

SCAILEX CORPORATION LTD.
(Formerly SCITEX CORPORATION LTD.)

2006 CONSOLIDATED FINANCIAL STATEMENTS

SCAILEX CORPORATION LTD.
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The amounts are stated in U.S. dollars (\$).

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders of

SCAILEX CORPORATION LTD.

We have audited the consolidated balance sheets of Scailex Corporation Ltd. (the "Company") and its subsidiaries as of December 31, 2006 and 2005 and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of an associated company, the Company's share in losses of which is \$1,418,000 in 2004. Those financial statements were audited by other independent registered public accounting firm whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for this company, is based solely on the report of the other independent registered public accounting firm.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Company's Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of the other independent registered public accounting firm provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of the other independent registered public accounting firm, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2006 and 2005 and the consolidated results of operations and cash flows for each of the three years in the period ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 1 to the consolidated financial statements, the Company changed the manner in which it accounts for share-based compensation effective January 1, 2006 to conform with FASB Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment".

Tel-Aviv, Israel
June 17, 2007

Kesselman & Kesselman
Certified Public Accountants (Isr.)

SCAILEX CORPORATION LTD.
CONSOLIDATED BALANCE SHEETS

	December 31	
	2006	2005
	U.S. dollars in thousands	
A s s e t s		
CURRENT ASSETS:		
Cash and cash equivalents	227,461	199,762
Available for sale securities	14,258	19,455
Current maturities of securities held-to-maturity	21,991	11,133
Other receivables	713	568
Deferred income taxes		1,260
Current assets of discontinued operations	31,764	86,522
T o t a l current assets	296,187	318,700
 INVESTMENTS AND OTHER NON-CURRENT ASSETS:		
Securities held-to-maturity	22,879	29,524
Other investments and prepaid expenses	404	1,529
Funds in respect of employee rights upon retirement	90	61
	23,373	31,114
PROPERTY AND EQUIPMENT , net of accumulated depreciation (note 4)	12	9
NON-CURRENT ASSETS OF DISCONTINUED OPERATIONS		1,195
	319,572	351,018

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Eran Schwartz) **Chairman of the Board of Directors**

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Yahel Shachar) **Chief Executive Officer**

	December 31	
	2006	2005
	U.S. dollars in thousands	
Liabilities and shareholders' equity		
CURRENT LIABILITIES:		
Trade payables	77	73
Income taxes payable	1,055	660
Accrued and other liabilities	988	1,142
Current liabilities related to discontinued operations	20,382	44,443
T o t a l current liabilities	22,502	46,318
LONG-TERM LIABILITIES:		
Liability for employee rights upon retirement (note 5)	176	107
Long-term liabilities related to discontinued operations		1,800
T o t a l long-term liabilities	176	1,907
COMMITMENTS AND CONTINGENT LIABILITIES (note 6)		
T o t a l liabilities	22,678	48,225
MINORITY INTEREST		
	11,860	41,190
SHAREHOLDERS' EQUITY (note 7):		
Share capital - ordinary shares of NIS 0.12 par value (authorized: December 31, 2006 and 2005 - 48,000,000 shares; issued and outstanding: December 31, 2006 and 2005 - 43,467,388 shares)	6,205	6,205
Capital surplus	280,637	280,269
Accumulated other comprehensive loss	(590)	(1,110)
Retained earnings	31,082	8,539
Treasury shares, at cost (December 31, 2006 and 2005 - 5,401,025 shares)	(32,300)	(32,300)
T o t a l shareholders' equity	285,034	261,603
	319,572	351,018

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

SCAILEX CORPORATION LTD.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year ended December 31		
	2006	2005	2004
U.S. dollars in thousands (except per share data)			
GENERAL AND ADMINISTRATIVE EXPENSES	(2,955)	(2,964)	(3,201)
FINANCIAL INCOME, net	13,202	4,283	2,757
OTHER INCOME, net	3,141	917	62
INCOME (LOSS) BEFORE TAXES ON INCOME	13,388	2,236	(382)
INCOME TAX BENEFITS (TAXES ON INCOME) (note 8)	(1,502)	94	1,121
SHARE IN RESULTS OF ASSOCIATED COMPANY (including gain from sale of the associated company in 2005 of \$ 2,981)		2,876	(1,418)
MINORITY INTEREST IN INCOME OF A SUBSIDIARY	(478)		
NET INCOME (LOSS) FROM CONTINUING OPERATIONS	11,408	5,206	(679)
NET INCOME FROM DISCONTINUED OPERATIONS, net of taxes and minority interests	11,135	100,932	47,932
NET INCOME	<u>22,543</u>	<u>106,138</u>	<u>47,253</u>
EARNING (LOSS) PER SHARE (“EPS”) - BASIC:			
Continuing operations	0.30	0.14	(0.02)
Discontinued operations	0.29	2.65	1.19
	<u>0.59</u>	<u>2.79</u>	<u>1.17</u>
“EPS” - DILUTED:			
Continuing operations	0.30	0.14	(0.02)
Discontinued operations	0.29	2.55	1.19
	<u>0.59</u>	<u>2.69</u>	<u>1.17</u>
WEIGHTED AVERAGE NUMBER OF SHARES USED IN COMPUTATION OF EPS (in thousands):			
Basic	38,066	38,066	40,336
Diluted	<u>38,156</u>	<u>38,134</u>	<u>40,336</u>

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

SCAILEX CORPORATION LTD.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Share capital	Capital surplus	Accumulated other comprehensive loss	Retained earnings (Accumulated deficit)	Treasury shares	Total shareholders' equity
	U.S. dollars in thousands					
BALANCE AT JANUARY 1, 2004	6,205	368,104	(552)	(144,852)	(4,207)	224,698
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2004:						
Net income				47,253		47,253
Other comprehensive income (loss), in respect of:						
Available-for-sale securities, net			(327)			(327)
Realization of currency translation adjustments			552			552
Total comprehensive income						47,478
Cash distribution		(89,837)				(89,837)
Stock - based compensation from options granted to employees		28				28
Treasury shares					(28,093)	(28,093)
BALANCE AT DECEMBER 31, 2004	6,205	278,295	(327)	(97,599)	(32,300)	154,274
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2005:						
Net income				106,138		106,138
Other comprehensive loss, in respect of:						
Available-for-sale securities, net			(783)			(783)
Total comprehensive income						105,355
Stock -based compensation from options granted to employees		1,974				1,974
BALANCE AT DECEMBER 31, 2005	6,205	280,269	(1,110)	8,539	(32,300)	261,603
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2006:						
Net income				22,543		22,543
Other comprehensive income, in respect of:						
Available-for-sale securities, net			183			183
Held-to-maturity securities amortization			337			337
Total comprehensive income						23,603
Payment made by shareholders to senior employees		274				274
Stock - based compensation from options granted to employees		94				94
BALANCE AT DECEMBER 31, 2006	6,205	280,637	(590)	31,082	(32,300)	285,034

