

AMPAL-AMERICAN ISRAEL CORP  
Form 10-K  
March 29, 2006

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**FORM 10-K**

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

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(Mark One)

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

For the fiscal year ended December 31, 2005

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**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**13-0435685**  
(I.R.S. Employer  
Identification No.)

**111 Arlozorov Street, Tel Aviv, Israel**  
(Address of Principal Executive Offices)

**62098**  
(Zip Code)

Registrant's telephone number, including area code (866) 447-8636  
Securities registered pursuant to Section 12(b) of the Act: None

**Securities registered pursuant to Section 12(g) of the Act:**  
**Class A Stock, par value \$1.00 per share**  
**4% Cumulative Convertible Preferred Stock, par value \$5.00 per share**  
**6 1/2% Cumulative Convertible Preferred Stock, par value \$5.00 per share**  
(Titles of Classes)

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

Securities registered pursuant to Section 12(g) of the Act: Class A Stock, par value \$1.00 per share 4% Cumulative

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Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K .

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

Yes  No

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes  No

The aggregate market value of the registrant's voting stock held by non-affiliates of the registrant on June 30, 2005, the last business day of the registrant's most recently completed second fiscal quarter was \$33,398,212 based upon the closing market price of such stock on that date. As of March 6, 2006, the number of shares outstanding of the registrant's Class A Stock, its only authorized and outstanding common stock is 20,157,772.

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AMPAL-AMERICAN ISRAEL CORPORATION AND SUBSIDIARIES

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**ANNUAL REPORT ON FORM 10-K  
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2005  
OF AMPAL-AMERICAN ISRAEL CORPORATION**

**PART I**

**ITEM 1. BUSINESS**

As used in this report (the Report), the term Ampal or registrant refers to Ampal-American Israel Corporation. The term Company refers to Ampal and its consolidated subsidiaries. Ampal is a New York corporation founded in 1942.

For industry segment financial information and financial information about foreign and domestic operations, see Note 13 to the Company's consolidated financial statements included elsewhere in this Report. The companies described below under Telecommunication, High Technology and Capital Markets and Other Holdings are included in the Finance segment. The companies described under Real Estate are included in the Real Estate segment. The companies described under Leisure-Time are included in the Leisure-Time segment.

The Company primarily acquires interests in businesses located in the State of Israel or that are Israel-related. Ampal's investment focus is principally on companies or ventures where Ampal can exercise significant influence, on its own or with investment partners, and use its management experience to enhance those investments. An important objective of Ampal is to seek investments in companies that operate in Israel initially and then expand abroad. In determining whether to acquire an interest in a specific company, Ampal considers quality of management, potential return on investment, growth potential, projected cash flow, investment size and financing, and reputable investment partners.

The Company's strategy is to invest opportunistically in undervalued assets with an emphasis on the following sectors: Energy, Real Estate and Project Development and Leisure Time. We believe that past experience, current opportunities and a deep understanding of the above-referenced sectors both domestically in Israel and internationally will allow the Company to bring high returns to its shareholders. The Company emphasizes investments which have long-term growth potential over investments which yield short-term returns.

The Company provides its investee companies with ongoing support through its involvement in the investees' strategic decisions and introduction to the financial community, investment bankers and other potential investors both in and outside of Israel.

On December 1, 2005, the Company acquired a 2% interest in East Mediterranean Gas Company, an Egyptian joint stock company which has been given the right to export natural gas from Egypt to Israel and other locations in the East Mediterranean basin. On October 3, 2005, the Company sold its interest in MIRS Communications Ltd. which it held through Ampal Communications L.P., a limited partnership controlled by Ampal and in which Ampal holds a 75% equity interest.

Listed below by industry segment are all of the substantial investee companies in which the Company had ownership interests as of December 31, 2005, the principal business of each and the percentage of equity owned, directly or indirectly, by Ampal. The table below also indicates whether the investee's securities are listed on the New York Stock Exchange ( NYSE ), NASDAQ National Market ( Nasdaq ), the American Stock Exchange ( AMEX ) or the Tel Aviv Stock Exchange ( TASE ). Further information with respect to the more significant investee companies is provided after the following table. For additional information concerning the investee companies, previously provided annual reports on Forms 10-K of Ampal are incorporated by reference herein.

