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KOOR INDUSTRIES LTD
Form 20-F/A
September 16, 2005

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 20-F/A
(Amendment No. 1)

Annual Report pursuant to Section 13 or 15(d) of
the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2004

Commission file number 1-9178

KOOR INDUSTRIES LTD.

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

Israel

(Jurisdiction of incorporation or organization)

14 Hamelacha Street, Rosh Ha'ayin 48091, Israel

(Address of principal executive offices)

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

| Title of Each Class | Name of Each Exchange On Which Registered |
|---|--|
| American Depositary Shares, Each Representing 0.20 Ordinary Shares, Par Value NIS 0.001 Per Share | New York Stock Exchange |

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

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d)
of the Act:

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of
capital or common stock as of the close of the period covered by the annual
report:

16,033,213 Ordinary Shares, Par Value NIS 0.001 Per Share

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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
 --- ---

Indicate by check mark which financial statements the registrant has elected to follow:

Item 17 X Item 18
 --- ---

=====

EXPLANATORY NOTE

Koor Industries Ltd. ("Koor") filed its Annual Report on Form 20-F for the fiscal year ended December 31, 2004 (the "Form 20-F") with the Securities and Exchange Commission ("SEC") on July 15, 2005.

This Amendment No. 1 to Koor's Form 20-F is filed in response to comments Koor received from the staff of the SEC to: (i) amend its disclosure under Item 15 (Controls and Procedures) to clarify that Koor's disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that it filed or submits under the Securities Exchange Act of 1934, as amended (the "Exchange Act") is accumulated and communicated to Koor's management, including its principal executive and principal financial officers, to allow timely decisions regarding required disclosure; (ii) amend its disclosure under Item 17 (Financial Statements) to provide clarifications of several differences between generally accepted accounting principles in Israel ("Israeli GAAP") and generally accepted accounting principles in the United States ("US GAAP") in its US GAAP reconciliation footnote, including providing a quantified description of the material differences between cash flows reported in Koor's primary financial statements under Israeli GAAP and cash flows that would be reported in accordance with US GAAP; (iii) amend the financial statements of Makhteshim-Agan Industries Ltd. ("M-A Industries"), which are included in Koor's Form 20-F pursuant to Rule 3-09 of Regulation S-X promulgated under the Exchange Act, to provide a quantified description of the material differences between cash flows reported in M-A Industries' primary financial statements under Israeli GAAP and cash flows that would be reported in accordance with US GAAP; and (iv) revise its auditors' report and the auditors' reports of several of its subsidiaries and affiliates to include the city and state where those auditors' reports were issued and, with respect to the auditors' report for M-A Industries, to clarify that the auditors conducted their audit in accordance with the standards of the Public Company Accounting Oversight Board (United States).

Pursuant to Rule 12b-15 under the Exchange Act, amendments to Form 20-F must set forth the complete text of each item as amended. Accordingly, Koor is amending and restating Items 15 and 17 of its Form 20-F in their entirety and is amending and restating M-A Industries' financial statements in their entirety. However, other than as described above, no part of Koor's Form 20-F filed on July 15, 2005, including its primary financial statements prepared in accordance with Israeli GAAP, is being amended, and no part of the Form 20-F or of the amended Items 15 and 17 as re-filed pursuant to this amendment speaks as of any date subsequent to July 15, 2005.

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Item 15. Controls and Procedures

Koor hereby amends Item 15 of its Form 20-F in its entirety and replaces it with the following:

Disclosure Controls and Procedures. Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act as of December 31, 2004. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective in alerting them on a timely basis to material information relating to us (including our consolidated subsidiaries) required to be included in our reports filed or submitted under the Exchange Act, and that our disclosure controls and procedures are effective to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Internal Control Over Financial Reporting. There were no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) or 15d-15(f) under the Exchange Act) that occurred during the year ended December 31, 2004 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 17. Financial Statements

Koor hereby amends Item 17 of its Form 20-F in its entirety and replaces it with the following:

See pages F-1 through F-144, incorporated herein by reference.

Financial Statements of Makhteshim-Agan Industries Ltd.

Koor hereby amends the financial statements of M-A Industries in their entirety and replaces them with the following:

See pages F-145 through F-232, incorporated herein by reference.

Item 19. Exhibits.

Index to exhibits filed with this Amendment No. 1 to Koor's Form 20-F.

| Exhibit No. ----- | Description ----- |
|----------------------|---|
| 12.1 | Certification of the Principal Executive Officer of Koor Industries Ltd. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 12.2 | Certification of the Principal Financial Officer of Koor Industries Ltd. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 13.1 | Certification of the Principal Executive and Financial |

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Officers of Koor Industries Ltd. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

- 14.1 Consent of KPMG Somekh Chaikin to the incorporation by reference into the effective registration statement on Form S-8 of Koor Industries Ltd. under the Securities Act of 1933 of their report with respect to the consolidated financial statements of Koor Industries Ltd., which appears in this Annual Report on Form 20-F.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F/A and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

KOOR INDUSTRIES LTD.

By: /s/ Jonathan B. Kolber

Jonathan B. Kolber
Chief Executive Officer

Date: September 16, 2005

Koor Industries Ltd. (an Israeli Corporation)

Financial Statements as at December 31, 2004

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[Letterhead of Somekh Chaikin, a Member Firm of KPMG International]

Report of Independent Registered Public Accounting Firm

The Shareholders
Koor Industries Ltd.

We have audited the accompanying balance sheets of Koor Industries Ltd. (hereinafter - the "Company" or Koor) and the consolidated balance sheets of the Company and its subsidiaries as at December 31, 2004 and 2003, and the related statements of operations, shareholders' equity and cash flows, for each of the three years, the last of which ended December 31, 2004. These financial statements are the responsibility of the Company's Board of Directors and of its Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of certain subsidiaries, including those consolidated by the proportionate consolidation method, whose assets constitute 12% and 20% of the total consolidated assets as at December 31, 2004 and 2003 respectively, and whose revenues constitute 14%, 19% and 20% of the total consolidated revenues for the years ended December 31, 2004, 2003 and 2002, respectively. Furthermore, we did not audit the financial statement of certain affiliates, whose company's investments constitute NIS 204,878 thousand and NIS 218,081 thousand, as at December 31, 2004 and 2003, respectively, and its equity in earnings constitute NIS 5,647 thousand for the year ended December 31, 2004 and its equity in losses, NIS 12,875 thousand and NIS 6,748 thousand for the years ended December 31, 2003 and 2002, respectively. The financial statements of those subsidiaries and affiliates were audited by other auditors whose reports thereon were furnished to us. Our opinion, insofar as it relates to amounts included for such subsidiaries and affiliates, is based solely on the said reports of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Board of Directors and Management, as well as evaluating the overall financial statement presentation. We believe that our audits, and reports of the other auditors, provide a reasonable basis for our opinion.

In our opinion, based on our audits and on the reports of the above-mentioned other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Company and the consolidated financial position of the Company and its subsidiaries as of December 31, 2004 and 2003 and the results of their operations, the changes in shareholders' equity and their cash flows for each of the three years, the last

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of which ended December 31, 2004, in conformity with accounting principles generally accepted in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America (US GAAP). Information related to the nature and effect of such differences is presented in Note 28 of the financial statements. As further described in Note 28 to the financial statements, the reconciliation of differences between Israeli GAAP and US GAAP as of and for the years ended December 31, 2003 and 2002 has been restated.

As explained in Note 2(B), the financial statements for dates and reporting periods subsequent to December 31, 2003 are stated in reported amounts, in accordance with the accounting standards of the Israel Accounting Standards Board. The financial statements for dates and reporting periods that ended up to the aforementioned date are stated in values that were adjusted to that date according to the changes in the general purchasing power of the Israeli currency, in accordance with opinions of the Institute of Certified Public Accountants in Israel.

/s/ Somekh Chaikin

Somekh Chaikin
Certified Public Accountants (Isr.)

March 29, 2005, except for Note 28, as to which the date is July 13, 2005.
Tel-Aviv, Israel

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Consolidated Balance Sheets as at December 31

| | | December 31 2004 | | |
|---|------|----------------------|--|--------------------|
| | | Reported amounts* | | Ad terms Dec |
| | | 2004 | | |
| | Note | NIS thousand | | |
| <hr style="border-top: 1px dashed black;"/> | | | | |
| Assets | | | | |
| Current assets | | | | |
| Cash and cash equivalents | | 617,310 | | |
| Short-term deposits and investments | 4 | 416,468 | | |
| Trade receivables | 5 | 2,173,599 | | 2 |
| Other receivables | 6 | 528,983 | | |
| Inventories and work in progress, net of customer advances | 7 | 2,294,885 | | 1 |

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| | | | |
|--|----|------------|-------|
| Assets designated for sale | | 41,765 | |
| | | ----- | ----- |
| Total current assets | | 6,073,010 | 5 |
| | | ----- | ----- |
| Investments and long-term receivables | | | |
| Investments in affiliates | 8 | 1,375,160 | |
| Other investments and receivables | 9 | 489,031 | |
| | | ----- | ----- |
| | | 1,864,191 | 1 |
| | | ----- | ----- |
| Fixed assets | 10 | 2,852,907 | 2 |
| | | ----- | ----- |
| Intangible assets deferred tax assets and deferred expenses | 11 | 2,357,458 | 2 |
| | | ----- | ----- |
| | | 13,147,566 | 11 |
| | | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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Koor Industries

| | | December 31 2004 | De |
|--------------------------------------|-------|----------------------|--------------------|
| | | ----- | ----- |
| | | Reported amounts* | Ad terms Dec |
| | | ----- | ----- |
| | | 2004 | |
| | | ----- | ----- |
| Note | | NIS thousan | |
| ----- | ----- | ----- | ----- |
| Liabilities and Shareholders' Equity | | | |
| Current liabilities | | | |
| Credit from banks and others | 12 | 1,738,456 | |
| Trade payables | 13 | 1,667,455 | |

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| | | | |
|---|-----|------------|-------|
| Other payables | 14 | 1,369,442 | |
| Customer advances, net of costs incurred on project | 7 | 211,207 | |
| | | ----- | ----- |
| Total current liabilities | | 4,986,560 | |
| | | ----- | ----- |
| Long-term liabilities | | | |
| Net of current maturities: | 15 | | |
| Bank loans | | 2,208,096 | |
| Other loans | | 133,019 | |
| Convertible debentures of consolidated company | | 646,200 | |
| Customer advances | | 142,164 | |
| Deferred taxes | 16G | 240,468 | |
| Liability for employee severance benefits, net | 17 | 197,168 | |
| | | ----- | ----- |
| Total long-term liabilities | | 3,567,115 | |
| | | ----- | ----- |
| Contingent liabilities and commitments | 18 | | |
| Convertible debentures of consolidated company | | 165,091 | |
| | | ----- | ----- |
| Minority Interest | | 2,552,333 | |
| | | ----- | ----- |
| Shareholders' Equity | 20 | 1,876,467 | |
| | | ----- | ----- |
| | | 13,147,566 | 1 |
| | | ===== | ===== |

/s/ Jonathan Kolber

Jonathan Kolber
Chief Executive Officer

/s/ Gabriela Shalev

Prof. Gabriela Shalev
Member of the Board of Directors

/s/ Yuval Yanai

Yuval Yanai
Vice President
Chief Financial

March 29, 2005, except for Note 28, as to which the date is July 13, 2005

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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

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Company Balance Sheets as at December 31

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| | | December 31 2004 | De |
|---|------|----------------------|--------------------|
| | | Reported amounts* | Ad terms Dec |
| | | 2004 | |
| | Note | NIS thousand | |
| Assets | | | |
| Current assets | | | |
| Cash and cash equivalents | | 29,665 | |
| Short-term deposits and investments | 4 | 298,641 | |
| Short-term loans and current maturities of loans to investee companies | | 49,928 | |
| Receivables: | | | |
| Investee companies | | 9,435 | |
| Others | 6 | 84,038 | |
| Assets designated for sale | | 41,765 | |
| | | ----- | ----- |
| Total current assets | | 513,472 | |
| | | ----- | ----- |
| Investments and long-term receivables | | | |
| Investments in investees | 8 | 3,601,557 | 3 |
| Other investments and receivables | 9 | 33,175 | |
| | | ----- | ----- |
| | | 3,634,732 | 3 |
| | | ----- | ----- |
| Fixed assets, net | 10 | 22,484 | |
| | | ----- | ----- |
| | | 4,170,688 | 3 |
| | | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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| | Note | December 31 2004 | December 31 2003 |
|---|------|----------------------|----------------------|
| | | Reported amounts* | Adjusted amounts* |
| | | 2004 | 2003 |
| | | NIS thousand | |
| Liabilities and Shareholders' Equity | | | |
| Current liabilities | | | |
| Credit from banks and others | 12 | 719,730 | 719,730 |
| Trade payables | 13 | 383 | 383 |
| Other payables: | | | |
| Investee companies | | 14,311 | 14,311 |
| Others | 14 | 49,132 | 49,132 |
| Total current liabilities | | 783,556 | 783,556 |
| Long-term liabilities | | | |
| Net of current maturities: | 15 | | |
| Loans from banks and others | | 1,505,690 | 1,505,690 |
| Liability for employee severance benefits, net | 17 | 4,975 | 4,975 |
| Total long-term liabilities | | 1,510,665 | 1,510,665 |
| Contingent liabilities and commitments | 18 | | |
| Shareholders' equity | 20 | 1,876,467 | 1,876,467 |
| | | 4,170,688 | 4,170,688 |

/s/ Jonathan Kolber

Jonathan Kolber
Chief Executive Officer

/s/ Gabriela Shalev

Prof. Gabriela Shalev
Member of the Board of Directors

/s/ Yuval Y

Yuval Y
Vice President
Chief Financial Officer

March 29, 2005, except for Note 28, as to which the date is July 13, 2005

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of December 2004

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

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Koor Industries

Consolidated Statements of Operations

| | Note | Year ended December 31 | | |
|--|------|------------------------|---|---|
| | | 2004 | 2003 | |
| | | Reported amounts* | Adjusted in terms of NIS thousands of December 2003 | |
| | | | | |
| Revenue from sales and services | 23A | 9,228,673 | 7,690,430 | 7 |
| Cost of sales and services | 23B | 6,287,679 | 5,392,944 | 5 |
| Gross profit | | 2,940,994 | 2,297,486 | 1 |
| Selling and marketing expenses | 23C | 1,172,204 | 940,457 | |
| General and administrative expenses | 23D | 526,004 | 460,744 | |
| Operating earnings | | 1,242,786 | 896,285 | |
| Financing expenses, net | 23E | 271,362 | 228,200 | |
| Other income (expenses), net | 23F | 971,424 | 668,085 | |
| Transfer to statement of income of translation differences of autonomous investee in voluntary liquidation | 3B | (78,759) | (219,721) | |
| Earnings (loss) before income tax | | 892,665 | 448,364 | |
| Income tax | 16H | (287,100) | (85,372) | |
| Group's equity in the operating results of affiliates, net | 23G | 605,565 | 362,992 | |
| Minority interest in consolidated company's results, net | | (27,687) | (113,823) | |
| | | 577,878 | 249,169 | |
| | | (432,888) | (202,807) | |

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| | | ----- 144,990 ===== | ----- 46,362 ===== | ----- |
|---|----|---------------------------|--------------------------|-------|
| Net earnings (loss) from continuing activities | | | | |
| | | ----- NIS | ----- NIS | ----- |
| Basic and diluted earnings (loss) per NIS 1 par value of ordinary shares: | 26 | ----- 8.851 ===== | ----- 2.950 ===== | ----- |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of December 2003.
The accompanying notes are an integral part of the financial statements.

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Koor Industries L

Company Statements of Operations

| | Note | Year ended December 31 | |
|---------------------------------------|------|------------------------|---|
| | | 2004 | 2003 |
| | | Reported amounts* | Adjusted in terms of NIS thousands of December 2003 |
| | | ----- | ----- |
| Income | | | |
| Management services from subsidiaries | | 22,334 | 25,006 |
| Other income | 23F | 234,959 | 5,691 |
| Total income | | ----- 257,293 | ----- 30,697 |
| Expenses | | | |
| General and administrative Expenses | 23D | 46,648 | 41,164 |
| Financing, net | 23E | 110,806 | 35,108 |

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| | | | | |
|---|-----|---------------------------|--------------------------|-------|
| Total expenses | | ----- 157,454 ----- | ----- 76,272 ----- | ----- |
| Earnings (loss) before income tax | | 99,839 | (45,575) | |
| Income tax | | 18,951 | 55,667 | |
| Earnings after income tax | | 118,790 | 10,092 | |
| Koor's equity in the operating results of investee companies, net | 23G | ----- 26,200 ----- | ----- 36,270 ----- | ----- |
| Net earnings (loss) for the year | | ===== | ===== | ===== |
| | | ----- NIS ----- | ----- NIS ----- | ----- |
| Basic and diluted earnings (loss) per NIS 1 par value of ordinary shares : | 26 | ===== | ===== | ===== |
| | | 8.851 | 2.950 | |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem
The accompanying notes are an integral part of the financial statements.

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Koor Industri

Statement of Shareholders' Equity

| Number of ordinary shares (1) | Share capital | Capital reserves | Company shares held by the Company and subsidiaries | Cumula for curr transla adjustm |
|-------------------------------------|------------------|---------------------|---|---|
| ----- | | | | |
| Adjusted in terms of NIS of Decem | | | | |
| ----- | | | | |
| NIS thousands | | | | |

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| | | | | | |
|--|-------------------|----------------|------------------|------------------|--------------|
| Balance at December 31, 2001 | 15,168,884 | 564,515 | 2,564,099 | (272,458) | (418) |
| Changes during 2002: | | | | | |
| Net loss | - | - | - | - | - |
| Exercise of stock options granted to Israeli banks | 4,493 | *- | - | - | - |
| Cumulative foreign currency translation adjustments, net | - | - | - | - | 12 |
| Provision for decline in value of autonomous investee (see Note 3A(1)) | - | - | - | - | (105) |
| Transfer to statement of income of translation differences of autonomous investee in voluntary liquidation (see Note 3B) | - | - | - | - | 390 |
| Balance as December 31, 2002 | <u>15,173,377</u> | <u>564,515</u> | <u>2,564,099</u> | <u>(272,458)</u> | <u>(120)</u> |
| Balance at December 31, 2002 | 15,173,377 | 564,515 | 2,564,099 | (272,458) | (120) |
| Changes during 2003: | | | | | |
| Net earnings | - | - | - | - | - |
| Exercise of stock options granted to employees | 67,783 | *- | - | - | - |
| Issuance of "treasury stock" (see Note 20B) | 500,000 | - | - | 192,137 | - |
| Cancellation of provision for decline in value of autonomous investee (see Note 3A(1)) | - | - | - | - | 73 |
| Cumulative foreign currency translation adjustments | - | - | - | - | (149) |
| Balance at December 31, 2003 | <u>15,741,160</u> | <u>564,515</u> | <u>2,564,099</u> | <u>(80,321)</u> | <u>(196)</u> |

* Represents an amount lower than NIS 1,000.

(1) Net of the Company holdings and its subsidiaries' holdings.

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

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Koor Industri

Statement of Shareholders' Equity (cont'd)

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| | Number of ordinary shares (1) | Share capital | Capital reserves | Company shares held by the Company and subsidiaries | Cumula for curr transla adjustm |
|---|-------------------------------------|------------------|---------------------|---|---|
| | Adjusted in terms of NIS | | | of Decem | |
| | NIS thousands | | | | |
| Balance at December 31, 2003 | 15,741,160 | 564,515 | 2,564,099 | (80,321) | (196,7 |
| Changes during 2004: | | | | | |
| Net earnings | - | - | - | - | |
| Exercise of stock options granted to employees | 83,025 | *- | - | - | |
| Cumulative foreign currency translation adjustments, net | - | - | - | - | (8,9 |
| Balance as December 31, 2004 | 15,824,185 | 564,515 | 2,564,099 | (80,321) | (205,6 |

* Represents an amount lower than NIS 1,000.

(1) Net of the Company holdings and its subsidiaries' holdings.

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

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Koor Industrie

Statement of Shareholders' Equity (cont'd)

Convenience translation into US Dollars (Note 2B)

| | Share capital | Capital reserves | Company shares held by the Company and subsidiaries | Cumulati forei curren translati adjustmen |
|---|----------------|---------------------|---|---|
| | US\$ thousands | | | |
| Balance at January 1, 2003 | 131,039 | 595,194 | (18,645) | (45,67 |
| Changes during 2004: | | | | |
| Net earnings | - | - | - | |
| Exercise of stock options granted to employees | *- | - | - | |

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| | | | | |
|---|---------|---------|----------|---------|
| Cumulative foreign currency translation adjustments | - | - | - | (2,07) |
| | ----- | ----- | ----- | ----- |
| Balance at December 31, 2004 | 131,039 | 595,194 | (18,645) | (47,74) |
| | ===== | ===== | ===== | ===== |

* Represents an amount lower than US\$ 1,000

** With respect to discontinuance of adjustment to the effect of inflation as from the CPI of Dec

(1) Net of the Company holdings and its subsidiaries' holdings.

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

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Koor Industrie

Consolidated Statement of Cash Flows

| | Year ended December 31 | |
|---|------------------------|---|
| | 2004 | 2003 |
| | Reported amounts* | Adjusted in terms of NIS thousands December 2003 |
| | NIS thousands | |
| Cash flows generated by operating activities: | | |
| Net earnings (loss) for the year | 144,990 | 46,362 |
| Adjustments to reconcile net earnings to net cash flows generated by operating activities (A) | 745,683 | 728,413 |
| | ----- | ----- |
| Net cash inflow generated by operating activities | 890,673 | 774,775 |
| | ----- | ----- |
| Cash flows generated by investing activities: | | |
| Purchase of fixed assets | (232,146) | (193,424) |
| Investment grants in respect of fixed assets | 6,908 | 8,482 |
| Amounts charged to intangible assets and deferred expenses | (153,206) | (313,125) |
| Additional investments in subsidiaries | - | (600) |
| Acquisition of subsidiaries (B) | (299,305) | (14,372) |
| Investments in affiliates | (646,672) | (6,316) |
| Investments in loans to affiliates | (1,680) | (1,616) |

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| | | |
|--|-----------|----------|
| Repayment of loans from affiliates and others | - | 226,765 |
| Proceeds from realization of investments in formerly consolidated subsidiaries, net of cash in those subsidiaries at the time they ceased being consolidated (c) | - | (14,182) |
| Repayment of liability in respect of subsidiary in prior years | (28,309) | - |
| Proceeds from realization of activity of prior year | - | - |
| Acquisition of minority in subsidiaries | (4,762) | - |
| Proceeds from disposal of investments in investee companies and others | 636,286 | 123,742 |
| Proceeds from sale of fixed assets and intangible assets | 10,519 | 30,998 |
| Investment in venture capital companies | (34,928) | (13,580) |
| Decrease (increase) in other investments, net | (5,110) | 7,465 |
| Decrease (increase) in short-term deposits and investments, net | (8,673) | 426,348 |
| Proceeds from realization of subsidiary's shares that became proportionately consolidated (D) | 38,239 | - |
| | ----- | ----- |
| Net cash inflow (outflow) generated by investing activities | (722,839) | 266,585 |
| | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of December 2003 (see Note 2B).

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

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Koor Industries L

Consolidated Statements of Cash Flows (cont'd)

| | Year ended December 31 | |
|---|------------------------|---|
| | 2004 | 2003 |
| | Reported amounts* | Adjusted in terms of NIS thousands December 2003 |
| | | NIS thousands |
| Cash flows generated by financing activities: | | |
| Issuance of equity | - | 43,011 |
| Issuance of shares to minority interest in subsidiaries | 14,617 | 14,137 |
| Dividend paid to minority interest | | |

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| | | | |
|--|-------------|-------------|-------|
| in subsidiaries | (107,006) | (56,529) | |
| Payment of suppliers credit received for the purchase of fixed assets | - | - | |
| Purchase of convertible debentures of subsidiary by its subsidiary in the market | - | - | |
| Issuance of convertible debentures in subsidiary | 665,982 | - | |
| Proceeds from principal of long-term loans and other long-term liabilities | 1,063,387 | 949,392 | 1 |
| Repayment of long-term loans, debentures and other long-term liabilities | (1,791,112) | (1,891,766) | (1 |
| Increase (decrease) in credit from banks and others, net | 26,063 | (268,028) | |
| | ----- | ----- | |
| Net cash outflow generated by financing activities | (128,069) | (1,209,783) | |
| | ----- | ----- | |
| Translation differences in respect of cash balances of autonomous foreign investee companies | (15,858) | (28,273) | |
| | ----- | ----- | |
| Increase (decrease) in cash and cash equivalents | 23,907 | (196,696) | |
| | ----- | ----- | |
| Balance of cash and cash equivalents at beginning of year | 593,403 | 790,099 | |
| | ----- | ----- | |
| Balance of cash and cash equivalents at end of year | 617,310 | 593,403 | |
| | ===== | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of December 2003 (see Note 2B).

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

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Koor Industries L

Consolidated Statements of Cash Flows (cont'd)

| Year ended December 31 | |
|------------------------|---|
| 2004 | 2003 |
| Reported amounts* | Adjusted in terms of N December 2003 |
| NIS thousands | |
| ----- | ----- |
| ----- | ----- |
| ----- | ----- |
| ----- | ----- |

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A. Adjustments to reconcile net earnings
(loss) to cash flows generated by operating
activities:

Income and expenses not involving cash flows:

| | | | |
|---|-----------|----------|-------|
| Minority interest in subsidiaries, net | 432,888 | 202,807 | |
| Equity in operating results of affiliates, net | 27,687 | 113,823 | |
| Depreciation and amortization | 463,800 | 440,856 | |
| Deferred taxes, net | 49,647 | (45,206) | |
| Increase (decrease) in liabilities in respect of employee severance benefits, net | 20,619 | (49,822) | |
| Net capital losses (gains) from realization: | | | |
| Fixed assets and intangible assets | 16,091 | 22,863 | |
| Investments in formerly consolidated subsidiaries | - | (16,428) | |
| Investments in investee companies | (227,477) | (4,852) | |
| Translation differences of autonomous investee in voluntary liquidation | - | - | |
| Inflationary erosion (linkage) of principal of long-term loans and other liabilities | 8,241 | (77,510) | |
| Inflationary erosion (linkage) of principal of credit from banks and others | - | (10,565) | |
| Inflationary erosion of value of investments, deposits and loans receivable | 9,314 | 32,540 | |
| Impairment in value of assets and investments | 58,144 | 70,503 | |
| | ----- | ----- | ----- |
| | 858,954 | 679,009 | 1 |
| | ===== | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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

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Koor Industries L

Consolidated Statements of Cash Flows (cont'd)

| Year ended December 31 | |
|------------------------|---|
| 2004 | 2003 |
| Reported amounts* | Adjusted in terms of N December 2003 |
| NIS thousands | |
| ----- | ----- |
| ----- | ----- |
| ----- | ----- |

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A. Adjustments to reconcile net earnings to cash flows generated by operating activities (cont'd)

Changes in operating asset and liability items:

| | | | |
|---|-----------|-----------|-------|
| Decrease (increase) in trade receivables and other receivables (after taking into account non-current receivables) | (71,964) | (218,826) | |
| Decrease (increase) in inventories, projects in progress and customer advances (including long-term customer advances and deposits) | (319,645) | (116,927) | |
| Increase (decrease) in trade payables and other payables | 278,338 | 385,157 | |
| | ----- | ----- | |
| | (113,271) | 49,404 | |
| | ----- | ----- | |
| | 745,683 | 728,413 | 1 |
| | ===== | ===== | ===== |

B. Acquisition of subsidiaries

Assets and liabilities of the subsidiaries at date of acquisition:

| | | | |
|--|-----------|----------|-------|
| Working capital deficit (surplus), excluding cash and cash equivalents | (34,493) | (12,160) | |
| Fixed assets and investments, net | (287,724) | (2,404) | |
| Issuance of shares by investee company | 34,238 | - | |
| Long-term liabilities | 187,144 | 192 | |
| Contingent liability | - | - | |
| Goodwill | (198,470) | - | |
| | ----- | ----- | |
| | (299,305) | (14,372) | |
| | ===== | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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

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Koor Industries L

Consolidated Statements of Cash Flows (cont'd)

Year ended December 31

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| | 2004 | 2003 |
|--|----------------------|---|
| | Reported amounts* | Adjusted in terms of N December 2003 |
| | | NIS thousands |
| C. Proceeds from realization of investments in formerly consolidated subsidiaries, net of cash in those subsidiaries at the time they ceased being consolidated: | | |
| Assets and liabilities of the formerly consolidated subsidiaries at the time they ceased being consolidated: | | |
| Working capital deficit, excluding cash and cash equivalents | - | (47,105) |
| Fixed assets and investments | - | 8,765 |
| Intangible assets | - | 15,440 |
| Long-term liabilities | - | (3,463) |
| Investments in affiliated companies, net | - | 12,971 |
| Capital loss on sale of investments in subsidiaries | - | (790) |
| | - | (14,182) |
| D. Proceeds from realization of subsidiary's shares that became proportionately consolidated | | |
| Working capital surplus excluding cash and cash equivalents | 23,057 | - |
| Fixed assets | 40,851 | - |
| Realization proceeds receivable | (25,544) | - |
| Capital gain | (125) | - |
| | ----- | ----- |
| | 38,239 | - |
| | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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Koor Industries L

Consolidated Statements of Cash Flows (cont'd)

Year ended December 31

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| | 2004 | 2003 | |
|---|----------------------|---------------------------------------|--|
| | Reported amounts* | Adjusted in terms of December 2003 | |
| | | NIS thousands | |
| E. Non-cash transactions: | | | |
| Purchase of fixed assets by credit | 9,172 | 24,514 | |
| Purchase of other assets by credit | 28,178 | 6,639 | |
| Proceeds from sale of fixed assets, formerly consolidated subsidiaries and realization of activities | - | 15,145 | |
| Proposed dividend to minority shareholders by subsidiaries | 29,614 | 15,446 | |
| Dividend in kind from affiliate company | 33,363 | - | |
| Loans converted into shareholders' equity of subsidiary | 14,042 | - | |
| Purchase of fixed and other assets and inventory in consideration of issuance subsidiary shares to minority | - | - | |
| Contingent liability from consolidated subsidiary | - | - | |
| Conversion of investment to loan in an affiliates | - | 470 | |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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

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Koor Industries L

Company Statements of Cash Flows (cont'd)

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| | Year ended December 31 | |
|---|------------------------|---|
| | 2004 | 2003 |
| | Reported amounts* | Adjusted in terms of NIS thousands December 2003 |
| | NIS thousands | |
| Cash flows generated by operating activities: | | |
| Net income (loss) for the year | 144,990 | 46,362 |
| Adjustments to reconcile net income to net cash flows generated by operating activities (A) | (136,907) | (163,429) |
| Net cash outflow generated by operating activities | 8,083 | (117,067) |
| Cash flows generated by investing activities: | | |
| Investee companies: | | |
| Acquisition of shares | (667,779) | (17,488) |
| Loans granted\received, capital notes and non-current accounts | 34,950 | 304,725 |
| Purchase of fixed assets | (423) | (392) |
| Increase in investments and other receivables, net | - | (31,428) |
| Proceeds from sale of fixed assets | - | 30 |
| Proceeds from realization of investments in investee companies | 562,177 | 102,875 |
| Investment in short-term deposits and investments, net | 63,412 | 460,818 |
| Net cash inflow (outflow) generated by investing activities | (7,663) | 819,140 |
| Cash flows generated by financing activities: | | |
| Equity issuance | - | 43,011 |
| Receipt of long-term loans and other long-term liabilities | 637,000 | 360,213 |
| Payments of long-term loans and other long-term liabilities | (628,703) | (1,107,283) |
| Credit from banks and others, net | 11,743 | (13,600) |
| Net cash (outflow) inflow generated by financing activities | 20,040 | (717,659) |
| Increase (decrease) in cash and cash equivalents | 20,460 | (15,586) |
| Balance of cash and cash equivalents at beginning of year | 9,205 | 24,791 |
| Balance of cash and cash equivalents at end of year | 29,665 | 9,205 |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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

Company Statements of Cash Flows (cont'd)

| | Year ended December 31 | |
|---|------------------------|---|
| | 2004 | 2003 |
| | Reported amounts* | Adjusted in terms of NIS thousands December 2003 |
| (A) Adjustments to reconcile net earnings (losses) to cash flows generated by operating activities: | | |
| Income and expenses not involving cash flows: | | |
| Equity in operating results of investee companies in addition, net of dividend received therefrom | 47,879 | (17,120) |
| Depreciation and amortization | 2,022 | 13,718 |
| Deferred taxes, net | (18,580) | (58,903) |
| Increase (decrease) in liability in respect of employee severance benefits, net | 3,491 | (6,898) |
| Net capital losses (gains) from realization: | | |
| Fixed assets | - | 96 |
| Investment in investee companies | (213,249) | (11,635) |
| Increase in value of deposits and other erosions, net | (6,623) | (11,260) |
| Exchange rate differences and erosion of long-term loans and other liabilities | 6,077 | (24,865) |
| Erosion (linkage) of loans from banks and others | - | (10,526) |
| Changes in value of investments and assets | - | 673 |
| | (178,983) | (126,720) |
| Changes in operating assets and liability items: | | |
| Increase in current accounts of investee companies, net | 36,543 | (43,975) |
| Decrease (increase) in receivables | (213) | 42,817 |
| Increase (decrease) in trade payables and other payables | 5,746 | (35,551) |
| | 42,076 | (36,709) |
| | (136,907) | (163,429) |

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(B) Significant non-cash transactions:

| | | | |
|---|-------|-------|-------|
| Dividend in kind from investee company | - | - | |
| | ===== | ===== | ===== |
| Proceeds from realization of affiliated company in capital note | - | - | |
| | ===== | ===== | ===== |
| Loans converted into shareholders' equity of subsidiary | 6,837 | - | |
| | ===== | ===== | ===== |

* With respect to discontinued of adjustment for the effect of inflation as from the CPI of Decem

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

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 1 - General

Koor Industries Ltd. is a holding company, which operates in the fields of telecommunications, defense electronics, agro-chemicals and other chemicals and venture capital investment, through its subsidiaries, proportionately consolidated companies and affiliates (hereinafter - the "Koor Group" or the "Group").

The Company's shares are traded both on the Tel Aviv Stock Exchange and on the New York Stock Exchange.

Note 2 - Significant Accounting Policies

The financial statements have been prepared in accordance with generally accepted accounting principles ("GAAP") in Israel.

The significant accounting policies, which were applied on a consistent basis, are as follows:

A. Definitions:

In these financial statements:

1. The Company - Koor Industries Ltd. ("Koor" or "the Company").
2. Subsidiaries - companies, including partnerships, whose statements are fully consolidated, directly or indirectly, with those of the Company.
3. Proportionately consolidated companies - jointly controlled companies, which are consolidated by the proportionate consolidation method, directly or indirectly, in Koor's

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consolidated financial statements.

4. Affiliates - companies in which Koor has voting rights which give it significant influence over the operating and financial policies of these companies, and which are not subsidiaries or proportionately consolidated companies. Such companies are included on the equity basis.
5. Investees - subsidiaries, proportionately consolidated companies or affiliates.
6. Other companies - companies, the investment in which does not confer significant influence, which are accounted for by the cost method.
7. Interested parties - as defined in Paragraph (1) to the definition of "related parties" in Section 1 of the Israeli Securities Law, including related parties as defined in Opinion 29 of the Institute of Certified Public Accountants in Israel ("ICPAI").

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

- A. Definitions (cont'd):
 8. Controlling shareholders - as defined in the Israeli Securities Regulations (Financial Statement Presentation of Transactions between a Company and its Controlling Shareholder), 1996.
 9. Venture capital fund - as defined in Standard No. 1 of the Israel Accounting Standards Board ("IASB").
 10. Venture capital investments - an investment in a company that meets the following two conditions:
 - (a) The company is engaged primarily in research, development or marketing of innovative, high-technology products or processes; and
 - (b) At least 90% of the company's financing stems from owners' capital (including shareholder loans and owner-guaranteed credit), with the support of state authorities or research grants.
 11. Consumer Price Index - the Israeli Consumer Price Index (CPI) published by the Central Bureau of Statistics.
 12. Dollar - U.S. dollar.
 13. Adjusted amount - the historical nominal amount that was

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adjusted in conformity with the provisions of Opinions 23 and 34 and Opinions 36 and 37.

14. Reported amount - an amount adjusted to the transition date (December 31, 2003), plus amounts in nominal values that were added after the transition date, minus amounts that were deducted after the transition date.
 15. Adjusted financial reporting - financial reporting based on the provisions of Opinions 23, 34, 36, 37 and 50.
 16. Nominal financial reporting - financial reporting based on reported amounts.
- B. Financial statements in reported amounts
- (1) In October 2001, the Israel Accounting Standards Board published Accounting Standard No. 12 on "Discontinuation of Adjustment of Financial Statements". According to this standard, and in accordance with Accounting Standard No. 17 published in December 2002, the adjustment of financial statements for the effects of changes in the general purchasing power of the shekel will be discontinued, commencing January 1, 2004. Until December 31, 2003, the Company continued to prepare adjusted financial statements in accordance with Opinion No. 36 of the ICPAI. The Company is applying the provisions of the Standard and, accordingly, the adjustment was discontinued, as stated, commencing January 1, 2004.
 - (2) In the past, the Company prepared its financial statements on the basis of historical cost, adjusted to the Consumer Price Index. The adjusted amounts that were included in the financial statements as at December 31, 2003, served as the starting point for the nominal financial reporting commencing January 1, 2004. Additions made during the period were included in nominal values.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

- B. Financial statements in reported amounts (cont'd)
- (3) The non-monetary asset amounts do not necessarily represent their realizable or current economic value, but rather the reported amounts of those assets.
 - (4) In the financial statements, the term "cost" means cost in reported amount.
 - (5) The financial statements of companies classified as autonomous units, are stated based on the changes in the exchange rates of their relevant functional currencies - see 2.D below.

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(6) All comparative data for earlier periods are stated adjusted to the CPI for December 2003.

C. Reporting principles

(1) Balance sheets:

a. Non-monetary items (namely - fixed assets, inventory of projects in progress and investments stated at cost) are stated in reported amounts.

b. Monetary items are stated in the balance sheet at historical nominal values as at the balance sheet date.

(2) Statements of operations:

a. Revenues and expenses deriving from non-monetary items (such as: depreciation and amortization, changes in inventory, prepaid expenses and income, etc.) or from balance sheet provisions, are derived from the change between the reported amounts in the opening balance and closing balance.

b. The remaining statement of operations items (such as: sales, purchases, current manufacturing costs, etc.) are stated at nominal values.

(3) Statement of changes in shareholders' equity

A dividend declared in the reporting period is stated at nominal values.

D. Effects of the changes in foreign currency exchange rates

The Company has been applying Accounting Standard No. 13 on "The Effect of Changes in Foreign Currency Exchange Rates" since January 1, 2004. The Standard deals with the translation of foreign currency transactions and the translation of financial statements of overseas operations for their inclusion in the financial statements of the reporting corporation. The Standard prescribes rules for classifying foreign operations as an autonomous foreign unit or as an integrated unit, based on indications listed in the Standard and the use of judgment, as well as the manner in which the financial statements of autonomous held units are to be translated.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

D. Effects of the changes in foreign currency exchange rates

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Foreign currency transactions

Transactions denominated in foreign currency are recorded when first recognized at the exchange rate prevailing on the transaction date. Exchange rate differences deriving from the discharge of monetary items, or deriving from the reporting of the Company's financial items at exchange rates that are different than those used for preliminary recording during the period, or from those reported in prior financial statements, will be charged to the statement of operations.

Foreign operations classified as an autonomous held unit

For certain investees which are domiciled in Israel, and whose revenues and most of their raw materials and fixed assets are acquired in dollars, and for which the dollar is the major currency in the economic environment in which the companies operate, the dollar constitutes the measurement and reporting currency in their financial statements. This is in accordance with the rules provided in Section 29A of Opinion 36 of the Institute of Certified Public Accountants in Israel.

The financial statements of investees operating in a foreign country as "an autonomous held unit" of the Group and companies registered in Israel, the measuring and reporting currency of which is foreign currency (dollar) as aforementioned, were translated to Israeli currency as follows:

- (1) The monetary and non-monetary assets and liabilities of an overseas autonomous held unit were translated at the closing rate. The goodwill balance created in the acquisition of the overseas autonomous held unit is treated as an asset of that unit and is translated at the closing rate as of January 1, 2004.
- (2) Income and expense items are translated at the exchange rate prevailing on the transaction date.
- (3) All exchange rate differences created were classified as a separate item in shareholders' equity until the net investment is realized.

The impairment of an investment in an autonomous held unit overseas does not constitute partial realization. Therefore, no part of the translation differences were charged to the statement of operations when the impairment was recorded.

The financial statements of investees operating overseas that are an "integrated unit" of the Group, in accordance with the indicators provided in Standard 13 of the Israeli Accounting Standard Board, are translated from foreign currency to Israeli currency - with non-monetary items translated at the historical exchange rate prevailing on the transaction date and monetary items translated at the exchange rate prevailing on the balance sheet date. Statement of operations items are translated at the average exchange rate, except for revenues and expenses related to non-monetary items that were translated at the historical exchange rates at which the related non-monetary items were translated. Differences created from the translation are charged to financing.

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- E. Consolidation of financial statements
- (1) The consolidated financial statements include the financial statements of Koor and of all the companies in which the Company has control. Jointly controlled companies are included in the consolidated financial statements by the proportionate consolidation method.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

- E. Consolidation of financial statements
- (2) For the purpose of the consolidation, the amounts included in the financial statements of the consolidated companies were included after the adjustments necessitated by the application of the uniform accounting principles adopted by the Group.
- (3) The consolidated financial statements include the pro rata share of asset, liability, income and expense items of proportionately consolidated companies, based on the holding percentages in these companies.
- (4) As to the financial statements of subsidiaries that are adjusted according to changes in foreign currency exchange rates - see Note 2.D.
- (5)
- a. The excess cost of an investment over the fair value of its identified assets less the fair value of the identified liabilities (after allocation of the tax deriving from temporary provisions) on acquisition date, is charged to goodwill.
 - b. The excess cost allocated to assets and liabilities is charged to the appropriate balance sheet items.
 - c. Material intercompany balances and transactions between Group companies were eliminated for consolidation purposes. Likewise, material unrealized income from intercompany sales not yet realized outside the Group were eliminated.
- (6) The Company's shares that were acquired by the Company and subsidiaries are presented as treasury stock.
- (7) When the sale and/or exercise of convertible securities that were issued by investees (including in respect of employee options) is probable, according to the criteria prescribed in

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Opinions 48 and 53 of the IACPA, and a decline in the shareholding percentage is expected when they are converted or exercised, as a result of which the holder will sustain a loss, an appropriate provision is included in respect of the anticipated loss.

- (8) The Company applies Accounting Standard No. 20 on the "Goodwill Amortization Period". Goodwill is stated in the consolidated balance sheet in "other assets and deferred expenses" and is amortized over its estimated useful life, in a methodical manner. The amortization period represents the best possible estimate of the period in which the Company expects to derive future economic benefit from the goodwill. The amortization period is not to exceed 20 years from the date of initial recognition. Accordingly, the Group companies amortize goodwill mainly over a period of 10 to 20 years.

The Standard applies to financial statements for periods beginning on or after January 1, 2004. The change in the amortization period of amortization balances as at January 1, 2004 is treated as a prospective change in estimate. These goodwill balances will be amortized methodically over the remainder of the prescribed amortization period.

F. Use of estimates:

Preparation of the financial statements in conformity with generally accepted accounting principles requires management to use estimates and assessments that influence the reported amounts of assets and liabilities and the disclosure relating to contingent assets and liabilities, as well as the revenues and expenses in the reporting period. It should be clarified that actual results may differ from such estimates.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

G. Cash and cash equivalents:

Cash and cash equivalents include short-term bank deposits and short-term government notes traded in banks, with an original maturity of three months or less and which are not restricted.

H. Marketable Securities:

- (1) Marketable securities
Investments in marketable securities held for the short term as a current investment are stated at realization value on the stock market as at the balance sheet date. Investments in marketable securities, which are permanent investments, are stated at cost (debentures - including accrued interest), as long as there has not been a decrease in value, which is not of a temporary nature (see also section

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(3) below). The changes in the value of the securities are charged in full to the statement of operations.

- (2) Non-marketable securities
Stated at cost (debentures - including accrued interest), which, in management's opinion is not higher than realization value (see also section (3) below).
- (3) Decrease in value of investments
From time to time, the Company reviews its permanent investments in other companies to identify if there has been a non-temporary decrease in their value. Such a review is carried out where there are indications of the possibility that the value of permanent investments has been impaired, including a drop in stock market prices, the investee's businesses, the industry in which the investee operates and other parameters. The impairment in the value of these investments, which management bases on an evaluation of all the relevant aspects, giving appropriate weight to each and which is not temporary, is charged to the statement of operations.

I. Allowance for doubtful accounts:

The financial statements include allowances for doubtful accounts, which management believes fairly reflect the loss inherent in accounts whose collection is doubtful. Among the factors on which management bases its determination of the appropriateness of the allowances are an assessment of risk, based on information it has on the financial status of the debtors, the volume of their activity and a valuation of the collateral received from them. The allowance is determined specifically for accounts whose collection is doubtful.

J. Inventories:

Inventories are included at the lower of cost or market value. Cost is determined as follows: Raw materials, auxiliary materials and spare parts - at "moving average" or by the "first-in, first-out" method. Finished goods and work-in-process - some on the basis of direct manufacturing costs (including materials, labor and subcontractor costs) plus the related part of indirect manufacturing costs, and some on an average basis (including raw materials, tools, labor) and other direct and indirect expenses. Merchandise at "first-in, first-out" method or by the "moving average".

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

K. Work in progress:

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Inventory of long-term projects in progress is stated at cost, less the part of cost that has been charged to the statement of operations by the "percentage of completion" method. The cost includes the direct cost of materials, wages, subcontractors, other direct costs and indirect manufacturing costs allocated to the said projects (also see Note 2.5 below).

Projects in progress and customer advances in respect of long-term contracts include amounts in respect of contracts to be executed over a period exceeding one year.

Where a loss is anticipated from the project, a provision is made for the entire loss anticipated until completion of the project.

L. Venture capital investments:

The holdings of a venture capital fund in venture capital investments are stated at cost in their reported amounts, net of provisions for decline in value, if a non-temporary decline occurs. Gains from venture capital investments are charged to the statement of operations when the investment is realized.

M. Investments in investees:

- (1) The investments in investees are presented by the equity method. Taken into account when computing the Company's share are losses due to the expected realization of convertible securities issued by investees, if the conversion or exercise of those securities is probable.

Taken into account when determining the equity value of the investments in these companies are the amounts as they are included in the companies' financial statements, after the adjustments necessitated by the application of generally accepted accounting principles.

- (2) Regarding the goodwill amortization policy - see Note 2E(8) above.

- (3) Regarding the decline in value of investments in investees - see Note 2.AD.

A list of investee companies is presented as an appendix to the financial statements.

N. Monetary balances stated at present value

Monetary balances - long-term debts and liabilities that are interest free or bear interest at below-market rates, are stated at their present value, computed using the interest rate prevailing in the market on the date created.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 2 - Significant Accounting Policies (cont'd)

- O. Fixed assets:
1. The assets are stated at cost, after deduction of related investment grants.
 2. Cost includes interest capitalized during the set-up period, which was calculated using the interest rates applicable to the sources used to finance the investment.
 3. Improvements are charged to the cost of assets and are amortized over the economic life of the asset. Repair and maintenance expenses are charged to the statement of operations as incurred.
 4. Depreciation is computed using the straight-line method, on the basis of the estimated useful lives of the assets.

The annual depreciation rates used are as follows:

| | % | |
|--|--------|---------------------|
| | ----- | |
| Buildings and leasehold rights | 1.2-10 | (mainly 2%) |
| Machinery, equipment and installations | 5-20 | (mainly 10%) |
| Vehicles and forklifts | 10-20 | (mainly 15%) |
| Office furniture and equipment | 6-33 | (mainly 6% and 25%) |
| Computers and auxiliary equipment | 20-33 | |
| Lease hold improvements | *10 | |

* or over the lease period, whichever shorter.

- P. Other assets and deferred expenses:

Other assets and deferred expenses are amortized on a straight-line basis over the expected period of benefit therefrom, as follows:

1. Licensing of products and acquisition of know-how are stated at cost and are mostly amortized over eight years.
2. Marketing rights are stated at cost and amortized over periods of five to ten years.
3. Intangible assets in the purchase of products are stated at cost and are mainly amortized over 20 years.
4. Deferred expenses - debenture issue costs:

These costs are amortized by the straight-line method over the life of the debentures - mainly six years.
5. See Note 2.E(8) regarding goodwill deriving from the acquisition of companies that were consolidated.
6. Non-compete and confidentiality agreements are mostly

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amortized over 5 years.