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

SCAILEX CORPORATION LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income from operations	22,543	106,138	47,253
Adjustments to reconcile net income from operations to net cash provided by (used in) operating activities:			
Income and expenses not involving cash flows:			
Gain from sale/Share in results of associated companies, net		(3,668)	1,418
Minority interest in profits of a subsidiary	478		
Depreciation	3	4	8
Amortization of deferred stock compensation	94	20	20
Gain from issuance of shares by an associated company			(137)
Write-down of investment in investee companies	660		137
Accrued severance pay, net	40	4	33
Deferred income taxes, net	1,260	(551)	(709)
Payment made by shareholders to senior employees	274		
Loss from sale of available-for-sale securities	288	59	70
Loss from sale of securities held-to-maturity	243		
Gain from sale of investment at cost	(1,327)		
Bonds interests Income, net	(29)		
Capital gain from dividend paid by investment at cost	(1,800)		
Changes in operating asset and liability items:			
Decrease (Increase) in other receivables	(145)	277	189
Increase (decrease) in accounts payable and accruals	245	540	(227)
Changes in asset and liability items of discontinued operations	1,848	(75,905)	(58,359)
Net cash provided by (used in) operating activities	<u>24,675</u>	<u>26,918</u>	<u>(10,304)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Acquisition of available for sale securities		(13,233)	(98,198)
Acquisition of held to maturity marketable securities	(18,998)		
Proceeds from sale of available-for-sale securities	5,000	8,972	49,034
Maturity of securities held-to-maturity	15,000		
Proceeds from sale of cost method investment	1,327		
Purchase of fixed assets	(6)	(11)	
Proceeds from sale of investments in discontinued operations		199,164	230,418
Proceeds from disposal of associated company		3,000	
Distribution of funds from cost method investment	2,890	1,006	
Investment in associated companies and cost method investments	(625)	(325)	(594)
Net cash used in discontinued operations	(5,019)	(13,974)	(7,497)
Net cash provided by (used in) investing activities	<u>(431)</u>	<u>184,599</u>	<u>173,163</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Purchase of treasury shares			(28,093)
Cash distribution			(89,837)
Net cash used in discontinued operations	(34,180)	(43,154)	(15,798)
Net cash used in financing activities	<u>(34,180)</u>	<u>(43,154)</u>	<u>(133,728)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(9,936)	168,363	29,131
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>254,255*</u>	<u>85,892</u>	<u>56,761</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>244,319*</u>	<u>254,255*</u>	<u>85,892</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Income taxes paid net of refunds	<u>2,633</u>	<u>123</u>	<u>6,137</u>

* Cash and cash equivalents includes cash and cash equivalents classified on the Company's balance sheet under "Current assets of discontinued operations" of \$16,858,000 and \$54,493,000, on December 31, 2006 and 2005, respectively.

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

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - GENERAL:

a. Nature of operations

Continuing operation:

Scailex Corporation Ltd. (the "Company") is a public company that is incorporated in Israel, and its shares are traded on the Tel Aviv Stock Exchange ("TASE") and are quoted on the OTC Bulletin Board ("OTCBB") in the United States. Through September 18, 2006, the Company's shares were traded in the NASDAQ Global Market ("NASDAQ"). On September 18, 2006, the SEC suspended the trading of Company shares on NASDAQ, and on October 23, 2006, the Company's shares were de-listed from NASDAQ because the Company was determined by Nasdaq to be a public shell lacking any business operations, pursuant to Marketplace Rule 4300. As from August 2006, the Company operates in one business sector – the management of the Company's assets and the identification of investments.

Amounts provided in these notes to the consolidated financial statements pertain to continuing operations, unless otherwise indicated.

b. Discontinued operations:

In the past, the Company operated, directly and through its subsidiaries (the "Group"), in three business segments, which have been sold over the course of the last three years. Consequently, operating results of these three segments have been reported in these financial statements as discontinued operations in accordance with SFAS 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144) and the Company has reclassified its results of operations, and the related assets and liabilities and cash flows for the prior periods in accordance with provisions of FAS 144.

The Company has revised the 2005 statements of cash flows to exclude cash and cash equivalents, attributable to discontinued operations, from the line item "Net cash provided by (used in) discontinued operation" Such amounts are now included in "cash and cash equivalents at beginning of the year" and "cash and cash equivalents at end of year."

Following is information on the businesses sold:

1) High-Speed Digital Printing segment

On January 5, 2004, the Company completed the sale of substantially all of the assets, liabilities and operations of its indirect wholly-owned subsidiary Scailex Digital Printing Inc. ("SDP") related to its High-Speed Digital Printing Business, including most of the distribution channels that served SDP, to Eastman Kodak Company ("Kodak"), for \$ 250 million in cash (in addition \$12 million was retained at SDP following the transaction). Pursuant to the agreement, a \$25 million was held in escrow, of which (1) \$15 million was released in February 2004 (2) \$5 million was released in January 2005 and (3) the remaining \$5 million was released in January 2006, in accordance with the applicable terms of the agreement. As a result of the transaction, the Company recorded a net gain of approximately \$60 million, of which approximately \$52 million was included in the statement of operations in 2004, and approximately \$8 million of which was recognized in the fourth quarter of 2003 as a tax benefit related to expected utilization of carryforward tax losses including capital losses and is recorded under "income from discontinued operation".

In December 2004, following the conclusion of tax audit by the Internal Revenue Services (IRS) in the consolidated companies SDP and SDC, for the years 1992 to 1996, the Company filed an application for refunds of federal taxation in respect of amended tax reports for the years 1994, 1995 and 1997.

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - GENERAL (continued):

In the year 2005, the Company recorded tax income in respect of the tax refunds as aforesaid, in the amount of \$7.8 million. In July 2006, the Company received the tax refunds, as aforesaid, in the amount of \$12.6 million and as a result, it recorded further tax income in the amount of \$4.8 million. The tax income has been recorded under “income from discontinued operations”,

On July 2006, SDP’s parent company (a wholly owned subsidiary of the Company) and SDP (which are registered in the State of Massachusetts in the USA) were liquidated.

The current assets and liabilities of SDP classified as discontinued operation in the Consolidated Balance Sheets, are as follows:

	Year ended December 31	
	2006	2005
	U.S. dollars in thousands	
A s s e t s		
Cash allocated for Federal income tax payable and restricted deposit	9,506	5,450
Federal Income tax receivable, net		7,800
T o t a l assets	9,506	13,250
L i a b i l i t i e s		
Other payables (mainly income tax payable)	9,506	13,250
T o t a l liabilities	9,506	13,250

Net income from the discontinued operations of SDP is as follow:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
General and administrative expenses			1,052
Other income , net	93	966	51,646
Income tax benefit	4,614	7,800	
Net income for the year	4,707	8,766	50,594

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - GENERAL (continued):

