 9.2% of the Company’s shares. Subsequently, the Israel Corporation Ltd. and PCH acquired additional shares, and as of the date of the financial statements, hold 45.08% and 15.76%, respectively.
3. The Group’s condensed consolidated interim financial statements as of March 31, 2009, include the statements of the Company, its subsidiary, and a jointly-owned company (hereinafter together: “the Group”) and the Group’s interests in associates. The Company’s shares are traded on the Tel Aviv Stock Exchange (“TASE”).

**NOTE 2 - BASIS OF PREPARATION**

**A. Statement of compliance**

The condensed consolidated interim financial statements have been prepared in accordance with IAS 34, *Interim Financial Reporting*, and do not include all of the information required for full annual financial statements. They should be read in conjunction with the financial statements for the year ended December 31, 2008. (“the **Annual Report**”). Additionally, these statements were prepared in accordance with Chapter D of the Securities Regulations (Periodic and Immediate Reports) - 1970.

The condensed consolidated interim financial statements were approved by the Company’s Board of Directors on May 17, 2009.

**B. Use of estimates and judgments**

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

The judgment of management, when applying the Group’s accounting policy and the principal assumptions used in assessments that involve uncertainty, are consistent with those used in the annual financial statements.

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

**Oil Refineries Ltd.**

**Notes to the Financial Statements  
As of March 31, 2009**

**NOTE 2 - BASIS OF PREPARATION**

**C. Capital management – objectives, procedures and processes**

Policy of the board of directors and management is consistent with the policy applied in the annual financial statements. The Company and the jointly-controlled company, Carmel Olefins Ltd. (Carmel Olefins) are subject to compliance with financial covenants, including a minimum balance of equity (see Note 8(B) below and Note 16(C) to the annual financial statements).

**D. Reclassified**

**1. Employee benefits for leave**

Employee benefits for leave previously presented under a long-term employee benefits were reclassified as short-term employee benefits (under other payables) in order to adjust their presentation method to the presentation in the financial statements as of March 31, 2009. See also Note 3(1)(C).

	<b>As previously reported</b>	<b>Effect of reclassification</b>	<b>As reported in these financial statements</b>
	<b>December 31, 2008</b>		
Other payables	70,056	915	70,971
Employee benefits	68,845	(915)	67,930
	<b>March 31, 2008</b>		
Other payables	100,690	1,194	101,884
Employee benefits	71,611	(1,194)	70,417

2. The comparative numbers in the statement of comprehensive income for the three months ended March 31, 2008 were reclassified in order to adjust their presentation method to the presentation in the financial statements as of March 31, 2009, as follows:

	<b>Three months ended March 31, 2008</b>		
	<b>As previously reported</b>	<b>Effect of reclassification</b>	<b>As reported in these financial statements</b>
Cost of sales, refinery and services	1,833,520	(9,346)	1,824,174
Revaluation of open transactions in derivatives on prices of goods and margins, net	11,141	9,346	20,487
Financing revenue	69,425	(38,013)	31,412
Financing expenses	(86,097)	38,013	(48,084)

Oil Refineries Ltd.

Notes to the Financial Statements  
As of March 31, 2009

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**NOTE 2 - BASIS OF PREPARATION (CONTD.)**

**D. Reclassified (contd.)**

3. Some of the comparative numbers in the statement of cash flows for the three months ended March 31, 2008 were reclassified in order to adjust their presentation method to the presentation in the statement of cash flows for the three months ended March 31, 2009 and the year ended December 31, 2008.

	<b>Three months ended March 31, 2008</b>		
	<b>As previously reported</b>	<b>Effect of reclassification</b>	<b>As reported in these financial statements</b>
Operating activities	(33,991)	92	(33,899)
Investment activities	(189,253)	(7)	(189,260)
Financing activities	3,433	3,538	6,971
Effect of exchange rate fluctuations on cash and cash equivalents	2,344	(3,623)	(1,279)

Notes to the Financial Statements  
As of March 31, 2009

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**NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES**

Other than the contents of section (1) below, the Group's accounting policy in these condensed consolidated interim statements is the same policy applied in the annual statements.

