

TOWER SEMICONDUCTOR LTD
Form 20-F/A
December 29, 2010

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F/A
Amendment No. 1

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2009

Commission File number: 0-24790

TOWER SEMICONDUCTOR LTD.

(Exact name of registrant as specified in its charter and translation of registrant's name into English)

Israel
(Jurisdiction of incorporation or organization)

Ramat Gavriel Industrial Park
P.O. Box 619, Migdal Haemek 23105, Israel
(Address of principal executive offices)

Nati Somekh Gilboa, +972-4-6506109, natiso@towersemi.com,
Ramat Gavriel Industrial Park P.O.Box 619, Migdal Haemek 23105, Israel

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Ordinary Shares, par value New Israeli Shekels 1.00 per share	NASDAQ Global Market
Convertible Debentures	NASDAQ Capital Market

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

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Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: 198,961,286 Ordinary Shares

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (section 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

US GAAP International Financial Reporting Standards as issued by the International Accounting Standards Board Other

If “Other” has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

EXPLANATORY NOTE

This Amendment No. 1 to Form 20-F amends our annual report on Form 20-F for the fiscal year ended December 31, 2009, filed with the Securities and Exchange Commission, on April 30, 2010, to revise the report of Brightman Almagor Zohar & Co., the Company's public registered independent accounting firm, to include a reference to the change in method of accounting that we use for inventory valuation. The paragraph had been included in the report on our 2009 audited financial statements included in our Report on Form 6-K that we filed on March 1, 2010 but was inadvertently omitted when we filed our 20-F. This amendment also includes Item 8 and Item 15 of our 20-F as originally filed without change. Except as described above, no change has been made to the financial statements or any other portion of the Annual Report on Form 20-F as filed on April 30, 2010. The filing of this amendment does not, and does not purport to, amend, update or restate the information in any other item of the annual report on Form 20-F as filed on April 30, 2010 or reflect any events that have occurred after such date.

ITEM FINANCIAL INFORMATION

8.

A. CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION

Our consolidated financial statements are incorporated herein by reference to the pages numbered F-1 to F-74 following the signature page of this Annual Report.

ITEM 15. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended (the "Act") as of the end of the period covered by this annual report on Form 20-F. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that these disclosure controls and procedures were effective as of such date, at a reasonable level of assurance, in ensuring that the information required to be disclosed by our company in the reports we file or submit under the Act is (i) accumulated and communicated to our management (including the Chief Executive Officer and Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f). Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the criteria in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation, management has concluded that our internal control over financial reporting was effective as of December 31, 2009.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risks that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Attestation Report of the Registered Public Accounting Firm.

The effectiveness of our internal control over financial reporting as of December 31, 2009 has been audited by Brightman Almagor Zohar & Co., a member firm of Deloitte Touche Tohmatsu, an independent registered public accounting firm, as stated in their report which appears herein.

Changes in Internal Control Over Financial Reporting.

Our internal control over financial reporting was changed to include enhanced controls over the consolidation process in connection with the acquisition of Jazz in September 2008.

ITEM 17. FINANCIAL STATEMENTS

Not applicable.

ITEM 18. FINANCIAL STATEMENTS

See Index to Financial Statements following the signature page.

ITEM 19. EXHIBITS

Except as indicated all exhibits not incorporated by reference were filed with the Annual Report on Form 20-F as originally filed on April 30, 2010.

1.1 Articles of Association of the Registrant, approved by shareholders on November 14, 2000, as amended (incorporated by reference to Exhibit 3.1 of the Registrant's Registration Statement on Form F-1, File No. 333-126909, "Form F-1 No. 333-126909").

1.2 Amendment to Articles of Association of the Registrant (incorporated by reference to exhibit 4.2 to the Registration Statement on Form S-8 No. 333-117565 ("Form S-8 No. 333-117565").

1.3 Amendment to the Articles of Association of the Registrant (approved by shareholders on September 28, 2006) (incorporated by reference to Exhibit 4.2 of the Registrant's Registration Statement on Form S-8, File No. 333-138837 (the "2006 Form S-8").

1.4 Amendment to Articles of Association of Registrant (approved by shareholders on September 24, 2008) (incorporated by reference to Exhibit 3.4 of the Registrant's Registration Statement on Form S-8, File No. 333-153710 (the "2008 Form S-8").

2.1 Bank Warrants, dated January 18, 2001, between the Registrant and Bank Hapoalim B.M. and Bank Leumi Le-Israel B.M. (incorporated by reference to exhibit 2.2 to the Registrant's Annual Report on Form 20-F for the year ended December 31, 2000 (the "2000 Form 20-F")).

2.2 Registration Rights Agreement, dated January 18, 2001, by and between SanDisk Corporation, Israel Corporation, Alliance Semiconductor Ltd. and Macronix International Co., Ltd. (incorporated by reference to exhibit 2.2 to the 2000 Form 20-F).

2.3 Terms of the Registrant's Convertible Debentures issued under an Indenture, dated January 22, 2002, (incorporated by reference to the summary of terms included under the caption "Description of the Debentures" in Exhibit C to the Registrant's Report on Form 6-K for January 2002 (No. 2), filed January 16, 2002 ("January 2002 Form 6-K")).

2.4 Terms of the Registrant's Options (Series 1) (incorporated by reference to the summary of terms included under the caption "Description of the Options" in Exhibit C to the January 2002 Form 6-K).

2.5 Form of Indenture (incorporated by reference to exhibit 4.2 to the Registrant's Amendment No. 6 to the Registration Statement on Form F-1/A No. 333-126909 (the "Form F-1 No. 333-126909").

2.6 Form of Note for the Debentures (incorporated herein by reference to Exhibit A to the Indenture filed as exhibit 4.2 to Form F-1 No. 333-126909).

2.7 First Amendment to a Warrant Issued on December 11, 2003 to Tarshish Hahzakot Vehashkaot Hapoalim Ltd., dated September 28, 2006 (incorporated by reference to exhibit 99.14 of the November 2006 Form 6-K).

- 2.8 First Amendment to a Warrant Issued on December 11, 2003 to Bank Leumi Le-Israel, dated September 28, 2006 (incorporated by reference to exhibit 99.15 of the November 2006 Form 6-K).
- 2.9 First Amendment to a Warrant Issued on August 4, 2005 to Bank Hapoalim B.M., dated September 28, 2006 (incorporated by reference to exhibit 99.16 of the November 2006 Form 6-K).
- 2.10 First Amendment to a Warrant Issued on August 4, 2005 to Bank Leumi Le- Israel B.M., dated September 28, 2006 (incorporated by reference to exhibit 99.17 of the November 2006 Form 6-K).
- 2.11 Form of Series I Warrant (incorporated by reference to exhibit 99.6 of the March 2007 Form 6-K).
- 2.12 Form of Series II Warrant (incorporated by reference to exhibit 99.7 of the March 2007 Form 6-K).
- 3.1 Consolidated Shareholders Agreement, dated January 18, 2001, by and between SanDisk Corporation, Israel Corporation, Alliance Semiconductor Ltd. and Macronix International Co., Ltd. (incorporated by reference to the correspondingly-numbered exhibit to the 2000 Form 20-F).
- 4.1 Registrant's Non-Employee Director Share Option Plan 2000/3 (incorporated by reference to exhibit 4.5 to the Registrant's Registration Statement on Form S-8 No. 333-83204 ("Form S-8 No. 333-83204")).
- 4.2 Form of Grant Letter for Non-Employee Directors Share Option Plan 2001/4 (incorporated by reference to exhibit 4.9 to the Form S-8 No. 333-83204).
- 4.3 Form of Grant Letter for Non-Employee Directors Share Option Plan 2001/5 (incorporated by reference to exhibit 4.10 to the Form S-8 No. 333-83204).
- 4.4 Investment Center Agreement related to Fab 1, dated November 13, 2001 (English translation of Hebrew original) (incorporated by reference to exhibit 10.2 to the Registrant's Registration Statement on Form F-2, No. 333-97043).
- 4.5 Employee Share Option Plan 2004 (incorporated by reference to Exhibit 4.3 to the Registrant's Registration Statement on Form S-8 No. 333-117565 ("Form S-8 No. 333-117565")).
- 4.6 Form of Grant Letter to Israeli Employees (incorporated by reference to Exhibit 4.4 to Form S-8 No. 333-117565).
- 4.7 Form of Grant Letter to US Employees (incorporated by reference to Exhibit 4.5 to Form S-8 No. 333-117565).
- 4.8 Bank Warrants, dated August 2005, between the Registrant and Bank Hapoalim B.M. and Bank Leumi Le-Israel B.M (incorporated by reference to exhibit 4.46 to the Registrant's Annual Report on Form 20-F for the year ended December 31, 2005 (the "2005 Form 20-F")).
- 4.9 Employee Share Option Plan 2005, as amended (incorporated by reference to Exhibit 4.1 of the 2008 Form S-8).
- 4.10 Form of Grant Letter to Israeli Employees (incorporated by reference to Exhibit 4.4 of the 2006 Form S-8).
- 4.11 Form of Grant Letter to US Employees (incorporated by reference to Exhibit 4.5 of the 2006 Form S-8).

4.12 Form of Grant Letter for grants to Jazz employees under the Employee Share Option Plan 2005 (incorporated by reference to Exhibit 4.4 of the 2008 Form S-8).

- 4.13 Jazz Technologies, Inc. 2006 Equity Incentive (incorporated by reference to Exhibit 4.5 of the 2008 Form S-8)
- 4.14 Form of Assumption Letter from the Registrant to holders of Jazz Technologies, Inc. 2006 Equity Incentive Plan options (incorporated by reference to Exhibit 4.6 of the 2008 Form S-8)
- 4.15 Form of Option Agreement under the Jazz Technologies, Inc. 2006 Equity Incentive Plan (incorporated by reference to Exhibit 4.7 of the 2008 Form S-8)
- 4.16 CEO Share Option Plan 2005 (incorporated by reference to Exhibit 4.6 of the 2006 Form S-8).
- 4.17 Option Grant Letter Agreement - CEO Share Option Plan 2005 from the Registrant to Russell Ellwanger, dated July 15, 2005 (incorporated by reference to Exhibit 4.7 of the 2006 Form S-8).
- 4.18 Option Grant Letter Agreement - CEO Share Option Plan 2005 from the Registrant to Russell Ellwanger, dated September 28, 2006 (incorporated by reference to Exhibit 4.8 of the 2006 Form S-8).
- 4.19 Option Grant Letter Agreement - CEO Share Option Plan 2005 from Tower Semiconductor USA, Inc. to Russell Ellwanger, dated July 15, 2005 (incorporated by reference to Exhibit 4.9 of the 2006 Form S-8).
- 4.20 Equity Convertible Capital Note, dated September 28, 2006, issued to Israel Corporation Ltd. (incorporated by reference to Exhibit 99.4 of the Form 6-K for the month of November 2006 No. 6 filed on November 7, 2006 (the "November 2006 Form 6-K"))).
- 4.21 Registration Rights Agreement, dated September 28, 2006, with Israel Corporation Ltd. (incorporated by reference to Exhibit 99.5 of the November 2006 Form 6-K).
- 4.22 Conversion Agreement, dated September 28, 2006, with Bank Hapoalim B.M. (incorporated by reference to Exhibit 99.8 of the November 2006 Form 6-K).
- 4.23 Conversion Agreement, dated September 28, 2006, with Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 99.9 of the November 2006 Form 6-K).
- 4.24 Registration Rights Agreement, dated September 28, 2006, with Bank Hapoalim B.M. (incorporated by reference to Exhibit 99.10 of the November 2006 Form 6-K).
- 4.25 Registration Rights Agreement, dated September 28, 2006, with Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 99.11 of the November 2006 Form 6-K).
- 4.26 Equity Convertible Capital Note, dated September 28, 2006, issued to Bank Hapoalim B.M. (incorporated by reference to Exhibit 99.12 of the November 2006 Form 6-K).
- 4.27 Equity Convertible Capital Note, dated September 28, 2006, issued to Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 99.13 of the November 2006 Form 6-K).
- 4.28 Form of Securities Purchase Agreement (incorporated by reference to Exhibit 99.2 of the Form 6-K for the month of March 2007 No.1 filed on March 15, 2007 (the "March 2007 Form 6-K"))).