The amortization period is reevaluated periodically, based on the estimated period of economic benefit.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

Q. Convertible securities:

1. Debentures, the conversion of which is not probable, are included at their liability value as at the balance sheet date, in accordance with the provisions of Opinion 53 of the ICPAI, and are stated in long term liabilities. Debentures, the conversion of which is probable, are included between the long-term liabilities item and the shareholders' equity item, according to the liability value or the capital value, whichever is the higher.
2. In accordance with Opinions 48 and 53 of the ICPAI, the provision for loss on a decline in the shareholding percentage in investee companies is included in the item "minority interest" in the consolidated balance sheet, and in the item "investment in investees" in the Company balance sheet.

R. Deferred taxes:

1. Deferred taxes are calculated in respect of temporary differences between the amounts included in the adjusted financial statements and the amount taken into account for tax purposes. Such deferred taxes are allocated for differences related to assets, the consumption or depreciation of which are deductible for tax purposes. As for the main components in respect of which deferred taxes have been created - see Note 16.G.
2. Deferred tax balances (asset or liability) are computed at the tax rate expected to be in effect at the time these taxes will be utilized, or when the tax benefit will be realized, based on the tax rates and tax laws legislated or whose legislation is essentially complete by the balance sheet date.

The deferred taxes amount in the statement of operations expresses the change in these balances during the year.
3. Taxes that would be imposed in the event of realization of investments in investees, the sale of which is not expected in the foreseeable future, are not included in deferred taxes.

Deferred taxes were not created for taxes to be imposed on

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earnings distributed by subsidiaries, as it is the Company's policy not to distribute taxable dividends in the foreseeable future. Likewise, tax benefits are not included in respect of temporary differences, the realization of which is doubtful.

S. Revenue recognition:

Revenues and costs from work in progress under long-term contracts are recognized in accordance with Accounting Standard No. 4 ("Standard 4") published by the Israel Accounting Standards Board ("IASB"), as follows:

- A. Revenues and costs from work in progress under long-term contracts will be recognized by the "percentage of completion" method, if the following conditions are met: the revenues are known or can be reliably estimated, the collection of revenues is expected, the costs involved in carrying out the project are known or can be reliably estimated, there is no material uncertainty as to the ability to complete the project and to meet the terms of the contract with the customer, and the percentage of completion may be reliably estimated.

As long as all the conditions listed above are not met, revenue will be recognized at an amount equal to the costs incurred and the recovery of which is expected ("zero margin").

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

- S. Revenue recognition: (cont'd)
- B. Revenues and costs in government contracts, which are based on cost plus a fixed margin ("cost plus"), are reported on the basis of the invoices submitted to the customer (essentially - on an accrual basis).
- C. The percentage of completion is determined based on the cost (actual cost vs. projected total cost) or based on the delivery of products, depending on the nature of the agreement.
- D. For contracts in which a loss is anticipated, a provision is recorded immediately for the full amount of the anticipated loss at the time it is identified by management.
- E. Projected earnings or losses from long-term contracts could change as a result of changes in estimate, between the actual performance and the original estimate. Such changes in estimates are charged to the statement of operations when identified.

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2. Sale of products and providing services:

Revenues from sales and services are recognized upon delivery of the products and transfer of the main risks and rewards involved in ownership of the products, or upon performance of the services.

In special contracts, sales are recognized after the work is performed and acceptance tests are passed, as prescribed in the product supply contract.

T. Sale of trade receivables:

See Note 3C(2).

U. Research and development expenses:

Research and development expenses -
Research and development costs, net of participations (mainly from the Government of Israel), are charged to the statement of operations as incurred. Research and development costs financed by the customer are charged to the cost of projects in progress, and are included in the statement of operations as part of the recognition of results from such projects.

Research and development in process -
Costs to acquire in-process research and development which have no alternative future use and which have not reached technological feasibility at the date of acquisition are expensed as incurred.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

V. Presentation of transactions between the Company and the controlling shareholder:

Transactions between the Company and its controlling shareholder are included in accordance with the Securities Regulations (Financial Statement Presentation of Transactions between a Company and its Controlling Shareholder), 1996. Accordingly, the difference between the price paid to the controlling shareholder on the sale of an asset and the book value of the asset to the controlling shareholder, is included in the shareholders' equity.

In addition, the amount of the erosion of an unlinked interest-free loan having no maturity date which was received from the controlling shareholder, and that the parties do not intend to repay, is included in shareholders' equity

W. Derivative financial instruments:

Koor and its subsidiaries enter into different kinds of option

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contracts and forward trades that are intended to reduce the financial risks (i.e. commitments for the import of raw materials, export of goods, liabilities linked to the CPI or foreign currency) involved in the exposure to fluctuations in inter-currency exchange rates, interest rates and changes in the CPI.

The results of financial derivatives held to hedge assets and liabilities are recorded in the statement of operations concurrently with the recording of the changes in the hedged assets and liabilities. Financial derivatives that are not held for hedging are stated in the balance sheet at fair value. Changes in the fair value are included in the statement of operation in the period they occurred.

The fair value of derivative financial instruments is determined according to their market values or quotes by financial institutions, and when such do not exist, according to a valuation model.

X. Earnings (losses) per share:

Earnings (losses) per share data are computed in accordance with Opinion 55 of the ICPAI.

Taken into account in the computation of basic earnings (losses) per share are convertible securities issued by the Company, if their conversion or exercise is probable, based on tests prescribed in the opinion. Taken into account in the computation of fully-diluted earnings (losses) per share are convertible securities issued by the Company and its investees, that were not included in the computation of basic earnings (losses) per share, when their conversion or exercise does not increase earnings per share.

Y. Dividend declared subsequent to balance sheet date

In accordance with Accounting Standard No. 7 on "Subsequent Events", the liability related to a dividend proposed or declared subsequent to the balance sheet date is expressed in the accounts only in the period in which it was declared. Likewise, separate expression is given in the statement of changes in shareholders' equity to the dividend amount to be distributed against a reduction in the retained earnings balance.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

Z. Segment reporting

Segment reporting is presented in accordance with Accounting Standard No. 11, which requires the inclusion of information in respect of business and geographical segments, as well as detailed guidelines for identification of the business and geographical segments.

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AA. Environmental costs

The current operating and maintenance costs of facilities to prevent environmental pollution and provisions for expected costs related to the rehabilitation of the environment deriving from current or past activities, are charged to the statement of operations. Construction costs of facilities for prevention of environmental pollution, which increase the economic life or efficiency of the facility or reduce or prevent environmental pollution, are charged to the cost of the fixed assets and are depreciated in accordance with the depreciation policies practiced by the Group.

AB. Impairment of assets

The Company applies Accounting Standard No. 15 - Impairment of Assets ("the Standard"), which prescribes procedures that the Company must implement in order to assure that its assets in the consolidated balance sheet (which are subject to the Standard) are not stated at an amount exceeding their recoverable value, which is the higher of the net sales price and the usage value (the present value of the estimated future cash flows expected to derive from the use and realization of the asset).

The Standard applies to all of the assets in the consolidated balance sheet, except for tax assets, construction contracts and monetary assets (aside from monetary assets that are investments in investees that are not subsidiaries). Likewise, the Standard prescribes the presentation and disclosure principles for assets that have declined in value. When the carrying value of an asset in the consolidated balance sheet exceeds its recoverable amount, the Company recognizes an impairment loss equal to the difference between the book value of the asset and its recoverable value. A loss so recognized will be reversed only if changes have occurred in the estimates used in determining the recoverable value of the asset, since the date on which the last impairment loss was recognized.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 2 - Significant Accounting Policies (cont'd)

AC. Data regarding the CPI and the Dollar exchange rate:

| | Israeli CPI* | Exchange rate of one Dollar |
|---------------------|-----------------|--------------------------------|
| | Points | NIS |
| For the year ended: | | |
| December 2004 | 180.74 | 4.308 |
| December 2003 | 178.58 | 4.379 |

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December 2002 182.01 4.737

| | % | % |
|-----------------|-------|-------|
| | ----- | ----- |
| Changes during: | | |
| 2004 | 1.2 | (1.6) |
| 2003 | (1.9) | (7.6) |
| 2002 | 6.5 | 7.3 |

| | % |
|--|-------|
| | ----- |
| Real rate of increase (decrease) in the CPI relative to the exchange rate of the dollar during the year: | |
| 2004 | 2.8 |
| 2003 | (5.7) |
| 2002 | (0.8) |

(*) According to the CPI for the month of the balance sheet date 1993 average basis

Assets and liabilities in foreign currency or linked thereto are included in the financial statements according to the representative exchange rate published by the Bank of Israel on the balance sheet date.

Assets and liabilities linked to the CPI are included in the financial statements according to the CPI of the balance sheet month, or the previous month, as relevant.

AD. Influence of new accounting standards prior to their application

In July 2004, the IASB published Accounting Standard No. 19, "Taxes on Income", which prescribes that a deferred tax liability is to be recognized for all temporary differences that are taxable, except for a limited number of exceptions. Likewise a deferred tax asset is to be recognized for all temporary differences that are deductible, losses for tax purposes and unutilized tax benefits, if it is expected that there will be taxable income against which it will be possible to utilize them, except for a limited number of exceptions. The new Standard will apply to financial statements beginning on January 1, 2005. The Standard will be adopted as the cumulative effect of a change in accounting method. First time application of the said Standard will have a net non-recurring impact, as at January 1, 2005, of increasing the net income by approximately NIS 19 million (which mainly derives from recording deferred taxes in an investee company in respect of unrealized profits which are anticipated to be realized in the near future).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees

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- A. ECI Telecom Ltd. ("ECI") - an affiliate
1. In November 2003, a valuation of ECI was performed by an independent appraiser, for the purpose of evaluating the recoverable value of Koor's investment in ECI. In accordance with this appraisal, the Company reversed the impairment loss from decline in value that had been created in 2001, based on various indications, including a valuation for ECI. The reversal of the loss of NIS 73 million was charged against the capital reserve from foreign currency translation adjustments (credit), which was realized when the provision was created.

At the request of the appraiser (who agreed that the Company would make use of the valuation), the Company undertook to indemnify him against any expense or financial damage he will sustain, if any, with respect to any claim to be filed by any third party against the appraiser, the cause of action of which is the valuation.

As at December 31, 2004, the balance of the investment in ECI, stated by the equity method, is NIS 673 million.

2. In its financial statements for 2003, ECI reported on a retroactive restatement of its financial statements for 2002 and for the fourth quarter of that year, relating to a decrease in the value of its investment in an affiliate (received in exchange for the transfer of certain assets), having an effect on the investment in ECI of about 2 million dollars.

The amount of the restatement was taken into account by the Company, when in the third quarter of 2002, it included an impairment provision for decline in value of its investment in ECI, based on a valuation obtained from an independent appraiser. Therefore, this restatement in the financial statements of ECI has no effect on the financial statements of the Company for the years 2002 and 2003.

3. On March 9, 2004, the board of directors of ECI resolved to distribute 7.6 million shares of ECTel (42% of the paid-up share capital of ECTel) as a dividend to the shareholders of ECI. The shares of ECTel were distributed on May 10, 2004, after all the requisite approvals were obtained. Prior to the distribution, ECI had held 10.5 million shares of ECTel (58% of the paid-up share capital of ECTel). Following the distribution, ECI holds 16% of the shares of ECTel and Koor directly holds 12.9% of the shares in ECTel. The investment in ECTel is presented in the financial statements of ECI and of Koor by the cost method.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 3 - Information Regarding Certain Investees (cont'd)

- A. ECI Telecom Ltd. ("ECI") - an affiliate (cont'd)
4. ECI prepares its financial statements in accordance with generally accepted accounting principles in the U.S. For the adjustment of ECI's net income (loss) as reported in accordance with U.S. generally accepted accounting principles (US GAAP) to the net losses according to Israeli generally accepted accounting principles:

| | Year ended | |
|---|----------------|------|
| | 2004 | |
| | US\$ thousands | US\$ |
| Net gain (loss) of ECI based on its reporting according to US GAAP | 10,153 | |
| Adjustments: | | |
| Temporary differences resulting from recognition of revenue arising from application of SAB 101 | - | |
| Finance income - FAS 133 | (8,303) | |
| Tax expenses | (1,529) | |
| Amortization of excess cost attributed to intangible assets | (1,233) | |
| Profit from marketable securities | (1,282) | |
| Decline in value of assets | 968 | |
| Cumulative effect of a change in accounting method - FAS 142 | - | |
| Discontinued activities | - | |
| Net loss of ECI according to Israeli GAAP | (1,226) | |

- B. Tadiran Ltd. (in voluntary liquidation) ("Tadiran") - a subsidiary

On March 7, 2002, Tadiran's Board of Directors adopted a resolution to begin the voluntary liquidation of Tadiran and to appoint a liquidator. Following the liquidation, the debit balance of the capital reserve from foreign currency translation adjustments at Koor in respect of its investment in Tadiran of approximately NIS 391 million was transferred to the statement of operations.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 3 - Information Regarding Certain Investees (cont'd)

- C. Makhteshim Agan Industries Ltd. ("M-A Industries") - a subsidiary
1. As at December 31, 2003, Koor held 48.59% of the voting rights in M-A Industries, and taking into account the voting agreement with certain other shareholders, Koor held most of the voting rights. Therefore, the financial statements of M-A Industries for 2003 were included in the consolidated financial statements of the Company.

In January 2004, Koor sold 27 million shares of M-A Industries for approximately NIS 418 million. The capital gain of NIS 160 million (before tax) is included in "other income". Likewise, a tax asset of NIS 59 million which had been created in 2003, because of the expectation that the carryforward tax losses would be utilized, was realized as a result of this sale.

As a result of this sale, and after the realization and conversion of convertible securities that had been allotted to the public and to employees, Koor's holding percentage in the voting rights of M-A Industries at December 31, 2004 is 38.6% (32.9% on a fully diluted basis).

Following the sale of the shares in January 2004, as a result of which Koor's shareholding percentage in M-A Industries fell below 50%, Koor evaluated the existence of effective control in M-A Industries and the implications for continuing to consolidate M-A Industries in the financial statements of Koor, beginning from the first quarter of 2004.

In the opinion of Koor's management, the range of circumstances that weight Koor's shareholding percentage in M-A Industries, the broad dispersal of voting rights among the other shareholders, the low level of shareholding by the other shareholders, the slim probability of the creation of a block of votes opposing Koor at shareholder meetings and past experience related to the attendance at shareholder meetings, as well as the voting percentages and opposition at the meetings, show that the economic substance that stood and continues to stand at the basis of the relationship between the Company and M-A Industries immediately before and after the said transactions demonstrates effective control, i.e., Koor's ability to set the financial and operational policies of M-A Industries.

See Note 27(4) regarding an additional sale of shares of M-A Industries.

2. In October 2001, M-A Industries and its subsidiaries entered into a securitization arrangement, pursuant to which those companies sold all of their trade receivables to foreign companies established for that purpose and which are neither owned nor controlled by M-A Industries ("the Special Purpose Companies"). Purchase of the receivables was financed by an American company from the Bank of America Group.

On September 28, 2004, M-A Industries and certain subsidiaries ("the Companies") signed an agreement with Bank

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of America to terminate the securitization undertaking. On that same date, the Companies entered into a new agreement with Rabobank International for the sale of trade receivables in a securitization transaction to replace the previous agreement with Bank of America. The new agreement is similar in principle to the prior agreement with certain changes including among others that in the new agreement additional M-A Industries subsidiaries are included in the transaction.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

- C. Makhteshim Agan Industries Ltd. (M-A Industries) - subsidiary (cont'd)
- 2. (cont'd)

Under the terms of the new securitization agreement, the Companies will sell their trade receivables to a foreign company established for this purpose and which are neither owned nor controlled by M-A Industries ("the Purchasing Company"). The purchase of the trade receivables by the Purchasing Company will be financed by the American company Erasmus Capital Corporation of the Rabobank International Group. During the transition from the previous agreement to the new agreement, the Purchasing Company purchased the trade receivables remaining in the ownership of the Special Purpose Companies. The trade receivables included in the securitization transaction meet certain criteria, as stipulated in the agreement.

The maximum amount of financial resources expected to be made available to the Purchasing Company to purchase the trade receivables of the Companies is 250 million dollars (compared with 150 million dollars in the previous securitization agreement), on a current basis, so that the proceeds received from the customers whose receivables had been sold will be used to purchase new trade receivables.

The period in which the companies will sell their trade receivables to the Purchasing Company will be one year from the closing date of the transaction. This period may be extended, with the consent of all the parties, for additional one-year periods, up to a maximum of 4 extensions.

As at balance sheet date, cash in the amount of about 142.5 million dollars was received from the sale of customer debts (December 31, 2003 - about 125.3 million dollars).

The price at which the trade receivables are sold is the amount of the sold receivables, which are reduced based on the period expected to elapse between the date the trade

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receivables are sold and the date they are repaid.

On the purchase date of the receivables, the Purchasing Company will pay most of the price of the receivables in cash, and the balance in a deferred liability that will be paid after collection of the sold receivables. The percentage of the cash proceeds varies according to the behavior of the trade receivables portfolio.

The companies will bear all the losses sustained by the Purchasing Company as a result of the non-payment of the trade receivables included in the securitization transaction, up to the balance of the total unpaid balance of the sales price included in the subordinated note.

The Purchasing Company will have no recourse against the companies in respect of amounts paid in cash, except for receivables in respect of which a commercial dispute arises between the companies and their customers, i.e. a dispute with respect to the non-fulfillment of the seller's obligation in the agreement to supply the product, such as: not supplying the correct product, a defective product, a delay in the supply date, etc.

The Companies will handle the collection of the trade receivables included in the securitization transaction for the Purchasing Company.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

- C. Makhteshim Agan Industries Ltd. (cont'd)
- 2. (cont'd)

The essence of the accounting treatment of the sale of trade receivables in a securitization transaction is the recognition of the sale of the trade receivables only for that part for which the control and risks were transferred finally and absolutely to the purchaser. Accordingly, the trade receivable balances included in the securitization transaction, for which the consideration of cash and/or non recourse liabilities was received, were written off. In respect of the part of the trade receivables included in the securitization transaction not recognized as a sale, a subordinated note was recorded in the amount of the difference between the trade receivable balances included in the securitization transaction and the proceeds, as noted, and the recording of receivables in respect of those trade receivables sold for which proceeds were received subsequent to the balance sheet date.

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A loss from the sale of trade receivables is charged at the time of sale to the statement of operations in the item "other expenses".

Under the terms of the agreement, M-A Industries undertook to meet certain financial covenants, mainly a ratio of liabilities to capital and profitability ratios. As at the balance sheet date, M-A Industries is in compliance with the covenants.

3. In April 2001, the board of directors of M-A Industries resolved to adopt a dividend policy of distributing 15%-30% of annual net earnings, subject to the existence of distributable earnings and to specific resolutions by the board of directors.

In accordance with this policy, a dividend was declared and paid in 2004 in the amount of 32.9 million dollars (of which 7.2 million dollars is in respect of the earnings of 2003). A dividend of 11.2 million dollars was declared in December 2004 and paid in early 2005.

Subsequent to balance sheet date, another dividend was declared in respect of the earnings of 2004, in the amount of 12.7 million dollars.

4. Acquisition of companies in the report year:

- a. In April 2004, M-A Industries, through a wholly-owned and controlled subsidiary, signed agreements to acquire ownership and control in a group of three companies, Vegetation Management LLC, Farm Saver.com LLC and Nation Ag II LLC ("the acquired companies"), which are engaged in the registration, import and marketing of agrochemicals in the U.S.

The total sales price amounted to NIS 303 million (the price is after an amendment to the original contract made in December 2004). NIS 34.4 million of the total sales price was paid through a transfer of 1,908 thousand shares of M-A Industries that had been held by a subsidiary (cost of shares - NIS 19.2 million).

The excess cost of investment created upon the acquisition was NIS 235.8 million, of which NIS 130.2 million was allocated to intangible assets (namely registration and licensing). The amount of NIS 2.3 million was attributed to tax liabilities and NIS 2.7 million was allocated to inventories. The balance of NIS 105.2 million was allocated to goodwill.

The excess cost allocated to licensing and registration, as well as to goodwill, are amortized over a 20-year period, which, in the estimation of M-A Industries, represents the period of economic benefit deriving from them.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

C. Makhteshim Agan Industries Ltd. (cont'd)

4. Acquisition of companies in the report year: (cont'd)

a. (cont'd)

The statements of operations and the statements of cash flows of the acquired operations were consolidated beginning May 1, 2004. The effect on the consolidated statement of operations of the first-time consolidation of the acquired operations is additional revenues of NIS 108 million for the period ended December 31, 2004 and an addition to net earnings (after amortization of goodwill) of NIS 25 million for that period (Koor's share in the additional net earnings is NIS 10 million). The effect on the consolidated balance sheet as at December 31, 2004 is an increase in assets of NIS 334 million.

b. In the report year, M-A Industries, through subsidiaries, signed agreements for the acquisition of three marketing companies, as follows:

1) In June 2004, M-A Industries, through a wholly owned and controlled subsidiary, signed an agreement for acquisition of 45% of the rights in the U.S. company, Control Solutions Inc. ("CSI"), which is engaged in the marketing of pesticides to the non-agricultural market in the United States.

Pursuant to the acquisition agreement, as long as the subsidiary holds 45% of the shares of CSI, decisions in areas critical to CSI are to be made jointly by all the shareholders of CSI. Therefore, CSI has been consolidated in the financial statements by the proportionate consolidation method.

In addition, the subsidiary was granted an option, which may be exercised at any time during the next three years, to increase its share in CSI to 60%, in exchange for a payment ranging between NIS 6.8 million and NIS 47.8 million, based on CSI's earnings in 2004-2006.

Furthermore, commencing in 2009, the subsidiary and the remaining shareholders of CSI have the right to require the

subsidiary to acquire from the remaining shareholders of CSI the balance of their shares in CSI in consideration for an amount to be determined based on the earnings of CSI in the three years preceding the acquisition date.

- 2) In July 2004, M-A Industries, through a wholly owned and controlled subsidiary, signed an agreement for acquisition of all the shares and rights of Farmoz PTY Limited, an Australian company engaged in the marketing and distribution of pesticides in Australia.
- 3) In August 2004, M-A Industries, through a subsidiary, signed an agreement for acquisition of 50.1% of the rights in the U.S. company, RiceCo LLC, which is engaged in the development and marketing of herbicides for rice.

The aggregate acquisition cost of the acquired marketing companies was NIS 185.7 million. The excess cost created as at the acquisition date totalled NIS 140.9 million, of which NIS 68 million was allocated to intangible assets (namely registration and licensing), the amount of NIS 15.8 million was attributed to deferred tax liabilities, NIS 3.1 million was allocated to inventories, and the balance of NIS 85.6 million was allocated to goodwill.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

C. Makhteshim Agan Industries Ltd. (cont'd)

4. Acquisition of companies in the report year: (cont'd)

b. (cont'd)

The excess cost that was allocated to registration and licensing as well as the goodwill are amortized over a 20-year period, which, in the estimation of M-A Industries, represents the period of economic benefit deriving from them.

The statements of operations and the statements of cash flows of the three marketing companies were consolidated from their acquisition date. The total effect of the first-time consolidation of the acquired marketing companies on the consolidated

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statement of operations is additional revenues of NIS 207 million for the period ended December 31, 2004 and a decrease in net earnings (after amortization of goodwill) of NIS 1 million during that period. The effect on the consolidated balance sheet as at December 31, 2004 is an increase in assets of NIS 314 million.

5. In a private placement to institutional investors (mainly overseas) in March 2004, M-A Industries allotted non-marketable convertible debentures in the amount of 150 million dollars par value (including 5 million dollars which was issued to the underwriters in April 2004), in consideration for their par value. See Note 15B(1).
6. In March 2004, a subsidiary of M-A Industries transferred to a third party, in an off-exchange transaction, 7 million shares of M-A Industries it had held. Under the terms of the agreement, the proceeds will be paid by the end of one year from the transfer date, whether in cash, based on the share price on the stock exchange on such date, or whether in the shares of M-A Industries plus an increment of 0.5% of the share price on the stock exchange. Since the cash proceeds have not yet been received, no capital issuance was recorded by M-A Industries in respect of the transferred shares. During the second quarter, 1,908 thousand shares of the above shares were returned, for the purpose of paying the consideration for the acquisition of a group of companies in the U.S., as discussed in Note 3(C)(4)(a) above. Subsequent to balance sheet date an additional 750 thousand shares were returned and an extension was granted with respect to the rest of the shares.

See Note 27(1) regarding the purchase of MABENO.

7. On February 3, 2005, Koor sold 15.9 million shares of M-A Industries for NIS 374 million. The resultant gain of NIS 204 million will be charged in the Company's financial statements for the first quarter of 2005. As a result of the sale, the utilization of carryforward tax losses is certain. Therefore, the Company recorded a deferred tax asset of NIS 69 million in the reporting period - (see Note 27(4)).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

- D. Telrad Networks Ltd. ("Telrad") - a subsidiary
1. On September 28, 2004, Koor and Telrad Holdings, a wholly-owned subsidiary ("the Koor Group") entered into an agreement to sell 39% of its holdings in Telrad Networks to Fortissimo GP Capital Fund L.P. ("Fortissimo") for 21 million

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dollars.

The sale will be effected in two stages. In the first stage, which was closed in November 2004, Koor transferred 19.5% of the Telrad Networks shares to Fortissimo for consideration of 10.5 million dollars. In the second stage, to be closed 180 days after the closing of the first stage, Fortissimo will transfer the balance of the consideration, amounting to 10.5 million dollars, and will receive the balance of the sold shares. The Koor Group and Fortissimo agreed on a formula, whereby if Fortissimo does not transfer the entire balance in the second stage, it will receive shares on a basis proportionate to the consideration paid. In such a situation, there are cases in which changes will be made to the composition of the board of directors, in the voting rights given to the minority shareholders, in the loan amounts and in the options terms, as described below.

Fortissimo was given an option, exercisable for a period of up to 48 months from the closing date of the first stage, to acquire additional shares from the Koor Group, whereby Fortissimo's total holdings will not exceed 49% of the shares of Telrad Networks. The exercise price will be determined according to the value of Telrad Networks, which will not be less than its shareholders' equity in the financial statements on the exercise date.

As part of the share-sale agreement, the parties agreed that upon the closing of the first stage of the sale, the Koor Group would transfer 9.5 million dollars as a loan to Telrad Networks, and with the closing of the second stage, would transfer an additional 11.5 million dollars. These loans will bear annual interest of Libor+2% per annum, and will mature 20 years from the closing date of the first stage. On the closing date of the first stage, the Koor Group provided Telrad Networks with the said 9.5 million dollar loan. As at December 31, 2004, based on estimates by the Company's management, forecasts on the operating results of Telrad Networks and a range of indemnifications provided in the transaction, the management of Koor Group assessed that the value of the loan was impaired. Therefore a provision was recorded in the amount of the net loss that will be incurred by the Group.

As to the indemnifications given by the Koor Group as part of this transaction, see Note 18A(5)(C).

Pursuant to the sale agreement, Telrad's board of director appointed 3 directors from Koor, 3 directors from Fortissimo, and an outside expert with the consent of the parties, who, as at the publication date of the financial statements, was not as yet appointed.

The agreement stipulates a list of matters which must be approved by the joint consent of the Koor Group and Fortissimo, including: approval Telrad's budget, appointment of Telrad's executives and determining their terms of employment and a dividend distribution. Those rights confer to the minority shareholders the right to actually participate in the significant decisions related to the Telrad's normal course of business, and, therefore, prevent Koor's Group, the majority shareholder, from actual control

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over Telrad Networks and require the joint consent of Koor and Fortissimo in decisions on matters that are critical for the operating objectives of Telrad.

Therefore, beginning from the fourth quarter of 2004, Telrad is included in Koor's financial statements by the proportionate consolidation method, at a rate of 80.5%.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

D. Telrad Networks Ltd. (cont'd)

1. (cont'd)

Below is the Company's share in the balance sheet date of Telrad as at December 31, 2004 (in NIS thousands):

| | |
|-----------------------|-----|
| Current assets | 296 |
| Non-current assets | 144 |
| Current liabilities | 197 |
| Long-term liabilities | 91 |

The Company's share in the results of Telrad at the fourth quarter of 2004 (in NIS thousands):

| | |
|--------------------|-----|
| Income | 93 |
| Costs and expenses | 155 |

2. During the report period Telrad recorded an impairment of its deferred tax assets by NIS 67 million, due to changes in management's estimation of the probability of utilization of the company's carryforward tax losses.

3. In 2004, Telrad's board of directors approved a reorganization plan that includes additional employee layoffs in addition to prior early retirement plans in 2000 to 2002. The financial statements for 2004 included in the item "other income (expenses), net" an expense of NIS 29 million (of which NIS 3 million is in respect of previous plans) (expenses of reorganization plan in 2003 and 2002 totaled NIS 2 million and NIS 107 million, respectively).

E. Elisra Electronic Systems Ltd. ("Elisra") - a subsidiary

1. On March 17, 2001, a fire broke out at the plants of Elisra's subsidiaries - Tadiran Systems Ltd. and Tadiran Spectralink Ltd. ("the companies"). The fire caused damage to equipment, building, inventories and projects in progress. The book value of the equipment, inventories and identified costs in projects in progress that were damaged

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in the fire, together with the building restoration costs and other costs, are estimated at approximately 36 million dollars. As at the balance sheet date, advances were received from the insurance company of approximately 10 million dollars. The claim sent by the companies to the insurance company, which was based on the terms of the insurance policy, also include a demand for amounts related to consequential damage and other damages that, in the opinion of the companies, is covered by the insurance policy. Therefore, the total amount of the claim is significantly higher than the book value damage and restoration cost of the building, as aforesaid.

The companies took legal measures to receive insurance compensation and even filed a lawsuit in Tel Aviv District Court against the insurance company and its appraisers in the amount of 96 million dollars. In view of the duration of the proceedings, the managements of the companies decided to classify the balance of the income receivable from the insurance companies as a long-term receivable.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

E. Elisra Electronic Systems Ltd. ("Elisra") - a subsidiary (cont'd)

1. (cont'd)

In the estimation of the companies, based on factors including opinions from their counsel on this matter, it is difficult to estimate at this stage what the chances are that the companies will receive the full amount of the claim, although they are assessed as solid. Nonetheless, the managements of the companies, based, as aforesaid, on the opinions of their counsel on this matter, estimate that the chances are good that indemnification will be received from the insurance company at an amount exceeding the balance of the receivable recorded by them as assets in the financial statements.

In April 2004, the companies filed a motion with the court to issue a partial ruling of 33 million dollars (beyond the advances already paid by the insurance company), based on the admission of liability by the insurance company and its representatives deriving from the insurance incident, whereas the dispute focuses on the level of damages. In December 2004, a hearing was held in the Court in which a ruling was put into effect, with the consent of the parties, whereby a separate bank account would be opened, in which the insurance company would deposit 15 million dollars. Any withdrawal from this account would require the Court's approval, until the

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conclusion of the proceedings in the lawsuit. According to the above agreement, the lawsuit was sent to arbitration before retired Supreme Court Justice Prof. Yitzhak Zamir, and at this time, the court proceedings will be stayed until the end of the arbitration.

2. In July 2002, the Company, Elisra and Elta Electronic Industries Ltd. ("Elta" or "the Buyer") signed an agreement ("the Purchase Agreement"), whereby Koor sold 30% of Elisra's shares to Elta for 100 million dollars. The sale was closed in November 2002. As a result of the sale, Koor recorded a capital gain in 2002 of NIS 339 million, under the item "other income, net".

In addition, Koor granted options to Elta, exercisable until December 31, 2003, to increase its holdings in Elisra by up to an additional 8% in consideration of a maximum sum of approximately 26 million dollars. This option expired and was not exercised by Elta. Under the Purchase Agreement, Koor agreed to indemnify Elta if certain conditions, set out in the Agreement, are fulfilled. Also see Note 18A(3).

As part of the agreement between Koor and Elta, an agreement was signed, to which Elisra is a party, setting forth the structure of Elisra's board of directors and the decision-making process, as well as certain limitations with respect to the sale of Elisra's shares. In addition, a cooperation agreement was signed between Elisra and Elta, with regard to activities between the companies, including a proposal for an agreed range of products and the principles for selecting a project leader from time to time.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

- F. Koor Corporate Venture Capital ("Koor CVC") - a consolidated partnership
 1. Regarding commitments to invest and other investments subsequent to balance sheet date, see Note 18B(5).
 2. During the current year, Koor CVC's management estimated that the value of the portfolio investments was lower than their cost, and therefore decided to write-down the value of the investment by approximately NIS 58 million (in 2003 and 2002 - NIS 72 million and NIS 93 million, respectively).
 3. In June 2004, Cisco Systems purchased all the shares of Riverhead Inc. from its shareholders for consideration of 39 million dollars. The share of Koor CVC in the proceeds is 7 million dollars. The gain to Koor CVC is NIS 17 million.
- G. Knafayim Holdings Arkia ("Knafayim") - affiliate

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1. During 2003 and in the first quarter of 2004, Knafayim acquired shares, which did not confer the status of related party, and various types of options of El Al Israel Airlines Ltd. ("El Al"). During the second quarter of 2004, after receiving the requisite approval to increase its stake in the shares of El Al above 5%, Knafayim exercised some of the options. Thus, after the exercise, Knafayim held 22% of El Al's issued share capital. Pursuant to a third-party voting agreement, Knafayim held 24.9% of the voting rights of El Al. During the third quarter of 2004, Knafayim filed a request with the State of Israel, which holds a special share in El Al, for approval to increase its stake in El Al above 25%. On August 5, 2004 the Anti-Trust Commissioner approved the merger between Knafayim and El-Al, with restrictive conditions, mainly regarding the sale of Knafayim's aviation activities to an independent third party.

On December 22, 2004, Knafayim received the requisite approval to increase its stake in the shares of El Al to 40%, and to a shareholding that would grant control over El Al. Upon receipt of this approval, Knafayim exercised part of the purchase option so that as of December 31, 2004 Knafayim holds approximately 39.8% of the issued and paid shares of El Al and approximately 42.8% of the voting rights in El Al according to authorization that was granted to Knafayim by a third-party.

2. On September 29, 2004 the Company signed two agreements to sell 16% of the shares of Knafayim for approximately NIS 121 million. In the statement of operations for the third quarter of 2004, the Company recorded a gain of NIS 43 million. As a result of the sale, the Company's shareholding in Knafayim decreased from approximately 28.3% to approximately 12.2%. Accordingly, the investment in Knafayim is stated by the cost method, beginning from the date of the sale.

In addition, on September 29, 2004, the Company signed an agreement for the sale of an additional 3% of the shares of Knafayim for approximately NIS 23 million. The conditions for closing the sale were fulfilled on October 20, 2004. Therefore a gain of approximately NIS 8 million was recorded in the fourth quarter of 2004.

As of the balance sheet date, the Company holds approximately 9% of Knafayim. Since management intends to sell the remainder of the shares in Knafayim, the investment is presented within current assets. As a result of management's intention to sell the remainder of its holding in Knafayim, the Company recorded deferred taxes of approximately NIS 8 million during the reporting period in respect of the anticipated utilization of carryforward tax losses.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 3 - Information Regarding Certain Investees (cont'd)

H. Tadiran Communications Ltd. ("Tadiran Communications") - an affiliated Company

1. On September 10, 2004 the Company signed an agreement to acquire about 33% of the shares of Tadiran Communications (about 31% taking into consideration stock options the exercise of which is probable) from two shareholders for approximately NIS 637 million (approximately 144 million dollars). Tadiran Communications develops, manufactures and markets communication devices and systems mainly for military purposes. The sale was closed in November 2004. The purchase was financed by a loan received from an Israeli bank in consideration for a lien in favor of the bank on the sold shares.

Excess cost created on the acquisition date totaled NIS 490 million (111 million dollars), which was allocated based on the valuation received from an independent appraiser. At the request of the appraiser (who agreed that the Company would make use of the valuation), the Company undertook to indemnify him against any expense or financial damage he will sustain, if any, with respect to any claim to be filed by any third party against the appraiser, the cause of action of which is the valuation.

Provided below is the allocation of excess cost (according to a holding rate of 31%):

| | NIS millions |
|---------------------------------------|--------------|
| | ----- |
| Current assets | 14 |
| Investments and long-term receivables | 1 |
| Fixed assets | 1 |
| Intangible assets (1) | 308 |
| Goodwill (2) | 242 |
| Current liabilities | 19 |
| Long-term liabilities | 3 |
| Deferred taxes (3) | (98) |

- (1) The intangible assets include NIS 20 million allocated to in-process research and development, which were charged to the statement of operations on the acquisition date, in accordance with the provisions of FIN 4. The balance of NIS 288 million was allocated to intangible assets with an average life of seven years, according to the following breakdown: NIS 14 million allocated to brand name, NIS 173 million allocated to customer list, NIS 98 million allocated to technology and NIS 3 million allocated to the orders backlog.
- (2) Useful life of goodwill is estimated at 10 years.
- (3) Deferred taxes deriving from the allocation of excess cost.

2. On December 27, 2004, Koor entered into a series of agreements with Elbit Systems Ltd. ("Elbit") and with Federman Enterprises Ltd. ("Federman"). Under the terms of

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the agreements, Koor will sell its entire holdings in Tadiran Communications (33%) to Elbit for 146 million dollars ("Elbit sale"). Concurrently, Koor will acquire 9.8% of Elbit's share capital from Federman for 99 million dollars ("Federman sale"). On the date the agreements were drafted, Elbit held 4.2% of the shares of Tadiran Communications and Federman held 50% of Elbit's shares. On March 1, 2005, a general meeting of the shareholders of Elbit ratified the Elbit sale.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 3 - Information Regarding Certain Investees (cont'd)

H. Tadiran Communications Ltd. ("Tadiran Communications") - an affiliate (cont'd)

2. (cont'd)

The two sales are interconnected and will be executed - subject to the conditions stipulated in the agreements, including approval of the Anti-Trust Commissioner and other approvals - in two stages.

In the first stage, Koor will sell 13.8% of Tadiran Communications to Elbit for 63 million dollars and concurrently Koor will acquire 5.3% of the shares of Elbit from Federman for 53 million dollars. The closing date for the first stage will be in the second quarter of 2005, or at a later date, if so agreed by the parties. After the closing of the first stage, Koor will be entitled to appoint one director to Elbit's board, and Elbit will be entitled to appoint three of the members of Tadiran Communications' board of directors.

In the second stage of the transaction, Koor will sell the balance of its holdings in Tadiran Communications (19.2%) to Elbit for 83 million dollars and concurrently will acquire 4.5% of the shares of Elbit for 46 million dollars. In addition to the aforementioned conditions, the second stage is contingent on the closing of a transaction in which Tadiran Communications will acquire from Koor the holdings of Koor (70%) in Elisra Electronic System Ltd.

The closing date for the second stage of the agreements was scheduled for September 30, 2005. If all the other conditions are fulfilled, but the Elisra transaction has not been closed, the date will be postponed to April 30, 2006 or to another date agreed upon by the parties.

After both stages in the Elbit sale and the Federman sale are executed, Koor will no longer hold shares of Tadiran Communications, although it will hold 9.8% of the Elbit shares and will have the right to appoint 20% of Elbit's directors. One of the directors nominated by Koor will serve

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as Vice Chairman of the Board of Directors of Elbit.

It was further agreed by the parties that if the second stage of the sales is not closed within sixteen months of the signature date of the agreements, then the board of directors of Tadiran Communications will be comprised in a manner whereby Koor and Elbit will have the same number of directors in the board of directors of Tadiran Communications, and there will be rotation of two-year terms for the chairman of the board, with Koor's candidate being the first to serve.

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Koor Industries L

Notes to the Financial Statements

Note 4 - Short-Term Deposits and Investments

| | Consolidated | |
|--|---------------|---------|
| | December 31 | |
| | 2004 | 2003 |
| | NIS thousands | |
| Marketable securities (1): | | |
| Debentures | 122,706 | 141,221 |
| Short-term Treasury notes | 145,927 | 74,628 |
| Shares and options | 106,773 | 56,010 |
| Mutual fund participation certificates | - | 5,618 |
| | 375,406 | 277,477 |
| Deposits in banks and financial institutions | 37,584 | 89,161 |
| Short-term loans and current maturities of long-term loans | 3,478 | 171 |
| | 416,468 | 366,809 |

(1) Presented at market value.

Note 5 - Trade Receivables

Consolidated:

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Open accounts
 Deferred promissory note and receivables from sale of
 customers' debts*
 Post dated checks receivable and credit card companies
 Current maturities of long-term trade receivables

Including:
 Net of allowance for doubtful accounts

* See Note 3C(2).

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Koor Industries

Notes to the Financial Statements

Note 6 - Other Receivables

| | Consolidated | |
|-------------------------------|---------------|---------|
| | December 31 | |
| | 2004 | 2003 |
| | NIS thousands | |
| Government agencies | 195,708 | 126,043 |
| Deferred taxes, see Note 16G | 171,310 | 156,030 |
| Accrued income | 31,639 | 31,289 |
| Prepaid expenses | 48,498 | 45,712 |
| Employees | 8,524 | 8,855 |
| Affiliates - current accounts | 643 | 2,378 |
| Others | 72,661 | 82,863 |
| | 528,983 | 452,170 |

Note 7 - Inventories and Work in Progress

Consolidated:

A. Inventories and work in progress, net of
 customer advances

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Presented as current assets:

Industrial inventory:

Raw and auxiliary materials

Goods and work in progress

Finished goods

Advances in respect of materials

Inventories for trading operations -merchandise,
including advance payments

Less - customer advances

B. Customer advances, net of work in progress

Presented as current liabilities:

Customer advances in respect of work in progress(1)(2)

Less - inventory and work in progress

(1) Not including long-term advances

(2) See Note 22 regarding guarantees provided for
securing the gross amounts of customer advances
(including long-term advances).

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Koor Industries

Notes to the Financial Statements

Note 7 - Inventories and Work in Progress (cont'd)

C. Financial value of contracts signed during the report
period

D. The balance of the financial value of existing contracts
which were not recognized as revenues as at the
balance sheet date

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Notes to the Financial Statements

Note 8 - Investments in Investee companies

A. Consolidated balance sheet - affiliates

Net asset value of the investments (1) (2)

Goodwill and original difference (2):

Original amount
Accumulated amortization

Long-term loans (3)

- (1) As follows:
 Net asset value of investments as at December 31, 1991
 Changes from January 1, 1992:
 Cost of shares acquired or received
 Accumulated losses, net
 Changes in capital reserves and foreign currency
 translation adjustments
 Initially consolidated subsidiaries, net
 Disposals, net
- (2) Including investments in companies traded on the
 Stock Exchange in Tel Aviv or abroad, in NIS millions:
 Carrying value at the balance

 Market value as at balance date
- (3) Linkage terms and interest rates relating to long-term loans:

 Linked to the CPI - bearing interest at the rate of 5.5%,
 without maturity date
 Linked to the Dollar - bearing interest at the rate of
 LIBOR + 1%, without maturity date (*)

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(*) On December 31, 2004, the LIBOR rate is 3.1%.

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Koor Industries

Notes to the Financial Statements

Note 8 - Investment in Investee Companies (cont'd)

B. Company balance sheet - investees

Shares:

Net asset value of the investments

Goodwill and original differences:

Original amount, net

Accumulated amortization

Book value (1)

Payments on account of shares (1)

Long-term loans and capital notes (2)

Non-current inter-company accounts (3)

(1) As follows:

Cost of shares including accumulated earnings as at
December 31, 1991

Changes from January 1, 1992:

Cost of acquired shares

Accumulated losses, net

Changes in capital reserves and erosion of capital notes, net

Disposals

Book value, including payments on account of shares (4)

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Notes to the Financial Statements

Note 8 - Investment in Investee Companies (cont'd)

B. Company balance sheet - investees (cont'd)

- (2) Long-term loans and capital notes:
 Long-term loans (a) (b)
 Capital notes - unlinked and not bearing interest (c)

Less - current maturities of long-term loans

(a) Long-term loans classified by linkage terms and interest rates:

| | Interest rate at December 31 | D |
|----------------------|---------------------------------|-------|
| | ----- | ----- |
| | 2004 | ----- |
| | % | ----- |
| Linked to the Dollar | 3 | ----- |
| Linked to the CPI | 7-2 | ----- |
| Linked to the CPI | No interest | ----- |

(b) The loans mature in the years subsequent to the balance sheet date (excluding current maturities) as follows:

- Second year
 Third year
 Fourth year
 Fifth year
 Thereafter

(c) Capital notes are not presented at their present value, since

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their repayment date has not yet been fixed by the parties.

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Koor Industries

Notes to the Financial Statements

Note 8 - Investment in Investee Companies (cont'd)

B. Company balance sheet - investees (cont'd)

(3) Non-current inter-company accounts:

Linked to the Dollar
Unlinked-bears interest at the rate of the increase in the CPI

(4) Including investments in marketable shares traded on the Tel Aviv Stock Exchange or abroad in NIS millions:

Carrying value

Market value as at balance date

Note 9 - Other Investments and Receivables

A. Composition:

| Consolidated | |
|---------------|------|
| ----- | |
| December 31 | |
| 2004 | 2003 |
| ----- | |
| NIS thousands | |
| ----- | |

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| | | |
|--|---------|---------|
| Deposits in banks and in financial institutions | 47,278 | 49,180 |
| Non-current trade receivables | 5,229 | 9,362 |
| Long-term loans receivable from others | 113,637 | 73,498 |
| | ----- | ----- |
| Total (see Note B above) | 166,144 | 132,040 |
| Marketable securities | 33,471 | 1,625 |
| Venture capital investment | 171,207 | 230,390 |
| Indemnification receivable for fire damages (1) | 111,508 | 113,346 |
| Non-marketable shares and payments on account | 1,040 | 1,036 |
| Others | 5,661 | 4,947 |
| | ----- | ----- |
| | 489,031 | 483,384 |
| | ===== | ===== |

(1) See Note 3E(1)

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Koor Industries

Notes to the Financial Statements

Note 9 - Other Investments and Receivables (cont'd)

B. Classification by linkage terms and interest rates of deposits, non - current
long - term loans from others:

Consolidated:

| | Interest rates at December 31 |
|---|----------------------------------|
| | ----- |
| | 2004 |
| | ----- |
| | % |
| | ----- |
| Linked to the CPI | Mainly 5.7 |
| Linked to the foreign currency (mainly to the Dollar) | Mainly 0 |
| Linked to dollar | Libor* + 2% |
| Unlinked | - |

* As at December 31, 2004 the Libor rate is 3.1%.

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Company:

Linked to the CPI

5.7

C. Repayment schedule of deposits, non-current customers balances and long-term loans from others, in the consolidated balance sheet:

| | Consolidated | |
|--|---------------|---------|
| | December 31 | |
| | 2004 | 2003 |
| | NIS thousands | |
| Amounts collectible in the: | | |
| Second year | 75,680 | 50,094 |
| Third year | 19,957 | 45,958 |
| Fourth year | 13,748 | 8,230 |
| Fifth year | 3,852 | 3,909 |
| Thereafter and without a specific maturity date | 52,907 | 23,849 |
| | 166,144 | 132,040 |

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Koor Industries

Notes to the Financial Statements

Note 10 - Fixed Assets

A. Consolidated

| | Land (including leasehold land) | Buildings | Machin equipment installat |
|----------------------------|---------------------------------------|-----------|----------------------------------|
| | NIS thousands | | |
| Cost as at January 1, 2004 | 115,651 | 1,705,294 | 3,751, |

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| | | | |
|---|----------------|-------------------|------------|
| Additions during the year | 679 | 34,908 | 146, |
| Disposals during the year | (8) | (5,446) | (18, |
| Adjustments resulting from foreign currency translation differences* | (257) | (7,153) | (41, |
| Acquisition of subsidiaries, net Company that became proportionately consolidated | 932 (4,184) | 2,694 (31,526) | 2, (55, |
| Balance as at December 31, 2004 | 112,813 | 1,698,771 | 3,784, |
| Accumulated depreciation as at January 1, 2004 | 1,233 | 652,118 | 2,072, |
| Additions during the year | 46 | 38,812 | 159, |
| Disposals during the year | - | (2,054) | (16, |
| Adjustments resulting from foreign currency translation differences* | (13) | (1,698) | (23, |
| Acquisition of subsidiaries, net Company that became proportionately consolidated | - (82) | 372 (9,178) | 1, (48, |
| Balance as at December 31, 2004 | 1,184 | 678,372 | 2,144, |
| Write down for decline in value | - | 11,707 | |
| Net book value as at December 31, 2004 | 111,629 | 1,008,692 | 1,639, |
| Net book value as at December 31, 2003 | 114,418 | 1,041,469 | 1,678, |
| * See Note 2B(5) | | | |

(TABLE CONTINUED)

A. Consolidated

| | Office furniture and equipment | Tools and instruments | Installation under construction and payment on account of acquisition of asset |
|---|--------------------------------------|--------------------------|--|
| Cost as at January 1, 2004 | 202,506 | 3,167 | 822 |
| Additions during the year | 18,391 | - | 764 |
| Disposals during the year | (3,185) | - | (92) |
| Adjustments resulting from foreign currency translation differences* | (283) | - | 71 |
| Acquisition of subsidiaries, net Company that became proportionately consolidated | 5,685 (6,973) | - - | - - |
| Balance as at December 31, 2004 | 216,141 | 3,167 | 1,565 |
| Accumulated depreciation as at January 1, 2004 | 130,618 | - | - |
| Additions during the year | 22,876 | - | - |

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| | | | |
|---|---------|-------|-------|
| Disposals during the year | (2,250) | - | |
| Adjustments resulting from foreign currency translation differences* | (2,094) | - | |
| Acquisition of subsidiaries, net Company that became proportionately consolidated | 1,592 | - | |
| | (3,900) | - | |
| | ----- | ----- | ----- |
| Balance as at December 31, 2004 | 146,842 | | |
| | ===== | ===== | ===== |
| Write down for decline in value | - | - | |
| | ----- | ----- | ----- |
| Net book value as at December 31, 2004 | 69,299 | 3,167 | 1,565 |
| | ===== | ===== | ===== |
| Net book value as at December 31, 2003 | 71,888 | 3,167 | 822 |
| | ===== | ===== | ===== |
| * See Note 2B(5) | | | |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 10 - Fixed Assets (cont'd)

A. Consolidated (cont'd)

- (1) Some of the real estate properties have not yet been registered in the Land Registry Office in the name of the subsidiaries, in some cases because of the absence of formal parceling of the area.