**(1) Initial application of new Accounting Standards**

The changes made in the accounting policy for the preparation of the condensed consolidated interim financial statements and their effect are described below:

**A. Presentation of financial statements**

Commencing from January 1, 2009, the Group applies IAS 1 – *Presentation of Financial Statements*, revised (“the Standard”). The Standard permits the presentation of one statement of comprehensive income (a statement combining profit or loss and other comprehensive income) or in two statements - a separate income statement and a statement of comprehensive income). The Group opted to present income and expenses and other comprehensive income in one statement of comprehensive income (statement combining profit or loss and other comprehensive income). The Group also presents a statement of changes in equity immediately after the statement of comprehensive income. The statement includes changes in equity arising from transactions with owners in their capacity as owners (such as dividends, transactions with controlling shareholders, share issues and options). The Standard is applied retrospectively.

**B. Segment reporting**

Commencing from January 1, 2009, the Group applies IFRS 8 – *Operating Segments* (“the Standard”). The Standard states that segment reporting shall be in accordance with the “management approach”, namely – in accordance with the format of the internal reports to the Group's decision-makers. Implementation of the Standard did not have an effect on the financial statements of the Group and segment information for prior reporting periods will not be restated.

An operating segment is a part of the Group that meets the three conditions set forth below:

1. The segment engages in business operations that may generate revenue and may incur expenses.
2. The operational results of the segment are reviewed regularly by the decision makers of the Group, in order to make decisions regarding resources to be allocated and to assess its performance.
3. Separate financial information is available.

For additional information, see Note 5 – Operating Segments.

**C. Employee benefits**

Commencing from January 1, 2009, the Group applies IAS 19 – *Employee Benefits*, revised (“the Amendment”), in accordance with Improvements to International Financial Reporting Standards 2008 (Improvements to IFRSs). The Amendment addresses the definition of “short-term employee benefits” and “other long-term employee benefits” to refer to when the benefits are due to be settled. The Amendment is applied retrospectively. Accordingly, Carmel Olefins presents benefits for leave as a short-term employee benefit, measured at the undiscounted amount, which Carmel Olefins expects to pay for exercising this right. For the effect of reclassification on the items in the financial statements, see Note 2(D)(1).

Application of the Amendment, other than the aforesaid, has no effect on the reports.

Notes to the Financial Statements  
As of March 31, 2009

**NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES**

**(2) New standards and interpretations not yet adopted**

In the framework of the *Improvements to IFRS* project, in April 2009 the IASB published and approved 15 amendments to various IFRS on a wide range of accounting issues. The amendments are effective for annual periods beginning on or after January 1, 2010, with an option for early adoption, subject to the terms prescribed for each amendment.

Presented hereunder is the amendment that may be relevant to the Group and is expected to have an effect on the financial statements:

IAS 17 – *Leases: Classification of leases of land and buildings* (revised) (“the Amendment”). The Amendment eliminates the requirement to classify a lease of land as an operating lease when the title is not expected to pass to the lessee at the end of the lease term. Under the Amendment, classification of the land lease should be based on the regular criteria for classifying a lease as a finance or operating lease.

The Amendment also states that when a lease includes both land and building elements, an entity should determine the classification of each element, based on the criteria in the Amendment, taking account of the fact that land normally has an indefinite economic life.

The Amendment is effective for annual financial statements commencing on or after January 1, 2010. Early application of the Amendment is permitted, with disclosure. The Amendment is effective retrospectively, meaning classification of the land lease is determined based on the information available when signing the lease. If there is a change in classification of the lease, the instructions of IAS 17 are effective prospectively from the date of the lease. If, however, information necessary to apply the Amendment retrospectively is not available, classification is determined based on the information available at the adoption date of the Amendment, and the asset and liability related to a land lease that was classified as a finance lease as a result of the Amendment are recognized at their fair values at that date. Any difference between the fair value of the asset and the fair value of the liability is recognized in retained earnings.

The management of the Group is assessing the effect of the Amendment on its financial statements.