4.29 Form of Registration Rights Agreement (incorporated by reference to Exhibit 99.4 of the March 2007 Form 6-K).

4.30 Loan Agreement, dated August 2006, between the Registrant and SanDisk Corporation (incorporated by reference to exhibit 4.82 to the 2006 Form 20-F).

- 4.31 Agreement and Plan of Merger and Reorganization, dated May 19, 2008, between the Registrant, Jazz Technologies, Inc. and Armstrong Acquisition Corp. (incorporated by reference to Exhibit 2.1 of the May 20, 2008 Form 6-K)
- 4.32 Facility Agreement, as amended and restated by the parties through September 29, 2008. (incorporated by reference to Exhibit 4.86 to the 2008 20-F)
- 4.33 Conversion Agreement, dated September 25, 2008, with Bank Hapoalim B.M. (incorporated by reference to Exhibit 4.87 to the 2008 20-F)
- 4.34 Conversion Agreement, dated September 25, 2008, with Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 4.88 to the 2008 20-F)
- 4.35 Conversion Agreement, dated September 25, 2008, with the Israel Corporation Ltd. (incorporated by reference to Exhibit 4.89 to the 200820-F)
- 4.36 Pledge Agreement, dated September 25, 2008, with Bank Hapoalim B.M. and Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 4.90 to the 2008 20-F)
- 4.37 Amended and Restated Registration Rights Agreement, dated September 25, 2008, with Bank Hapoalim B.M. (incorporated by reference to Exhibit 4.91 to the 2008 20-F)
- 4.38 Amended and Restated Registration Rights Agreement, dated September 25, 2008, with Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 4.92 to the 2008 20-F)
- 4.39 Undertaking by Israel Corporation Ltd., dated September 25, 2008. (incorporated by reference to Exhibit 4.93 to the 2008 20-F)
- 4.40 Securities Purchase Agreement, dated September 25, 2008, with the Israel Corporation Ltd. (incorporated by reference to Exhibit 4.94 to the 2008 20-F)
- 4.41 Equity Convertible Capital Note, dated September 29, 2008, issued to Bank Hapoalim B.M. (incorporated by reference to Exhibit 4.95 to the 2008 20-F)
- 4.42 Equity Convertible Capital Note, dated September 29, 2008, issued to Bank Leumi Le-Israel B.M. (incorporated by reference to Exhibit 4.96 to the 2008 20-F)
- 4.43 Equity Convertible Capital Note, in the principal amount of \$30 million, dated September 25, 2008, issued to the Israel Corporation Ltd. in connection with the conversion of debt. (incorporated by reference to Exhibit 4.97 to the 2008 20-F)
- 4.44 Equity Convertible Capital Note, in the principal amount of \$20 million, dated September 25, 2008, issued to the Israel Corporation Ltd. in connection with the conversion of debt. (incorporated by reference to Exhibit 4.98 to the 2008 20-F)
- 4.45 Equity Convertible Capital Note, in the principal amount of \$20 million, dated September 25, 2008, issued to the Israel Corporation Ltd. in connection with the investment. (incorporated by reference to Exhibit 4.99 to the 2008 20-F)

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4.46 Equity Convertible Capital Note, in the principal amount of \$20 million, dated January 7, 2008, issued to the Israel Corporation Ltd. in connection with the investment. (incorporated by reference to Exhibit 4.100 to the 2008 20-F)

4.47 Amended and Restated Registration Rights Agreement, dated September 25, 2008, with the Israel Corporation Ltd. (incorporated by reference to Exhibit 4.101 to the 2008 20-F)

- 4.48 Amendment to Undertaking by the Israel Corporation Ltd., dated January 6, 2009. (incorporated by reference to Exhibit 4.102 to the 2008 20-F)
- 4.49 Standby Equity Purchase Agreement between Tower and YA Global Master SPV Ltd., dated August 11, 2009, Amendment No. 1 dated August 27, 2009 and Amendment No. 2 dated February 4, 2010 (incorporated by reference to Exhibits 99.1, 99.2 and 99.3, respectively, of the February 5, 2010 Form 6-K).
- 4.50 Amendment No. 3 to Standby Equity Purchase Agreement between Tower and YA Global Master SPV Ltd., dated August 11, 2009 (incorporated by reference to Exhibit 99.1 to the April 23, 2010 6-K)
- 8.1 List of Subsidiaries.
- *12.1 Certification by Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- *12.2 Certification by Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- *13.1 Certification by Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- *13.2 Certification by Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- *15.1 Consent of Brightman Almagor Zohar & Co.

* Filed herewith

SIGNATURES

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the registrant hereby certifies that it meets all the requirements for filing on Form 20-F and has duly caused and authorized the undersigned to sign this Amendment No. 1 to its Annual Report to be signed on its behalf.

TOWER SEMICONDUCTOR LTD.

By: /s/ Russell
 C. Ellwanger
 Russell C. Ellwanger
 Chief Executive
 Officer

December 29, 2010

TOWER SEMICONDUCTOR LTD.
AND SUBSIDIARIES
CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2009

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and the shareholders of
Tower Semiconductor Ltd.

We have audited the accompanying consolidated balance sheets of Tower Semiconductor Ltd. and subsidiaries (“the Company”) as of December 31, 2009 and 2008, and the related consolidated statements of operations, shareholders’ equity and cash flows for each of the three years in the period ended December 31, 2009. 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 conducted our audits in accordance with the 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 also 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 management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Tower Semiconductor Ltd. and subsidiaries as of December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2009, in conformity with accounting principles generally accepted in United States of America.

As discussed in Note 5 to the financial statements, the Company changed its method of accounting for inventory valuation.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2009, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 24, 2010 expressed an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting.

Brightman Almagor Zohar & Co.
Certified Public Accountants
A Member Firm of Deloitte Touche Tohmatsu

Tel Aviv, Israel
February 24, 2010

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To Board of Directors and the shareholders of
Tower Semiconductor Ltd.

We have audited the internal control over financial reporting of Tower Semiconductor Ltd. and subsidiaries (the "Company") as of December 31, 2009, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's Board of Directors and management are responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in ITEM 15 CONTROLS AND PROCEDURES - INTERNAL CONTROL OVER FINANCIAL REPORTING. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

F- 1.2

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on the criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2009 of the Company and our report dated February 24, 2010 expressed an unqualified opinion on those financial statements.

Brightman Almagor Zohar & Co.
Certified Public Accountants
A Member Firm of Deloitte Touche Tohmatsu

Tel Aviv, Israel
February 24, 2010

Audit.Tax.Consulting.Financial Advisory.

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TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(dollars in thousands)

	Note	As of December 31,	
		2009	2008
A S S E T S			
CURRENT ASSETS			
Cash and cash equivalents		\$81,795	\$34,905
Trade accounts receivable	18	40,604	45,860
Other receivables	4	2,520	2,320
Inventories	5	32,250	40,899
Other current assets	20	10,304	6,777
Total current assets		167,473	130,761
LONG-TERM INVESTMENTS	6	29,361	29,499
PROPERTY AND EQUIPMENT, NET	7	371,400	449,697
INTANGIBLE ASSETS, NET	8	67,601	81,034
GOODWILL	3	7,000	7,000
OTHER ASSETS , NET	9	8,002	8,802
TOTAL ASSETS		\$650,837	\$706,793
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES			
Current maturities of convertible debentures	13	\$--	\$8,330
Short-term bank loan	10	7,000	7,000
Trade accounts payable		42,012	49,462
Deferred revenue and short-term customers' advances		24,696	6,634
Other current liabilities	11	23,652	35,202
Total current liabilities		97,360	106,628
LONG-TERM LOANS FROM BANKS	10, 12, 14	187,606	222,989
DEBENTURES	13, 14	241,207	208,512
LONG-TERM CUSTOMERS' ADVANCES	16A	8,262	11,138
OTHER LONG-TERM LIABILITIES	15	60,388	45,959
Total liabilities		594,823	595,226
SHAREHOLDERS' EQUITY		56,014	111,567

13, 16A,
17

TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$650,837	\$706,793
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See notes to consolidated financial statements.

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TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(dollars in thousands, except per share data)

	Note	Year ended December 31,		
		2009	2008	2007
REVENUES	18	\$298,812	\$251,659	\$230,853
COST OF REVENUES		325,310	296,513	284,771
GROSS LOSS		(26,498)	(44,854)	(53,918)
OPERATING COSTS AND EXPENSES				
Research and development		23,375	14,969	13,790
Marketing, general and administrative		31,943	33,223	31,604
Write-off of in-process research and development	3	--	1,800	--
Merger related costs		--	520	--
Fixed assets impairment	7B	--	120,538	--
		55,318	171,050	45,394
OPERATING LOSS		(81,816)	(215,904)	(99,312)
FINANCING EXPENSE, NET	14, 19	(45,710)	(17,566)	(34,976)
GAIN ON DEBT RESTRUCTURING	12B	--	130,698	--
OTHER INCOME (EXPENSE), NET		2,045	(918)	92
LOSS BEFORE INCOME TAX		(125,481)	(103,690)	(134,196)
INCOME TAX BENEFIT (PROVISION)	20	5,022	(1,455)	--
LOSS FOR THE YEAR		\$(120,459)	\$(105,145)	\$(134,196)
BASIC AND DILUTED LOSS PER ORDINARY SHARE				
Loss per share		\$(0.71)	\$(0.78)	\$(1.13)
Weighted average number of ordinary shares outstanding - in thousands		170,460	134,749	118,857

See notes to consolidated financial statements.

TOWER SEMICONDUCTOR LTD.
STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(dollars in thousands)

	Ordinary shares	Additional	Cumulative	Accumulated						
	Shares- in thousands	Amount	paid-in capital	Capital notes	Cumulative stock based compensation	Treasury stock	Comprehensive gain (loss)	Accumulated deficit	Comprehensive income (loss)	Total
BALANCE - JANUARY 1, 2007	102,053	\$24,187	\$570,984	\$176,401	\$4,870	\$(9,072)	\$(203)	\$(727,651)		\$39,516
Issuance of shares and warrants	22,705	5,398	29,469							34,867
Conversion of convertible debentures to shares	592	142	674							816
Employee stock-based compensation					8,731					8,731
Exercise of options	176	44	183							227
Reclassification of bifurcated conversion option to shareholders' equity			28,377							28,377
Stock-based compensation, Note 17B(5)			1,331							1,331
Other comprehensive loss							(167)		(167)	(167)
Cumulative effect adjustment of the Facility Agreement to retained earnings								65,207	65,207	65,207
Loss for the year								(134,196)	(134,196)	(134,196)
								(69,156)	(69,156)	(69,156)

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Comprehensive
loss

BALANCE -
DECEMBER
31, 2007

125,526 \$29,771 \$631,018 \$176,401 \$13,601 \$(9,072) \$(370) \$(796,640) \$44,709

Issuance of
shares and
warrants

34,257 9,699 37,045 46,744

Conversion of
convertible
debentures to
shares

1,543 459 1,692 2,151

Employee
stock-based
compensation

6,127 6,127

Exercise of
options

--

Reclassification
of bifurcated
conversion
option to
shareholders'
equity

3,907 3,907

Capital notes

115,071 115,071

Other
comprehensive
loss

(1,997) (1,997) (1,997)

Loss for the
year

(105,145) (105,145) (105,145)

Comprehensive
loss

(107,142)

BALANCE -
DECEMBER
31, 2008

161,326 \$39,929 \$673,662 \$291,472 \$19,728 \$(9,072) \$(2,367) \$(901,785) \$111,567