2) Wide Format Digital Printing Segment

On November 1, 2005, the Company completed the sale of substantially all of the assets and the liabilities of the business of Scailex Vision (Tel-Aviv) Ltd ("Scailex Vision"). (formerly Scitex Vision Ltd.), a majority-owned subsidiary of the Company, to Hewlett-Packard Company ("HP"). Under the terms of the agreement, HP paid approximately \$230 million in cash to Scailex Vision (subject to certain adjustments under the agreement), of which \$23 million is retained in escrow for 24 months to cover possible indemnification claims and \$1 million was retained for 12 months to cover possible tax payments related to 2005. The amount of \$1 million was released to Scailex Vision account on November 10, 2006. As a result, the company recognized during 2005, a net income of approximately \$92 million from discontinued operations. In addition, the Company has agreed to assign its rights to the "Scitex" trade name to HP, and has agreed to change its corporate name (accordingly the Company changed its name to Scailex Corporation Ltd.). In April 2006, HP paid Scailex Vision an additional amount of approximately \$6.6 million in respect of the adjustment of the purchase price, as determined in accordance with the sale agreement. As a result of this additional consideration, the Company recognized an additional gain in the amount of \$2.8 million (net of minority and related tax payments) under gain from discontinued operations in the statement of income for the year ended December 31, 2006. On October 27, 2006, HP presented a claim to the trustee to receive an amount of \$5.26 million out of the \$23 million that was deposited in escrow to cover for possible claims for indemnification within the framework of the sale agreement. In the claim, HP claimed that it is entitled to the said indemnity since Scailex Vision was in breach of representations and commitments in the sale agreement. Scailex Vision has rejected these claims and has filed its objection with the trustee. Nevertheless, there is no certainty that Scailex Vision will succeed in defending its position and, in such a case, the trustee will be bound to transfer the said amount to HP. In the Company's opinion, sufficient provision has been made to cover the expenses in respect of this claim in the event that it will be realized. After balance sheet date, HP notified the Company that there were a number of additional legal claims that it intended to serve on the trusteeship. In the Company's opinion, there are sufficient provisions to cover these claims.

On February 9, 2006, Scailex Vision distributed cash dividend equivalent to the amount available for distribution, following the conclusion of the transaction for the sale of the assets to HP. The amount of the net accumulated dividend that was distributed amounted to approximately \$135 million (of which \$101 million was received by the Company), by the way of the payment of \$0.80 per share to each of the shareholders and \$0.39 per option warrant to each of the holders of the option warrants (constituting the net amount less the exercise price).

After balance sheet date, and with the Court's consent, Scailex Vision distributed to its shareholders an additional dividend of \$20 million (out of which \$14.3 million was received by the Company).

At December 31, 2006 and 2005, the remaining cash and assets classified as discontinued operations are estimated to be used for future payment of the related liabilities of the discontinued operations. At December 31, 2006 and 2005, the remaining liabilities classified as discontinued operation represent liabilities for payments of transaction expenses and related taxes.

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - GENERAL (continued):

After balance sheet date, on January 23, 2007 Scailex Vision and Scailex Vision International Ltd. (a wholly owned subsidiary of Scailex Vision) signed tax assessment agreements with the Israeli Tax Authorities, for tax years 2001- 2005. As a result of the assessments the Company recorded a gain from the reduction of tax provisions in the amount of \$3.1 million under discontinued operations.

The assets and liabilities of Scailex Vision classified as discontinued operation in the Consolidated Balance Sheets, are as follows:

	December 31	
	2006	2005
	U.S. dollars in thousands	
A s s e t s		
Current assets:		
Cash	7,352	53,905
Other receivables	14,906	19,049
T o t a l current assets	<u>22,258</u>	<u>72,954</u>
L i a b i l i t i e s		
Current liabilities	10,876	30,572
Long-term liabilities net of current maturities		1,192
	<u>10,876</u>	<u>31,764</u>
Minority interest in discontinued operation	11,382	41,190
T o t a l liabilities	<u>22,258</u>	<u>72,954</u>

Revenues and net income from the discontinued operations of Scailex Vision are as follow:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
Revenues		126,964	128,186
Cost of revenues		<u>73,778</u>	<u>69,165</u>
Gross profit		53,186	59,021
Operation expenses		<u>40,797</u>	<u>50,037</u>
Operating income		12,389	8,984
Financial expense, net	(131)	(506)	(3,449)
Other income, net	<u>3,877</u>	<u>123,049</u>	<u>212</u>
Income before taxes on income	3,746	134,932	5,747
Income tax benefit (Taxes on income)	<u>4,379</u>	<u>(963)</u>	<u>(1,054)</u>
	8,125	133,969	4,693
Minority interests in income of discontinued operation	<u>(2,370)</u>	<u>(37,334)</u>	<u>(3,918)</u>
Net income	<u>5,755</u>	<u>96,635</u>	<u>775</u>

In 2006 and 2005, the Company recognized a gain of \$2.8 million and \$92.3 million respectively on the said sale (net of minority interest and related taxes).

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - GENERAL (continued):

3) The Continuous Ink-Jet Digital Printing for Industrial Applications segment

On August 4, 2006, an agreement was signed by the Company and the senior management of Jemtex InkJet Printing Ltd. ("Jemtex"), according to which the Company transferred the major part of its holdings in Jemtex to two of Jemtex's senior managers and as a result thereof the Company's percentage of holding in Jemtex was reduced from approximately 75% to approximately 15%.

Within the framework of the reorganization agreement, the Company converted convertible loans in the amount of approximately \$6.7 million, out of the total amount of the loans that were provided to Jemtex by the Company over the years in the amount of approximately \$9.7 million, into shares in Jemtex. The balance of the loans in an amount of \$3 million was repayable over a period of 5 to 7 years, in accordance with the terms of the sale agreement, unless the Company was paid an amount of \$1 million by January 4, 2007. In that case, the said payment will be considered to be a full repayment of all of the loans. In addition, so long as the balance of the loans in the amount of \$3 million remains outstanding, the Company will have an option to purchase additional shares in Jemtex, for an overall consideration of \$5 million, according to a valuation of Jemtex at \$20 million. Management estimates the value of this option to be de-minimis.

The Company does not recognize the balance of the said loans as an asset, since Jemtex has no repayment capacity as of December 31, 2006. In January 2007, Jemtex entered into an investment agreement with a third party under which Jemtex repaid the Company \$1 million, and as a result thereof, the Company regarded the loan as fully repaid. In the framework of the investment, certain terms of said reorganization agreement were also amended. See also note 11a.

Subsequent to the aforementioned sale agreement and the reduction in the percentage of holding, the Company discontinued the consolidation of the financial statements of Jemtex and Jemtex's activities have been classified as discontinued operations.

The assets and liabilities of Jemtex classified as discontinued operation in the Consolidated Balance Sheets are as follows:

	December 31, 2005
	U.S. dollars in thousands
A s s e t s	
Current assets:	
Cash	303
Trade and other receivables	15
T o t a l current assets	318
None current assets	1,195
T o t a l assets	1,513
Liabilities	
Current liabilities	621
Long-term liabilities - employee rights upon retirement	608
T o t a l liabilities	1,229

SCAILEX CORPORATION LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - GENERAL (continued):

Net loss from the discontinued operations of Jemtex is as follows:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
Research & development expenses	1,235	2,549	2,168
Marketing expenses	31	55	51
Administrative and general expenses	278	660	556
Amortization of intangible assets	722	1,215	1,215
Other Income			(586)
Financing expenses (income)	17	(10)	33
Net loss	<u>2,283</u>	<u>4,469</u>	<u>3,437</u>

4) Other income from discontinued operations

In the year ended December 31, 2006, the Company recorded an income of \$3 million from discontinued operation, which was sold in the year 2000 due to beneficial final tax assessments.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES:**a. General:**

1) Risk factors and concentration

As of December 31, 2006, the Company and its subsidiaries are subject to various risks, including but not limited to: (i) business and industry risks like diversification of the business and uncertainty as to a prospective business model of the Company; changes in domestic and foreign economic and market conditions and classification as investment company under US securities laws; (ii) financial risks such as currency fluctuations, credit risks, decreases in the value of its financial investments and classification as a passive foreign investment company for US tax law purpose; and (iii) risks related to operations in Israel like political, economic and military instability in Israel or the Middle East. See also note 9 for financial instruments and other risks.