**(3) The following table presents information of the dollar exchange rate.**

	As at		
	March 31, 2009	March 31, 2008	December 31, 2008
Representative exchange rate of USD1/NIS	4.188	3.553	3.802
	Three months ended		Year ended
	March 31, 2009	March 31, 2008	December 31, 2008
Change in the dollar exchange rate	10.15%	(7.62)%	(1.14)%

**Notes to the Financial Statements  
As of March 31, 2009**

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**NOTE 4 – SEASONAL FLUCTUATIONS**

The Company manufactures oil products based on standards that change according to the seasons. The standards are intended to ensure that the quality of the products complies with changing environmental conditions, in accordance with seasonal climates.

In addition, there are seasonal fluctuations in consumption of the Company's products which affect the relative prices of the various products.

The abovementioned effect of seasonal fluctuations is relatively small compared to the effect of other factors (such as the condition of the facilities, the Company's general refining capacity, and the viability of refining and competing imports) on the scope of product sales by the Company and on its product mix.

**NOTE 5 – OPERATING SEGMENTS**

The Group has three areas of operations, which are reported as business segments in the Group's financial statements and which are strategic business units. Further to Note 29 to the financial statements as of December 31, 2008, there were no changes in the Group's operating segments set forth below.

These strategic business units are managed separately for the purpose of allocation of resources and assessment of performance.

1. Refining: refining of crude oil and production of fuel products
2. Trade: trade in crude oil and distillates and trade in derivatives on the prices of oil and its products
3. Petrochemicals:
  - Polymers: production of polymer raw materials in the plastics industry
  - Aromatics: production of aromatics and solvents used as raw materials and production of other products

Most trade operations are integrated vertically with operations in the refining segment. The external trade operations are presented as a separate segment commencing from the first quarter in 2008.

**Oil Refineries Ltd.**

**Notes to the Financial Statements  
As of March 31, 2009**

**NOTE 5 – OPERATING SEGMENTS (CONTD.)**

	Refining		Trade		Petrochemicals				Adjustments to consolidated		Consolidated	
					Polymers		Aromatics					
	2009	2008	2009	2008	2009	2008	2009	2008	2009	2008	2009	2008
	<b>Three months ended</b>											
Income from external entities	783,838	1,561,799	58,491	79,000	84,314	107,646	57,715	137,251	-	-	984,358	1,885,696
Income from sales between segments	86,184	186,798	-	-	-	-	8,602	11,645	(94,786)	(198,443)	-	-
Income from the segment	870,022	1,748,597	58,491	79,000	84,314	107,646	66,317	148,896	(94,786)	(198,443)	984,358	1,885,696
Operating profit (loss)	72,078	5,273	363	2,000	1,946	(1,010)	5,855	9,338	-	234	80,242	15,835
Financing revenue											58,772	31,412
Financing expenses											(44,407)	(48,084)
Financing income (expenses), net											14,365	(16,672)
Company's share in profits (losses) of associates (net of tax)											4,591	(5,070)
Profit (loss) before taxes on income											99,198	(5,907)

**Oil Refineries Ltd.**

**Notes to the Financial Statements  
As of March 31, 2009**

**NOTE 5 – OPERATING SEGMENTS (CONTD.)**

	<b>Petrochemicals</b>				<b>Adjustments to consolidated</b>	<b>Consolidated</b>
	<b>Refining</b>	<b>Trade</b>	<b>Polymers</b>	<b>Aromatics</b>		
<b>Year ended December 31, 2008</b>						
<b>(Audited)</b>						
Income from external entities	6,911,565	383,291	475,193	487,409	-	8,257,458
Income from sales between segments	706,988	-	-	57,033	(764,021)	-
Income from the segment	7,618,553	383,291	475,193	544,442	(764,021)	8,257,458
Operating profit (loss)	(121,381)	11,379	(51,698)	7,834	1,532	(152,334)
Financing revenue						64,979
Financing expenses						(126,034)
Financing expenses, net						(61,055)
Company's share in profits (losses) of associates (net of tax)						(3,111)
Loss before taxes on income						(216,500)

**NOTE 6 – PROPERTY, PLANT AND EQUIPMENT**

As of the date of the financial statements, the balance of agreements for approved establishment works amounts to \$104 million.

