AMPAL-AMERICAN ISRAEL CORP
Form 10-Q
May 10, 2005

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2005

OR

o 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
111 Arlozorov Street, Tel Aviv, Israel	62098
(Address of Principal Executive Offices)	(Zip code)

Registrant's Telephone Number, Including Area Code (866) 447-8636

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 x No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

The number of shares outstanding of the issuer s Class A Stock, its only authorized common stock, is 19,951,426 (as of May 2, 2005).

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

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ITEM 1. FINANCIAL STATEMENTS

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31,	**2005**	**2004**
(Dollars in thousands, except per share amounts)	**(Unaudited)**	**(Unaudited)**
REVENUES		
Equity in earnings of affiliates	$ 6,633	$ 1,916
Real estate income	2,336	2,174
Realized and unrealized gains on investments	4,027	830
Interest	127	128
Other	2,511	2,421
Total revenues	15,634	7,469
EXPENSES		
Interest	1,144	843
Real estate expenses	2,159	2,131
Loss from impairment of investments	-	1,463
Translation loss	564	1,227
Other (mainly general and administrative)	2,188	2,518
Total expenses	6,055	8,182
Gain (loss) before income taxes	9,579	(713)
Provision for income taxes	2,506	473
Gain (loss) after income tax	7,073	(1,186)
Minority interest	(345)	375
Net Gain (loss)	$ 6,728	$ (811)
Basic EPS:		
Gain (loss) per Class A share	$ 0.33	$ (0.04)
Shares used in calculation (in thousands)	19,925	19,793
Diluted EPS:		
Gain (loss) per Class A share	$ 0.30	$ (0.04)
Shares used in calculation (in thousands)	22,342	19,793

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

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

ASSETS AS OF	**March 31, 2005**	**December 31, 2004**
(Dollars in thousands)	**(Unaudited)**	**(Audited)**
Cash and cash equivalents	$ 21,025	$ 17,618
Deposits, notes and loans receivable	1,379	3,534
Marketable Securities	53,988	50,433
Other investment	117,660	127,023
Total Investments	171,648	177,456
Real estate property, less accumulated depreciation of $12,605 and $12,190	63,397	63,191
Other assets	46,043	43,148
Total Assets	$ 303,492	$ 304,947

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

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

LIABILITIES AND SHAREHOLDERS' EQUITY AS OF	March 31, 2005	December 31, 2004
(Dollars in thousands except per share amounts)	(Unaudited)	(Audited)
LIABILITIES		
Notes and loans payable	$ 119,114	$ 118,760
Debentures	-	2,036
Deposits from tenants	52,334	52,152
Accounts payable, accrued expense and others	24,078	26,002
Total Liabilities	195,526	198,950
Minority interests	6,303	5,984
SHAREHOLDERS EQUITY		
4% Cumulative Convertible Preferred Stock, $5 par value; authorized 189,287 shares; issued 122,408 and 124,024 shares; outstanding 119,058 and 120,674 shares	612	620
6-1/2% Cumulative Convertible Preferred Stock, $5 par value; authorized 988,055 shares; issued 643,419 and 662,219 shares; outstanding 520,883 and 539,683 shares	3,217	3,311
Class A Stock; $1 par value; authorized 60,000,000 shares; issued 25,779,783 and 25,715,303 shares; outstanding 19,948,119 and 19,883,639 shares	25,780	25,715
Additional paid-in capital	58,248	58,211
Retained earnings	64,252	57,524
Accumulated other comprehensive loss	(19,350)	(14,272)
Treasury Stock, at cost	(31,096)	(31,096)
Total shareholders' equity	101,663	100,013
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 303,492	$ 304,947

