NewMed Energy – Limited Partnership

(the "Partnership")

September 5, 2022

Israel Securities Authority
22 Kanfei Nesharim Street
Jerusalem

Tel Aviv Stock Exchange Ltd.
2 Ahuzat Bayit Street
Tel Aviv

Dear Sir/Madam,

Re: **Response of the Board of Directors of the Partnership's General Partner to the Position Paper on behalf of the Holders of the Partnership's Participation Units**

The board of directors of the Partnership's general partner respectfully responds to the position paper of Mr. Ariel Yanko and of other participation unit holders (the "**Opponents**"), regarding items no. 3-8 on the agenda of the annual and special general meeting that was summoned for September 21, 2022.

However, before the board addresses the items on the agenda, it is important to clarify that the board regrets the Opponents' misuse of the platform for submission of position papers **in connection with items on the agenda** to submit a combative, erroneous paper, a large portion of which is not at all pertinent or relevant to the issues put to the vote. The right to submit a position paper is given in relation to the items on the agenda of the general meeting and through it, the unit holder may express its personal and focused position **regarding such specific issues on the agenda**. It is not a right that is conferred on any person to publish, through the Partnership, the entirety of its conceptual and ideological doctrine on each and every issue it wishes to address.

Unfortunately, the document prepared by the Opponents includes, in its large part, misuse of this mechanism, in which the Opponents publish their positions **on issues that are in no way related to the issues on the agenda** in a document that is more like an opinion column rather than a pertinent position paper. Thus, for illustration purposes, the Opponents present "political" arguments at length, against amendments made in relation to the taxation of partnerships, which belong in discussions before the Finance Committee of the Knesset or the Tax Authority and have nothing to do with the general meeting of the Partnership. Needless to say, the unit holders were not asked to vote in the general meeting regarding the accepting of the binding law in the State of Israel, and the attempt to argue before them that the tax laws are inappropriate, is of no relevance. Similarly, the document includes historical (and distorted) descriptions of past legal proceedings, unfounded comparisons between the Partnership and other partnerships, and other issues that have nothing to do with the issues raised on the agenda.

In addition to the fact that all of the irrelevant issues included in the objection document constitute misuse of the mechanism of position papers, the attempt to convince the unit holders to vote on the issues on the agenda in a manner that will cause **damage to the Partnership** and only to provoke a discussion on issues that are not on the agenda of the meeting, is particularly grave. The Opponents do not present any pertinent reason for opposing a

significant portion of the resolutions on the agenda of the meeting, but they try to persuade the unit holders to oppose the resolutions "at this stage" until their position is accepted on an issue that is not at all on the agenda (an issue that they call "transparency in the distribution of profits"). In this context, it is clearly absurd that the Opponents' claim that they "in principle" support Resolution no. 7 on the agenda regarding the approval of refrainment from the distribution of profits for investment in Block 12, but call the holders to abstain – against the interests of the Partnership, of all unit holders, and of the Opponents themselves – and this until their position is accepted on another issue that is not currently up for discussion at all. In this context, it is necessary to keep in mind what is stated in the notice of meeting report in relation to such resolution, namely that the approval of the meeting is required in order to comply with the development plan of the Aphrodite reservoir to which the Partnership is committed in accordance with the terms and conditions of the Production Sharing Contract (PSC). Needless to say, the damage that may be caused by not complying with the development plan is very significant, and it is very unfortunate that the Opponents are calling to vote in an impertinent and irrational manner which may also lead to damage to all parties concerned.

It is for good reason that the legislator established a clear framework for raising issues on the agenda, stating that not every holder of a fraction of participation units may raise an issue on the agenda as it deems fit (see Section 65BB-65DD of the Partnerships Ordinance [New Version], 5735-1975 (the "**Ordinance**"). However, the Opponents are trying to circumvent the legislator's requirement and instead of recruiting additional unit holders with the help of which they can raise an issue on the agenda of the general meeting in accordance with the requirements of the law, they decided to try and spread their thoughts in a framework that is not at all intended therefor.

The above is a clear violation of the duty of good faith imposed on each participation unit holder. Thus, Section 65QQ of the Ordinance instructs that: "A participation unit holder shall **exercise its rights** and fulfill its obligations **towards the other participation unit holders, towards the general partner company and towards the public limited partnership, in good faith and fair dealing, and refrain from abusing its power in the public limited partnership, including in the voting at the general meeting**". It is clear that bypassing the procedure outlined by the legislator for raising issues on the agenda of the general meeting, through the right to express a position in the general meeting, is a serious violation of the duty of good faith that is imposed on the unit holders.