Issuance of
shares and
warrants

36,114 9,572 24,534 34,106

Conversion of
convertible
debentures to
shares

2,796 744 3,357 4,101

Employee
stock-based
compensation

2,841 2,841

Exercise of
options

25 6 15 21

3,829 3,829

Stock-based compensation, Note 17B(5)										
Reclassification of options and warrants			(13,661)					12,800		(861)
Capital notes				20,000						20,000
Other comprehensive loss							869		869	869
Loss for the year								(120,459)	(120,459)	(120,459)
Comprehensive loss									(119,590)	
BALANCE - DECEMBER 31, 2009	200,261	\$ 50,251	\$ 691,736	\$ 311,472	\$ 22,569	\$(9,072)	\$(1,498)	\$(1,009,444)		\$ 56,014
BALANCE, NET OF TREASURY STOCK - AS OF DECEMBER 31, 2009, NOTE 17D	198,961									

See notes to consolidated financial statements.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)

	2009	Year ended December 31, 2008	2007
CASH FLOWS - OPERATING ACTIVITIES			
Loss for the year	\$ (120,459)	\$ (105,145)	\$ (134,196)
Adjustments to reconcile loss for the year to net cash provided by operating activities:			
Income and expense items not involving cash flows:			
Gain on debt restructuring	--	(130,698)	--
Depreciation and amortization	143,404	138,808	154,343
Effect of indexation, translation and fair value measurement on debt	3,131	(6,937)	6,227
Fixed assets impairment	--	120,538	
Other expense (income), net	(2,045)	918	(92)
Write-off of in-process research and development	--	1,800	--
Changes in assets and liabilities:			
Trade accounts receivable	5,256	15,666	(13,479)
Other receivables and other current assets	234	6,407	333
Inventories	8,649	(6,178)	459
Trade accounts payable	(6,185)	(5,119)	15,435
Deferred revenue and customers' advances	15,435	(13,522)	(11,919)
Other current liabilities	(5,595)	(7,224)	(1,363)
Other long-term liabilities	(4,576)	3,247	935
Net cash provided by operating activities	37,249	12,561	16,683
CASH FLOWS - INVESTING ACTIVITIES			
Investments in property and equipment	(28,066)	(87,224)	(107,485)
Investment grants received	--	--	1,654
Proceeds related to sale and disposal of property and equipment	--	--	108
Acquisition of subsidiary consolidated for the first time (a)	(1,472)	2,616	--
Investments in other assets and intangible assets	--	(1,004)	(1,547)
Decrease in short-term interest-bearing deposits	--	--	1,230
Long-term investments	--	--	(950)
Net cash used in investing activities	(29,538)	(85,612)	(106,990)
CASH FLOWS - FINANCING ACTIVITIES			
Proceeds from long-term loans	--	52,000	28,000
Proceeds on account of shareholders' equity	52,922	20,000	26,761
Proceeds from issuance of debentures and warrants, net	--	1,440	50,690
Repayment of debenture	(8,254)	(8,179)	(7,088)

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Debts repayment	(5,416)	(2,000)	(3,230)
Net cash provided by financing activities	39,252	63,261	95,133
Effect of foreign exchange rate change	(73)	159	--
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	46,890	(9,631)	4,826
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	34,905	44,536	39,710
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 81,795	\$ 34,905	\$ 44,536

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TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(dollars in thousands)

	Year ended December 31,		
	2009	2008	2007
NON-CASH ACTIVITIES			
Investments in property and equipment	\$5,703	\$11,667	\$17,982
Stock-based compensation	\$3,829	\$--	\$1,331
Investments in other assets	\$--	\$--	\$--
Conversion of long-term customers' advances to share capital	\$--	\$--	\$6,414
Conversion of long term debt and convertible debentures to capital notes	\$--	\$95,071	\$--
Conversion of convertible debentures to share capital	\$4,101	\$2,151	\$816
Cumulative effect adjustment of the Facility Agreement to retained earnings	\$--	\$--	\$65,207
Reclassification of bifurcated conversion option to shareholders' equity	\$404	\$3,907	\$28,377
Issuance of shares and warrants relating the merger with Jazz	\$--	\$46,744	\$--
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION			
Cash paid during the year for interest	\$25,717	\$18,520	\$28,831
Cash paid during the year for income taxes	\$2,010	\$7	\$55
(a) ACQUISITION OF SUBSIDIARY CONSOLIDATED FOR THE FIRST TIME, SEE ALSO NOTE 3 :			
Assets and liabilities of the subsidiary as of September 19, 2008 :			
Working capital (excluding cash and cash equivalents)		\$(1,086)	
Fixed assets		95,244	
Long-term investments		17,100	
Intangible assets		59,500	
Other assets		66	
Convertible debenture		(108,600)	
Long-term liabilities		(22,640)	
Goodwill		7,000	
		46,584	
Less :			
Issuance of share capital and warrants		46,744	
Accrued merger related costs		2,456	
		49,200	
		\$2,616	

See notes to consolidated financial statements.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 1 - DESCRIPTION OF BUSINESS AND GENERAL

The consolidated financial statements of Tower Semiconductor Ltd. (“Tower”) include the financial statements of Tower and its wholly-owned subsidiaries, Tower Semiconductor USA, a marketing and sales subsidiary in the United States and Jazz Technologies (“Jazz”), the parent company of its wholly-owned subsidiary, Jazz Semiconductor, Inc., an independent semiconductor foundry focused on specialty process technologies for the manufacture of analog intensive mixed-signal semiconductor devices (Jazz Technologies and Jazz Semiconductor shall collectively be referred to herein as “Jazz”). Tower and its wholly owned subsidiaries are referred to as the “Company”. References to the “Company” for dates prior to the merger of Tower and Jazz on September 19, 2008 (the “Jazz Merger”), shall exclude Jazz.

The Company is a pure-play independent specialty wafer foundry manufacturing integrated circuits with geometries ranging from 1.0 to 0.13-micron. The Company provides industry leading design enablement tools to allow complex designs to be achieved quickly and more accurately and offers a broad range of customizable process technologies including SiGe, BiCMOS, Mixed-Signal and RFCMOS, CMOS Image Sensor, Power Management (BCD), and Non-Volatile Memory (NVM) as well as MEMS capabilities. To provide world-class customer service, the Company maintains two manufacturing facilities in Israel and a one in the U.S. with additional manufacturing capacity available in China.

Tower’s ordinary shares are traded on the NASDAQ Global Market and on the Tel-Aviv Stock Exchange.

During the past years, the Company has experienced significant recurring losses and a substantial accumulated deficit. The Company has been working in various ways to mitigate these financial losses and has been successful in increasing its customer base, increasing its sales, improving its EBITDA and cash flow from operations, increasing its installed capacity level, raising funds, restructuring its debt and modifying its organizational structure to better address its customers’ needs and to improve its market position.

The worldwide economic downturn that commenced in 2008 and its effect on the semiconductor industry resulted in global decreased demand, downward price pressure, excess inventory and unutilized capacity worldwide. While many market analysts and others report signs of recovery, there is no assurance that markets will sufficiently recover from the effect of the downturn. A lack of, or slower than expected, market recovery may adversely affect the future financial results and position of the Company, including its ability to fulfill its debt obligations and other liabilities. Measures that may assist the Company to fulfill its debt obligations and other liabilities include fund-raising, sale of assets, intellectual property licensing, possible sale and lease-back of real estate assets, debt refinancing or restructuring, improving operational efficiencies and sales and the receipt of all or part of pending grants from the Israeli Investment Center. There is no assurance that the Company will be able to obtain sufficient funding from these or other sources to allow it to have sufficient cash to fulfill its debt obligations and other liabilities and support its growth plans. See further details in Notes 7C, 12B, 11, 13, 17F and 17I-J.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company's consolidated financial statements are presented in accordance with U.S. generally accepted accounting principles ("US GAAP").

A. Use of Estimates in Preparation of Financial Statements

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

B. Principles of Consolidation

The Company's consolidated financial statements include the financial statements of Tower and its wholly-owned subsidiaries, which include its marketing and sales subsidiary in the United States and Jazz. The Company's consolidated financial statements include the results of Jazz from September 19, 2008. The Company's consolidated financial statements are presented after elimination of inter-company transactions and balances. For additional data regarding the merger, see also Note 3.

C. Cash and Cash - Equivalents

Cash and cash equivalents consist of banks deposits and short-term investments (primarily time deposits and certificates of deposit) with original maturities of three months or less.

D. Allowance for Doubtful Accounts

The allowance for doubtful accounts is computed mainly on the specific identification basis for accounts whose collectability, in the Company's estimation, is uncertain.

E. Inventories

Inventories are stated at the lower of cost or market. Cost is determined for raw materials and supplies mainly on the basis of the weighted moving average cost per unit. Cost is determined for work in process and finished goods on the basis of actual production costs.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 (dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

F. Property and Equipment

(1) Property and equipment are presented at cost, including financing expenses and other capitalizable costs. Capitalizable costs include only incremental direct costs that are identifiable with, and related to, the property and equipment and are incurred prior to its initial operation. Identifiable incremental direct costs include costs associated with the funding, acquiring, constructing, establishing and installing property and equipment (whether performed internally or by others), and costs directly related to pre-production test runs of property and equipment that are necessary to get it ready for its intended use. Those costs include payroll and payroll-related costs of employees who devote time and are dedicated to the acquiring, constructing, establishing and installing of property and equipment. Allocation, when appropriate, of capitalizable incremental direct costs is based on the Company's estimates and methodologies including time sheet inputs. Maintenance and repairs are charged to expense as incurred.

Cost is presented net of investment grants received, and less accumulated depreciation and amortization.

During 2007, the Company reassessed the estimated useful lives of its machinery and equipment and as a result, machinery and equipment are depreciated over estimated useful lives of 7 years commencing the second quarter of 2007 (as opposed to 5 years prior to such period). The change was based on the Company's best estimate of the useful lives of its equipment, its experience accumulated from Fab 1 and recent trends in industry practices. The Company believes that the change better reflects the economics associated with the ownership of the equipment. This change has been accounted for as a change in estimate and was applied prospectively.

Depreciation is calculated based on the straight-line method over the estimated economic lives commonly used in the industry of the assets or terms of the related leases, as follows:

Buildings and building improvements (including facility infrastructure).	10-25 years
Machinery and equipment, software and hardware.	3-7 years

(2) Impairment examinations and recognition are performed and determined based on the accounting policy outlined in R below.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

G. Intangible Assets

Technology

The cost of Fab 2 technologies includes the technology process cost and incremental direct costs associated with implementing the technologies until the technologies are ready for their intended use. The costs in relation to Fab 2 technologies are amortized over the expected estimated economic life of the technologies commonly used in the industry. Amortization phases commence on the dates on which each of the Fab2 manufacturing lines is ready for its intended use. Fab 2 technologies are presented net of accumulated amortization as of December 31, 2009 and 2008 in the amounts of \$82,849 and \$73,948, respectively.

Impairment examinations and recognition are performed and determined based on the accounting policy outlined in R below.

H. Other Assets

Prepaid Long-Term Land Lease

Prepaid lease payments to the Israel Land Administration (“ILA”) as detailed in Notes 16A(7) and 16C are amortized over the lease period.

I. Convertible Debentures

Under ASC 470-20 Debt with Conversion and Other Options (formerly “APB 14”), the proceeds from the sale of securities are allocated to each security issued based on their relative fair value.

ASC Topic 815 "Derivatives and Hedging" generally provides criteria that, if met, require companies to bifurcate conversion options from their host instruments and account for them as free standing derivative financial instruments. These three criteria are (a) the economic characteristics and risks of the embedded derivative instrument are not clearly and closely related to the economic characteristics and risks of the host contract, (b) the hybrid instrument that embodies both the embedded derivative instrument and the host contract is not remeasured at fair value under otherwise applicable generally accepted accounting principles with changes in fair value reported in earnings and (c) a separate instrument with the same terms as the embedded derivative instrument would be considered a derivative instrument subject to the requirements of Topic 815. In determining whether the embedded derivative should be bifurcated, the Company considers all other scope exceptions provided by that topic. One scope exception particularly relevant to convertibles provides that if the embedded conversion feature is both indexed to and classified in the Company's equity.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

I. Convertible Debentures (cont.)

Stock-Based Instruments in Financing Transactions

The Company calculates the fair value of stock-based instruments included in the units issued in its financing transactions. That fair value is recognized in equity, if determined to be eligible for equity classification. The fair value of such stock-based instruments, when included in issuance of debt that is not itself accounted at fair value is considered a discount on the debt and results in an adjustment to the yield of the debt .

