

AMPAL-AMERICAN ISRAEL CORP
Form 10-Q
November 13, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2003

OR

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

For the transition period from _____ to _____

Commission file number 0-538

AMPAL-AMERICAN ISRAEL CORPORATION

(Exact Name of Registrant as Specified in Its Charter)

New York

13-0435685

(State or Other Jurisdiction of
Incorporation of Organization)

(I.R.S. Employer
Identification Number)

555 Madison Avenue, New York, New York

10022

(Address of Principal Executive Offices)

(Zip code)

Registrant's Telephone Number, Including Area Code (212) 593-9842

Former Name, Former Address and Former Fiscal Year, If Changed Since Last Report.

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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

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Yes No

The number of shares outstanding of the issuer's Class A Stock, its only authorized common stock, is 19,732,506 (as of November 6, 2003).

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

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ITEM 1. FINANCIAL STATEMENTS

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES CONSOLIDATED STATEMENTS OF OPERATIONS

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| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|---|-------------|-------------|
| (Dollars in thousands, except per share amounts) | (Unaudited) | (Unaudited) |
| REVENUES | | |
| Equity in earnings of affiliates | \$ 1,925 | \$ 1,301 |
| Interest | 420 | 830 |
| Real estate income | 6,686 | 5,647 |
| Realized and unrealized gains (losses) on investments | 24,662 | (7,573) |
| Gain on sale of real estate rental property | - | 141 |
| Other | 7,490 | 7,753 |
| | <hr/> | <hr/> |
| Total revenues | 41,183 | 8,099 |
| | <hr/> | <hr/> |
| EXPENSES | | |
| Interest | 4,381 | 6,129 |
| Real estate expenses | 6,212 | 5,804 |
| Loss from impairment of investments & real estate | 10,884 | 13,561 |
| Minority interests | 1,463 | 289 |
| Translation loss (gain) | 2,739 | (1,877) |
| Other (mainly general and administrative) | 6,987 | 5,501 |
| | <hr/> | <hr/> |
| Total expenses | 32,666 | 29,407 |
| | <hr/> | <hr/> |
| Gain (loss) before income taxes | 8,517 | (21,308) |
| Benefit (provision) for income taxes | 1,067 | (5,464) |
| | <hr/> | <hr/> |
| Net gain (loss) | \$ 9,584 | \$ (26,772) |
| | <hr/> | <hr/> |
| Basic EPS: | | |
| Gain (loss) per Class A share | \$ 0.48 | \$ (1.38) |
| | <hr/> | <hr/> |
| Shares used in calculation (in thousands) | 19,706 | 19,501 |
| | <hr/> | <hr/> |
| Diluted EPS: | | |
| Gain (loss) per Class A shares | \$ 0.43 | \$ (1.38) |
| | <hr/> | <hr/> |
| Shares used in calculation (in thousands) | 22,103 | 19,501 |
| | <hr/> | <hr/> |

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

ITEM 1. FINANCIAL STATEMENTS

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

| THREE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--|-------------|-------------|
| (Dollars in thousands, except per share amounts) | (Unaudited) | (Unaudited) |
| REVENUES | | |
| Equity in earnings of affiliates | \$ 1,731 | \$ 261 |
| Interest | 153 | 216 |

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| THREE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|---|-----------------|--------------------|
| Real estate income | 2,301 | 1,991 |
| Realized and unrealized (losses) on investments | (1,680) | (736) |
| Other | 2,751 | 2,437 |
| Total revenues | 5,256 | 4,169 |
| EXPENSES | | |
| Interest | 747 | 1,951 |
| Real estate expenses | 2,291 | 2,024 |
| Loss from impairment of investments | 2,751 | 7,481 |
| Minority interests | 368 | 92 |
| Translation loss (gain) | 426 | (920) |
| Other (mainly general and administrative) | 2,404 | 2,018 |
| Total expenses | 8,987 | 12,646 |
| (Loss) before income taxes | (3,731) | (8,477) |
| Benefit (provision) for income taxes | 5,251 | (2,962) |
| Net gain (loss) | \$ 1,520 | \$ (11,439) |
| Basic EPS: | | |
| Gain (loss) per Class A share | \$ 0.07 | \$ (0.58) |
| Shares used in calculation (in thousands) | 19,724 | 19,654 |
| Diluted EPS: | | |
| Gain (loss) per Class A shares | \$ 0.07 | \$ (0.58) |
| Shares used in calculation (in thousands) | 22,103 | 19,654 |

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

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

| ASSETS AS OF | September 30, 2003 | December 31, 2002 |
|---|-----------------------|----------------------|
| (Dollars in thousands) | (Unaudited) | (Audited) |
| Cash and cash equivalents | \$ 3,043 | \$ 1,557 |
| Deposits, notes and loans receivable | 12,052 | 10,962 |
| Investments | 233,729 | 215,094 |
| Real estate property, less accumulated depreciation of \$16,327 and \$8,748 | 64,986 | 65,598 |

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| | September 30, 34,863 | December 31, 30,488 |
|--------------|-------------------------|------------------------|
| Other assets | <u>34,863</u> | <u>30,488</u> |
| | | |
| Total Assets | \$ 348,673 | \$ 323,699 |

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

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

| LIABILITIES AND SHAREHOLDERS' EQUITY AS OF | September 30, 2003 | December 31, 2002 |
|---|-----------------------|----------------------|
| (Dollars in thousands except per share amounts) | (Unaudited) | (Audited) |
| LIABILITIES | | |
| Notes and loans payable | \$ 134,461 | \$ 114,257 |
| Debentures | 3,851 | 22,546 |
| Accounts payable, accrued expense and others | 96,545 | 86,718 |
| | <u>234,857</u> | <u>223,521</u> |
| SHAREHOLDERS EQUITY | | |
| 4% Cumulative Convertible Preferred Stock, \$5 par value; authorized 189,287 shares; issued 132,962 and 139,391 shares; outstanding 129,612 and 136,041 shares | 665 | 697 |
| 6-1/2% Cumulative Convertible Preferred Stock, \$5 par value; authorized 988,055 shares; issued 697,380 and 706,450 shares; outstanding 574,844 and 583,914 shares | 3,487 | 3,532 |
| Class A Stock; \$1 par value; authorized 60,000,000 shares; issued 25,562,160 and 25,502,805 shares; outstanding 19,730,496 and 19,671,141 shares | 25,562 | 25,503 |
| Additional paid-in capital | 58,143 | 58,125 |
| Retained earnings | 77,059 | 67,475 |
| Treasury Stock, at cost | (31,096) | (31,096) |
| Accumulated other comprehensive loss | (20,004) | (24,058) |