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Industry Segment	Principal Business	Percentage as of December 31, 2005 <sup>(1)</sup>
<b>Energy</b>		
East Mediterranean Gas Company (E.M.G)	Natural Gas Provider & Pipeline Owner	2.0
<b>Real Estate</b>		
Am-Hal Ltd	Chain of Senior Citizen Facilities	100.0
Ampal (Israel) Ltd	Holding Company and Real Estate	100.0
Bay Heart Limited	Shopping Mall Owner/Lessor	37.0
Ophir Holdings Ltd. ("Ophir Holdings")	Holding Company	42.5
Lysh The Coastal High-way Ltd	Commercial Real Estate	10.6 <sup>(2)</sup>
Meimadim Investments Ltd.	Commercial Real Estate	4.2 <sup>(2)</sup>
New Horizons (1993) Ltd	Commercial Real Estate	34.0 <sup>(2)</sup>
<b>Leisure-Time</b>		
Coral World International Limited	Underwater Observatories and Marine Parks	50.0
Country Club Kfar Saba Limited	Country Club Facility	51.0
Hod Hasharon Sport Center (1992) Limited Partnership	Country Club Facility	50.0
<b>Finance:</b>		
<b>Capital Markets and Other Holdings</b>		
Ampal Development (Israel) Ltd	Holding Company	100.0
Ampal Holdings (1991) Ltd	Holding Company	100.0
Carmel Container Systems Limited	Packaging Materials and Carton Production	
	Holding Company	21.8
Fimi Opportunity Fund, L.P	Investment Fund	2.1
<b>High Technology</b>		
<b>Telecommunication</b>		
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(1) Based upon current ownership percentage. Does not give effect to any potential dilution.

(2) As of December 31, 2005, Ophir Holdings held the following percentage interests:

Lysh The Coastal High-way Ltd.	25.0
Meimadim Investments Ltd.	10.0
New Horizons (1993) Ltd.	80.0

The Company's percentage interest in the above-referenced companies set forth in the chart reflects the Company's 42.5% ownership of Ophir Holdings.

**Significant Developments Since the Fiscal Year Ended December 31, 2005**

None

**Energy**

**EAST MEDITERRANEAN GAS COMPANY ( EMG )**

On December 1, 2005, the Company, through Merhav Ampal Energy, Ltd., a wholly-owned subsidiary of the Company, entered into an agreement with Merhav M.N.F. Ltd. ( Merhav ) for the purchase from Merhav of a portion of its interest in EMG. Under the terms of the transaction, the Company acquired the beneficial ownership of 1,200 shares of EMG's capital stock, representing a 2% beneficial ownership in EMG. The purchase price for the shares was \$29,960,000. Additionally, the Company was granted the exclusive right to negotiate to acquire a substantial portion of Merhav's remaining shares of EMG. The Company also has the right for a period of time to require Merhav to repurchase the EMG interest.

EMG is an Egyptian joint stock company organized in accordance with the Egyptian Special Free Zones system which has been given the right to export natural gas from Egypt to Israel and other locations in the East Mediterranean basin and other countries. Egyptian natural gas shall reach the Israeli market via an underwater pipeline owned by EMG, which EMG expects to be completed during 2007. (See also Item 7. Related Party Transactions).

**Real Estate**

In Israel, most land is owned by the Israeli government. In this Report, reference to ownership of land means either direct ownership of land or a long-term lease from the Israeli Government, which in most respects is regarded in Israel as the functional equivalent of ownership. It is the Israeli government's policy to renew its long-term leases (which usually have a term of 49 years) upon their expiration.

**AM-HAL LTD. ( AM-HAL )**

Am-Hal is a wholly-owned subsidiary of the Company, which develops and operates luxury retirement centers for senior citizens.

In March 1992, the first center was opened in Rishon LeZion, a city located approximately 10 miles south of Tel-Aviv. This center, of about 120,000 square feet, includes 149 self-contained apartments, a 74-bed nursing care ward, a 21-bed assisted-living ward, a swimming pool, a health care center and other recreational facilities. The nursing care ward is leased to a non-affiliated health care provider until 2006.

In June 2000, the second center was opened in Hod Hasharon, a city located approximately 7 miles north of Tel Aviv. This center, which is approximately 250,000 square feet, includes 235 self-contained apartments, a 33-bed nursing care ward and a 22-bed assisted-living ward.

On April 7, 2005 Am-Hal Ltd. entered into an agreement to build a new project in Tel-Aviv. Am-Hal Ltd. holds 75% of the new project through a limited partnership (Ad 120 Ramat-Hahayal), the project, which is in its early stages, is still subject to further regulatory and financing approvals.

**AMPAL HOLDINGS (1991) LTD. ( AMPAL HOLDINGS )**

In 2004, as part of the Company's reorganization of certain of its wholly owned subsidiaries, Ampal Holdings purchased most of the high-tech investee companies from Ampal Industries (Israel) Ltd. In 2005, Ampal Holdings sold most of its investee companies.

**AMPAL (ISRAEL) LTD. ( AMPAL ISRAEL )**

In 2004, as part of the Company's reorganization of certain of its wholly owned subsidiaries, Ampal Israel purchased various investee companies from Ampal Industries (Israel) Ltd.

**OPHIR HOLDINGS LTD. ( OPHIR HOLDINGS )**

Ophir Holdings is a holding company that owns interests in real estate companies and is owned 42.5% by the Company. The Company and Polar Investments Ltd., which owns 57.5% of Ophir Holdings, are parties to a shareholders' agreement regarding joint voting, directorships and rights of first refusal with respect to Ophir Holdings.