Furthermore, in order to promote their affairs, **the Opponents do not hesitate to cause damage to the Partnership**, and this by an attempt to paralyze the Partnership and not allow it to act in routine and customary matters such as donations (to entities that are not related to the controlling shareholder) as is customary in companies of the Partnership's size, or on essential matters required by law, such as the approval of a compensation policy for the Partnership, approval of a management arrangement and approval of the required investments in the Aphrodite reservoir. It seems that as far as the Opponents are concerned, they are willing to 'throw the baby out with the bathwater', so long as their (groundless) demands are not fully met, the Partnership can do nothing.

Under these grave circumstances, it is doubtful whether it was appropriate to publish the "position paper" of the Opponents, and in any case, the board of directors deemed it fit to emphasize that in this case, a platform intended for pertinent discussion of issues on the agenda of the general meeting was misused, in order to promote other issues that are not at all related to the agenda.

After the required clarification, it is further noted that even though the Opponents did not present pertinent arguments, the board of directors will relate, once again, to the items on the agenda, on the merits.

The board of directors reiterates all of the reasons detailed in the notice of meeting report in relation to the aforementioned issues on the agenda, and seeks to briefly emphasize the following points:

1. Item no. 3: Approval of a new arrangement regarding the Partnership's management expenses and amendment of the Partnership agreement in connection therewith –

   It is clarified that the importance of this item and the urgency of now approving the new arrangement regarding the management expenses have already been specified in the invitation to the meeting and there is no need to repeat the statements. However, in view of the impertinent objection of those opposed to the issue, the new arrangement does not include any component of profit for the controlling shareholder, unlike the standard arrangements at other public corporations, and in particular other public partnerships, including most of the petroleum partnerships.

   Furthermore, contrary to the statements in the position paper, the passing of responsibility for the payment of the Partnership's management expenses onto the Partnership amounts to an annual amount that is negligible relative to the Partnership's annual profits.

   The Opponents also ignore in the position paper the fact that the general partner waives its right under the existing arrangement to receive 7.5% of half of the Partnership's expenses for oil exploration activities. This is a right that may represent very significant amounts.

   In any case, this is a required modification of the existing arrangement which expired following Amendment no. 5 to the Ordinance, which underwent, until the convening of the meeting, a review of all of the supervision mechanisms in the Partnership, as required by law, and which was also conducted in other public limited partnerships that passed the responsibility for payment of the expenses from the general partner to the partnership.

2. Issues no. 4-6: Approval of a new compensation policy for officers in the Partnership and in the general partner; Approval of an update to the terms of office and employment of the general partner's CEO; Amendment of the limited partnership agreement on issues of donations and community aid –

   As stated, the arguments regarding the lack of transparency of the Partnership in connection with the distribution of profits are irrelevant to item no. 4-6 on the agenda and lack an actual basis that can be directly linked to the aforementioned items, and the mere raising of the above within such framework of this platform constitutes misuse.

   The issue of item no. 4 on the agenda is the approval of a new compensation policy for the Partnership, following the expiration of the previous compensation policy and in accordance with the requirements of the law. It is noted that the arguments made in the position paper are entirely impertinent and no attempt has been made to establish any

semblance of a connection between these arguments and any specific provisions in the new compensation policy.

Also, the matter of item no. 5 is an update to the terms of employment of the CEO of the general partner in the Partnership, in accordance with the new compensation policy and subject to approval thereof, which is presented for the approval of the meeting in accordance with the requirements of the law.

It is clarified that, the provisions of the law that apply to the Partnership require the approval of a compensation policy for officers in the Partnership and in the general partner in the Partnership, with the aim of creating a reasonable and adequate set of incentives for the aforementioned officials who are entrusted with promoting the business of the Partnership and maximizing its profits.

The purpose of item no. 6 on the agenda is to allow the Partnership to formulate a plan of donations and aid to the community, as part of promotion of aspects of Environmental, Social, and Governance (ESG) by the Partnership, which will provide a solution for regulatory goals in Israel and in the world and also for the expectations of investors, mainly institutional, who, when examining and approving the financing of energy projects, consider ESG as part of their investment policy. The vague argument put into writing in the position paper against this issue does not constitute an actual objection and does not include an explanation as to why the Partnership shall not be allowed to make donations like any other company of the same size as the Partnership.

In other words, items 4-6 on the agenda, as detailed above, are expected to contribute to the promotion of the Partnership's business and maximize its profits and thereby also lead to maximizing value to the participation unit holders in the Partnership. Conversely, the position paper does not even purport to present any factual objection to the aforementioned items, and it seems that its entire purpose is to try and paralyze the Partnership until it meets the Opponents' demands.