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| | | |
|---|----------------------|---------------------|
| LIABILITIES AND | September 30, | December 31, |
| Total shareholders' equity | 113,816 | 100,178 |
| | <hr/> | <hr/> |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | \$ 348,673 | \$ 323,699 |
| | <hr/> | <hr/> |

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

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--|--------------------|--------------------|
| (Dollars in thousands) | (Unaudited) | (Unaudited) |
| Cash flows from operating activities: | | |
| Net gain (loss) | \$ 9,584 | \$ (26,772) |
| Adjustments to reconcile net (gain) loss to net cash provided by operating activities: | | |
| Equity in earnings of affiliates | (1,925) | (1,301) |
| Realized and unrealized (gain) losses on investments | (24,662) | 7,573 |
| Gain on sale of real estate rental property | - | (141) |
| Depreciation expense | 1,640 | 1,618 |
| Net amortization | (1,081) | 13 |
| Loss from impairment of investments and loans | 10,884 | 13,561 |
| Translation loss (gain) | 2,739 | (1,877) |
| Minority interests | 1,463 | 289 |
| (Increase) decrease in other assets | (4,513) | 8,519 |
| Increase in accounts payable, accrued expenses and others | 6,439 | 4,455 |
| Investments made in trading securities | (39,845) | (3,235) |
| Proceeds from sale of trading securities | 41,418 | 4,514 |
| Dividends received from affiliates | 3,529 | 83 |
| | <hr/> | <hr/> |
| Net cash provided by operating activities | 5,670 | 7,299 |
| | <hr/> | <hr/> |
| Cash flows from investing activities: | | |
| Deposits, notes and loans receivable collected | 1,888 | 3,393 |
| Deposits, notes and loans receivable granted | (3,363) | (1,089) |
| Investments made in affiliates and others | (1,200) | (1,726) |
| Proceeds from sale of real estate property, net | 1,100 | 264 |
| Return of capital by partnership | 157 | 209 |
| Capital improvements | (2,851) | (1,133) |
| Change of minority interest due to acquisition | 1,464 | - |
| | <hr/> | <hr/> |
| Net cash used in investing activities | (2,805) | (82) |
| | <hr/> | <hr/> |

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

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

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| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--|-------------------|-------------------|
| (Dollars in thousands) | (Unaudited) | (Unaudited) |
| Cash flows from financing activities: | | |
| Notes and loans payable received | \$ 21,725 | \$ 1,235 |
| Notes and loans payable repaid | (3,893) | (13,114) |
| Proceeds from exercise of stock options | - | 1,974 |
| Debentures repaid | (19,271) | (1,763) |
| | <u> </u> | <u> </u> |
| Net cash used in financing activities | (1,439) | (11,668) |
| | <u> </u> | <u> </u> |
| Effect of exchange rate changes on cash and cash equivalents | 60 | (2,337) |
| | <u> </u> | <u> </u> |
| Net increase (decrease) in cash and cash equivalents | 1,486 | (6,788) |
| Cash and cash equivalents at beginning of period | 1,557 | 7,973 |
| | <u> </u> | <u> </u> |
| Cash and cash equivalents at end of period | \$ 3,043 | \$ 1,185 |
| | <u> </u> | <u> </u> |
| Supplemental Disclosure of Cash Flow Information | | |
| Cash paid during the period: | | |
| Interest paid to others | \$ 5,067 | \$ 5,844 |
| | <u> </u> | <u> </u> |
| Income taxes paid | \$ 103 | \$ 225 |
| | <u> </u> | <u> </u> |
| Supplemental Disclosure of Non-cash Investing Activities: | | |
| Investments in investees | 780 | - |
| | <u> </u> | <u> </u> |

The accompanying notes are an integral part of the consolidated financial statement.

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--|-------------------|-------------------|
| (Dollars in thousands, except share amounts) | (Unaudited) | (Unaudited) |
| 4% PREFERRED STOCK | | |
| Balance, beginning of year | \$ 697 | \$ 731 |
| Conversion of 6,429 and 3,480 shares into Class A Stock | (32) | (17) |
| | <u> </u> | <u> </u> |
| Balance, end of period | \$ 665 | \$ 714 |
| | <u> </u> | <u> </u> |
| 6-1/2% PREFERRED STOCK | | |
| Balance, beginning of year | \$ 3,532 | \$ 3,633 |
| Conversion of 9,070 and 20,230 shares into Class A Stock | (45) | (101) |
| | <u> </u> | <u> </u> |
| Balance, end of period | \$ 3,487 | \$ 3,532 |
| | <u> </u> | <u> </u> |

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| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|---|------------------|------------------|
| CLASS A STOCK | | |
| Balance beginning of year | \$ 25,503 | \$ 25,408 |
| Issuance of shares upon conversion of Preferred Stock | 59 | 78 |
| Balance, end of period | <u>\$ 25,562</u> | <u>\$ 25,486</u> |
| ADDITIONAL PAID-IN CAPITAL | | |
| Balance, beginning of year | \$ 58,125 | \$ 58,253 |
| Conversion of Preferred Stock | 18 | 40 |
| Issuance of shares upon exercise of stock options | - | (168) |
| Balance, end of period | <u>\$ 58,143</u> | <u>\$ 58,125</u> |
| RETAINED EARNINGS | | |
| Balance, beginning of year | \$ 67,475 | \$ 111,740 |
| Net gain (loss) | 9,584 | (26,772) |
| Balance, end of period | <u>\$ 77,059</u> | <u>\$ 84,968</u> |

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

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--|--------------------|--------------------|
| (Dollars in thousands, except share amounts) | (Unaudited) | (Unaudited) |
| TREASURY STOCK | | |
| 4% PREFERRED STOCK | | |
| Balance, end of period | <u>(84)</u> | <u>(84)</u> |
| 6-1/2% PREFERRED STOCK | | |
| Balance, end of period | <u>(1,853)</u> | <u>(1,853)</u> |
| CLASS A STOCK | | |
| Balance, beginning and end of period - 5,831,664 and 6,160,664 shares, at cost | (29,159) | (31,301) |
| Issuance of shares upon exercise of 329,000 stock options | - | 2,142 |
| Balance, end of period | <u>(29,159)</u> | <u>(29,159)</u> |
| Balance, end of period | <u>\$ (31,096)</u> | <u>\$ (31,096)</u> |