As of March 31, 2009, property, plant and equipment include advance payments made by the Group on account of the purchase of property, plant and equipment in the amount of \$41 million.

Notes to the Financial Statements  
As of March 31, 2009

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**NOTE 7 – CONTINGENT LIABILITIES AND AGREEMENTS**

**A. Lawsuits**

1. Further to Note 20(B), sections 2(a), 2(b), 2(e), 3, 7, 15, 16 and 17 to the financial statements and Note 34(B) to the financial statements as of December 31, 2008, suits have been filed against the Group for physical injury and damage to property allegedly incurred to the plaintiffs as a result of pollution of the Kishon River. There are legal proceedings against the Group, laws have been enacted and orders have been issued regarding the fuel and gas sector and the infrastructure facilities pertaining to the Group. Based on the opinion of the legal counsels of the Company and its subsidiaries, the Company estimates that, at this stage, it is not possible to assess the aforementioned impact on the financial statements as of March 31, 2009, if any exists, and therefore, no provision regarding this matter was included in the financial statements.
2. Further to Note 20 and Note 34(B) to the financial statements as of December 31, 2008, during the reporting period, there were no significant changes in the lawsuits and contingent liabilities of the Group, other than those described in Note 8 below

**B. Agreements**

To maintain the operations of the Company, the Company is dependent upon services from the infrastructure companies, PEI and EAPC, which own crucial infrastructure pertaining to the unloading, shipping, storage, and production of crude oil and distillates. In the first half of 2009, PEI is expected to carry out reinforcement works on the offshore pipeline used to unload crude oil in Haifa bay, subject to approvals by the competent authorities.

**NOTE 8 – MATERIAL EVENTS IN THE REPORTING PERIOD**

- A.** In January 2009, the Company and Gadiv received from the Ministry of Environmental Protection a warning and summons to a hearing relating to violations and alleged defective application of the provisions of the personal order ("the warning"). The warning described the alleged violations which referred, inter alia, to the timetables set forth in the order, the results of the stack samples, the submission of certain plans stipulated in the personal order and to the way information is sent to the Ministry, as stipulated in the order.

Prior to the date of the hearing, the Company and Gadiv submitted their responses to the warning received. In the response, they detailed their arguments and responses to the issues included in the warning. At the conclusion of the hearing, goals and timetables were set for actions to be taken by the Company to reduce the pollution emitted by its facilities. The Company is preparing to implement the mandatory actions under the personal orders and is holding discussions with the Ministry of Environmental Protection regarding additional actions that the Ministry requires.

On January 25, 2009, a hearing was held at the Ministry of Environmental Protection for the Company and PEI regarding two specific sites where, according to the Ministry, soil and groundwater were contaminated by fuel products. After the hearing, the Company and PEI were required to close the two pipelines along which leakage was found; to return them to operation following repair and/or replacement; to test impermeability of all the pipelines and to submit the results to the Ministry of Environmental Protection. In the hearing, the Company and PEI were warned that if the repair and rehabilitation process does not commence within seven days after the hearing, including the removal of the contaminated soil, the Ministry would issue an order for cleanup and removal of the toxic substances. The Ministry gave notice that the Green Police of the Ministry of Environmental Protection would investigate the events, including the Company's failure to act to minimize damage and prevent further contamination of the river and its environs.

Notes to the Financial Statements  
As of March 31, 2009

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**NOTE 8 – MATERIAL EVENTS IN THE REPORTING PERIOD (CONTD.)**

**A.** (contd.)

On March, 1, 2009, the Company received a removal order for toxic substances, pursuant to section 16(A) of the Hazardous Substances Law - 1993 and a clean-up order, pursuant to section 13(B) of the Maintenance of Cleanliness Law - 1984, demanding that the Company, PEI and their CEOs submit plans to the Ministry of Environmental Protection for soil gas, soil and groundwater surveys and to fence off the contaminated areas and conduct the survey in accordance with the approved plans. The parties are further required to submit to the Ministry a report of the survey findings, including recommendations for the clean-up and rehabilitation of the contaminated soil and groundwater and the restoration of the river and its banks to their former condition, based on the findings of the survey. The parties will also define a short-term and binding timetable for implementing the recommendations of the survey, until all waste and toxins are removed from the soil and groundwater.