Ophir Holdings owns a 25% equity interest in Lysh The Coastal High-way Ltd. ( Lysh ). Lysh has a 50% holding in Beit Herut-Lysh Development Company Ltd. ( BHL ), which is constructing a 180,000 square foot commercial project for rental near Moshav Beit Herut on land owned by the Israeli Land Authority. Ophir Holdings has also undertaken to provide guarantees in an amount equivalent to 25% of the construction costs. As of December 31, 2005, BHL had taken out bank loans of approximately \$14.3 million, by drawing on a credit line extended by a financial institution in connection with the project.

Ophir Holdings owns a 10% interest in a joint venture which had agreed to purchase 4.4 million square feet of land near Haifa for approximately \$15 million, on which the parties intend to develop a commercial real estate project for rent. Ophir Holdings has obligated itself to invest up to \$1.5 million in the first stage of this project and its share of development costs is estimated to be as much as \$17 million.

**BAY HEART LIMITED ( BAY HEART )**

Bay Heart was established in 1987 to develop and lease a shopping mall (the Mall ) in the Haifa Bay area. Haifa is the third largest city in Israel. The Mall, which opened in May 1991, is a three-story facility with approximately 280,000 square feet of rentable space. The Mall is located at the intersection of two major roads and provides a large mix of retail and entertainment facilities including seven movie theaters. The total cost of the Mall was approximately \$53 million, which was financed principally with debt instruments. A train station on the west side of the Mall was completed in September 2001. A transportation complex, in conjunction with a subsidiary of Egged Bus Corporation, was opened in January 2002. The Company owns 37% of Bay Heart. Bay Heart has refinanced the loan relating to the Mall, which loan has a fifteen years term. Bay Heart received an additional approval for NIS. 18.5 million for renovating the Mall which started in 2005. The Company has agreed to guarantee a portion of the new loan in an amount equal to NIS 6.8 million.

**Leisure-Time**

**CORAL WORLD INTERNATIONAL LIMITED ( CORAL WORLD )**

Coral World, which is 50%-owned by the Company, owns and controls three marine parks in Eilat (Israel), Perth (Australia) and Maui (Hawaii).

Coral World's Eilat marine park is located next to the coral reefs and visitors to this park view marine life in its natural coral habitat through a unique underwater observatory. Coral World's marine parks in Perth and Maui allow visitors to walk through a transparent acrylic tube on the bottom of a man-made aquarium surrounded by marine life. In addition to admission charges, Coral World derives significant revenue from its food and beverage facilities and retail outlets.

Coral World's parks hosted 1,034,283 visitors during 2005. Coral World has approximately 220 full-time equivalent positions as of December 31, 2005.

Coral World has entered into a joint development project for a new marine park in Palma de Majorca which is scheduled to open at the end of 2006.

**COUNTRY CLUB KFAR SABA LIMITED ( KFAR SABA )**

Kfar Saba operates a country club facility (the Club) in Kfar Saba, a town north of Tel Aviv. Kfar Saba holds a long-term lease to the real estate property on which the Club is situated. The Club's facilities include swimming pools, tennis courts and a clubhouse. The Club currently is seeking to obtain building permits for an additional 30,000 square feet of commercial development on the Club grounds.

The Club, which has a capacity of 2,000 member families, had approximately 1,735 member families for the 2005 season. The Company owns 51% of Kfar Saba.

**HOD HASHARON SPORT CENTER (1992) LIMITED PARTNERSHIP ( HOD HASHARON )**

Hod Hasharon operates a country club facility (the H.H. Club) in Hod Hasharon, a town north of Tel Aviv. The H.H. Club, which opened in July 1994 and has a capacity of 1,600 member families, has operated at capacity for the past three years. In 2005, the H.H. Club repaid owner's loans of \$0.2 million to each of the partners. As of December 31, 2005, the Company holds a 50% direct interest in Hod Hasharon.

**Capital Markets And Other Holdings**

**AMPAL DEVELOPMENT (ISRAEL) LTD. ( AMPAL DEVELOPMENT )**

Ampal Development, a wholly owned subsidiary of the Company, issued debentures which were publicly traded on the TASE. An aggregate of approximately \$2.0 million of these debentures were outstanding as of December 31, 2004. On March 1, 2005, Ampal Development paid off all of its outstanding and remaining debentures which were publicly traded on the TASE.

**CARMEL CONTAINERS SYSTEMS LIMITED ( CARMEL )**

Carmel is one of the leading Israeli companies in designing, manufacturing and marketing carton boards and packaging products. Carmel and its subsidiaries manufacture a varied line of products, including corrugated shipping containers, moisture-resistant packaging, consumer packaging, triple-wall packaging and wooden pallets and boxes. The Company's equity interest in Carmel is 21.75%. As of December 31, 2005, the Company accounts for this investment pursuant to the equity method as \$2.4 million (which includes impairment in an amount of \$3.0 million).