It is emphasized that the Partnership operates in accordance with the provisions determined regarding the profit distribution in the limited partnership agreement and subject to the provisions of the law, including the distribution tests applicable to the Partnership according to the Ordinance, as well as the provisions of the law in connection with reporting and disclosure to participation unit holders in the Partnership, and intends to continue to do so also in the future.

3. Item no. 7: Approval to refrain from the distribution of profits for purposes of investment in the petroleum asset "Block 12" in Cyprus –

In accordance with the terms and conditions of the PSC granted to the partners in Block 12 by the Cyprus government, the Partnership is required to comply with the terms and conditions of the development plan. Accordingly, to the extent that item no. 7 on the agenda is not approved for the investment in the aforementioned development plan, it is possible that the PSC will be expropriated from the Partnership. Such a dreadful scenario would lead to enormous damage to the Partnership. However, the Opponents show once again that the best interests of the Partnership are of no concern to them and they are willing to harm the Partnership merely to advance their affairs.

It is clarified that the investment in the development plan will only be made in accordance with the work plan and budgets approved and/or to be approved by the partners in Block 12, according to the PSC and the joint operation agreement.

It is once again emphasized that the Partnership operates and will continue to operate in accordance with the provisions set forth regarding the distribution of profits in the limited partnership agreement and subject to the provisions of the law.

4. Item no. 8: Approval for the Partnership's entry into the field of renewable energies, in the framework of collaboration with Enlight Renewable Energy Ltd. ("**Enlight**") –

Entering the field of renewable energies is a supplementary and necessary means of maximizing value to investors in the oil and gas sector, which may contribute to the dispersion of the Partnership's risks.

Furthermore, entry into the field of renewable energies is also part of ESG considerations, as specified in Section 2 above, such that the possibility of adding projects in this field is expected to increase the attractiveness of the Partnership to investors and prevent damage to investments as a result of expanding the application of ESG considerations.

It is clarified that, the audit committee and the board of directors were convinced that despite the personal interest of the CEO of the general partner in the Partnership in the transaction, the approval of the transaction, under the circumstances and as detailed above in the notice of meeting report, is consistent with the Partnership's best interests.

It is emphasized that, contrary to the statements in the position paper, unlike other oil and gas partnerships that seek to enter the field of renewable energies, in this case, as part of the proposed deal with Enlight, Delek Group Ltd., the controlling shareholder of the Partnership, has no personal interest in the transaction and will not be entitled to a royalty or another benefit from the Partnership's activity in this field.

In fact, it is precisely the claim of the Opponents that there is a minimal connection between the partnership's areas of expertise and the field of renewable energy that proves that it is necessary to approve the issue, in a manner that will allow cooperation with a leading partner in the field of renewable energies, where the Partnership will contribute its experience in regional policy as well as the development and the partner will provide its expertise in the field.

Before concluding, and although there is no need to refer to the matter of profit distribution, which is not on the agenda, it is emphasized that the unfounded claims by the Opponents of concealing information and minor distribution of profits are divorced from reality. Thus, for the sake of illustration, in 2021 the Partnership distributed an amount of 200 million dollars, and so far, in the current year, an amount of 100 million dollars has been distributed, without taking into account the balancing payments made.

In conclusion, in view of all of the aforesaid, both in the notice of meeting report and in this response of the board of directors of the Partnership's general partner, the board of directors believes that items no. 3-8 on the agenda of the meeting contribute to the promotion of the Partnership's business and the results of its activities, to realize its goals and maximize its profits, and it recommends the general meeting to approve the aforementioned items. The

objection expressed in the position paper is entirely impertinent and constitutes an abuse of a participation unit holder's right to express its position in connection with the items in the agenda of the general meeting, and therefore it is doubtful whether this detailed response is fitting.

September 4, 2022

To Delek Drilling, Secretariat, VP Adv. Sari Singer-Kaufman (sent via e-mail)
Delek Drilling, Supervisor, Adv. Uri Keidar, CPA Micha Blumenthal (sent via e-mail)

From Ariel Yanko and Holders

Re: Position Paper for Annual and Special Meeting for 2022

Ref: 1) Delek Drilling – Limited Partnership, *'Immediate report on the summoning of an annual meeting of the participation unit holders'* (Invitation to Annual Meeting for 2022), August 15, 2022

Ahead of the annual and special meeting for 2022 (Ref. 1) which was summoned for September 21, 2022, please release the position paper attached hereto.

Certificates on our holding of the Partnership's units on the record date, have been provided to the supervisor.

We appreciate your assistance.