Leasehold rights are for a period of 49 years, ended in the year 2004 and thereafter. Certain leases provide an option for extension for another 49 years.

The cost of leasehold real estate as at December 31, 2004, is approximately NIS 751 million, of which approximately NIS 402 million is under capitalized lease.

- (2) After deduction of investment grants, net of depreciation, which have been received from the State of Israel by certain subsidiaries under the terms of the Law for the Encouragement of Capital Investments, 1959, amounting to NIS 553 million and NIS 181 million as at December 31, 2004 and 2003, respectively (see also Note 16A).
- (3) Includes capitalized interest amounting to about NIS 137 million and about NIS 141 million to December 31, 2004 and 2003, respectively.
- (4) As for amounts charged to cost of fixed assets, see Notes 23B and E.
- (5) Including fully depreciated assets amounting to NIS 895

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million to December 31, 2004.

(6) See Note 22 regarding liens.

B. Company

Composition of the assets and accumulated depreciation, according to major groups, and changes therein during the current year, are as follows:

| | Offices and land(*) | Office Equipment |
|--|------------------------|---------------------|
| | NIS thousands | NIS thousands |
| Cost as at January 1, 2004 | 36,275 | 5,370 |
| Additions during the year | - | 423 |
| Balance as at December 31, 2004 | 36,275 | 5,793 |
| Accumulated depreciation as at January 1, 2004 | 4,252 | 2,363 |
| Additions during the year | 721 | 541 |
| Balance as at December 31, 2004 | 4,973 | 2,904 |
| Write down for decline in value | 11,707 | - |
| Net book value as at December 31, 2004 | 19,595 | 2,889 |
| Net book value as at December 31, 2003 | 20,316 | 3,007 |

(*) Represents the ownership of two stories in an office building in Tel Aviv and leasehold rights to land in Dimona, in an area of 27 dunams, not yet registered in the Company's name. The offices have not as yet been registered in the name of the Company at the Land Registry Office. The offices are on land leased under a capital lease for a period of 49 years ending in 2044.

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Koor Industries L

Notes to the Financial Statements

Note 11 - Intangible Assets, Deferred Tax Assets and Deferred Expenses

A. Consolidated balance sheet

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Intangible assets-goodwill:

Original amounts

Accumulated amortization

Licensing of products abroad:

Original amounts

Accumulated amortization

Intangible assets in the purchase of products:(1)

Original amounts

Accumulated amortization

Marketing rights and others:

Original amounts

Accumulated amortization

Deferred expenses:

Debentures issuance costs:

Original amount

Accumulated amortization

Deferred taxes receivable (see Note 16(G))

(1) Including intellectual property rights, trade mark, technological know-how, etc.

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Koor Industries L

Notes to the Financial Statements

Note 12 - Credit from Banks and Others

A. Composition:

Consolidated

December 31

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| | 2004 | 2003 |
|---|---------------|-----------|
| | ----- | ----- |
| | NIS thousands | |
| | ----- | ----- |
| From banks | 1,084,944 | 914,260 |
| Current maturities of long-term loans and debentures | 653,512 | 663,142 |
| | ----- | ----- |
| | 1,738,456 | 1,577,402 |
| | ===== | ===== |

See also Note 15A

B. Classification by linkage terms and interest rates:

| | Interest rates at |
|--|----------------------------------|
| | December 31 |
| | 2004 |
| | ----- |
| | % |
| | ----- |
| Linked to foreign currency (mainly to the Dollar) | 3.0 - 16.9 (mainly 3.5 - 4.8) |
| Unlinked | 1.8 - 11.4 (mainly 10.6) |

| | Interest rates at |
|----------------------|-------------------|
| | December 31 |
| | 2004 |
| | ----- |
| | % |
| | ----- |
| Linked to the Dollar | 3.5 - 4.8 |
| Unlinked | 5.5 |

C. See Note 22 regarding liens to secure credit.

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Note 13 - Trade Payables

| | Consolidated | |
|---------------------------|------------------|------------------|
| | December 31 | |
| | 2004 | 2003 |
| | NIS thousands | |
| Open debts | 1,660,762 | 1,337,442 |
| Cheques and notes payable | 6,693 | 5,341 |
| | <u>1,667,455</u> | <u>1,342,783</u> |

Note 14 - Other Payables

| | Consolidated | |
|---|------------------|------------------|
| | December 31 | |
| | 2004 | 2003 |
| | NIS thousands | |
| Employees and withholdings remitted | 162,639 | 162,035 |
| Provision for vacation pay and vacation expense allowance | 93,436 | 100,006 |
| Expenses to be paid | 360,760 | 252,491 |
| Government agencies (including taxes) | 252,894 | 192,770 |
| Provision for warranty and repairs and provision for losses in respect of long-term contracts | 104,171 | *87,695 |
| Payables for purchase of assets and investees | 30,036 | *27,588 |
| Severance pay payable and current portion of early retirement pensions (see Note 17) | 59,873 | 87,438 |
| Dividend proposed by subsidiary | 29,615 | 15,231 |
| Deferred income | 23,037 | 43,148 |
| Liability in respect of securities that were sold short | 24,241 | 67,515 |
| Liabilities regarding forward transaction | 46,388 | 57,061 |
| Others | 182,352 | *177,239 |
| | <u>1,369,442</u> | <u>1,270,217</u> |

Includes interested parties

* Reclassified

Notes to the Financial Statements

Note 15 - Long Term Liabilities

A. Loans

| | | Consolidated | |
|----|---|---------------|------------------|
| | | December 31 | |
| | | 2004 | 2003 |
| | | NIS thousands | NIS thousands |
| 1. | Loans from banks | 2,859,180 | 3,668,341 |
| | Less - current maturities | 651,084 | 661,998 |
| | | ----- | ----- |
| | | 2,208,096 | 3,006,343 |
| | | ----- | ----- |
| 2. | Loans from others: | | |
| | Shareholders in subsidiaries | | |
| | and in proportionately | | |
| | consolidated companies | 37,611 | 52,386 |
| | Investees | - | - |
| | Receipts from | | |
| | time-sharing units | 33,053 | 33,765 |
| | Others and long-term | | |
| | accrued expenses | 64,783 | 28,487 |
| | | ----- | ----- |
| | | 135,447 | 114,638 |
| | Less - current maturities | 2,428 | 1,144 |
| | | ----- | ----- |
| | | 133,019 | 113,494 |
| | | ----- | ----- |
| | | 2,341,115 | 3,119,837 |
| | | ===== | ===== |
| 3. | Classification by linkage terms and interest rates: | | |
| | The consolidated balance sheet: | | |
| | | | Interest rate at |
| | | | December 31 |
| | | | ----- |
| | | | 2004 |
| | | | ----- |
| | | | % |
| | | | ----- |
| | Linked to the foreign currency | | |
| | (mainly Dollar) | | 1.7-8.1 |
| | Linked to the CPI | | 3.7-7.7 |

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| | |
|---------------------------|---------|
| Linked to the CPI | - |
| Unlinked | 6.2-7.9 |
| Less - current maturities | |

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Koor Industries L

Notes to the Financial Statements

Note 15 - Long Term Liabilities (cont'd)

A. Loans (cont'd)

The Company balance sheet:

| | Interest rate at December 31 |
|---------------------------|---------------------------------|
| | 2004 |
| | % |
| a. From banks: | |
| Linked to the CPI | 6.2-6.9 |
| Linked to the Dollar | 3.6-7.7 |
| Unlinked | 6.2 |
| Less - current maturities | |
| | Interest rate at December 31 |
| | 2004 |
| | % |
| b. From investees: | |
| Capital note | - |
| Linked to the CPI | - |
| Linked to the CPI | - |

Less - current maturities

B. Debentures

1. Presented at long-term liabilities
Debentures convertible into shares of subsidiary (1)
2. Presented between long-term liabilities and shareholders equity
Debentures convertible into shares of subsidiary (2)

(1) In a private placement to institutional investors (mainly overseas) in March 2004, M-A Industries allotted non-marketable convertible debentures in the amount of 150 million dollars par value (including 5 million dollars which was issued to the underwriters in April 2004), in consideration for their par value. The debentures are for a 7-year period and bear annual interest at the rate of 1.75%. The debentures may be converted into ordinary shares of M-A Industries, of NIS 1 par value each, at a conversion rate of NIS 20.5 par value, according to a fixed exchange rate of NIS 4.514 per 1 U.S. dollar. The ordinary shares to be allotted as a result of the conversion of the debentures will be listed for trading on the Tel Aviv Stock Exchange.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 15 - Long Term Liabilities (cont'd)

B. Debentures (cont'd)

(1) (cont'd)

On March 22, 2007, the debenture holders will have the right, by serving prior written notice to M-A Industries (between 30 and 60 days prior to March 22, 2007), to demand redemption of the debentures (principal and interest balance at such date).

M-A Industries will have the right to force the

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conversion of the debentures, beginning March 22, 2007, as long as the average share price of M-A Industries in the period of 20 business days preceding the notice of forced conversion will be more than 30% higher than the conversion price of the debentures.

M-A Industries committed to the debenture purchasers that it would refrain from creating additional liens on its property, the purpose of which is the guarantee of marketable securities or other securities which the M-A Industries intends to register for trading.

The issue costs for these debentures amounted to NIS 11 million.

- (2) a. In 2001, M-A Industries issued convertible bonds and options for net consideration of NIS 276 million, of which NIS 257 million was allocated to the fair value of the convertible bonds.

M-A Industries issued NIS 270,000 thousand par value of debentures (Series A) listed on the Tel Aviv Stock Exchange, bearing interest at 2.5% p.a. and linked (principal and interest) to the representative exchange rate of the Dollar. The debentures are repayable in one payment in November 2007 if not converted before then into shares. The debentures are convertible into ordinary shares of NIS 1 par value each of M-A Industries at the rate of NIS 10.03 (following distribution of a dividend) par value of debentures per one ordinary share.

- b. In January 2002 M-A Industries issued NIS 133,980 thousand par value of debentures (Series A) in a private placement in a total consideration of approximately NIS 129 million. The terms of the debentures are the same as the terms of the debentures (Series A) issued by M-A Industries as above.
- c. In June 2002 a consolidated company of M-A Industries purchased in the stock exchange approximately NIS 16,684 thousand par value of debentures (Series A) in consideration of approximately NIS 14 million. During June 2003, all of the above debentures were sold for NIS 18.8 million.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 15 - Long Term Liabilities (cont'd)

B. Debentures (cont'd)

(2) (cont'd)

d. In 2003, NIS 57,661 thousand par value of debentures (Series A) were converted into 5,566 thousand ordinary shares, NIS 1 par value, most at an exercise price of NIS 10.36 par value of debenture per ordinary, NIS 1 par value, share. M-A Industries total share capital issued as a result of the conversion is 1,270 thousand dollars, at a premium of 11,331 thousand dollars. In 2004, 179,608 thousand par value of debentures (Series A) was converted into 17,582 thousand ordinary shares, NIS 1 par value, at a conversion rate of between NIS 10.03 and NIS 10.36 in par value of the debentures for 1 ordinary share, NIS 1 par value. The total share capital issued as a result of the conversion is 3,974 thousand dollars, with a premium of 35,581 thousand dollars.

Subsequent to the balance sheet date and proximate to the approval date of the financial statements, NIS 12,839 thousand par value of debentures (Series A) was converted into 1,280 thousand ordinary shares, NIS 1 par value.

Subsequent to the balance sheet date and proximate to the approval date of the financial statements, NIS 12,839 thousand par value of debentures (series A) was converted into 1,280 thousand ordinary shares, NIS 1 par value.

The debentures are secured by a symbolic fixed senior lien on a deposit of NIS 1 in favor of the trustee for the debenture-holders.

Beginning from 2003, conversion of the debentures became probable. Accordingly, the balance of the debentures is stated in a separate item between long-term liabilities and shareholders' equity.

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Koor Industries L

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Note 15 - Long Term Liabilities (cont'd)

C. Liabilities (net of current maturities) that will mature in the following years date are as follows:

1. Consolidated

| | Loans from banks | | D |
|------------------|------------------|-----------|-------|
| | December 31 | | |
| | 2004 | 2003 | |
| | NIS thousands | | |
| Second year | 1,284,673 | 626,983 | 20, |
| Third year | 598,769 | 1,649,252 | 17, |
| Fourth year | 182,326 | 308,944 | 12, |
| Fifth year | 52,786 | 224,854 | 9, |
| Sixth year | 18,710 | 43,029 | 1, |
| Subsequent years | 70,832 | 153,281 | 72, |
| | 2,208,096 | 3,006,343 | 133, |
| | ===== | ===== | ===== |

2. The Company

| | | | |
|------------------|--|--|--------|
| | | | D |
| | | | 2 |
| | | | |
| Second year | | | 1,027, |
| Third year | | | 461, |
| Fourth year | | | |
| Fifth year | | | 8, |
| Sixth year | | | |
| Subsequent years | | | 1,497, |
| | | | ===== |

D. See Note 22 for details of security pledged to secure loans.

(Table Continued)

| | Debentures | | D |
|-------------|--------------|------|---|
| | December 31 | | |
| | 2004 | 2003 | |
| | NIS thousand | | |
| Second year | - | - | 1 |

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| | | | |
|------------------|---------|---------|-------|
| Third year | 165,091 | - | |
| Fourth year | - | 340,270 | |
| Fifth year | - | - | |
| Sixth year | - | - | |
| Subsequent years | 646,200 | - | |
| | ----- | ----- | ----- |
| | 811,291 | 340,270 | 3 |
| | ===== | ===== | ===== |

2. The Company

| | | | |
|------------------|--|--------|-------|
| | Loans and capital note from investees | | |
| | December 31 | | |
| | ----- | ----- | ----- |
| | 2004 | 2003 | |
| | ----- | ----- | ----- |
| | NIS thousand | | |
| | ----- | ----- | ----- |
| Second year | - | 47,564 | 1 |
| Third year | - | - | |
| Fourth year | - | - | |
| Fifth year | - | - | |
| Sixth year | - | - | |
| Subsequent years | 8,125 | 8,125 | |
| | ----- | ----- | ----- |
| | 8,125 | 55,689 | 1 |
| | ===== | ===== | ===== |

D. See Note 22 for details of security pledged to secure loans.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 16 - Taxes on Income

A. Tax benefits under the Law for Encouragement of Capital Investments, 1959:

Under this law, by virtue of the "approved enterprise" status granted to certain enterprises of several investees, these companies are entitled to various tax benefits. The income derived from these enterprises during a period of up to 10 years, from the year in which these enterprises first had taxable income (limited to 12 years from commencement of production or 14 years from the date of the approval, whichever is earlier), is subject to a corporate tax rate of 0 - 25%. According to the alternative track, some of the plants of subsidiaries were granted a tax exemption for a two to four year period and are taxed at the preferential rate of 25% during the remaining benefits period.

For fixed assets serving the approved enterprise, investees are entitled to an accelerated amortization deduction over five years.

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In the event that an investee distributes a dividend to shareholders out of income attributable to revenues from an approved enterprise which received a tax exemption, the company that distributes the dividend would be liable to tax at 25% of the earnings distributed.

Deferred taxes in respect of income from approved enterprises were not provided, since it is the Subsidiaries policy not to initiate a distribution of dividend that involves an additional tax liability to the Group.

Benefits are conditional upon the fulfillment of terms set out in law or in deeds of approval. Non-fulfillment of terms could cause cancellation of the benefit, in whole or in part, and the return of benefit sums, plus interest and linkage differentials. The investees met all terms set out as above as at the dates of the financial reports.

As security for the implementation of the approved projects and compliance with the conditions of the approval, a pledge has been registered on the above subsidiaries' assets in favor of the State of Israel.

B. Measurement of results for tax purposes in accordance with the Income Tax (Inflationary Adjustments) Law, 1985 (hereinafter - "the Adjustments Law"):

The Income Tax (Inflationary Adjustments) Law, 1985 (hereinafter - "the Adjustments Law") which has been in effect since the 1985 tax year, instituted the measurement of results for tax purposes on a real basis. The various adjustments required under the Adjustments Law are meant to bring about taxation of income on a real basis. However, the adjustment of nominal income under the tax laws is not always identical to the inflationary adjustment according to the Opinions of the ICPAI. Consequently, differences are created between reported incomes according to the financial statements and between the adjusted income for tax purposes.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 16 - Taxes on Income (cont'd)

C. Law for the Encouragement of Industry (Taxation), 1969:

Certain companies qualify as "industrial companies" under the above law. By virtue of this status and certain regulations published under the inflationary adjustments law, the companies are entitled to claim, and have in fact claimed, accelerated rates of depreciation. Likewise, certain subsidiaries are entitled to file consolidated tax returns with the tax authorities.

D. Tax rates applicable to income from other sources:

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Income not eligible to "approved enterprise" benefits, mentioned in Note 16 A. above, is liable to tax at the regular rate of 35% (or if the investee is registered and operates outside of Israel, at the tax rate prescribed for that territory).

E. Losses for tax purposes carried forward to future years and tax assessments:

1. The consolidated balance of tax loss as at December 31, 2004 carryforwards to next years amounted to approximately NIS 3,030 million as at balance sheet date, out of which NIS 1,432 million relates to Koor.

Carryforward tax losses are linked to the CPI, according to the Adjustments Law.

2. The Company has received final assessments until 2002 tax year.
3. See Note 18A(7)(C) regarding fiscal claims against a subsidiary of M-A Industries.

F. Amendment to the Income Tax Ordinance

On June 29, 2004, the Knesset passed the "Law for the Amendment of the Income Tax Ordinance (Amendment No. 140 and Temporary Order) - 2004" (hereinafter - the Amendment). The amendment provides for a gradual reduction in the company tax rate from 36% to 30% in the following manner: in 2004 the tax rate will be 35%, in 2005 the tax rate will be 34%, in 2006 the tax rate will be 32% and from 2007 onward the tax rate will be 30%.

Current taxes and deferred tax balances as at December 31, 2004 were calculated based on the new tax rates prescribed in the Amendment. The effect of the change in the consolidated financial statements as at the beginning of 2004 is a decrease in income tax expenses of NIS 5,083 thousand.

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Koor Industries Lt

Notes to the Financial Statements

Note 16 - Taxes on Income (cont'd)

G. Deferred taxes:

1. Deferred taxes are presented in the consolidated balance sheet as follows:

Within current assets in respect of:
Provision for vacation pay and severance benefits
Operating loss and capital loss carried forwards (2)
Inventory, net of customer advances
Timing differences in respect of recognition of income
and expenses, net

Total in current assets, net

Within long-term assets in respect of:
Depreciation
Operating loss and capital loss carried forwards
Liability in respect of employee severance benefits
Other

Balance not expected to be realized (1)

Total in other long-term assets

Within short-term liabilities in respect of:
Provision for vacation pay and severance benefits
Timing differences in respect of recognition of income
and expenses

Total in other payables

Within long-term liabilities in respect of:
Depreciation
Operating loss and capital loss carried forwards
Inventories less customer advances
Liability in respect of employee severance benefits
Other

(1) The Company and certain subsidiaries have deferred tax assets, that are not expected to be realized, because of accumulated tax loss carryforwards and other timing differences. Companies Management's believes that it is not likely that these balances will be realized and, accordingly, no deferred taxes were created in respect thereof.

(2) The Company's balance - see Notes: 3G(2), 3C(7).

* Reclassified

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Koor Industries Lt

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Note 16 - Taxes on Income (cont'd)

G. Deferred taxes (cont'd):

2. Balances and movement of deferred taxes in the consolidated balance sheet:

| | Depreciable fixed assets | Inventories net of customer advances | Provisions for employee rights | Losses and deductions carried forward | Tim dif res rec of and |
|--|--------------------------------|---|---|--|---------------------------------------|
| | ----- | ----- | ----- | ----- | ----- |
| | NIS thousands | | | | |
| | ----- | ----- | ----- | ----- | ----- |
| Balance as at January 1, 2003 | (400,721) | (6,905) | 140,842 | 178,883 | |
| Translation differences in subsidiaries | 21,304 | 1,386 | (7,627) | (9,026) | |
| Amounts charged to statement of operations | (18,745) | 9,276 | (34,437) | 109,766 | |
| Balance as at December 31, 2003 | (398,162) | 3,757 | 98,778 | 279,623 | |
| Translation differences in subsidiaries | 8,057 | (59) | (1,124) | (4,219) | |
| Adjustments to changes in tax rate | 19,202 | (93) | (918) | (9,704) | |
| Amounts charged to statement of operations | (7,229) | 74,197 | (26,066) | (66,922) | |
| Other differences, net* | (17,739) | - | - | (3,463) | |
| Balance as at December 31, 2004 | (395,871) | 77,802 | 70,670 | 195,315 | |
| | ===== | ===== | ===== | ===== | ===== |

* Mainly subsidiaries that were sold/acquired, net.

Deferred taxes were computed at tax rates of 22% - 35%.

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Notes to the Financial Statements

Note 16 - Taxes on Income (cont'd)

H. Taxes on income included in consolidated statements of operations:

1. Composition:

| | Year ended |
|-----------------------------------|------------|
| | ----- |
| | 2004 |
| | ----- |
| | NIS t |
| | ----- |
| Current taxes | 242,082 |
| Deferred taxes | 49,647 |
| In respect of previous years, net | (4,629) |
| | ----- |
| | 287,100 |
| | ===== |

2. Below is the adjustment between the theoretical tax amount which would have been applicable if all the income of Koor Group and the consolidated companies were taxable at 35%, and the tax amount charged in the statement of income.

| | Year ended |
|--|------------|
| | ----- |
| | 2004 |
| | ----- |
| | NIS t |
| | ----- |
| Earnings (losses) before taxes on income, as reported in the statement of operations | 892,665 |
| | ===== |
| Statutory tax rate | 35% |
| | ===== |
| Theoretical tax expenses (income) in respect of these earnings (losses) | 312,433 |
| Increase (decrease) in taxes resulting from the following factors - the tax effect: | |
| Tax benefits under various encouragement laws | (49,676) |
| Non-deductible expenses for tax purposes | 19,611 |
| Losses for which deferred taxes were not recorded | 113,347 |
| Provisions for anticipated losses from the sale of assets, net | - |
| Tax loss carried forwards from prior years for which deferred taxes were not created and which were utilized during the current year | (20,037) |
| Deferred taxes in respect of prior years and which were written-off at the reporting year | 75,601 |
| Tax losses from prior years, for which deferred taxes were recorded this year | (77,483) |
| Differences between the measurement basis according to the financial statement | |

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| | |
|---------------------------------------|----------|
| to measurement basis for tax purposes | 9,520 |
| Taxes in respect of prior years | (4,629) |
| Effect of foreign subsidiaries * | (93,213) |
| Others ** | 1,626 |
| | ----- |
| Total taxes on income | 287,100 |
| | ===== |

* Relates to territories of operations in which the statutory tax rate is lower
 ** Including influence of changes in tax rate.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 17 - Liabilities for Employee Severance Benefits, Net

A. Pension, severance pay and retirement grants:

Under current labor laws and existing labor agreements, the companies in the Group are required to make severance payments, to employees who are dismissed or who retire. In respect of these liabilities, regular deposits are made by Group companies with pension and severance pay funds. The balance sheet amount represents the unfunded balance of the liabilities. As the funds deposited are not under the control and management of the Group companies, the funded amounts are not reflected in the balance sheets. These deposits and the amount stated in the balance sheet fully cover the Company's liability for employee severance benefits. Employees dismissed before reaching retirement age are entitled to severance pay, computed on the basis of their latest salary. Where amounts accumulated in the pension funds are insufficient to cover such severance pay, the company and its subsidiaries will make up the amount of the shortfall at the time of payment.

In certain subsidiaries, past experience has shown that the vast majority of employees continue to work until they reach retirement age, and these companies were not required, in the past, to make up significant shortfalls for employees who chose early retirement. Accordingly, the managements of these companies believe that there is a low probability that such shortfalls will be paid. Therefore, the financial statements of these companies do not include a provision. The financial statements of the other Group companies include a suitable provision, based on management's estimate of the salary components used to compute the pension for full coverage of the said obligation.

Regarding companies in which enhanced severance has been planned or agreed upon for the employees, appropriate provisions have been made for the supplementary amounts.

In January 2004, the Retirement Age Law, 2004 ("the Law") was enacted. The Law raises the retirement age for men and women. In the estimation of the management of the Company and its investees, the Law will not have a material impact on the Group's recorded liability for early

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pension in respect of its employees, beyond the provisions that were included in this respect.

B. Funds for severance pay and retirement grants:

The funds provisions in severance pay funds include accrued linkage differences and interest, and they are deposited in severance pay funds in banks and insurance companies. Withdrawals from the funded provision monies are contingent on fulfillment of the provisions of the Severance Pay Law.

C. Early retirement pension:

Under agreements with certain employees who retired from service, Koor Group companies have undertaken to make pension payments until they reach retirement age. The entire liability for such pensions is included in the accounts on the basis of the present value of future pension payments, computed at a monthly discount rate of 0.3%-0.4% per month (3.6% - 5% per annum).

D. Compensation for unutilized sick leave:

A provision for unutilized sick leave, according to agreements, is included in the accounts in respect of those employees who have reached the age of 55. Due to the uncertainty as to whether employees who have not reached that age will be entitled to such compensation (as a result of utilization of sick leave or early retirement), no provision has been made. The provision is computed on the basis of the latest salary for 8 working days in respect of each year during which the sick leave was not utilized.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 17 - Liabilities for Employee Severance Benefits, Net (cont'd)

E. Liabilities for severance benefits, which are presented in the balance sheet, and the amount funded in severance pay funds, are as follows:

| | Consolidated | |
|-------------------------------------|---------------|---------|
| | December 31 | |
| | 2004 | 2003 |
| | NIS thousands | |
| Severance pay and retirement grants | 265,013 | 259,455 |
| Amount accrued for | | |

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| | | |
|---|---------|---------|
| early retirement | 184,335 | 186,059 |
| Amount accrued in respect of unutilized sick leave | 14,177 | 11,853 |
| | ----- | ----- |
| | 463,525 | 457,367 |
| Less - amount funded | 266,357 | 265,365 |
| | ----- | ----- |
| | 197,168 | 192,002 |
| | ===== | ===== |

Note 18 - Contingent Liabilities and Commitments

A. Contingent liabilities

1. Anti-Trust Commissioner:

- a) During 1997, an investigation was conducted on behalf of the Anti-Trust Commissioner ("the Commissioner") in connection with alleged violations of the Anti-Trust Law, 1988 ("the Anti-Trust Law"), relating to alleged price fixing and absence of competition between Tadiran Ltd. (a subsidiary of Koor - "Tadiran") and Tadiran Telecommunications Ltd. (a former subsidiary of Koor that merged with ECI - "Telecommunications") and between Telrad Networks Ltd. (a subsidiary of Koor - "Telrad").

On September 7, 2004 it was agreed with the Commissioner that he would issue an order according to Section 50B of the Anti-Trust Law by which Tadiran and Telrad would pay to the State Treasury the total amount of NIS 8 million, without this being considered an admission of guilt by the above companies and/or any of their officers to committing any crime. It was further agreed that indictments would not be filed, in the field of public switches and in the field of private switches, and the Commissioner would not take any further action against the companies and/or their officers. The order was approved by the Court. In accordance with the agreement with the Commissioner, a provision of NIS 8 million was included in the consolidated financial statements as at December 31, 2004.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments

A. Contingent liabilities (cont'd)

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1. Anti-Trust Commissioner (cont'd)
 - b) On February 2, 2005, Koor's offices received notice from the Anti-Trust Authority that it was considering the possibility of prosecuting Koor, together with 7 other companies that are not members of the Koor Group (including 2 companies that had been owned by Koor on the relevant dates, and were later sold to third parties) and 9 executives (including 2 who had been salaried employees of Koor on the relevant dates), for violations of the anti-Trust Law. The notice came in the wake of an investigation opened by the Anti-Trust Authority in the other companies during 2001, with respect to price fixing and collusion, and the lack of competition in the frozen and canned vegetable industry. The Anti-Trust Authority claims that two companies that belonged to the Koor Group in the past had colluded with two other companies in the years 1992-1998.

According to the Anti-Trust Law, penalties can be imposed on those who violate the Law, but the Company believes, based on its legal counsel, that the said penalties, if imposed, will not have a material effect on the financial statements. Moreover, there may be civil implications if it is possible to prove that damages were caused by the aforementioned violation. The Company is unable to assess the implications in the civil law track, if any, especially due to the fact that in the opinion of the Company and its legal counsel, for the vast majority of the period involved, the statute of limitations has expired.

2. On September 21, 2004 a suit was filed against the Company, Bezeq - the Israel Telecommunications Company Ltd., Tadiran Ltd., Telecommunications, Tadiran Public Switching Ltd., (a former subsidiary in Telecommunications), and Telrad in connection with the public switches. A motion for recognition of the suit as a class action was filed together with the suit in accordance with the Law, and according to Civil Procedure regulations. In the Statement of Claim, the plaintiff alleges that during the previous decade, the defendants had engaged in activities prohibited by the Anti-Trust Law that resulted in damages to Bezeq's customers. In respect of the actions alleged by the Plaintiff, the plaintiff is asking for damages for the group that he is seeking to represent in the amount of NIS 1.7 billion.

On March 10, 2005, the Company and the other defendants submitted to the District Court their decisive objection to the request of the plaintiff to certify the claim as a class action.

In the estimation of the Company, based on its legal counsel, the chances for the suit and for the action to be recognized as a class action are remote.

As to the indemnification Tadiran gave to ECI, see Note

18A(6) (a) below.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

A. Contingent liabilities (cont'd)

3. Elisra

a) As part of the agreement for the sale of part of the Company's holdings in Elisra to Elta, as described in Note 3E(2), Koor undertook to indemnify Elta for damages, as defined in the agreement, which will be sustained as a result of breach of representations made to Elta in the agreement. The main points of the indemnification undertaking liabilities that have not expired are as follows:

1. Any amount of damages that will be sustained as a result of breach of the representation concerning the insurance indemnity rights to which the Elisra Group is entitled, relating to the fire that occurred at the Group's plants, see Note 3E(1). Elta's right to demand payment of the indemnity in this matter carries no time limit.

2. Any amount of damages that will be sustained as a result of tax payments in respect of the tax year 2001, for which Elisra will be liable, and that are at least 4 million dollars higher than the total provisions for taxes included in Elisra's financial statements for 2001; provided that the demand for payment of indemnity is submitted by Elta not later than 30 days after the date on which the self-assessment in respect of that tax year becomes final.

b) Financial covenants

1. Elisra's undertakings with banks are secured by negative pledges. Under the terms of the negative pledges, Elisra undertook to maintain financial covenants (which will be measured on the basis of the consolidated financial statements), including a minimum ratio of shareholders' equity to total assets (as described in the agreement), minimum current ratio, amount

of shareholders' equity and minimum pre-tax earnings. In addition, certain limitations were imposed on the Elisra with respect to furnishing guarantees to third parties, creating new liens and the sale or transfer of assets in material amounts.

2. During 2004, Elisra took out long-term loans totalling 20 million dollars. Under the terms of these loans, Elisra's undertakings toward the credit providers include meeting financial covenants as provided in Note 18(b) (1) above, as well as a debt coverage ratio, as defined in the agreement, which will be measured on the basis of Elisra's unconsolidated financial statements. Likewise, limitations were also imposed on Elisra relating to the distribution of a dividend and other payments to its shareholders, as stipulated in the agreement.

In the estimation of Elisra's management, during the report period and as at the balance sheet date, Elisra was in compliance with the above financial covenants.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

- A. Contingent liabilities (cont'd)
4. In accordance with the agreements with the banks, Koor undertook to maintain certain financial covenants, including minimum shareholders' equity and debt capital - of Koor and certain investees, ratio of shareholders' equity to debt capital, a ban on creating pledges or furnishing guarantees without the advance consent of the banks, and limitations prescribed in the agreement. Koor also undertook to repay part of the existing debt, by using the proceeds to be received from the realization of certain assets, if they are realized.

Additionally, Koor undertook not to sell the shares of a certain investee, except for cash, and at a percentage not to exceed that stipulated in the agreement with the banks and other limitations as mentioned in the above agreements.

As at the balance sheet date, Koor is in compliance with the above covenants.

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5. Telrad

- a. In October 1994, a claim in an unspecified amount was filed by the Engineers Union against Telrad. The claim pertains to recognition of the applicability to Telrad engineers of the salary tables included in the general collective agreements signed in the years 1994 and 1995, between the Engineers Union and employers in the public service sector, beginning January 1, 1993.

On January 31, 1996, Tel Aviv District Labor Court issued a ruling, which dismissed outright the claims of the Engineers Union.

The Engineers Union appealed the ruling to the National Labor Court, which ruled that the agreement is a collective agreement governing the relations between Telrad, the Union and the Telrad employees. Telrad filed an appeal with the Supreme Court.

On January 29, 2002, a ruling was issued dismissing Telrad's appeal. Consequently, the next stage is a hearing of evidence by the Labor Court concerning the applicability of public service sector to salaries in Telrad.

In April 1996 a parallel claim was filed by the Lod Workers Council and the Monthly Workers Committee, to have the salary scales of the public services sector applied to the employees of Telrad.

- b. In 1999, a claim was filed against Telrad by company employees who are members of Telrad's workers' committee. They are suing to be given accounts so that the plaintiffs can examine the calculation of the distribution of earnings to employees. They are also suing for a declaratory judgment which will rule that Telrad is obliged to draw up new accounts for the distribution of earnings. In addition, a motion was filed to recognize the plaintiffs as representatives of all of Telrad's workers and employees. The court dismissed the motion for a class action. A defense brief has been filed by Telrad.

Telrad recorded an appropriate provision in respect of the above claims.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

- A. Contingent liabilities (cont'd)

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5. Telrad (cont'd)

- c. As part of the agreement for the sale of shares of Telrad Networks (see Note 3D(1)), Koor and Telrad Holdings (a wholly-owned subsidiary of Koor) undertook indemnifications in respect of the following events:
1. Damage or loss sustained by the buyer from a decline in the value of the acquired shares as a result of a decrease in the equity value of Telrad Networks due to erroneous representations made on the transaction date. This indemnification will be in force until 30 days after publication of the financial statements of Telrad Networks as at December 31, 2006, except for representations on the capital structure of Telrad Networks and tax items in the financial statements, for which there is no time limit on indemnification.
 2. Telrad Networks not meeting certain targets as defined in the agreements. The indemnifications listed in this item are for between two and five years.
 3. Damage or loss sustained by the buyer in respect of erroneous representations with respect to the sellers' ownership of the shares being sold and their ability to execute the sale. This indemnification will have no time limit.

The total amount of the indemnification is limited to the amount of the consideration received from the sale of the shares of Telrad Networks (except in respect of claims, the cause of action of which is fraud, in which the amount is unlimited). As at the publication date of the financial statements, the amount of the proceeds received is about 10 million dollars.

In the event the indemnification is invoked according to one of the causes of action described previously, the amount of the indemnification will be deducted from the loans that the seller made available to Telrad Networks as part of the sale agreement.

Additionally, indemnification was given in respect of expenses that Telrad Networks will incur at an amount exceeding the sum stipulated in the agreement in respect of the recognition of a class action filed in September 2004 relating to anti-trust activities (see Note 18A(2)).

6. Tadiran and its investees

- a. In the 1999 merger agreement between ECI and Tadiran Telecommunications Ltd. ("TTL"), Tadiran Ltd. undertook to indemnify ECI for any damages (in

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excess of the amount defined in the agreement) it sustains as a result of matters under investigation by the Anti-Trust Commissioner.

This indemnification will remain valid for a period of seven years from the date of the merger and may be extended for an additional period, as long as these matters are under investigation by the Commissioner.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

- A. Contingent liabilities (cont'd)
- 6. Tadiran and its investees (cont'd)
 - b. Employees of a Tadiran plant that closed during 1990 filed actions against Tadiran, alleging that they sustained injuries or certain work-related illnesses resulting from alleged exposure to certain substances.

Tadiran has insurance policies which, relying on legal opinions, substantially cover possible damages resulting from these claims. Therefore, no provisions have been made in respect of these claims. Tadiran recorded provisions in respect of possible damages which had been covered by an insurance company currently in liquidation.

- c. In October 1999, Bezeq - The Israel Telecommunication Corp. Ltd. ("Bezeq") lodged a claim against Tadiran Ltd. whose main cause is various losses sustained by Bezeq due to delays in the performance of projects ordered in development and application contracts originally signed between Bezeq and TTL, in the amount of approximately 8.6 million dollars ("main claim").

Alternatively, Bezeq is suing for the balance of arrearage penalties to which it alleges it is entitled pursuant to these contracts, and which were not paid in full, in the amount of approximately 1.7 million dollars ("alternative claim").

In an arbitration judgment issued on February 17, 2000, all of Bezeq's arguments regarding Tadiran's liability for the main claim were dismissed. The arbitration judgment rules that pursuant to the contractual commitments between the parties, Bezeq is entitled to compensation within the framework of

arrearage penalties only. The negotiations between the parties for a settlement were unsuccessful, and the matter was returned to the arbitrator for his decision. In February 2003, a supplementary arbitration agreement was signed. The parties submitted their written arguments and the arbitrator issued his ruling on February 26, 2004. In his ruling, the arbitrator affirmed Tadiran's position and ruled in accordance with the parameters for calculating the damages that Tadiran is meant to pay to Bezeq. The parties conducted negotiations regarding implementation of the aforementioned parameters, and they agreed that the final amount would be NIS 4.6 million, which was paid subsequent to balance sheet date. The financial statements of the Company include an adequate provision.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

- A. Contingent liabilities (cont'd)
- 7. M-A Industries and its investees
 - a. Quality of the environment

The activities of M-A Industries are exposed to the risks of harming the environment, since it manufactures, stores and sells chemicals. M-A Industries invests significant amounts in order to comply with the provisions of environmental laws and regulations, and in the opinion of the management it does comply therewith. According to M-A Industries' insurance experts, the insurance policies provide coverage in the event of a sudden unexpected occurrence of environmental pollution in Israel and worldwide, subject to the relevant terms of the policy. As at balance sheet date, M-A Industries does not have insurance coverage for continuous environmental pollution.

Such insurance is difficult to obtain, and even where it can be obtained, M-A Industries believes that the terms of the insurance, including the sum insured, do not at present justify taking out such insurance.

Pursuant to an agreement with the Ministry of environmental Protection, subsidiaries decided to construct facilities for the biological treatment of waste. Construction of the facility will take about 3 years. In the estimation of M-A Industries management, the aggregate construction cost will be

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between 30 million dollars and 40 million dollars.

One of the plants of M-A Industries subsidiary is located in Ramat Hovav, along with other chemical plants, since the Government decided that the area is suitable for the construction of chemical plants under the assumption that the geological layers in that particular area are completely impermeable to seepage or pollution. The Ministry of the Environment ("The Ministry") conducted tests, which determined that there are indications of subterranean pollution in Ramat Hovav. The investigators recommended that steps be taken to prevent the continuation of leakages from active and inactive plants, which could constitute a source of pollution of the water table in the area. The subsidiary may be required to clean up the relevant areas or subterranean layers if and when it is found that the subsidiary is responsible for the said contamination. Over the past several years various tests have been performed by different agencies to test the ground contamination in the Ramat Hovav area as well as the area surrounding the subsidiary's premises in Be'er Sheva. In the opinion of the subsidiary Management, no material consequences on the financial statements are expected due to application of the recommendations deriving from the said examinations.

In May 2004, a subsidiary of M-A Industries owning additional plants at the Ramat Hovav site, received notice of a change in the terms of the license, whereby the plants must change the method used to treat sewage from the existing treatment, do so independently and through the implementation of vaporization processes. These terms include demands that, within a short period of time, the plants conduct research and development for the purpose of customizing the process to the composition of each plant's sewage, and later, to build a suitable facility. Additionally, formulation processes are to be implemented, whereby the plants must present the Ministry with a research and development program for the purpose of implementing the process with respect to the sewage. At the same time, the Ministry of the Environment set the date by which the plants must treat the sewage in the requisite format and to stop the flow of sewage into the Council's vaporization pools and treatment facilities.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

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- A. Contingent liabilities (cont'd)
- 7. M-A Industries and its investees
 - a. Quality of the environment (cont'd)

On October 10, 2004, a subsidiary of M-A Industries, together with the Israel Manufacturers Association and other companies, filed an administrative appeal with the Beer Sheba District Court against the Ministry of the Environment. The subject of the appeal is the additional conditions for obtaining a business license imposed on the appealing plants in May 2004 which are engaged in the treatment and discharge of sewage created by their activities. In the appeal, the District Court was asked to issue an order declaring that the additional terms are nullified.

On December 29, 2004 a preliminary hearing on the appeal was held. The hearing on the appeal was scheduled for March 2005.

In the estimation of M-A Industries management, based on its legal counsel, in view of the preliminary stage of the process, it is not possible at this time to estimate the prospects of the administrative appeal. In the estimation of M-A Industries, if the appeal is dismissed, it will have a material effect on the activities of the plant in Ramat Hovav and/or will require investments of amounts that M-A Industries is unable to estimate at this time.

On November 28, 2004, the Government reached a decision approving a plan related to reducing air and water pollution deriving from the "Ramat Hovav" industrial area.

The key points of the plan are:

- (a) Treatment of the plants' sewage
 - 1. By June 30, 2006, the flow of untreated sewage to the joint biological treatment facility will be halted and each plant will treat the sewage to the quality level prescribed by the Ministry of the Environment (as derive from the additional conditions for a business license from May 2004).
 - 2. By December 31, 2007, the flow of waste water to the vaporization pools will be halted and each plant will treat the waste water, to the level of quality and concentration of salts prescribed by the Ministry of the Environment (as derived from the additional conditions for a business license

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from May 2004).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

A. Contingent liabilities (cont'd)

7. M-A Industries and its investees (cont'd)

a. Quality of the environment (cont'd)

(b) Rehabilitation of existing vaporization pools

1. On January 1, 2005, the Ramat Hovav Industrial Council will begin taking action to dry and rehabilitate the area of the vaporization pools spanning 15,000 square meters, in an attempt to complete the drying and rehabilitation activities by not later than the end of 2012.

2. The Ramat Hovav Industrial Council will submit a detailed plan and timetable for drying and rehabilitating the vaporization pools site to the Ministry of the Environment for approval by December 31, 2004.

(c) Treatment of air pollution

The Ministry of the Environment will formulate and operate a plan to prevent exceptional emission of hazardous materials into the air from the Ramat Hovav industrial area.

As to the possible implications of the Government's decision on the activities of M-A Industries, see above.

A criminal complaint was filed against M-A Industries and one of its executives by the Man, Nature and Law Foundation. The complaint accuses M-A Industries that in several instances during 1999-2002, there were measurements at its Ramat Hovav plant of chimney emissions of materials at prohibited concentrations, which created strong air pollution.

M-A Industries does not admit to the charges in the complaint.

In the opinion of M-A Industries and its legal counsel, because of the early stage of the proceedings, it is not possible to estimate the outcome of the complaint and/or the resultant exposure. Therefore, the financial statements do not include a provision in respect thereof.

- b. In 1995, a claim was filed against a subsidiary of M-A Industries and several other defendants, totaling approximately NIS 137.5 million, by a group that had acquired the rights of two banks which declared bankruptcy. The subsidiary is being sued as the guarantor of debts of agricultural cooperatives that were its former shareholders.

The position of the subsidiary is that it was removed from the guarantee agreement under the terms of a subsequent agreement between the bank, the previous shareholders and a subsidiary of the former shareholders. The subsidiary's financial statements include a provision of NIS 8.6 million, based on the possibility of a compromise agreement with the plaintiffs. In the estimation of the subsidiary, based on the opinion of its legal counsel, the provision recorded is sufficient to cover any possible loss from this claim.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

- A. Contingent liabilities (cont'd)
7. M-A Industries and its investees (cont'd)
- c. Administrative proceedings, civil actions and other monetary claims of approximately NIS 209 million have been filed against a subsidiary of M-A Industries. Based on the opinion of its legal counsel, the subsidiary's management estimates that the chances of the subsidiary's success in the proceedings and its defense against the above claims and demands are high. The subsidiary believes that the provisions recorded in its financial statements are adequate to cover any possible damage which may result, if any, from these claims.
- d. On the matter of undertaking in securitization of transactions, and on the matter of compliance with financial covenants, see Note 3C(2).

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8. The other shareholders ("the plaintiffs") in Herods, a proportionately consolidated company of Sheraton Moriah (Israel) Ltd., a subsidiary of Koor, filed a "motion for approval of a claim as a derivative action" with the Tel Aviv District Court against Sheraton and a subsidiary. The derivative action for which they are seeking approval is for the cancellation of the management agreement between Herods and a subsidiary, as part of the arbitration process to which the claim has been referred. The claim itself deals with the plaintiffs' arguments regarding breaches in the management and image promotion agreements.

As a result of negotiations conducted between the parties, a compromise agreement was signed on February 26, 2005, pursuant to which the motion for approval of the derivative claim will be dismissed, and the proceedings of the derivative claim will be stricken. The compromise agreement is subject to the approval of the board of directors of the parties. After such approval is given, a final binding agreement will be signed and the parties will appeal to stay the proceedings.

9. In addition, a number of claims have been filed against certain investees concerning various matters arising in the normal course of business, including litigation with tax, customs and VAT authorities, which are in various legal proceedings. In the estimation of the managements of these companies, based on the opinions of their legal counsel, the provisions for these claims included in their financial statements, are adequate in light of the circumstances.
10. On conditions relating to an investment grant - see Note 10A(2).
11. In Israel, the Stamp Duty on Documents Law, 1961 ("the Law") is applicable to various documents at different rates, depending on the kind of document and the amount stipulated therein, or not stipulated therein. In June 2003, the wording of Section 15.A of the Law was amended, prescribing who is obligated for the stamping of documents. Since June 2003, the Israeli tax authorities have intensified the enforcement of the Law. The amendment to the Law and the enforcement activities of the tax authorities were brought before the Supreme Court for a hearing, on which a ruling has not yet been issued. Moreover, according to the legislative trends, the Stamp duty tax is expected to be gradually eliminated, until it is fully cancelled in 2008.

Certain investee companies received a request from Tax Authorities to produce documents.

In the estimation of the managements of the Company and the investees, based on the opinions of their legal counsel, the Companies are not expected to have material exposure in respect of any demand related to the Stamps Duty Law.

12. On the indemnity granted to Claridge as advisor - see Note 25C(2).
13. In connection with the indemnification of the appraiser who conducted a valuation for ECI, see Note 3A(1).

Notes to the Financial Statements

Note 18 - Contingent Liabilities and Commitments (cont'd)

A. Contingent liabilities (cont'd)

14. The liabilities of directors and officers in the Company and investees are insured by leading insurance companies in Directors and Officers Insurance (D&O), subject to the terms of the insurance policy.