ACCUMULATED OTHER COMPREHENSIVE LOSS

Cumulative translation adjustments:

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| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|---|--------------------|--------------------|
| Balance, beginning of year | (20,750) | (20,163) |
| Foreign currency translation adjustment | (99) | (2,171) |
| Balance, end of period | <u>(20,849)</u> | <u>(22,334)</u> |
| Unrealized gain on marketable securities: | | |
| Balance, beginning of year | (3,308) | 4,856 |
| Unrealized gain (loss), net | 2,940 | (14,713) |
| Sale of available-for-sale securities | 1,213 | (701) |
| Balance, end of period | <u>845</u> | <u>(10,558)</u> |
| Balance, end of period | <u>\$ (20,004)</u> | <u>\$ (32,892)</u> |

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

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE GAIN (LOSS)

| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--|--------------------|--------------------|
| (Dollars in thousands) | (Unaudited) | (Unaudited) |
| Net gain (loss) | <u>\$ 9,584</u> | <u>\$ (26,772)</u> |
| Other comprehensive gain (loss), net of tax: | | |
| Foreign currency translation adjustments | (99) | (2,171) |
| Unrealized gain(loss) on securities | 2,940 | (14,713) |
| Other comprehensive income(loss) | <u>2,841</u> | <u>(16,884)</u> |
| Comprehensive gain (loss) | <u>\$ 12,425</u> | <u>\$ (43,656)</u> |
| Related tax(expense) on other comprehensive gain (loss): | | |
| Foreign currency translation adjustments | \$ (98) | \$ (120) |
| Unrealized (loss) on securities | \$ (1,662) | \$ (2,507) |

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

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

- As used in these financial statements, the term the Company refers to Ampal-American Israel Corporation (Ampal) and its consolidated subsidiaries.

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2. The September 30, 2003 consolidated balance sheet presented herein was derived from the audited December 31, 2002 consolidated financial statements of the Company.

Reference should be made to the Company's consolidated financial statements for the year ended December 31, 2002 for a description of the accounting policies, which have been continued without change. Also, reference should be made to the notes to the Company's December 31, 2002 consolidated financial statements for additional details of the Company's consolidated financial condition, results of operations and cash flows. The details in those notes have not changed except as a result of normal transactions in the interim. All adjustments (of a normal recurring nature) which are, in the opinion of management, necessary to a fair presentation of the results of the interim period have been included.

3. Recently Issued Accounting Pronouncements

In January 2003, the FASB issued FASB Interpretation No. 46 Consolidation of Variable Interest Entities (FIN 46). Under FIN 46 entities are separated into two populations: (1) those for which voting interests are used to determine consolidation (this is the most common situation) and (2) those for which variable interests are used to determine consolidation. FIN 46 explains how to identify Variable Interest Entities (VIE) and how to determine when a business enterprise should include the assets, liabilities, non-controlling interests, and results of activities of a VIE in its consolidated financial statements.

FIN 46 is effective as follows: for variable interests in variable interest entities created after January 31, 2003, FIN 46 shall apply immediately, for variable interests in variable interest entities created before that date, the FIN shall apply for calendar year-end company as of December 31, 2003. The Company does not expect the adoption of FIN 46 to have a material effect on its consolidated financial statements.

4. Employee Stock Based Compensation

The Company accounts for all plans under APB Opinion No. 25, under which no compensation costs were incurred. The following table illustrates the effect on net income and net loss and EPS as if the Company had applied the fair value-recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation, to stock based incentive plans for the periods indicated below:

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| Nine Months Ended September 30 | 2003 | 2002 |
|--|----------|----------------------------|
| (In thousands, except per share data) | | |
| Basic EPS: | | |
| Net gain (loss): | | |
| As reported ⁽¹⁾ | \$ 9,420 | \$ (26,942) |
| Less-stock based compensation expense determined under fair value method | (370) | (7,358) |
| Pro forma | \$ 9,050 | \$ (34,300) |
| As reported | \$ 0.48 | \$ (1.38) |
| Pro forma | \$ 0.46 | \$ (1.76) |
| Diluted EPS: | | |
| Net gain (loss): | | |
| As reported | \$ 9,584 | \$ (26,942) ⁽²⁾ |
| Less-stock based compensation expense determined under fair value method | (370) | (7,358) |
| Pro Forma | \$ 9,214 | (34,300) |

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| Nine Months Ended September 30 | 2003 | 2002 |
|--------------------------------|---------|-----------|
| As Reported | \$ 0.43 | \$ (1.38) |
| Pro forma | \$ 0.42 | \$ (1.76) |

| Three Months Ended September 30 | 2003 | 2002 |
|--|----------|----------------------------|
| (In thousands, except per share data) | | |
| Basic EPS: | | |
| Net gain (loss): | | |
| As reported ⁽¹⁾ | \$ 1,465 | \$ (11,496) |
| Less-stock based compensation expense determined under fair value method | (124) | (66) |
| Pro forma | \$ 1,341 | \$ (11,562) |
| As reported | \$ 0.07 | \$ (0.58) |
| Pro forma | \$ 0.07 | \$ (0.59) |
| Diluted EPS: | | |
| Net gain (loss): | | |
| As reported | \$ 1,520 | \$ (11,496) ⁽²⁾ |
| Less-stock based compensation expense determined under fair value method | (124) | (66) |
| Pro forma | \$ 1,396 | \$ (11,562) |
| As Reported | \$ 0.07 | \$ (0.58) |
| Pro forma | \$ 0.06 | \$ (0.59) |

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⁽¹⁾After deduction of accrued Preferred Stock Dividend of \$164 and \$170 (for the three months \$55 and \$57) respectively.

⁽²⁾In 2002, the conversion of the 4% and 6-1/2% Preferred Stock was excluded from the diluted EPS calculation due to the antidilutive effect.

Under SFAS No. 123, the fair value of each option is estimated on the date of grant using the Black Scholes option-pricing model with the following assumptions: (1) expected life of options; (2) dividend yield; (3) volatility; and (4) risk-free interest rate. For the periods of nine and three months ended September 30, 2003 and 2002, no options were granted. The fair value generated by the Black-Scholes model may not be indicative of the future benefit, if any, that may be received by the optionholder.