J. Income Taxes

The Company accounts for income taxes in accordance with ASC 740, "Income Taxes". This Topic prescribes the use of the liability method whereby deferred tax asset and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities. Deferred taxes are computed based on the tax rates anticipated (under applicable law as of the balance sheet date) to be in effect when the deferred taxes are expected to be paid or realized.

Deferred tax assets are recognized if it is probable that such assets would be realized, for temporary differences, which will result in deductible amounts in future years and for carryforwards. An allowance against such deferred tax assets is recognized if it is probable that some portion or all of the deferred tax assets will not be realized. Due to the material loss carryforward amount of Tower as of December 31, 2009 and uncertainties with regard to its utilization in the future, no such deferred tax assets were recorded in Tower's results of operations, however deferred tax assets were recorded in Jazz, see Note 20C.

The future utilization of Jazz's net operating loss carry forwards to offset future taxable income is subject to an annual limitation as a result of ownership changes that have occurred, see Note 20E.

The Company accounts for its uncertain tax positions in accordance with ASC 740 sections codified from Financial Accounting Standards Board ("FASB") Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" ("FIN 48"). The Company recognizes interest and penalties that would be assessed in relation to the settlement value of unrecognized tax benefits as a component of income tax expense.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

K. Revenue Recognition

The Company's net revenues are generated principally from sales of semiconductor wafers. The Company derives the remaining balance of its net revenues from engineering services and other support services. The majority of the Company's sales are achieved through the efforts of its direct sales force.

In accordance with ASC Topic 605 "Revenue Recognition", the Company recognizes revenues from sale of products when the following fundamental criteria are met: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred or services have been rendered, (iii) the price to the customer is fixed or determinable; and (iv) collection of the resulting receivable is reasonably assured. These criteria are usually met at the time of product shipment. Revenues are recognized when the acceptance criteria are satisfied, based on performing electronic, functional and quality tests on the products prior to shipment. Such Company testing reliably demonstrates that the products meet all of the specified criteria prior to formal customer acceptance, hence, collection of payment for services is reasonably assured.

The Company provides for sales returns and allowances relating to specified yield or quality commitments as a reduction of revenues at the time of shipment based on historical experience and specific identification of events necessitating an allowance.

Revenues for engineering and other services are recognized ratably over the contract term or as services are performed. Revenues from contracts with multiple elements are recognized as each element is earned based on the relative fair value of each element and when there are no undelivered elements that are essential to the functionality of the delivered elements and when the amount is not contingent upon delivery of the undelivered elements. Advances received from customers towards future engineering services, product purchases and in some cases capacity reservation are deferred until services are rendered, products are shipped to the customer, or the capacity reservation period ends.

Revenue relating to a turn-key agreement with an Asian entity (as detailed in Note 16D(4)) are recognized based on ASC 605-35 (formerly SOP 81-1 "Accounting for Performance of Construction Type and Certain Production Type Contracts") using contract accounting of the percentage of completion method. Measurement of the percentage toward completion is determined, based on the ratio of actual labor hours incurred to total labor hours estimated to be incurred over the duration of the contract.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

L. Research and Development

Research and development costs are charged to operations as incurred. Amounts received or receivable from the government of Israel and others, as participation in research and development programs, are offset against research and development costs. The accrual for grants receivable is determined based on the terms of the programs, provided that the criteria for entitlement have been met.

M. Loss Per Ordinary Share

Basic earnings per share is calculated, in accordance with ASC Topic 260, "Earnings Per Share", by dividing profit or loss attributable to ordinary equity holders of Tower (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) during the reported period. Diluted earnings per share is calculated by adjusting profit or loss attributable to ordinary equity holders of Tower, and the weighted average number of shares outstanding, for the effects of all dilutive potential ordinary shares.

N. Comprehensive Income (Loss)

In accordance with ASC Topic 220, "Comprehensive Income", comprehensive income (loss) represents the change in shareholders' equity during a reporting period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a reporting period except those resulting from investments by owners and distributions to owners. Other comprehensive income (loss) represents gains and losses that are included in comprehensive income but excluded from net income.

O. Functional Currency and Transaction Gains and Losses

The currency of the primary economic environment in which the Company conducts its operations is the U.S. dollar ("dollar"). Accordingly, the dollar is the functional and reporting currency. Financing expenses, net in 2009 and 2007 include net foreign currency transaction losses of \$4,952 and \$3,526, respectively. Financing expenses, net in 2008 includes net foreign currency transaction gains of \$2,401.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

P. Jazz's Pension Plans

Jazz's liabilities relating its retirement plan for hourly employees and postretirement health and life benefits plans are stated at their fair value.

Jazz adopted ASC Subtopic 715-20 Defined Benefit Plans - General, which requires recognition of the funded status of the defined benefit and other postretirement benefit plans in the balance sheet, with changes in the funded status recognized through comprehensive income, net of tax, in the year in which they occur. This Subtopic requires the amounts recognized in financial statements to be determined on an actuarial basis. To accomplish this, extensive use is made of assumptions about inflation, investment returns, mortality, turnover, medical trend rates and discount rates. A change in these assumptions could cause actual results to differ from those reported.

Q. Stock-Based Compensation

The Company applies the provisions of ASC Topic 718 Compensation - Stock Compensation, under which employee share-based equity awards are accounted for under the fair value method. Accordingly, stock-based compensation to employees and directors is measured at the grant date, based on the fair value of the award. The Company uses the straight-line attribution method to recognize stock-based compensation costs over the service period of the award.

R. Impairment of Assets

Impairment of Property, Equipment and Intangible Assets

The Company reviews long-lived assets and intangible assets on a periodic basis, as well as when such a review is required based upon relevant circumstances, to determine whether events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Application of ASC Subtopic 360-10 Property, Plant, and Equipment, resulted in an impairment charge which was recorded during 2008, see Note 7B.

Impairment of Goodwill

Goodwill is subject to an impairment test on at least an annual basis or upon the occurrence of certain events or circumstances. Goodwill impairment is assessed based on a comparison of the fair value of the unit, to which the goodwill is ascribed, as against the underlying carrying value of its net assets, including goodwill. If the carrying amount of the unit exceeds its fair value, the implied fair value of the goodwill is compared with its carrying amount to measure the amount of impairment loss, if any.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

S. Derivatives

Tower issues derivatives from time to time, whether embedded or freestanding, that are denominated in currency other than its functional currency (generally the NIS in which its shares are also traded). Instruments that are denominated in a currency other than the Company's functional currency are not eligible to be included in equity.

T. Initial Adoption of New Standards

Amendment to Accounting Standards Codification ("ASC") 815 (SFAS No. 161)

Effective January 1, 2009, the Company adopted the disclosure requirements in the amendment to ASC 815 (added by SFAS No. 161), "Disclosures about Derivative Instruments and Hedging Activities", which expands disclosures but does not change accounting for derivative instruments and hedging activities. The adoption of the amendment did not have any impact on the consolidated results of operations or financial position of the Company.

ASC 470-20-15 (FSP APB 14-1)

Effective January 1, 2009, the Company applied the amendment to ASC 470-20-15 (formerly FSP No. APB 14-1), "Accounting for Convertible Debt Instruments that may be Settled in Cash upon Conversion (Including Partial Cash Settlement)". The provision of the amendment applies to any convertible debt instrument that may be wholly or partially settled in cash and requires the separation of the debt and equity components of cash-settleable convertibles at the date of issuance. The amendment is effective for the 8% convertible debt issued by Jazz due in 2011. Following the Jazz Merger, as part of the purchase method, Jazz was required to fair value its convertible debt instrument. As a result, a new basis was determined for the convertible notes of \$108,600. The debt discount was \$19,600. Upon adoption of the amendment, the Company evaluated the equity component as of the date of the Jazz Merger and determined that it is immaterial. As such, the Company expects no impact on the Company's consolidated results of operations or financial position resulting from the adoption of this amendment for periods following the Jazz Merger.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 (dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

T. Initial Adoption of New Standards (cont.)

ASC 815-40 (EITF 07-5)

In June 2008, the FASB Emerging Issues Task Force reached a consensus on EITF Issue No. 07-5, “Determining Whether an Instrument (or an Embedded Feature) is Indexed to an Entity’s Own Stock”. The consensus is an amendment to ASC 815-40 Contract in Entity’s Own Equity.

The Company applies this consensus effective January 1, 2009. The Company identified several instruments that are affected by the consensus all of which were, before the adoption of the consensus, classified in equity and upon the adoption were reclassified from equity to liabilities. These instruments include warrants and a previously bifurcated conversion option, with either an anti-dilution feature or with an exercise price denominated in New Israel Shekels (“NIS”). At the date of adoption and in accordance with the transition provisions of the consensus, the Company measured those instruments at fair value. The difference between the fair values and the amount previously recorded in equity was recognized as an adjustment to the opening balance of retained earnings.

The effect of the adoption on equity retained earnings is as follows:

	January 1, 2009
Additional paid in capital	\$ (14,065)
Retained earnings	12,800
Fair value reclassified to liability	\$ (1,265)

The effect of the adoption on the Company’s consolidated results of operations and net loss for the year ended December 31, 2009 was \$13,723.

ASC 320-10-65 (FSP FAS 115-2 and FAS 124-2)

In April 2009, the FASB issued an amendment to ASC 320-10-65 (Investments - Debt and Equity Securities) through the issuance of FASB staff position 115-2 and 124-2, “Recognition and Presentation of Other-Than-Temporary Impairments” (“OTTI”) for investment in debt securities. This amendment applies to all entities and is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

T. Initial Adoption of New Standards (cont.)

ASC 320-10-65 (FSP FAS 115-2 and FAS 124-2) (cont.)

Under the amendment, the primary change to the OTTI model for debt securities is the change in focus from an entity's intent and ability to hold a security until recovery. Instead, an OTTI is triggered if (1) an entity has the intent to sell the security, (2) it is more likely than not that it will be required to sell the security before recovery, or (3) it does not expect to recover the entire amortized cost basis of the security. In addition, the amendment changes the presentation of an OTTI in the income statement if the only reason for recognition is a credit loss (i.e., the entity does not expect to recover its entire amortized cost basis). That is, if the entity has the intent to sell the security or it is more likely than not that it will be required to sell the security, the entire impairment (amortized cost basis over fair value) will be recognized in earnings.

However, if the entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security, but the security has suffered a credit loss, then the impairment charge will be separated into the credit loss component, which is recorded in earnings, and the remainder of the impairment charge, which is recorded in other comprehensive income. The adoption of this standard did not have any impact on the consolidated results of operations or financial position of the Company.

Amendment to ASC Topic 820 (FSP FAS 157-4)

In April 2009, the FASB issued an amendment to ASC Topic 820 through the issuance of FASB staff position 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions that are Not Orderly". This amendment applies to all assets and liabilities within the scope of accounting pronouncements that require or permit fair value measurements, except as discussed in ASC 820-10-15-2. The amendment is effective for interim and annual reporting periods ending after June 15, 2009, and shall be applied prospectively.

ASC 820-35-51 relates to determining fair values when there is no active market or where the price inputs being used represent distressed sales. It reaffirms the objective of fair value measurement, as stated in ASC 820, to reflect how much an asset would be sold for in an orderly transaction (as opposed to a distressed or forced transaction) at the date of the financial statements under current market conditions. Specifically, it reaffirms the need to use judgment to ascertain if a formerly active market has become inactive and in determining fair values when markets have become inactive.