Additionally, in accordance with a resolution of the general meeting of the Company's shareholders, the Company resolved to indemnify the directors and officers for various events that are not covered by the insurance, at a monetary amount exceeding the insured amounts, all as provided in the said resolution.

15. In connection with the indemnification of the appraiser who conducted a valuation for Tadiran Communications Ltd, see note 3H(1).

B. Commitments

1. Several companies in the Group have research and development contracts with the Government of Israel. Under these contracts, the companies are required to pay royalties to the Government of Israel if they generate income from such research (at rates of 2% - 5% of sales proceeds from products resulting from the research and development), in amounts not exceeding 100% - 150% of the amounts of the grants, linked to the dollar, received by the companies as participation in the research and development projects.

Royalty expenses paid to the Government of Israel in respect of these research and development contracts, are as follows:
In the year ended December 31, 2004 - NIS 29,758 thousand.
In the year ended December 31, 2003 - NIS 22,902 thousand. In the year ended December 31, 2002 - NIS 24,662 thousand.

2. Certain subsidiaries undertook to pay royalties at the rate of 3% per year in respect of the incremental export sales, up to the amount financed by the Fund for the Encouragement of Marketing Abroad. Such amounts are linked to the exchange rate of the dollar.
3. Commitments for the purchase of fixed assets: December 31, 2004 - NIS 22 million; December 31, 2003 - NIS 50 million.
4. Certain companies in the Group lease and rent industrial and office premises under long-term contracts. The lease contracts are non-cancelable and in most cases include renewal options. The expenses of these companies were NIS 43

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million in 2004, NIS 50 million in 2003 and NIS 60 million in 2002.

Future minimum payments under the operating leases and rental fees for the years subsequent to balance sheet date, are as follows:

| | December 31 2004 |
|---------------------------|-----------------------------------|
| | ----- (NIS thousands) ----- |
| First year | 41,960 |
| Second year | 34,044 |
| Third year | 21,514 |
| Fourth year | 8,748 |
| Fifth year and thereafter | 26,961 |
| | ----- 133,227 ===== |

5. Koor Corporate Venture Capital's commitment for additional investments in a venture capital fund, as at the signing date of the financial statements is approximately 5 million dollars.
6. A subsidiary of M-A Industries has agreements regarding long-term supply contracts with a multinational company in the amount of 17 million dollar per year for a period of five years (2001-2006).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 19 - Convertible Securities of Investee Companies

Option warrants to employees:

Certain investees issued options to their employees until 2004 inclusive. Employee entitlement to such options is usually accrued over a number of years from their date of issue, subject to continued employment. The exercise term of the options varies according to the terms of the different plans.

Convertible debentures and options

See Note 15B.

At each reporting period, Koor reviews the probability that the convertible securities will be exercised. If a loss, as a result of dilution, following the convertible securities exercise, is expected, the Company records the loss.

Note 20 - Share Capital and Stock Options

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A. Share capital is composed as follows:

| | December 31, 2004 | | December 31 |
|---|-------------------|------------------------|-------------|
| | Authorized | Issued and Outstanding | Authorized |
| Number of shares: | | | |
| Ordinary shares, par value of NIS 0.001 (1) (3) (5) | 83,932,757 | 16,033,213 | 83,932,757 |
| Deferred shares, par value of NIS 0.001 (2) (4) | 15,792,243 | 15,156,533 | 15,792,243 |
| Amount in nominal NIS: | | | |
| Ordinary shares, par value of NIS 0.001 | 83,933 | 16,033 | 83,933 |
| Deferred shares, par value of NIS 0.001 | 15,792 | 15,157 | 15,792 |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 20 - Share Capital and Stock Options

A. Share capital is composed as follows:

- (1) These shares are listed on the Tel Aviv Stock Exchange (TASE). On December 31, 2004, the share price on the TASE was NIS 224.90.

The ADS, (American Depository Shares) each of which represents 0.2 ordinary shares, par value of NIS 0.001 (hereinafter - Ordinary Shares), are traded on the New York Stock Exchange (NYSE). The ADS price on the NYSE on December 31, 2004 was 10.56 dollars.

- (2) The holders of the deferred shares are entitled to recovery of paid up capital upon liquidation in its nominal amount, after payment of the nominal amount to the holders of the Ordinary Shares. The holders of the deferred shares do not have voting rights, and they are not entitled to participate in a dividend distribution of any kind.

- (3) On the balance sheet date, subsidiaries hold 15,799 Ordinary Shares.

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- (4) A subsidiary of Koor - Koor Trusts (1995) Ltd. (in voluntary liquidation) had held 624,577 deferred shares of Koor, and in anticipation of its final liquidation, sold them to Koor Investments Ltd. (a subsidiary of Koor) in 2004.
- (5) During 2004, options in the employee stock option plans (See Note 20C) were exercised for 83,025 ordinary shares.

B. Buy-back of Company shares

On April 7, 2000, Koor's Board of Directors resolved to approve a framework of 50 million dollars for buying back ordinary shares of Koor.

In the framework, which was fully utilized in 2000, 538,592 ordinary shares were purchased (approximately 3.4% of the ordinary share capital), at a cost of approximately NIS 219 million. This amount is deducted from the shareholders' equity of the Company.

On December 31, 2001, the Company purchased 154,637 of its ordinary shares from a subsidiary at the market price. The transaction was treated according to the Israeli Securities Regulations (Financial Statement Presentation of Transactions between a Corporation and its Controlling Shareholders), 1996.

On May 27, 2003, a foreign institutional investor (hereinafter - "the Buyer") purchased 500,000 of the aforementioned Company's shares. The Purchaser declared that the sale was effected without his requesting or receiving any information from the Company, and undertook not to trade the shares to be purchased within a specified period.

The sale was effected on that day in an off-market transaction, at the market price, for total consideration of NIS 43 million.

The Company holds a total of 193,229 of its shares. The amount deducted from shareholders' equity at the balance sheet date in respect of the shares held by the Company and subsidiaries is NIS 80,321 thousand.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 20 - Share Capital and Stock Options (cont'd)

C. Stock options to senior employees

1. 1997 plan:

In 1997, 188,968 stock options were allotted under this plan.

On March 22, 2000, Koor's Board of Directors resolved to amend the plan so that for an employee who resigned and who holds stock options that vested before his resignation, their exercise period would be until the end of the five years from

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the inception date of the plan (hereinafter - "Amendment of the exercise period for employees who resign").

On August 6, 2000, Koor's Board of Directors resolved that for Company employees who are not related parties in the Company and who did not resign before the end of 2000, the exercise period of each stock option would be extended to the end of 5 years from the vesting date (hereinafter - "Amendment of extension of the exercise period").

On November 15, 2001, Koor's Board of Directors resolved that for Company employees on the date of resolution and who are not related parties in the Company the exercise price of their stock options would be amended to NIS 101.38 per share. The Board of Directors also resolved that the technical method of exercise would be the "Bonus Component Method" (see below, in sub-section 2).

On June 5, 2003, the Company's Board of Directors resolved to extend the exercise period of the options of Koor Group employees on the date of the resolution, to December 31, 2010.

| Balance of stock option not exercised | Exercise price | Exercise date |
|---|-------------------|------------------|
| ----- | ----- | ----- |
| | NIS | |
| | ----- | |
| 2,519 | 101.38 | 05/2005 |
| 3,000 | 101.38 | 12/2010 |
| ----- | | |
| 5,519 | | |
| ----- | | |

2. 1998 plan:

On August 30, 1998, an extraordinary general meeting of the shareholders of the Company approved a private placement of 400,000 stock options, free of charge, to Company employees. The options are exercisable for up to 400,000 ordinary shares of a par value of NIS 0.001 each (hereinafter - "the Plan").

Under the terms of the Plan, each stock option is theoretically exercisable for one share, subject to adjustments. However, in practice, offerees who exercise the options will not be allotted the full quantity of shares underlying each option, but only shares which reflect the amount of the financial benefit inherent in their option, computed on the date of exercise. Accordingly, the exercise price of each stock option is intended only for computation of the benefit component (above and hereafter - "the Benefit Component Method").

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 20 - Share Capital and Stock Options (cont'd)

C. Stock options to senior employees (cont'd)

2. 1998 plan: (cont'd)

On March 22, 2000, the Board of Directors approved an amendment of extension of the exercise period for employees who resign, applicable to option holders under the Plan who are not related parties (see Note 20C(1)). The Board of Directors also resolved that for these option holders, the exercise price would be adjusted in respect of distribution of a dividend for all the options, even if the vesting date preceded the entitlement to the dividend.

On October 6, 2000, the Board of Directors approved the amendment of extension of the exercise period for Company employees who are not related parties in the Company and who did not retire before the end of 2000.

On November 15, 2001, the Board of Directors approved the amendment of the exercise price to NIS 101.38 per share for Company employees on the resolution date who are not related parties in the Company.

On June 5, 2003, the Company's Board of Directors resolved to extend the exercise period of the options for Koor Group employees on the resolution date to December 31, 2010.

| Balance of stock option not exercised | Exercise price | Exercise date |
|---|-------------------|------------------|
| ----- | ----- | ----- |
| | NIS | |
| ----- | ----- | ----- |
| 670 | 101.38 | 07/2006 |
| 52,593 | 101.38 | 12/2010 |
| ----- | | |
| 53,263 | | |
| ----- | | |

3. 2000 Plan:

On August 6, 2000, the Board of Directors of the Company approved the 2000 stock options plan, which was previously approved on June 14, 2000 by the Executive Committee of the Board of Directors. The main points of the plan are these:

- 1) A total framework was approved for the allotment of 400,000 stock options theoretically exercisable for up to 400,000 ordinary shares of the Company, i.e. about 2.5% of the ordinary issued share capital of the Company.
- 2) The options will be exercised for shares in a quantity reflecting the amount of the financial benefit inherent in the options, according to the Benefit Component Method.
- 3) The exercise price of each stock option, pursuant to the amendment by the Board of Directors of the

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Company on November 15, 2001, will be NIS 101.38 per share.

- 4) The options are designated for Company employees who are not related parties in the Company and will not become related parties in the Company as a result of allotment of the stock options.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 20 - Share Capital and Stock Options (cont'd)

C. Stock options to senior employees (cont'd)

3. 2000 Plan: (cont'd)

- 5) The stock options will vest in accordance with a division of the options into three batches, so that at the end of the first year from the record date (June 14, 2000) or from the date on which the employee started work in the Company (whichever is the later), one third of the quantity allotted will vest, and the remaining two thirds of the quantity will vest at the end of each of the two subsequent years. The exercise period of each vested option is 5 years from the vesting date.

- 6) On October 5, 2000, the total quantity of 400,000 stock options was allotted to a trustee.

- 7) On June 5, 2003, the Company's Board of Directors resolved to extend the exercise period of the options of Koor Group employees on the date of the resolution to December 31, 2010.

| Balance of stock option not exercised | Exercise price | Exercise date |
|---|-------------------|------------------|
| ----- | ----- | ----- |
| | NIS | |
| ----- | ----- | |
| 1,734 | 101.38 | 6/2007 |
| 30,000 | 101.38 | 12/2010 |
| ----- | | |
| 31,734 | | |
| ----- | | |

4. 2003 Plan:

On July 27 2003, a general meeting of shareholders approved Stock Option Plan 2003, which had been approved previously by the Audit Committee of the Company's Board of Directors and by the Board of Directors, on May 25, 2003 and June 5, 2003, respectively. The key points of the Plan are:

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- 1) A total framework was approved for the allotment of 1,200,000 stock options, theoretically exercisable for up to 1,200,000 ordinary shares of the Company, i.e. about 6.8% of the ordinary shares (fully diluted) of the Company.
- 2) The options allotted to the trustee will be exercised for shares in a quantity reflecting the amount of the financial benefit inherent in the options, according to the Benefit Component Method.
- 3) The exercise price of every option will be NIS 96, linked to the CPI, unless the Company decides to prescribe a higher exercise price for options that will be allotted on dates subsequent to the approval date of the plan.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 20 - Share Capital and Stock Options (cont'd)

- C. Stock options to senior employees (cont'd)
4. 2003 Plan: (cont'd)
 - 4) The options are designated for Company employees who are not related parties in the Company and will not become related parties in the Company as a result of allotment of the stock options. In any event, the total number of offerees under Plan 2003 will not exceed 35 offerees, including the Company's directors and the CEO.
 - 5) The right of every offeree to exercise the options for shares will vest in six stages during the three-year period from the record date, whereby at the end of every calendar half-year, one-sixth of the number of options allotted to the trustee on his behalf will vest.
 - 6) Options not exercised by December 31, 2010 will expire.
 - 7) The Plan will be taxed under the Capital Gains Track, under the provisions of Section 102 of the Income Tax Ordinance and the regulations promulgated hereunder. Any tax to be imposed in respect of the exercise of the options will be borne solely by the offerees. And on the other hand, the Company will be unable to claim any tax deduction for the expense.
 - 8) Also approved within the framework of the approval of Plan 2003 was the granting of 350,000 options out

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of the total number, to seven directors (except for two directors who are controlling shareholders in the Company, directly or indirectly), divided equally, as well as 175,000 options to the Company's CEO. The balance of the options is intended for other employees and officers of the Koor Group.

- 9) The balance of options remaining as at December 31, 2004 is 939,450 options.

| | Balance of stock option not exercised | | |
|-------------------------------------|---|-----------|-----------|
| | ----- | | |
| | | | 856,450 |
| | | | 33,000 |
| | | | 50,000 |
| | | | ----- |
| | | | 939,450 |
| | | | ===== |
| Changes in the options during 2004: | | | |
| | 1997 Plan | 1998 Plan | 2000 Plan |
| | ----- | ----- | ----- |
| Balance as at beginning of year | 26,039 | 65,926 | 61,667 |
| Granted | - | - | - |
| Exercised | (20,520) | (12,663) | (29,933) |
| | ----- | ----- | ----- |
| Balance as at end of year | 5,519 | 53,263 | 31,734 |
| | ===== | ===== | ===== |

* Because of the "Benefit Component Method", a total of 83,025 ordinary shares of

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 21 - Financial Instruments and Linkage Terms of Monetary Balances

A. General:

The Company and certain subsidiaries have entered into forward transactions and option contracts, in order to hedge assets and liabilities denominated in foreign currency and in order to reduce the overall exposure of commitments for the purchase of raw materials and the sale of goods, in currencies other than the function currency. Those subsidiaries neither hold nor issue financial instruments for

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trading purposes.

- B. Details of the open foreign exchange transactions made to hedge the company's and subsidiaries' assets and liabilities in foreign currency as at December 31, 2004:

| | Forward Transaction | Call options | |
|--------------------------------------|------------------------|-----------------|------|
| | | | |
| | NIS thousands | | |
| | | | |
| Purchase of Dollars in exchange for: | | | |
| NIS | 25,848 | 124,932 | 33 |
| European currencies | 53,850 | 1,185,992 | 14 |
| Brazilian Real | 15,078 | 43,080 | 4 |
| Others | 45,234 | 99,515 | 17 |
| | 140,010 | 1,453,519 | 69 |
| | 140,010 | 1,453,519 | 69 |
| Sale of Dollars in exchange for: | | | |
| NIS | 17,232 | 142,164 | 19 |
| European currencies | 28,433 | 189,983 | 1,33 |
| Brazilian Real | - | - | |
| Others | - | 178,351 | 9 |
| | 45,665 | 510,498 | 1,62 |
| | 45,665 | 510,498 | 1,62 |

- C. The Company entered into an interest rate swap (IRS) in the amount of 50 million dollars, in order to reduce its exposure to fluctuations in interest rates. In the transaction, variable interest was exchanged for fixed interest. Additionally, the Company executed hedges on its CPI-linked loans and acquired a CPI-dollar forward contract in the amount of NIS 170 million.

- D. Fair value of financial instruments:

Condensed data of monetary assets and liabilities, whose fair value as at December 31, 2004, based on their market value, is different from those presented in the financial statements, is as follows:

| | Carrying amount | Fair value |
|---------------------------|--------------------|---------------|
| | | |
| | NIS millions | |
| | | |
| Investments in affiliates | 1,275 | 1,754 |
| | 1,275 | 1,754 |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 21 - Financial Instruments and Linkage Terms of Monetary Balances (cont'd)

D. Fair value of financial instruments: (cont'd)

The carrying amounts of cash and cash equivalents, short-term investment, trade receivables, other accounts receivable, credits from banks and others, trade payables and other accounts payable, debentures and convertible debentures derivatives and other financial instruments is approximate or similar to at their fair value.

E. Credit risk of trade receivables:

Condensed data of credit risk of trade receivables as at December 31, 2004:

Receivables insured by credit card companies
 Receivables insured by foreign trade risk insurance
 Receivables - Government authorities and Bezeq
 Other receivables, including checks and credit card companies

Total, including non-current receivables

In Management's opinion, the financial statements include suitable provisions in respect of exposure to doubtful debts.

The exposure to credit risks relating to trade receivables is limited, due to the relatively large number of customers.

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Koor Industries Lt

Notes to the Financial Statements

Note 21 - Financial Instruments and Linkage Terms of Monetary Balances (cont'd)

F. Linkage terms of monetary balances:

(1) Consolidated

| | December 31, 2004 | |
|---|-------------------------|------|
| In foreign currency or linked thereto | Linked to the CPI | Unli |
| | | |

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NIS thousands

| | | | |
|---|-----------|-----------|--------|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | 512,511 | - | 104, |
| Short-term deposits and investments | 91,312 | 101,785 | 223, |
| Trade receivables | 1,968,387 | 13,546 | 191, |
| Other accounts receivable | 177,180 | 29,131 | 102, |
| Investments and other long-term receivables | 236,974 | 58,562 | 10, |
| | ----- | ----- | ----- |
| | 2,986,364 | 203,024 | 632, |
| | ===== | ===== | ===== |
| Liabilities | | | |
| Current liabilities: | | | |
| Credits from banks and others (not including current maturities of long-term liabilities) | | | |
| | 753,900 | - | 331, |
| Trade payables | 1,371,290 | - | 296, |
| Other accounts payable | 840,327 | 130,893 | 375, |
| Long-term loans and debentures (including current maturities) | 1,793,566 | 1,368,683 | 643, |
| | ----- | ----- | ----- |
| | 4,759,083 | 1,499,576 | 1,645, |
| | ===== | ===== | ===== |

(Table Continued)

Koor Industries Lt

Notes to the Financial Statements

Note 21 - Financial Instruments and Linkage Terms of Monetary Balances (cont'd)

F. Linkage terms of monetary balances:

(1) Consolidated

December 31, 2003

| | In foreign currency or linked thereto | Linked to the CPI | Un |
|-------------------------------------|---|-------------------------|-------|
| | ----- | ----- | ----- |
| | NIS thousands | | |
| | ----- | ----- | ----- |
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | 491,889 | - | 10 |
| Short-term deposits and investments | 87,534 | 150,495 | 12 |
| Trade receivables | 1,794,141 | 11,945 | 24 |
| Other accounts receivable | 139,050 | 25,770 | 8 |
| Investments and other | | | |

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| | | | |
|---|-----------|-----------|-------|
| long-term receivables | 217,970 | 59,565 | |
| | ----- | ----- | ----- |
| | 2,730,584 | 247,775 | 56 |
| | ===== | ===== | ===== |
| Liabilities | | | |
| Current liabilities: | | | |
| Credits from banks and others (not including current maturities of long-term liabilities) | 647,098 | - | 26 |
| Trade payables | 1,030,693 | - | 31 |
| Other accounts payable | 642,646 | 171,487 | 40 |
| Long-term loans and debentures (including current maturities) | 2,488,222 | 1,627,955 | |
| | ----- | ----- | ----- |
| | 4,808,659 | 1,799,442 | 99 |
| | ===== | ===== | ===== |

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Note 21 - Financial Instruments and Linkage Terms of Monetary Balances (cont'd)

F. Linkage terms of monetary balances (cont'd):

(2) Company

| | December 31, 2004 | | |
|---|---|-------------------------|--------|
| | In foreign currency or linked thereto | Linked to the CPI | Unli |
| | ----- | ----- | ----- |
| | NIS thousands | | |
| | ----- | ----- | ----- |
| Assets | | | |
| Cash and cash equivalents | 2,547 | - | 27, |
| Short-term deposits and investments | 51,909 | 80,235 | 166, |
| Other receivables | 1,121 | - | 14, |
| Short term loans to investee companies | - | 12,548 | |
| Other investments and receivables | 107 | 32,028 | |
| Investments and other long-term receivables: | | | |
| Investee companies (including current maturities of loans) | 43,364 | 50,711 | 1,255, |
| | ----- | ----- | ----- |
| | 99,048 | 175,522 | 1,463, |
| | ===== | ===== | ===== |
| Liabilities | | | |
| Current liabilities: | | | |
| Credits from banks and others (not including current maturities of long-term liabilities) | 166,427 | - | 15, |
| Trade payables | 43 | - | |
| Other accounts payable | 18,864 | 17,143 | 27, |
| Long-term liabilities (including current maturities of loans) | 102,829 | 1,296,014 | 645, |

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| | | |
|---------|-----------|-------|
| ----- | ----- | ----- |
| 288,163 | 1,313,157 | 687, |
| ===== | ===== | ===== |

(Table Continued)

Note 21 - Financial Instruments and Linkage Terms of Monetary Balances (cont'd)

F. Linkage terms of monetary balances (cont'd):

(2) Company

| | December 31, 2003 | | |
|---|---|-------------------------|-------|
| | In foreign currency or linked thereto | Linked to the CPI | Unl |
| | ----- | ----- | ----- |
| | NIS thousands | | |
| | ----- | ----- | ----- |
| Assets | | | |
| Cash and cash equivalents | 4,066 | - | 5 |
| Short-term deposits and investments | 57,202 | 144,133 | 109 |
| Other receivables | 11,074 | - | 23 |
| Short term loans to investee companies | - | 13,951 | |
| Other investments and receivables | 109 | 32,028 | |
| Investments and other long-term receivables: Investee companies (including current maturities of loans) | 12,753 | 53,449 | 1,319 |
| | ----- | ----- | ----- |
| | 85,204 | 243,561 | 1,458 |
| | ===== | ===== | ===== |
| Liabilities | | | |
| Current liabilities: | | | |
| Credits from banks and others (not including current maturities of long-term liabilities) | 169,704 | - | |
| Trade payables | 85 | - | |
| Other accounts payable | 4,408 | 12,057 | 26 |
| Long-term liabilities (including current maturities of loans) | 373,268 | 1,648,201 | 8 |
| | ----- | ----- | ----- |
| | 547,465 | 1,660,258 | 35 |
| | ===== | ===== | ===== |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 22 - Liens and Guarantees

- A. In order to secure some liabilities, certain subsidiaries have mortgaged their real estate and have placed fixed charges on plant, equipment and bank deposits, as well as floating charges on all of their assets. They also pledged a portion of their shares in investee companies.

Regarding the pledge in respect to an investment grant - see Note 10A(2).

- B. The balances of secured liabilities are as follows:

Credit from banks

Loans from banks and others and debentures (including current maturities), see Note 15, and also C and D, E, below

- C. The Company financed the acquisition of Tadiran Communications through a NIS 637 million loan from a bank in Israel, in consideration for a lien on the acquired shares in favor of the bank.

- D. The convertible debentures, which were issued by M-A Industries, are guaranteed by first level fixed symbolic lien with a deposit to the amount of NIS 1 for the Trustee of the convertible debenture holders (see Note 15B).

- E. Guarantees to banks and others for loans and for assuring credit lines and other guarantees in favor of: Consolidated Company December 31 December 31 2004 2003 2004 2003 NIS thousands NIS thousands

| Consolidated | |
|--------------|------|
| December 31 | |
| 2004 | 2003 |
| | |

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| | NIS thousands | |
|--------------|---------------|--------|
| | ----- | |
| Subsidiaries | - | - |
| Affiliates | - | 340 |
| Others | 78,473 | 67,723 |
| | ----- | ----- |
| | 78,473 | 68,063 |

- 1) In certain cases when advances from customers are received, a subsidiary provides its customers with bank guarantees to secure the advances. Guarantees in excess of the amount of advance payments stated as liabilities in the balance sheet, amounted to NIS 265,786 thousand, and NIS 302,782 thousand, as at the years ending December 31, 2004 and 2003, respectively.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 22 - Liens and Guarantees (cont'd)

- E. Guarantees to banks and others for loans and for assuring credit lines and other guarantees: (cont'd)
- 2) In connection with the Bezeq agreement to transfer ownership of public switching, Bezeq received from Koor a guarantee in the amount of NIS 125 million.
- 3) A subsidiary has a guarantee for a major customer to pay any amounts up to 40 million dollars in relation to an indemnification that the subsidiary signed for the same customer, on account of breaches of contracts to Bezeq, the Israeli Communication Company. The guarantee is at least till 2015.
- 4) A subsidiary and its subsidiary in Brazil are, under certain conditions, a guarantor to financial institutions for credit that its customers received in relation to commercial sales of the consolidated company to those customers. The balance of guarantees, as at the balance sheet date, was approximately 98 million dollars. (December 31, 2003 approximately 85 million dollars).
- 5) There are also guarantees, in an unlimited amount, to ensure due performance of work and customer agreements, product warranty, advance payments received and guarantees on behalf of liabilities to customs and excise authorities.
- 6) As a condition for the continued availability, see Notes 3 and 18.

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Note 23 - Data concerning Items in Statements of Operations

A. Revenues from sales and services - net (1) (2):

Consolidated:

| | Year ended | |
|--|------------|-------|
| | ----- | |
| | 2004 | ----- |
| | | NIS t |
| | | ----- |
| Local: | | |
| Industrial operations | 874,861 | |
| Trading operations | 505,293 | |
| Abroad: | | |
| Industrial operations - export and international operations | 6,947,748 | |
| Trading operations | 900,771 | |
| | ----- | |
| | 9,228,673 | |
| | ===== | |
| (1) Not including agency sales | 425,224 | |
| | ===== | |
| (2) Revenues and expenses relating to work performed under long-term contracts: | | |
| Revenues | 880,959 | |
| Costs | (709,899) | |
| | ----- | |
| | 171,060 | |
| | ===== | |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 23 - Data to Items in Statements of Operations (cont'd)

B. Cost of sales and services - consolidated:

| | Year e | |
|------------------------|--------|-------|
| | ----- | |
| | 2004 | ----- |
| | | N |
| | | ----- |
| Industrial operations: | | |

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| | |
|---|-----------|
| Materials | 3,817,178 |
| Labor | 750,457 |
| Subcontracted work | 41,640 |
| Depreciation and amortization | 177,535 |
| Research and development expenses, net (*) | 212,115 |
| Other manufacturing expenses | 645,915 |
| | ----- |
| | 5,644,840 |
| Less - expenses charged to cost of fixed assets | 6,510 |
| | ----- |
| | 5,638,330 |
| (Decrease) increase in inventory of goods and work in process | (39,305) |
| | ----- |
| | 5,599,025 |
| Increase in inventory of finished goods | (176,611) |
| | ----- |
| | 5,422,414 |
| | ----- |
| Trading operations: | |
| Merchandise | 508,189 |
| Labor | 55,394 |
| Depreciation | 26,155 |
| Others | 275,527 |
| | ----- |
| | 865,265 |
| | ----- |
| | 6,287,679 |
| | ===== |
| (*) Net of grants and participations that were received and royalties that were paid, net | 14,220 |
| | ===== |

C. Selling and marketing expenses - consolidated:

| | Year e |
|-------------------------------|-----------|
| | ----- |
| | 2004 |
| | ----- |
| | N |
| | ----- |
| Salaries | 338,629 |
| Commissions | 150,556 |
| Advertising expenses | 40,993 |
| Depreciation and amortization | 113,638 |
| Other | 528,388 |
| | ----- |
| | 1,172,204 |
| | ===== |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 23 - Data to Items in Statements of Operations (cont'd)

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D. General and administrative expenses:

| | Consolidated | | | Year ended December 31 2004 |
|-------------------------------|------------------------|---------|---------|--------------------------------|
| | Year ended December 31 | | | |
| | 2004 | 2003 | 2002 | |
| | NIS thousands | | | |
| Salaries | 229,180 | 217,525 | 234,098 | 22,399 |
| Bad and doubtful debts | 54,959 | 36,903 | 33,933 | - |
| Depreciation and amortization | 24,171 | 24,070 | 30,797 | 1,262 |
| Other | 217,694 | 182,246 | 190,541 | 22,987 |
| | 526,004 | 460,744 | 489,369 | 46,648 |

E. Financing expenses (income), net:

| | Consolidated | | | Year ended December 31 2004 |
|--|------------------------|----------|----------|--------------------------------|
| | Year ended December 31 | | | |
| | 2004 | 2003 | 2002 | |
| | NIS thousands | | | |
| In respect of convertible debentures | 18,942 | 15,319 | 17,825 | - |
| In respect of debentures | (480) | - | 651 | - |
| In respect of long-term loans | 200,509 | 141,078 | 240,713 | 111,396 |
| In respect of short-term loans and credit | 79,521 | 182,868 | 168,478 | 10,756 |
| Amortization of capital raising expenses | 4,334 | 2,106 | 2,250 | - |
| Losses (gains) from marketable securities, net | (24,238) | (72,681) | 44,112 | (18,568) |
| Interest capitalized to fixed assets and work in process | (1,544) | (371) | (14,860) | - |
| Expenses (income) from | | | | |

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| | | | | |
|---|---------|----------|----------|---------|
| balance with investees, net | - | - | - | 1,430 |
| Expenses (income) from deposits and others, net | (5,682) | (40,119) | (50,732) | 5,792 |
| | ----- | ----- | ----- | ----- |
| | 271,362 | 228,200 | 408,437 | 110,806 |
| | ===== | ===== | ===== | ===== |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 23 - Data to Items in Statements of Operations (cont'd)

F. Other income (expenses), net

1. Consolidated

| | Year e |
|---|-----------|
| | ----- |
| | 2004 |
| | ----- |
| | N |
| | ----- |
| Sale of investments and activities in investees (including changes in rates of holding) | 223,095 |
| Expenses relating to the termination, sale of activities and sale and write down of assets, net | (73,078) |
| Supplemental severance pay and pensions | (54,010) |
| Management services - affiliated companies | 2,682 |
| Securitization costs (see Note 3C(2)) | (27,783) |
| Compensation for damages | - |
| Amortization of goodwill | (136,437) |
| Miscellaneous, net | (13,228) |
| | ----- |
| | (78,759) |
| | ===== |

2. Company

| | Year e |
|--|--------|
| | ----- |
| | 2004 |
| | ----- |

| | |
|--|---------|
| Profit (loss) from sale of investments in investee companies | 212,024 |
| Net changes in value of long-term assets | - |
| Rental income, net* | 8,135 |
| Capital gain from sale of fixed assets | - |
| Dividend | 4,701 |
| Miscellaneous, net | 10,099 |
| | ----- |
| | 234,959 |
| | ===== |
| * Depreciation included in the item | 760 |
| | ===== |

** Reclassified

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 23 - Data to Items in Statements of Operations (cont'd)

G. Equity of the Koor Group in the operating results of affiliates, net

1. Consolidated

| | Year e |
|--|--------|
| | ----- |
| | 2004 |
| | ----- |
| | ----- |
| Affiliated companies, net (1) | 3,406 |
| Amortization of goodwill * | 24,281 |
| | ----- |
| | 27,687 |
| | ===== |
| (1) Including loss from a discontinued operation in an affiliate | - |
| | ===== |

* In 2004 - net of in process research and development in the amount of NIS 20 million affiliated company - See Note 3H.

2. Company

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| | Year e | |
|---|----------|----|
| | ----- | |
| | 2004 | |
| | ----- | |
| | ----- | N |
| Equity of Koor in operating results for the year (1) | 57,192 | |
| Amortization of goodwill | (30,992) | |
| | ----- | -- |
| | 26,200 | |
| | ===== | == |
| Dividend received/proposed | 74,201 | |
| | ----- | -- |
| | ===== | == |
| (1) Including loss from a discontinued operation in an affiliate | - | |
| | ----- | -- |
| | ===== | == |

| | Year e | |
|--|----------|----|
| | ----- | |
| | 2004 | |
| | ----- | |
| | ----- | N |
| Subsidiaries | 122,172 | |
| Proportionately consolidated companies | (61,114) | |
| Affiliates | (34,858) | |
| | ----- | -- |
| | 26,200 | |
| | ===== | == |

* In 2004 - net of in process research and development in process in the amount of NIS 20 million with respect to purchase of affiliated company. - See Note 3H.

** Reclassified

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

 Note 23 - Supplementary Data to Items in Statements of Operations (cont'd)

I. Income (expenses) from investee companies and their participation in expenses - Company

Year ended December 31

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| | 2004 | | 2003 | |
|--|------------------------|----------------------|------------------------|----------------------|
| | Consolidated companies | Affiliated companies | Consolidated companies | Affiliated companies |
| | NIS thousands | | | |
| Income: | | | | |
| Management services | 22,334 | - | 25,006 | - |
| Administrative expenses -- Salary and other administrative expenses | 1,457 | - | 1,679 | - |
| Financing income (expenses), net | (1,430) | - | 2,828 | 5 |
| Rental income, net | - | - | - | - |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 24 - Business Segments

A. The Koor Group operates in the following business segments:

The Company's telecommunication activities are focused in two companies - Telrad Networks Ltd., which develops and markets telecom products and provides end-user solutions, and ECI Telecom Ltd., an affiliated company, that provides solutions for access networks (Inovia) and transmission systems and optical networks (Enavis, Lightscape).

The Company's agrochemical activities are carried out through M-A Industries considered a world's foremost manufacturer of generic crop protection solutions. M-A Industries produces a full range of products, including insecticides, fungicides and herbicides, as well as plant growth regulators. In addition, the M-A Industries is engaged in specialty aroma chemicals and other different kinds of chemicals.

Activities in the defense space are carried out mainly by the Elisra Electronics Industries Ltd. Group, a leader in the

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planning, development and manufacturing of solutions for electronic warfare and defense, wireless communication systems, command and control systems, pilot rescue systems and advanced communications systems.

Activities in venture capital investments space are carried out through the Koor Corporate Venture Capital partnership, which invests in high-tech companies and venture capital funds with high growth potential. Most of the investments are in the fields of communication and life sciences.

The Company's remaining business activities are in tourism, through Sheraton Moriah, which holds the Sheraton Hotel chain in Israel and Knafayim-Arkia (an affiliated company until the third quarter of 2004) which holds 40% of the EL-AL airline company which provides aviation and holiday services and leases aircrafts to other companies. Additional activities include international trade through several companies.

- B. Segment sales include products sold and services rendered to unrelated customers, which are not part of the group. Inter-industry segment sales are immaterial and are based primarily on prices determined in the ordinary course of business. Accordingly, these sales are not presented separately.

Segment operating earnings include all costs and expenses directly related to the relevant segment and charged on a proportionate basis, expenses that benefit more than one segment. Expenses and revenue presented in the statements of operations after operating earnings are not taken in account in the determination of operating earnings or loss. Identifiable assets and liabilities by industry segments are those that are used by Koor in its activities in each segment.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 24 - Business Segments (cont'd)

- C. Data regarding business segments of the Koor Group:

| Year ended December 31 | | | | |
|------------------------|-------|---------------|-------|-------|
| 2004 | | 2003 | | |
| NIS thousands | % | NIS thousands | % | NI |
| ----- | ----- | ----- | ----- | ----- |

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| | | | | |
|-------------------------------------|-----------|--------|-----------|--------|
| Revenues from sales and services: | | | | |
| Segments: | | | | |
| Telecommunication* | 615,057 | 6.66 | 796,059 | 10.35 |
| Defense electronics | 1,165,998 | 12.63 | 1,286,432 | 16.73 |
| Agro-chemicals and other chemicals | 6,895,238 | 74.72 | 5,191,913 | 67.51 |
| Others | 552,380 | 5.99 | 416,026 | 5.41 |
| Total segments | 9,228,673 | 100.00 | 7,690,430 | 100.00 |
| ===== | ===== | ===== | ===== | ===== |
| * Including sales to major customer | 586,114 | | 753,863 | |
| ===== | ===== | ===== | ===== | ===== |

Year ended December 31

| | 2004 | | 2003 | | |
|--|---------------|--------|---------------|--------|---------------|
| | NIS thousands | % | NIS thousands | % | NIS thousands |
| Pre-tax earnings (losses): | | | | | |
| Operating earnings (loss) according to segments: | | | | | |
| Telecommunication | (64,491) | (5.02) | 3,158 | 0.34 | |
| Defense electronics | 30,865 | 2.4 | (4,294) | (0.46) | |
| Agro-chemicals and other chemicals | 1,312,534 | 102.1 | 949,290 | 102.61 | |
| Venture capital investments | (1,457) | (0.11) | (1,445) | (0.16) | |
| Others | 8,030 | 0.63 | (21,536) | (2.33) | |
| Total segments | 1,285,481 | 100.00 | 925,173 | 100.00 | |
| ===== | ===== | ===== | ===== | ===== | ===== |
| Joint general expenses | (42,695) | | (28,888) | | |
| Total operating earnings | 1,242,786 | | 896,285 | | |
| Financing expenses, net | (271,362) | | (228,200) | | |
| Other income (expenses), net | (78,759) | | (219,721) | | |
| Transfer to statement of income of translation differences of autonomous investee in voluntary liquidation | - | | - | | |
| ===== | ===== | ===== | ===== | ===== | ===== |
| Pre-tax earnings (losses) | 892,665 | | 448,364 | | |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 24 - Business Segments (cont'd)

C. Data regarding business segments of the Koor Group: (cont'd)

The Koor Group's equity in the excess of losses over earnings of affiliates, net, is as follows:

| | Year ended December 31 | | | |
|-----------------------------|------------------------|----------|---------------|----------|
| | 2004 | | 2003 | |
| | NIS thousands | % | NIS thousands | % |
| Telecommunications | (15,919) | (57.5) | (101,795) | (89.43) |
| Defense electronics | - | - | (130) | (0.11) |
| Venture capital investments | (329) | (1.19) | (329) | (0.30) |
| Others | (11,439) | (41.31) | (11,569) | (10.16) |
| | (27,687) | (100.00) | (113,823) | (100.00) |

| | December 31 | | |
|------------------------------------|---------------|-------|-------|
| | 2004 | | |
| | NIS thousands | % | NIS t |
| Identifiable assets Segments: | | | |
| Telecommunications | 550,914 | 4.97 | |
| Defense electronics | 1,119,371 | 10.10 | |
| Agro-chemicals and other chemicals | 8,242,246 | 74.33 | |
| Venture capital investments | 175,818 | 1.58 | |
| Others | 1,000,295 | 9.02 | |

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| | | | |
|------------------|------------|--------|---|
| Total segments | 11,088,644 | 100.00 | 1 |
| Corporate assets | 683,762 | | |
| Affiliates** | 1,375,160 | | |
| | 13,147,566 | | 1 |

** Including an investment in ECI as at December 31, 2004 and 2003 in the amount of NIS 673 million and NIS 726 million respectively, which operates in the telecommunications segment and investment in Tadiran Communications Ltd. which operates in the defense electronics in the amount of NIS 602 million as at December 31, 2004.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 24 - Business Segments (cont'd)

C. Data regarding business segments of the Koor Group: (cont'd)

| | December 31 | | |
|------------------------------------|---------------|--------|-------|
| | 2004 | | |
| | NIS thousands | % | NIS t |
| Identifiable liabilities | | | |
| Segments: | | | |
| Telecommunications | 215,060 | 6.87 | |
| Defense electronics | 668,157 | 21.34 | |
| Agro-chemicals and other chemicals | 2,089,083 | 66.72 | |
| Venture capital investments | 24 | - | |
| Others | 158,607 | 5.07 | |
| Total segments | 3,130,931 | 100.00 | |
| Corporate liabilities | 49,515 | | |
| | 3,180,446 | | |
| Financing commitments | 4,725,771 | | |
| Others | 647,458 | | |
| | 8,553,675 | | |

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| | Year ended December 31 | | | | NI |
|------------------------------------|------------------------|--------|---------------|--------|----|
| | 2004 | | 2003 | | |
| | NIS thousands | % | NIS thousands | % | |
| Capital investments: | | | | | |
| Segments: | | | | | |
| Telecommunications | 21,015 | 2.39 | 7,173 | 2.25 | |
| Defense electronics | 21,408 | 2.44 | 28,210 | 8.85 | |
| Agro-chemicals and other chemicals | 816,287 | 92.9 | 277,195 | 86.94 | |
| Others | 19,991 | 2.27 | 6,262 | 1.96 | |
| Total segments | 878,701 | 100.00 | 318,840 | 100.00 | |
| Corporate assets | 423 | | 392 | | |
| | 879,124 | | 319,232 | | |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 24 - Business Segments (cont'd)

C. Data regarding business segments of the Koor Group: (cont'd)

| | Year ended December 31 | | | | NI |
|--------------------------------|------------------------|------|---------------|-------|----|
| | 2004 | | 2003 | | |
| | NIS thousands | % | NIS thousands | % | |
| Depreciation and amortization: | | | | | |
| Segments: | | | | | |
| Telecommunications | 31,863 | 6.89 | 44,696 | 10.17 | |
| Defense electronics | 35,721 | 7.72 | 39,297 | 8.94 | |

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| | | | | |
|--|---------|--------|---------|--------|
| Agro-chemicals and other chemicals | 364,995 | 78.91 | 318,492 | 72.47 |
| Others | 29,957 | 6.48 | 37,029 | 8.42 |
| Total segments | 462,536 | 100.00 | 439,514 | 100.00 |
| Corporate assets | 1,264 | | 13,050 | |
| | 463,800 | | 452,564 | |

D. Revenues from sales and services by geographic destinations according to customer location

| | Year end |
|--------------------|-----------|
| | 2004 |
| | NIS |
| North America | 1,542,409 |
| Europe | 3,150,853 |
| South America | 2,056,261 |
| Asia and Australia | 842,986 |
| Africa | 256,010 |
| Israel | 1,380,154 |
| | 9,228,673 |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 24 - Business Segments (cont'd)

E. Assets by geographic location of manufacturing operation

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Israel
South America
Europe
United States
Others

F. Capital investments in assets by geographic location

Israel
Brazil
United States
Others

Note 25 - Transactions and Balances with Interested Parties

- A. The following are details of interested parties in Koor resulting from their holdings of Koor's ordinary shares:
1. Claridge Group (Claridge).
 2. Anfield Ltd.
- B. On October 15, 2002 the Board of Directors of Bank Hapoalim B.M. decided, on the distribution of a dividend in kind of all its holdings in the Company. On November 27, 2002, the date of actual distribution, Bank Hapoalim B.M. ceased to be an interested party in the Company.

During the period when Bank Hapoalim B.M. was an interested party, Koor and its consolidated companies also made transactions with Bank Hapoalim. These transactions, which were mainly for receipt of banking services, were made in the normal course of business, and therefore, no separation is made with regard to the management and the recording of the transactions.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 25 - Transactions and Balances with Interested Parties (cont'd)

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- C. Benefits to interested parties - Company
 1. Directors (*)

| | 2004 | Year |
|---|------|------|
| Directors not employed by the Company: Annual compensation and participation in meetings: | | |
| Claridge Group | 116 | |
| Number of directors | 2 | |
| Poalim Assets (Shares) Ltd. | - | |
| Number of directors | - | |
| Other directors | 516 | |
| Number of directors | 8 | |

(*) Including directors who have been replaced during the year.

2. Consultancy services

| | 2004 | Year |
|--|-------|------|
| Claridge | 1,788 | |
| Poalim Capital Markets and Investment Ltd. | - | |

The Company has agreements with interested parties - Poalim Capital Markets and Investments Ltd. (Poalim) (at the time when Bank Hapoalim B.M. was an interested party) and Claridge for the receipt of consultancy services. These services include, inter alia, advice in respect of investment strategies, monetary policies, international activities, strategic partnerships and company structuring. The agreements include instructions regarding the indemnification of the consultants (Claridge/Poalim) in respect of claims connected to the consultancy, except for cases of gross negligence and/or intentional damage.

In consideration for the consultancy the Company has agreed

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to pay an annual sum which will not exceed 400,000 dollars to each of the consultants. The agreements are for the period of one year and are automatically renewable each year, unless one of the parties gives 60 days' prior notice of the termination of the agreement.

On the date on which Bank Hapoalim ceased to be an interested party in Koor, the agreement with Poalim expired.

3. See Note 18A(14) regarding insurance and indemnification of interested parties.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

 Note 26 - Earnings (Loss) Per Share

- A. Adjusted net earnings (loss) used in the computation of earnings per NIS 1 par value of the share capital:

| | | Year end |
|--|---------|----------|
| | 2004 | ----- |
| | | NIS |
| | ----- | ----- |
| Net earnings (loss) used in the computation of earnings (loss) per NIS 1 par value of shares | 144,990 | ===== |

- B. Weighted number of ordinary shares of NIS 0.001 used in the computation of net earnings (loss) per NIS 1 par value of the share capital:

| | | Number o |
|---|------------|----------|
| | 2004 | ----- |
| | | ----- |
| Total share capital used in the computation of 16,381,279 | 16,381,279 | ===== |

- C. To examine that the conversion or exercise of convertible securities is reasonable, the present value of these securities was computed according to a discount rate of 3.5% (December 31, 2003 - 4%, December 31, 2002 - 6%) for securities linked to the CPI.

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Note 27 - Events Subsequent to the Balance Sheet Date

1. In January 2005, M-A Industries, through a wholly-owned and controlled subsidiary, signed an agreement to acquire 49% of the shares and rights of Mabeno, a Dutch company serving as exclusive distributor of the agrochemical products of the Makhteshim-Agan Group in Benelux and Scandinavia. Under the terms of the agreement, the purchase will be effected in consideration for the allotment of the number of shares of M-A Industries equal to 2,940 thousand euro (about NIS 17 million), according to the share's market price on the transfer date. Additionally, M-A Industries received an option to increase its holdings in Mabeno to 55%.
2. In January 2005, a lawsuit and a motion to recognize it as a class action, were filed in a U.S. court against ECTel, directors and officers of ECTel and against ECI. In their lawsuit, the plaintiffs claim that, in the period between April 2001 and April 2003, ECTel violated provisions of the U.S. securities laws, and that directors and officers of ECTel breached their duty of faith in connection with the disclosure of its business results in its financial statements. The lawsuit was also directed against ECI, because control in ECTel during that period was held by ECI, and the plaintiffs claim that the acts and omissions of ECTel were directed by and carried out at ECI's initiative. The plaintiffs did not cite the amount they are claiming. Management of ECI is of the opinion that the plaintiffs' claims, as they relate to it, are baseless.
3. In February 2005, ECI entered into a preliminary agreement with ABN Amro Bank for the sale of the balance of long-term receivables for cash totalling 96 million dollars, as well as possible future consideration of 3.3 million dollars. The sale is subject to several conditions and approvals, including approval from the shareholders of ECI, and is expected to be approved in April 2005. The sale is expected to generate a gain to ECI of 11 million dollars (excluding the future consideration). The Company's share in the aforementioned gain will be NIS 15 million.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 27 - Events Subsequent to the Balance Sheet Date (cont'd)

4. On February 3, 2005, Koor sold 15.9 million shares of M-A Industries for NIS 374 million, at a gain of NIS 204 million, which will be charged in the Company's financial statements for the first quarter of 2005.

Within the framework of the sale, Koor undertook to not sell additional shares of M-A Industries for a nine-month period beginning from the date of the sale.

Following the sale of the shares by Koor in February 2005, as

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a result of which Koor's shareholding percentage in M-A Industries fell to 34.6% (29.5% on a fully diluted basis), the management of Koor reevaluated the issue of continuing to consolidate M-A Industries, beginning from the first quarter of 2005.

Based on an evaluation of the range of circumstances, as discussed in Note 3C(1), Koor decided that due to the combination of new circumstances created as a result of the aforementioned sale of its holdings, continuation of the consolidation of M-A Industries is not consistent with the economic substance. Therefore, beginning from the first quarter of 2005, the consolidation of M-A Industries in the financial statements of Koor will be discontinued, and the investment therein will be stated by the equity method.

5. On March 14, 2005, M-A Industries published a prospectus offering employees of M-A Industries and its subsidiaries up to 14,900 thousand stock options exercisable for up to 14,900 ordinary registered shares of par value NIS 1 of M-A Industries.
- Assuming all the options are exercised, the grantees will hold approximately 3.05% of M-A Industries issued and paid share capital. However, the grantees will not be issued the full number of shares underlying the options, but only the number of shares reflecting the monetary benefit implicit in the options.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements

A. Differences between Israel GAAP and US GAAP

Koor's consolidated financial statements conform with Israeli generally accepted accounting principles ("Israeli GAAP"), which differ in certain respects from those generally accepted in the United States of America ("US GAAP") as described below:

1. Effect of inflation

In accordance with Israeli GAAP:

The Company, in accordance with Israeli GAAP, comprehensively includes the effect of price level changes in the accompanying financial statements, as described in Note 2B. According to such Israeli accounting principles, the Company has discontinued the adjustment of the financial statements as of January 1, 2004.