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5. Segment information presented below results primarily from operations in Israel.

| NINE MONTHS ENDED SEPTEMBER 30, | 2003 | 2002 |
|--------------------------------------|------------|-------------|
| (Dollars in thousands) | | |
| <u>Revenues:</u> | | |
| Finance | \$ 31,122 | \$ (202) |
| Real Estate | 6,686 | 5,785 |
| Leisure-time | 1,505 | 1,272 |
| Intercompany adjustments | (55) | (57) |
| | <hr/> | <hr/> |
| Total | \$ 39,258 | \$ 6,798 |
| | <hr/> | <hr/> |
| <u>Pretax Operating Gain (Loss):</u> | | |
| Finance | \$ 9,352 | \$ (22,162) |
| Real Estate | (1,447) | (19) |
| Leisure-time | 150 | (139) |
| | <hr/> | <hr/> |
| Total | \$ 8,055 | \$ (22,320) |
| | <hr/> | <hr/> |
| <u>Total Assets:</u> | | |
| Finance* | \$ 266,361 | \$ 247,052 |
| Real Estate | 68,566 | 68,565 |
| Leisure-Time | 16,467 | 15,406 |
| Intercompany adjustments | (2,721) | (4,431) |
| | <hr/> | <hr/> |
| Total | \$ 348,673 | \$ 326,592 |
| | <hr/> | <hr/> |

*Includes an investment in MIRS Communications Ltd. of \$111 million.

Corporate office expense is principally applicable to the financing operations and has been charged to that segment above. Revenues exclude equity in earnings of affiliates and pretax operating gain (loss) excludes equity in earnings of affiliates and minority interests.

The real estate segment consists of rental property owned in Israel leased to unrelated parties and of the operations of Am-Hal Ltd., the Company's wholly-owned subsidiary which owns and operates a chain of senior citizens facilities located in Israel. The leisure-time segment consists primarily of Coral World International Limited (marine parks located around the world) and Country Club Kfar Saba (the company's 51%-owned subsidiary located in Israel).

6. The following table summarizes securities that were outstanding as of September 30, 2003 and 2002, but not included in the calculations of diluted earnings per Class A share because such shares are anti-dilutive.

| (Shares in thousands) | September 30, | |
|------------------------|---------------|-------|
| | 2003 | 2002 |
| Options and Rights | 1,338 | 3,132 |
| 6-1/2% Preferred Stock | -- | 584 |
| 4% Preferred Stock | -- | 139 |

7. Legal Proceedings

Yakhin Hakal

Further to the legal proceedings description in the 2002 financial statements, on July 15, 2003, the Israeli Supreme Court dismissed the appeal filed by the Company on March 12, 2002, regarding the Tel Aviv District Court's previous decision to dismiss the Company's request for a preliminary injunction and other remedies in relation to the validity and enforceability of Etz Vanir's and Yakhin Mataim's decisions to redeem the debentures owned by the Company and to require the Company to surrender all of its preferred shares in Etz Vanir and Yakhin Mataim for approximately \$0.8 million.

MIRS

A petition to certify a class action against MIRS in the amount of NIS 170 million (\$36 million) was filed in the Tel Aviv District Court in September 2001. The claim is in connection with the change in MIRS' tariffs resulting from the implementation of MIRS' own dialing prefix, which replaced its previous dialing prefix, the Tel-Aviv area code. As a result, persons in the Tel Aviv area code claimed that they are subject to higher tariffs than those they had been subject to under MIRS' previous dialing prefix. On May 14, 2003 the petitioners withdrew their claim.

A petition to certify a class action against MIRS and the other three cellular operators in Israel in the total amount of NIS 600 million (\$127 million) was filed in the Tel Aviv District Court in May 2002. The claim involves the inter-connect fees that were collected from the customers of the other operators with regard to phone calls that were made to voice recorder applications through the cellular operators' dialing numbers. On June 22, 2003 the petitioners withdrew their claim.

AMPAL (ISRAEL) LTD.

In May 2002, the Israeli Income Tax Authority issued an assessment to Ampal (Israel) Ltd., the Company's wholly-owned subsidiary, for payment of approximately NIS 34 million (\$7,655,933) for the tax years 1997-2000. Ampal (Israel) filed an appeal regarding this assessment. In October, 2003, Ampal and the Israeli Income Tax Authority signed a settlement agreement pursuant to which Ampal agreed to pay the sum of NIS 6 million (\$1,351,047) as a final payment for the tax years 1997-2000. The reserve previously established to cover the Company's estimated exposure has been adjusted accordingly.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

CRITICAL ACCOUNTING POLICIES

The preparation of Ampal's consolidated financial statements is in conformity with accounting principles generally accepted in the United States which requires management to make estimates and assumptions in certain circumstances that affect amounts reported in the accompanying consolidated financial statements and related footnotes. Actual results may differ from these estimates. To facilitate the understanding of Ampal's business activities, described below are certain Ampal accounting policies that are relatively more important to the portrayal of its financial condition and results of operations and that require management's subjective judgments. Ampal bases its judgments on its experience and various other assumptions that it believes to be reasonable under the circumstances. Please refer to Note 1 to Ampal's consolidated financial statements included in the Annual Report for the year ended December 31, 2002 for a summary of all of Ampal's significant accounting policies.

Portfolio Investments

The Company accounts for a number of its investments, including many of its investments in the high-technology and communications industries, on the basis of the cost method. Application of this method requires the Company to periodically review these investments in order to determine whether to maintain the current carrying value or to write off some or all of the investment. While the Company uses some objective measurements in its review, such as the portfolio company's liquidity, burn rate, termination of a substantial number of employees, achievement of milestones set forth in its business plan or projections and seeks to obtain relevant information from the company under review, the review process involves a number of judgments on the part of the Company's management. These judgments include assessments of the likelihood of the company under review to obtain additional financing, to achieve future milestones, make sales and to compete effectively in its markets. In making these judgments the Company must also attempt to anticipate trends in the particular company's industry as well as in the general economy. There can be no guarantee that the Company will be accurate in its assessments and judgments. To the extent that the Company is not

correct in its conclusion it may decide to write down all or part of the particular investment.