**EMPLOYEES**

On March 31, 2004, the Company closed its New York office located at 555 Madison Ave, New York, New York. Other than the executive officers listed in Item 11 below, Ampal has no other employees. As of December 31, 2005, Ampal (Israel) Ltd. had 13 employees, Am-Hal Ltd. (a wholly owned subsidiary of Ampal) had 170 employees and Country Club Kfar Saba Ltd. (owned 51% by the Company) had 103 employees.

Relations between the Company and its employees are satisfactory.

**CONDITIONS IN ISRAEL**

Most of the companies in which Ampal directly or indirectly invests conduct their principal operations in Israel and are directly affected by the economic, political, military, social and demographic conditions there. A state of hostility, varying as to degree and intensity, exists between Israel and the Arab countries and the Palestinian Authority (the PA). Israel signed a peace agreement with Egypt in 1979 and with Jordan in 1994. Since 1993, several agreements have been signed between Israel and Palestinian representatives regarding conditions in the West Bank and Gaza. While negotiations have taken place between Israel, its Arab neighbors and the PA to end the state of hostility in the region, it is not possible to predict the outcome of these negotiations and their eventual effect on Ampal and its investee companies. Political developments in Israel, notably the ability of the Hamas movement to win a majority of seats in the Palestinian parliament has increased the economic, political and military uncertainty in Israel and the Middle East. See Item 1A Risk Factors below for further discussion of the possible impact of this situation on the Company.



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All male adult citizens and permanent residents of Israel under the age of 48 are obligated, unless exempt, to perform military reserve duty annually. Additionally, all these individuals are subject to being called to active duty at any time under emergency circumstances. Some of the officers and employees of Ampal's investee companies are currently obligated to perform annual reserve duty. While these companies have operated effectively under these requirements since they began operations, Ampal cannot assess the full impact of these requirements on their workforce or business if conditions should change. In addition, Ampal cannot predict the effect on its business in a state of emergency in which large numbers of individuals are called up for active duty.

### **Economic and Financial Developments**

In 2005, unemployment in Israel averaged 9.0%. The rate of unemployment in 2004 averaged 10.4% as compared to 10.7% in 2003. Management believes that the decrease resulted mainly from the improvement in the industrial and high tech sectors and the Israeli government's employment initiatives.

2005 was characterized by rapid growth in all components of Israeli GDP. The GDP grew by 5.2% and the business-sector product grew by 6.7%. In 2004 and 2003, GDP growth was 4.4% and 1.7%, respectively.

The change in consumer price index in 2005 was 2.4% compared to 1.2% in 2004.

### **CERTAIN UNITED STATES AND ISRAELI REGULATORY MATTERS**

#### **SEC Exemptive Order**

In 1947, the SEC granted Ampal an exemption from the Investment Company Act of 1940, as amended (the 1940 Act), pursuant to an Exemptive Order. The Exemptive Order was granted based upon the nature of Ampal's operations, the purposes for which it was organized, which have not changed, and the interest of purchasers of Ampal's securities in the economic development of Israel. There can be no assurance that the SEC will not reexamine the Exemptive Order and revoke, suspend or modify it. A revocation, suspension or material modification of the Exemptive Order could materially and adversely affect the Company unless Ampal were able to obtain other appropriate exemptive relief. In the event that Ampal becomes subject to the provisions of the 1940 Act, it could be required, among other matters, to make changes, which might be material, to its management, capital structure and methods of operation, including its dealings with principal shareholders and their related companies.

### **TAX INFORMATION**

Ampal (to the extent that it has income derived in Israel) and Ampal's Israeli subsidiaries are subject to taxes imposed under the Israeli Income Tax Ordinance. Through December 31, 2003, the corporate tax rate was 36%. In July 2004, Amendment No. 140 to the Income Tax Ordinance was enacted. One of the provisions of this amendment is that the corporate tax rate is to be gradually reduced from 36% to 30%. In August 2005, a further amendment (No. 147) was published, which makes a further revision to the corporate tax rates prescribed by Amendment No. 140. As a result of the aforementioned amendments, the corporate tax rates for 2004 and thereafter are as follows: 2004 35%, 2005 34%, 2006 31%, 2007 29%, 2008 27%, 2009 26% and for 2010 and thereafter 25%.

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A tax treaty between Israel and the United States became effective on January 1, 1995 ( the Treaty ). The Treaty has not substantially affected the tax position of the Company in either the United States or in Israel.

Ampal generated income from interest and dividends resulting from its investments in Israel. Under Israeli law, Ampal has been required to file tax returns, with the Israeli tax authorities with respect to such income. Under Israeli domestic law Ampal, as a non-resident, is generally subject to withholding tax at a rate of 25% on dividends it receives from Israeli companies (20% as of January 1, 2006). This rate may be reduced to either 15% or 12.5%, (under Israeli law and/or the provisions of the Treaty), depending on the ownership percentage in the investee company, and on the type of income generated by such investee company, from which the dividend is distributed (by contrast, dividends received by one Israeli company from another Israeli company are generally exempt from Israeli corporate tax, unless (i) they arise from income generated from sources outside of Israel, in which case they are subject to tax at a rate of 25%; or (ii) they are paid out of the profits of an approved enterprise to either residents or non-residents, in which case tax is withheld at a rate of 15%).