The amendment provides guidance on (1) estimating the fair value of an asset or liability (financial and nonfinancial) when the volume and level of activity for the asset or liability have significantly decreased and (2) identifying transactions that are not orderly. The adoption of this standard did not have any impact on the consolidated results of operations or financial position of the Company.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

T. Initial Adoption of New Standards (cont.)

ASC 855 (SFAS 165)

In May 2009, the FASB issued ASC 855 (SFAS No. 165), "Subsequent Events". ASC 855 establishes general standards of accounting for, and disclosure of, events that occur after the balance sheet date but before financial statements are issued or are available to be issued. In particular, this statement sets forth: (1) the period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements, (2) the circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements and (3) the disclosures that an entity should make about events or transactions that occurred after the balance sheet date. ASC 855 is effective for the interim or annual financial periods ending after June 15, 2009. The adoption of this standard did not have any impact on the consolidated results of operations or financial position of the Company.

ASC 105 (SFAS 168)

In June 2009, the FASB issued ASC 105, "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles". ASC 105 establishes the "FASB Accounting Standards Codification" ("Codification"), and was officially launched on July 1, 2009, for the purpose of serving as the source of authoritative U.S. generally accepted accounting principles ("GAAP") recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under the authority of federal securities laws are also sources of authoritative U.S. GAAP for SEC registrants. The subsequent issuances of new standards will be in the form of Accounting Standards Updates that will be included in the Codification. In general, the Codification is not expected to change U.S. GAAP. All other accounting literature excluded from the Codification will be considered non-authoritative. ASC 105 is effective for financial statements issued for interim and annual periods ending after September 15, 2009. Effective September 30, 2009, all references made to GAAP in our consolidated financial statements include the new Codification numbering system along with original references.

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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

U. Recently Issued Accounting Standards

ASU 2009-13

In October 2009, the FASB issued "Accounting Standards Update ("ASU") 2009-13 Multiple Deliverable Revenue Arrangements a consensus of EITF" (formerly topic 08-1) an amendment to ASC 605-25. The update provides amendments to the criteria in Subtopic 605-25 for separating consideration in multiple-deliverable arrangements. The amendments in this update establish a selling price hierarchy for determining the selling price of a deliverable. The selling price used for each deliverable will be based on vendor-specific objective evidence if available, third-party evidence if vendor-specific objective evidence is not available, or estimated selling price if neither vendor-specific objective evidence nor third-party evidence is available. The amendments in this update will also replace the term "fair value" in the revenue allocation guidance with the term "selling price" in order to clarify that the allocation of revenue is based on entity-specific assumptions rather than assumptions of a marketplace participant.

The amendments will also eliminate the residual method of allocation and require that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method. The relative selling price method allocates any discount in the arrangement proportionally to each deliverable on the basis of each deliverable's selling price.

The update will be effective for revenue arrangements entered into or modified in fiscal years beginning on or after June 15, 2010 with earlier adoption permitted. The adoption of this update is not expected to have material impact on the Company's consolidated financial statements.

V. Reclassification

Certain amounts in prior years' financial statements have been reclassified in order to conform to the 2009 presentation.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 3 - MERGER WITH JAZZ

Introduction

In connection with the Jazz Merger described in Note 1 in a stock for stock transaction, upon the closing of the Jazz Merger, each outstanding share of Jazz common stock was converted into 1.8 ordinary shares of Tower and each outstanding warrant, option and convertible debenture to acquire one Jazz common stock became exercisable for 1.8 ordinary shares of Tower. Effective September 19, 2008, Jazz's common stock, warrants and units were no longer traded on the American Stock Exchange (AMEX).

In consideration for the shares, options and warrants of Jazz, Tower issued approximately 34.3 million ordinary shares, 5.4 million options and 59.5 million warrants with a total value of \$46,744 (or \$50,070 including transaction costs). The per share value, as well as the value of the options and warrants, was calculated based on Tower's stock price prevailing around May 19, 2008, the date of signing and announcement of the definitive agreement of the Jazz Merger, in accordance with provisions of EITF 99-12 "Determination of the Measurement Date for the Market Price of Acquirer Securities Issued in a Purchase Business Combination". The merger was accounted for under the purchase method of accounting. Under this method, Jazz was treated as the "acquired" company. The results of Jazz's operations have been included in the consolidated financial statements as of September 19, 2008.

Estimated Fair Values of Jazz's Assets and Liabilities as of the Date of Merger

The following table summarizes the estimated fair values of Jazz's assets and liabilities at the date of merger:

	September 19, 2008
Current assets	\$ 42,035
Long-term investments	17,100
Property, plant, and equipment	95,244
Intangible assets	59,500
Other assets	66
Goodwill	7,000
Total assets as of merger date	220,945
Current liabilities	39,635
Convertible debentures	108,600
Other long-term liabilities	22,640
Total liabilities as of merger date	170,875
Net assets as of merger date	\$ 50,070

Of the \$59,500 of intangible assets, \$1,300 were assigned to existing technology, \$15,100 were assigned to patents and other core technology, \$1,800 were assigned to in-process research and development, \$2,600 were assigned to customer relations, \$5,200 were assigned to trade name and \$33,500 were assigned to real estate lease agreements; \$7,000 represent goodwill. The fair values set forth above are based on a valuation of Jazz's assets and liabilities performed by the Company in accordance with SFAS No. 141, "Business Combinations".

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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(dollars in thousands, except share data and per share data)

NOTE 3 - MERGER WITH JAZZ (cont.)

Pro-Forma Financial Information

The following unaudited pro-forma financial information assumes that the Jazz Merger occurred on January 1, 2007 (and assumes that the acquisition of Jazz Semiconductor by Jazz occurred on January 1, 2007). Such information is presented for illustrative purposes only and is not necessarily indicative of the operating results that would have been achieved if the merger had taken place on the date specified, nor are they indicative of the Company's future operating results.

	Year ended December 31,	
	2008	2007
	(Unaudited)	
Revenues	\$ 384,044	\$ 438,502
Loss	(106,647)	(146,409)
Loss per share - basic and diluted	\$ (0.67)	\$ (0.96)

NOTE 4 - OTHER RECEIVABLES

Other receivables consist of the following:

	As of December 31,	
	2009	2008
Government agencies	\$ 2,267	\$ 2,277
Others	253	43
	\$ 2,520	\$ 2,320

NOTE 5 - INVENTORIES

Inventories consist of the following:

	As of December 31,	
	2009	2008
Raw materials	\$ 10,294	\$ 13,673
Work in process	17,743	13,966
Finished goods	4,213	13,260
	\$ 32,250	\$ 40,899

Work in process and finished goods are presented net of aggregate write-downs to net realizable value of \$3,107 and \$12,488 as of December 31, 2009 and 2008, respectively.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 5 - INVENTORIES (cont.)

Following the Jazz Merger, Tower and Jazz have been working to align their reporting and information systems. During 2009, the Company completed this process with Jazz adopting in its financial statements the same method of calculating the cost of inventories used by Tower. The primary result of such adoption is the inclusion of depreciation and amortization as part of the cost of inventory. In addition, indirect raw material that had been previously immediately charged in Jazz to earnings, is now being capitalized and presented as part of raw material inventory of Jazz until it is consumed. Comparative financial statements of prior periods (in which Jazz was consolidated) have been adjusted to apply the new method retrospectively. The following financial statement line items for fiscal year 2008 were affected by the change in accounting principles.

As of December 31, 2008:

	As originally reported	As adjusted	Effect of change
Inventories	\$ 38,729	\$ 40,899	\$ 2,170
Other current assets (related to deferred tax asset)	7,657	6,777	(880)
Shareholders' Equity	\$ 110,277	\$ 111,567	\$ 1,290

For the year ended December 31, 2008:

	As originally reported	As adjusted	Effect of change
Net loss	\$ (106,435)	\$ (105,145)	\$ 1,290

NOTE 6 - LONG-TERM INVESTMENTS

Long-term investments consist of the following:

	As of December 31,	
	2009	2008
Severance pay funds (see Note 15B)	\$ 12,078	\$ 12,193
Investment in HHNEC (see below)	17,100	17,100
Investment in limited partnership (see below)	183	206
	\$ 29,361	\$ 29,499

Investment in Limited Partnership:

In December 2007, Tower together with CMT Medical Technologies Ltd., a leading provider of advanced digital X-ray imaging systems for medical diagnosis, established a limited partnership to develop and market X-ray detectors for medical applications. Tower owns 38% of the limited partnership and accounts for the investment in the limited partnership using the equity method.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 6 - LONG-TERM INVESTMENTS (cont.)

Investment in HHNEC:

Jazz is holding an equity investment in HHNEC (Shanghai Hua Hong NEC Electronics Company, Ltd.). As of December 31, 2009, the investment represented a minority interest of approximately 10% in HHNEC, hence the investment in HHNEC was recorded at fair value as of the date of the Jazz Merger and subsequently carried using the cost method of accounting for investments, as Jazz does not have the ability to exercise significant influence, see Note 3.

As part of the Jazz's acquisition of 10% interest in HHNEC, Jazz was obligated to pay additional amounts to former stockholders of Jazz Semiconductor if it would have realized proceeds in excess of \$10,000 from a liquidity event through February 16, 2010. In that event, Jazz would have been obligated to pay the former Jazz Semiconductor stockholders an amount equal to 50% of the proceeds over \$10,000. No liquidity event occurred on or before February 16, 2010, and accordingly, that obligation has expired. Jazz has no further obligation to pay the former Jazz Semiconductor shareholders any amount realized from a liquidity event relating to its interest in HHNEC.

NOTE 7 - PROPERTY AND EQUIPMENT, NET

A. Composition:

Cost:	As of December 31,	
	2009	2008
Buildings (including facility infrastructure)	\$ 263,506	\$ 262,332
Machinery and equipment , see B below	1,033,563	1,010,370
	1,297,069	1,272,702
Accumulated depreciation		
Buildings (including facility infrastructure)	106,363	89,914
Machinery and equipment	819,306	733,091
	925,669	823,005
	\$ 371,400	\$ 449,697

Supplemental disclosure relating to cost of property and equipment:

- (1) As of December 31, 2009 and 2008, the cost of buildings, machinery and equipment was reflected net of investment grants in the aggregate of \$265,587 and \$267,922, respectively.
- (2) Depreciation expenses, in relation to Fab 2 property and equipment were \$80,998, \$94,211 and \$113,393 in 2009, 2008 and 2007, respectively.
- (3) Depreciation expenses, in relation to Jazz property and equipment were \$18,808 in 2009 and \$5,513 in the period between the Jazz Merger date and December 31, 2008.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 7 - PROPERTY AND EQUIPMENT, NET (cont.)

B. Fixed Assets Impairment

Machinery and equipment presented above are net of impairment charges. Due to the worldwide economic downturn that commenced in 2008 and its effect on the semiconductor industry that resulted in global decreased demand, downward price pressure and excess inventory (see also Note 1), Tower has determined during 2008 that the events and circumstances indicate that the carrying amount of its machinery and equipment may not be recoverable. In accordance with ASC 360-10 Property, Plant and Equipment, Tower tested the recoverability of its machinery and equipment based, among others, on its business plan and market conditions, and determined that the carrying amounts of its machinery and equipment may not be recoverable. Tower evaluated the fair value of its machinery and equipment and determined that the carrying amounts exceed the fair values by \$120,538. Tower recorded a charge in that amount in a separate line in its 2008 statement of operations.

The fair values of the machinery and equipment were determined using expected cash flows discounted at a discount rate commensurate with the risk involved in generating such cash flows.

C. Investment Grants

In December 2000, the Investment Center approved an investment program in connection with Fab 2 for expansion of Tower's plant. The approval certificate for the program provided for a benefit track entitling Tower to investment grants at a rate of 20% of qualified investments of up to \$1,250,000, or an aggregate of up to \$250,000, of which as of the balance sheet date, an aggregate of approximately \$165,000 has been received from the Investment Center. Under the terms of the program, investments in respect of Fab 2 were to be completed by December 31, 2005, five years from the date the approval certificate was obtained. Due to the later than planned construction of Fab 2, market conditions and slower than planned ramp-up, Tower completed approximately 72% of the investments within the time frame stipulated in the approved enterprise program. In December 2007, Tower submitted the final report in relation to the program. Tower has been holding discussions with the Investment Center to achieve satisfactory arrangements to approve a new expansion program since January 1, 2006.