Sincerely,

Holders

For your information (via e-mail)
Unit holders
Other
September 4, 2022

Position Paper for Annual and Special Meeting for 2022

We, the undersigned, holders of the Partnership's participation units, hereby request the general partner and the supervisor, to release the position paper below, ahead of the annual special meeting summoned for September 21, 2022.
The resolutions being put to the meeting are material and are expected to affect the **core rights of the 'public' holders** (who are not control holders) which are **the Partnership's obligation to distribute, each year, the profits and the use of profits that belong to the holders**, and we therefore turn to all holders, specifically **the institutionals** and other entities that manage public money (the partnership has many billions of shekels) to consider our recommendation below. Explanations to follow:

- **To object** to resolutions, approval of which will **affect the obligation** to distribute the profits and/or the use thereof:
  - Resolution **3:** *'Approval of a new arrangement regarding the management expenses of the Partnership'* – Passes all of the Partnership's expenses, which the general partner is obligated to pay, onto the holders (many millions of ILS per year).
  - Resolution **6:** To amend the Partnership agreement such as to allow to *'donate reasonable amounts for worthy causes…*' – we support donations to the community but prefer that the Partnership distributes the profits as it is obligated, and we will donate at our discretion.
  - Resolution **8:** *'Approval for the Partnership's entry into the field of renewable energies*' – a resolution which allows not to distribute the profits to the holders in order to use them for ventures that are not included in the objectives for which the Partnership was established.
- The significance of the following resolutions is use of the profits of the holders in favor of officers in the Partnership, therefore, so long as the general partner refuses to conduct **with transparency in the distribution resolutions**, we recommend:
  - **Objecting** to resolutions to use profits of the holders for improving the conditions of the officers in the Partnership, including:
    - Resolution **4:** *'Approval of new compensation policy*' – which means improving the conditions of officers in the Partnership.
    - Resolution **5:** *'Approval for an update to the terms of office and employment of the CEO of the general partner*' – the significance is similar to resolution **4**.

- **Abstaining** in Resolution **7**: *'Approval to refrain from the distribution of profits for investment in Block 12 in Cyprus'* – the significance of which is sweeping approval for investment in Block 12 (without amounts and an expiration date). We support the development, but approving the resolution is contingent on securing transparency in the distribution of the profits.

Following are explanations for the voting considerations.

A public limited partnership engages in one exclusive occupation, with the purpose of the petroleum partnerships being defined as exploration, development and production of oil and gas within the boundaries of the State of Israel, while later, the scope was also extended to nearby areas (Block 12 in Cyprus). In recent years, to our understanding with the pressure of the petroleum partnerships, the regulator (the stock exchange and the Israel Securities Authority) expanded the areas of operations also to include investment in petroleum ventures overseas, and investment in renewable energies (an important issue but with minimal connection between it and the areas of expertise of the partnerships).

There are substantial gaps between the partners in the Partnership, in terms of information, rights and revenues. On the one hand, the **general partner** (held by the control holders), an exclusive and entrenched manager which, although not required to take risks (invested 0.01% of the Partnership's capital!), is (greatly) rewarded also financially, at any time and in any situation, on an ongoing basis with generous management fees and operator fees, and if there are discoveries, in overriding royalties ('initiative fees') in huge amounts (tens of billions in aggregate), from the Partnership's revenues (not from the profits).

On the other hand, there are **public holders** (who hold units in the limited partnership), those who have assumed all of the (significant) risks while investing in oil explorations (99.99% of the capital). The holders agreed to take (great) risks for **one singular economic consideration**, which was guaranteed in the Partnership agreements, a consideration that is in fact their only asset in the Partnership, that given discoveries and profits (a not so high chance), **the Partnership committed to distribute the profits each year**.

The high road, which will guarantee the public holders to receive the full consideration for the risk they assumed, is for the Partnership to distribute each year the profits as it has committed, such that they will receive in aggregate the full economic value of the gas discoveries (conduct which will finally be reflected also in the Partnership's value). Value is not guaranteed to the holders by use of profits for ventures that are not in the field of expertise of the Partnership, where each one is actually a new 'adventure').

The enormous gas discoveries create **huge profits** for the Partnership, hundreds of millions of dollars per year from gas sales, which, with the large profit from the sale of Tamar, have already accumulated to billions of shekels, except that the profit distributions were much more modest, inconsistent (there were periods where the Partnership did not distribute at all) and mainly **not transparent**, a conduct that has already significantly harmed the holders (as we shall demonstrate below).

Therefore clearly, it is not possible to make do merely with a distribution commitment, which is written in the agreements, but tools are also required to ensure that the distribution is performed in practice, and this includes **a distribution mechanism and reporting rules for the holders**.