Pursuant to an arrangement with the Israeli tax authorities, Ampal's income from Israeli sources has been taxed based on principles generally applied in Israel to income of non-residents. Ampal has filed tax returns with the Israeli tax authorities through the tax year 2004. Based on the tax returns filed by Ampal through 2004, it has not been required to make any additional tax payments in excess of the tax withheld on dividends it has received. In addition, pursuant to Ampal's arrangement with the Israeli tax authorities, the aggregate taxes paid by Ampal in Israel and in the United States on interest, rent and dividend income derived from Israeli sources has not exceeded the tax which would have been payable by Ampal in the United States had such interest, rent and dividend income been derived by Ampal from United States sources. There can be no assurance that this arrangement will continue to be effective in the future. This arrangement does not apply to taxation of Ampal's Israeli subsidiaries.

Generally, under the provisions of the Israeli Income Tax Ordinance, taxable income from Israeli sources paid to non-residents of Israel by residents of Israel is subject to withholding tax at the rate of 25%. However, such rate of withholding tax may be reduced under the Treaty, with respect to certain payments made by Israeli tax residents to US tax residents that qualify for benefits of the Treaty. For example, under the Treaty, the rate of withholding tax applicable to interest is generally reduced to 17.5%. The continued tax treatment of Ampal by the Israeli tax authorities in the manner described above is based, among other things, on Ampal continuing to be treated, for tax purposes, as a non-resident of Israel that is not doing business in Israel. As of January 1, 2006, a different withholding rate may apply.

Under Israeli law, Israeli tax residents are taxed on capital gains generated from sources in Israel or outside of Israel, whereas non residents are taxable only with respect to gains generated from sources in Israel. Gains are generally regarded as being from Israeli sources if arising from the sale of assets either located in Israel or which represent a right to assets located in Israel (including gains arising from the sale of shares of stock in companies resident in Israel, and of rights in non-resident entities that mainly represent ownership and rights to assets located in Israel, with regard to such assets). Under the Treaty, US tax residents are subject to Israeli capital gains tax on the sale of shares in Israeli companies, if they have held 10% or more of the voting rights in such company at any time during the 12 months immediately preceding the sale.

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Since January 1, 1994, the portion of the gain attributable to inflationary differences prior to that date is taxable at a rate of 10%, while the portion of the gain attributable to inflationary differences between such date and the date of disposition of the asset is exempt from tax. Non-residents of Israel are exempt from the 10% tax on the inflationary gain derived from the sale of shares in companies that are considered Israeli tax residents if they elect to compute the inflationary portion of the gain based on the change in the rate of exchange between Israeli currency and the foreign currency in which the shares were purchased, rather than the change in the Israeli consumer price index<sup>(1)</sup>. The remainder of the gain ( Real Capital Gain ), if any, is taxable to corporations at the rate of 25%. However, Real Capital Gains arising from the sale of capital assets that had been acquired prior to January 1, 2003 shall be apportioned on a linear basis to the periods before and after the same date, namely the portion of the gain attributed to the period before January 1, 2003 shall be subject to tax at a rate equal to the corporate tax rate in effect at the time of the sale (in 2005 34%), whereas the portion of the gain attributed to the period after January 1, 2003 shall be taxed at the preferential rate of 25%. This 25% preferential tax rate may also apply to a certain portion of the profit upon the sale of Israeli shares.

Foreign corporations are generally exempt from tax on gains from the sale of shares in publicly traded companies. Amendment No. 147 introduces a broader exemption under domestic law for non-residents regardless of their percentage holding in an Israeli company (not holding real estate rights) to include capital gains from the sale of securities (even where not traded in Israel), which were purchased between July 1, 2005 through December 31, 2006, provided certain conditions are met.

The Income Tax Law (Adjustment for Inflation), 1985, which applies to companies which have business income in Israel or which claim a deduction in Israel for financing costs, has been in force since the 1985 tax year. The law provides for the preservation of equity, whereby certain corporate assets are classified broadly into Fixed (inflation resistant) and Non-Fixed (non-inflation resistant) Assets. Where shareholders equity, as defined therein, exceeds the depreciated cost of Fixed Assets, a tax deduction which takes into account the effect of the annual inflationary change on such excess is allowed, subject to certain limitations. Conversely, if the depreciated cost of Fixed Assets exceeds shareholders equity, then such excess, multiplied by the annual inflation change, is added to taxable income.