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

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

THREE MONTHS ENDED MARCH 31,	**2005**	**2004**
(Dollars in thousands)	**(Unaudited)**	**(Unaudited)**
Cash flows from operating activities:		
Net gain (loss)	$ 6,728	$ (811)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Equity in earnings of affiliates	(6,633)	(1,916)
Realized and unrealized gain on investments	(4,027)	(830)
Depreciation expense	521	538
Amortization of deposits from tenants	(494)	(448)
Impairment of investments and loans	-	1,463
Translation loss	564	1,227
Minority interests	345	(375)
Increase in other assets	(2,831)	(2,228)
Increase (decrease) in accounts payable, accrued expenses and others	3,504	(3,993)
Investments made in trading securities	(12,052)	(15,241)
Proceeds from sale of trading securities	16,996	31,835
Dividends received from affiliates	2,351	76
Net cash provided by operating activities	4,972	9,297
Cash flows from investing activities:		
Deposits, notes and loans receivable collected	2,066	4,850
Deposits, notes and loans receivable granted	-	(5,057)
Investments made in affiliates and others	(314)	(5,788)
Proceeds from sale of investments	1,066	1,522
Return of capital by partnership	-	35
Capital improvements	(649)	(214)
Net cash provided by (used in) investing activities	2,169	(4,652)

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

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

THREE MONTHS ENDED MARCH 31,	**2005**	**2004**
(Dollars in thousands)	**(Unaudited)**	**(Unaudited)**
Cash flows from financing activities:		
Notes and loans payable received	$ -	$ 6,247
Notes and loans payable repaid	(1,586)	(2,496)
Debentures repaid	(2,023)	(1,753)
Net cash (used in) provided by financing activities	(3,609)	1,998
Effect of exchange rate changes on cash and cash equivalents	(125)	(3,546)
Net increase in cash and cash equivalents	3,407	3,097
Cash and cash equivalents at beginning of period	17,618	4,572
Cash and cash equivalents at end of period	$ 21,025	$ 7,669
Supplemental Disclosure of Cash Flow Information		
Cash paid during the period:		
Interest paid to others	$ 1,162	$ 2,257
Income taxes paid	$ 23	$ 3,700
Supplemental Disclosure of Non-cash Investing Activities:		
Proceeds in tradable securities received from realization of an investment	3,316	2,267
Dividend in kind from an affiliate	6,541	-

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

(Dollars in thousands, except share amounts)	March 31 2005 (Unaudited)	December 31 2004 (Audited)
4% PREFERRED STOCK		
Balance, beginning of year	$ 620	$ 660
Conversion of 1,616 and 7,928 shares into Class A Stock	(8)	(40)
Balance, end of period	$ 612	$ 620
6-1/2% PREFERRED STOCK		
Balance, beginning of year	$ 3,311	$ 3,487
Conversion of 18,800 and 35,161 shares into Class A Stock	(94)	(176)
Balance, end of period	$ 3,217	$ 3,311
CLASS A STOCK		
Balance beginning of year	$ 25,715	$ 25,567
Issuance of shares upon conversion of Preferred Stock	65	148
Balance, end of period	$ 25,780	$ 25,715
ADDITIONAL PAID-IN CAPITAL		
Balance, beginning of year	$ 58,211	$ 58,143
Conversion of Preferred Stock	37	68
Balance, end of period	$ 58,248	$ 58,211
RETAINED EARNINGS		
Balance, beginning of year	$ 57,524	$ 76,109
Net gain (loss)	6,728	(18,385)
Dividends:		
4% Preferred Stock - $0.2 per share	-	(24)
6-1/2% Preferred Stock - $0.325 per share	-	(176)
Balance, end of period	$ 64,252	$ 57,524

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

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

(Dollars in thousands, except share amounts)	March 31, 2005 (Unaudited)	December 31, 2004 (Audited)
TREASURY STOCK		
4% PREFERRED STOCK		
Balance, end of period	(84)	(84)
6-1/2% PREFERRED STOCK		
Balance, end of period	(1,853)	(1,853)
CLASS A STOCK		
Balance, end of period	(29,159)	(29,159)
Balance, end of period	$ (31,096)	$ (31,096)