US GAAP does not provide for recognition of the effects of

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such price level changes. Such effects have not been included in a reconciliation to US GAAP.

2. Debt arrangement within the framework of an overall financial arrangement

In accordance with Israeli GAAP:

Koor reported an extraordinary gain in 1991 as a result of restructuring part of its debts.

In accordance with US GAAP:

In accordance with FAS No. 15 - "Accounting by Debtors and Creditors for Doubtful Debt Restructuring" future interest payments were deducted from the restructuring of an old debt. The recognition of non-realized earnings (which represents deferred interest) is affected by payments of interest over the period from the date of the restructuring of the debt up to its repayment date.

As at December 31, 2002, the entire balance of the deferred interest was fully amortized.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

3. Deferred taxes
 - a) Measurement differences

In accordance with Israeli GAAP:

Deferred taxes should be recognized in respect of differences related to assets and liabilities that result from translation of the local currency into the functional currency using historical exchange rates and that result from (1) changes in exchange rates or (2) indexing for tax purposes.

In accordance with US GAAP:

According to paragraph 9(f) of FAS No. 109, deferred tax liabilities or assets are not provided for differences related to assets and liabilities that are remeasured from the local currency into the functional currency and that result from (1) changes in exchange rates or (2) indexing for tax purposes.

- b) Earnings from "Approved Enterprises"

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Under the Israeli Law for the Encouragement of Capital Investments, 1959, a 25% tax rate is generally applicable on the profits of an "approved enterprise" that received investment grants, usually during a period of seven years.

An "approved enterprise" which chooses the "alternative benefits" track is generally eligible for tax benefits during the benefit period (seven or ten years, depending on the geographical location of the approved enterprise) as follows: tax exemption on undistributed profits during a period of two to ten years depending on the geographical location of the approved enterprise and a reduced tax rate of 25% for the remainder of the benefit period.

In the event that a dividend is distributed out of tax-exempt earnings of the "approved enterprise" under the "alternative benefits" track, the distributing company will generally be subject to 25% tax on the distributed earnings.

Dividends paid to shareholders from the earnings of an "approved enterprise" are subject to income tax at a rate of 15%. However, if the shareholder is a company, that shareholder will be entitled to a 15% tax credit, if and when such dividend out of "approved enterprise" earnings is distributed to its shareholders.

In accordance with Israeli GAAP:
Deferred taxes should be provided on the excess of the financial statement carrying value over the tax basis of an investment in an Israeli subsidiary as the Company does not have any means under local tax law to recover this difference in a tax-free manner.

Koor has not provided deferred tax in respect of undistributed tax-exempt or tax reduced earnings attributed to the "approved enterprise" of subsidiaries, which may be distributed, since it is the Group's policy not to initiate such a dividend distribution.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

3. Deferred taxes (cont'd)

In accordance with US GAAP:

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A reserve for deferred tax should be provided on the undistributed tax-exempt earnings of local subsidiaries established subsequent to December 15, 1992, as their distribution results in additional tax.

4. Salary expenses in respect of share options issued to employees

In accordance with Israeli GAAP:

No expense is recorded due to stock options granted to employees.

In accordance with US GAAP:

- a) Fixed Option Plan:

Under APB-25, the expense is measured as the difference between the share market price and the exercise price of the option, at the date of grant. The difference is charged as a salary expense during the period in which the employee performs the services for which the benefit was granted.

- b) Variable Option Plan:

Under APB-25 the expense is measured as the difference between the share market price and the exercise price of the option at the end of each reporting period. In each reporting period the expense is recorded based on the vested part of the period which has passed, taking into consideration amounts previously recorded as expenses.

5. The accounting treatment of marketable securities:

In accordance with Israeli GAAP:

Marketable securities which constitute a short-term investment are stated at market value. Changes to the market value are recorded as profits or losses.

Marketable securities which constitute a permanent investment are stated at cost (regarding debentures, including accumulated interest), except where market value is lower, and the decline in value is not considered to be temporary. (See Note 2H).

In accordance with US GAAP:

FAS No. 115 differentiates between three categories of marketable securities: securities held for a short period and traded at a high frequency (trading securities), available for sale securities and held to maturity securities.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

5. The accounting treatment of marketable securities:
(cont'd)

A change in the value of trading securities, including unrealized earnings, is charged to the statement of operations, while unrealized earnings after tax, if any, of the available for sale type is reported as a separate item within shareholders' equity.

Marketable securities that are classified as held-to-maturity are stated at cost (regarding debentures, including accumulated interest), except where market value is lower, and the decline in value is not considered to be temporary.

Most of the short term securities held by the Company are available-for-sale securities.

6. Allocation of proceeds from an issuance of debentures and stock warrants, when securities are issued as a package (issuance by Koor in 1994):

According to the accounting policy at this issuance: The proceeds from an issuance of debentures and stock warrants, as a package, are allocated to debentures according to their face value while the remainder of the proceeds is attributed to the share warrants.

In accordance with US GAAP:

The proceeds from an issuance of share options and convertible debentures, as a package, are split based on the relative fair value, of these securities at the date of issuance. This will sometimes result in the recording of a discount in respect of the convertible debentures that is to be amortized as interest expense over the term of debentures.

As at December 31, 2003, the entire balance of the deferred interest was amortized in full.

7. Provisions for anticipated losses from realization of convertible securities of investee companies:

In accordance with Israeli GAAP:

According to Opinions No. 48 and 53 of the ICPAI, a parent company is required to create a provision for losses, which it may incur from the dilution of its holdings in investee companies, when it is probable that the share options will be exercised or the debentures will be converted.

In accordance with US GAAP:

A loss in the parent company resulting from the dilution of its holdings, because of share options being exercised or debentures being converted, is recorded only at the time of exercise or conversion.

8. Employee severance benefits as a part of an efficiency program:

In accordance with Israeli GAAP:

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Up to and including 2002 employee severance benefits, as part of future anticipated dismissals, were recorded when management decided on the dismissals, and/or when management declared its intention regarding the dismissals. Since 2003, management's decision or intention regarding the dismissals does not in itself constitute a reason to record a provision for employee severance benefits, rather a provision is recorded only when an obligation to the employees exists.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

8. Employee severance benefits as a part of an efficiency program: (cont'd)

In accordance with US GAAP:

One-time termination benefits are benefits provided to current employees that are involuntarily terminated under the terms of a one-time benefit arrangement. A one-time benefit arrangement is an arrangement established by a plan of termination that applies for a specified termination event or for a specified future period.

A one-time benefit arrangement exists at the date the plan of termination meets all of the following criteria and has been communicated to employees (hereinafter referred to as the communication date):

- a. Management, having the authority to approve the action, commits to a plan of termination.
- b. The plan identifies the number of employees to be terminated, their job classifications or functions and their locations, and the expected completion date.
- c. The plan establishes the terms of the benefit arrangement, including the benefits that employees will receive upon termination (including but not limited to cash payments), in sufficient detail to enable employees to determine the type and amount of benefits they will receive if they are involuntarily terminated.
- d. Actions required to complete the plan indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

9. Earnings per share:

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In accordance with Israeli GAAP:

In accordance with Opinion No. 55, the dilutive effect of share options and convertible debentures is included in the computation of basic earnings per share if their exercise or conversion is considered to be probable. Calculation of the probability is based on the ratio between the market price of the shares and the present value of the price of exercising the stock options into shares or the present value of the payments for conversion of the debentures into shares.

In accordance with US GAAP:

In accordance with FAS 128 "Earnings Per Share" - basic earnings per share is computed on the basis of the weighted average number of shares outstanding during the year and does not include any dilutive potential effect of convertible instruments. Diluted earnings per share are computed on the basis of the weighted average number of shares outstanding during the year, plus the dilutive potential effect of ordinary share options considered outstanding during the year.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

10. Venture capital fund investments:

In accordance with Israeli GAAP:

Venture capital fund investments in venture capital investments are presented according to their cost less a provision for devaluation in the event of a permanent devaluation.

In accordance with US GAAP:

Venture capital fund investments are presented according to their fair value.

11. Revenue recognition - Adoption of SAB 101:

In accordance with US GAAP:

During the fourth quarter of 2000, the US SEC published Staff Accounting Bulletin No. 101 (hereinafter - "SAB 101"), which provides stricter criteria for revenue recognition implemented retroactively to the beginning of 2000, by way of cumulative effect at the beginning of the year and presentation of the previous quarters once again.

ECI implemented these guidelines in its financial statements, which are prepared in accordance with US GAAP. The cumulative effect, of the sales deferred upon initial adoption of SAB

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101, under US GAAP, was recognized over the years 2000 through 2003. Commencing in 2004, there is no additional impact from the deferral of these revenues.

In accordance with Israeli GAAP:

The provision does not apply in Israel, although it is possible to adopt the principles set out in the rule, if management estimates that the method of revenue recognition prescribed in SAB 101 is appropriate for economic and commerce conditions presently existing in its area of business.

This rule was adopted prospectively as of the fourth quarter of 2000, without implementing cumulative effect to the beginning of 2000 and without presenting data, which has already been published in the past.

12. Exchange of assets:

In accordance with Israeli GAAP:

Certain share exchange transactions were considered as exchanges of similar assets transactions and therefore neither a profit nor a loss was recorded subsequent to the transaction and the newly acquired assets were recorded based on book value of the original assets.

In accordance with US GAAP:

According to EITF 98-3 and EITF 01-2 such transactions are not considered as exchanges of similar assets transaction and therefore the newly acquired assets were recorded based on their fair values.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

13. Derivatives

In accordance with Israeli GAAP:

The Company applied FAS 52, FAS 80 and EITF 90-17 to account for its financial derivatives.

The results of financial derivatives held to hedge assets and liabilities are recorded in the statement of operations concurrently with the recording of the changes in the hedged assets and liabilities. Financial derivatives that are not held for hedging are stated in the balance sheet at fair value. Changes in the fair value are included in the statement of operations in the period they occurred.

In accordance with US GAAP:

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The Company applied FAS 133 to the derivatives.

Most derivatives in the consolidated group do not meet the hedging criteria prescribed by FAS 133, therefore they are stated at fair value and changes in the fair value are charged to the statement of operations in the period they occurred.

14. Impairment of Long-lived Assets to be Held and Used

In accordance with Israeli GAAP:

The Company applied Standard No. 15 under which the Company is required to test the recoverable amount of the assets, which is the higher of the net sales price and usage value. A loss from impairment will be reversed only if changes have occurred in the estimates used in determining the recoverable value of the asset, from the date of recognition of the last impairment.

In accordance with US GAAP:

The Company applied FAS 144 according to which a long-lived asset to be held and used is considered to be impaired only if the undiscounted cash flows of the related asset do not exceed its book value and reversals of impairments are not allowed.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

15. Impairment of Investments in ECI

In accordance with Israeli GAAP:

The Company applied Standard No. 15 under which the Company is required to test the recoverable amount of the investment, which is the higher of the net sales price and usage value. A loss from impairment will be reversed only if changes have occurred in the estimates used in determining the recoverable value of the investment, from the date of recognition of the last impairment.

In accordance with US GAAP:

The Company applied APB 18 according to which a loss is recorded only when the impairment of the investee is other than temporary and reversals of impairments are not allowed.

The impact of the differences between Israel GAAP and US GAAP was as follows:

1. Recording of impairment in value

Subsequent to the negative indications concerning ECI, an impairment provision of NIS 130 million was recorded under both Israeli GAAP and US GAAP. According to Israeli GAAP, the impairment in value is recorded first by writing-off credit balances of foreign currency translation differences that were recorded directly to equity in the amount of NIS 105 million, and only the remainder of NIS 25 million was recorded as an expense in the statement of income. According to US GAAP, foreign currency translation differences are not written-off and the entire impairment is recorded as an expense in the statement of income. This difference is presented in the reconciling item entitled "foreign currency translation due to impairment".

2. Amortization differences

The Company allocated the excess of fair value of ECI's net assets over the book value of those assets ("the impairment provision") to the net assets of ECI and amortized the impairment provision over the useful life of these assets. According to Israeli GAAP, the allocation is first to the intangible assets of the investee and then to the non-monetary assets of the investee on a proportional basis. According to US GAAP the allocation is to non-current assets only, on a proportional basis. The different bases of allocation between Israeli GAAP and US GAAP resulted in differences in the amortization amounts recorded in the statement of income, due to different amortization rates of different asset types (inventory, fixed assets, intangible assets). These differences are presented in the reconciling item entitled "differences from investee due to impairment previously recorded".

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

15. Impairment of Investments in ECI (cont'd)

3. Reversal of impairment

Subsequent to the recovery of ECI, under Israeli GAAP the impairment provision was reversed and Koor once again presented its investment in ECI according to the

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equity method.

According to Israeli GAAP, an impairment provision may be reversed if there is an increase in the fair value of the investee company. According to US GAAP, an impairment provision may not be reversed.

The reversal according to Israeli GAAP was not recorded in the statement of income, but rather as a credit to equity as foreign currency translation differences.

16. Amortization of Goodwill:

In accordance with Israeli GAAP:

Goodwill is amortized over its economic life which may not exceed 20 years. Goodwill is monitored for an impairment in value where there are indications indicating a permanent impairment in the value of the goodwill.

In accordance with US GAAP:

Effective January 1, 2002, goodwill balances are not amortized systematically but are instead evaluated for recoverability by means of an impairment test to be performed at least once a year on a fixed date in accordance with the directives of FAS 142. Impairment of goodwill subsequent to the first implementation of the impairment test on January 1, 2002, was recorded as a cumulative effect in respect of a change in the accounting method. Accordingly, a cumulative effect of NIS 806 thousand was recorded in the adjustment note in 2002. No further impairments have been required subsequent to the initial implementation.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

17. Consolidation of M-A Industries

As a result of the sale of shares of M-A Industries at the beginning of 2004, Koor's share in M-A Industries decreased to below 50%.

In accordance with Israeli GAAP:

The position of the Israeli Securities Authority is that when a company has been consolidated in the financial statements of the holding company and there has been a decrease in the voting rights to below 50%, if the overall economic circumstances have not essentially changed the consolidation of the investee company should be continued because of the importance of continuity and consistency of the accounting reports. Therefore and as explained in Note 3C(1) Koor continues to consolidate M-A Industries' financial statements.

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In accordance with US GAAP:

The condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one company, directly or indirectly, of over fifty percent of the outstanding voting shares of another company is a prerequisite for consolidation. Therefore, M-A Industries is accounted under the equity method for US GAAP purposes, beginning in 2004.

18. Capitalization of licensing costs

In accordance with Israeli GAAP:

Certain costs incurred by the Company in connection with the registration process to obtain licenses to sell products in various jurisdictions are capitalized.

In addition, amounts which are paid by the Company to the original registrant as data compensation costs only after the U.S. Environmental Protection Agency (hereinafter: "EPA") issues a registration to the Company are also capitalized.

The capitalized licensing costs are amortized over the expected benefit period.

In accordance with U.S. GAAP:

The costs incurred by the Company in connection with the registration process to obtain licenses to sell products in various jurisdictions are deemed to be development costs under US GAAP and are expensed as incurred.

The amounts paid by the Company to the original registrant as data compensation costs only after the EPA issues a registration to the Company are capitalized and amortized over the expected benefit period.

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

19. Liabilities for employee severance benefits

In accordance with Israeli GAAP:

Amounts funded by purchase of insurance policies and by deposits with recognized severance pay funds are deducted from the related severance pay liability, which is then presented at a net amount.

In accordance with US GAAP:

The amounts funded would be presented as other long-term assets and the amount of the liability would be presented

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under long-term liabilities.

20. Gains from decline in holdings in consolidated and affiliated companies

Various GAAP differences affecting the shareholders' equity of the consolidated or affiliated company, cause differences in the book value of the investment at the Company level, i.e. the Company's book value of the holdings according to US GAAP differs from the book value according to Israeli GAAP. Therefore the amounts of the gains according to US GAAP differ from the amounts of the gains according to Israeli GAAP.

21. Restatement

In prior years, one of the Company's subsidiaries capitalized for U.S. GAAP purposes certain costs incurred in connection with the registration process to obtain licenses to sell products in various jurisdictions. Under U.S. GAAP these costs are deemed to be development costs and should have been expensed as incurred.

In addition, one of the Company's subsidiaries incorrectly applied FAS No 109 with respect to the calculation of certain deferred tax items relating to temporary differences that arose from currency exchange rate differences.

Therefore, the reconciliation of material differences between Israeli and US GAAP has been restated. The impact on the reconciliation is disclosed below:

| | As reported | As restated |
|-------------------------------------|-------------|-------------|
| | ----- | ----- |
| 2003 | | |
| Net loss | (105,308) | (108,924) |
| Earnings (loss) per ordinary share | (6.81) | (7.04) |
| Intangible assets | 2,240,439 | (2,011,874) |
| Deferred taxes | 269,468 | 206,189 |
| Minority interests | 1,774,894 | 1,689,966 |
| Shareholders equity | 1,662,480 | 1,582,122 |
| 2002 | | |
| Net loss | (761,561) | (762,511) |
| Earnings (loss) per ordinary shares | (50.18) | (50.25) |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

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Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Differences between Israel GAAP and US GAAP (cont'd)

22. Statements of cash flows

(a) Translation differences in respect of cash and cash equivalents

In accordance with Israeli GAAP:

The statements shall report the effect of exchange rate changes on cash and cash equivalents balances held in foreign currencies, only in "autonomous foreign entities".

In accordance with US GAAP:

The statements shall report the effect of exchange rate changes on all cash and cash equivalents balances held in foreign currencies.

(b) Securitization transaction

In accordance with Israeli GAAP:

The securitization transaction (see Note 3C(2)) was classified as a sale of trade receivables. Thus, cash flows, derived from that transaction, were classified as cash flows from operating activities.

In accordance with US GAAP:

Until June 30, 2003 the securitization transaction did not meet the criteria set out by FAS 140 for the classification as a sale of trade receivables and was classified as a secured borrowing. Therefore, cash flows derived from this transaction until June 30, 2003 were classified as cash flows from financing activities.

(c) Consolidation of M-A Industries

In accordance with Israeli GAAP:

In 2004, Koor consolidates M-A Industries' cash flows.

In accordance with US GAAP:

Beginning in 2004, M-A Industries is accounted under the equity method for US GAAP purposes, therefore M-A Industries' cash flows are not consolidated.

See also Note 28A(17).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

- B. The effect of the material differences between Israeli and US GAAP on the financial statements
1. Statements of operations:

| | | Year |
|--|----------|----------|
| | | ----- |
| | | 2004 |
| | | ----- |
| | | NI |
| | | ----- |
| a) Net earnings (loss) as reported, according to Israeli GAAP | 144,990 | |
| Amortization of deferred interest in respect of the restructuring of debts - Note 28A(2) | - | |
| Salary expenses in respect of share options issued to employees - Note 28A(4) | (91,318) | |
| Loss (gain) from marketable securities, net - Note 28A(5) | (4,295) | |
| Provisions for anticipated losses from realization of convertible securities in investee companies - Note 28A(7) | 10,106 | |
| Amortization of discount in respect of convertible debentures - Note 28A(6) | - | |
| Severance pay arising from an efficiency program - Note 28A(8) | 17,326 | |
| Gains from decline in holding in consolidated and affiliated companies - Note 28A(20) | 11,829 | |
| Venture capital investments - Note 28A(10) | (20,726) | |
| Temporary differences resulting from recognition of revenue arising from application of SAB 101 - Note 28A(11) | - | |
| Profit from exchange of assets - Note 28A(12) | - | |
| Discontinued activities | - | |
| Impairment in value of long-lived assets to be held and used - Note 28A(14) | (1,277) | |
| Differences from investee due to impairment previously recorded - Note 28A(15) | 29,588 | |
| Foreign currency translation due to impairment - Note 28A(15) | - | |
| Amortization of goodwill - Note 28A(16) | 39,938 | |
| Expensing of licensing costs - Note 28A(18) | (8,859) | |
| Derivatives (FAS 133) - Note 28A(13) | 4,602 | |
| Other | 711 | |
| | | ----- |
| | | (12,375) |
| Income taxes - Note 28A(3) | | (21,212) |
| Minority interests in respect of the above differences | | 170 |

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| | | |
|--|----------|-------|
| | ----- | ----- |
| | (33,418) | |
| Cumulative effect as beginning of the year | - | |
| | ----- | ----- |
| | (33,418) | |
| | ----- | ----- |
| Net earnings (loss) according to US GAAP | 111,572 | * |
| | ===== | ===== |

* Restated, see Note 28A(21).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

- B. The effect of the material differences between Israeli and US GAAP on the financial statements (cont'd)
- 1. Statements of operations (cont'd):
- b) Earnings (loss) per ordinary share

| | | | |
|---|--|------------|-------|
| | | ----- | ----- |
| | | 2004 | Yea |
| | | ----- | ----- |
| | | ----- | ----- |
| Basic earnings per ordinary share: | | | |
| As reported according to Israeli GAAP | | 8.85 | |
| As reported according to US GAAP | | 7.05 | |
| | | ===== | ===== |
| Weighted average of number of shares and share equivalents according to US GAAP | | 15,824,185 | 1 |
| | | ===== | ===== |
| Fully diluted earnings per ordinary share: | | | |
| As reported according to Israeli GAAP | | 8.85 | |
| | | ===== | ===== |
| As reported according to US GAAP | | 4.89 | |
| | | ===== | ===== |

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Weighted average of number of shares and
share equivalents according to US GAAP

16,242,770 **1
=====

* Restated, see Note 28A(21).

** Share equivalents are not reflected in US GAAP due to the
fact that they are anti-dilutive.

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Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on
the Financial Statements (cont'd)

B. The effect of the material differences between Israeli and US
GAAP on the financial statements (cont'd)

2. Balance sheet:

| | Israeli GAAP | Discontinuance consolidation |
|---|-----------------|---------------------------------|
| Cash and cash equivalents | 617,310 | (174,375) |
| Short-term deposits and investment (1) | 416,468 | (6,733) |
| Receivables | 2,173,599 | (1,590,552) |
| Other receivables | 528,983 | (332,817) |
| Inventories and projects in progress | 2,294,885 | (1,985,428) |
| Assets designed for sale | 41,765 | - |
| Investments in affiliates (2) | 1,375,160 | 1,471,197 |
| Investments and other receivables (1)(3) | 489,031 | (95,073) |
| Fixed assets, net | 2,852,907 | (1,876,731) |
| Intangible assets after amortization (4) | 2,357,458 | (2,316,290) |
| Total assets | 13,147,566 | (6,906,802) |
| Short-term liabilities | 1,738,456 | (603,210) |
| Trade payables | 1,667,455 | (1,404,171) |
| Other payables (5)(6) | 1,369,442 | (867,233) |
| Customer advances | 353,371 | (9,891) |
| Bank loans and other | 2,341,115 | (440,968) |
| Convertible debentures | 811,291 | (811,291) |
| Deferred taxes (7) | 240,468 | (234,157) |
| Liability for employee severance benefits (3) | 197,168 | (115,061) |
| Minority interests (8) | 2,552,333 | (2,420,820) |
| Capital reserve for "available-for-sale" securities (2) | - | - |

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| | | |
|----------------------------|-----------|---|
| Capital reserves (9) (10) | 2,358,425 | - |
| Retained losses (8) | (966,152) | - |
| Total shareholders' equity | 1,876,467 | - |

* Restated, see Note 28A(21).

Continued --

| | ----- 2003 ----- Israeli GAAP | ----- Adjustment ----- |
|---|---|------------------------------|
| Cash and cash equivalents | 593,403 | - |
| Short-term deposits and investment (1) | 366,809 | - |
| Receivables | 2,052,461 | 10,847 |
| Other receivables | 452,170 | - |
| Inventories and projects in progress | 1,885,751 | - |
| Assets designed for sale | 42,525 | - |
| Investments in affiliates (2) | 943,764 | (60,839) |
| Investments and other receivables (1) (3) | 483,384 | 290,230 |
| Fixed assets, net | 2,928,407 | 11,455 |
| Intangible assets after amortization (4) | 2,121,083 | *(109,209) |
| Total assets | 11,869,757 | *142,484 |
| Short-term liabilities | 1,577,402 | - |
| Trade payables | 1,342,783 | - |
| Other payables (5) (6) | 1,270,217 | 75,551 |
| Customer advances | 350,535 | - |
| Bank loans and other | 3,119,837 | - |
| Convertible debentures | 340,270 | - |
| Deferred taxes (7) | 199,787 | *6,402 |
| Liability for employee severance benefits (3) | 192,002 | 265,365 |
| Minority interests (8) | 1,736,531 | *(46,565) |
| Capital reserve for "available-for-sale" securities (2) | - | (30,074) |
| Capital reserves (9) (10) | 2,367,341 | *229,863 |
| Retained losses (8) | (1,111,142) | *(358,060) |
| Total shareholders' equity | 1,740,393 | *(158,271) |

* Restated, see Note 28A(19).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on

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the Financial Statements (cont'd)

- B. The effect of the material differences between Israeli and US GAAP on the financial statements (cont'd)
- (1) Adjustment of value of investment securities to market value.
 - (2) Adjustments to the investments in M-A Industries and ECI
 - (3) Reconciliation of deposits funded in respect of severance pay.
 - (4) Reversal of periodical provisions related to goodwill and intangible assets.
 - (5) Provision for employee severance benefits resulting from an efficiency program.
 - (6) Financial derivatives.
 - (7) Change in deferred taxes.
 - (8) Effects of the reconciliation to US GAAP.
 - (9) Share options issued to employees.
 - (10) Cumulative foreign currency translation adjustments, cancellation of provision for decline in value of autonomous investee.
 - (11) See Note 28 A(17).
3. Comprehensive loss

"Comprehensive earnings (loss)" consists of the change, during the current period, in the Company's shareholder equity that does not derive from shareholders' investments or from the distribution of earnings to shareholders.

Comprehensive earnings (loss) include two components - net earnings and other comprehensive earnings. Net earnings are the earnings stated in the statement of operations and other comprehensive earnings include the amounts that are recorded directly in shareholders' equity and that do not derive from transactions with shareholders.

| | Year ended December 31 | |
|--|------------------------|------------|
| | 2004 | 2003 |
| | NIS thousands | |
| Net earnings (loss) according to US GAAP | 111,572 | *(108,924) |
| Other comprehensive earnings, after tax: | | |
| Adjustments from translation of financial statements of investee companies | (9,546) | *(143,585) |
| FAS 133 | (10,964) | 6,487 |
| Unrealized gains (loss) from securities | 36,516 | 32,572 |
| Total other comprehensive earnings (loss) | 16,006 | (104,526) |
| Total comprehensive earnings (loss) | 127,578 | (213,450) |

* Restated, see Note 28A(21).

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

B. The effect of the material differences between Israeli and US GAAP on the financial statements (cont'd)

4. Cash flows:

| | 2004 (1) | Year ended December 31 2003 (2) |
|--|---------------|------------------------------------|
| | ----- | ----- |
| | NIS thousands | |
| | ----- | ----- |
| Net cash flows from operating activities: | | |
| Israeli GAAP | 890,673 | 774,775 |
| Adjustments | (907,798) | (235,808) |
| US GAAP | (17,125) | 538,967 |
| Net cash flows from investing activities: | | |
| Israeli GAAP | (722,839) | 266,585 |
| Adjustments | 383,650 | - |
| US GAAP | (339,189) | 266,585 |
| Net cash flows from financing activities: | | |
| Israeli GAAP | (128,069) | (1,209,783) |
| Adjustments | 340,457 | 211,182 |
| US GAAP | 212,388 | (998,601) |
| Translation differences in respect of cash and cash equivalents: | | |
| Israeli GAAP | (15,858) | (28,273) |
| Adjustments (3) | 9,316 | 24,626 |
| US GAAP | (6,542) | (3,647) |
| Increase (decrease) in cash and cash equivalents: | | |
| Israeli GAAP | 23,907 | (196,696) |
| Adjustments | (174,375) | - |
| US GAAP | (150,468) | (196,696) |
| Balance of cash and cash equivalents at beginning of year: | | |

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| | | | | |
|-----|--|-----------|--|---------|
| | Israeli GAAP and US GAAP | 593,403 | | 790,099 |
| | | | | |
| | Balance of cash and cash equivalents at end of year: | | | |
| | Israeli GAAP | 617,310 | | 593,403 |
| | Adjustments | (174,375) | | - |
| | | | | |
| | US GAAP | 442,935 | | 593,403 |
| | | | | |
| (1) | See Note 28A(22) (c). | | | |
| (2) | See Note 28A(22) (b). | | | |
| (3) | See Note 28A(22) (a). | | | |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

- C. Condensed figures of M-A Industries and ECI according to Regulation S-X 4-08
- (1) M-A Industries condensed figures
- A. As at December 31, 2004

| | Israeli GAAP | Adjustments | US GAAP |
|-------------------------|----------------|----------------|----------------|
| | US\$ thousands | US\$ thousands | US\$ thousands |
| | | | |
| Current assets | 949,338 | 5,323 | 954,661 |
| Non-current assets | 985,229 | 42,118 | 1,027,347 |
| Current liabilities | 669,571 | 14,685 | 684,256 |
| Non-current liabilities | 333,423 | 24,631 | 358,054 |
| Minority interests | 18,756 | (1,981) | 16,775 |
| Convertible debentures | 38,322 | - | 38,322 |

- B. For the year ended December 31, 2004 according to Israeli GAAP

| | |
|--------------------------------------|-----------|
| Revenue from sales and services | 1,539,702 |
| Gross profit | 595,794 |
| Net income according to Israeli GAAP | 165,527 |
| Adjustment to US GAAP | (41,789) |
| Net income according to US GAAP | 123,738 |

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| | | |
|--|--|----------------|
| (2) | ECI's condensed figures according to US GAAP | |
| | 2004 | 2003 |
| | ----- | ----- |
| | US\$ thousands | US\$ thousands |
| | ----- | ----- |
| As at December 31 | | |
| Current assets | 449,556 | 537,528 |
| Non-current assets | 405,253 | 364,468 |
| Current liabilities | 248,012 | 242,037 |
| Non-current liabilities | 50,943 | 86,673 |
| Minority interests | 4,086 | 3,781 |
| For the year ended December 31 | | |
| Revenues | 496,712 | 392,567 |
| Gross profit | 195,741 | 153,269 |
| Income (loss) from continuing operations | 14,056 | (44,723) |
| Net income (loss) | 10,153 | (71,040) |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 28 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

D. Summarized financial information of proportionately consolidated companies

(1) Telrad
A. As at December 31, 2004

| | | | |
|-------------------------|---------------|---------------|-----|
| | Israeli GAAP | Adjustments | --- |
| | ----- | ----- | --- |
| | NIS thousands | NIS thousands | NI |
| | ----- | ----- | --- |
| Current assets | 295,867 | 4,735 | |
| Non-current assets | 144,386 | 6,735 | |
| Current liabilities | 197,173 | (17,326) | |
| Non-current liabilities | 86,589 | - | |
| Minority interests | 4,814 | 3,765 | |

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B. For the three months ended December 31, 2004 (1)

| | |
|--------------------------------------|----------|
| Revenue from sales and services | 93,403 |
| Gross profit (loss) | (11,565) |
| Net loss according to Israeli GAAP | (61,114) |
| Adjustment to US GAAP | 18,970 |
| Net loss according to US GAAP | (42,144) |
| Cash flows from operating activities | 7,259 |
| Cash flows from investing activities | (13,043) |
| Cash flows from financing activities | 27,757 |

(1) Telrad is included in Koor's financial statements by the proportionate consolidation method from the fourth quarter of 2004. See Note 3D(1).

(2) Proportionately consolidated companies of Sheraton

A. As at December 31, 2004

| | Israeli GAAP | Adjustments | |
|-------------------------|---------------|---------------|-------|
| | ----- | ----- | |
| | NIS thousands | NIS thousands | NI |
| | ----- | ----- | ----- |
| Current assets | 20,694 | - | |
| Non-current assets | 220,893 | (2,516) | |
| Current liabilities | 29,530 | - | |
| Non-current liabilities | 219,890 | - | |

B. For the year ended December 31, 2004

| | |
|--------------------------------------|---------|
| Revenue from sales and services | 83,238 |
| Gross profit | 22,710 |
| Net loss according to Israeli GAAP | (1,416) |
| Adjustment to US GAAP | 1,078 |
| Net loss according to US GAAP | (338) |
| Cash flows from operating activities | 5,808 |
| Cash flows from investing activities | 942 |
| Cash flows from financing activities | (3,584) |

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Koor Industries Ltd. (An Israeli Corporation)

Notes to the Financial Statements

Note 29 - Events (Unaudited) Subsequent to the Date of the Independent Auditors' Report

A. On July 6, 2005 the Company signed an amendment to the agreements with Elbit and Federman (see Note 3H(2)), pursuant to which the

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Company will sell its entire holdings in Elisra to Elbit, instead of to Tadiran Communications as per the original agreements, for approximately \$70 million and additional consideration following receipt of future insurance proceeds. The Company also received the right to acquire Dekolink Ltd., a start-up company in the cellular field that is wholly-owned by Elisra. As originally agreed, the Company will sell the balance of its holdings in Tadiran Communications to Elbit for \$83 million. However, under the amended terms of the transactions, contrary to the terms of the original agreement, this sale will be conducted in two parts, and the Company and Elbit will share joint control of Tadiran Communications, as described in Note 3H(2), following the sale of the first 5%. The sale of the Company's remaining shares in Tadiran Communications is contingent on the execution of the sale of its holdings in Elisra to Elbit. Elbit's acquisition of Elisra is subject to the approvals of Elbit's shareholders at general meeting to be held within sixty days and Israel's Anti-Trust Commissioner. In addition, under the amended terms of the transactions, contrary to the terms of the original agreement, the Company will acquire only an additional 2.3% of Elbit from Federman for \$25 million, regardless of whether the sale of Elisra is approved by the Israeli Anti-Trust Commissioner. Upon completion of all the stages of these transactions, the Company will hold approximately 7.6% of Elbit.

- B. On April 10, 2005, as part of a private placement to Israeli institutional investors, the Company issued NIS 400 million par value in debentures for NIS 400 million in cash, as well as 800,000 options without consideration. The debentures bear annual interest of 3.75%, linked to the CPI, which is paid on April 30 and October 31 of each year. The debentures are linked to the CPI and will be repaid in a balloon payment on April 30, 2010. Each option is exercisable for one ordinary share par value NIS 0.001 of the Company until April 30, 2010, at an exercise price of NIS 300. The Company intends to register for trade on the Tel-Aviv stock exchange the shares that will ensue from exercise of the options.
- C. On June 7, 2005, the Company received a bill of indictment from the Anti-Trust Authority in accordance with the notice from February, 2 2005 as described in Note 18A(1)(b).

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of Ernst & Young Global]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE SHAREHOLDERS OF

TADIRAN COMMUNICATIONS LTD.

We have audited the consolidated balance sheet of Tadiran communications Ltd. ("the Company") and its subsidiaries as of December 31, 2004 (not presented separately herein.) This balance sheet is the responsibility of the Company's management. Our responsibility is to express an opinion on this balance sheet based on our audit. We did not audit the balance

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sheet of a certain subsidiary, whose assets included in consolidation constitute approximately 7% of total consolidated assets as of December 31, 2004. The balance sheet of this subsidiary was audited by other independent auditor, whose report has been furnished to us, and our opinion, insofar as it relates to amounts included for this certain subsidiary, is based solely on the report of the other independent auditors.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of other independent auditors, the consolidated balance sheet referred to above presents fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2004, in conformity with generally accepted accounting principles in Israel, which differ in certain respects from accounting principles generally accepted in the United States (see Note 32 to the consolidated financial statements).

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
March 20, 2005

KOST, FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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[Letterhead of Hoberman, Miller, Goldstein & Lesser, P.C.]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholder and Board of Directors
Talla-Com, Tallahassee Communications Industries, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Talla-Com, Tallahassee Communications Industries, Inc. and Subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations and retained earnings and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Talla-Com, Tallahassee Communications Industries, Inc. and Subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for the years then needed, in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States vary in certain significant respects from accounting principles generally accepted in Israel. Application of accounting principles generally accepted in Israel did not have a material effect on the results of operations, shareholder's equity and cash flows for the years ended December 31, 2004 and 2003.

/s/ Hoberman, Miller, Goldstein & Lesser, CPA'S, P.C.

January 28, 2005
New York, New York

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[Letterhead of Brightman Almagor & Co., a Member Firm of
Deloitte & Touche Tohmatsu]

Report of Independent Registered Public Accounting Firm To The
Shareholders of
Tadiran Electronic System Ltd.

We have audited the accompanying balance sheets of Tadiran Electronic System ("the Company") as of December 31, 2004 and 2003 and the related statements of operations, changes in shareholders' equity and cash flows, for each of the three years, in the period ended December 31, 2004. These financial statements are the responsibility of the Company's Board of Directors and of its management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting

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the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of its operations, changes in its shareholders' equity and its cash flows for the three years, in the period ended December 31, 2004, in conformity with generally accepted accounting principles in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of such differences is presented in Note 16 to the financial statements.

As explained in Note 2A, the financial statements are presented in U.S. dollars.

/s/ Brightman Almagor & Co.
Brightman Almagor & Co.
Certified Public Accountants
Tel Aviv, Israel
February 14, 2005

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[Letterhead of Brightman Almagor & Co., a Member Firm of
Deloitte & Touche Tohmatsu]

Report of Independent Registered Public Accounting Firm To The
Shareholders of
Tadiran Spectralink Ltd.

We have audited the accompanying balance sheets of Tadiran Spectralink Ltd. ("the Company") as of December 31, 2004 and 2003 and the related statements of operations, changes in shareholders' equity and cash flows, for each of the three years, in the period ended December 31, 2004. These financial statements are the responsibility of the Company's Board of Directors and of its management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

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In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of its operations, changes in its shareholders' equity and its cash flows for the three years, in the period ended December 31, 2004, in conformity with generally accepted accounting principles in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. Information relating to the nature and effect of such differences is presented in Note 22 to the financial statements.

As explained in Note 2A, the financial statements are presented in U.S. dollars.

/s/ Brightman Almagor & Co.
Brightman Almagor & Co.
Certified Public Accountants
Tel Aviv, Israel
February 14, 2005

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[Letterhead of Hoberman, Miller, Goldstein & Lesser, P.C.]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Member and Board of Directors
Tadiran Electronic Industries, LLC

We have audited the accompanying balance sheet of Tadiran Electronic Industries, LLC (formerly Tadiran Electronic Industries, Inc.) as of December 31, 2004 and the consolidated balance sheet of Tadiran Electronic Industries, LLC and Subsidiary as of December 31, 2003, and the consolidated statements of operations, member's equity, and cash flows for each of the three years in the period ended December 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Tadiran Electronic Industries, LLC as of December 31, 2004 and the consolidated financial position of Tadiran Electronic Industries, LLC and Subsidiary as of December 31, 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

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Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The additional information on pages 13 through 16 is presented for the purpose of additional analysis rather than to present the financial position and results of operations of the individual companies, and is not a required part of the basic consolidated financial statements. This additional information is the responsibility of the Company's management. Such information has been subjected to the auditing procedures applied in our audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic consolidated financial statements taken as a whole.

Accounting principles generally accepted in the United States vary in certain significant respects from accounting principles generally accepted in Israel. Application of accounting principles generally accepted in Israel did not have a material effect on the results of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2004.

/s/ Hoberman, Miller, Goldstein & Lesser, CPA'S, P.C.

January 21, 2005
New York, New York

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[Letterhead of Hoberman, Miller, Goldstein & Lesser, P.C.]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and Board of Directors
Microwave Networks, Inc. and Subsidiary

We have audited the accompanying consolidated balance sheet of Microwave Networks, Inc. and Subsidiary as of December 31, 2004 and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements of material mismanagement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Microwave Networks, Inc. and Subsidiary as of December 31, 2004, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States vary in certain significant respects from accounting principles generally accepted in Israel. Application of accounting principles generally accepted in Israel did not have

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a material effect on the results of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2004.

/s/ Hoberman, Miller, Goldstein & Lesser, CPA'S, P.C.

January 21, 2005
New York, New York

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of Ernst & Young Global]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders of

KOOR TRADE LTD.

We have audited the accompanying balance sheets of Koor Trade Ltd. ("the Company") as of December 31, 2004 and 2003 and the related statements of operations, changes in shareholder's equity and cash flows for each of the three years in the period ended December 31, 2004 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of certain companies the investment in which based on the equity method of accounting, amounted to NIS 49 million and NIS 34.1 million as of December 31, 2004 and 2003, respectively, and the Company's equity in their income amounted to NIS 8.7 million, NIS 5.6 million and NIS 6.5 million for the years ended December 31, 2004, 2003 and 2002, respectively. Those financial statements which presented in accordance with U.S. generally accepted accounting principles, were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts utilized by Company's management (before reconciliation to Israel generally accepted accounting principles), is based solely on the reports of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts (including the Company's reconciliation of the financial statements of the aforementioned certain subsidiaries to Israel generally accepted accounting principles from U.S. generally accepted accounting principles) and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the financial statements referred to above present fairly, in all material

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respects, the financial position of the Company at December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the three years in the period ended of December 31, 2004, in conformity with accounting principles generally accepted in Israel, which differ in certain respects from those followed in the United States, as described in Note 7 to the financial statements.

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
March 21, 2004

KOST, FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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[Letterhead of Blick Rothenberg, Chartered Accountants]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM TO THE
SHAREHOLDERS OF BALTON CP LIMITED

We have audited the accompanying consolidated balance sheets of Balton CP Limited (the "Company") and its subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the company's internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries at December 31, 2004 and 2003, and the consolidated results of their operations and cash flows for each of the three years in the period ended of December 31, 2004, in conformity with accounting principles generally accepted in United States.

/s/ Blick Rothenberg
Blick Rothenberg
Chartered Accountants and Registered Auditors
London, England

20 March 2005

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[Letterhead of Einfeld Symonds Vince]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE SHAREHOLDERS OF KOOR INTER-TRADE (ASIA)
PTY LIMITED AND ITS SUBSIDIARIES

We have audited the accompanying consolidated balance sheets of KOOR INTER-TRADE (ASIA) PTY LIMITED ("the Company") and its subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts (including the Company's reconciliation of the financial statements to Israel generally accepted accounting principles and to U.S. generally accepted accounting principles) and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2004 and 2003, and the consolidated results of their operations and cash flows for each of the three years in the period ended of December 31, 2004, in conformity with Australian generally accepted accounting principles, which differ in certain respects from those followed in the United States and in Israel as described in Note 1 to the consolidated financial statements.

Dated at Sydney the 8th day of March 2005

/s/ Einfeld Symonds Vince
EINFELD SYMONDS VINCE

Chartered Accountants

/s/ Graham B. Einfeld
GRAHAM B. EINFELD
Partner

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of
Ernst & Young Global]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders of

LUXEMBURG PHARMACEUTICAL LTD.

We have audited the accompanying consolidated balance sheets of Luxembourg Pharmaceutical Ltd. ("the Company") and its subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the two years in the period ended December 31, 2004 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts (including the Company's reconciliation of the consolidated financial statements to U.S. generally accepted accounting principles) and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2004 and 2003, and the consolidated results of their operations and cash flows for each of the two years in the period ended of December 31, 2004, in conformity with Israel generally accepted accounting principles, which differ in certain respects from those followed in the United States, as described in Note 21 to the consolidated financial statements.

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
February 17, 2005

KOST, FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of
Ernst & Young Global]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders of

LYCORED NATURAL PRODUCTS INDUSTRIES LTD.

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We have audited the accompanying consolidated balance sheets of Lycored Natural Products Industries Ltd. ("the Company") and its subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of a certain subsidiary, whose assets included in consolidation constitute approximately 18% and 16% of total consolidated assets as of December 31, 2004 and 2003, and whose revenues included in consolidation constitute approximately 37% and 35% of total consolidated revenues for the two years ended December 31, 2004. Those financial statements, presented in accordance with accounting principles generally accepted in the United Kingdom and including reconciliation to United States generally accepted accounting principles, were audited by other auditors whose reports as of and for the years ended December 31, 2004 and 2003, have been furnished to us, and our opinion, insofar as it relates to the amounts utilized by Company's management (before reconciliation to Israel generally accepted accounting principles) of and for the years ended December 31, 2004 and 2003, is based solely on the reports of other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the company's internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts (including the Company's reconciliation of the financial statements of the aforementioned subsidiary to Israel generally accepted accounting principles) and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2004 and 2003, and the consolidated results of their operations and cash flows for each of the three years in the period ended of December 31, 2004, in conformity with Israel generally accepted accounting principles, which differ in certain respects from those followed in the United States, as described in Note 21 to the consolidated financial statements.

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
February 24, 2005

KOST, FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders of

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Nutriblend LTD.

We have audited the accompanying balance sheets of Nutriblend Ltd. ("the Company") as at December 31, 2004 and 2003, and the related statements of operations, changes in shareholder's equity and cash flows for each of the two years in the period ended December 31, 2004 (not presented separately herein). These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the company's internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of its operations and its cash flows for each of the two years in the period ended of December 31, 2004, in conformity with accounting principles generally accepted in United Kingdom, which differ in certain respects from those followed in the United States, as described in Note 22 to the financial statements.

/s/ Goodman Jones
London
January 20, 2005

Goodman Jones
Chartered Accountants Registered Author

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of
Ernst & Young Global]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of

TELRAD CONNEGY COMMUNICATIONS INC.

We have audited the accompanying consolidated balance sheet of Telrad Connegy Communications Inc. ("the Company") and its subsidiaries as of December 31, 2004 and 2003 and the related consolidated statements of operations in shareholders' equity (deficiency) and the consolidated cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on

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our audits.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2004, and 2003 and the consolidated results of their operations and cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States, which differ in certain respects from those followed in Israel, as described in Note 14 to the consolidated financial statements.

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
March 27, 2005

KOST, FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of
Ernst & Young Global]

Report Of Independent Registered Public Accounting Firm

to the Partners of Koor Venture Capital L.P.

We have audited the accompanying balance sheets of Koor Ventures Capital L.P. (the "Partnership") as at December 31, 2004 and 2003, and the related statements of operations, shareholders' equity and cash flows, for each of the three years, the last of which ended December 31, 2004. These financial statements are the responsibility of the Partnership's Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of an affiliate, which Partnership's investment constitute NIS 12,466 thousand and NIS 7,313 thousand, as of December 31, 2004 and 2003, respectively, and its equity in losses constitute NIS 329 thousand for the years ended December 31, 2004, 2003 and 2002, respectively. The financial statements of the affiliate were audited by other auditors whose reports thereon were furnished to us. Our opinion, insofar as it relates to amounts included for the affiliate, is based solely on the said reports of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we

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plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Management, as well as evaluating the overall financial statement presentation. We believe that our audits, and reports of the other auditors, provide a reasonable basis for our opinion.

In our opinion, based on our audits and on the reports of the above-mentioned other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Partnership as of December 31, 2004 and 2003 and the results of their operations, the changes in shareholders' equity and their cash flows for each of the three years, the last of which ended December 31, 2004 in conformity with accounting principles generally accepted in Israel.

As explained in Note 2, the financial statements for dates and reporting periods subsequent to December 31, 2003 are stated in reported amounts, in accordance with the accounting standards of the Israel Accounting Standards Board. The financial statements for dates and reporting periods that ended up to the aforementioned date are stated in values that were adjusted to that date according to the changes in the general purchasing power of the Israeli currency, in accordance with opinions of the Institute of Certified Public Accountants in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. (US GAAP). Information relating to the nature and effect of such differences is presented in Note 8 to the financial statements.

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
March 20, 2005

KOST, FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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[Letterhead of Brightman Almagor & Co., a Member Firm of
Deloitte & Touche Tohmatsu]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Scopus Network Technologies Ltd

We have audited the accompanying balance sheets of Scopus Network Technologies Ltd ("the Company") as of December 31, 2004 and 2003 and the related consolidated statements of operations, changes in shareholders' equity and cash flows, for each of the three years, in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes

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consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2004 and 2003, and the consolidated results of its operations, changes in its shareholders' equity and its cash flows for the three years, in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America vary in certain respects from accounting principles generally accepted in Israel. As stated in Note 2Q, for purposes of these financial statements, the application of the latter would not have materially effected the Company's net loss for each of the three years in the period ended December 31, 2004, and its shareholders' equity and its financial position as of December 31, 2004 and 2003 as reported in these financial statements.