Investment in MIRS

MIRS is our largest investment and is being accounted for at cost (our equity interest is 25%). The cost method is applied due to preference features we have been granted in our investment in preferred shares in MIRS. Revenues from guaranteed payments from Motorola are recognized as income. We perform annual tests for impairment regarding our investment.

Marketable Securities

We determine the appropriate classification of marketable securities at the time of purchase. To date, we hold marketable securities classified as trading securities that are carried at fair value, and marketable securities classified as available-for-sale that are carried at fair value with unrealized gains and losses included in the component of accumulated other comprehensive loss in stockholders' equity. If according to management's assessment it is determined that a decline in the fair value of the available-for-sale securities is other than temporary, an impairment loss is recorded and included in the consolidated statements of income as loss from impairment of investments.

Long-Lived Assets

On January 1, 2002, Ampal adopted FAS 144, Accounting for the Impairment or Disposal of Long-Lived Assets. FAS 144 requires that long-lived assets, to be held and used by an entity, be reviewed for impairment and, if necessary, written down to the estimated fair values, whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable through undiscounted future cash flows.

Accounting for Income Taxes

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves us estimating our current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the statement of operations. A valuation allowance is currently set against certain tax assets because management believes it is more likely than not that these deferred tax assets will not be realized through the generation of future taxable income. We also do not provide for taxes on undistributed earnings of our foreign subsidiaries, as it is our intention to reinvest undistributed earnings indefinitely outside the United States.

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Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and our future taxable income for purposes of assessing our ability to realize any future benefit from our deferred tax assets. In the event that actual results differ from these estimates or we adjust these estimates in future periods, our operating results and financial position could be materially affected.

Recently Issued Accounting Pronouncements

In January 2003, the FASB issued FASB Interpretation No. 46 Consolidation of Variable Interest Entities (FIN 46). Under FIN 46 entities are separated into two populations: (1) those for which voting interests are used to determine consolidation (this is the most common situation) and (2) those for which variable interests are used to determine consolidation. FIN 46 explains how to identify Variable Interest Entities (VIE) and how to determine when a business enterprise should include the assets, liabilities, non-controlling interests, and results of activities of a VIE in its consolidated financial statements.

FIN 46 is effective as follows: for variable interests in variable interest entities created after January 31, 2003, FIN 46 shall apply immediately, for variable interests in variable interest entities created before that date, the FIN shall apply for calendar year-end Company as of December 31, 2003. The Company does not expect the adoption of FIN 46 to have a material effect on its consolidated financial statements.

Results of Operations

Nine months ended September 30, 2003 compared to nine months ended September 30, 2002:

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Ampal-American Israel Corporation (Ampal) and its subsidiaries (the Company) recorded a consolidated net gain of \$9.6 million for the nine months ended September 30, 2003, as compared to a net loss of \$26.8 million for the same period in 2002. The increase in net gain is primarily attributable to the realized and unrealized gains on investments to a decrease in losses from impairment of investments and tax benefits in the nine months ended September 30, 2003, as compared to the realized and unrealized losses on investment and a tax provision in the same period of fiscal 2002. This increase in net gain was partially offset by an increase in other expenses and a translation loss for the nine months ended September 30, 2003 as compared to a translation gain in the same period of fiscal 2002.

In the nine month period ended September 30, 2003, the Company recorded \$24.7 million of realized and unrealized gains on investments, as compared to \$7.6 million of realized and unrealized losses in the same period in 2002. The gains recorded in the nine months ended September 30, 2003 are mainly attributable to the gains from the Company's investment in Blue Square Israel Ltd. (Blue Square) (\$2.6 million) and Granite Hacarmel Investments Ltd. (Granite) (\$18.2 million). During the nine months ended September 30, 2003, the Company sold approximately 10% of its interest in Granite. Consequently, the Company's investment in Granite, which was previously accounted for by the equity method, was accounted for as an investment in a trading marketable security. The realized and unrealized losses recorded in the nine month period ended September 30, 2002, were primarily attributable to the Company's investment in shares of Bank Leumi Le Israel B.M. (Leumi), Alvarion Ltd. (Alvarion) and Sonic Foundry, Inc. (Sonic).

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Equity in earnings of affiliates increased to \$1.9 million for the nine months ended September 30, 2003 from \$1.3 million for the same period in 2002. The increase in 2003 is primarily attributable to a \$3.3 million gain recorded by Ophir Holdings Ltd. (Ophir), (42.5%-owned by the Company) as a result of the sale of its real estate assets. The gain was offset by a \$1.7 million loss in Granite, which was recorded in the first quarter of 2003.

Real estate income increased to \$6.7 million for the nine months ended September 30, 2003, as compared to \$5.6 million for the same period in 2002. The increase is attributable to the higher number of units sold in Am-Hal Ltd., the Company's 100%-owned subsidiary, which owns and operates a chain of senior citizen facilities in Israel.

In the nine month period ended September 30, 2003, the Company recorded \$10.9 million in losses from the impairment of its investments in XACCT Technologies Ltd (XACCT) (\$9.0 million), Identify Solutions Ltd. (Identify) (\$1.3 million) and real estate in Migdal Haemek (\$0.6 million). In the same period in 2002, the Company recorded a \$13.6 million loss from the impairment of its investments.

The Company recorded a translation loss of \$2.7 million in the nine months ended September 30, 2003 as compared to a translation gain of \$1.9 million in the same period in 2002. The translation loss in 2003 and the translation gain in 2002 are attributable to the revaluation and devaluation of the new Israeli shekel against the U.S. dollar in the respective periods.

The Company recorded lower interest expense (\$4.4 million) in the nine months ended September 30, 2003, as compared to the \$6.1 million in the same period in 2002, primarily as a result of lower interest rates.

The Company recorded higher other expenses in the nine months ended September 30, 2003 as compared to the same period in 2002, primarily as a result of higher rates in Directors and Officers liability insurance premiums.

In the nine months ended September 30, 2003, the Company recorded a tax benefit of \$1.1 million as compared to a provision for tax of \$5.5 million in the same period in 2002. The change in the effective income tax rate in 2003 as compared to 2002 is attributable to a tax adjustment resulted from the settlement agreement reached with the Israeli Tax Authority in October 2003.