THREE MONTHS ENDED MARCH 31,	2005 (Unaudited)	2004 (Unaudited)
ACCUMULATED OTHER COMPREHENSIVE LOSS		
Cumulative translation adjustments:		
Balance, beginning of year	(20,083)	(20,597)
Foreign currency translation adjustment	(179)	(1,236)
Balance, end of period	(20,262)	(21,833)
Unrealized gain on marketable securities:		
Balance, beginning of year	5,811	2,750
Unrealized (loss)gain, net	(733)	769
Sale of available-for-sale securities	(4,166)	(334)
Balance, end of period	912	3,185
Balance, end of period	$ (19,350)	$ (18,648)

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

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

THREE MONTHS ENDED MARCH 31,	**2005**	**2004**
(Dollars in thousands)	**(Unaudited)**	**(Unaudited)**
Net Gain (loss)	$ 6,728	$ (811)
Other comprehensive gain (loss), net of tax:		
Foreign currency translation adjustments	(179)	(1,236)
Unrealized (loss) gain on securities	(733)	769
Other comprehensive (loss) income	(912)	(467)
Comprehensive income (loss)	$ 5,816	$ (1,278)
Related tax (expense) on other comprehensive gain:		
Foreign currency translation adjustments	$ (2)	$ 264
Unrealized gain on securities	$ (2,638)	$ (235)

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

AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

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

2. The March 31, 2005 consolidated financial statements should be read in conjunction with the audited financial statements and the notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2004.

Reference should be made to the Company s consolidated financial statements for the year ended December 31, 2004 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, 2004 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 December 2004, the FASB revised Statement No. 123 (FAS 123R), Share-Based Payment, which requires companies to expense the estimated fair value of employee stock options and similar awards. On April 14, 2005, the U.S. Securities and Exchange Commission adopted a new rule amending the compliance dates for FAS 123R. In accordance with the new rule, the accounting provisions of FAS 123R will be effective for the Company in fiscal 2006. The Company expects to adopt the provisions of FAS 123R using a modified prospective application.

Under such transition method, upon the adoption of SFAS 123R, Ampal s financial statements for periods prior to the effective date of the statement will not be restated. The impact of this statement on Ampal s financial statements or its results of operations in 2006 and beyond will depend upon various factors, among them Ampal s future compensation strategy. We expect that the effect of applying this statement on Ampal s results of operations in 2006 as it relates to existing option plans would not be materially different from the SFAS 123 pro forma effect previously reported.

4. Employee Stock Based Compensation

The Company accounts for all employee stock options plans under APB Opinion No. 25, under which no compensation costs were incurred.

SFAS No. 123 Accounting for Stock-Based Compensation (SFAS No. 123) established a fair value-based method of accounting for employee stock options of similar equity instruments and encourages adoption of such method for stock compensation plans. However, it also allows companies to continue to account for those plans using the accounting treatment prescribed by APB No. 25 and accordingly discloses pro forma data assuming the Company had accounted for employee stock option grants using the fair value based method as defined in SFAS in No. 123.

If compensation cost for the options under plans in effect been determined in accordance with SFAS No. 123, the Company net income (loss) and EPS would have been reduced as follows:

Three Months Ended March 31	2005	2004
(In thousands, except per share data)		
Basic EPS:		
Net Gain (loss):		
As reported[1]	$ 6,678	$ (864)
Less-stock based compensation expense Determined under fair value method	(219)	(131)
Pro forma	$ 6,459	$ (995)
As reported	$ 0.33	$ (0.04)
Pro forma	$ 0.32	$ (0.05)
Diluted EPS:		
Net Gain (loss):		
As reported	$ 6,728	$ (864)[2]
Less-stock based compensation expense Determined under fair value method	(219)	(131)
Pro Forma	$ 6,509	(995)
As Reported	$ 0.30	$ (0.04)
Pro forma	$ 0.29	$ (0.05)

1. After deduction of accrued Preferred Stock Dividend of $50 and $53 respectively.

2. In 2004, the effect of the conversion of the 4% and 6½% Preferred Stock was excluded from the basic and diluted EPS calculation due to its 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 of 5 years; (2) dividend yield of 0%; (3) volatility ranging from 57% to 60%; and (4) risk-free interest rate ranging from 3.3% to 3.46%.