Against this background, several years ago, the holders turned to the producing (profiting) partnerships Isramco and later on to Delek Drilling (currently NewMed) (and the supervisors) (the holders even submitted, for illustration purposes only, a distribution model including considerations, mechanism and reporting rules). Isramco, backed-up by the previous supervisor (CPA David Valiano) **defined a simple and clear mechanism for distribution, and even anchored it in the partnership agreements!** Due to its importance, we shall present it below: In May of each year, the partnership shall declare an amount for distribution, subject to meeting the distribution tests and the financing agreements, which shall be no less than the lower amount of the full balance of the financial assets deposited in the partnership accounts, or profits available for distribution (according to Section 302 of the Companies Law), and each year the partnership shall distribute all of the money in the fund (except for a fixed amount that will be used as a 'reserve fund'). Isramco distributed the profits according to such mechanism.

Delek Drilling Partnership refused to present a distribution mechanism, and also refused additional requests made by the holders (at meetings, in letters and position papers) to release annual reports (considerations and data) that will explain the distribution resolutions, the Partnership's response, that the Partnership is not obligated to report the same (neither by law nor by agreements) and holders may apply to the Israel Securities Authority. Hence, the general partner, who enjoys generous revenues from the income, does not hesitate to ask the holders to pay payments for which the general partner is liable (Resolution **3**), and to risk their profits in order for it to invest in new ventures (Resolution **8**), but refuses to conduct with transparency and present the necessary information to the holders such that they understand how the managing partner is conducting with their profits (the distribution resolutions).

Initiatives taken by the general partner over the years not only did not alleviate the concerns of the holders of attempts to impair the commitment to distribute profits, to the point of canceling the same, but only strengthened them. Among the initiatives:

(a) In 2004, an attempt was made to approve the **Dorad agreement** (investment of the profits in a power plant which would have opened the door to an investment of the profits in various projects (the move was thwarted). **(b)** Decisions to approve the sweeping use of profits (without amounts and without an expiration date) for development of the gas discoveries (the previous ones: Yam Tethys Tamar Leviathan, currently, Block 12), which blurs (for the holders) the distribution considerations and ostensibly allows the 'bringing about' of resolutions not to distribute (the previous resolutions were approved). **(c)** In 2015 in Amendment (no. 5) to the Partnerships Ordinance, the general partner attempted to add to the law, the possibility of **turning the Partnership into a company** (which is not obligated in distribution) (the move was thwarted). **(d)** In 2017, the general partner attempted to **merge the Partnership into Delek Energy** (the move was thwarted). **(e)** Under the initiative of the petroleum partnerships (to our understanding), the stock exchange added to its rules, provisions that allow to approve, for three years, a 'sweeping' investment in gas and oil projects (which the general partner will perform as it wishes, without requiring a separate

approval for each project as was customary), i.e. projects which the holders have no information on the voting date, where in practice, it is also an investment for an unlimited period (since there is no chance that a project will stop and the investment will go down the drain, merely because the 'three years have come to an end'). **(f)** The attempt at present, to approve an arrangement **that will merge the Partnership into a company in London** (in terms of the holders' rights, will in practice, turn it into a company with no distribution obligation (in the meantime, through the Supreme Court, the attempt has been halted). (g) Promoting activities for investment in renewable energies, a new field as stated, that is outside the expertise of the Partnership.

We support activities aimed at maximizing profits **for the holders**, which are performed on the basis of the objectives and agreements of the Partnership and the authorizations by virtue of the law, tools designed **to protect** the rights and assets of the public holders. We therefore also support the development of Block 12, but a sweeping approval (as mentioned, without amounts and without an expiration date, Resolution **7**) should be given subject to the commitment of the Partnership that it will conduct itself transparently (conduct a mechanism and reports) in the distribution of the profits.

From reading the resolutions for the meeting, it is possible to gain the (wrong) impression that the Partnership is intended to serve mainly the control holders, the managers and the employees, at the expense of the partners of the public. Our position is that **there is no justification for the holders to approve resolutions that would adversely affect their profits and/or the commitment to distribute the same and/or the demand for transparent conduct in distribution**, meaning:

Object to Resolution **3** (that the holders will pay expenses for which the general partner is liable) and Resolutions **6** and **8** (to use the profits for ventures that are not of the Partnership's objectives) (resolutions to which also the resolution currently taking shape – an arrangement that will in practice turn the Partnership into a company, belongs).

Object, at least until the Partnership agrees to conduct itself with transparency in the distribution of profits (distribution mechanism, annual report on the distribution considerations and data), to Resolutions **4** and **5** (improvement of compensation for officers and the CEO's salary and conditions), and **abstain** in Resolution **7** (a sweeping approval for the investment in Block 12, an issue that we support in principle, as aforesaid,).