Three months ended September 30, 2003 compared to three months ended September 30, 2002:

The consolidated net gain increased to \$1.5 million for the three months ended September 30, 2003 as compared to a net loss of \$11.4 million for the same period in 2002. The increase in net gain is primarily attributable to a decrease in losses from impairment on investments to the increase in equity in earnings of affiliates and a tax benefit recorded in the three months ended September 30, 2003 as compared to a provision for tax in the same period in 2002. These increases were partially offset by the increase in realized and unrealized losses on investments, and a translation loss in the three months ended September 30, 2003, as compared to a translation gain in the same period in 2002.

In the three-month period ended September 30, 2003, the Company recorded a \$1.7 million realized and unrealized loss on investments, as compared to a \$0.7 million realized and unrealized losses on investments in the same period of fiscal 2002. The losses recorded in 2003 are primarily attributable to the Company's investment in Granite (\$2.0 million). The \$0.7 million realized and unrealized loss on investments recorded in the three months ended September 30, 2002 is attributable to the Company's investment in Bank Leumi Le Israel B.M. (Leumi).

Equity in earnings of affiliates increased to \$1.7 million for the three months ended September 30, 2003, from \$0.3 million for the same period in 2002. The increase is primarily attributable to a \$1.7 million gain recorded by Ophir as a result of the sale of one of its real estate assets.

In the three-month period ended September 30, 2003, the Company recorded \$2.7 million in losses from the impairment of its investments in XACCT Technologies Ltd (XACCT), while in the same period in 2002, the Company recorded a \$7.5 million loss from the impairment of its investments.

The Company recorded a translation loss of \$0.4 million in the three months ended September 30, 2003 as compared to a translation gain of 0.9 million in the same period in 2002. The translation loss in 2003 and the translation gain in 2002 are attributable to the revaluation and devaluation of the new Israeli shekel against the U.S. dollar in the respective periods.

The Company recorded lower interest expense (\$0.7 million) in the three months ended September 30, 2003, as compared to \$2.0 million in the same period in 2002, primarily as a result of lower interest rates.

The Company recorded higher other expenses in the three months ended September 30, 2003 as compared to the same period of 2002, primarily as a result of higher rates in Directors and Officers liability insurance premiums.

In the three months ended September 30, 2003, the Company recorded a tax benefit of \$5.3 million as compared to a tax provision of \$3.0 million in the same period in 2002. The tax benefits are attributable to a \$0.8 million adjustment with respect to a settlement reached by Ampal (Israel) with the Israeli Tax Authority related to the tax assessment issued for tax years 1997-2000, and to a \$5 million decrease in the valuation allowance due to the high likelihood of utilizing capital losses in subsidiaries in Israel from the gain on the sale of marketable securities.

Liquidity and Capital Resources

Cash Flows

On September 30, 2003, cash and cash equivalents were \$3.0 million, as compared with \$1.6 million at December 31, 2002.

The Company's sources of cash include cash and cash equivalents, marketable securities, cash from operations, cash from investing activities and amounts available under credit facilities, as described below. The Company believes that these sources are sufficient to fund the current requirements of operations, capital expenditures, investing activities, dividends on preferred stock and other financial commitments of the Company for the next 12 months. However, to the extent that contingencies and payment obligations described below and in other parts of this Report require the Company to make unanticipated payments, the Company would need to further utilize these sources of cash. To the extent that the Company intends to rely on the sale of its unpledged marketable securities in order to satisfy its cash needs, it is subject to the risk of a shortfall in the amount of proceeds from any such sale as compared with the anticipated sale proceeds due to a decline in the market price of those securities. In the event of a decline in the market price of its marketable securities, the Company may need to draw upon its other sources of cash, which may include additional borrowing, refinancing of its existing indebtedness or liquidating other assets, the value of which may also decline. In addition, the shares of MIRS owned by the Company have already been pledged as security for specific loans provided to the Company for the purchase of these shares and would therefore be unavailable if the Company wished to pledge them in order to provide an additional source of cash.

Cash flows from operating activities

Net cash provided by operating activities totaled approximately \$5.7 million for the nine months ended September 30, 2003, as compared to approximately \$7.3 million for the same period in 2002. The decrease is primarily attributable to the increase in other assets. This decrease was partially offset by the dividends received from the affiliates and a net gain (after adjustments), in 2003 as compared to a net loss in 2002.

Cash flows from investing activities

Net cash used in investing activities totaled approximately \$2.8 million for the nine months ended September 30, 2003, as compared to approximately \$0.1 million used in investing activities for the same period in 2002. The increase in investing activities is primarily attributable to an increase of deposits in banks.

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Cash flows from financing activities

Net cash used in financing activities was approximately \$1.4 million at September 30, 2003, as compared to approximately \$11.7 million at September 30, 2002. The decrease in the cash used in 2003 is primarily attributable to the pay down of notes and loans repayments (\$3.9 million and \$13.1 million in 2003 and 2002, respectively).

Investments

On September 30, 2003, the aggregate fair value of trading and available-for-sale securities was approximately \$62.5 million, as compared to \$18.6 million at December 31, 2002. The increase in 2003 is attributable to the change in the accounting treatment of the shares of Granite as described above, the purchase of various trading securities (mostly debentures) and to increases in the market value of marketable securities.

During fiscal 2003, the Company made a \$1.2 million investment.

On January 6, 2003, the Company entered into a definitive agreement to sell its holding in Carmel Container Systems Ltd (Carmel), a packaging manufacturer based in Israel. On June 2, 2003, the Company announced that the agreement has been cancelled due to the fact that the Israeli Antitrust Authority has objected to the merger between Carmel and Best Carton Ltd., a merger that was a condition precedent to the closing of the sale of the Ampal group's holdings in Carmel to a subsidiary of Carmel.

Debt

In connection with its investment in MIRS, the Company has two long-term loans from Bank Hapoalim Ltd. (Hapoalim) and Bank Leumi le-Israel B.M. (Leumi) in the outstanding amount of \$37.3 million and \$34.9 million, respectively, as of September 30, 2003. Both loans are due on March 31, 2008 and bear interest at a rate of LIBOR plus 0.8%. Other than as described in this paragraph, the loans are non-recourse to the Company and are secured by the Company's shares in MIRS. The principal payments are due as follows: 10% on March 31, 2004, 15% on March 31, 2005 and 25% on each of March 31, 2006, 2007 and 2008. Interest is required to be paid annually on March 31 of each year from March 31, 2002 until and including March 31, 2008. These loans are subject to the compliance by MIRS with covenants regarding its operations and financial results. As a result of renegotiations with the bank regarding the covenants, Leumi will have recourse to the Company for an additional \$0.5 million beginning in 2006 with respect to the Company's repayment obligations under the loan.