2) Functional currency

The U.S. dollar is the functional currency for the Company and its subsidiaries. Monetary accounts maintained in currencies other than the U.S. dollar (principally cash and liabilities) are remeasured using the representative foreign exchange rate at the balance sheet date. Operational accounts and non monetary balance sheet accounts are measured and recorded at the rate in effect at the date of the transaction. The effects of foreign currency remeasurement are reported in current operations and have not been material to date.

SCAILEX CORPORATION LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

3) Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting years. Actual results could differ from those estimates.

4) Accounting principles

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America

b. Principles of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. Intercompany balances and transactions have been eliminated in consolidation.

c. Cash equivalents

The Company and its subsidiaries consider all highly liquid investments, with an original maturity of three months or less at time of investment, that are not restricted as to withdrawal or use, to be cash equivalents.

d. Investments in marketable securities

Pursuant to SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities", part of the Company's investments in marketable securities has been designated as held to maturity and part of it has been classified as available-for-sale.

Investments classified as available-for-sale are reported at fair value with unrealized gains and losses, net of related tax, recorded as a separate component of comprehensive income in shareholders' equity until realized. Interest and amortization of premiums and discounts for debt securities and gains and losses on securities sold are included in financial income. For all investment securities, unrealized losses that are other than temporary are recognized in net income.

In the fourth quarter of 2005, the Company decided to hold some securities to maturity and changed some of the classifications to held-to-maturity in accordance with the policy of the Company, the unrealized holding gain or loss at the date of the change in classification continues to be reported as a separate component of comprehensive income in shareholders' equity, but is being amortized over the remaining life of the security as an adjustment of yield.

Investment in marketable securities - which are to be held to maturity - are stated at amortized cost with the addition of computed interest accrued as of the balance sheet date (such interest represents the computed yield on cost from acquisition to maturity). Interest and amortization of premium or discount for those debt securities are carried to financial income or expenses.

SCAILEX CORPORATION LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

e. Other non-current investments

These investments are carried at cost, net of write-down for decrease in value, which is not of a temporary nature.

f. Investments in associated companies

Associated companies are companies over which significant influence is exercised, but which are not consolidated subsidiaries, and are accounted for by the equity method, net of write-down for decrease in value, which is not of a temporary nature. The excess of cost of investment in associated companies over the Company's share in their net assets at date of acquisition ("excess of cost of investment") represents amounts attributed to know-how and technology. The excess of cost of investment is amortized over a period of 5 years, commencing in the year of acquisition.

g. Property and equipment

Property and equipment are carried at cost and are depreciated by the straight-line method over their estimated useful life.

Annual rates of depreciation are as follows:

	<u>%</u>
Equipment	7-20
Computers	33

h. Intangible assets

Intangible assets which consist of technology are presented at cost in discontinued operations and are amortized by the straight-line method over the estimated useful life of 5 years.

i. Impairment of long-lived assets

FAS 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" ("FAS 144"), requires that long-lived assets including certain intangible assets, to be held and used by an entity be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. Under FAS 144, if the sum of the expected future cash flows (undiscounted and without interest charges) of the long-lived assets is less than the carrying amount of such assets, an impairment loss would be recognized, and the assets would be written down to their estimated fair values.

j. Deferred income taxes

Deferred taxes are determined utilizing the asset and liability method based on the estimated future tax effects of differences between the financial accounting and tax bases of assets and liabilities under the applicable tax laws. Deferred income tax provisions and benefits are based on the changes in the deferred tax asset or tax liability from period to period. Valuation allowances are provided for deferred tax assets when it is more likely than not that all or a portion of the deferred tax assets will not be realized. The Company may incur an additional tax liability in the event of an intercompany dividend distribution by non-Israeli subsidiaries.

SCAILEX CORPORATION LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

k. Comprehensive income (loss)

SFAS No. 130, "Reporting Comprehensive Income" ("SFAS No. 130"), establishes standards for the reporting and presentation of comprehensive income, its components and accumulated balances in a full set of general purpose financial statements.

The Company's component of comprehensive income (loss), in addition to the loss for the year, includes unrealized gains and losses on available-for-sale securities and currency translation adjustments of non-dollar currency financial statements of a subsidiary.

l. Treasury shares

Company's shares held by the Company, are presented as a reduction of shareholders' equity, at their cost to the Company.

m. Stock based compensation

Prior to January 1, 2006, the Company accounted for employees' stock-based compensation under the intrinsic value model in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations. In accordance with SFAS No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123"), as amended by SFAS No. 148, "Accounting for Stock-Based Compensation—Transition and Disclosure," the Company disclosed pro forma information, assuming the Company had accounted for employees' stock-based compensation using the fair value-based method defined in SFAS 123.

Effective January 1, 2006, the Company adopted SFAS No. 123 (revised 2004), "Share-based Payment" ("SFAS 123(R)"). SFAS 123(R) supersedes APB 25 and related interpretations and amends SFAS No. 95, "Statement of Cash Flows." SFAS 123(R) requires that awards classified as equity awards be accounted for using the grant-date fair value method. The fair value of stock options is determined based on the number of shares granted and the price of the Company's common stock, and determined based on the Black&Scholes option-pricing models, net of estimated forfeitures. The Company estimated forfeitures based on historical experience and anticipated future conditions.

In March 2005, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 107 ("SAB 107"). SAB 107 provides supplemental implementation guidance on SFAS 123(R), including guidance on valuation methods, inventory capitalization of stock-based compensation cost, income statement effects, disclosures and other issues. SAB 107 requires stock-based compensation to be classified in the same expense line items as cash compensation. The Company has applied the provisions of SAB 107 in its adoption of SFAS 123(R)..

The Company elected to recognize compensation cost for option granted with service conditions that has a graded vesting schedule using the graded vesting attribution method.

SCAILEX CORPORATION LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

The Company elected to adopt the modified prospective transition method permitted by SFAS 123(R). Under this transition method, the Company implemented SFAS 123(R) as of the first quarter of 2006 with no restatement of prior periods. The valuation provisions of SFAS 123(R) apply to new awards and to awards modified, repurchased or cancelled after January 1, 2006. Additionally, compensation cost for the portion of awards for which the requisite service has not been rendered that are outstanding as of January 1, 2006 are recognized over the remaining service period using the grant-date fair value of those awards as calculated for pro forma disclosure purposes under SFAS 123.

In November 2005, the Financial Accounting Standards Board ("FASB") issued Staff Position No. SFAS 123(R)-3 "Transition Election Related to Accounting for Tax Effects of Share-Based Payment Awards." The Company has elected to adopt the alternative transition method provided in the FASB Staff Position for calculating the tax effects of stock-based compensation pursuant to SFAS 123(R).

As of January 1, 2006, the cumulative effect of the Company's adoption of SFAS 123(R) was not material.