The Company has submitted its plan for the soil gas, soil and groundwater survey to the Ministry of Environmental Protection for approval and it is carrying out the survey in accordance with the plan.

As of the reporting date, the Company is unable to assess the outcome of the survey, the actions required according to the outcome and the expenses arising for the Company when implementing these measures.

At the beginning of 2009, the Company and EAPC were required, under the terms added to their business licenses, to conduct soil surveys along the pipeline corridor and to apply the survey recommendations according to the suggested timetable approved by the Ministry of Environmental Protection. The Company appealed this condition in its business license through the procedure set up by the law. The Ministry of Environmental Protection has not yet responded to the appeal and the Company cannot estimate whether it will be required to implement the additional term and the expense required to implement the term. The Company and the Ministry agreed that until the court hearing, the Company will not carry out the required survey.

**B. Financial position of Carmel Olefins**

1. As reflected in the financial statements of Carmel Olefins as of March 31, 2009, Carmel Olefins has an operating capital deficit of \$253 million. The deficit is mainly due to reclassification of long-term loans of \$230 million to short-term as a result of non-compliance with the financial covenants set with the banks.
2. Carmel Olefins is currently negotiating with the banks to reach a settlement by which new covenants will be set and/or it will receive deeds of waiver. Carmel Olefins is in advanced stages of negotiations with the banks. The banks set requirements from Carmel Olefins and its shareholders. Carmel Olefins and its shareholders have accepted most of the bank's requirements, therefore Carmel Olefins hopes to receive the deeds of waiver from the banks within the next few weeks.

**Notes to the Financial Statements  
As of March 31, 2009**

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**NOTE 9 – MATERIAL EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE**

- A.** On April 23, 2009, Maalot S&P (Maalot) announced that the rating of the Company's debentures (non-negotiable series and negotiable series A-C) has been placed on CreditWatch Negative. due to its assessment of the possible consequences of uncertainty regarding the refining industry in the medium term and its impact on the Company's cash flows, uncertainty connected with financing the investment plan and the resulting debt and uncertainty regarding the timing of the acquisition of Carmel Olefins, including the consequences for the Company should Carmel Olefins fail to meet the financial covenants and the changes in the structure of ownership and core control and the possible acquisition of Carmel Olefins.
- B.** On May 7, 2009, IPE announced that it had received a control permit. On that date, the Company received notice from the Government Companies Authority regarding this control permit. The control permit sets forth the requirements for the operation of IPE and PCH under the control permit, to be fulfilled within 30 days: the validation or the complete fulfillment of the series of agreements signed between Mogdal Ltd. and Mogdal Industries (99) Ltd. and Charabancs Investment N.V; and the validation of the joint control agreement between IPE and PCH and the Israel Corporation Ltd. The Government Companies Authority further announced that it would notify the Company when the conditions exist to allow IPE and PCH to operate under the control permit.

On May 7, 2009, IPE issued an immediate report announcing that Modgal Ltd. and Mogdal Industries (99) Ltd. had informed IPE of the validation and complete fulfillment of the series of agreements signed between them and Charabanc N.V. and that all the terms for the validation of the joint control agreement between IPE and PCH and the Israel Corporation Ltd. had been met. In addition, IPE announced that it had decided that it would not exercise, and would act that PCH would not exercise the call options given to PCH in accordance with the provisions of the joint control agreement.

Management of the Group is assessing the implications of the aforesaid on the financial statements.

- C.** On April 23, 2009, Carmel Olefins signed an agreement for the purchase of feedstocks from ORL. The agreement included terms for the purchase of 60,000 tons of propylene per year, which ORL undertook to sell to Carmel Olefins under the obligations that were assigned in the split of the refineries, and terms for the purchase of at least 40,500 tons of 4C per year. The agreement is valid for 10 years commencing from January 1, 2009, subject to the rights of the parties to terminate the agreement earlier in accordance with the provisions in the agreement.