Our opinion is that the correct way for the control holders to act vis-à-vis the partners is first of all **to conduct with transparency in the profits such that each holder will receive its profits**. And in new fields, that will be established by new designated companies, and any holder that will be interested will be able to invest therein.

The non-transparent conduct in the distribution of profits has already led to significant harm to the holders, mainly to individuals but also to companies. We shall explain:

With respect to individuals: Starting from 2022, the tax regime for partnerships has changed (such that they pay tax in the same way as companies), and this significantly impairs individuals, in two ways. The first, **a holder** who is an individual will pay maximum tax (consisting of the corporate tax that the Partnership pays plus tax on dividends that the individual will pay), which is in lieu of the **marginal** tax that the

individual paid before the new arrangement (the Partnership paid maximum tax for him and the individual recipient may receive a refund from the Tax Authority). Most individuals probably pay a marginal tax that is lower than the maximum.

The second, very significant harm: **No distribution will be made to individuals of the 'undistributed' profits**, estimated at **many hundreds of millions of dollars**, for which they were not required to pay tax (profits on which the tax has already been paid by the Partnership for each holder according to his status, for an individual, the maximum tax accumulated in the Partnership until 2021 inclusive). In the new arrangement, the individuals are required to pay tax on the 'dividends' which in practice is a kind of double tax (paying tax on profits for which the tax has already been paid). The 'compensation' that will ostensibly be given to individuals will be **reduced tax when the units are sold?!** This is a mockery. Oil investors usually hold units for many years and it is entirely unclear what (if any) will be the profit for tax deduction upon sale of the units, and it is also not possible to predict what the tax laws will be years from now. All of the above indicates that the individuals were simply the weak link in the chain, where it is easy to create a tax agreement where they are the injured parties.

We shall state that the undistributed profits problem exists only in NewMed, which did not distribute the profits (Isramco, for example, distributed all of the profits without the individuals being required to pay tax, such that no undistributed profits were created), NewMed must have understood the effect of the new tax system on individuals, the problem was not really explained to them (when the Tax Authority sent a draft in 2020 for reference), nor is it clear to what extent the general partner, which was interested in the new arrangement (in which the Partnership only pays corporate tax, much less than in the distribution of profits in the amount of the maximum tax for an individual), acted with the determination required vis-à-vis the tax authorities in order to protect the rights of the individuals (and unfortunately probably neither did the supervisor).

With respect to companies: In the last year, the Partnership distributed to the companies (according to the Tel Aviv District Court ruling), 'balancing payments' for the years 2015 and 2016 (in Isramco 2013 to 2016 inclusive) in order to 'balance' the excess tax payments it paid **for individuals** (according to Section 19 of the Petroleum Profit Taxation Law, 5771-2011, and rulings of the District and Supreme court). **Except that the payments** to the companies were **significantly lower (many tens of millions of dollars) than they would have received had the Partnership timely distributed the profits equitably to individuals and companies**. We shall explain.

In the year until the law (2011) the Partnership distributed profits at the end of each year at the maximum tax amount to an individual for payment of the tax (according to the tax assessor for large enterprises agreement from 2004). The distribution was equal to the holders, companies and individuals, and withholding tax was deducted therefrom, maximum tax from an individual, and only corporate tax was deducted from a company, such that the balance of the distribution remained in its hands. Following the law, the Partnership decided, at its discretion, to pay equal and 'weighted' tax (average between an individual and a company and according to the holding rate of each of them) for each holder, a company and an individual, and therefore the Partnership began to distribute profits for tax payment at a rate that is significantly lower than those distributed up to the law. The general partner did not agree on the weighted tax method with the Tax Authority (it was clear that it would object because of the substantial consequences on the method of tax payment), neither did it turn to the court (to determine a position on

the matter), nor did it conduct itself transparently with the holders (certainly the individuals who did not really understand from the reports of the Partnership the serious implications with respect to them). When the court (the Tel Aviv District Court and later the Supreme Court in the appeal filed by the general partner) disqualified the weighted tax method in 2017 (following requests from holders to the supervisor, who turned to the court, and with the participation of the Tax Authority), it was no longer possible to turn back time, and since the profits that the general partner distributed were too low, and covered only the maximum tax payment for individuals and the corporate tax for companies, a situation of distribution inequality was created – profits were distributed to companies at a significantly lower rate than to individuals.