In May 2008, Tower filed a petition with the Israeli High Court of Justice in which Tower asked the Court to order that its expansion plan (in connection with its Fab 2 Approved Enterprise Program) be brought before the relevant Israeli Governmental bodies for their respective approvals without delay. On August 11, 2008, the Investment Center rejected Tower's expansion plan request. Tower has appealed this decision before the Israeli Minister of Finance and the Israeli Minister of Industry, Trade and Labor. To date, the appeal committee has not yet reviewed Tower's appeal. In February 2010, the Israeli High Court of Justice dismissed the petition and instructed the appeal committee to review this matter as soon as possible and provide its recommendation to the investment center and the Ministers of Finance and Industry.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(dollars in thousands, except share data and per share data)

NOTE 7 - PROPERTY AND EQUIPMENT, NET (cont.)

C. Investment Grants (cont.)

As of the approval date of the financial statements, Tower cannot estimate when, if at all, Tower will receive approval of its request for a new expansion program or will receive the grants under it.

Entitlement to the above grants and other tax benefits is subject to various conditions stipulated by the Israeli Law for the Encouragement of Capital Investments - 1959 ("Investments Law") and the regulations promulgated thereunder, as well as the criteria set forth in the certificates of approval. In the event Tower fails to comply with such conditions, Tower may be required to repay all or a portion of the grants received plus interest and certain inflation adjustments. In order to secure fulfillment of the conditions related to the receipt of investment grants, floating liens were registered in favor of the State of Israel on substantially all of Tower's assets, see Note 20A.

Any failure by Tower to meet the conditions of the 2000 approval certificate may result in the cancellation of all or a portion of the grants and tax benefits to which Tower is entitled and in the Investment Center requiring Tower to repay all or a portion of grants already received. Under Israeli law, Tower's non-completion of total qualified investments of \$1,250,000 by December 31, 2005 may permit the Investment Center to require Tower to repay all or a portion of grants already received. The Company believes that it is improbable that the Investment Center would demand that Tower repay all or a portion of grants already received, due to its non-completion of such investments by December 31, 2005. See also Note 20A.

D. For liens, see Notes 12D and 16D(2).

NOTE 8 - INTANGIBLE ASSETS, NET

Intangible assets, net consist of the following:

	Useful Life	As of December 31,	
		2009	2008
Real estate lease	19	\$ 31,171	\$ 32,988
Technologies in relation to Fab2	4	14,897	23,799
Patents and other core technology rights	9	12,941	14,625
Trade name	9	4,456	5,037
Customers relationship	15	2,378	2,551
Technology	9	1,083	1,259
Others		675	775
		\$ 67,601	\$ 81,034

In process research and development in the amount of \$1,800 was immediately written off and included in a separate line in the statement of operations for 2008.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 9 - OTHER ASSETS, NET

Other assets, net consist of the following:

	As of December 31,	
	2009	2008
Prepaid long-term land lease, net (see Note 16C)	\$ 4,382	\$ 4,503
Debentures issuance expenses, net	2,282	2,781
Prepaid expenses - long-term	1,135	1,202
Deferred financing charges, net	203	316
	\$ 8,002	\$ 8,802

NOTE 10 - ASSET-BASED REVOLVING CREDIT FACILITY

On September 19, 2008, Jazz Technologies entered into a Second Amended and Restated Loan and Security Agreement, as guarantor of its subsidiary Jazz Semiconductor, Inc., with Wachovia Capital Markets, LLC, as lead arranger, bookrunner and syndication agent, and Wachovia Capital Finance Corporation (Western), as administrative agent, and Jazz Semiconductor, Inc. and Newport Fab, LLC, as borrowers (the "Loan Agreement"), with respect to a three-year secured asset-based revolving credit facility in the total amount of up to \$55,000. In December 2008, Wells Fargo acquired Wachovia Corporation, its businesses and obligations and therefore now administers the Loan Agreement as administrative agent.

The borrowing availability varies according to the levels of the borrowers' eligible accounts receivable, eligible equipment and other terms and conditions described in the Loan Agreement. The maturity date of the facility is September 2011, unless terminated earlier. Loans under the facility bear interest at a rate equal to, at the borrowers' option, either the lender's prime rate plus a margin ranging from 0.25% to 0.75% or the USD LIBOR rate plus a margin ranging from 2.0% to 2.5% per annum.

The Loan Agreement contains customary covenants and other terms, including covenants based on Jazz's EBITDA (as defined in the Loan Agreement), as well as customary events of default. The facility is secured by the assets of Jazz and the borrowers. If any event of default occurs, Wachovia may declare due immediately, all borrowings under the facility and foreclose on the collateral. Furthermore, an event of default under the loan agreement would result in an increase in the interest rate on any amounts outstanding. As of December 31, 2009, Jazz was in compliance with all of the covenants under this facility.

Borrowing availability under the facility as of December 31, 2009, was approximately \$100. Outstanding borrowings were \$27,000 and \$1,800 of the facility supporting outstanding letters of credits on that date. Jazz considers borrowings of \$20,000 to be long-term debt as of December 31, 2009.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 11 - OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

	As of December 31,	
	2009	2008
Accrued compensation and benefits	\$ 10,329	\$ 10,648
Vacation accrual	5,426	4,652
Interest payable (primarily in relation to convertible debentures)	1,260	5,726
Due to related parties	2,518	11,324
Other (*)	4,119	2,852
	\$ 23,652	\$ 35,202

(*)As of December 31, 2009 includes \$745 of 5.2 million warrants (“Series 5 Warrants”) issued in 2006, exercisable through December 2010, at an exercise price of NIS 9.48 linked to the CPI. Series 5 Warrants were originally presented in shareholders’ equity, however following the adoption of EITF 07-5 as codified in ASC 815-40 on January 1, 2009, Series 5 Warrants were classified from equity to liabilities.

NOTE 12 - LONG-TERM LOANS FROM BANKS

A. Composition

	As of December 31, 2009		
	Effective interest rate (*)		
In U.S. Dollar (**)	2.75	%	\$ 110,120
In U.S. Dollar	5.30	%	120,000
Total long-term debt from Banks-principal amount			230,120
Fair value adjustments			(42,514)
Total long-term debt from Banks			\$ 187,606

	As of December 31, 2008		
	Effective interest rate (*)		
In U.S. Dollar	5.30	%	\$ 120,000
In U.S. Dollar (**)	4.00	%	106,087
Total long-term debt from Banks-principal amount			226,087
Fair value adjustments			(3,098)
Total long-term debt from Banks			\$ 222,989

(*)The effective interest rate as of December 31, 2009 and 2008 of loans in the amounts of \$120,000 and \$200,000, respectively, takes into account the terms of the hedging agreements described in Note 14A.

(**)Including \$20,000 Jazz's Loan Agreement, see Note 10.

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TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 12 - LONG-TERM LOANS FROM BANKS (cont.)

B. Facility Agreement

Introduction

In January 2001, Tower entered into a credit Facility Agreement with the Banks, which was revised several times, to fund the establishment and equipping of Fab 2 ("Facility Agreement"), under which the outstanding debt as of December 31, 2009, is approximately \$210,000, and the annual interest rate is the three-month USD LIBOR plus 2.5%. For details, see below.

September 2006 Amendment

In September 2006, Tower signed definitive agreements with the Banks and TIC. Pursuant to the agreements, among other things:

- (i) \$158,000 of debt under the Facility Agreement was converted into equity equivalent capital notes of Tower, at a conversion ratio of \$3.04 per share, representing twice the average closing price per share during the ten days prior to signing the Memorandum of Understanding ("MOU") that preceded the final amendment.
- (ii) the interest rate applicable for the quarterly actual interest payment on the loans was decreased from three-month USD LIBOR plus 2.5% per annum to three-month USD LIBOR plus 1.1% per annum, effective from May 17, 2006 (the "Decreased Amount"). As compensation for the Decreased Amount and subject to adjustment, it was agreed that in January 2011, the Banks would be issued such number of shares (or equity equivalent capital notes or convertible debentures) that equals the Decreased Amount divided by the average closing price of Tower's ordinary shares during the fourth quarter of 2010 (the "Fourth Quarter 2010 Price"). If during the second half of 2010, the closing price Tower's ordinary shares on every trading day during this period exceed \$3.49, then the Banks will only be granted such number of shares (or equity equivalent capital notes or convertible debentures) that equals half of the Decreased Amount divided by the Fourth Quarter 2010 Price.
- (iii) TIC invested \$100,000 in Tower in exchange for approximately 65.8 million equity equivalent capital notes exercisable into Tower's ordinary shares, based on the average closing price per share during the ten days prior to signing the MOU that preceded the final agreement.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 12 - LONG-TERM LOANS FROM BANKS (cont.)

B. Facility Agreement (cont.)

September 2007 Credit Line Agreements with the Banks and TIC and September 2007 Amendment

In September 2007, Tower signed and closed definitive agreements with the Banks and with TIC, providing for credit lines totaling up to \$60,000, 25% of which was to be provided by each Bank and 50% by TIC, \$28,000 of which had been borrowed during 2007 and the remainder during 2008. Loans under the credit lines carried an interest at an annual rate of three-month USD LIBOR plus 3% and were repayable 2 years from the date any loan was borrowed. The above described loans' terms, including repayment schedule, outstanding amounts and other terms, were later revised to result in postponed schedule, lower amount outstanding and other terms, for details, see "September 2008 definitive agreement with the Banks and TIC" and "September 2009 amendment to the Facility Agreement" below. Tower paid the Banks and TIC customary fees. For details regarding 5.4 million warrants granted to the Banks and TIC in connection with this agreement, see Note 17B(5). Further, in September 2007, the Company signed and closed a definitive amendment to the Facility Agreement mainly to reflect into it the Credit Line Agreements described above and to revise the financial ratios and covenants that Tower was to satisfy.

September 2008 Definitive Agreement with the Banks and TIC

In September 2008, Tower signed and closed definitive agreements with the Banks and TIC. Pursuant to the agreements: (i) \$200,000 of Tower's debt to the Banks was converted into equity equivalent capital notes of Tower at a conversion ratio of \$1.42, exercisable into Tower's ordinary shares, representing two times the average closing price per share on NASDAQ for the ten trading days prior to August 7, 2008 (the date of Tower's public announcement regarding its debt conversion negotiations with the Banks and TIC); (ii) the commencement date for the repayment of the remaining principal of the Banks' loans was postponed from September 2009 to September 2010, such that the outstanding loans shall be repaid in eight equal quarterly installments between September 2010 and June 2012 (which was further revised in the "August 2009 amendment to the Facility Agreement" below); (iii) interest payments owed to the Banks and originally due September 2008 through June 2009 were added to the remaining principal of the Banks' loans and will be paid according to the same schedule; (iv) the interest rate on the remaining principal of the Banks' loans was set to be USD LIBOR plus 2.5% per annum; (v) the compensation for the Decreased Amount agreed to in the September 2006 amendment was revised pro-rata to the decreased loans; (vi) the Banks waived in full Tower's compliance with financial covenants through the end of 2008; (vii) \$50,000 of debt owed by Tower to TIC (consisting of \$30,000 owed under a loan facility and \$20,000 of Tower's convertible debentures series B held by TIC) were converted into equity equivalent capital notes at a conversion ratio of \$1.42 exercisable into Tower's ordinary shares, representing two times the average closing price per share on NASDAQ for the ten trading days prior to August 7, 2008;

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NOTE 12 - LONG-TERM LOANS FROM BANKS (cont.)