SCALEX CORPORATION LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

The following table illustrates the effect on net income (loss) and earning (loss) per share for the years ended December 31, 2005 and 2004 assuming the Company and its subsidiaries had applied the fair value recognition provisions of FAS 123 to its stock-based employee compensation:

	Year ended	
	December 31	
	2005	2004
	U.S. dollars in thousands	
	(except for per share data)	
Net income (loss) from continuing operations - as reported	5,206	(679)
Add: stock based employee compensation expenses, included in reported net loss from continuing operations	20	20
Deduct: stock based employee compensation expenses determined under fair value method	(95)	(156)
Pro-forma net income (loss) from continuing operations	<u>5,131</u>	<u>(815)</u>
Net income from discontinued operations - as reported	100,932	47,932
Add: stock based employee compensation expenses, included in reported net income from discontinued operations (net of minority interest and related taxes)	1,954	8
Deduct: stock based employee compensation expenses determined under fair value method (net of minority interest and related taxes)	(3,434)	(437)
Pro-forma net income from discontinued operations	<u>99,452</u>	<u>47,503</u>
Pro-forma net income	<u>104,583</u>	<u>46,688</u>
Basic EPS - as reported:		
Continuing operations	0.14	(0.02)
Discontinued operations	2.65	1.19
Net income	<u>2.79</u>	<u>1.17</u>
Basic Pro-forma EPS:		
Continuing operations	0.14	(0.02)
Discontinued operations	2.61	1.18
Net income	<u>2.75</u>	<u>1.16</u>
Diluted EPS- as reported:		
Continuing operations	0.14	(0.02)
Discontinued operations	2.55	1.19
Net income	<u>2.69</u>	<u>1.17</u>
Diluted Pro-forma EPS:		
Continuing operations	0.14	(0.02)
Discontinued operations	2.51	1.18
Net income	<u>2.65</u>	<u>1.16</u>

SCAILEX CORPORATION LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

n. Earning (loss) per share ("EPS")

Basic EPS are computed based on the weighted average number of shares outstanding during each year excluding the treasury shares held by the Company. Diluted EPS reflects the increase in the weighted average number of shares outstanding that would result from the assumed exercise of options, calculated using the treasury-stock-method (in 2004 such effect was not included since it would have been anti -dilutive).

o. Revision of prior years statements of cash flows

The 2005 and 2004 statements of cash flows were revised to separately disclose the operating, investing, and financing portions of the cash flows attributable the Company's discontinued operations. The Company had previously reported these amounts on a combined basis.

p. Reclassifications

Certain comparative figures have been reclassified to conform to the current year presentation.

q. Recently issued accounting pronouncements:

- 1) In July 2006, FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement 109" ("FIN 48"). FIN 48 prescribes a comprehensive model for recognizing, measuring and presenting in the financial statements tax positions taken or expected to be taken on a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties and disclosure requirements for uncertain tax positions. FIN 48 is effective beginning as of January 1, 2007. The provisions of FIN 48 shall be applied to all tax positions upon initial adoption of this interpretation. Only tax positions that meet the "more likely than not" recognition threshold at the effective date may be recognized or continue to be recognized upon adoption of this FIN 48. The Company is currently assessing the impact of that adoption of FIN 48 will have on its consolidated financial statements.
- 2) In September 2006, the SEC issued Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"), which provides interpretive guidance on the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 is effective for fiscal years ending after November 15, 2006. The adoption of SAB No. 108 did not result in corrections of the Company's consolidated financial statements.
- 3) In September 2006, FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with GAAP, and expands disclosures about fair value measurements; however, it does not require any new fair value measurements. SFAS 157 is effective for the Company beginning as of January 1, 2008, although earlier adoption is encouraged. The Company is currently evaluating the impact of the provisions of SFAS 157 on its consolidated financial position and results of operations.

SCAILEX CORPORATION LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (continued):

- 4) In June 2006, EITF reached a consensus on Issue No. 06-03, "How Taxes Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement (That Is, Gross versus Net Presentation)." EITF 06-03 relates to any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction. EITF 06-03 states that the presentation of the taxes, either on a gross or net basis, is an accounting policy decision that should be disclosed pursuant to Accounting Principles Board Opinion No. 22, "Disclosure of Accounting Policies," if those amounts are significant. The Company must adopt EITF 06-03 for interim and annual reporting periods beginning as of January 1, 2007. The Company does not expect that the adoption of EITF 06-03 will have a material effect on its consolidated financial position or results of operations.
- 5) In February 2007, FASB issued SFAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities." This standard permits companies to choose to measure many financial assets and financial liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. This statement will be effective for the Company beginning January 1, 2008. The Company is currently evaluating the impact that the adoption of SFAS 159 will have on its consolidated financial statements.

NOTE 3 - OTHER INVESTMENTS:

The following investments are included in the Company's balance sheets under "Other investments and prepaid expenses". As of December 31, 2006, the carrying amount of these investments approximated their fair value:

- a. In May 2005, the Company received approximately \$1 million as a return on investment from Dor Venture Capital ("Dor"). As a result, the Company recognized a gain of \$0.8 million presented in other income. During 2006 the Company received approximately \$0.3 million as a return on investment, and invested in Dor approximately \$0.6 million. As of December 31, 2006, the Company wrote-off the investment in Dor in the amount of \$0.7 million following the company's decision to discontinue its investments in this fund.
- b. During the first quarter of 2006 the Company received a cash distribution of \$2.6 million from Real Time Image Ltd. ("RTI") following the sale of RTI's operations in 2005, and recorded income of \$1.8 million. After the cash distribution, there is cash held in escrow that the Company expects to receive approximately \$0.4 million. The investment in RTI is presented in the Company's 2006 balance sheet under Other Investments and prepaid expenses, while income is presented in the statement of operations under "other income."
- c. On November 9, 2006, XMPie Inc., was sold to Xerox Corporation for approximately \$48 million. The Company's share of the proceeds was \$1.5 million, of which \$1.3 million was received in December 2006. The balance is held in trust and is expected to be paid subject to the terms of the acquisition agreement. The Company recognized a gain of \$1.3 million as a result.
- d. For details on the investment in Oil Refineries Ltd. ("ORL") - see note 11b.

SCAILEX CORPORATION LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 4 - PROPERTY AND EQUIPMENT

Grouped by major classifications, the assets are composed as follows:

	December 31	
	2006	2005
	U.S. dollars in thousands	
Equipment	3	3
Leasehold improvements	10	4
Computers	73	73
	86	80
Less - accumulated depreciation	74	71
	12	9

Depreciation of property and equipment from continuing operations totaled \$3,000, \$4,000 and \$8,000 in 2006, 2005 and 2004, respectively.

NOTE 5 - EMPLOYEE RIGHTS UPON RETIREMENT:

- a.** Israeli labor laws and agreements require the payment of severance pay upon dismissal of an employee or upon termination of employment in certain circumstances. The liability is based upon the length of service and the latest monthly salary (one month's salary for each year worked), and is mainly funded through monthly payments by the Company and its Israeli subsidiaries to severance pay and pension funds as well as insurance companies (principally, an insurer which is an affiliate of the two major shareholders of the Company).

The Company records the long-term obligation as if it was payable at each balance sheet date on an undiscounted basis.

- b.** Severance pay and defined contribution plan expenses totaled \$69,000, \$26,000 and \$52,000, in 2006, 2005 and 2004, respectively.
With respect to the Company's employees, as of December 31, 2006, the Company expects to contribute approximately \$30,000 in respect of severance pay for the year ending December 31, 2007.