/s/ Brightman Almagor & Co.
Brightman Almagor & Co.
Certified Public Accountants
A member firm of Deloitte Touche Tohmatsu
Tel Aviv, Israel
February 17, 2005

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[Letterhead of Brightman Almagor & Co., a Member Firm of
Deloitte & Touche Tohmatsu]

Report Of Independent Registered Public Accounting Firm

To the Shareholders of
Koorshével Ltd

We have audited the accompanying balance sheets of Koorshével ("the Company") as of December 31, 2004 and 2003 and the related consolidated statements of operations, shareholders' equity, and cash flows, for each of the three years, in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as

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well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits and on the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of operations and cash flows of the Company for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in Israel.

As explained in Note 2(2), the financial statements for dates and reporting periods subsequent to December 31, 2003 are stated in reported amounts, in accordance with the accounting standards of the Israel Accounting Standards Board. The financial statements for dates and reporting periods ended up to the aforementioned date are stated in values that were adjusted to that date according to the changes in the general purchasing power of the Israeli currency, in accordance with opinions of the Institute of Certified Public Accountants in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America (U.S. GAAP). Information relating to the nature and effect of such differences is presented in Note 8 to the financial statements.

/s/ Brightman Almagor & Co.
Brightman Almagor & Co.
Certified Public Accountants (Isr.)
A member firm of Deloitte Touche Tohmatsu
Tel Aviv, March 9, 2005

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[Letterhead of Brightman Almagor & Co., a Member Firm of
Deloitte & Touche Tohmatsu]

Report Of Independent Registered Public Accounting Firm

To the Shareholders of
Sheraton Moriah (Israel) Ltd.

We have audited the accompanying balance sheets of Sheraton Moriah (Israel) Ltd. (the "Company") as of December 31, 2004 and 2003, and the consolidated balance sheets of the Company and its subsidiaries as at such dates, and the related statements of operations, shareholders' equity, and cash flows, for each of the three years, in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries, including those whose assets constitute 2% of the total consolidated assets as of December 31, 2003, and whose revenues constitute 12% and 18% of the total consolidated revenues for the years ended December 31, 2003 and 2002 respectively. Furthermore, we did not audit the financial statements of an affiliate accounted for by use of the equity method. The Company's equity in that affiliate's net assets as of December 31, 2004 and 2003, amounts to NIS 4.7 million and NIS 5.6 million, respectively and its shares in losses constitutes NIS 0.9 million, NIS 1.1 million and NIS 2.2 million in that affiliate's net loss for the years ended December 31, 2004, 2003 and 2002, respectively. The financial statements of those consolidated subsidiaries and the affiliate which were prepared in accordance with Israeli GAAP, were audited by other auditors whose reports thereon were furnished to us, and our opinion,

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insofar as it relates to amounts included for such subsidiaries and affiliate, before conversion to generally accepted accounting principles in the United States of America, is based solely on the reports of the other auditors.

We conducted our audits in accordance with standards of the Public Company Accounting Oversight Board (United States) as established by the Auditing Standards Board (United States) and in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits and on the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the Company and the consolidated financial position of the Company and its subsidiaries as of December 31, 2004 and 2003, and the results of operations and cash flows - of the Company and on a consolidated basis - for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in Israel.

As explained in Note 2(1), the financial statements for dates and reporting periods subsequent to December 31, 2003 are stated in reported amounts, in accordance with the accounting standards of the Israel Accounting Standards Board. The financial statements for dates and reporting periods ended up to the aforementioned date are stated in values that were adjusted to that date according to the changes in the general purchasing power of the Israeli currency, in accordance with opinions of the Institute of Certified Public Accountants in Israel.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America. The effect of the application of the latter on the consolidated financial position as of December 31, 2004 and on the consolidated results of operation for the year then ended is summarized in Note 28.

As described in Note 2 (15) to the financial statements the 2002 and 2003 annual financial statements have been restated due to an expense paid by a controlling party for the Company to a third party.

/s/ Brightman Almagor & Co.
Brightman Almagor & Co.
Certified Public Accountants (Isr.)
A member firm of Deloitte Touche Tohmatsu
Tel Aviv, March 9, 2005

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[Letterhead of Kost, Forer Gabbay & Kasierer, a Member of
Ernst & Young Global]

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Venturers of the

Joint Venture - Sheraton City Tower

We have audited the balance sheets of the Joint Venture - Sheraton City Tower ("the Joint Venture") as of December 31, 2004 and 2003, and the related statements of operations, changes in venturers' deficiency and cash flows for the years then ended (not presented separately herein). These financial statements are the responsibility of the Joint Venturer's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Joint Venture's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above, present fairly, in all material respects, the financial position of the Joint Venture as of December 31, 2004 and 2003 and the results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles in Israel (which principles differ in certain respects from accounting principles generally accepted in the United States - see Note 18).

As described in Note 2A, the financial statements as of the dates and for the reported periods subsequent to December 31, 2003, are presented in reported amounts, in conformity with Accounting Standards of the Israel Accounting Standards Board. The financial statements as of the dates and for the reported periods until the aforementioned date are presented in values that were adjusted until that date according to the changes in the general purchasing power of the Israeli currency, in accordance with pronouncements of the Institute of Certified Public Accountants in Israel.

/s/ Kost, Forer Gabbay & Kasierer

Tel-Aviv, Israel
March 2, 2005

KOST, FORER GABBAY & KASIERER
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Makhteshim-Agan Industries Ltd.

Financial Statements as at December 31, 2004

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[Letterhead of Somekh Chaikin, a Member Firm of KPMG International]

AUDITORS' REPORT TO THE SHAREHOLDERS OF
MAKHTESHIM-AGAN INDUSTRIES LTD.

We have audited the accompanying balance sheets of Makhteshim-Agan Industries Ltd. (the Company) as at December 31, 2004 and 2003, and the consolidated balance sheets of the Company and its subsidiaries as at such dates, and the related statements of income, changes in shareholders' equity and cash flows -

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Company and consolidated - for each of the three years, the last of which ended December 31, 2004. These financial statements are the responsibility of the Company's Board of Directors and its Management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of certain subsidiaries, whose assets constitute 5% and 4% of the total consolidated assets as at December 31, 2004 and 2003, respectively, and whose revenues constitute 4%, 6% and 1% of the total consolidated revenues for each of the three years last of which ended December 31, 2004, respectively. The financial statements of those subsidiaries were audited by other auditors whose reports thereon were furnished to us. Our opinion, insofar as it relates to the amounts included for those companies, is based solely on the said reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards as established by the Auditing Standards Board (United States) and in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and on the reports of other auditors, as mentioned above, the financial statements referred to above present fairly, in all material respects, the financial position of the Company and the consolidated financial position of the Company and its subsidiaries, as at December 31, 2004 and 2003, and the results of the operations, the changes in the shareholders' equity and the cash flows - Company and consolidated - for each of the three years, the last of which ended December 31, 2004, in conformity with generally accepted accounting principles in Israel. Furthermore, these statements have, in our opinion, been prepared in accordance with the Securities Regulations in Israel (Preparation of Annual Financial Statements), 1993.

Accounting principles generally accepted in Israel vary in certain significant respects from accounting principles generally accepted in the United States of America (US GAAP). Information related to the nature and effect of such differences is presented in Note 34 of the financial statements.

As explained in Note 2(A), since the Company's functional currency is the U.S. dollar, the financial statements are prepared in U.S. dollars.

Somekh Chaikin
Certified Public Accountants (Isr.)

March 8, 2005, except for Note 34, as to which the date is July 13, 2005.
Tel-Aviv, Israel

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Consolidated Balance Sheets

| | | As at December 31 | |
|--|------|-------------------|----------------|
| | | 2004 | 2003 |
| | Note | US\$ thousands | US\$ thousands |
| Current assets | | | |
| Cash and cash equivalents | | 40,477 | 49,849 |
| Short-term investments | | 1,563 | 1,100 |
| Trade receivables | 3 | 369,209 | 301,694 |
| Other receivables | 4 | 77,219 | 54,538 |
| Inventories | 6 | 460,870 | 360,993 |
| | | 949,338 | 768,174 |
| Long-term investments, loans and receivables | | | |
| | 8 | 22,070 | 18,044 |
| Fixed assets | | | |
| Cost | 9 | 824,544 | 786,416 |
| Less - accumulated depreciation | | 388,805 | 359,671 |
| | | 435,739 | 426,745 |
| Other assets and deferred charges | | | |
| | 10 | | |
| Cost | | 743,310 | 612,275 |
| Less - accumulated amortization | | 215,890 | 163,873 |
| | | 527,420 | 448,402 |
| | | 1,934,567 | 1,661,365 |

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| | Note | As at December 31 | |
|--|------|-------------------|----------------|
| | | 2004 | 2003 |
| | | US\$ thousands | US\$ thousands |
| Current liabilities | | | |
| Credit from banks | 11 | 140,021 | 142,817 |
| Trade payables | 12 | 325,945 | 243,070 |
| Other payables | 13 | 192,405 | 150,541 |
| Proposed dividend | | 11,200 | 7,000 |
| | | 669,571 | 543,428 |
| Long-term liabilities | | | |
| Loans from banks | 14 | 93,023 | 269,233 |
| Convertible debentures | 15 | 150,000 | - |
| Other long-term liabilities | 16 | 9,337 | 2,470 |
| Deferred taxes, net | 17 | 54,354 | 43,778 |
| Employee severance benefits, net | 18 | 26,709 | 24,774 |
| | | 333,423 | 340,255 |
| Minority interest | | 18,756 | 6,436 |
| Commitments and contingent liabilities | 19 | | |
| Convertible debentures | 15 | 38,322 | 77,705 |
| Shareholders' equity | 21 | 874,495 | 693,541 |
| | | 1,934,567 | 1,661,365 |

/s/ Danny Biran

Danny Biran
Chairman of the Board of Directors

/s/ Shlomo Yanai

Shlomo Yanai
Chief Executive Officer

/s/ Eli Assraf

Eli Assraf
Chief Financial Officer

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Date of approval of the financial statements: March 8, 2005, except for Note 34, as to which the

The notes and appendix to the financial statements are an integral part thereof.

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Makhteshim-Agan Industries

Company Balance Sheets

| | | As at December 31 | |
|---|------|-------------------|----------------|
| | | 2004 | 2003 |
| | Note | US\$ thousands | US\$ thousands |
| Current assets | | | |
| Cash and cash equivalents | | 2,649 | 3,000 |
| Short-term investments | | 1,900 | 5,000 |
| Other receivables | 4 | 11,699 | 12,000 |
| Loans to investee companies | 5 | 30,959 | 16,000 |
| | | 47,207 | 37,000 |
| Long-term investments, loans and receivables | | | |
| Investee companies | 7 | 1,008,999 | 735,000 |
| Bank deposits | 8 | 19,016 | 29,000 |
| Deferred taxes, net | 17 | 6,674 | 1,000 |
| | | 1,034,689 | 765,000 |
| Office furniture and equipment, net | | 601 | |
| Deferred charges | 10 | 2,458 | 1,000 |
| | | 1,084,955 | 804,000 |
| Current liabilities | | | |
| Credit from banks | 11 | - | 4,000 |
| Other payables | 13 | 6,760 | 6,000 |
| Proposed dividend | | 11,200 | 7,000 |
| | | 17,960 | 17,000 |
| Long-term liabilities | | | |
| Loans from banks | 14 | - | 12,000 |
| Convertible debentures | 15 | 150,000 | |
| Employee severance benefits, net | 18 | 4,591 | 3,000 |

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| | | | |
|--|----|-----------|------|
| | | 154,591 | 16, |
| Commitments and contingent liabilities | 19 | | |
| Convertible debentures | 15 | 37,909 | 77, |
| Shareholders' equity | 21 | 874,495 | 693, |
| | | 1,084,955 | 804, |

| | | |
|---|---|---------------------------------------|
| Danny Biran Chairman of the Board of Directors | Shlomo Yanai Chief Executive Officer | Eli Assraf Chief Financial Officer |
|---|---|---------------------------------------|

Date of approval of the financial statements: March 8, 2005, except for Note 34, as to which the

The notes and appendix to the financial statements are an integral part thereof.

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Consolidated Statements of Income

| | | For the year | |
|-------------------------------|------|------------------------|------|
| | Note | 2004 US\$ thousands | US\$ |
| Revenues | 23 | 1,539,702 | 1 |
| Cost of sales | 24 | 943,908 | |
| Gross profit | | 595,794 | |
| Expenses | | | |
| Research and development, net | 25 | 19,480 | |
| Selling and marketing | 26 | 220,212 | |
| General and administrative | 27 | 66,915 | |
| | | 306,607 | |

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| | | | |
|--|----|---------|-------|
| Operating income | | 289,187 | |
| Financing expenses, net | 28 | 27,571 | ----- |
| Income before other expenses, net | | 261,616 | |
| Other expenses, net | 29 | 42,735 | ----- |
| Income before taxes on income | | 218,881 | |
| Taxes on income | 17 | 52,334 | |
| Income after taxes on income | | 166,547 | |
| Minority interest in income of subsidiaries, net | | (1,020) | ----- |
| Net income | | 165,527 | ----- |
| | | US\$ | ----- |
| Earnings per share | 31 | | |
| Basic earnings per NIS 1 par value of shares | | 0.39 | ===== |
| Fully diluted earnings per NIS 1 par value of shares | | 0.37 | ===== |

The notes and appendix to the financial statements are an integral part thereof.

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Company Statements of Income

For the year

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| | Note | 2004 US\$ thousands | US\$ |
|---|-------|------------------------|-------|
| | ----- | ----- | ----- |
| Income | | | |
| Company's equity in income of investee companies, net | | 163,406 | |
| Management fees from investee companies | | 13,559 | |
| | | ----- | ----- |
| | | 176,965 | |
| | | ----- | ----- |
| Expenses | | | |
| Research and development, net | | - | |
| General and administrative | 27 | 15,371 | |
| | | ----- | ----- |
| | | 15,371 | |
| | | ----- | ----- |
| Operating income | | 161,594 | |
| Financing income, net | 28 | (5,036) | |
| | | ----- | ----- |
| Income before other expenses (income), net | | 166,630 | |
| Other expenses (income), net | | 1,850 | |
| Income before taxes on income (tax benefit) | | 164,780 | |
| Taxes on income (tax benefit) | 17 | (747) | |
| | | ----- | ----- |
| Net income | | 165,527 | |
| | | ===== | ===== |
| | | | |
| | | US\$ | |
| | | ----- | ----- |
| Earnings per share | 31 | | |
| Basic earnings per NIS 1 par value of shares | | 0.39 | |
| | | ===== | ===== |
| Fully diluted earnings per NIS 1 par value of shares | | 0.37 | |
| | | ===== | ===== |

The notes and appendix to the financial statements are an integral part thereof.

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Makhteshim-

Statements of Changes in Shareholders' Equity

| | Share capital | Premium on shares | Receipts issuance opt |
|--|------------------|----------------------|-----------------------------|
| | US\$ thousands | US\$ thousands | US\$ thous |
| Balance as of December 31, 2001 | 101,757 | 357,090 | 4, |
| Employee options exercised | 47 | 234 | |
| Adjustments deriving from translation of financial statements of investee companies | - | - | |
| Realization of Company shares held by a subsidiary (see Note 21C) | - | - | |
| Capital reserve from acquisition of convertible debenture by a subsidiary | - | - | |
| Dividend | - | - | |
| Proposed dividend subsequent to the balance sheet date | - | - | |
| Net income for the year ended December 31, 2002 | - | - | |
| Balance as of December 31, 2002 | 101,804 | 357,324 | 4, |
| Employee options exercised | 581 | (581) | |
| Conversion of convertible debentures into shares | 1,270 | 11,331 | |
| Options exercised | 138 | 1,469 | (|
| Adjustments deriving from translation of financial statements of investee companies | - | - | |
| Dividend | - | - | |
| Proposed dividend | - | - | |
| Proposed dividend subsequent to the balance sheet date | - | - | |
| Net income for the year ended December 31, 2003 | - | - | |
| Balance as of December 31, 2003 | 103,793 | 369,543 | 3, |
| Employee options exercised | 578 | (578) | |
| Conversion of convertible debentures into shares | 3,974 | 35,581 | |
| Options exercised | 913 | 9,637 | (|
| Adjustments deriving from translation of financial statements of investee companies | - | - | |
| Realization of Company shares held by a subsidiary (see Note 21C) | - | 3,304 | |
| Dividend | - | - | |
| Proposed dividend | - | - | |
| Proposed dividend subsequent to the balance sheet date | - | - | |
| Net income for the year ended December 31, 2004 | - | - | |
| Balance as of December 31, 2004 | 109,258 | 417,487 | 3, |

Composition of capital reserves: *

Capital reserve in the framework of the arrangement plan (Note 1B(2))

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Adjustments deriving from translation of financial statements of investees
 Adjustment of commitment to purchase Company shares
 Capital reserve from acquisition of convertible debentures by a subsidiary

[table continued]

| | Proposed dividend subsequent to balance sheet date | Retained earnings | Comp shares h by subsidi |
|--|--|----------------------------------|--------------------------------|
| | ----- US\$ thousands ----- | ----- US\$ thousands ----- | ----- US\$ thousa ----- |
| Balance as of December 31, 2001 | - | 115,862 | (18,0 |
| Employee options exercised | - | - | |
| Adjustments deriving from translation of financial statements of investee companies | - | - | |
| Realization of Company shares held by a subsidiary (see Note 21C) | - | - | 2,5 |
| Capital reserve from acquisition of convertible debenture by a subsidiary | - | - | |
| Dividend | - | (8,500) | |
| Proposed dividend subsequent to the balance sheet date | 9,500 | (9,500) | |
| Net income for the year ended December 31, 2002 | - | 60,078 | |
| | ----- | ----- | ----- |
| Balance as of December 31, 2002 | 9,500 | 157,940 | (15,4 |
| Employee options exercised | - | - | |
| Conversion of convertible debentures into shares | - | - | |
| Options exercised | - | - | |
| Adjustments deriving from translation of financial statements of investee companies | - | - | |
| Dividend | (9,500) | (16,600) | |
| Proposed dividend | - | (7,000) | |
| Proposed dividend subsequent to the balance sheet date | 7,200 | (7,200) | |
| Net income for the year ended December 31, 2003 | - | 102,774 | |
| | ----- | ----- | ----- |
| Balance as of December 31, 2003 | 7,200 | 229,914 | (15,4 |
| Employee options exercised | - | - | |
| Conversion of convertible debentures into shares | - | - | |
| Options exercised | - | - | |
| Adjustments deriving from translation of financial statements of investee companies | - | - | |
| Realization of Company shares held by a subsidiary (see Note 21C) | - | - | 4,1 |
| Dividend | (7,200) | (25,700) | |
| Proposed dividend | - | (11,200) | |
| Proposed dividend subsequent to the balance sheet date | 12,700 | (12,700) | |
| Net income for the year ended December 31, 2004 | - | 165,527 | |
| | ----- | ----- | ----- |
| Balance as of December 31, 2004 | 12,700 | 345,841 | (11,2 |
| | ===== | ===== | ===== |

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Composition of capital reserves: *

Capital reserve in the framework of the arrangement plan (Note 1B(2))
 Adjustments deriving from translation of financial statements of investees
 Adjustment of commitment to purchase Company shares
 Capital reserve from acquisition of convertible debentures by a subsidiary

The notes and appendix to the financial statements are an integral part thereof.

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Consolidated Statements of Cash Flows

| | For the year | |
|---|----------------|------|
| | 2004 | |
| | US\$ thousands | US\$ |
| Cash flows from operating activities | | |
| Net income | 165,527 | |
| Adjustments to reconcile net income to net cash flows from operating activities (see A. below) | 50,126 | |
| | 215,653 | |
| Net cash provided by operating activities | | |
| Cash flows from investing activities | | |
| Acquisition of fixed assets | (38,823) | |
| Investment grant received | 686 | |
| Additions to other assets and deferred charges, net | (33,749) | |
| Purchase of products and intangible assets | - | |
| Short-term investments, net | (463) | |
| Investments in newly consolidated companies (see B. below) | (72,152) | |
| Proceeds from disposal of fixed and other assets | 574 | |
| Proceeds from sale of long-term investments | 2,819 | |
| Other long-term investments | (828) | |
| Acquisition of minority interest in subsidiaries | (1,056) | |
| | (142,992) | |
| Net cash used in investing activities | | |
| Cash flows from financing activities | | |
| Receipt of long-term loans from banks | 24,700 | |
| Repayment of long-term loans and liabilities from banks and others | (227,851) | |

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| | |
|---|----------|
| Issuance of convertible debentures less issuance expenses | 147,450 |
| Realization (acquisition) of Company debentures by a subsidiary | - |
| Increase (decrease) in short-term credit from banks and others, net | 4,222 |
| Proceeds from options exercised | 9,647 |
| Proceeds from employee options exercised | - |
| Dividend to shareholders | (39,900) |
| Dividend to minority shareholders in subsidiaries | (301) |
| | ----- |
| Net cash (used in) provided by financing activities | (82,033) |
| | ----- |
| Translation differences in respect of cash in autonomous units | - |
| | ----- |
| Decrease in cash and cash equivalents | (9,372) |
| Cash and cash equivalents at beginning of the year | 49,849 |
| | ----- |
| Cash and cash equivalents at end of the year | 40,477 |
| | ===== |

The notes and appendix to the financial statements are an integral part thereof.

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Consolidated Statements of Cash Flows (cont'd)

| | For the year | |
|---|----------------|-------|
| | 2004 | |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| A. Adjustments to reconcile net income to net cash flows from operating activities: | | |
| Revenues and expenses not affecting operating cash flows | | |
| Depreciation and amortization | 82,624 | |
| Adjustment of long-term liabilities to banks and others | 1,791 | |
| Minority interest in income of subsidiaries, net | 998 | |
| Increase in employee severance benefits, net | 1,973 | |
| Deferred taxes, net | (163) | |
| Amortization of discount on convertible debentures | 916 | |
| Capital loss on disposal of fixed and other assets, net | 511 | |
| Provision for loss with respect to options granted to employees of subsidiaries | 2,090 | |
| Gain on issuance of a subsidiary to a third party | (926) | |

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| | |
|--|----------|
| Changes in operating assets and liabilities | |
| Decrease (increase) in trade and other receivables | (53,236) |
| Increase in inventories | (69,345) |
| Increase (decrease) in trade and other payables | 82,893 |
| | ----- |
| | 50,126 |
| | ===== |

B. Investments in newly consolidated companies

| | |
|---|----------|
| Working capital (excluding cash and cash equivalents) | (6,485) |
| Fixed assets, net | (2,258) |
| Other assets, net | (63,081) |
| Goodwill created on acquisition | (41,851) |
| Long-term liabilities | 33,896 |
| Contingent liability | - |
| Exercise of Company shares held by a subsidiary | 7,500 |
| Minority interest | 6,398 |
| | ----- |
| | (65,881) |

| | |
|---|----------|
| Repayment of liability in respect of investee company previously acquired | (6,271) |
| | ----- |
| | (72,152) |
| | ===== |

C. Non-cash activities

| | |
|--|-------|
| Acquisition of other assets on supplier credit | 6,287 |
| | ===== |
| Acquisition of fixed assets on supplier credit | - |
| | ===== |

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Consolidated Statements of Cash Flows

| | For the year | |
|--|----------------|---------|
| | 2004 | |
| | ----- | ----- |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| Cash flows from operating activities | | |
| Net income | | 165,527 |
| Adjustments to reconcile net income to cash flows from | | |

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| | | |
|---|-----------|-------|
| operating activities (see A. below) | (130,946) | |
| | ----- | ----- |
| Net cash provided by operating activities | 34,581 | |
| | ----- | ----- |
| Cash flows from investing activities | | |
| Investment in investee companies | (3,938) | |
| Long-term loans to investee companies | (135,582) | |
| Repayment of long-term loans to investee companies | - | |
| Short-term credit to investee companies, net | (9,056) | |
| Acquisition of fixed assets | (431) | |
| Investment in short-term bank deposits, net | 3,554 | |
| Realization of long-term bank deposits | 10,000 | |
| Proceeds from sales of fixed assets | 8 | |
| | ----- | ----- |
| Net cash (used in) provided by investing activities | (135,445) | |
| | ----- | ----- |
| Cash flows from financing activities | | |
| Issuance of convertible debentures less issuance expenses | 147,450 | |
| Proceeds from options exercised | 9,647 | |
| Dividend to shareholders | (39,900) | |
| Proceeds from employee options exercised | - | |
| Receipt of long-term loans from banks | - | |
| Repayment of long-term loans from banks | (16,875) | |
| Receipt of long-term loan from investee company | - | |
| Increase (decrease) in short-term credit from banks, net | - | |
| | ----- | ----- |
| Net cash (used in) provided by financing activities | 100,322 | |
| | ----- | ----- |
| Increase (decrease) in cash and cash equivalents | (542) | |
| Cash and cash equivalents at beginning of the year | 3,191 | |
| | ----- | ----- |
| Cash and cash equivalents at end of the year | 2,649 | |
| | ===== | ===== |

The notes and appendix to the financial statements are an integral part thereof.

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Consolidated Statements of Cash Flows

| | | | |
|--|----------------|--------------|-------|
| | | For the year | |
| | | ----- | ----- |
| | | 2004 | |
| | | ----- | ----- |
| | US\$ thousands | | US\$ |
| | | ----- | ----- |

A. Adjustments to reconcile net income to net cash

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flows from operating activities

Revenues and expenses not affecting operating cash flows:

| | |
|---|-----------|
| ----- | |
| Depreciation and amortization | 1,235 |
| Capital loss (gain) on disposal of fixed assets | 25 |
| Company's equity in undistributed earnings of investee companies, net | (122,931) |
| Increase in employee severance benefits, net | 680 |
| Amortization of discount on convertible debentures | 916 |
| Adjustment of long-term investments | (5,333) |
| Adjustment of long-term bank loans | - |
| Deferred taxes, net | (749) |
| | |
| Changes in operating assets and liabilities: | |
| ----- | |
| Decrease (increase) in other receivables | (5,143) |
| Increase (decrease) in other payables | 354 |
| | ----- |
| | (130,946) |
| | ===== |

The notes and appendix to the financial statements are an integral part thereof.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 1 - General

- | | | |
|-----|--|--|
| A. | Definitions | |
| (1) | The Company | - Makhteshim-Agan Industries Ltd. |
| (2) | The Group | - Makhteshim-Agan Industries Ltd. and its investees. |
| (3) | Subsidiaries | - Companies, including partnerships, whose financial statements are fully consolidated, directly or indirectly, with the financial statements of the Company. |
| (4) | Proportionately consolidated companies | - Companies, including partnerships, whose financial statements are consolidated, directly or indirectly, with those of the Company by the proportionate consolidation method. |
| (5) | Investees | - Subsidiaries and proportionately consolidated companies. |

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- (6) Related parties - As defined in Opinion 29 of the Institute of Certified Public Accountants in Israel.
- (7) Interested parties - As defined in Paragraph (1) of the definition of an "interested party" in a corporation, in Section 1 of the Securities Law, 1968.
- (8) Controlling shareholders - As defined in the Securities Regulations (Financial Statement Presentation of Transactions between a Company and a Controlling Shareholder Therein), 1996.
- (9) CPI - The Consumer Price Index as published by the Central Bureau of Statistics.
- (10) Dollar - The US dollar.

B. Description of the Company and its activity

1. The Company is engaged through its local and foreign investee companies primarily in the manufacture and marketing of pesticides, intermediate materials for other industries and synthetic fragrances, mainly for export. The Company is held by Koor Industries Ltd. (Koor). As at December 31, 2004, Koor holds 38.6% of the Company's shares whereas on December 31, 2003, Koor held 48.6% of the Company's shares. In addition, at that time Koor had a voting agreement, that was not of a temporary nature, with two other shareholders who hold together 3.82% of the Company's shares. In July 2004, the voting agreements was cancelled.

The Company was established on December 8, 1997 for the purpose of executing a plan for implementing changes in the holdings in Makhteshim Chemical Works Ltd. (Makhteshim) and Agan Chemical Industries Ltd. (Agan), as described below.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 1 - General (cont'd)

- B. Description of the Company and its activity (cont'd)
- 2. On April 26, 1998, the shareholders of Makhteshim and of Agan approved an exchange arrangement, the substance of which was a change in the structure of holdings in the Makhteshim-Agan Group. Prior to the implementation of the arrangement, Makhteshim was a 67% subsidiary of Koor, Makhteshim held a 46.6% interest in Agan and Koor held a 5% direct interest in Agan.

On May 4, 1998, the Court approved the arrangement, which was consummated pursuant to the provisions of Section 233 of the

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Companies Ordinance (New Version). On May 7, 1998, the shares of Makhteshim and of Agan were delisted from the Tel-Aviv Stock Exchange and on May 11, 1998, trading commenced in the shares of the Company.

On May 10, 1998, the following actions were taken pursuant to the approved exchange arrangement:

- The Company issued shares to all of the shareholders of Makhteshim and of Agan (except in respect of the shares of Agan held by Makhteshim) in exchange for the transfer to the Company of the shares of Makhteshim and Agan held by them.
- Pursuant to the exchange ratio that was determined (based on the opinion of economic appraisers), the shareholders of Makhteshim received 2.446 shares of the Company for each share of Makhteshim, and the shareholders of Agan (excluding Makhteshim) received 10.247 shares of the Company for each share of Agan.

Following the implementation of the above-mentioned transactions, the Company fully owns and controls Makhteshim and Agan.

Note 2 - Reporting Principles and Accounting Policy

A. Financial statements in US dollars

General:

The Company and its Israeli subsidiaries maintain their current accounting records in nominal shekels and dollars using a multi-currency system. Since most of the Group's revenues are received in dollar and the principal raw materials and fixed assets are purchased in dollar. The dollar is the principal currency of the economic environment in which the Group operates ("the functional currency"). Accordingly, the dollar is the measurement and reporting currency in these financial statements. It should not be construed that the translated amounts actually represent or can be converted into dollars, unless otherwise indicated in these statements.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

A. Financial statements in US dollars (cont'd)

1. Balance sheet:

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- a) Non-monetary items (items, the stated amounts of which reflect their historical value upon acquisition or creation) that were acquired in a currency other than the dollar, were translated according to the exchange rate of the dollar on their date of acquisition or creation. The following items were treated as non-monetary items: fixed assets and the related accumulated depreciation, inventory, other assets, deferred expenses and the related accumulated amortization, and shareholders' equity items which derive from funds invested by shareholders.

The amounts of the non-monetary assets do not necessarily represent their realizable value or current economic value, rather only the original dollar cost thereof in nominal values.

- b) The net asset value of investments in investees and the minority interest in consolidated subsidiaries are determined on the basis of the dollar translated financial statements of those companies.
- c) Monetary items (items, the amounts of which as stated in the balance sheet reflect current or realizable values, as at the balance sheet date) were translated into dollars at the exchange rate at the balance sheet date.

2. Statement of income:

-
- a) The components of the statement of income reflecting transactions carried out during the year - sales, purchases, labor costs, etc. - in a currency other than the dollar, were translated according to the exchange rate of the dollar on the date of the cash flow. The erosion in monetary balances is included in the specific expense or income items to which they relate.
- b) The components of the statement of income relating to non-monetary balance sheet items have been translated according to the same exchange rate used for translating the related balance sheet items (mainly: changes in inventory, depreciation and amortization, capital gain, etc.).
- c) Company equity in operating results of investees is determined on the basis of the financial statements of those companies.
- d) Taxes on income:

Current taxes are composed of payments on account during the year, plus amounts due as at the balance sheet date (or net of amounts refundable at the balance sheet date). The payments on account were translated according to the exchange rate of the dollar on the date of each payment, while the amounts due or refundable are included without adjustment. Therefore, current taxes also include

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the expense or income resulting from the erosion of the payments on account, from the payment date until the balance sheet date. Deferred taxes - see Note 2R and Note 17G.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

B. Proposed dividend subsequent to the Balance Sheet Date

Pursuant to Accounting Standard No. 7, "Events Occurring Subsequent to the Balance Sheet Date", a liability which relates to a dividend proposed or declared subsequent to the balance sheet date, is reflected in the financial statements only in the period declared. In addition, separate expression of the amount of the dividend intended for distribution is provided as part of the statement of changes in shareholders' equity, as stated, against reduction of the retained earnings' balance.

C. Foreign investee companies

As of January 1, 2004, the Company applies Accounting Standard No. 13, "Effect of changes in Exchange Rates of Foreign Currency". The Standard discusses the translation of transactions in foreign currency and the translation of financial statements of foreign operations for purposes of including them in the financial statements of the reporting entity. The Standard provides rules for classifying foreign operations as an autonomous foreign investee or as an integrated investee, on the basis of the indications described in the standard and the use of discretion, and it provides the method for translating the financial statements of autonomous foreign investees.

The financial statements of foreign investees that are integral to the Group's operations based on the criteria provided in Accounting Standard No. 13, are translated into dollars as follows: non-monetary items in the balance sheet are translated at the historical exchange rates as at the transaction date whereas monetary balance sheet items are translated at the exchange rate in effect on the balance sheet date. Items in the statement of income are translated at average exchange rates, except for revenues and expenses relating to non-monetary items that were translated based on the historical exchange rates according to which the corresponding non-monetary items were translated. Translation differences are recorded in the statement of income.

The financial statements of foreign investees that operate as "autonomous entities" based on the criteria provided in Accounting Standard No. 13, are translated into dollars as follows: monetary and non-monetary balance sheet items are translated based on the closing exchange rate. Items in the statement of income are translated at the exchange rate on the transaction date. Translation differences are

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recorded in the statement of income in a separate category in the shareholders' equity section ("adjustments deriving from translation of financial statements of investee companies") up to the time of realization of the net investment.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

- D. Consolidated financial statements
- (1) The financial statements of the Company are consolidated with the statements of those companies that it controls. Companies, which are under joint control, are consolidated by the proportionate consolidation method.
 - (2) A list of companies whose financial statements are included in the consolidated statements as well as the rate of control and ownership thereof, is presented in the appendix to the financial statements.
 - (3) For purposes of the consolidation, the amounts appearing in the financial statements of the subsidiaries were taken into account, after the adjustments required by the application of the uniform accounting policies used by the Group.
 - (4) The excess of the cost of investments in subsidiaries over the fair value of identified assets, less the identified liabilities (net of taxes in respect of temporary differences) at the date of acquisition, is recorded as goodwill.

The goodwill is presented in the consolidated balance sheet in the category "other assets and deferred charges" and is amortized in the "other expenses" item (regarding the amortization period, see Section L., below).
 - (5) The consolidated financial statements include the share of assets, liabilities, income and expenses of proportionately consolidated subsidiaries, based on the percentage interest held in these companies.
 - (6) Material intercompany balances and transactions, including profits on intercompany sales which have not yet been realized outside the Group, are eliminated in consolidation.
- E. Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and

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expenses during the reporting period. Actual results could differ from those estimates.

F. Cash equivalents

Cash equivalents include short-term bank deposits with an original maturity not exceeding three months.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

G. Short-term investments

Marketable securities held as a short-term investment are stated at their market value as at balance sheet date. Changes in the value of the marketable securities are fully recognized on a current basis.

H. Allowance for doubtful accounts

The financial statements include an allowance for specific doubtful accounts which fairly reflects, in management's estimation, the loss expected from receivables the collection of which is doubtful. Management determines the allowance, based, in part, on an evaluation of credit risk using available information regarding the financial position of the debtors, the extent of their activities and evaluation of collateral received from them. The financial statements include specific allowances for doubtful accounts and, as mentioned in section I below, with respect to trade receivables included in the framework of a subordinated capital note received as part of a securitization transaction.

I. Sale of financial assets

The sale of financial assets is recognized as a sale when control over the asset is transferred in full to an independent third party, and the full amount of the risks and rewards embodied by the asset are transferred to an independent third party.

J. Inventories

Inventories are valued at the lower of cost or market, cost being determined as follows:

- Raw materials, packing materials, purchased products, spare parts and maintenance materials on the "moving average" basis.
- Finished products and work in progress on the basis of

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average production cost including materials, labor and manufacturing expenses.

- K. Investments in investee companies
- (1) Investments in investee companies are stated in the Company's balance sheet according to the equity method. In determining the net asset value of the investments in these companies, the amounts taken into account are based on the financial statements of these companies, after making the adjustments thereto required by the application of generally accepted accounting principles.
 - (2) Regarding goodwill amortization - see Note 2M.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

- L. Fixed assets
- (1) The fixed assets are presented at cost.
 - (2) The cost of assets includes financing expenses related to the financing of their construction during the pre-operation period. The financing expenses were capitalized as follows:
 - A. Where the assets under construction are financed by specific credit - the financing expenses relating to such credit.
 - B. Where the financing is not made by specific credit - by using a rate representing the weighted average cost rate of the credit sources, the cost of which was not specifically capitalized.
 - (3) The cost of the self-constructed assets includes materials and labor costs during the pre-operation period.
 - (4) The cost of assets with respect to which an investment grant was received is presented after deduction of the investment grant received with respect thereto. The investment grant is amortized to the statement of income based on the rate of depreciation of the assets in respect of which it was received.
 - (5) Depreciation is computed by the straight-line method over the estimated useful lives of the assets. Annual rates of depreciation are:

| | % |
|--------------------------------|----------------|
| Leasehold rights and buildings | ----- 2 - 4 |

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| | | |
|----------------------------------|---------|-------------|
| Plant and equipment | 4.5 | |
| Motor vehicles | 15 - 20 | |
| Office furniture and equipment | 6 - 15 | (mainly 7%) |
| Computer and auxiliary equipment | 20 - 33 | |

M. Other assets and deferred charges

Other assets and deferred charges are amortized by the straight-line method over the expected benefit period as follows:

- Product registration and acquisition of know-how - mainly eight years.
- Goodwill arising on the acquisition of subsidiaries - ten or twenty years (mainly twenty years).
- Intangible assets in purchase of products and companies - mainly twenty years.
- Marketing rights - five years to ten years.
- Debenture issuance expenses - six years.
- Non-competition and confidentiality agreement - five years.

The amortization periods are re-examined from time to time in accordance with the estimated expected benefit period of the assets.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

N. Debentures convertible into shares

Debentures convertible into shares are included in the balance sheet based on the probability of their conversion, as provided in Opinion 53 of the Institute of Certified Public Accountants in Israel. Debentures, the conversion of which is not probable, are included as a liability at their liability amount. Debentures, the conversion of which is probable, are stated between the items "long-term liabilities" and "shareholders' equity", in accordance with the higher of the liability or capital value.

Convertible debentures issued by the Company and held by a subsidiary, are included net of the liability value of the debentures issued. The difference between the acquisition cost and the liability value which was deducted, is recorded in a capital reserve in the shareholders' equity category.

O. Company shares held by subsidiary

Company shares held by a subsidiary are stated at cost, as a deduction

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from the Company's shareholders' equity.

P. Revenue recognition

Revenues from sales of products are recognized upon shipment to the customer along with transfer of the main risks involved with ownership of the products sold.

Q. Research and development costs

Research and development costs, net of grants and participations, are charged to the statement of income as incurred. The net research and development expenses are presented separately in the statement of income after gross profit.

R. Deferred taxes

The Group companies create deferred taxes in respect of temporary differences. The temporary differences are differences in the value of assets and liabilities for tax purposes and for financial reporting purposes. Allocation of the taxes, as stated, is executed with respect to the differences applying to assets, the amortization of which is deductible for tax purposes.

The deferred tax balances (asset or liability) are calculated according to the liability approach, i.e., the tax rates expected to be in force when the deferred tax liability is utilized, or when the deferred tax asset is realized, as they are known proximate to the date of approval of the financial statements.

In calculation of the deferred taxes, no account was taken of the taxes, which would apply in a case of sale of the investments in the investee companies, since it is the intention of the Company to hold these investments and not to sell them.

The Group may be subject to additional tax in a case of distribution of dividends between the Group companies. This additional tax was not provided for in the financial statements in cases where Group policy is not to distribute a dividend which involves additional tax to the Group.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

S. Earnings per share

The earnings per share data is calculated in accordance with opinion No. 55 of the Institute of Certified Public Accountants in Israel, retroactively adjusted for the bonus element in the issuance of rights, and taking into consideration the likelihood of the exercise

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of option warrants and convertible debentures issued by the Company.

T. Derivative financial instruments

The results of derivative financial instruments held as hedge for existing assets and liabilities are recognized concurrently with the results of the hedged assets and liabilities.

The results of derivative financial instruments held as a hedge for firm commitments are deferred, and are recognized in the same period in which the results from the hedged transactions are recognized.

Derivative financial instruments, which are not earmarked for hedging purposes, are presented in the balance sheet based on their fair value. Changes in fair value are recorded in the statement of income in the period in which they occur.

The fair value of derivative financial instruments is determined based on their market value, and in the absence of such a price, fair value is determined based on a valuation model.

U. Environmental costs

The ongoing cost of maintenance and operation of facilities for the prevention of environmental pollution and projected provisions for environment rehabilitation costs stemming from current or past activities, are charged to expense as incurred. The cost of constructing facilities to prevent pollution, which increase the life expectancy of a facility or its efficiency, or decrease or prevent pollution, are charged to the cost of fixed assets and are depreciated according to the usual depreciation rates used by the Group.

V. Impairment in value of assets

The Company applies Accounting Standard No. 15 - Impairment in Value of Assets (hereinafter - "Standard"). The Standard provides procedures which a company must apply in order to ensure that its assets in the consolidated balance sheet (to which the Standard applies), are not presented at an amount which is in excess of their recoverable value, which is the higher of the net selling price or the realization value (the present value of the estimated future cash flows expected to be derived from use and disposal of the asset).

The Standard applies to all the assets in the consolidated balance sheet, except for tax assets and monetary assets. In addition, the Standard provides rules for presentation and disclosure with respect to assets whose value has declined. Where the value of an asset in the balance sheet is greater than its recoverable value, the Company recognizes a loss from impairment in value in an amount equal to the difference between the book value of the asset and its recoverable value. The loss recognized, as stated, will be eliminated only if there have been changes in the estimates used in determining the asset's recoverable value from the date on which the last loss from impairment in value was recognized.

W. Balances in foreign currency and linked balances

Balances in or linked to foreign currency are included in the

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financial statements at the representative exchange rates on the balance sheet date. Balances linked to the Consumer Price Index are included on the basis of the index relevant to each linked asset or liability.

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Notes to the Financial Statements as at December 31, 2004

Note 2 - Reporting Principles and Accounting Policy (cont'd)

W. Balances in foreign currency and linked balances (cont'd)

Data regarding the representative exchange rate of the US dollar and the Consumer Price Index are as follows:

| | Consumer Price Index (Points) | Exchange rate of the US dollar against the NIS | Exchange rate of the US dollar against the Brazilian real | Excha of the U aga |
|------------------------------|--|---|--|--------------------------|
| As at | | | | |
| December 31, 2004 | 107.44 | 4.308 | 2.654 | |
| December 31, 2003 | 106.16 | 4.379 | 2.889 | |
| Changes during the year: | | | | |
| 2004 | 1.21% | (1.62%) | (8.13%) | |
| 2003 | (1.9%) | (7.5%) | (18.2%) | |
| 2002 | 6.5% | 7.3% | 52.3% | |

X. Disclosure of the impact of new accounting standards in the period prior to their application

In July 2004, the Israeli Accounting Standards Board published Accounting Standard No. 19, "Taxes on Income". The Standard provides that a liability for deferred taxes is to be recorded for all temporary differences subject to tax, except for a limited number of exceptions. In addition, a deferred tax asset is to be recorded for all temporary differences that may be deducted, losses for tax purposes and tax benefits not yet utilized, if it is anticipated that there will be taxable income against which they can be offset, except for a limited number of exceptions. The new Standard applies to financial statements for periods beginning on January 1, 2005. The Standard provides that it is to be implemented by means of a cumulative effect of a change in accounting method. First time application of the said Standard will have a net non-recurring impact, as at January 1, 2005, of increasing the net income by approximately US\$ 11.6 million (which mainly derives from recording deferred taxes in respect of unrealized profits which are anticipated to be realized in the near future).

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Note 3 - Trade Receivables

Consolidated

Composition:

| | December |
|---|-------------------------|
| | ----- 2004 ----- |
| | US\$ thousands ----- |
| Open accounts - | |
| Foreign | 312,661 |
| Domestic (Israel) | 14,812 |
| Checks receivable | 5,796 |
| Subordinated capital note and receivables related to sale of trade receivables in a securitization transaction (1) | 60,586 |
| | ----- |
| | 393,855 |
| Net of allowance for doubtful debts | 24,646 |
| | ----- |
| | 369,209 |
| | ===== |

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Makhteshim-Aga

Notes to the Financial Statements as at December 31, 2004

Note 3 - Trade Receivables (cont'd)

(1) Sale of trade receivables in a securitization transaction:

| | December |
|--|-------------------------|
| | ----- 2004 ----- |
| | US\$ thousands ----- |
| Trade receivables included in the securitization transaction as at the balance sheet date | 202,832 |
| Less - proceeds in respect of such receivables, net (*) | 141,654 |
| Subordinated capital note | 61,178 |
| Trade receivables which were collected and the proceeds in respect thereof were paid subsequent to the balance sheet date, net | (592) |
| Subordinated capital note and receivables related to sale of trade receivables in a securitization transaction | 60,586 |

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(*) As at the balance sheet date cash proceeds in the amount of US\$ 142.2 million were received in respect of the sale of trade receivables in a securitization transaction (December 31, 2003 - approximately US\$ 125.3 million).

In October 2001, the Company and certain subsidiaries signed an agreement according to which those companies entered into a securitization transaction, under which such companies sold all their trade receivables to foreign companies, which were incorporated for this purpose and which are not owned or controlled by the Makhteshim Agan Industries Group (hereinafter - "the Target Companies"). The purchase of the debts by the purchasing companies was financed by Kitty Hawk Funding Corp., a US corporation of the Bank of America Group.

On September 28, 2004, the Company and subsidiaries signed an agreement with Bank of America to end the undertaking in the securitization transaction. On the same date, the Company and certain subsidiaries (hereinafter - "the Companies") entered into a new agreement with Rabobank International for sale of customer receivables in the framework of a securitization transaction, this being in place of the prior agreement with Bank of America. The new agreement is similar in principle to the prior agreement with certain changes including, among others, that in the new agreement additional Company subsidiaries are included in the transaction. Pursuant to the new securitization agreement, the Companies will sell their trade receivables to a foreign company which was set up for this purpose and which is not owned or controlled by the Makhteshim Agan Industries Group (hereinafter - "the Acquiring Company").

Acquisition of the trade receivables by the Acquiring Company will be financed by a U.S. company, Erasmus Capital Corporation, of the Rabobank International Group. At the time of transition from the prior agreement to the new agreement the Acquiring Company purchased the trade receivables that remained in the ownership of the Target Companies. Trade receivables included in the securitization transaction are those who stand in compliance with a number of criteria, as determined in the agreement.

The maximum expected volume of the financial means available to the Acquiring Company for the purpose of purchasing the trade receivables of the consolidated subsidiaries, is US\$ 250 million (as opposed to US\$ 150 million in the former securitization agreement) on a current basis, such that the amounts to be collected from customers whose debts were sold, will serve to purchase new trade receivables.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 3 - Trade Receivables (cont'd)

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- (1) Sale of trade receivables in a securitization transaction: (cont'd)

The period in which the Companies will sell their trade receivables to the Acquiring Company is one year from the date of the closing of the transaction. The period may be extended, with the consent of both parties, for additional one-year periods, up to a maximum of 4 extensions.

The price at which the trade receivables will be sold is the amount of the debt being sold less an amount calculated on the basis of the period anticipated to pass between the date the debt was sold and the repayment date.

On the date of purchasing the debt, the acquiring company will pay in cash the major part of the debt price. The balance of the debt price will be embodied in a subordinated capital note to be paid after the debt is collected. The rate of the cash payment will vary in accordance with the composition of the client portfolio and its performance.

The Company shall bear in full losses sustained by acquiring companies due to the non-payment of the trade receivables included in the securitization transaction, up to the amount of the total outstanding balance of the debt included in the subordinated capital note.

The acquiring company will not have a right of recourse to the Companies with respect to the amounts paid in cash, except in the case of debts in respect of which a commercial dispute arises between the Companies and their customers, namely, a dispute arising from an alleged failure to comply with an obligation of the seller in the supply agreement for the product, such as: failure to supply the correct product, defect in the product, non-compliance with the supply date, etc.

The Companies will handle for the acquiring company the collection of the sold trade receivables included as part of the securitization transaction.

The main principle of the accounting treatment of the sale of trade receivables in a securitization transaction is the recognition of the sale of only that part of the debt where the risk and control thereof has been finally and absolutely transferred to the buyer. Accordingly, trade receivables sold were deleted where the consideration in respect thereof had been received in cash and/or by a non-deferred liability. With respect of that part of the trade receivables included in the securitization transaction, which was not recognized as a sale, a subordinated capital note receivable was recorded in the amount of the difference between the amount of trade receivables included in the transaction and the amounts of consideration received, as above, and receivables were recorded in respect of the debts sold where the consideration in respect thereof was received subsequent to the balance sheet date.