The problem was referred to the Tel Aviv District Court, which ruled that the Partnership will pay 'balancing payments' to the companies to make up for the inequality in the tax payment, except that no alternative was found that made it possible to make a 'full balancing' that the companies required (it was not possible to make distributions for previous years) such that **the companies received 'balancing' payments in amounts significantly lower** than those they would have received had the general partner continued and distributed the profits for tax payment according to the tax assessor for large enterprises agreement (or alternatively, coordinated the tax payment with the Tax Authority, or referred to the court).

The resolutions for the meeting

Item number **3**: *Approval of a new arrangement regarding the Partnership's management expenses and amendment of the Partnership agreement*

Our position: **Object** to the resolution. We shall explain.

Explanation: The resolution passes to the holders all of the management expenses that apply to the general partner, according to the agreements – many **millions of shekels per year** (and in aggregate, huge amounts).

The reasons given for the resolution (that the gas discoveries significantly increased the management expenses of the Partnership) are irrelevant, since when the Partnership agreements were drafted, and the management expenses were imposed on the general partner, it was clear that given discoveries and reservoirs would be developed, the management expenses would increase significantly, yet it was decided that the general partner will bear them, without conditions and without expiration dates.

This means that the application of the management expenses on the general partner was done for good reason, it is not a 'non liquet' nor a *lapsus calami*, but rather a resolution that was made consciously and on purpose, and the reasons are clear, unlike as claimed by the general partner (the control holders) it did not 'fund from its own pocket' the payments for the management of the Partnership, which it is currently trying to pass to the holders (CEO's salary, salary of the chairman of the board and of directors, rent, office maintenance, etc., etc.), expenses that are only expected to grow over the years.

Imposing the management expenses on the general partner was part of the **deal for the establishment of the Partnership**, which handsomely rewards the general partner, also before the discoveries (with generous management fees and operator fees, also when the Partnership is at a loss), but especially if there are discoveries, at which point the

general partner receives **overriding royalties** from the Partnership's income, **in huge amounts**. Therefore, in the agreement, **all** of the management expenses were imposed on the general partner, also before discoveries, as well as 'increased' expenses in the event of discoveries, because it is clear that the expenses are tiny compared to the huge royalties that the general partner receives in the event of discoveries (in aggregate many billions). We are convinced that any business entity would be happy for such a deal (receipt of royalties and payment of the expenses).

Moreover, and pertinently, the board of directors is of the general partner, and it selects the CEO, and it is clear that the management expenses should apply to the general partner. However, since the agreement was drafted, and assuming that people have short memories, the general partner is trying to pass the management expenses to the public, and it is recalled, for example, that the same also occurred at the meeting of July 2011, but at that time, the holders objected, discussions were held with the general partner and with the supervisor, and finally a compromise was established where some of the expenses were passed to the holders. This should not have happened back then and certainly not today.

Item **4**: *Approval of a new compensation policy*

Our position: **Object** to the resolution (at least so long as the Partnership is conducted without transparency in the distribution of the profits). We shall explain.

Explanation: Approval of the new compensation policy means an increase in the salary and improvement of the conditions of the CEO, the chairman of the board of directors and other officers, at the expense of the holders' profits. These are significant expenses on an ongoing basis (millions per year), which are only expected to grow and accumulate to high amounts over the years (also if the meeting approves Resolution **3** as well).

The background to our position is that the Partnership earns hundreds of millions of dollars each year, a profit of billions of ILS in aggregate, of which it distributed only a modest portion. The problem for the holders is that the distribution is not conducted with transparency, no mechanism for the distribution was defined (as was Isramco's custom), and the considerations for the distribution decisions (considerations backed-up by data), are not reported despite repeated applications of holders to the Partnership and the supervisor, for the information to be reported so that they can understand the distribution decisions (which, as mentioned, is the only asset they have in the Partnership). It is inconceivable that a managing partner, in a business that is obligated to distribute the profits, will refuse to present to its partners the considerations in the distribution decisions.

We shall reiterate that the Partnership was established for the benefit of all of the partners, including the holders who assumed all of the risk in the investment, and not just to reward the control holders, the CEO, the organs and the officers, therefore the holders should act with the means given to them by the legislator and not approve the compensation policy, at least until the Partnership conducts with transparency in the distribution of the profits.