SCAILEX CORPORATION LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 6 - COMMITMENTS AND CONTINGENT LIABILITIES:

a. Commitments:

- 1) On December 14, 2006, the Company signed an agreement with third parties for the lease and management of offices in Herzliya Pituah, Israel, commencing from May 1, 2007 for a period of five years and may be extended an additional ten-year period (with an option to extend the lease five consecutive times for a period of terms of two years each, rather than one additional ten-year period). Annual lease and management fees amount to a total of approximately \$ 95 thousands, stated in NIS and linked to the Consumer Price Index. To secure said payments the Company issued a non-recourse bank guarantee of approximately \$23 thousands.

The future lease payments amount to approximately \$ 95 thousands annually, stated in NIS and linked to the Consumer Price Index.

Until completion of the construction work, the Company will continue to rent office space in Tel Aviv. Rental and management payments totaled approximately \$67 thousand annually, during 2006, 2005 and 2004.

- 2) For details on the agreement with the Israel Corporation Ltd. – see note 11b.

b. Contingent liabilities:

The Company has several other claims in various legal processes, the majority of which are claims of long standing. The Company does not believe that the settlement or removal of these claims will result any material liability to the Company.

As for the claim relating the SV transaction – see note 1b2.

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - SHAREHOLDERS' EQUITY:

a. Share capital:

- 1) The Company's shares are quoted on the "OTCBB" under the symbol SCIXF.OB, and are traded on "TASE".

On December 31, 2006, the Company's share closed on the OTCBB and TASE at \$7.95 and approximately \$7.98 (in NIS), respectively.

- 2) The number of shares stated as issued and outstanding - 43,467,388 shares at December 31, 2006 and 2005 - includes, at December 31, 2006 and 2005, 5,401,025 shares repurchased by the Company and held by the Company or by a trustee. These shares bear no voting rights or rights to cash dividends. In February 2007 the number of outstanding shares increased to 43,579,388 shares as a result of the exercise of options by employees, see note 11c.

b. Cash distribution and treasury stock

In 2004, approximately \$118 million were transferred by the Company to its shareholders through a repurchase of shares from the shareholders and a cash distribution:

- 1) In June 2004, the Company completed a self tender offer and purchased 4,952,050 shares for an aggregate amount of approximately \$28.1 million that represented \$5.67 per share.
- 2) In July 2004, the Company distributed in cash \$2.36 per ordinary share, or approximately \$89.8 million in the aggregate, to its shareholders.

c. Stock option plans

2001 and 2003 Plans

In December 2001, the Company's shareholders approved the adoption of the Company's 2001 Stock Option Plan ("2001 Plan"), designed primarily for employees and directors of the Company and its subsidiaries. In December 2003, the Company's shareholders approved the adoption of the Company's 2003 Share Option Plan ("2003 Plan"), designed for employees, directors and consultants of the Company who are Israeli residents, and also approved an increase in the aggregate number of shares reserved for issuance under the 2001 Plan from an initial 750,000 shares to 1,900,000 shares, with all such reserved shares being available for issuance under either the 2001 Plan or the 2003 Plan. Option awards may be granted under the 2001 Plan until November 5, 2011 and under the 2003 Plan until November 23, 2013. Terms of the options granted under the plans, such as length of term, exercise price, vesting and exercisability, are determined by the board of directors. The maximum term of an option may not exceed ten years. Each option can be exercised to purchase one share having the same rights as other ordinary shares of the Company.

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - SHAREHOLDERS' EQUITY (continued):

The 2003 Plan is designed to be governed by the terms stipulated by Section 102 of the Israeli Income Tax Ordinance. Inter alia, these terms provide that the Company will be allowed to claim, as an expense for tax purposes, the amounts credited to the employees as a benefit in respect of shares or options granted under the plan. The amount allowed as an expense for tax purposes, at the time the employee utilizes such benefit, is limited to the amount of the benefit that is liable to tax as labor income, in the hands of the employee; all being subject to the restrictions specified in Section 102 of the Income Tax Ordinance.

On September 20, 2004, the board of directors resolved to grant two senior employees of the Company options under the 2003 Plan to purchase an aggregate amount of 168,000 shares of the Company at an exercised price of \$3.70 per share. The fair value of one share at the day of grant was \$4.11. The options vest ratably over three years and are exercisable for ten years until September 20, 2014. Any options not exercised by then will expire. In the year 2004, the Company recorded \$69,000 of deferred stock compensation for the excess of the fair value of shares over the exercise price at the date of grant related to these options. The deferred stock compensation is amortized over the vesting period using the straight-line method. The compensation costs of \$23,000 and \$22,000 are presented under "general and administrative expenses" in 2005 and 2004 respectively. In 2006, the Company recorded additional amount of \$76,000 as stock-based compensation due to the adoption of FAS 123(R), see also note 2m. As a result, the compensation costs presented under "general and administrative expenses" in 2006 were \$94,000.

In the years ended December 31, 2006 and 2005, no options were granted under either the 2001 Plan or 2003 Plan.

On February 19, 2007, options were exercised for purchase of 112,000 shares. See note 11c.

A summary of the status of the Company's plans at December 31, 2006, 2005 and 2004, and changes during the years ended on those dates, is presented below:

	Year ended December 31					
	2006		2005		2004	
	Number	Weighted average exercise price \$	Number	Weighted average exercise price \$	Number	Weighted average exercise price \$
Options outstanding at beginning of year	346,754	6.91	519,922	8.09	987,066	10.48
Changes during the year:						
Granted					168,000	3.70
Forfeited and canceled	(153,754)	9.71	(173,168)	10.46	(635,144)	10.64
Options outstanding at end of year	<u>193,000</u>	4.68	<u>346,754</u>	6.91	<u>519,922</u>	8.09
Options exercisable at end of year	<u>137,000</u>	5.08	<u>234,754</u>	8.44	<u>351,922</u>	10.19
Options available for future awards	<u>1,732,000</u>		<u>1,732,000</u>		<u>1,732,000</u>	

SCALEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - SHAREHOLDERS' EQUITY (continued):

The weighted average fair value of options granted during 2004 is \$1.69.

The weighted average fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions: risk-free interest rate of 3.1%; dividend yields of zero; expected life of the options of approximately three years; and expected volatility of 52%.

The expected volatility is based on a historical volatility, by statistical analysis of the daily share price for periods corresponding the option's expected term. The expected term is expected length of time until expected date of exercising the options, based on expected employee's exercise behavior.

As of December 31, 2006, there was \$ 6,000 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the plans.

The following table summarizes information about options under the Company's plans outstanding at December 31, 2006:

Range of exercise prices	Options outstanding			Options exercisable	
	Number outstanding at December 31, 2006	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at December 31, 2006	Weighted average exercise price
\$		<u>Years</u>	\$		\$
3.70	168,000	7.72	3.70	112,000	3.70
10.00	9,000	2.0	10.00	9,000	10.00
11.00 to 11.99	11,000	1.82	11.60	11,000	11.60
12.68	5,000	1.0	12.68	5,000	12.68
	<u>193,000</u>	<u>6.94</u>	<u>4.68</u>	<u>137,000</u>	<u>5.08</u>

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 – TAXES ON INCOME:

a. The Company and its Israeli subsidiary:

Measurement of results for tax purposes under the Income Tax (Inflationary Adjustments) Law, 1985 (the Inflationary Adjustments Law)

Under this law, results for tax purposes are measured in real terms, in accordance with the changes in the Israeli CPI, or in the exchange rate of the dollar for a “foreign investors’ company”. The Company and its Israeli subsidiaries elected to measure their results on the basis of the changes in the Israeli CPI.