Individuals and companies in Israel pay VAT at a rate of 16.5% (17% until August 2005) of the price of assets sold and services rendered. However, according to a Temporary Order issued by the state of Israel the VAT rate was increased from 17% to 18% for the period commencing on June 15, 2002 and ending on December 31, 2003. This period was extended by an additional two months and was terminated on February 29, 2004, when the VAT rate was reduced back to 17%. In computing its VAT liability, Ampal's Israeli subsidiaries are entitled to claim as a deduction input VAT it has incurred with respect to goods and services acquired for the purpose of the business.

### United States Federal Taxation of Ampal

Ampal and its United States subsidiaries (in the following discussion, generally referred to collectively as Ampal U.S.) are subject to United States taxation on their taxable income, as computed on a consolidated basis, from domestic as well as foreign sources. The gross income of Ampal U.S. for United States tax purposes includes or may include (i) income earned directly by Ampal U.S., (ii) Ampal U.S.'s pro rata share of certain types of income, primarily subpart F income earned by certain Controlled Foreign Corporations in which Ampal U.S. owns or is considered as owning 10 percent or more of the voting power; and (iii) Ampal U.S.'s pro rata share of ordinary income and capital gains earned by certain Passive Foreign Investment Companies in which Ampal U.S. owns stock, and with respect to which Ampal has elected that such company be treated as a Qualified Electing Fund. Subpart F income includes, among other things, dividends, interest and certain rents and capital gains. Since 1993, the maximum rate applicable to domestic corporations is 35%.

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<sup>(1)</sup> Beginning January 1, 2006, the section of the Israeli Tax Ordinance under which the regulations providing such tax exemption to non-Israeli residents were promulgated, was rescinded. It is therefore unclear whether this exemption shall continue to be applicable

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Certain of Ampal's non-U.S. subsidiaries have elected to be treated as partnerships for U.S. tax purposes. As a result, Ampal is generally subject to US tax on its distributive share of income earned by such subsidiaries (generally computed with reference to Ampal's proportionate interest in such entity), as it is earned, i.e. without regard to whether or not such income is distributed by the subsidiary. Certain of Ampal's wholly-owned non-U.S. subsidiaries have elected to be treated as disregarded entities for U.S. federal tax consequences. As a result, Ampal is subject to US tax on all income earned by such subsidiaries, as it is earned.

Ampal U.S. is generally entitled to claim as a credit against its United States income tax liability all or a portion of income taxes, or of taxes imposed in lieu of income taxes, paid to foreign countries. If Ampal U.S. receives dividends from a non-US corporation in which it owns 10% or more of the voting stock, Ampal U.S. is treated (in determining the amount of foreign income taxes paid by Ampal U.S. for purposes of the foreign tax credit) as having paid the same proportion of the foreign corporation's post-1986 foreign income taxes as the amount of such dividends bears to the foreign corporation's post-1986 undistributed earnings.

In general, the total foreign tax credit that Ampal U.S. may claim is limited to the same proportion of Ampal U.S.'s United States income taxes that its foreign source taxable income bears to its taxable income from all sources, US and non-US. This limitation is applied separately with respect to various items of income ( baskets ), which may further limit Ampal's ability to claim foreign taxes as a credit against its U.S. tax liability. The use of foreign taxes as an offset against United States tax liability is further limited by certain rules pertaining to the sourcing of income and the allocation of deductions. As a result of the combined operation of these rules, it is possible that Ampal U.S. would exercise its right to elect to deduct the foreign taxes, in lieu of claiming such taxes as a foreign tax credit.

Ampal U.S. may also be subject to the alternative minimum tax ( AMT ) on corporations. Generally, the tax base for the AMT on corporations is the taxpayer's taxable income increased or decreased by certain adjustments and tax preferences for the year. The resulting amount, called alternative minimum taxable income, is then reduced by an exemption amount and subject to tax at a 20% rate. As with the regular tax computation, AMT can be offset by foreign tax credits as well as net operating losses ( NOLs ) both of which are separately calculated under AMT rules and both of which are generally limited to 90% of AMT liability as specially computed for this purpose. The 90% limitation of the foreign tax credit allowed against AMT was repealed in the Jobs Creation Act of 2004, effective for tax years beginning after December 31, 2004.

### FORWARD-LOOKING STATEMENTS

This Report (including but not limited to factors discussed in the Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as those discussed elsewhere in this Report on Form 10-K) 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 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 in the global business and economic conditions in the different sectors and markets where the Company's portfolio companies operate. These risks and uncertainties include, but are not limited to, those described in Part I, Item 1A. Risk Factors and elsewhere in this report and those described from time to time in our future reports filed with the Securities and Exchange Commission.

Should any of those risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results or outcome may vary from those described therein 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 Report and other Reports filed with the Securities and Exchange Commission.