The Partnership's arguments (which were provided to us) in refusing to release an annual report of the distribution considerations, are at best irrelevant: **(a)** That the

supervisor participates in the meetings and is aware of the distribution considerations – the role of the supervisor is to supervise the conduct of the general partner, but with all due respect, it does not replace the partners who own the asset (the holders) who are the ones that are supposed to understand how the Partnership manager conducts in their assets. **(b)** That a report of the distribution considerations may reveal 'commercial secrets' or 'investment strategies' – it is possible to present the distribution considerations without revealing any of the above. **(c)** That the holders, especially individuals, can 'extract' the relevant information from the Partnership reports that enables them to understand the distribution considerations – holders, mainly individuals, are not able nor should they try to locate, out of hundreds of pages of reports, the required information, the Partnership should transparently report to them on the conduct on the main commitment it has towards them. **(d)** The most outrageous claim, that the general partner is 'not required' to make such a report (neither by law nor by agreements) – we shall reiterate that the distribution is the only (asset) reward of the holders who have assumed all of the risks of the Partnership, therefore the general partner, who is obligated to distribute the profits (and it is so written), is also obligated to report (even if no one thought to draft it explicitly in the agreements). However, if the Partnership is 'not obligated' to the holders then surely, they are not obligated to approve the compensation required thereby in the resolutions.

Item no. **5**: *Approval of an update to the terms of office and employment of the general partner's CEO*

Our position: **Reject** the resolution. We shall explain.

The significance of the resolution is to increase the compensation and salary costs of the CEO at the expense of the holders. Our recommendation is therefore similar to Resolution **4**.

Item no. **6**: *Authorization of the Partnership to donate 'reasonable amounts' at its discretion*

Our position: **Object to** the resolution. We shall explain.

We support donations to the community for worthy causes, however, a donation is a personal matter and we are of the opinion that each partner (holder) should decide at its discretion to whom and how much to donate.

Furthermore, it is incorrect to create another mechanism that may impair the distribution resolutions.

Item no. **7**: *Approval to refrain from the distribution of profits for purposes of investment in the petroleum asset "Block 12" in Cyprus*

Our position: **Abstain** the resolution. We shall explain.

As holders, we support activities aimed at promoting projects included in the Partnership's mandate (exploration, development and production of oil and gas), which activities the **operator approved and even initiated** (set a budget framework and timetable therefor). However, Resolution **7** is once again a sweeping approval for the development of Block 12 (similar to the approval given for the Leviathan development

(neither a budget nor a date for the resolution's expiration are specified). The concern is that 'incorrect understanding and conduct' regarding the sweeping approval for investment in Block 12, may harm resolutions on the distribution of profits.

Therefore, we turn to the Partnership: First, to unequivocally clarify that the Partnership will allocate profits for the development of Block 12 solely for the performance of activities that the operator has actually approved (amounts and timetables have been determined), and that the Partnership will not 'pledge' profits (which will not be distributed) in favor of 'possible' activities (which the operator spoke of, but has not yet approved).

Second, as we have requested, the Partnership will undertake to release an annual report that presents the considerations and data for the distribution resolutions.

Item no. 8: *Approval for the Partnership's entry into the field of renewable energies, in the framework of collaboration with Enlight*

Our position: **Object** to the resolution. We shall explain.

Investment in renewable energies, a field that is fundamentally different to the exploration and production of hydrocarbons, will continue **to erode the Partnership's obligation to distribute the profits to the holders**.

Although the regulator authorized the petroleum partnerships to invest in renewable energies (in our understanding, with the pressure of the partnerships), the Partnership, as aforesaid, has no expertise in the field (other than, perhaps, financing ability and connections in target countries, which is certainly true for many other fields). Therefore it is actually an investment in a new business venture in which the general partner and the control holders have an interest (in the present case, also a direct interest for the Partnership's CEO), but the field is not relevant to the holders (who invested in petroleum explorations, not in the 'businesses' of the control holders), and as mentioned, the investment is another 'initiative' that will harm the commitment for distribution. It is also clear that the initial investment in renewable energies is only the tip of the iceberg, and thereafter, significant additional investments will be required, to which the holders will not be able to object (so as not to lose what has already been invested), and such an investment is an opening for investments in other new fields (which will ultimately completely erode the commitment to distribute profits).

If the control holders wish to invest in renewable energies, they should set up projects separately from the Partnership (together with Enlight or whomever they wish) and any holder in the Partnership who wishes to invest its profits in a venture may do so, and will not be 'dragged' into it through the Partnership.

Furthermore and pertinently, it does not seem reasonable that the Partnership will invest in a venture in which the Partnership's CEO, who is supposed to dedicate 100% of his time to the Partnership, is also a partner, the above may create a conflict of interests.

We shall state that the **Isramco partnership has already twice presented for the meeting's approval, resolutions to invest in renewable energies, and the meeting rejected them by a large majority**.

Signed: Ariel Yanko, Amikam Reshef, Drora Reshef, Itzhak Lasman, Amit Lasman, Gabi Sudri, Geula Sudri, David Yifrah, Moshe Sudri, Moshe Weindberg, David Hemo, Eli Atia, Vered Atia.