B. Facility Agreement (cont.)

September 2008 Definitive Agreement with the Banks and TIC (cont.)

and (viii) TIC invested \$20,000 in Tower in exchange for approximately 28.2 million equity equivalent capital notes exercisable into Tower's ordinary shares, based on the average closing price per share on NASDAQ for the ten trading days prior to August 7, 2008.

Furthermore, TIC committed to invest up to an additional \$20,000 under certain conditions. In January 2009, such conditions were satisfied and TIC invested said amount in exchange for approximately 76.9 million equity equivalent capital notes of Tower, exercisable into ordinary shares of Tower.

The debt conversion to equity equivalent capital notes as detailed above resulted in a gain of \$130,698 that was recorded in the Company's statement of operations for 2008.

August 2009 amendment to the Facility Agreement

During 2009, the Banks and Tower entered into an amendment to the Facility Agreement to: (i) postpone the repayment schedule of the outstanding loans, to be repaid in 8 equal quarterly installments from September 2011 until June 2013; (ii) waive the financial covenants stipulated in the Facility Agreement through December 31, 2009; and (iii) upon certain circumstances, as stipulated in the amendment, and following receipt by Tower of significant amounts of proceeds from a certain source, Tower will pay a portion of such proceeds on account of the outstanding loans prior to the due date specified above. As part of the terms of the amendment, Tower agreed to extend the Banks' existing warrants to June 2013, grant the Banks new warrants in three annual tranches of \$1,000 each, at a quantity and price to be calculated based on the market stock price prior to any such grant and pay the Banks fees in the aggregate amount of \$350.

Accounting for the Loans under the Facility Agreement

Loans received under the Facility Agreement, as amended to date, are presented commencing January 1, 2007 at fair value, with changes in value reflected on the statement of operations, following an early adoption by the Company of ASC 825-10 Fair Value Option and Tower's election to apply the fair value option to the Facility Agreement.

The effect of the election of fair value option to the Facility Agreement as of January 1, 2007 was a gain of \$65,207 which has been recorded as a cumulative-effect adjustment to retained loss (no tax effects have been recorded).

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 12 - LONG-TERM LOANS FROM BANKS (cont.)

B. Facility Agreement (cont.)

Accounting for the Loans under the Facility Agreement (cont.)

The September 2008 amendment was accounted for by calculating the fair value of the remaining outstanding obligation to the Banks. The excess of the fair value of the obligation prior to the amendment over the fair value of the remaining obligation was considered settled (“the Settled Amount”). A gain on conversion of debt was recognized in the amount of the excess of the Settled Amount over the fair value of the equity equivalent capital notes issued. The fair value of the notes was calculated based on the price of the stock of Tower around September 25, 2008, the date of signing and closing of the definitive agreements with the Banks and TIC.

August 2009 amendment to the Facility Agreement - since the loans are carried at fair value, the fair value following the August 2009 amendment includes the effects of the amendment. The cost of the new warrants (all three tranches) granted pursuant to the August 2009 amendment and the additional cost of the existing warrants, which is determined based on the fair value at the date of the amendment, were expensed and recorded in financing expenses, as they relate to an item carried at fair value.

C. Repayment Schedule

The principal amount of the long-term loans as of December 31, 2009 is repayable as follows:

2011	\$72,530
2012	105,060
2013	52,530
	\$230,120

According to August 2009 amendment detailed in B above, following receipt by Tower of significant amounts of proceeds from a certain source, Tower will pay a portion of such proceeds on account of the outstanding loans prior to the due date specified above.

D. The Facility Agreement with the Banks restricts Tower’s ability to place liens on its assets (other than to the State of Israel in respect of investment grants - see Note 7C and to SanDisk - see Note 16D(2)), without the prior consent of the Banks. Furthermore, the agreements contain certain restrictive financial ratios and covenants. For further details concerning the Facility Agreement and its amendments, see Note 16A(5).

E. For long term bank loans of Jazz see Note 10.

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NOTE 13 - DEBENTURES

A. Composition:

	Interest rate	As of December 31, 2009		
		Carrying amount	Fair value	Total
2005 Convertible debentures series B	5	% \$6,976	\$--	\$6,976
2006 Convertible debentures series C	--	(*) 54,484	--	54,484
2007 Non-convertible debentures series D	8	% 31,434	--	31,434
2007 Convertible debentures series E, see Note 14	8	% --	37,342	37,342
			92,894	130,236
Jazz's Convertible notes	8	% 110,971	--	110,971
			\$203,865	\$241,207

(*) See D below.

	Interest rate	As of December 31, 2008		
		Carrying amount	Fair value	Total
2002 Convertible debentures series A (**)	4.7	% \$8,330	\$--	\$8,330
2005 Convertible debentures series B	5	% 5,283	--	5,283
2006 Convertible debentures series C	--	(*) 46,738	--	46,738
2007 Non-convertible debentures series D	8	% 29,614	--	29,614
2007 Convertible debentures series E, see Note 14	8	% --	16,825	16,825
			89,965	106,790
Jazz's Convertible notes	8	% 110,052	--	110,052
Less - current maturities			8,330	8,330
			\$191,687	\$208,512

(*) See D below.

(**) In January 2009, the outstanding amount was fully paid and the debentures were redeemed in full.

If on a payment date of the principal or interest on the debentures (series B-E) there exists an infringement of certain covenants and conditions under the Facility Agreement, the dates for payment of interest and principal on the debentures may be postponed, depending on various scenarios under the Facility Agreement until such covenant or condition is settled. Such debentures and interest thereon are unsecured and subordinated to Tower's existing and future secured indebtedness, including indebtedness to the Banks under the Facility Agreement - see Note 16A(5), to SanDisk - see Note 16D(2) and to the government of Israel - see Note 7C.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 13 - DEBENTURES (cont.)

B. 2002 Convertible Debentures Series A

In 2002, Tower raised approximately \$24,300 in a public offering for the issuance of convertible debentures, the outstanding principal amounts of which as of December 31, 2009 is \$0. The debentures were linked to the Israeli Consumer Price Index ("CPI"), issued at 96% of their par value, and bore annual interest at the rate of 4.7%, payable in January of each year commencing in January 2003. The principal amount was payable in four equal installments in January of each year between 2006 and 2009. The debentures were convertible until December 31, 2008 into ordinary shares, at a conversion rate of one Ordinary Share per each NIS 41.00 principal amount of the debentures. In January 2009, the outstanding amount was fully paid and the debentures were redeemed in full.

C. 2005 Convertible Debentures Series B

In January 2006, Tower raised \$48,169 of convertible debentures by way of a rights offering based on a prospectus which became effective on December 2005, the outstanding principal amounts of which as of December 31, 2009 is \$10,550. The debentures are listed for trade on the Tel-Aviv Stock Exchange and on the NASDAQ Capital Market ("Series B"). The debentures accrue annual interest at the rate of 5% which will be payable, together with the principal of the debentures, in one installment in January 2012.

The debentures are convertible into Tower's ordinary shares at a conversion price of \$1.10 per share. The conversion price was subject to downward adjustment under certain circumstances if Tower had sold securities in future financings at a price per share which was lower than the conversion price, provided that such financings closed, or agreements for such financings were signed, through December 2006. No such adjustment was or will be required and the downward adjustment mechanism has expired.

In analyzing whether the conversion feature requires bifurcation, Tower considered whether the conversion feature would be classified as a liability or within shareholders' equity. To determine classification, the conversion feature must be analyzed under ASC Subtopic 815-40 "Contracts in Entity's Own Equity". The first step in the Subtopic analysis for these features is to determine whether the host contract is a conventional convertible instrument. Since the conversion feature in Series B contained, a reset provision that adjusts the conversion rate through 2006, Tower determined that Series B cannot be considered a "conventional convertible instrument". Since Series B does not qualify as conventional convertible debt, it must be analyzed to determine whether the conversion feature should be accounted for as a liability or as equity.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 13 - DEBENTURES (cont.)

C. 2005 Convertible Debentures Series B (cont.)

Tower considered the provisions of Series B and determined that the number of shares issuable upon conversion of the convertible instrument through 2006 is uncapped and thus requires bifurcation and treatment as derivative classified as liability. Such classification remained until the adjustment feature expired in 2006 and the number of shares issuable was fixed. The conversion feature was bifurcated using the “with and without” method and subsequently marked the conversion feature to fair value through profit and loss.

(i) In December 2006, the downward adjustment to the conversion rate expired resulting in the change to the embedded derivative such that it no longer requires bifurcation and the amount of the liability for the conversion option reclassified to shareholder' equity was \$28,377.

(ii) The remaining balance of unamortized discount as of December 31, 2009 and 2008 was \$3,573 and 5,398, respectively.

SanDisk Corporation, Alliance Semiconductor Corporation and Macronix International Co. Ltd. (collectively, the “Primary Wafer Partners”) and TIC have invested \$27,811 in the framework of the rights offering.

As part of the September 2008 definitive agreement with the Banks and TIC, \$20,000 in convertible debentures series B were converted into equity equivalent capital notes of Tower, see Note 12B.

The outstanding principal amounts of convertible debentures Series B as of December 31, 2009 and 2008 were \$10,550 and \$10,681, respectively.

D. 2006 Convertible Debentures Series C

In 2006, Tower raised approximately \$31,219 in a public offering of convertible debentures linked to the CPI and issued at 85% of the par value, together with options each exercisable for three months ending on September 27, 2006 for NIS 100 principal amount of convertible debentures at an exercise price equal to 85% of their face amount, linked to the CPI. Such options were exercised fully to convertible debentures. In addition, Tower issued warrants Series 4, exercisable for three years ending on June 28, 2009 for one ordinary share of Tower at a price of NIS 7.40. On January 1, 2009, following the adoption of EITF 07-5 as codified in ASC 815-40, warrants Series 4 were reclassified from equity to liabilities through their expiration in June 2009.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 13 - DEBENTURES (cont.)

D. 2006 Convertible Debentures Series C (cont.)

The convertible debentures were convertible into Tower's ordinary shares at a conversion rate of one ordinary share per NIS 8.40 principal amount of convertible debentures. The conversion price was subject to a reduction feature until June 2008, according to which the conversion rate of Series C was reduced in July 2008 from NIS 8.4 to NIS 4.31. The convertible debentures carry a zero coupon with principal payable at maturity in December 2011, at a premium of 37% over principal value, linked to the CPI.

The outstanding principal amounts of the convertible debentures as of December 31, 2009 and 2008 were \$55,439 and \$56,150, respectively.

The net proceeds received were allocated to each of the components in the units sold using the relative fair value method. Tower determined the fair values of each component using the average quoted prices at the first 2 days of trading. The allocation to each component was as follow:

	Fair Values	Amount allocated
Total net proceeds received for the units issued as of issuance date		\$ 28,752
Proceeds allocated to convertibles debentures as of issuance date based on relative fair value	\$ 31,402	\$ 26,735
Proceeds allocated to short term options to purchase additional debentures	246	210
Proceeds allocated to long term warrants	1,513	1,287
Proceeds allocated to short term warrants	611	520
Total allocated	\$ 33,772	\$ 28,752

Tower further bifurcated the conversion feature from the convertible debt using the "with and without" method. That bifurcation was done, as a next step, after the determination of the allocated proceeds described above. Following the adoption of EITF 07-5 as codified in ASC 815-40, on January 1, 2009, the conversion feature was reclassified from equity to liabilities.

The embedded feature was measured at fair value using a valuation technique that utilizes the discounted cash flows of Black-Scholes and Monte Carlo simulation. The Monte Carlo simulation was used to incorporate the possible adjustment of the conversion rate in different scenarios. The key inputs included were interest rate, the spot price of Tower's share and its volatility.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 13 - DEBENTURES (cont.)