The loss on sale of the trade receivables is recognized at the date of sale and is reflected in the item "other expenses".

As part of the agreement, the Company committed to maintain certain financial ratios, mainly, debt to equity and profitability

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ratios - see Note 20C.

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Notes to the Financial Statements as at December 31, 2004

Note 4 - Other Receivables

| | Consolidated | | US\$ |
|--|----------------|----------------|------|
| | December 31 | | |
| | 2004 | 2003 | |
| | US\$ thousands | US\$ thousands | |
| Claims from the government in respect of participations and tax refunds | 28,277 | 15,410 | |
| Advance tax payments, net of provisions | 11,071 | 7,895 | |
| Employees (1) | 1,376 | 1,259 | |
| Deferred taxes (Note 17G) | 17,037 | 10,256 | |
| Current maturities of long-term receivables | 420 | 380 | |
| Prepaid expenses and accrued income | 10,372 | 9,819 | |
| Dividend receivable | - | - | |
| Other | 8,666 | 9,519 | |
| | 77,219 | 54,538 | |
| (1) Includes a non-linked bank deposit designated for the purpose of granting loans to employees and bearing annual interest at the rate of 5% | 417 | 566 | |

Note 5 - Loans to Investee Companies

Company

| | December 31 | |
|---------------------------------------|----------------|----------------|
| | 2004 | 2003 |
| | US\$ thousands | US\$ thousands |
| Current maturities of long-term loans | - | 4,500 |

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| | | |
|----------------------|--------|--------|
| Short-term loans (1) | 16,056 | 2,500 |
| Current accounts (2) | 14,903 | 9,111 |
| | ----- | ----- |
| | 30,959 | 16,111 |
| | ===== | ===== |

- (1) The loan is a dollar loan and bears interest of 1.8% - 2.4%.
(2) The accounts are mainly linked to the US dollar and are non-interest bearing.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 6 - Inventories

Consolidated

| | December 31 | |
|---------------------------------------|----------------|----------------|
| | 2004 | 2003 |
| | ----- | ----- |
| | US\$ thousands | US\$ thousands |
| | ----- | ----- |
| Finished products | 263,579 | 225,678 |
| Work in progress | 29,117 | 23,772 |
| Raw materials | 115,046 | 76,100 |
| Packing materials | 4,863 | 3,078 |
| Spare parts and maintenance materials | 12,820 | 13,739 |
| | ----- | ----- |
| Purchased products | 425,425 | 342,367 |
| | 35,445 | 18,626 |
| | ----- | ----- |
| | 460,870 | 360,993 |
| | ===== | ===== |

Note 7 - Investments in Investee Companies

Company

A. Composition

| | December 31 | |
|--|----------------|----------------|
| | 2004 | 2003 |
| | ----- | ----- |
| | US\$ thousands | US\$ thousands |
| | ----- | ----- |

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| | | |
|--|-----------|----------|
| Subsidiaries - | | |
| Cost of shares | 424,865 | 417,623 |
| Company's equity in retained earnings and capital reserves accumulated from date of acquisition, net | 351,475 | 232,744 |
| Adjustments deriving from translation of financial statements of investee companies | (1,425) | (4,250) |
| | ----- | ----- |
| | 774,915 | 646,117 |
| Less - investment in Company shares held by subsidiary | (11,232) | (15,428) |
| Capital reserve from acquisition and sale of debentures convertible into shares of the Company by a subsidiary | 399 | 399 |
| | ----- | ----- |
| | 764,082 | 631,088 |
| Loans - C(1) | 242,417 | 101,417 |
| Perpetual loan - C(2) | 2,500 | 2,500 |
| | ----- | ----- |
| | 1,008,999 | 735,005 |
| | ===== | ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 7 - Investments in Investee Companies

Company

B. Movement during the year

| | 2004 |
|---|----------------|
| | ----- |
| | US\$ thousands |
| | ----- |
| Balance at beginning of year | 735,005 |
| Company's equity in net earnings of investee companies, net | 163,406 |
| Adjustments deriving from translation of financial statements of investee companies | 2,825 |
| Dividend | (44,675) |
| Realization of Company shares held by a subsidiary | 4,196 |
| Additional investments, net | 7,242 |
| Change in loans and capital notes, net | 141,000 |
| | ----- |
| Balance at end of year | 1,008,999 |
| | ===== |

A list of the investee companies is presented in the Appendix.

C. Terms of loans and capital notes

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- (1) The loans bear interest at the Libor rate plus a margin which ranges between 0.8% and 2%. The loans as at December 31, 2004 are presented net of current maturities in the amount of US\$ 4.5 million.
 - (2) The perpetual loan is non-linked and does not bear interest.
- D. Additional information

- (1) Acquisition of companies during the year of the report:

- a. In April 2004, the Company, through wholly owned and controlled subsidiaries, signed agreements for acquisition of the ownership and control of a group of three companies: Vegetation Management LLC, Farm Saver. Com LLC, and Nation Ag II LLC - which are engaged in licensing the import and marketing of herbicides from the United States (hereinafter - "the Companies Acquired").

The aggregate consideration for the acquisition amounted to approximately US\$ 67 million (the consideration is after an amendment to the original agreement made in December 2004). Approximately US\$ 7.5 million of the aggregate consideration was paid through a transfer of 1,908 of the Company's shares that were held by a subsidiary (the cost of the shares is US\$ 4.2 million).

The excess cost created on the acquisition date amounted to US\$ 51.4 million, of which \$28.4 million was attributed to intangible assets (mainly licensing and licenses), US\$ 0.5 million was attributed to deferred tax liability, US \$0.6 million was attributed to inventory and the balance, in the amount of US\$ 22.9 million, was recorded as goodwill.

The excess cost attributed to the licensing and the licenses, as well as the goodwill, are being amortized over a period of 20 years which, in the Company's estimation, represents the period of economic benefit to be derived therefrom.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 7 - Investments in Investee Companies (cont'd)

Company

D. Additional information (cont'd)

- (1) Acquisition of companies during the year of the report: (cont'd)

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a. (cont'd)

The statements of income and cash flows of the Companies Acquired were consolidated as of May 1, 2004.

The effect of the first time consolidation of the activities acquired on the consolidated statements of income is an increase in revenues of US\$ 24.1 million for the period ended December 31, 2004, and an increase to net income (after amortization of goodwill) of US\$ 5.6 million for the same period. The impact on the consolidated balance sheet as at December 31, 2004 is an increase of assets in the amount of US\$ 77.5 million.

b. During the year of the report, the Company signed, through subsidiaries, agreements for acquisition of three marketing companies, as follows:

- 1) In June 2004, the Company, through a wholly owned and controlled subsidiary, signed an agreement for acquisition of 45% of the rights in the U.S. company, Control Solutions Inc. (hereinafter - "CSI"), which is engaged in the marketing of pesticides to the non-agricultural market in the United States.

Based on the acquisition agreement, so long as the subsidiary holds 45% of the shares of CSI, decisions in areas critical to CSI are to be made jointly by all the shareholders of CSI. Therefore, CSI has been consolidated in the financial statements by means of the proportionate consolidation method.

In addition, the subsidiary was given an option, which may be exercised at any time during the next three years, to increase its share in CSI to 60%, in exchange for a payment ranging between US\$ 1.5 million and US\$ 10.5 million, in accordance with the earnings of CSI in 2004-2006.

Furthermore, commencing from 2009, both the subsidiary and the remaining shareholders of CSI have the right to require the subsidiary to acquire from the remaining shareholders of CSI the balance of their shares in CSI in consideration of an amount to be determined based on the income of CSI in the three years preceding the acquisition date.

- 2) In July 2004, the Company, through a wholly owned and controlled subsidiary, signed an agreement for acquisition of all the shares and rights of Farmoz PTY Limited, an Australian company engaged in the marketing and distribution of pesticides in Australia.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 7 - Investments in Investee Companies (cont'd)

D. Additional information (cont'd)

(1) Acquisition of companies during the year of the report: (cont'd)

- 3) In August 2004, the Company, through a subsidiary, signed an agreement for acquisition of 50.1% of the rights in the U.S. company, RiceCo LLC, which is engaged in the development and marketing of herbicides in the rice sector.

The aggregate cost of the acquisition of the marketing companies amounted to US\$ 41 million. The excess cost created on the acquisition date amounted to US\$ 31.1 million, of which US\$ 15 million was attributed to intangible assets (mainly licensing and licenses), US\$ 3.5 million was attributed to deferred tax liability, US\$ 0.7 million was attributed to inventory and the balance, in the amount of US\$ 18.9 million, was recorded as goodwill.

The excess cost attributed to the licensing and the licenses, as well as the goodwill, are being amortized over a period of 20 years which, in the Company's estimation, represents the period of economic benefit to be derived therefrom.

The statements of income and cash flows of the three marketing companies acquired were consolidated as of their acquisition dates. The total effect of the first time consolidation of the aforementioned marketing companies on the consolidated statements of income from the date of their initial consolidation is an increase in revenues of US\$ 46.2 million for the period ended December 31, 2004 and a reduction of net earnings (after goodwill amortization) of US\$ 0.3 million for that period. The effect on the consolidation on the balance sheet as at December 31, 2004, is an increase of assets in the amount of US\$ 72.8 million.

(2) Subsequent to the balance sheet date, in January 2005, the Company signed an agreement by means of a company it wholly owns and controls, for acquisition of 49% of the shares and rights of Makhteshim Agan Benelux & Nordic B.V. ("Mabeno"), a Dutch company that serves as the exclusive distributor of herbicides of the Makhteshim Agan Group in the areas of Benelux and Scandinavia. In accordance with the agreement, the acquisition will be executed in exchange for an issuance of Company shares in the amount of (euro) 2,940 thousand, according to the market price of the share on the day of the transfer. In addition, the Company received an option to increase its holdings in Mabeno to 55%.

(3) With respect to Goodwill on acquisition of investee companies and the unamortized balance thereof - see Note 10.

(4) With respect to guarantees for investee companies - see Note 19E.

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E. Convertible securities in investee companies

- (1) A subsidiary, Lycored - Natural Products Industries Ltd. (hereinafter - "Lycored"), has granted stock options to employees, which, if exercised, will dilute the Company's holding in Lycored to about 87.72%.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 7 - Investments in Investee Companies (cont'd)

E. Convertible securities in investee companies (cont'd)

- (2) On October 28, 2003, the Board of Directors of Luxembourg Medicine Ltd. (hereinafter - "Luxembourg") approved the issuance of options to employees of Luxembourg and its subsidiary. Exercise of the options will dilute the holding of the Company in Luxembourg to about 92%.
- (3) As at the balance sheet date, exercise of the said options is reasonable and if all of the options are exercised (see Note 7E (1) (2)), the Company will sustain a loss from decline in the holdings' percentage, in the amount of US\$ 2 million. The financial statements include a provision for this amount.

Note 8 - Long-Term Investments, Loans and Receivables

A. Composition

| | Consolidated | | |
|--|---------------------|---------------------|------------------|
| | December 31 2004 | December 31 2003 | December 2002 |
| | US\$ thousands | US\$ thousands | US\$ thousand |
| | ----- | ----- | ----- |
| Long-term investments, loans and receivables [B(1)] | 23,265 | 18,349 | |
| Bank deposits [B(2)] | - | - | 19,000 |
| | ----- | ----- | ----- |
| Net of allowance for doubtful debts | 23,265 | 18,349 | 19,000 |
| | 1,500 | 1,500 | |
| | ----- | ----- | ----- |
| Less - current maturities | 21,765 | 16,849 | 19,000 |
| | 420 | 380 | |
| | ----- | ----- | ----- |
| Other investments [B(3)] | 21,345 | 16,469 | 19,000 |
| | 725 | 1,575 | |
| | ----- | ----- | ----- |
| | 22,070 | 18,044 | 19,000 |

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B. Additional information

(1) Long-term investments, loans and receivables

A. Linkage terms and interest rates

| | Consolidated | |
|----------------------------------|---------------------|---------------------|
| | December 31 2004 | December 31 2003 |
| | US\$ thousands | US\$ thousands |
| | ----- | ----- |
| In Israeli currency - not linked | 2,353 | - |
| In dollars | 1,710 | 5,485 |
| In Brazilian reals | 15,715 | 7,699 |
| In Argentine pesos | 2,352 | 4,319 |
| Other foreign currency | 1,135 | 846 |
| | ----- | ----- |
| | 23,265 | 18,349 |
| | ===== | ===== |

The above investments, loans and receivables are non-interest bearing.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 8 - Long-Term Investments, Loans and Receivables (cont'd)

B. Additional information (cont'd)

(1) Long-term investments, loans and receivables (cont'd)

B. Maturities

The investments, loans and receivables mature as follows:

| | US\$ thousands |
|---------------------------------|----------------|
| | ----- |
| First year (current maturities) | 420 |
| | ----- |
| Second year | 6,333 |
| Third year | 2,865 |
| Fourth year | 2,180 |
| Fifth year | 662 |

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| | |
|--------------------------------|---------|
| With no defined repayment date | *10,805 |
| | ----- |
| | 22,845 |
| | ----- |
| | 23,265 |
| | ===== |

* Including restricted deposits and other assets in the amount of \$5.3 million.

(2) Bank deposits

| | Interest rate as at balance sheet date | Company | |
|-----------------|--|---------------------|---------------------|
| | | December 31 2004 | December 31 2003 |
| | % | US\$ thousands | US\$ thousands |
| | ----- | ----- | ----- |
| Dollar deposits | 4.0 | 10,711 | 20,799 |
| Dollar deposits | 5.1 | 8,305 | 8,302 |
| | | ----- | ----- |
| | | 19,016 | 29,101 |
| | | ===== | ===== |

During the years 2001 and 2000, the Company made deposits in a Brazilian bank in the amount of US\$ 8,300 thousand and US\$ 45,600 thousand, respectively, for a five-year period. Such deposits serve as sole security for loans taken out by a subsidiary from the same bank and in the same amounts. The loans are in dollars, bear interest at the rate of 5.3% and 3.5% p.a. and are scheduled to be repaid in 2006 and 2005, respectively. The Company and the subsidiary are able to realize the deposit and make early repayment of the loan on certain dates as provided in the agreement.

In September 2003, the amount of \$ 25 million was paid out of these deposits and in February 2004 the amount of an additional US\$ 10 million was paid out of these deposits. Concurrently, loans were repaid in the same amount.

In the consolidated balance sheet, the amounts of the deposits were set-off against the amounts of the loans taken out by the subsidiary (see Note 14A).

(3) In 1998, the Company entered into an agreement with the shareholders of Hazera Genetics Ltd. and established a joint venture intended to function as a venture capital fund for the investment in companies which are engaged in the field of agricultural biotechnology. Other investments include the Group's share (50%) in biotechnology companies. In the year of account the subsidiary provided the amount of US\$ 1.1 million as impairment in value of these investments.

Notes to the Financial Statements as at December 31, 2004

Note 9 - Fixed Assets

A. Composition

Consolidated

| | Land and buildings | Plant and equipment | Motor vehicles | and |
|---|-----------------------|------------------------|-------------------|------|
| | US\$ thousands | US\$ thousands | US\$ thousands | US\$ |
| Cost | | | | |
| Balance as at the beginning of the year | 123,345 | 635,438 | 4,824 | |
| Additions net of grants | 6,979 | 26,174 | 1,101 | |
| Newly consolidated company | 809 | 635 | 587 | |
| Disposals | (408) | (925) | (1,513) | |
| Balance as at the end of the year | 130,725 | 661,322 | 4,999 | |
| Accumulated depreciation | | | | |
| Balance as at the beginning of the year | 44,304 | 297,561 | 2,812 | |
| Additions | 4,059 | 22,717 | 719 | |
| Newly consolidated company | 82 | 264 | 227 | |
| Eliminated on disposals | (408) | (589) | (1,158) | |
| Balance as at the end of the year | 48,037 | 319,953 | 2,600 | |
| Net book value | | | | |
| As at December 31, 2004 | 82,688 | 341,369 | 2,399 | |
| As at December 31, 2003 | 79,041 | 337,877 | 2,012 | |

Cost of assets includes:
 Buildings and development on freehold land
 Buildings and development on land held under capitalized leases
 Capitalized financing expenses
 Fully-depreciated equipment
 Cost of assets is net of grants received

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 9 - Fixed Assets (cont'd)

B. Additional information

(1) Makhteshim's plants are located on land in Ramat Hovav and in Beer-Sheva which is leased from the Israel Lands Administration. The leasehold periods terminate between 2018 and 2029 with renewal options. The leasehold rights have not yet been registered in the name of Makhteshim in the Israel Land Registry. (The legal advisors of Makhteshim are attending to the registration).

Agan's plant is located on freehold land of approximately 121 dunams in Ashdod, of which 90 dunams are registered in the name of Agan in the Land Registry with the remaining area of approximately 30 dunams, which was acquired in 1996, currently undergoing the registration process.

Plants of foreign investee companies are constructed on freehold land.

(2) Regarding liens - see Note 20.

Note 10 - Other Assets and Deferred Charges

A. Composition:

Consolidated

| December 31, 2004 | |
|-------------------|-----------------------------|
| Cost | Accumulated amortization |
| ----- | ----- |
| US\$ thousands | US\$ thousands |

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| | | |
|--|----------------|----------------|
| Product registration and acquisition of know-how | 265,719 | 110,206 |
| Goodwill on acquisition of subsidiaries | 153,963 | 51,489 |
| Intangible assets on purchase of products | 281,223 | 41,186 |
| Marketing rights | 36,099 | 10,705 |
| Debenture issuance expenses | 3,730 | 1,272 |
| Non-competition and confidentiality agreement | 2,576 | 1,032 |
| | <u>743,310</u> | <u>215,890</u> |

December 31, 2003

| | Cost | Accumulated amortization |
|--|----------------|-----------------------------|
| | US\$ thousands | US\$ thousands |
| Product registration and acquisition of know-how | 178,855 | 94,483 |
| Goodwill on acquisition of subsidiaries | 111,056 | 37,093 |
| Intangible assets on purchase of products | 281,223 | 23,063 |
| Marketing rights | 36,099 | 7,870 |
| Debenture issuance expenses | 2,466 | 848 |
| Non-competition and confidentiality agreement | 2,576 | 516 |
| | <u>612,275</u> | <u>163,873</u> |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 10 - Other Assets and Deferred Charges (cont'd)

Company

December 31, 2004

| | Cost | Accumulated amortization | Unamortized balance |
|-----------------------------|----------------|-----------------------------|------------------------|
| | US\$ thousands | US\$ thousands | US\$ thousands |
| Debenture issuance expenses | 3,730 | 1,272 | 2,458 |

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December 31, 2003

s

| | Cost | Accumulated amortization | Unamortized balance |
|-----------------------------|----------------|-----------------------------|------------------------|
| | US\$ thousands | US\$ thousands | US\$ thousands |
| Debenture issuance expenses | 2,466 | 848 | 1,618 |

B. Additional details

- In October-November 2002, subsidiaries, which are wholly-controlled by the Company, signed a number of agreements with Bayer Crop Science AG for acquisition of a number of products, licenses and distribution rights in the area of vegetation protection. The total consideration for acquisition of the products amounted to US\$ 185.3 million, which is presented in the "other assets and deferred expenses" category.

Approximately US\$ 34.6 million of the consideration was allocated to acquisition of permits and licenses in connection with the products and is amortized over a 20-year period in the "selling and marketing expenses" category, and approximately US\$ 144.1 million was allocated to acquisition of the products in the framework of a "going concern", which constitutes goodwill on the acquisition of products, and which is amortized over a 20-year period in the "other expenses" category.

The consideration in respect of acquisition of the marketing and distribution rights, in the amount of US\$ 6.6 million, is being amortized over a period of 6-8 years.

- In 2001, fully controlled subsidiaries of the Company signed agreements with Aventis and Syngenta A.G. for the purchase of four new agrochemical products as well as the purchase of marketing and distribution rights of a product package in the Scandinavian countries. One of the products which was purchased is still protected by patents which were transferred to the purchasing company.

The total price paid for purchase of the four products totaled US\$105 million, and it is included in the "other assets and deferred charges" category. Of the amount paid, US\$20 million was attributed to registration costs and licensing, which are amortized over a period of 20 years in the "selling and marketing expenses" category, US\$2.5 million was attributed to the purchase of agreements with third parties, which is amortized over a period of 10 years, and the balance of the amount was attributed to the purchase of the product as a going concern which includes: intellectual rights, trade name, brand name, technological know-how, information on customers and suppliers of materials, etc., which constitutes goodwill on the purchase of the products and is amortized over a period of 20 years under other expenses. The price of the marketing and distribution rights was US\$5 million and is amortized over a period of 9 years.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 10 - Other Assets and Deferred Charges (cont'd)

- B. Additional details (cont'd)
- 3. Regarding goodwill and other assets created in the framework of acquisition of companies during the period of the report, see Note 7D.
- 4. In connection with a non-competition and confidentiality agreement with the former CEO of Milenia, see Note 30A(4).

Note 11 - Short-term Credit from Banks

A. Composition

| | Consolidated | | US\$ |
|---------------------------------------|----------------|----------------|------|
| | December 31 | | |
| | 2004 | 2003 | |
| | US\$ thousands | US\$ thousands | |
| Credit from banks | | | |
| Overdrafts | 55,613 | 54,656 | |
| Short-term loans | 57,366 | 24,946 | |
| | 112,979 | 79,602 | |
| Current maturities of long-term loans | 27,042 | 63,215 | |
| | 140,021 | 142,817 | |

B. Linkage terms and interest rates

| | Consolidated | | US\$ |
|--|----------------|----------------|------|
| | December 31 | | |
| | 2004 | 2003 | |
| Weighted interest rate at balance sheet date % | US\$ thousands | US\$ thousands | |
| Credit from banks | | | |

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Overdrafts:

| | | | |
|-----------------------|------|--------|--------|
| ----- | | | |
| In Israeli currency | 1.8 | 2,892 | 543 |
| In US dollars | 4.0 | 39,272 | 33,996 |
| In Euro | 4.5 | 11,350 | 17,228 |
| In Brazilian currency | 16.9 | 1,814 | 2,408 |
| In other currencies | | 285 | 481 |
| | | ----- | ----- |
| | | 55,613 | 54,656 |
| | | ----- | ----- |

Short-term credit:

| | | | |
|---------------------|-----|---------|--------|
| ----- | | | |
| In Euro | | - | 1,807 |
| In dollars (1) | 3.5 | 51,677 | 18,895 |
| In other currencies | 4.7 | 5,689 | 4,244 |
| | | ----- | ----- |
| | | 57,366 | 24,946 |
| | | ----- | ----- |
| | | 112,979 | 79,602 |
| | | ===== | ===== |

(1) The loans mainly bear variable interest at an annual rate of between 0.8% and 1.7% a

C. Regarding collateral - see Note 20A.

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Notes to the Financial Statements as at December 31, 2004

Note 12 - Trade Payables

Consolidated

Open accounts
Checks payable

US\$ thou

325,

325,
=====

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Note 13 - Other Payables

| | Consolidated | | US\$ thou |
|---|----------------|----------------|-----------|
| | December 31 | | |
| | 2004 | 2003 | |
| | US\$ thousands | US\$ thousands | |
| Salaries and payroll accruals | 32,591 | 29,852 | 2, |
| Accrued income taxes, net of advance payments | 38,047 | 17,819 | |
| Government agencies | 5,804 | 7,058 | |
| Subsidiaries - current account | - | - | |
| Liability for securities sold short (1) | 5,627 | 15,418 | |
| Payables in respect of currency transactions | 9,608 | 9,956 | |
| Accrued expenses and deferred income | 63,672 | 34,180 | 3, |
| Payables in respect of acquisition of subsidiary | 6,500 | 6,300 | |
| Others | 30,556 | 29,958 | |
| | 192,405 | 150,541 | 6, |

(1) Subsidiary borrows marketable bonds from a bank for purposes of the short sale thereof. The borrowing period is three months, which is renewed every three months subject to the lender's agreement.

The subsidiary's liability in respect of the bonds borrowed, is presented based on the market value of the bonds as at the balance sheet date.

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Notes to the Financial Statements as at December 31, 2004

Note 14 - Long-Term Loans from Banks

A. Composition

Consolidated

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| | December 31 | | US\$ thou |
|--|----------------|----------------|-----------|
| | 2004 | 2003 | |
| | US\$ thousands | US\$ thousands | |
| Loans from banks* | 120,065 | 332,448 | |
| Less - current maturities | 27,042 | 63,215 | |
| | 93,023 | 269,233 | |
| * After the deduction of an investment in bank deposits (see Note 8B2) in the amount of: | 19,016 | 29,101 | |

B. Linkage terms and interest rates

| | Weighted interest rate at balance sheet date % | Consolidated | | US\$ |
|---------------------------|--|----------------|----------------|------|
| | | December 31 | | |
| | | 2004 | 2003 | |
| | | US\$ thousands | US\$ thousands | |
| In US dollars | 3.6 | 103,124 | 313,148 | |
| In Euro | 3.5 | 9,189 | 9,396 | |
| In Israeli currency | 7.4 | 1,548 | 2,633 | |
| In other foreign currency | 5.2 | 6,204 | 7,271 | |
| | | 120,065 | 332,448 | |

* Most of the loans bear interest at the Libor rate plus a margin.

C. Maturities

| | Consolidated |
|---------------------------------|----------------|
| | US\$ thousands |
| First year - current maturities | 27,042 |
| Second year | 51,015 |
| Third year | 19,282 |
| Fourth year | 11,830 |
| Fifth year | 5,896 |
| Sixth year and thereafter | 5,000 |

120,065
=====

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 14 - Long-Term Loans from Banks (cont'd)

- D. Regarding the commitment of the Company and certain subsidiaries to banks, to maintain certain financial criteria, mainly, debt-equity and profitability ratios - see Note 20C.
- E. Collaterals - see Note 20A.

Note 15 - Convertible Debentures

- A. Presented in the "long-term liabilities" category

| | Consolidated | | Comp |
|---------------------|----------------|----------------|----------------|
| | December 31 | | December |
| | 2004 | 2003 | 2004 |
| | US\$ thousands | US\$ thousands | US\$ thousands |
| Debenture principal | 150,000 | - | 150,000 |
| | ===== | ===== | ===== |

1. In March 2004, the Company issued, as part of a private issuance to institutional investors (mainly overseas), non-marketable convertible debentures, in the amount of US\$ 150 million par value (including US\$ 5 million which was issued to the underwriters in April 2004), in exchange for their par value. The period of the debentures is 7 years and they bear annual interest at the rate of 1.75%, which is to be paid once a year, in March. The debentures may be converted into ordinary registered shares of NIS 1 par value each, at a conversion rate of NIS 20.5 par value, based on a fixed rate of exchange of US\$1 = NIS 4.514. The ordinary

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shares to be issued as a result of conversion of the debentures shall be registered for trading on the Tel-Aviv Stock Exchange.

The owners of the debentures shall have the right to demand payment of the debentures (principal and interest up to that date) on March 22, 2007, by means of advance written notice (which is given 30-60 days prior to March 22, 2007).

The Company shall have the right to execute a forced conversion of the debentures commencing on March 22, 2007, this being so long as the average price per Company share in the period of 20 business days which preceded its notification of forced conversion, shall be at least 30% higher than the price of the conversion rate of the debentures.

The Company committed to the debenture purchasers that it would refrain from creating additional liens on its property, the purpose of which is the guarantee of marketable securities or other securities which the Company intends to register for trading.

The total issuance expenses with respect to the aforementioned debentures amounted to US\$ 2.5 million.

2. As at the balance sheet date, conversion of the said debentures is not expected and, accordingly, they are presented in the balance sheet as part of the "long-term liabilities" category.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 15 - Convertible Debentures (cont'd)

- B. Presented in a separate category between "long-term liabilities" and "shareholders' equity"

| | Consolidated | | Comp |
|-----------------------|----------------|----------------|----------------|
| | December 31 | | Decembe |
| | 2004 | 2003 | 2004 |
| | US\$ thousands | US\$ thousands | US\$ thousands |
| Debtenture principal | 39,474 | 81,950 | 39,474 |
| Discount balance, net | (1,152) | (4,245) | (1,565) |

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| | | |
|--------|--------|--------|
| ----- | ----- | ----- |
| 38,322 | 77,705 | 37,909 |
| ===== | ===== | ===== |

1. In November 2001, convertible debentures and options were issued pursuant to a prospectus, as follows:

NIS 270,000,000 par value registered debentures (Series A) offered at 90% of the par value, repayable in a lump-sum payment on November 20, 2007, bearing interest at the annual rate of 2.5% and linked (interest and principal) to the representative exchange rate of the dollar. On any trading day, commencing with the registration date of the debentures (Series A) for trading on the stock exchange and up to and including October 31, 2007, the debentures (Series A) are convertible into fully paid-up ordinary registered shares of NIS 1 par value each, based on a conversion rate of NIS 10.68 par value debentures (Series A) for one ordinary share of NIS 1 par value.

As a result of dividend distributions, the conversion rate was updated and, as at the balance sheet date, it stands at NIS 10.03 par value.

18,000,000 registered options (Series 1), exercisable for 18,000,000 ordinary shares of NIS 1 par value each of the Company, on any trading day, commencing with the registration date thereof for trading on the stock exchange and up to and including November 20, 2005, such that every option (Series 1) may be exercised for one ordinary share of NIS 1 par value (subject to adjustments), against a cash payment of the exercise price of NIS 10.68, linked to the representative exchange rate of the dollar. In any case, the exercise price will not be less than NIS 10.68. An option (Series 1) which is not exercised up to and including November 20, 2005, will be invalid and will not convey to its holder any right vis-a-vis the Company.

As a result of dividend distributions, the exercise price was updated and, as at the balance sheet date, it stands at NIS 10.03

The securities were offered to the public in 1,200,000 units by means of a tender on the unit price, where the composition of each unit is NIS 225 par value of debentures (Series A) at the price of 90% of their par value (NIS 202.5) and 15 options (Series 1) for no consideration. The total minimum price per unit was NIS 202.5.

The price per unit determined as part of the tender was NIS 220. Taking into account the economic value of the options (Series 1) the discount rate with respect to the debentures (Series A) is 9.3%. The gross consideration received in the issuance is US\$ 62.5 million, of which US\$ 58.5 million was attributed to the debentures (Series A) and US\$ 4.0 million was attributed to the options (Series 1).

Notes to the Financial Statements as at December 31, 2004

Note 15 - Convertible Debentures (cont'd)

- B. Presented in a separate category between "long-term liabilities" and "shareholders' equity" (cont'd)
-

2. In January 2002, the Company issued to investors, as part of a private placement, NIS 133,980 thousand par value convertible debentures (Series A), at a price of NIS 1.015 for NIS 1 par value of debentures (Series A), for an aggregate consideration of US\$ 29.5 million. The terms of the convertible debentures (Series A) are identical to the terms of the debentures (Series A), issued by the Company, as stated in Section A., above.
3. In June 2002, a subsidiary acquired on the stock exchange, approximately NIS 16,684 thousand par value of debentures (Series A), for a consideration of US\$ 3.2 million. The difference between the acquisition cost and the liability value of the debentures acquired on the books, in the amount of US\$ 0.4 million, was recorded as a capital reserve in the shareholders' equity section. During June 2003, all the above-mentioned debentures were sold for a consideration of US\$ 4.3 million.
4. In 2003, NIS 57,660,575 par value of debentures (Series A) were converted into 5,565,649 ordinary shares of NIS 1 par value, the majority at a conversion rate of NIS 10.36 par value debentures for one ordinary share of NIS 1 par value. The total share capital issued as a result of the conversion is US\$ 1,270 thousand, with a premium of US\$ 11,331 thousand.

In the year of account, NIS 179,607,707 par value of debentures (Series A) were converted into 17,582,221 ordinary shares of NIS 1 par value, at a conversion rate of NIS 10.03-10.36 par value debentures for one ordinary share of NIS 1 par value. The total share capital issued as a result of the conversion is US\$ 3,974 thousand, with a premium of US\$ 35,581 thousand. Subsequent to the balance sheet date and proximate to the date of authorization of the financial statements, NIS 12,839 thousand par value of debentures (Series A) were converted into 1,280 thousand ordinary shares of NIS 1 par value.

5. As at the balance sheet date, conversion of the said debentures is expected and, accordingly, they are presented in the balance sheet in a separate category between the "long-term liabilities" and the "shareholders' equity" sections based on their liability value.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 16 - Other Long-Term Liabilities

Consolidated

Linkage terms and interest rates

| | Weighted interest rate as of balance sheet date ----- ----- % | December 31 | |
|---|---|---------------------------------|---------------------------------|
| | | 2004 US\$ thousands ----- | 2003 US\$ thousands ----- |
| Liabilities linked to the US dollar | 2 | 9,195 | 400 |
| Liabilities linked to the Brazilian Real | | - | 1,880 |
| Liabilities linked to another currency | 4.5 | 142 | 190 |
| | | ----- 9,337 | ----- 2,470 |
| | | ===== | ===== |

The liabilities are schedule for repayment in the years 2006 - 2008.

Note 17 - Taxes on Income

A. Benefits under the Law for the Encouragement of Capital Investments, 1959

The plants of the subsidiaries in Israel have been granted "Approved Enterprise" status under the Law for the Encouragement of Capital Investments, 1959. Part of the income deriving from the approved enterprises during the benefit period is subject to tax at the rate of 25% (the total benefit period is for seven years and in certain circumstances ten years, but does not exceed beyond either 14 years from the date of the letter of approval or 12 years from the date the approved enterprise commenced operations).

Other plants of subsidiaries in Israel are entitled to a tax exemption for periods of between two and six years and a reduced tax rate of 25% for the remainder of the benefit period. Should a dividend be distributed from the tax-exempt income, the subsidiaries will be liable to pay tax on the income from which the dividend was distributed at a rate of 25%.

The benefit period has ended for some of the plants of the subsidiaries and the benefit period for others will end during years up to 2008. In

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addition, subsidiaries have other investment programs in progress, or for which the benefit period with respect thereto has not yet commenced.

The abovementioned benefits are conditional upon compliance with certain conditions specified in the Law and related Regulations, and in the letters of approval, in accordance with which the investments in the approved enterprises were made. Failure to meet these conditions may lead to cancellation of the benefits, in whole or in part, and to repayment of any benefits already received, together with interest. Management believes that the companies are complying with these conditions.

B. Benefits under the Law for the Encouragement of Industry (Taxes), 1969

Under the Law for the Encouragement of Industry (Taxes) 1969, the Company is an industrial holding company and the subsidiaries in Israel are "industrial companies". The main benefit under this law is the filing of consolidated income tax returns. The Company files a consolidated income tax return with Makhteshim.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 17 - Taxes on Income (cont'd)

C. Taxation under inflationary conditions

The Company and its subsidiaries in Israel are subject to the Income Tax Law (Inflationary Adjustments), 1985. Under this Law, the results for tax purposes are adjusted principally for the changes in the Consumer Price Index. The financial statements are presented in US dollars.

D. Benefits for development areas

A subsidiary is subject to the Income Tax Regulations (Tax Reductions in Certain Settlements and Agriculture-based Army Units ("Nahal")), 1978. Under these Regulations, the subsidiary is entitled to an additional deduction, at the rate of 25% of the tax depreciation claimed in respect of the plants constructed in Ramat Hovav. These Regulations were in effect until December 31, 2003.

E. Foreign subsidiaries

The subsidiaries are assessed according to the tax laws applicable in the respective countries where these subsidiaries operate.

F. Change in tax rate

On June 29, 2004, Income Tax Ordinance Amendment (No. 140 and Temporary Order), 2004 (hereinafter - "the Amendment") passed the second and third reading in the Israeli Knesset. The Amendment provides that the Companies Tax rate shall be gradually reduced, commencing from January 1, 2004 from 36% to 30% in the following manner: in 2004 - 35%, in 2005 - 34%, in 2006 - 32% and in 2007 and

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thereafter - 30%.

G. Deferred taxes

| | | Consolidated | | |
|-----|---|----------------|----------------|--------|
| | | December 31 | | |
| | | 2004 | 2003 | |
| | | US\$ thousands | US\$ thousands | US\$ t |
| (1) | Movement | | | |
| | Balance at beginning of year | 33,522 | 30,289 | |
| | Included in statement of income | (163) | 3,233 | |
| | Newly consolidated | 3,958 | - | |
| | Balance at end of year | 37,317 | 33,522 | |
| | Classified as: | | | |
| | Other receivables | (17,037) | (10,256) | |
| | Long-term liabilities (in the balances of the long-term debt) | 54,354 | 43,778 | |
| | | 37,317 | 33,522 | |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 17 - Taxes on Income (cont'd)

G. Deferred taxes (cont'd)

(2) Composition

| | | Consolidated | | |
|--|--|----------------|----------------|------|
| | | December 31 | | |
| | | 2004 | 2003 | |
| | | US\$ thousands | US\$ thousands | US\$ |

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| Deferred taxes in respect of: | ----- | ----- | ----- |
|-------------------------------------|----------|----------|-------|
| Depreciable assets | 81,606 | 81,876 | |
| Carryforward tax losses | (19,864) | (33,233) | |
| Inventories | (17,615) | (7,124) | |
| Employee severance benefits, net | (11,467) | (11,142) | |
| Other temporary differences | 699 | 3,145 | |
| Newly consolidated | 3,958 | - | |
| | ----- | ----- | ----- |
| | 37,317 | 33,522 | |
| | ===== | ===== | ===== |

In the consolidated balance sheet, deferred taxes are computed at rates ranging approximately 29% and 35% (Company - 29%).

H. Composition of tax expense (benefit)

Consolidated

| | For the year ended December 31 | |
|--|--------------------------------|----------------|
| | 2004 | 2003 |
| | ----- | ----- |
| | US\$ thousands | US\$ thousands |
| | ----- | ----- |
| Taxes in respect of the reported period: | | |
| Current | 51,228 | 24,702 |
| Deferred | (3,034) | 3,173 |
| | 48,194 | 27,875 |
| Taxes in respect of prior years: | | |
| Current | 1,269 | 4,683 |
| Deferred | 2,871 | 60 |
| | 4,140 | 4,743 |
| | ----- | ----- |
| | 52,334 | 32,618 |
| | ===== | ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 17 - Taxes on Income (cont'd)

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H. Composition of tax expense (benefit) (cont'd)

Company

| | For the year ended December 31 | | |
|----------|--------------------------------|----------------|----------------|
| | 2004 | 2003 | 2002 |
| | US\$ thousands | US\$ thousands | US\$ thousands |
| Current | 2 | 29 | - |
| Deferred | (749) | (2,507) | 214 |
| | (747) | (2,478) | 214 |

I. Theoretical tax

Following is a reconciliation between the theoretical tax and the tax expense included in the statement of income:

Consolidated

| | For the year ended December 31 | |
|--|--------------------------------|----------------|
| | 2004 | 2003 |
| | 35% | 36% |
| | US\$ thousands | US\$ thousands |
| Tax expense computed at regular tax rate | 76,608 | 49,030 |
| Tax benefit for approved enterprises | (10,203) | (3,727) |
| Benefit for plants in development areas | - | (2,109) |
| Difference between financial statement measurement of income and tax basis | 2,559 | (4,868) |
| Change in rate of deferred taxes | (1,912) | 2,384 |
| Income taxable at other tax rates | (20,732) | (14,490) |
| Taxes in respect of previous years | 4,140 | 4,743 |
| Nondeductible expenses and other differences | 1,874 | 1,655 |
| | 52,334 | 32,618 |

Company

| | For the year ended December 31 | |
|--|--------------------------------|----------------|
| | 2004 | 2003 |
| | 35% | 36% |
| | US\$ thousands | US\$ thousands |
| Tax expense computed at regular tax rate | 57,673 | 36,107 |
| Difference between financial statement | | |

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| | | |
|---|----------|----------|
| measurement of income and tax basis | 353 | 166 |
| Equity in earnings of investee companies, net | (57,192) | (37,446) |
| Nondeductible expenses and other differences | (1,581) | (1,305) |
| | ----- | ----- |
| | (747) | (2,478) |
| | ===== | ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 17 - Taxes on Income (cont'd)

J. Final assessments

The Company, Makhteshim, Agan and Lycored have received final tax assessments up to and including the 2001 tax year. Luxembourg and Bio-Dar Ltd. have received final tax assessments up to and including 1998. Other companies in Israel have not received tax assessments since their inception.

K. Losses and deductions available for carryforward to future years

As at the balance sheet date, the losses for tax purposes which are available for carryforward to future tax years, amount to US\$ 66 million.

The Company has recorded a deferred tax asset with respect to the accrued losses, in the amount of US\$ 19.9 million, based on Management's estimation that there is a high level of certainty that such losses will be utilized in the upcoming years.

L. Additional Information

Regarding fiscal claims against Milenia - see Note 19D(3).

Note 18 - Employee Termination Benefits, Net

A. Composition

| | | |
|----------------|----------------|-------|
| Consolidated | | |
| ----- | | |
| December 31 | | |
| ----- | | |
| 2004 | 2003 | |
| ----- | ----- | |
| US\$ thousands | US\$ thousands | US\$ |
| ----- | ----- | ----- |

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| | | |
|---|--------|--------|
| Accrued severance pay and retirement grants | 26,576 | 23,831 |
| Less - deposits in severance pay funds | 15,957 | 13,763 |
| | ----- | ----- |
| | 10,619 | 10,068 |
| Early retirement pension | 13,248 | 12,399 |
| Accrual for unutilized sick leave | 2,842 | 2,307 |
| | ----- | ----- |
| | 26,709 | 24,774 |
| | ===== | ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 18 - Employee Termination Benefits, Net

B. Severance pay and retirement grants

The Company and its subsidiaries in Israel make regular deposits with "Nativ" (the Pension Fund of the Workers and Employees of the Histadrut Ltd.) and insurance companies. These deposits are intended to provide employees with pension rights or severance pay upon reaching retirement age. Amounts deposited in the pension fund and insurance companies are not included in the balance sheet because they are not under the management or control of the companies.

Employees dismissed before attaining retirement age are eligible for severance benefits, computed on the basis of their most recent salary. Where the amounts accumulated in the pension fund are not sufficient to cover the computed severance benefits, the companies will cover the difference. Experience has shown that the majority of salaried employees continue to work until retirement age and the companies have not been required to cover substantial differences in severance pay to employees who retire prior to reaching retirement age. Management of the Company and the subsidiaries accordingly believe that it is unlikely that it will be necessary to cover such differences and therefore no accrual has been made in the financial statements.

In addition to their abovementioned pension rights, employees are entitled to receive retirement grants at the rate of 2.33% of their salary at retirement age. The accrual in the balance sheet covers the companies' obligations with regard to these retirement grants, as well as their liability to pay severance benefits to some of their employees for the period prior to the date on which these employees joined the pension plan, during which period no deposits had been made in the fund in the name of the employee.

C. Deposits with severance pay fund and retirement grants

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The deposits in the severance pay funds include accrued linkage differences and interest and are made in severance pay funds with banks and insurance companies. Withdrawal of the amounts on deposit is contingent upon the fulfillment of the provisions set forth in the Severance Pay Law.

D. Compensation for unutilized sick leave

The financial statements include an accrual for compensation in respect of unutilized sick leave for employees who are 55 and older. No accrual is made in respect of employees under the age of 55 as it is uncertain as to whether or not they will receive such compensation (by reason of utilization of sick leave or early retirement). The accrual is computed, using the latest wage rates, on the basis of eight work days for each year of employment in which sick leave was not utilized.

E. Early retirement pension

The financial statements include a provision for payment of pension benefits to a number of employees whose work was terminated before they reached retirement age. The provision was calculated by reference to the period from the time their work was terminated until the date stipulated in the agreement, on the basis of the present value of the pension payments (the interest rate used in the present value calculation was 3.6% per annum).

At the beginning of 2004, the Knesset passed a law according to which the Articles of Association for pension funds were changed, such that the retirement age will be gradually raised for men from 65 to 67 and for women from 60 to 62.

In the estimation of Company Management, the above-mentioned law will have no effect on the Company's liabilities for early retirement in connection with its employees who left prior to reaching retirement age.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities

A. Commitments

- (1) The Articles of Association of the Company and its subsidiaries permit, subject to the governing companies' laws, including the provision of the Companies Law, indemnification and insurance of the responsibilities of directors and officers therein, provided that if the Company decides to provide advance indemnification, the amount of such indemnification shall be limited to 25% of the Company's shareholders' equity as at the date the indemnification is granted.

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- (2) Liability of directors and officers of the Company and its subsidiaries is insured as part of a policy. The limit of the insured responsibility is US\$ 100 million. The directors who were insured within the policy include all of the Company's directors as well as the directors of the subsidiaries.
- (3) A subsidiary has a long-term supply contract with an international company in the annual amount of US\$ 17 million for a five-year period (2001 - 2006). Based on the contracts, a multi-national company participates in part of the manufacturing costs.
- (4) Regarding undertakings of the Company and its subsidiaries as part of a securitization transaction - see Note 3(1).
- (5) Regarding undertakings with interested parties - see Note 30A.

B. Contingent liabilities

- (1) In accordance with the Law for the Encouragement of Capital Investments, 1959, subsidiaries received grants from the State of Israel in respect of investments made in fixed assets as part of plant expansion projects authorized by the Investment Center. Receipt of grants is conditional upon fulfillment of the terms of the letter of approval which include, among other things, exports at certain rates. If the companies do not comply with the required terms, the grants will have to be refunded, together with interest from the date of their receipt. Management believes that the subsidiaries are in compliance with the conditions for approval.
- (2) In accordance with the Law for the Encouragement of Research and Development in Industry, 1984, subsidiaries received grants from the State of Israel in respect of their research and development expenses incurred on projects approved by the Industrial Research and Development Administration. Receipt of the grants is conditional upon compliance with the terms of the letter of approval which include, among other things, the payment of royalties to the State at rates of between 2%-3.5% of the sales of products, up to the amount of the State's participation.

The balance of the State's participation in the companies' research and development expenses (net of royalties paid in respect thereof), after deduction of participations in expenses of unsuccessful research projects which were abandoned, amounts to approximately US\$ 6 million.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities (cont'd)

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- B. Contingent liabilities (cont'd)
- (3) The Company has undertaken to indemnify the economic consultants who determined the exchange ratio for the Arrangement (see Note 1B) for reasonable expenses that they may be required to pay for legal consultation and representation in the event that legal proceedings are brought against them in connection with their opinion. In addition, the Company will indemnify the economic consultants for any damages payable in consequence of legal proceedings which exceed US\$ 1.5 million. The Company shall not be liable to indemnify the economic consultants if it is determined that they acted with gross negligence or willful misconduct in connection with their opinion.
- (4) A subsidiary has an agreement pursuant to which it will pay royalties at the rate of 4% of sales, with certain reductions stated in the agreement, with respect to a product whose development rights were acquired by the subsidiary, for a period of 10 years beginning from the year 2000, the date on which sales of the product to outsiders reached the level of sales stipulated in the agreement. Under certain conditions, the royalties may be reduced to a rate of not less than 2%.
- (5) In Israel the Stamp Duty on Documents Law - 1961 (hereinafter - the Law) applies to various documents at various rates, according to the type of the document and the amount specified or not specified in it. In June 2003 Section 15A of the Law regarding the identity of those required to pay stamp duty was amended.

Beginning from June 2003 the Israeli Tax Authorities increased enforcement of the law. The amendment to the Law and the enforcement measures taken by the Tax Authorities were raised for discussion at the Supreme Court, which has not yet established its opinion on the matter. Furthermore, in accordance with legislative trends it is anticipated that the Stamp Duty Law will be gradually annulled and that by 2008 it will be completely annulled.

In August 2004 the Customs and VAT Department requested from a subsidiary to produce documents the company had signed after June 1, 2003. The Customs and VAT Department contends that the Law requires the payment of stamp duty on the requested documents. Furthermore, the company was issued a stamp duty notice with respect to a document it had signed with a third party.

In the opinion of management of the Company, which is based on the opinion of its legal counsel, the Company does not stand before any material exposure in respect of any demand arising from the Stamp Duty Law.