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On March 31, 2003, the Company redeemed 17.5 million in principal amount of its outstanding debentures. The transaction was financed by a loan from Bank Hapoalim, the principal repayments of which are due as follows: 50% on April 1, 2006, and 10% on each of April 1, 2004, 2005, 2006, 2007 and 2008. The loan bears interest at a rate of libor plus 2.5% on the 50% of the loan which is to be repaid on April 1, 2006 and libor plus 2.4% on the balance of the loan. The interest is payable semi-annually on October 1 and April 1 of each year. The loan is secured by certain of the Company's marketable securities and the Company's investment in Ophir Holdings Ltd. As of September 30, 2003, the company had \$3.9 million in debentures outstanding with interest rates of 7.5%. These debentures, which mature in 2005, are secured by \$3.9 million in cash held in a secured account.

The Company financed a portion of the development of Am-Hal, a wholly-owned subsidiary which develops and operates luxury retirement centers for senior citizens, through bank loans from Hapoalim. At September 30, 2003, the amounts outstanding under these loans were \$10.2 million, as compared to \$12.7 million at December 31, 2002. The loans are dollar linked, mature through 2007-2010 and have interest rates of LIBOR plus 2.25%. The Company generally repays these loans with the proceeds received from deposits and other payments from the apartments in Am-Hal facilities. The loans are secured by a lien on Am-Hal's properties. The Company also issued guarantees in the amount of \$4.6 million in favor of clients of Am-Hal in order to secure their deposits.

The Company finances its operations and other financial commitments through short-term borrowings, mainly from Hapoalim. The term of these borrowings is up to one year. The weighted average interest rates and the balances of these short-term borrowings at September 30, 2003 and December 31, 2002 were 3.9% on \$42.6 million and 4.03% on \$39.8 million, respectively.

As of September 30, 2003, the Company had issued guarantees on certain outstanding loans to its investees and subsidiaries in the aggregate principal amount of \$11.6 million. This includes:

\$0.5 million guarantee to Leumi with respect to the MIRS loan as described above.

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\$5.7 million guarantee on indebtedness incurred by Bay Heart (\$3.8 million of which is recorded as a liability in the Company's financial statements) in connection with the development of its property. There can be no guarantee that Bay Heart will become profitable or that it will generate sufficient cash to repay its outstanding indebtedness without relying on the Company's guarantee.

\$4.6 million guarantee to Am-Hal tenants as described above.

\$0.8 million guarantee to Galha 1960 Ltd.

FOREIGN CURRENCY CONTRACTS

The Company's derivative financial instruments consist of foreign currency forward exchange contracts. These contracts are utilized by the Company, from time to time, to manage risk exposure to movements in foreign exchange rates. None of these contracts have been designated as hedging instruments. These contracts are recognized as assets or liabilities on the balance sheet at their fair value, which is the estimated amount at which they could be settled based on market prices or dealer quotes, where available, or based on pricing models. Changes in fair value are recognized currently in earnings.

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FORWARD LOOKING STATEMENTS

This Quarterly Report (including but not limited to factors discussed above, in the Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as those discussed elsewhere in this Quarterly Report on Form 10-Q) includes forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) and information relating to the Company that are based on the beliefs of management of the Company as well as assumptions made by and information currently available to the management of the Company. When used in this Quarterly Report, the words anticipate, believe, estimate, expect, intend, plan, and similar expressions, as they relate to the Company or the management of the Company, identify forward-looking statements. Such statements reflect the current views of the Company with respect to future events or future financial performance of the Company, the outcome of which is subject to certain risks and other factors which could cause actual results to differ materially from those anticipated by the forward-looking statements, including among others, the economic and political conditions in Israel, the Middle East, including the situation in Iraq, and the global business and economic conditions in the different sectors and markets where the Company's portfolio companies operate.

Should any of those risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results or outcome may vary from those described herein as anticipated, believed, estimated, expected, intended or planned. Subsequent written and oral forward-looking statements attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by the cautionary statements in this paragraph and elsewhere described in this quarterly Report and other Reports filed with the Securities and Exchange Commission.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

MARKET RISKS AND SENSITIVITY ANALYSIS

The Company is exposed to various market risks, including changes in interest rates, foreign currency rates and equity price changes. The following analysis presents the hypothetical loss in earnings, cash flows and fair values of the financial instruments which were held by the Company at September 30, 2003, and are sensitive to the above market risks.

During the nine months ended September 30, 2003, there have been no material changes in the market risk exposures facing the Company as compared to those the Company faced in the fiscal year ended December 31, 2002.

Interest Rate Risks

At September 30, 2003, the Company had financial assets totaling \$14 million and financial liabilities totaling \$138.3 million. For fixed rate financial instruments, interest rate changes affect the fair market value but do not impact earnings or cash flows. Conversely, for variable rate financial instruments, interest rate changes generally do not affect the fair market value but do impact future earnings and cash flows, assuming other factors are held constant.

At September 30, 2003, the Company had fixed rate financial assets of \$6.9 million and variable rate financial assets of \$7.1 million. Holding other variables constant, a ten percent increase in interest rates would decrease the unrealized fair value of the fixed financial assets by

approximately \$0.1 million.

At September 30, 2003, the Company had fixed rate debt of \$13.7 million and variable rate debt of \$124.6 million. A ten percent decrease in interest rates would increase the unrealized fair value of the fixed rate debt by approximately \$0.1 million.

The net decrease in earnings for the next year resulting from a ten percent interest rate increase would be approximately \$0.5 million, holding other variables constant.

Exchange Rate Sensitivity Analysis

The Company's exchange rate exposure on its financial instruments results from its investments and ongoing operations in Israel. During 2003, the Company entered into various foreign exchange forward purchase contracts to partially hedge this exposure. At September 30, 2003, the Company had open foreign exchange forward purchase contracts in the amount of \$6 million. Holding other variables constant, if there were a ten percent devaluation of the foreign currency, the Company's cumulative translation (loss) reflected in the Company's accumulated other comprehensive (loss) would increase by \$1.7 million, and in the statements of operations, a ten percent devaluation of the foreign currency would decrease net earnings in the amount of approximately \$3.1 million.