#### **ITEM 1A. RISK FACTORS**

An investment in our securities involves risks and uncertainties. These risks and uncertainties could cause our actual results to differ materially from our historical results or the results contemplated by any forward-looking statements contained in this report on Form 10-K or that we make in other filings with the SEC under the Securities and Exchange Act of 1934 or in other public statements. The risks described below are not the only risks facing the Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results. You should consider the following factors carefully, in addition to the other information contained in this Form 10-K, before deciding to purchase, sell or hold our securities:

***Because most of the companies in which we invest conduct their principal operations in Israel, we may be adversely affected by the economic, political, social and military conditions in the Middle East.***

Most of the companies in which we directly or indirectly invest conduct their principal operations in Israel. We may, therefore, be directly affected by economic, political, social and military conditions in the Middle East, including Israel's relationship with the Palestinian Authority and Arab countries. In addition, many of the companies in which we invest are dependent upon materials imported from outside of Israel, including East Mediterranean Gas Company, an Egyptian joint stock company in which we own a 2% stake. We also have interests in companies that export significant amounts of products from Israel. Accordingly, our operations could be materially and adversely affected by acts of terrorism or if major hostilities should occur in the Middle East or trade between Israel and its present trading partners should be curtailed, including as a result of acts of terrorism in the United States. Any such effects may impact our value and the value of our investee companies.

***The SEC may re-examine, suspend or modify our exemption from the Investment Company Act of 1940, as amended.***

In 1947, the SEC granted us an exemption from the Investment Company Act of 1940, as amended (the "1940 Act"), pursuant to an exemptive order. The exemptive order was granted based upon the nature of our operations, the purposes for which we were organized, which have not changed, and the interest of purchasers of our securities in the economic development of Israel. There can be no assurance that the SEC will not re-examine the exemptive order and revoke, suspend or modify it. A revocation, suspension or material modification of the exemptive order could materially and adversely affect us unless we were able to obtain other appropriate exemptive relief. In the event that we become subject to the provisions of the 1940 Act, we could be required, among other matters, to make changes, which might be material, to our management, capital structure and methods of operation, including our dealings with principal shareholders and their related companies.

*As most of our investee companies conduct business outside of the United States, we are exposed to foreign currency and other risks.*

We are subject to the risks of doing business abroad, including, among other risks, foreign currency exchange rate risks, changes in interest rates, equity price changes of our investee companies, import restrictions, anti-dumping investigations, political or labor disturbances, expropriation and acts of war. No assurances can be given that we will be protected from future changes in foreign currency exchange rates that may impact our financial condition or performance.

Foreign securities or illiquid securities in our portfolio involve higher risk and may subject us to higher price volatility. Investing in securities of foreign issuers involves risks not associated with U.S. investments, including settlement risks, currency fluctuations, local withholding and other taxes, different financial reporting practices and regulatory standards, high costs of trading, changes in political conditions, expropriation, investment and repatriation restrictions, and settlement and custody risks.

*Changes in accounting standards and taxation requirements could affect our financial results.*

New accounting standards or pronouncements that may become applicable to the Company from time to time, or changes in the interpretation of existing standards and pronouncements, could have a significant effect on our reported results for the affected periods. We are also subject to income tax in the numerous jurisdictions in which we generate revenues. Increases in income tax rates could reduce our after-tax income from affected jurisdictions.

*The loss of key executives could cause our business to suffer.*

Yosef A. Maiman, our Chairman, and other key executives have been key to the success of our business to date. The loss or retirement of such key executives services could adversely affect us.

*Y.M. Noy Investments Ltd. s control of us could discourage attempts to acquire us.*

Y.M. Noy Investments Ltd., an Israeli company held approximately 58.29% of the voting power of our Class A Stock as of March 6, 2006. Yosef A. Maiman, the Chairman of our board of directors, owns 100% of the economic shares and one-third of the voting shares of Y.M. Noy Investments Ltd. In addition, Mr. Maiman holds an option to acquire the remaining two-thirds of the voting shares of Y.M. Noy Investments Ltd. (which are currently owned by Ohad Maiman and Noa Maiman, the son and daughter, respectively, of Mr. Maiman). By virtue of its ownership of Ampal, Y.M. Noy Investments Ltd. is able to control our affairs and to influence the election of the members of our board of directors. Y.M. Noy Investments Ltd. also has the ability to prevent or cause a change in control of Ampal.

*Because we are a controlled company, we are exempt from complying with certain Nasdaq listing standards.*

Because Y.M. Noy Investments Ltd. own more than 50% of our voting power, we are deemed to be a controlled company under the rules of the Nasdaq National Market. As a result, we are exempt from the Nasdaq rules that require listed companies to have (i) a majority of independent directors on the board of directors, (ii) a compensation committee and nominating committee composed solely of independent directors, (iii) the compensation of executive officers determined by a majority of the independent directors or a compensation committee composed solely of independent directors and (iv) a majority of the independent directors or a nominating committee composed solely of independent directors elect or recommend director nominees for selection by the board of directors. Accordingly, our directors who hold management positions or who are otherwise not independent have greater influence over our business and affairs.