Tax rates

The income of the Company and its Israeli subsidiaries is taxed at the regular rate. Through December 31, 2003, the corporate tax was 36%. In July 2004, Amendment No. 140 to the Income Tax Ordinance was enacted. One of the provisions of this amendment is that the corporate tax rate is to be gradually reduced from 36% to 30%. In August 2005, a further amendment (No. 147) was published, which makes a further revision to the corporate tax rates prescribed by Amendment No. 140. As a result of the aforementioned amendments, the corporate tax rates for 2004 and thereafter are as follows: 2004 – 35%, 2005 – 34%, 2006 – 31%, 2007 – 29%, 2008 – 27%, 2009 – 26% and for 2010 and thereafter – 25%.

b. Non-Israeli subsidiaries

The non-Israeli subsidiaries are taxed under the laws of their countries of residence.

c. Carryforward tax losses and deductions

Carryforward tax losses and deductions of the Company and its subsidiaries, including capital losses and losses from realization of marketable securities approximated \$439 million at December 31, 2006. Most of the carryforward amounts are available indefinitely with no expiration date.

d. Deferred income taxes:

	December 31		
	2006	2005	2004
	U.S. dollars in thousands		
Computed in respect of the following:			
Carryforward tax losses and credits	109,750	136,946	141,028
Investments		4,191	5,447
	<u>109,750</u>	<u>141,137</u>	<u>146,475</u>
L e s s - valuation allowance (attributed mainly to loss carryforwards and expenses deductible upon payment)	<u>(109,750)</u>	<u>(139,877)</u>	<u>(145,766)</u>
		<u>1,260</u>	<u>709</u>
Deferred income taxes are included in the balance sheets as current assets		<u>1,260</u>	<u>709</u>

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - TAXES ON INCOME (continued):

e. Income (loss) before taxes on income from continuing operation:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
The Company and its Israeli subsidiaries	11,438	(447)	(2,154)
Non-Israeli subsidiaries	1,950	2,683	1,772
	<u>13,388</u>	<u>2,236</u>	<u>(382)</u>

f. Taxes on income included in the statements of operations - from continuing operation:

1) As follows:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
Current:			
Israeli	242	185	103
Non-Israeli		272	
	<u>242</u>	<u>457</u>	<u>103</u>
Deferred, see e. above -			
Non-Israeli	1,260	(551)	(1,224)
	<u>1,502</u>	<u>(94)</u>	<u>(1,121)</u>

2) Following is a reconciliation of the theoretical tax expense, assuming all income is taxed at the regular tax rate applicable to Israeli corporations (see a. above) and the actual tax expense:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
Profit (loss) before taxes on income	<u>13,388</u>	<u>2,236</u>	<u>(382)</u>
Theoretical tax expense (tax benefit) on the above amount	4,150	760	(134)
Decrease in taxes resulting from different tax rates – net	78	(175)	(75)
Change in valuation allowance	(30,127)	(5,889)	8,392
Changes in deferred taxes resulting from carryforward tax losses	27,196	4,082	(8,028)
Increase (decrease) in taxes resulting from prior years	50		(515)
Increase (decrease) in taxes arising from differences between non-dollar currencies income and dollar income, net, and other*	<u>155</u>	<u>1,128</u>	<u>(761)</u>
Tax benefit (taxes on income) in the consolidated statements of operations	<u>1,502</u>	<u>(94)</u>	<u>(1,121)</u>

* Resulting mainly from the difference between the changes in the Israeli CPI (the basis for computation of taxable income of the Company and its Israeli subsidiaries, see a. above) and the changes in the exchange rate of Israeli currency relative to the dollar.

SCALEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - TAXES ON INCOME (continued):

g. Tax assessments:

The Company has received, or is considered to have received, final tax assessments through the 2002 tax year.

NOTE 9 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT:

a. Concentrations of credit risks

At December 31, 2006 and 2005, the Company and its subsidiaries held cash and cash equivalents, most of which were deposited with major U.S, Israeli and European banks. Substantially, all of the marketable securities held by the Company are debt securities of the U.S. Treasury and highly rated corporations. The Company considers the inherent credit risks to be remote.

b. Cash Management and Fair value of financial instruments

The financial instruments of the Company and its subsidiaries consist mainly of cash and cash equivalents, marketable securities and short-term investments.

In view of their nature, the fair value of the financial instruments included in working capital is usually identical or close to their carrying amount.

As to the fair value of held-to-maturity securities-see note 10

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION:

Balance sheets:

a. Information on securities available for sale and held for maturity:

1) Held-to-maturity securities:

At December 31, 2006 and 2005 the amortized cost basis, aggregate fair value and unrealized holding gains and losses, as follows:

	Amortized Cost*	Aggregate Fair Value	Unrealized Losses	Unrealized Gains
	<u>\$ i n t h o u s a n d s</u>			
December 31, 2006:				
U.S. Treasury notes and agencies	<u>44,509</u>	<u>44,780</u>	<u>(271)</u>	<u>0</u>
December 31, 2005:				
U.S. Treasury notes and agencies	<u>40,417</u>	<u>41,037</u>	<u>(620)</u>	<u>0</u>

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

It is expected that the debt securities would not be settled at a price less than the amortized cost of the investment. Because the Company has the capability, and intends, to hold this investment until a recovery of fair value, which may be maturity, it does not consider the investment in these debentures to be other-than-temporarily impaired at December 31, 2006.

(*) Not including amounts of interest receivable of \$361 thousands and \$240 thousands at December 31, 2006 and 2005, respectively.

2) Available for sale securities:

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses*</u>	<u>Estimated Fair Value***</u>
	<u>\$ i n t h o u s a n d s</u>			
December 31, 2006:				
Corporate bonds	<u>14,302</u>	<u>6</u>	<u>(325)</u>	<u>13,983</u>
December 31, 2005:				
Corporate bonds	<u>19,578</u>	<u>4</u>	<u>(494)</u>	<u>19,088</u>

(*) Such unrealized holding losses are the result of an increase in market interest rates during 2005 and 2006 and are not the result of credit or principal risk. Based on the nature of the investments, management concluded that such unrealized losses were not other than temporary as of December 31, 2006. Amounts reclassified out of accumulated comprehensive income into earning are determined by specific identification. As of December 31, 2006, the Company held investments in available for sale securities with unrealized holding losses totaling \$319,000. Realized losses in 2006 were approximately \$337,000 (including amortization of comprehensive loss related to Held-to-maturity securities as described in note 2d), compared to 2005 that were approximately \$82,000.

(**) Of which \$49,000 has been in continuous unrealized loss position for over 12 months.

(***) Not including amounts of interest receivable of \$275 thousands and \$367 thousands at December 31, 2006 and 2005 respectively.