E. 2007 Non-Convertible Debentures Series D and Convertible Debentures Series E

In the second half of 2007, Tower consummated a private placement with Israeli institutions of long-term convertible and non-convertible debentures and warrants, by which Tower raised gross proceeds of approximately \$40,000. In the funding, 342 units were sold, each comprised of: (i) long-term non-convertible-debentures, repayable in six equal annual installments between the dates of December 2011 and December 2016, with a face amount of NIS 250,000 (approximately \$59.7) linked to the CPI and carrying an annual interest rate of 8 percent (“series D”); (ii) long-term convertible-debentures repayable in December 2012 with a face amount of NIS 262,500 (approximately \$62.7) linked to the CPI, carrying an annual interest of 8 percent (“series E”). Convertible debentures series E were convertible into Tower’s ordinary shares at a conversion rate of one ordinary share per NIS 17.2 principal amount of convertible debentures and (iii) 5,800 warrants series 6, which were exercisable until 2011, for one Tower Ordinary Share at a price of \$2.04. The conversion price of Convertibles debentures series E was subject to adjustments under certain limited circumstances during a two year period. According to such terms, the conversion price was reduced from NIS 17.2 to NIS 4.15. Convertibles debentures series E are carried at fair value through profit and loss and the effect of the reduction in conversion price was reflected in the mark to market of the convertibles. The conversion price of warrants series 6 was subject to adjustments under certain limited circumstances during a two year period. Under such circumstances, the conversion price was reduced from \$2.04 to \$1.06. Warrants series 6 were classified as liabilities and carried at fair value due to the existence of the ratchet described above. After the exercise price was adjusted and the ratchet expired, the warrants were adjusted to fair value through earnings and reclassified to equity.

In September 2007, Tower expanded its series of long-term debentures and warrants by selling 12,118 units, each comprised of long-term non-convertible debentures, with a face amount of NIS 2,500 (approximately \$0.62), long-term convertible debentures, with a face amount of NIS 2,625 (approximately \$0.65), and 58 warrants. The debentures were issued at 90% of par value and with the other same terms as the debentures and the warrants issued in the private placement. In this expansion, Tower raised gross proceeds of approximately \$14,000.

The outstanding principal amounts of series D as of December 31, 2009 and 2008 were \$34,121 and \$32,632, respectively.

The outstanding principal amounts of series E as of December 31, 2009 and 2008 were \$37,659 and \$36,095, respectively.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 13 - DEBENTURES (cont.)

F. Convertible Notes Issued By Jazz

In 2006, Jazz completed private placements of convertible notes. The convertible notes bear interest at a rate of 8% per annum payable semi-annually and mature in December 2011. The convertible notes may be redeemed for cash at a redemption price equal to par plus accrued and unpaid interest plus a redemption premium equal to 2% in the year beginning December 31, 2009 until December 31, 2010 and 0% thereafter.

As of December 31, 2009, the holders of the convertible notes have the option to convert the convertible notes into Tower's ordinary shares based on an implied conversion price of \$4.07 per Tower ordinary share. Jazz's obligations under the convertible debentures are not being guaranteed by Tower.

As of December 31, 2009 and 2008, \$123,334 and \$128,200, respectively in principal amount of convertible notes were outstanding.

According to the terms of the notes, Tower has the right to deliver, in lieu of shares, cash or a combination of cash and Tower ordinary shares to satisfy the conversion obligation. The amount of such cash and Tower ordinary shares, if any, will be based on the trading price of Tower's ordinary shares during the 20 consecutive trading days beginning on the third trading day after proper delivery of a conversion notice.

Jazz's obligations under the convertible debentures are guaranteed by Jazz's wholly owned domestic subsidiaries.

Upon the occurrence of certain specified fundamental changes, the holders of the convertible debentures will have the right, subject to various conditions and restrictions, to require Jazz to repurchase the convertible debentures, in whole or in part, at par plus accrued and unpaid interest to, but not including, the repurchase date.

NOTE 14 - FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS

The Company makes certain disclosures with regard to financial instruments, including derivatives. These disclosures include, among other matters, the nature and terms of derivative transactions, information about significant concentrations of credit risk and the fair value of financial assets and liabilities.

A. Interest Rate Derivatives

A derivative is typically defined as an instrument whose value is derived from an underlying instrument, index or rate, has a notional amount, requires no or little initial investment and can be net settled.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 14 - FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (cont.)

A. Interest Rate Derivatives (cont.)

ASC Topic 815 “Derivatives and Hedging” requires that all derivatives be recorded in the financial statements at their fair value at the date of the financial statements. The changes in the fair value of the derivatives are charged to the statement of operations unless designated as a hedging item in a cash flows hedge at which time changes are classified in other comprehensive income, to the extent effective.

Tower, from time to time, enters into agreements to hedge variable interest rate exposure on long-term loans. Tower uses interest rate collar agreements, some with knock-out and knock-in features to hedge its LIBOR-based variable long-term debt cash flow exposure. The knock-out feature was set above the cap level and the knock-in feature was set below the floor level. The derivatives, although used as economic hedges, are not treated as hedges for accounting purposes. The changes in fair value are recorded immediately in earnings.

As of December 31, 2009 and 2008, Tower had outstanding agreements to economically hedge interest rate exposure on loans drawn down under the Facility Agreement, the aggregate amount of \$120,000 and \$200,000, respectively. These agreements resulted in a loss of \$1,552 and \$2,097 for the years ended December 31, 2009 and 2008, respectively and resulted in a gain of \$1,074 for the year ended December 31, 2007.

The Company does not hold or issue derivative financial instruments for non-hedging purposes.

B. Concentration of Credit Risks

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, short-term bank deposits, trade receivables and government agencies receivables. The Company's cash and cash equivalents are maintained with large and reputable banks, and the composition and maturities of investments are regularly monitored by the Company. Generally, these securities may be redeemed upon demand and bear minimal risk.

The Company generally does not require collateral insurance, however, in certain circumstances the Company maintains a credit insurance policy or may require letters of credit. An allowance for doubtful accounts is determined with respect to those amounts that were determined to be doubtful of collection. The Company performs ongoing credit evaluations of its customers, see Note 18.

The Company is exposed to credit-related losses in respect of derivative financial instruments in a manner similar to the credit risk involved in the realization or collection of other types of assets. The Company believes that its exposure to credit risk is immaterial considering its overall position with the Banks that are the counterparty to the derivatives.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 14 - FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (cont.)

C. Fair Value of Financial Instruments

The estimated fair values of the Company's financial instruments, excluding long-term debentures and long-term Banks loans, do not materially differ from their respective carrying amounts as of December 31, 2009 and 2008. The fair values of Tower and Jazz's debentures, based on quoted market prices as of December 31, 2009 and 2008, were \$240,272 and \$60,264, respectively compared to carrying amounts of \$241,207 and \$208,512, for the above dates, respectively.

D. Fair Value Measurements

Fair values were determined, as follows:

- For Tower's loans based on the income approach using a present value technique - the cash flows used in the technique reflect the cash stream expected to be used to satisfy the obligation over its economic life. The Company discounted expected cash flows as forecasted each quarter using the appropriate discount rate for the applicable maturity.
 - For Embedded Derivatives and Warrants - the Company utilized the Black Scholes Merton formula.
- For Over the Counter derivatives - the Company used the market approach using quotation from independent brokers and dealers.
 - For Tower's convertible debentures series E - the market approach using quoted market prices was used.

Recurring Fair Value Measurements Using the Indicated Inputs:

	December 31, 2009	Quoted prices in active market for identical liability (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Convertible debentures series E	\$37,342	\$37,342	\$--	\$ --
Tower's long-term debt	167,606	--	--	167,606
Derivatives	3,502	--	3,502	--
Warrants and previously bifurcated conversion option	12,779	745	--	12,034
	\$221,229	\$38,087	\$3,502	\$ 179,640

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NOTE 14 - FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (cont.)

D. Fair Value Measurements

Liabilities measured on a recurring basis using significant unobservable inputs (Level 3):

	Long-term debt	Convertible debentures series E	Warrants and previously bifurcated conversion option
As of January 1, 2009 - at fair value	\$ 202,989	\$ 16,825	\$ --
Reclassification of warrants and previously bifurcated conversion option from equity to liability - see Note 2T - Initial Adoption of New Standards - ASC 815-40-15	--	--	89
Warrants exercise	--	--	(1,325)
Decrease in bifurcated conversion option due to conversions	--	--	(477)
Total losses (gains) unrealized in earnings	(35,383)	5,922	13,747
Transfer out of level 3	--	(22,747)	--
As of December 31, 2009 - at fair value	\$ 167,606	\$ --	\$ 12,034
Unrealized losses (gains) recognized in earnings from liabilities held at period end	\$ (35,383)	\$ 5,922	\$ 13,747

Recurring Fair Value Measurements Using the Indicated Inputs:

	December 31, 2008	Quoted prices in active market for identical liability (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Convertible debentures series E	\$ 16,825	\$--	\$--	\$ 16,825
Long-term debt	202,989	--	--	202,989
Derivatives	3,236	--	3,236	--
	\$ 223,050	\$--	\$ 3,236	\$ 219,814

Liabilities measured on a recurring basis using significant unobservable inputs (Level 3):

	Long-term debt	Convertible debentures series E	Derivatives
As of January 1, 2008 - at fair value	\$365,563	\$28,484	\$7,313
Total losses (gains) recognized in earnings	2,670	(11,659)	(3,406)
Conversion of Bank loans under the Definitive Agreements with the Banks and TIC, see Note 12B	(165,244)	--	--
Reclassification of previously bifurcated conversion option to shareholders' equity	--	--	(3,907)
As of December 31, 2008 - at fair value	\$202,989	\$16,825	\$--
Unrealized losses (gains) recognized in earnings from liabilities held at period end	\$6,301	\$(11,659)	\$(3,406)

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TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 15 - OTHER LONG-TERM LIABILITIES

	As of December 31,	
	2009	2008
Accrued severance pay and other employee benefit plans, see B and C below	\$26,770	\$27,880
Long-term liability to a Primary Wafer Partner net of current maturity, see Notes 16A(4) and 16D(2)	4,929	710
Deferred tax liability	11,195	11,749
Warrants and previously bifurcated conversion option	12,034	--
Others (*)	5,460	5,620
	\$60,388	\$45,959

(*)Includes \$1,370 and \$718 as of December 31, 2009 and 2008, respectively, of interest payable to related parties in regard to convertible debentures Series B, see also Note 13C.

B. Employee Termination Benefits

Israeli law and labor agreements determine the obligations of Tower to make severance payments to dismissed employees and to employees leaving employment under certain circumstances. Generally, the liability for severance pay benefits, as determined by Israeli Law, is based upon length of service and the employee's monthly salary. This liability is primarily covered by regular deposits made each month by Tower into recognized severance and pension funds and by insurance policies purchased by Tower, based on the employee's salary for the relevant month. The amounts so funded and the liability are reflected separately on the balance sheets in long-term investments and other long-term liabilities, respectively. Commencing January 1, 2005, Tower started implementing a labor agreement with regard to most of its employees, according to which monthly deposits into recognized severance and pension funds or insurance policies release it from any additional severance obligation to its employees and therefore Tower incurs no liability or asset, since that date. Any net severance pay amount as of such date will be released on the employee's termination date. Payments relating to Israeli employee termination benefits were approximately \$2,496, \$4,018 and \$3,323 for 2009, 2008 and 2007, respectively.

C. Employee Benefit Plans

The following information recognizes the periodic expenses and changes in benefit obligations in the years ended December 31, 2009 and 2008 due to the new bargaining agreement effective May 2, 2008 entered into by Jazz with its collective bargaining unit employees.

TOWER SEMICONDUCTOR LTD. AND SUBSIDIARIES
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NOTE 15 - OTHER LONG-TERM LIABILITIES (cont.)

C. Employee Benefit Plans (cont.)

Postretirement Medical Plan

The components of the net periodic benefit cost and other amounts recognized in other comprehensive income (loss) for postretirement medical plan expense are as follows:

	Year ended December 31, 2009	Year ended December 31, 2008
Net periodic benefit cost		
Service cost	\$ 178	\$ 46
Interest cost	463	126
Expected return on the plan's assets	--	--
Amortization of transition obligation (asset)	--	