Securities Price Risk

The Company's investments at September 30, 2003, included marketable securities (trading and available-for-sale) which are recorded at fair value of \$62.5 million. Those securities have exposure to price risk. The estimated potential loss in fair value resulting from a hypothetical ten percent decrease in prices quoted on stock exchanges is approximately \$6.2 million.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's management with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)) as of the end of the period covered by this report. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures are effective. Notwithstanding the foregoing, a control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that it will detect or uncover failures within the Company to disclose material information otherwise required to be set forth in the Company's periodic reports.

Internal Control Over Financial Reporting

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

Part II OTHER INFORMATION

Item 1. Legal Proceedings

Yakhin Hakal

In February 1995, Yakhin Hakal and its affiliates commenced a legal proceeding in Tel Aviv District Court seeking to cause Etz Vanir and Yakhin Mataim to redeem the perpetual debentures owned by the Company for approximately \$700,000 and to require the Company to surrender all of its preferred shares of Etz Vanir and Yakhin Mataim for their par value (which is a nominal amount), on the alleged grounds that the perpetual debentures are debt and not equity investments. It is the Company's view that its investments in these companies, which were made in the 1950's, are equity investments and are not subject to redemption by these companies, other than upon liquidation.

On July 27, 1998, a Tel Aviv District Court ruled in favor of Yakhin Hakal, the manager and co-owner of the Company's 50%-owned affiliates Etz Vanir and Yakhin Mataim. The judge's decision allows Etz Vanir and Yakhin Mataim to redeem debentures owned by the Company for approximately \$800,000 and to require the Company to surrender all of its preferred shares of Etz Vanir and Yakhin Mataim for their par value. After the redemption and surrender, the Company will no longer have any interest in Etz Vanir or Yakhin Mataim.

On October 15, 1998, the Company filed an appeal with the Israeli Supreme Court in Jerusalem. On September 30, 2001, the Supreme Court dismissed the appeal filed by the Company, on the grounds that the Company failed to timely produce a guarantee to cover Yakhin Hakal's expenses in the appeal. On November 1, 2001, the Company filed a petition to the Israeli Supreme Court, contending that the dismissal of an appeal due to a delay in producing guarantees as part of the appeal is unreasonable and that the law allowing this should be changed. The petition was withdrawn by the Company on October 6, 2002.

On December 30, 2001, the Company filed a motion to allow it to file a new appeal in this case. The Supreme Court dismissed the motion on September 10, 2002.

On October 12, 2001, the Company filed a request with the Tel-Aviv District Court for a preliminary injunction and other remedies in relation to the validity and enforceability of Etz Vanir's and Yakhin Mataim's decisions to redeem the debentures owned by the Company and to require the Company to surrender all of its preferred shares in Etz Vanir and Yakhin Mataim. On January 28, 2002, the Tel Aviv District Court dismissed the request. On March 12, 2002, the Company filed an appeal with regard to this decision with the Israeli Supreme Court. On July 15, 2003, the Israeli Supreme Court dismissed the appeal.

MIRS

A petition to certify a class action against MIRS in the amount of NIS 170 million (\$36 million) was filed in the Tel Aviv District Court in September 2001. The claim is in connection with the change in MIRS' tariffs resulting from the implementation of MIRS' own dialing prefix, which replaced its previous dialing prefix, the Tel-Aviv area code. As a result, persons in the Tel Aviv area code claimed that they are subject to higher tariffs than those they had been subject to under MIRS's previous dialing prefix. On May 14, 2003 the petitioners withdrew their claim.

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AMPAL (ISRAEL) LTD.

In May 2002, the Israeli Income Tax Authority issued an assessment to Ampal (Israel) Ltd., the Company's wholly-owned subsidiary, for payment of approximately NIS 34 million (\$7,655,933) for the tax years 1997-2000. Ampal (Israel) filed an appeal regarding this assessment. In October, 2003, Ampal and the Israeli Income Tax Authority signed a settlement agreement pursuant to which Ampal agreed to pay the sum of NIS 6 million (\$1,351,047) as a final payment for the tax years 1997-2000. The reserve previously established to cover the Company's estimated exposure has been adjusted accordingly.

Item 2. Changes in Securities and Use of Proceeds
None.

Item 3. Defaults upon Senior Securities
None.

Item 4. Submission of Matters to a Vote of Security Holders

The Annual Meeting of Shareholders was held on September 16, 2003. The following proposals were approved by the margins indicated below:

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To elect seven (7) directors to the Board of Directors of the Company to hold office for one year terms and until their respective successors shall be elected and qualified:

| Names | For | Withheld Authority |
|-----------------------|------------|--------------------|
| Yosef A. Maiman | 12,391,622 | 144,687 |
| Jack Bigio | 12,303,106 | 233,203 |
| Leo Malamud | 12,320,933 | 215,376 |
| Dr. Joseph Yerushalmi | 12,504,148 | 32,161 |
| Michael Arnon | 12,089,165 | 447,144 |
| Yehuda Karni | 12,391,022 | 145,287 |
| Eitan Haber | 12,391,115 | 145,194 |

To ratify the nomination of Kesselman & Kesselman, a member firm of PricewaterhouseCoopers International Limited, as the independent auditors of the Company for the fiscal year ending December 31, 2003:

| For | Against | Abstain |
|------------|---------|---------|
| 12,523,900 | 6,302 | 6,107 |

Item 5. Other Information
None.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

11.1 Schedule Setting Forth Computation of Loss per Share of Class A Stock.

31.1 Certification of Jack Bigio pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Irit Eluz pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Jack Bigio and Irit Eluz pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K: None

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto dully authorized.

AMPAL-AMERICAN ISRAEL CORPORATION

BY: /S/ Jack Bigio

Jack Bigio
Chief Executive Officer
(Principal Executive Officer)

BY: /S/ Irit Eluz

Irit Eluz
CFO and Vice President - Finance
and Treasurer
(Principal Financial Officer)

BY: /S/ Alla Kanter

Alla Kanter
Vice President - Accounting
(Principal Accounting Officer)

BY: /S/ Giora Bar-Nir

Giora Bar-Nir
Controller
(Principal Accounting Officer)

Dated: November 13, 2003

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

Exhibit Index

| Exhibit No. | Description |
|-------------|---|
| 11.1 | Schedule Setting Forth Computation of Earnings Per Share of Class A Stock..... |
| 31.1 | Certification of Jack Bigio pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2 | Certification of Irit Eluz pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Jack Bigio and Irit Eluz pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |

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