For the period of three months ended March 31, 2004, 15,000 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 option holder.

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

THREE MONTHS ENDED MARCH 31,	**2005**	**2004**
(Dollars in thousands)		
Revenues:		
Finance	$ 6,098	$ 2,865
Real Estate	2,336	2,174
Leisure-time	581	532
Intercompany adjustments	(14)	(18)
	9,001	5,553
Equity	6,633	1,916
Total	$ 15,634	$ 7,469
Pretax Operating Gain (Loss):		
Finance	$ 2,740	$ (2,931)
Real Estate	92	200
Leisure-time	114	102
	2,946	(2,629)
Equity	6,633	1,916
Total	$ 9,579	$ (713)
Total Assets:		
Finance	$ 226,046	$ 267,322
Real Estate	64,622	65,753
Leisure-Time*	17,860	16,600
Intercompany adjustments	(5,036)	(4,189)
Total	$ 303,492	$ 345,486

Corporate office expense is principally applicable to the financing operations and has been charged to that segment above.

The real estate rental segment consists of rental property owned in Israel and leased in the United States and leased or subleased to unrelated parties, and of the operations of Am-Hal Ltd., a wholly-owned subsidiary which owns and operates a chain of senior citizen facilities located in Israel.

* The leisure-time segment consists primarily of Coral World International Limited (marine parks located in Israel and around the world) and Country Club Kfar Saba, the Company s 51%-owned subsidiary located in Israel.

5. The following table summarizes securities that were not included in the calculations of diluted earnings per Class A share for the three-month periods ended March 31, 2005 and 2004 because such shares are anti-dilutive.

(Shares in thousands)	**MARCH 31,**	
	2005	**2004**
Options and Rights	70	1,411
6-1/2% Preferred Stock	-	668
4% Preferred Stock	-	131

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6. LEGAL PROCEEDINGS:

Ampal Communications L.P.

1. On May 10, 2004, Ampal Communications L.P., a limited partnership controlled by Ampal and in which Ampal holds a 75% equity interest, filed a claim in the Tel-Aviv District Court against Motorola Communications Israel Ltd., Motorola Israel Ltd., Elisha Yanai, Peter Brum, Rami Guzman, Nathan Gidron, Shimon Tal and MIRS Communications Ltd. (collectively, the Defendants), for injunctive and declaratory relief as described below. The claim is in connection with the exploitation by the defendants of Ampal Communications minority rights by virtue of its 33% holding in MIRS Communications Ltd.

   Ampal Communications L.P. requested the Court to issue relief as follows:

   A. Declaring that the business of MIRS Communications Ltd. is conducted in such a way as to be prejudicial to the rights of Ampal Communications L.P. as a minority shareholder;

   B. Appointing an appraiser to conduct a valuation of MIRS Communications Ltd. and Ampal Communications L.P. s holdings therein, which will encompass a review of the way MIRS Communications Ltd. conducts its business, including a review of the related party transactions between MIRS Communications Ltd. and Motorola Israel Ltd. and/or any other of the Defendants;

   C. Instructing each of the Defendants to acquire and purchase from Ampal Communications L.P. the shares it holds in MIRS Communications Ltd. at the highest of the following prices:

      (1) based on a company valuation of MIRS Communications Ltd. as presented to Ampal Communications L.P. by Motorola prior to the signing of the Share Purchase Agreement for MIRS Communications Ltd.; or

      (2) based on the amount paid by Ampal Communications L.P. for its share holding in MIRS Communications Ltd. plus linkage to the Israeli consumer index and interest; or

      (3) based on the company valuation that will be determined by the valuation specified in Section B above, excluding any material negative effect brought about by the Defendants omissions and/or negligence in their management of MIRS Communications Ltd., all as may be assessed and computed by the appraiser specified in Section B above;

   D. Determining that each of the individual Defendants, as officers in MIRS Communications Ltd., has violated his respective fiduciary obligations towards Ampal Communications L.P. as a minority shareholder in MIRS Communications Ltd.; and

   E. Declaring that the Share Purchase Agreement pursuant to which Ampal Communications L.P. acquired its shareholding in MIRS Communications Ltd. and the Shareholders Agreement in respect thereof, are void.