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

3) The marketable securities are presented in the balance sheets as follows:

	December 31	
	2006	2005
	\$ in thousands	
Among current assets:		
Held-to-maturity securities*	21,991	11,133
Available for sale securities	14,258	19,455
	<u>36,249</u>	<u>30,588</u>
As long-term investments:		
Held-to-maturity securities*	22,879	29,524
	<u>59,128</u>	<u>60,112</u>
* The above securities mature as follows:		
2006		11,133
2007	21,991	16,643
2008	12,965	2,967
2009	8,922	8,922
2010	992	992
	<u>44,870</u>	<u>40,657</u>

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

Statements of operations:

	Year ended December 31		
	2006	2005	2004
	U.S. dollars in thousands		
b. Financial income, net:			
Interest income	13,766	4,470	2,874
Loss on trading marketable securities, net	(384)	(84)	(70)
Bank charges	(87)	(48)	(67)
Other (including foreign exchange transaction losses, net)	(93)	(55)	20
	<u>13,202</u>	<u>4,283</u>	<u>2,757</u>
c. Other income, net:			
Write-down of investment in cost	(660)		
Distribution of funds from cost method investment	1,800	793	
Gain from sale of investment in cost	1,327		
Other	674	124	62
	<u>3,141</u>	<u>917</u>	<u>62</u>

d. Transactions with Related Parties

- 1) In 2006, the CEO and the CFO of the Company received a payment of \$250 thousands and \$20 thousands, respectively, directly from the former Company controlling shareholders. Such compensation is presented in the statements of changes in shareholders' equity for 2006 as "Payment made by shareholders to senior employees".
- 2) See note 11c
- 3) See note 11e.

NOTE 11 - SUBSEQUENT EVENTS:

- a. On January 4, 2007, Jemtex signed an investment agreement with a third party, and as a result, the Company received \$1 million (plus interest) in repayment of the loans made by the Company, the remaining loans were cancelled pursuant to the reorganization agreement in which the Company transferred its controlling interest in Jemtex (see Note 1b(3)). In addition, a number of conditions included in the said reorganization agreement were amended, as follows: the Company waived most of its veto rights that it received under Jemtex's Articles of Association; its rights to receive information from Jemtex were reduced; it agreed that the protection given to maintain its holdings of 15% of capital (fully diluted) would be valid until August 2009, The option described in note 1b(3) was revised as to allow the Company to invest \$3 million in Jemtex at a company pre-money valuation of \$20 million, until August 3, 2009. The Company estimates the value of this option at the date granted at a de-minimis value.

NOTE 11 - SUBSEQUENT EVENTS (continued):

- b. On January 8, 2007, in anticipation of a public offering by the State of Israel of shares of the Oil Refineries Ltd., which is located in Haifa, Israel ("ORL"), the Company and Linura Holding AG, a Swiss company indirectly held by one of the largest global natural resource companies ("Linura"), established Petroleum Capital Holdings Ltd. ("PCH") to purchase shares in ORL, pursuant to a shareholders agreement between the Company and Linura. Under the shareholders agreement, the Company holds 80.1% of PCH's share capital, while Linura holds 19.9%.

In February and March 2007, Scailex, through PCH, and Israel Corporation Ltd. ("Israel Corp.") jointly acquired 53.6% of ORL's issued share capital pursuant to an MOU signed by the parties, which provided for, among other things, the joint acquisition of ORL shares by PCH and Israel Corp. and an option for PCH to acquire additional shares in ORL from Israel Corp. Of the 53.6%, PCH acquired 12.62% of ORL's outstanding shares and Israel Corp. acquired 40.98% of the outstanding shares. Total consideration paid by PCH for the purchase of the ORL's shares was \$192.9 million.

Israeli law requires that in order to exercise the rights associated with control of ORL or 24% or more of ORL's share capital, including the right to receive dividends, the right to appoint directors and officials, and the right to exercise voting rights in the Annual General Meeting, a control permit from the Minister of Finance and the Prime Minister must be obtained, pursuant to the Israeli Government Companies Order (Declaration of the State's Vital Interests in ORL) (2007). In addition, upon the acquisition of 25% or more of ORL's share capital, Israeli law requires receipt of approval by the Commissioner of the Israeli Antitrust Authority. While we did receive the required approval from the Israeli Antitrust Commissioner on March 27, 2007, we have experienced delays in receiving the control permit. As a result, on May 10, 2007 we and Israel Corp. revoked the MOU and entered into an irrevocable Deed of Undertaking, pursuant to which the parties agreed to apply separately for the control permit. Pursuant to the Deed of Undertaking in the event that PCH succeeds in receiving the control permit and any additional regulatory approvals required from the Antitrust Commissioner by May 15, 2009, the parties will enter into the Control Agreement for the joint control of ORL. The decision to apply separately stemmed from the fact that the parties assume that Israel Corp., which until February 2007 held 26% of ORL, would succeed in obtaining a control permit in a relatively short time. Furthermore, PCH has experienced delays in receiving the control permit due to the fact that additional information was requested about Linura, which holds 19.9% of PCH.

The Deed of Undertaking further provides that in the event that PCH succeeds in obtaining the required permit by May 15, 2009, Scailex, PCH and Israel Corp. agree to enter into the Control Agreement for the joint control of ORL. In addition, pursuant to the Deed of Undertaking, the Company was granted the right to exercise a call option, allowing it to increase its holdings in ORL to 45% of the 50.25% control core of ORL within 120 days of the receipt of mandatory regulatory approvals required to control ORL or until May 15, 2009, whichever is earlier. Deed of Undertaking further provides that the right to enter into the Control Agreement is transferable to a third party, subject to Israel Corp.'s right of first refusal, provided that such third party receives a control permit by May 15, 2009.

Following the adoption of the Deed of Undertaking, PCH acquired, independently of Israel Corp., an additional 15.5 million shares of ORL for \$12.9 million, bringing its total current holdings in ORL to approximately 13.4%.

SCAILEX CORPORATION LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 11 - SUBSEQUENT EVENTS (continued):

- c. During February 2007, two officers of the Company exercised options to purchase 112,000 shares of the Company at an exercise price of \$3.70 per share. As a result of the exercise, 112,000 shares were issued and added to the Company's issued share capital. On the day of exercise, Israel Petrochemical Enterprises Ltd., the parent company purchased the said shares, through a wholly owned subsidiary, from the officers.
- d. At the end of December 2006, the Company submitted a request to the Court to distribute \$20 million to its shareholders. On January 29, 2007, Scailex Vision received Court approval and, on February 5, 2007, distributed \$20 million in cash to its shareholders. The Company received \$14.3 million from said distribution.
- e. On March 20, 2007, the audit committee and board of directors approved the terms of a service agreement with Globecom Investments Ltd. ("Globecom"), a private company controlled by Mr. Eran Schwartz, pursuant to which Globecom will render the services of Mr. Eran Schwartz, as active Chairman of the Company's board of directors beginning on the commencement of his incumbency as Chairman in July 2006 for a period of 18 months. The agreement with Globecom was approved by the shareholders in an extraordinary general meeting of the Company on April 30, 2007.

According to the Service Agreement, the scope of services will be determined in accordance with actual needs of the Company, and monthly aggregate cost to be paid by the Company for the services will be NIS 100,900 (approximately \$24,000), linked to the Israeli consumer price index. In addition, Globecom and Schwartz will receive exculpation, indemnification and insurance under similar terms of other office holders in the company.