***Our activities could be restricted as a result of agreements between our controlling shareholder and its lender.***

Based upon statements of beneficial ownership filed with the SEC by Y.M. Noy Investments Ltd., Yosef A. Maiman, Ohad Maiman and Noa Maiman, the repayment of the borrowed funds used to finance Y.M. Noy Investment's Ltd.'s acquisition of a controlling interest in us, consisting of 11,444,112 shares of our Class A Stock, was principally financed by Bank Leumi Le-Israel B.M. According to the statements of beneficial ownership, the repayment of the borrowings are guaranteed by a personal guarantee by Mr. Maiman and secured by Y.M. Noy Investment Ltd.'s pledge of such shares of our Class A Stock to the bank.

The statements of beneficial ownership report that the pledge agreement with the bank includes restrictions on Y.M. Noy Investments Ltd.'s voting rights and grants the bank certain voting rights with respect to the pledged shares, and that its credit agreement with the bank requires Y.M. Noy Investments Ltd. to maintain a controlling interest in us for so long as any amounts remain outstanding pursuant to the credit facilities. The statements of beneficial ownership also report that Y.M. Noy Investments Ltd. agreed that it will cause us to not issue any shares of our Class A Stock or options to acquire shares of our Class A Stock, except for employee stock options to our employees, consultants and directors and provided that Y.M. Noy Investments Ltd. owns at least 50.1% of Ampal. In addition, the statements of beneficial ownership reported that Y.M. Noy Investments Ltd. has agreed, unless it has received the prior consent of the bank and until the borrowings have been repaid in full, to cause us to refrain from making any decisions with regard to our winding-up, change in corporate structure, reorganization or merger. The statements of beneficial ownership also reported that Y.M. Noy Investments Ltd. has agreed, unless it has received the prior consent of the bank, not to sign any voting or other agreement regarding the shares and to oppose any change in our certificate of incorporation and by-laws and any resolution or other act which will or might result in the dilution of Y.M. Noy Investments Ltd.'s interest in Ampal.

***We do not typically pay cash dividends on our Class A Stock.***

We have not paid a dividend on our Class A Stock other than in 1995. Past decisions not to pay cash dividends on Class A Stock reflected our policy to apply retained earnings, including funds realized from the disposition of holdings, to finance our business activities and to redeem debentures. The payment of cash dividends in the future will depend upon our operating results, cash flow, working capital requirements and other factors we deem pertinent.

***The market price per share of our Class A Stock on Nasdaq fluctuates and has traded in the past at less than our book value per share.***

Stock prices of companies, both domestically and abroad, are subject to fluctuations in trading price. Therefore, as with company like ours that invests in stocks of other companies, our book value and market price will fluctuate, especially in the short term. As of December 31, 2005, the market price on Nasdaq of \$3.95 per share of our Class A Stock is less than our book value of \$4.43 per share calculated in accordance with our consolidated financial statements. You may experience a decline in the value of your investment and you could lose money if you sell your shares at a price lower than you paid for them.

***We do not publish the value of our assets.***

It is our policy not to publish the value of our assets or our views on the conditions of or prospects for our investee companies. To the extent the value of our ownership interests in our investee companies were to experience declines in the future, our performance would be adversely impacted.

***Our Class A Stock may not be liquid.***

Our Class A Stock is currently traded on Nasdaq. The trading volume of our Class A Stock may be adversely affected due to the limited marketability of our Class A Stock as compared to other companies listed on Nasdaq. Accordingly, any substantial sales of our Class A Stock may result in a material reduction in price of our Class A Stock because relatively few buyers may be available to purchase our Class A Stock.

**ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2. PROPERTY**

Ampal's corporate headquarters in Israel, which is owned by the Company, is located at 111 Arlozorov Street in Tel Aviv.

Ampal currently leases an office at 555 Madison Avenue in New York City from Rodney Company N.V., Inc. The lease period is seven years commencing on October 15, 2002. The annual rent for this lease is \$119,794. On March 31, 2004, the Company closed this office. The office space has been subleased.

Country Club Kfar Saba Ltd. occupies a 7-1/4 acre lot in the town of Kfar Saba which will be leased for five consecutive ten-year periods, at the end of which the land returns to the lessor. The lease expires on July 14, 2038, and lease payments in 2005 totaled \$179,619.

Other properties of the Company are discussed elsewhere in this Report. See Item 1. Business.

**ITEM 3. 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., MIRS Communications Ltd. (MIRS), Motorola Israel Ltd., Elisha Yanai, Peter Brum, Rami Guzman, Nathan Gidron, and Shimon Tal (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.

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

A. Declaring that the business of MIRS 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 and Ampal Communications L.P.'s holdings therein, which will encompass a review of the way MIRS conducts its business, including a review of the related party transactions between MIRS 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 at the highest of the following prices:

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

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



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(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, 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, has violated his respective fiduciary obligations towards Ampal Communications L.P. as a minority shareholder in MIRS; and

E. Declaring that the Share Purchase Agreement pursuant to which Ampal Communications L.P. acquired its shareholding in MIRS 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