2. On May 24, 2004 and on May 31, 2004 the Defendants requested the district court to strike out the claim in limine, on the grounds that Ampal had allegedly not paid sufficient fees when filing the claim, and further requested an extension of the time for filing statements of defense until after the district court had reached a decision regarding the request to strike out the claim. Ampal and the Defendants filed various responses and on June 30, 2004, the district court requested the Attorney General to furnish an opinion regarding the Defendants request before issuing its own decision. On October 11, 2004 the Attorney General furnished its opinion that supported the Defendants request that Ampal should pay the fees calculated on the basis of the value of the requested remedies in the claim. On November 10, 2004 Ampal filed its response. The Court also decided that the statements of defense should be filed 10 days after it issues its decision regarding the striking out of the claim. The Court has scheduled a hearing on this matter for June 1, 2005.

6. LEGAL PROCEEDINGS: (CONT.)

Ampal Communications L.P.

3. On March 1, 2005, Ampal requested the district court to enter judgment against Peter Brum on the grounds that he failed to file a defense to the Company s claim. On March 15, 2005, the district court granted Ampal s request and entered judgment against Peter Brum. On March 17, 2005, the district court ordered Mr. Brum to acquire and purchase from Ampal the shares it holds in MIRS for a total company valuation of $765,998,000, which is the highest of the prices set forth in the complaint. The litigation with regard to the other defendants is ongoing. Peter Brum, Motorola and MIRS have appealed the district court s judgment on numerous grounds. Ampal has filed responses to the appeal. The appellate court has not ruled on this appeal.

4. The Company has not received dividends from MIRS in the aggregate amount of $14.2 million, included among "other assets", due March 31, 2004 ($7.1 million) and March 31, 2005 ($7.1 million). The dividends were not received due to the legal dispute discussed above. As a result of not receiving the dividends, the principal and the interest of the loan which were due March 31, 2004 and March 31, 2005 were only partially paid.

7. SUBSEQUENT EVENT

On April 7, 2005, Am-Hal, Ltd. (Am-Hal), a wholly owned subsidiary of the Company, entered into an agreement to build a senior citizen facility in Tel-Aviv. The project, in which Am-Hal will hold a 75% interest, is projected to cost $50 million. The project, which is in its initial stages, is subject to regulatory and financing approvals. Am-Hal has paid $5.7 million to acquire real estate for the project. This payment was financed by Bank Hapoalim, and Ampal has deposited $1.6 million in Bank Hapoalim to secure Am-Hal's loan. If the project is not consummated, the $5.7 million payment will be refunded to Am-Hal, Am-Hal will repay its loan to Bank Hapoalim and the $1.6 million deposited by Ampal as security will be returned.

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, 2004 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. 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. We classify investment in marketable securities as investment in trading securities, if those securities are bought and held principally for the purpose of selling them in the near term (held for only a short period of time). All the other securities are classified as available for sale securities.

Statement of Financial Accounting Standards (SFAS) 115, Accounting for Certain Investments in Debt and Equity Securities, and Securities and Exchange Commission (SEC) Staff Accounting Bulletin (SAB) 59, Accounting for Noncurrent Marketable Equity Securities, provides guidance on determining when an investment is other-than-temporarily impaired. Investments are reviewed quarterly for indicators of other-than-temporary impairment. This determination requires significant judgment. In making this judgment, we evaluate, among other factors, the duration and extent to which the fair value of an investment is less than its cost; the financial health of the investee; and our intent and ability to hold the investment. Investments with an indicator are further evaluated to determine the likelihood of a significant adverse effect on the fair value and amount of the impairment as necessary. If market, industry and/or investee conditions deteriorate, we may incur future impairments.

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.

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