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Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities (cont'd)

C. Environmental quality

- (1) The operations of the Company and of its investee companies are exposed to risks related to environmental contamination, since they produce, store and sell chemicals. The Group invests substantial sums in order to comply with environmental laws and regulations, and management believes that the Group companies are in compliance with those laws. In accordance with the estimate of the Company's insurance experts, the Group insurance policies cover any sudden, unexpected environmental contamination caused in Israel and the rest of the world, subject to the conditions of the relevant policies. As at December 31, 2004, the Group did not have any coverage against ongoing environmental contamination. Such insurance is difficult to obtain, and in cases when it can be obtained, the Company believes that the terms of the policy, including the amount of the insurance coverage, do not presently justify obtaining such a policy.
- (2) Pursuant to an agreement with the Ministry of Environmental Protection, subsidiaries decided to construct facilities for the biological treatment of waste. Construction of the facility will take about 3 years. In the estimation of the subsidiary's management, the aggregate construction cost will be between US\$ 30 million and US\$ 40 million.
- (3) One of the subsidiary's plants, together with other chemical plants, was constructed in Ramat Hovav, since the Government of Israel determined that the location was suitable for chemical plants as it was assumed that the layers of the soil in that area were absolutely sealed against penetration by liquid discharges or contamination. The Ministry of Environmental Protection conducted tests as a result of which it was reported that data exist indicating subterranean contamination in Ramat Hovav. The inspectors recommended that steps be taken to prevent further leakage from active and dormant installations which are likely to constitute a source of contamination of the subterranean water in the region.

The subsidiary may be required to clean up the relevant areas or subterranean layers if and when it is found that the subsidiary is responsible for the said contamination. Over the past several years various tests have been performed by different agencies to test the ground contamination in the Ramat Hovav area as well as the area surrounding the subsidiary's premises in Be'er Sheva. In the opinion of Company Management, no material consequences on the financial statements are expected due to application of the recommendations deriving from the said examinations.
- (4) In May 2004, a subsidiary and other factories in the Ramat Hovav area received a notification of a change in the terms of the license, according to which the factories will be required to treat their waste, in contrast with the current treatment, independently and through application of evaporation procedures, in the framework of which the

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factories are required to perform within a short time, research and development for purposes of conformance of the procedures to the composition of each factory's waste, and later on to construct an appropriate facility, as well as application of formulation procedures, in the framework of which the factories are required to present research and development plans to the Ministry for purposes of application of the procedures with respect to the waste. At the same time, the Ministry of Environmental Protection set a date by which the factories are required to treat their waste in the required format and to stop the flow of waste into the evaporation pools and the waste treatment facilities of the Council.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities (cont'd)

C. Environmental quality (cont'd)

(4) (cont'd)

On October 10, 2004, the subsidiary, together with the Israeli Union of Industrialists and other companies, filed an administrative petition with the District Court of Be'er Sheva against the Ministry of Environmental Protection. The subject of the petition is in respect of the additional conditions for receipt of a business license that were imposed on the petitioning factories in May 2004 that deal with treatment and removal of waste accumulated as a result of their operations.

As part of the petition, the Court was requested to issue an order declaring that the additional conditions are null and void.

On December 29, 2004, a preliminary hearing was held with respect to the petition and it was determined that the hearing on the petition will be held on March 7, 2005.

In the estimation of Company Management, based on the advice of its legal advisors, in light of the early stage of the proceedings, it is not possible at this stage to predict the chances of the administrative petition succeeding.

In the Company's estimation, if the petition is rejected, such rejection will have a material impact on the activities of the factory in Ramat Hovav and/or investments will be required, the scope of which the Company is unable to estimate at this point.

(5) On November 28, 2004, a Government decision was received that approves a plan in connection with reduction of damaging air

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and water pollution agents deriving from the Ramat Hovav area.

A. Treatment of Factory Waste

1. By June 30, 2006, flow of the untreated waste into the joint biological treatment facility will be discontinued, and every factory will treat its waste up to the quality level determined by the Ministry of Environmental Protection (as determined in additional terms of the business license from May 2004).
2. By December 31, 2007, flow of the runoff into the existing evaporation pools will be discontinued, and every factory will treat its runoff up to the quality level determined by the Ministry of Environmental Protection (as determined in additional terms of the business license from May 2004).

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities (cont'd)

C. Environmental quality (cont'd)

B. Rehabilitation of the Existing Evaporation Pools

1. From January 1, 2005, the Ramat Hovav Industrial Council will commence activities to dry out and rehabilitate the area of the evaporation pools spanning an area of about 1,500 dunams, in an attempt to complete such drying out and rehabilitation activities no later than the end of 2012.
2. The Ramat Hovav Industrial Council will submit a detailed plan along with timetables for the drying out and rehabilitation of the area of the evaporation pools for approval by the Ministry of Environmental Protection by December 31, 2004.

C. Treatment of Air Pollution

The Ministry of Environmental Protection will formulate and operate a plan for prevention of exceptional emissions of dangerous substances into the air in the Ramat Hovav Industrial Area.

Regarding the possible consequences of the said Government decision on the Company's activities, see Section 4, above.

D. Claims against subsidiaries

- (1) A claim has been submitted against Milenia on the grounds that a certain process it uses is a protected trade secret, which was copied from the plaintiff. Accordingly, Milenia is demanded to indemnify the plaintiff for unfair competition at an amount of approximately US\$ 9 million (based on a calculation of the amount of the material used). Furthermore, the plaintiff demands that Milenia be fined US\$ 25 per day, in respect of the unlawful use of trade secrets.

In February 2004, Milenia and the plaintiff reached a settlement with no indemnity to the parties, under which each of the parties paid fees to their own attorneys. The total cost to Milenia amounted to approximately US\$ 0.2 million.

- (2) In 1995, a claim was submitted against Milenia and a number of other parties for a total amount of approximately US\$ 36 million by a group which purchased the rights of two banks which went bankrupt. The remainder of the claim is being submitted against Milenia in its capacity as a guarantor for agricultural cooperatives, which were its former shareholders.

Milenia's position is that it was excluded from the guarantee agreement by a later agreement between the bank, the former shareholders and the other subsidiary of the former shareholders. A provision of approximately US\$ 2 million was recorded in the financial statements for this claim, based on a possibility of settlement in due course. Milenia's position, based on an analysis by their legal advisors, is that, the provision recorded is sufficient to cover any probable losses it may have on this case.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities (cont'd)

D. Claims against subsidiaries (cont'd)

- (3) Administrative proceedings as well as civil and other fiscal claims have been submitted against Milenia totaling approximately US\$ 48.5 million. Milenia's management believes based on, inter alia, the opinion of its legal advisors, that its chances of winning in the administrative proceedings and successfully defending against the aforesaid claims and demands, are probable and the provisions included in the financial statements are sufficient to cover any losses, which may be incurred as a result of these claims.

- (4) A claim was filed against Agan in the District Labor Court,

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for payment of approximately US\$1 million, in respect of severance pay. The plaintiff contends that he was a salaried employee of Agan and that the payments made by Agan to a company which he owned must be considered his determining salary for purposes of payment of severance pay. Agan submitted a statement of defense. In the estimation of Agan's Management based on the opinion of its legal advisors, the claim's chances are remote. No provision has been included in the financial statements in respect of this claim.

- (5) A criminal complaint has been filed against Makhteshim and one of its managers by the Man, Nature and Law Amuta (Society). In the charge sheet, it is stated that in a number of cases during 1999-2002, discharges of materials were measured in the exhaust vents in Makhteshim's factory in Ramat Hovav in forbidden concentrations which created strong pollution. Makhteshim does not admit to the allegations stated in the complaint. In the estimation of Makhteshim and its legal advisors, in light of the early stage of the proceedings, it is not possible to predict the results of the complaint and/or the related exposure and, therefore, no provision has been recorded in the books in respect thereof.
- (6) A number of other claims have been filed against Agan, the total amount of which is US\$ 3.5 million, in respect of damages which, according to the plaintiffs, were caused due use of Agan's products, breach of agreement to market a product, supply of a faulty product, as well as in connection with additional claims. In Agan's estimation, based on the opinion of its legal advisors, with respect to some of these claims the chances of defense are good, while regarding some of the claims it is not possible, at this stage, to predict their outcome. Accordingly, no provisions have been recorded on the books in connection with these claims.
- (7) A number of other claims have been filed against Makhteshim, the total amount of which is US\$ 1.4 million, in respect of damages which, according to the plaintiffs, were caused by, among other reasons, use of its products as well as a claim of a supplier which provided the planning work with respect to construction of the plant in Ramat Hovav. In Makhteshim's estimation, based on the opinion of its legal advisors, with respect to some of these claims the chances of defense are good or the provisions included in the books are adequate. With respect to claims regarding which it is not possible, at this stage, to predict their outcome, no provisions have been included in the financial statements.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 19 - Commitments and Contingent Liabilities (cont'd)

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- E. Guarantees
- (1) The Company has guaranteed the liabilities to banks of a subsidiary without any limitation as to amount. As at the balance sheet date, the outstanding liabilities of the subsidiary to the banks totaled US\$ 51 million.
 - (2) The Company has guaranteed the liabilities to banks and suppliers of subsidiaries, the amount of which as at the balance sheet date totaled US\$ 42 million.
 - (3) Makhteshim and Agan have guaranteed the liabilities to banks of subsidiaries in the amount of US\$ 15 million.
 - (4) Foreign suppliers and banks have provided credit lines in the approximate amount of US\$ 137 million to foreign subsidiaries and to one subsidiary in Israel relying upon, among other things, the commitments of Makhteshim and Agan as to their proper fiscal management and the policies of Makhteshim and Agan to take steps that will enable those companies to meet their obligations. The amount of the credit lines utilized as at December 31, 2004, amounted to approximately US\$ 91 million.
 - (5) The Company and Milenia committed to indemnify financial institutions, upon the existence of certain conditions, in respect of credit received by Milenia's customers from those financial institutions, which were used for repayment of the debts of such customers to Milenia in respect of its sales to those customers. The amount of the commitment for indemnification, as at the balance sheet date, was approximately US\$ 98 million, of which approximately US\$ 80 million was a commitment for indemnification of Milenia and approximately US\$ 18 million was a commitment for indemnification of the Company and Milenia (December 31, 2003 - approximately US\$ 85 million, of which approximately US\$ 55 million was a commitment for indemnification of Milenia and approximately US\$ 30 million was a commitment for indemnification of the Company and Milenia).

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 20 - Liens and Collaterals

A. Following are details of collateralized liabilities to banks:

December 31
2004
US\$ thousands

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| | |
|--|--------|
| Current liabilities | - |
| | ===== |
| Long-term liabilities (including current maturities) | 78,632 |
| | ===== |

As collateral for the above liabilities, a subsidiary has registered a mortgage on land and buildings, and other subsidiaries have registered a first degree charge on assets including machinery and equipment, share capital and intangible assets.

- A foreign subsidiary has deposited with banks, documents for collection amounting to US\$ 17 million and other foreign subsidiary companies have registered charges on some of their assets.
- The Company and its Israeli subsidiaries have made commitments to banks not to register charges on their assets in favor of other parties, except specific liens for acquisition of an asset for the benefit of the party financing the acquisition on certain terms and subject to the giving of notification to the bank, and except for creation of liens related to receipt of investment grants, as stated in Section B, below.

In addition, the Company committed not to transfer or sell any one of its assets (except for sales in the Company's ordinary course of business and at customary market terms, including sale of trade receivables), without obtaining the bank's written consent in advance, except for the following:

- (a) Transfer to a subsidiary which did not create and will not create general liens and which commits not to pledge or sell the pledged assets without obtaining the bank's consent in advance.
 - (b) Sale or transfer of assets, the value of the Company's interest in which does not exceed US\$20 million for any particular year and provided that the cumulative value of the total assets to be transferred or sold will not exceed US\$ 60 million.
- Regarding bank deposits which serve as the sole security for repayment of loans taken by a subsidiary from that bank - see Note 8B(2).

- B. As collateral for the fulfillment of the requirements in respect of investment grants received (see Note 17A), the Company and its subsidiaries have registered floating charges in unlimited amounts on all of their assets and have provided an unlimited guarantee in favor of the State of Israel.

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Notes to the Financial Statements as at December 31, 2004

Note 20 - Liens and Collaterals (cont'd)

- C. The Company and its subsidiary have committed to banks to maintain financial criteria, the main ones of which are as follows:
- The ratio of the interest-bearing financial liabilities to shareholders' equity shall not exceed 1.0.
 - The ratio of the interest-bearing financial liabilities to income before financing expenses, taxes, depreciation and amortization (EBITDA) shall not exceed 3.3 (in subsidiary - 4).
 - The shareholders' equity will not be less than US\$ 720 million.

In the opinion of the management of the Company and its subsidiary, as at the balance sheet date the company and its subsidiary are in compliance with the aforementioned financial ratios.

Note 21 - Shareholders' Equity

A. Share capital

| | December 31 | | |
|------------------------------------|------------------|--------------------|-------------|
| | 2004-2003 | 2004 | 2003 |
| | Number of shares | | |
| | Authorized | Issued and paid-up | |
| Ordinary shares of NIS 1 par value | 500,000,000 | 402,088,045 | 377,916,800 |
| | ===== | ===== | ===== |

All of the shares are registered for trading on the Tel Aviv Stock Exchange.

B. Employee stock options

1. On April 23, 2001 (hereinafter - the determining date), the Company's Board of Directors resolved to grant options to employees of the Company and to employees of its subsidiaries. In accordance with this plan, the said employees will be allotted 17,400,000 option warrants which are exercisable for up to 17,400,000 ordinary shares of a par value of NIS 1 each, of the Company, at an exercise price of US\$ 1.882 as at the balance sheet date after adjustments made

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to all options due to a dividend distribution (the market value of a share as of April 22, 2001 was NIS 8.12).

All options warrants are to be issued to a trustee pursuant to the plan. The options were issued in accordance with Section 102 of the Income Tax Ordinance and the shares to be issued on the exercise thereof will be held by the trustee for a period of at least two years from the date of issuance of the options.

Eligibility to receive the option warrants, subject to the terms of the plan, is in three portions, as follows: One third on the determining date, an additional third after the elapse of one year from the determining date and the balance after the elapse of two years from the determining date.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 21 - Shareholders' Equity (cont'd)

B. Employee stock options (cont'd)

The options of each portion can be exercised after the elapse of one year from the date of entitlement, and they expire after the elapse of five years from the date of the beginning of the exercise period of each portion.

Pursuant to the option plan, at the time of exercise of the options the Company will issue shares in a number which reflects the amount of the monetary benefit inherent in the option, that is, the difference between the regular price of a Company share on the exercise date and the exercise price of the option.

Under this plan, the CEO of the Company will be allotted 1,400,000 option warrants exercisable into 1,400,000 ordinary shares of a par value of NIS 1 each of the Company, which constitute 8% of the total amount of options to be granted under the plan.

In 2003, 7,361,923 options were exercised by Company employees for 2,551,247 of the Company's ordinary shares of NIS 1 par value each.

In 2004, 4,159,719 options were exercised by Company employees for 2,505,938 of the Company's ordinary shares of NIS 1 par value each.

Subsequent to the balance sheet date and proximate to the date of authorization of the financial statements, approximately 262 thousand options were exercised by Company employees for 171 thousand of the Company's ordinary shares of NIS 1 par value each.

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2. On April 14, 2003 (hereinafter - "the determination date"), the Company's Board of Directors resolved to adopt an employee compensation plan for the employees of the Company and its subsidiaries and for their directors (hereinafter - "the Plan"), pursuant to which 17,000,000 options will be issued to the employees, which are exercisable for up to 17,000,000 of the Company's ordinary shares of NIS 1 par value each, at an exercise price of NIS 7.72 as at the balance sheet date after adjustments made due to a dividend distribution (the closing share price of the Company's shares on the stock exchange on the Determination Date, was NIS 9.13 per share).

All of the options will be issued under Section 102 of the Income Tax Ordinance. The options issued and the shares issued upon the exercise thereof, will be held by a trustee for a period of at least two years from the end of the year in which the options are issued.

In accordance with the Plan, at the time of exercise of the options, the Company will issue shares in an amount which reflects the amount of the monetary benefit implicit in the options, that is, the difference between the price of an ordinary share of the Company on the exercise date and the exercise price of the option.

In the framework of the Plan, Company employees who were issued options under the Company's prior employee compensation plan, which was adopted on April 23, 2001 (hereinafter - "the Prior Plan") were offered to convert the options issued to them under the Prior Plan into 12,180,000 options under the Plan. The offer was not accepted by any of the Company's employees.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 21 - Shareholders' Equity (cont'd)

- B. Employee stock options (cont'd)
2. (cont'd)

The right to exercise the options, with respect to offerees who are not included with those who received options under the Prior Plan and are converting them to options issued under the Plan, is in three increments, as follows: one-third at the end of one year from the Determination Date, an additional one-third at the end of two years from the Determination Date and the balance at the end of three years from the Determination Date. The expiration date of the options is five years from the beginning of the exercise

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period of each increment.

In the framework of the Plan, the former CEO of the Company was entitled to convert the options issued to him pursuant to the Prior Plan into 980,000 options pursuant to the Plan, which are exercisable for up to 980,000 of the Company's ordinary shares of NIS 1 par value each and which constitute 5.8% of the total options issued in the framework of the Plan. The Company's former CEO did not convert the options.

In addition, in the framework of the Plan, the Company's CEO was issued 1,600,000 options which are exercisable for up to 1,600,000 of the Company's ordinary shares of NIS 1 par value each and which constitute 9.4% of the total options issued in the framework of the Plan.

In addition, in the framework of the Plan, the Company's directors were issued a total of 1,800,000 options which constitute 10% of the total options issued in the framework of the Plan.

In 2004, 1,420,000 options were distributed to Company directors and employees.

In 2004, 105,663 options were exercised by Company employees for 64,746 of the Company's ordinary shares of NIS 1 par value.

Subsequent to the balance sheet date and proximate to the date of authorization of the financial statements, Company employees exercised 8,000 options for 5,000 of the Company's ordinary shares of NIS 1 par value.

3. Subsequent to balance sheet date, on March 8, 2005, the Company's Board of Directors resolved to adopt a new stock option plan for the officers and employees of the Company and its subsidiaries. Pursuant to the plan they will be issued up to 20,000,000 options exercisable into up to 20,000,000 ordinary shares of the Company of a par value of NIS 1 each, of which up to 3,000,000 options will be issued to the Company's CEO and directors.

Regardless of the aforementioned, the assumption regarding the full exercise of the options is purely theoretical, since the offerees that exercise the options will not actually be issued the full amount of the shares deriving from them, but only shares in an amount which reflects the amount of the monetary benefit implicit in the options, that is, the difference between the price of an ordinary share of the Company on the exercise date and the exercise price of the option.

The options are offered to the offerees at no cost. The options will be issued to the offerees in three equal portions, with the vesting period of the first portion of the plan beginning after the third and last vesting period of the employee stock option plan from 2003 (meaning after April 14, 2006).

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 21 - Shareholders' Equity (cont'd)

B. Employee stock options (cont'd)

3. (cont'd)

The exercise price is NIS 25.10, which is equal to the opening price of the Company's share on the stock exchange when the decision was made by the Company's Board of Directors (March 8, 2005).

The options of the plan will be issued to the offerees according to the provisions of Section 102 of the Income Tax Ordinance under the capital track.

The issuance under this plan is subject to the publication of all the reports required by the Securities Law - 1968 and its related regulations, the Company's General Meeting approving the issuance of the options to directors, the Income Tax Commission approving the issuance being executed according to the provisions of Section 102 under the capital track and the Stock Exchange approving registration for trading of the shares issued upon exercise of the options.

C. Acquisition of Company shares by a subsidiary

As at December 31, 2003, a subsidiary holds 7,017,152 of the Company's shares.

In March 2004, a subsidiary transferred to a third party, in an off-market transaction, 7 million shares of the Company which it held. Pursuant to the agreement, the consideration will be paid by the end of one year from the transfer date, whether in cash, linked to the share price at the same date on the stock market, or in Company shares plus 0.5% of price of the shares on the stock market. Since the consideration has not yet been received in cash, issuance of the shares in respect of the shares transferred has not yet been recorded.

During the second quarter, 1,908 thousand of the aforementioned shares were returned, for purposes of payment of the consideration in respect of acquisition of a group of companies in the United States, as stated in Note 7D(1)a above.

As at the balance sheet date, the subsidiary holds 5,108,755 of the Company's shares, which constitute 1.3% of the Company total issued and paid-up share capital.

Regarding acquisition of Mabeno, subsequent to the balance sheet date, in exchange for transfer of shares of an investee company by a subsidiary - see Note 7D(2).

Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 21 - Shareholders' Equity (cont'd)

D. Dividend distribution policy

On April 23, 2001, the Company's Board of Directors resolved to adopt a dividend policy at rates of between 15% and 30% of net annual income, beginning from 2001. In accordance with this policy an interim quarterly dividend will be distributed. The amount of the dividend will be calculated according to the net income for the quarter and will be within the limits specified above. This interim dividend will be considered as an advance on account of the annual dividend.

Application of the policy is subject to there being sufficient income for distribution on the relevant dates, to the provisions of any law regarding dividend distribution, to specific decisions of the Company's Board of Directors in respect of each distribution and to any other decision the Board of Directors is permitted to make at any time, including regarding a different designation of the Company's earnings and a change in this policy.

In March 2004, the Company's Board of Directors decided to distribute a dividend in respect of the earnings of 2003, in the amount of US\$ 7,200 thousand.

During 2004, the Company's Board of Directors decided to make three interim dividend distributions, in the total amount of US\$ 36,900 thousand.

Subsequent to the balance sheet date, the Company's Board of Directors decided to distribute a dividend in the amount of US\$ 12,700 thousand.

E. Convertible debentures and options (Series 1)

Regarding the convertible debentures and the options (Series 1) issued in the framework of a prospectus from November 2001 - see Note 15A.

In the year of account, 4,018,625 options (Series 1) were converted into 4,018,625 ordinary shares of NIS 1 par value, based on a conversion rate of 10.03 per share. The total share capital issued as a result of the conversion was US\$ 913 thousand, at a premium of US\$ 9,637 thousand.

Subsequent to the balance sheet date and proximate to the date of authorization of the financial statements, 909 thousand options were converted into 909 thousand ordinary shares of NIS 1 par value.

Regarding conversion of the debentures - see Note 15B(4).

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements as at December 31, 2004

Note 22 - Linkage Terms of Monetary Balances

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| | In or linked to US dollars | In Euro | In Brazilian reals | In or linked to another currency |
|--|----------------------------------|----------------------------------|----------------------------------|--|
| | ----- US\$ thousands ----- | ----- US\$ thousands ----- | ----- US\$ thousands ----- | ----- US\$ thousands ----- |
| December 31, 2004 | | | | |
| Assets: | | | | |
| Cash and cash equivalents | 10,751 | 14,799 | 3,418 | 10,624 |
| Short-term investments | - | 603 | - | 160 |
| Trade and other receivables | 126,638 | 74,775 | 136,831 | 51,673 |
| Long-term investments, loans and other receivables | 1,710 | 328 | 15,715 | 1,239 |
| | ----- | ----- | ----- | ----- |
| | 139,099 | 90,505 | 155,964 | 63,660 |
| | ===== | ===== | ===== | ===== |
| Liabilities: | | | | |
| Credit from banks | 90,949 | 11,350 | 1,814 | 5,974 |
| Trade and other payables | 158,430 | 146,850 | 64,328 | 54,287 |
| Proposed dividend | 11,200 | - | - | - |
| Long-term bank loans and other (including current maturities) and long-term liabilities | 112,319 | 9,331 | - | 6,204 |
| Liability for employee severance benefits, net | 78 | 481 | 310 | 105 |
| | ----- | ----- | ----- | ----- |
| | 372,976 | 168,012 | 66,452 | 66,570 |
| | ===== | ===== | ===== | ===== |
| December 31, 2003 | | | | |
| Assets: | | | | |
| Cash and cash equivalents | 27,662 | 8,392 | 4,457 | 6,875 |
| Short-term investments | 1,034 | 39 | - | 27 |
| Trade and other receivables | 74,126 | 98,078 | 91,149 | 48,061 |
| Long-term investments, loans and other receivables | 5,485 | 333 | 7,699 | 2,517 |
| | ----- | ----- | ----- | ----- |
| | 108,307 | 106,842 | 103,305 | 57,480 |
| | ===== | ===== | ===== | ===== |
| Liabilities: | | | | |
| Credit from banks | 52,883 | 19,035 | 2,408 | 4,733 |
| Trade and other payables | 83,708 | 147,209 | 40,562 | 32,606 |
| Proposed dividend | 7,000 | - | - | - |
| Long-term bank loans and | | | | |

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| | | | | |
|--|---------|---------|--------|--------|
| other (including current maturities) | 313,548 | 9,586 | 1,880 | 7,271 |
| Liability for employee severance benefits, net | 246 | 134 | 324 | 24 |
| | ----- | ----- | ----- | ----- |
| | 457,385 | 175,964 | 45,174 | 44,634 |
| | ===== | ===== | ===== | ===== |

With respect to futures transactions in foreign currency, see Note 32.

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Notes to the Financial Statements

Note 23 - Revenues

Consolidated

| | For the year e | |
|-----------------------------------|----------------|-------|
| | 2004 | |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| Foreign sales - | | |
| Industrial | 1,351,450 | 1 |
| Commercial | 85,007 | |
| | ----- | ----- |
| | 1,436,457 | 1 |
| | ----- | ----- |
| Domestic sales - | | |
| Industrial | 47,461 | |
| Commercial | 55,784 | |
| | ----- | ----- |
| | 103,245 | |
| | ----- | ----- |
| | 1,539,702 | 1 |
| | ===== | ===== |
| Foreign sales by geographic area: | | |
| Latin America | 428,638 | |
| Europe | 649,859 | |
| North America | 198,035 | |
| Far East | 55,467 | |
| Africa and Australia | 104,458 | |
| | ----- | ----- |
| | 1,436,457 | 1 |
| | ===== | ===== |

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Note 24 - Cost of Sales

Consolidated

| | For the year e | |
|--|------------------------|------|
| | ----- 2004 ----- | |
| | US\$ thousands | US\$ |
| | ----- | |
| Industrial: | | |
| Materials | 674,675 | |
| Labor | 71,534 | |
| Subcontractors | 5,822 | |
| Other manufacturing expenses | 111,624 | |
| Depreciation | 25,891 | |
| | ----- | |
| | 889,546 | |
| Less - expenses capitalized to fixed assets (mainly engineering salaries) | 848 | |
| Change in work in progress and finished products inventories | (43,246) | |
| | ----- | |
| | 845,452 | |
| Commercial: | | |
| Cost of merchandise sold | 98,456 | |
| | ----- | |
| | 943,908 | |
| | ===== | |

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Notes to the Financial Statements

Note 25 - Research and Development Expenses, Net

Consolidated

| | For the year e | |
|------------------------------|------------------------|------|
| | ----- 2004 ----- | |
| | US\$ thousands | US\$ |
| | ----- | |
| Payroll and related expenses | 10,508 | |
| Materials | 267 | |

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| | | |
|--|--------|-------|
| Other expenses | 9,758 | |
| | 20,533 | |
| Less - | | |
| Government participation in R&D expenses | 1,053 | |
| | ----- | ----- |
| | 19,480 | |
| | ===== | ===== |

Note 26 - Selling and Marketing Expenses

Consolidated

| | For the year e | |
|----------------------------------|----------------|-------|
| | ----- | |
| | 2004 | |
| | ----- | ----- |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| Payroll and related expenses | 52,460 | |
| Commissions and delivery costs | 70,480 | |
| Advertising | 14,049 | |
| Depreciation and amortization | 24,685 | |
| Registration | 11,504 | |
| Professional services | 6,263 | |
| Insurance to the Chief Scientist | 6,474 | |
| Royalties | 4,758 | |
| Other | 29,539 | |
| | ----- | ----- |
| | 220,212 | |
| | ===== | ===== |

Note 27 - General and Administrative Expenses

Consolidated

| | For the year | |
|---|----------------|-------|
| | ----- | |
| | 2004 | |
| | ----- | ----- |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| Payroll and related expenses | 24,743 | |
| Administrative services and directors' fees to Koor | 2,557 | |
| Depreciation and amortization | 3,359 | |
| Bad and doubtful accounts | 11,481 | |
| Professional services | 12,058 | |
| Insurance | 1,925 | |
| Other | 10,792 | |
| | ----- | ----- |
| | 66,915 | |
| | ===== | ===== |

Notes to the Financial Statements

Note 27 - General and Administrative Expenses (cont'd)

Company

| | For the year e | |
|---|----------------|-------|
| | ----- | |
| | 2004 | |
| | ----- | ----- |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| Payroll and related expenses | 6,073 | |
| Administrative services and directors' fees to Koor | 2,557 | |
| Depreciation and amortization | 269 | |
| Professional services | 3,607 | |
| Other | 2,865 | |
| | ----- | ----- |
| | 15,371 | |
| | ===== | ===== |

Note 28 - Financing Expenses, Net

Consolidated

| | For the year | |
|---|----------------|-------|
| | ----- | |
| | 2004 | |
| | ----- | ----- |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| In respect of long- term liabilities, net | 17,885 | |
| In respect of short- term liabilities and credit, net | 9,686 | |
| Less - Interest capitalized to fixed assets | - | |
| | ----- | ----- |
| Financing expenses, net | 27,571 | |
| | ===== | ===== |

Company

| | For the year e | |
|--|----------------|-------|
| | ----- | |
| | 2004 | |
| | ----- | ----- |
| | US\$ thousands | US\$ |
| | ----- | ----- |

| | |
|---|--------|
| Expenses: (*) | |
| In respect of long-term liabilities | 5,193 |
| In respect of short-term liabilities and credit | - |
| | 5,193 |
| Less: | |
| Financing income | 10,229 |
| Financing income, net | 5,036 |

* See Note 32C.

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Notes to the Financial Statements

Note 29 - Other Expenses, Net

Consolidated

| | For the year | |
|--|----------------|------|
| | 2004 | |
| | US\$ thousands | US\$ |
| Expenses with respect to devaluation of the currency and bad debts in Argentina (Note 32C) | - | |
| Expenses in respect of early retirement of employees and payment of early pension benefits | 4,802 | |
| Expenses relating to sale of trade receivables as part of securitization transaction | 1,825 | |
| Loss on sale of trade receivables as part securitization transaction | 4,374 | |
| Loss on sale of fixed assets and other, net | 1,099 | |
| Provision for loss with respect to options granted to employees of subsidiaries | 2,090 | |
| Amortization of goodwill in investee companies | 14,396 | |
| Amortization of goodwill on acquisition of products | 10,164 | |
| Write-off of fixed and other assets | 2,555 | |
| Sundry expenses (income), net | 1,430 | |
| | 42,735 | |

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Note 30 - Transactions and Balances with Related and Interested Parties

- A. Transactions with interested parties
- (1) In the ordinary course of business, Group companies conduct transactions with entities that are related parties (principally, sales of the companies' products and purchases of raw materials and services). It is impracticable to identify the abovementioned related parties and to separately record these transactions in the accounting records. Therefore, the Securities Authority has exempted the Company from providing details of immaterial transactions involving acquisitions and sales of goods and services at market value that the Company is likely to execute in the normal course of its business with Bank Leumi LeIsrael Ltd., Bank Hapoalim Ltd. and their investee companies. In any event, the Company is required to disclose any unusual transactions.
- (2) On April 1, 2000, the Company signed an agreement with Koor according to which the Company will pay Koor \$2.5 million per year for consulting and management services to be rendered by Koor to the Company. The agreement was effective up to May 2003. The agreement was extended for additional three years, effective from May 2003 (see Note 27).

In addition, the Company pays directors' fees to Koor Industries Ltd. in amounts identical to those paid to public directors, see B., below. Regarding payments made to Koor - see Section A(10), below.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 30 - Transactions and Balances with Related and Interested Parties (cont'd)

- A. Transactions with interested parties (cont'd)
- (3) The Company has an agreement covering management fees with Agan and Makhteshim according to which Agan and Makhteshim paid management fees at the rate of 1% of the annual revenues. In 2003, this agreement was revised for management fees at the rate of 1.8% of the annual revenues. In 2004, Makhteshim and Agan paid management fees to the Company amounting to US\$ 13.5 million (2003 - US\$ 10.0 million, 2002 - US\$ 9.2 million).
- (4) The Company entered in an agreement with the former CEO of Milenia (who is a director of the Company), covering non-competition and confidentiality, pursuant to which on

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April 30, 2002 (shortly after the termination of his service as Milenia's CEO), he received 1,000,000 of the Company's shares in consideration for his agreement not to compete with the Company and to protect all the Company's confidential information, provided that up to this time he complies with his obligation as stated.

The agreement is valid for a period up to the later of July 2007 or the end of 3 years from the date on which he ceases to serve as CEO, director or other position in the one of the Group companies.

- (5) In November 2002, the Company's Board of Directors decided to appoint a new CEO who took up his position in May 2003.

The Company entered into an employment agreement with the new CEO, pursuant to which the CEO will serve in his position for an unlimited period, unless one of the parties gives notice of its wish that the employment shall not be continued, by means of an advance notice of three months.

In a case of transfer of control of the Company up to July 1, 2005, where as a result the CEO's employment is discontinued, in circumstances under which he is entitled to severance benefits pursuant to law, the CEO is entitled to an annual salary, including the accompanying benefits.

- (6) A subsidiary has an agreement with STIM Holdings (1991) Ltd., a company owned by a shareholder who served as a director of the Company until September 2003, which was extended up to September 30, 2004, according to which his company will supply to the subsidiary management and business organization services, for a consideration of NIS 60,000 per month plus linkage differences based on the CPI for December 2001. In July 2004, the aforesaid shareholder ceased being an interested party.

- (7) A subsidiary has an agreement with S.H.M. Ltd., a company owned by a shareholder who served as a director of the Company until September 2003, which was extended up to September 30, 2004, according to which his company will supply to the subsidiary management and business organization services, for a consideration of NIS 60,000 per month plus linkage differences based on the CPI for December 2001. In July 2004, the aforesaid shareholder ceased being an interested party.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 30 - Transactions and Balances with Related and Interested Parties (cont'd)

A. Transactions with interested parties (cont'd)

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- (8) Regarding insurance and indemnification of interested parties
- see Note 19(A) (1) and (2).
- (9) Transactions between Makhteshim and Agan with Koor and its subsidiaries, are made in the regular course of business and on usual business terms. Set forth below are details of the transactions:

Consolidated

| | For the year ended D | |
|--|----------------------|--------------|
| | 2004 | 20 |
| | US\$ thousands | US\$ thousan |
| Management services and directors fees to Koor | 2,557 | 2,67 |
| Other related parties: | | |
| Revenues - | 5,638 | 7,54 |
| Expenses - | | |
| Selling | 1,863 | 1,59 |
| Financing | - | |

B. Benefits to interested parties

| | For the year ended D | |
|--|----------------------|--------------|
| | 2004 | 20 |
| | US\$ thousands | US\$ thousan |
| Fees to interested parties employed by the Group (*) | 1,147 | *3,65 |
| Number of interested parties | **4 | 5 |
| Fees to directors appointed by Koor Industries Ltd. | 57 | 176 |
| Number of directors | 4 | 5 |
| Fees to other directors | 75 | 57 |
| Number of directors | 6 | 5 |

(*) Including settlements in respect of employee severance benefits with the Company's former CEO. Regarding options issued to the Company's present and former CEOs, see Note 21B.

(**) In July 2004, two of the four directors ceased being interested parties - see paragraphs A7 and A8 above.

Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 30 - Transactions and Balances with Related and Interested Parties (cont'd)

C. Balances with related and interested parties

Consolidated

| | December 31 2004 |
|---|----------------------------------|
| | ----- US\$ thousands ----- |
| Trade receivables (1) - Related parties | 3,403 ===== |
| Trade payables - Related parties | 445 ===== |
| Other payables Koor Industries Ltd. | 748 ===== |
| Severance pay fund administered by related companies | 2,331 ===== |
| (1) Highest balance during the year - trade receivables | 3,403 ===== |

Bank Hapoalim Ltd. and Bank Leumi Ltd. are related parties of the Company due to their holdings in the Company through mutual funds and provident funds which they manage. Financing transactions with these parties are conducted in the ordinary course of business under normal commercial terms.

Note 31 - Earnings per Share

Share capital and net income used as the basis for the computation of basic earnings per share are as follows:

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| | For the y |
|--|------------------|
| | ----- |
| | 2004 |
| | ----- |
| Weighted-average par value of share capital (in thousands) | 432,776 ===== |
| Net income used for the computation (US\$ thousands) | 166,900 ===== |
| Interest rates used in computing earnings per share (linked to the US dollar) | 2.5% ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 31 - Earnings per Share (cont'd)

Share capital and net income used as the basis for the computation of fully diluted earnings per share are as follows:

| | For the y |
|--|------------------|
| | ----- |
| | 2004 |
| | ----- |
| Weighted-average par value of share capital (in thousands) | 457,548 ===== |
| Net income used in computing earnings per share (US\$ thousands) | 168,817 ===== |
| Interest rates used in computing earnings per share (linked to the US dollar) | 2.5% ===== |

Note 32 - Financial Instruments and Risk Management

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A. General

The Group has extensive international operations, and, therefore, it is exposed to risks that derive from exchange rate fluctuations, and to changes in interest rates, in respect of credit received. In order to reduce the overall exposure to those risks, the Group uses financial instruments, including derivative instruments and options (hereinafter - "the Derivatives"). The Group does not hold financial instruments for trading purposes.

Transactions in derivatives are undertaken with major financial institutions in Israel and abroad and, therefore, in the opinion of Group Management the credit risk in respect thereof is low.

B. Exchange rate risk management

The Group uses foreign currency derivatives - forward transactions and option contracts - in order to hedge the risk that the dollar cash flows, which derive from existing assets and liabilities and anticipated sales and costs, may be affected by exchange rate fluctuations.

Subsidiaries execute swap transactions in order to reduce the exposure to exchange rate fluctuations. In 2004 a subsidiary entered into transactions with banks for swapping dollar liabilities (loans and supplier credit) amounting to a principal of \$ 60 million with liabilities in Brazilian reais at a variable interest rate of a weighted average of 6%. The transactions will expire in 2005.

In 2004 another subsidiary and a bank entered into transactions swapping a long-term loan denominated in Colombian pesos with a variable interest of 7.7% amounting to a principal of 13 million pesos with a dollar loan bearing variable interest of the Libor rate minus 0.1%. The transactions expire in semi-annual amounts until the end of 2006.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 32 - Financial Instruments and Risk Management (cont'd)

B. Exchange rate risk management (cont'd)

As at the balance sheet date, the Company and its subsidiaries had open forward exchange contracts, which are intended to hedge exposure with respect to assets and liabilities in foreign currency, as described below:

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| | Futures transactions ----- | Foreign- currency options purchased ----- |
|---|----------------------------------|---|
| Acquisition of dollars in exchange for: | | |
| Shekels | 6.0 | 4.0 |
| Pounds sterling | 6.3 | 27.5 |
| Euro | - | 236.3 |
| Brazilian reals | 3.5 | 10.0 |
| South African rands | 6.2 | 3.1 |
| Japanese yen | 2.3 | 2.4 |
| Australian dollars | 2.0 | 17.6 |
| Swiss francs | - | - |
| Polish zloty | 6.5 | 11.5 |
| Korean Yuan | - | - |
| Swedish krona | - | - |
| | ----- | ----- |
| | 32.8 | 312.4 |
| | ===== | ===== |

| | Futures transactions ----- | Foreign- currency options purchased ----- |
|----------------------------------|----------------------------------|---|
| Sale of dollars in exchange for: | | |
| Shekels | - | 26.5 |
| Pounds sterling | - | 2.0 |
| Euro | 6.6 | 32.1 |
| Swedish krona | - | 3.0 |
| South African rands | - | - |
| Japanese yen | - | 1.4 |
| Australian dollars | - | - |
| Swiss francs | - | 7.0 |
| Polish zloty | - | - |
| Korean Yuan | - | 40.0 |
| | ----- | ----- |
| | 6.6 | 112.0 |
| | ===== | ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 32 - Financial Instruments and Risk Management (cont'd)

C. Credit risks

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General

The Group's revenues are derived from a large number of geographically-dispersed customers in many different countries. Customers include multi-national companies and manufacturing companies, as well as distributors, agriculturists and agents of plant protection chemicals manufacturers who purchase the products either as finished goods or as intermediate products in relation to their own requirements.

The agricultural sector to which most of the Group's products are directed, is characterized by lengthy periods of credit.

The financial statements contain specific provisions for doubtful debts, which properly reflect in management's estimate, the loss inherent in debts, the collection of which is in doubt. In addition, up to June 2004, the Company insured its trade receivables by means of credit insurance in a joint policy with the entire Makhteshim-Agan Group. Pursuant to the policy, the aggregate amount of credit insurance for the entire Group is an annual cumulative amount of US\$ 25 million. The insurance indemnification is limited to 90% of the debt per event. The terms of the insurance policy require the implementation of a credit control system for the entire Group which is required to operate in accordance with procedures stipulated in the insurance policy. Commencing from July 2004, the Company discontinued the said insurance because of it not being worthwhile.

Subsequent to balance sheet date, a subsidiary in Brazil purchased a credit insurance policy which insures deliveries made in Brazil as of January 1, 2005. The indemnity of the insurer is limited to 85% of the debt per event in respect of the insured customers. The total amount of insurance is anticipated to amount to an overall amount of US\$ 20 million per year.

Economic Crisis in Argentina

A serious deterioration in the political and economic situation in Argentina began in December 2001, and a situation of paralysis of the political and economic systems in the country has developed, together with almost complete uncertainty as to the future, followed by a temporary discontinuation of foreign currency trading. In January 2002, the Congress empowered the President to execute a devaluation of the Argentine Peso as against the dollar (to which the Peso was linked under the law for a period of about ten years). Following approval by Congress, the Argentine Government declared a devaluation of 29% (namely, Peso 1.4 for US\$ 1).

During February 2002, the law was changed in Argentina providing for total flexibility in the rate of exchange, and that the exchange rate of 1.4 to the dollar applying to importers and exporters no longer exists. Foreign currency trading was resumed on January 11, 2002, and the exchange rate was fixed at Peso 1.7 = US\$ 1. This rate is the applicable rate at December 31, 2001. As a result of the devaluation, the assets of the subsidiary in Argentina (mainly trade and other receivables) were eroded by US\$ 15 million. Furthermore, in view of the economic and political situation in the country in 2001, the subsidiary in Argentina recorded a one-time write-off of US\$ 8 million, mainly in respect of bad debts.

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In 2002, the severe economic crisis in Argentina continued. The Peso was devalued by additional 98% (from the rate of US\$ 1 = Peso 1.7, at December 31, 2001, to US\$ 1 = Peso 3.37, at December 31, 2002).

In March 2002, the Argentine government issued Regulation 10/02 to the Conversion Law, pursuant to which trade receivables resulting from the sale of agricultural inputs, are to be paid on the basis of the same exchange rate applying to the consideration received from the export sale of the agricultural products in respect of which those inputs were used.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 32 - Financial Instruments and Risk Management (cont'd)

C. Credit risks (cont'd)

In July 2002, the Argentine government issued Regulations 143/02 and 24/02, which cancel Regulation 10/02 and which provide the various rates for linking customer debt to the dollar in such a manner that trade receivables resulting from the sale of agricultural inputs denominated in dollars, are to be paid on the basis of the dollar exchange in effect on the date of payment, less a discount at rates between 25%-60%, in accordance with those products which used the agricultural inputs as detailed in these Regulations.

Due to the devaluation and the continuing economic crisis in Argentina, and in light of the accumulated experience regarding application of Regulations 143/02 and 24/02, in 2002, the subsidiary included an additional provision, in the amount of US\$ 10.8 million, with respect to bad debts and erosion of its assets in Argentina.

In the estimation Company Management, after the additional write-downs made in 2001 and 2002, no further material effect is expected on the results of operations and the financial position of the subsidiary in Argentina.

The Company and the subsidiaries are guarantors for the subsidiary's liabilities to banks in Argentina, in the aggregate amount of approximately US\$ 10 million.

D. Currency risks

As at December 31, 2004, monetary assets in excess of monetary liabilities in Brazilian reais amounted to approximately US\$ 90 million, monetary assets in Israeli shekels in excess of monetary liabilities in Israeli shekels amounted to approximately US\$ 75 million, and monetary liabilities in excess of monetary assets in Euro amounted to approximately US\$ 78.

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The Group has taken measures to reduce the exposure in respect to this excess as described in Note B. above.

Regarding the linked balance sheet covering monetary balances - see Note 22.

E. Fair value of financial instruments

The Group's financial instruments consist of mainly non-derivative assets and liabilities, e.g.; cash and cash equivalents, investments in deposits, other receivables, long-term investments, short-term credit, payables, loans and other long-term liabilities, as well as derivatives.

In view of their nature, the fair value of financial instruments included in working capital is usually identical or close to their carrying amount. Also the fair value of deposits and long-term receivables and loans and other long-term liabilities is close to their fair value, as these financial instruments bear interest at rates which are close to the prevailing market rates.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 33 - Segment Information

A. Geographical segments according to location of assets

For the year ended December 31, 2004

| | Israel US\$ thousands ----- | Latin America US\$ thousands ----- | Europe* US\$ thousands ----- | Ad US\$ ----- |
|------------------------------|-----------------------------------|--|------------------------------------|---------------------|
| Income | | | | |
| Income from external sources | 937,769 | 337,123 | 264,810 | |
| Inter-segment income | 95,558 | 13,084 | 25,722 | |
| | ----- | ----- | ----- | ----- |
| Total income | 1,033,327 | 350,207 | 290,532 | |
| | ===== | ===== | ===== | ===== |
| Segment results** | 146,996 | 56,764 | 61,260 | |
| | ===== | ===== | ===== | ===== |

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| | | | | |
|--------------------------------|-----------|---------|---------|-------|
| Additional information | | | | |
| Assets utilized by the segment | 1,148,344 | 414,428 | 371,795 | |
| | ===== | ===== | ===== | ===== |
| Liabilities of the segment | 499,168 | 255,637 | 286,511 | |
| | ===== | ===== | ===== | ===== |
| Capital investments | 139,031 | 8,631 | 7,823 | |
| | ===== | ===== | ===== | ===== |
| Depreciation and amortization | 60,437 | 9,352 | 12,835 | |
| | ===== | ===== | ===== | ===== |

* Mainly products manufactured by non-Group companies.

** Includes amortization of goodwill on the acquisition of products and amortization of assets arising on the acquisition of subsidiaries.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 33 - Segment Information (cont'd)

A. Geographical segments according to location of assets (cont'd)

For the year ended December 31, 2003

| | Israel US\$ thousands | Latin America US\$ thousands | Europe* US\$ thousands | Ad US\$ |
|------------------------------|--------------------------|---------------------------------|---------------------------|------------|
| | ----- | ----- | ----- | ----- |
| Income | | | | |
| Income from external sources | 684,619 | 246,757 | 245,879 | |
| Inter-segment income | 57,431 | 18,360 | - | |
| | ----- | ----- | ----- | ----- |
| Total income | 742,050 | 265,117 | 245,879 | |
| | ===== | ===== | ===== | ===== |
| Segment results** | 92,520 | 47,466 | 48,326 | |
| | ===== | ===== | ===== | ===== |

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| | | | | |
|--------------------------------|---------|---------|---------|-------|
| Additional information | | | | |
| Assets utilized by the segment | 977,530 | 342,542 | 334,832 | |
| | ===== | ===== | ===== | ===== |
| Liabilities of the segment | 417,921 | 211,166 | 288,523 | |
| | ===== | ===== | ===== | ===== |
| Capital investments | 47,685 | 9,300 | 6,316 | |
| | ===== | ===== | ===== | ===== |
| Depreciation and amortization | 51,022 | 12,413 | 12,238 | |
| | ===== | ===== | ===== | ===== |

* Mainly products manufactured by non-Group companies.

** Includes amortization of goodwill on the acquisition of products and amortization of assets arising on the acquisition of subsidiaries.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 33 - Segment Information

A. Geographical segments according to location of assets

For the year ended December 31, 2002:

| | Israel US\$ thousands | Latin America US\$ thousands | Other US\$ thousands | Ad US\$ |
|------------------------------|--------------------------|---------------------------------|-------------------------|------------|
| | ----- | ----- | ----- | ----- |
| Income | | | | |
| Income from external sources | 616,470 | 196,804 | 77,589 | |
| Inter-segment income | 43,500 | 7,820 | - | |
| | ----- | ----- | ----- | ----- |
| Total income | 659,970 | 204,624 | 77,589 | |
| | ===== | ===== | ===== | ===== |
| Segment results* | 98,302 | 25,026 | 3,750 | |
| | ===== | ===== | ===== | ===== |
| Additional information | | | | |

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| | | | | |
|-----------------------------------|--------------------|------------------|------------------|-------|
| Assets utilized by the segment | 1,055,519 ===== | 323,230 ===== | 244,807 ===== | ===== |
| Liabilities of the segment | 590,604 ===== | 213,214 ===== | 206,175 ===== | ===== |
| Capital investments | 278,215 ===== | 12,174 ===== | 1,270 ===== | ===== |
| Depreciation and amortization | 46,048 ===== | 9,309 ===== | 2,748 ===== | ===== |

* Includes amortization of goodwill on the acquisition of products and amortization of arising on the acquisition of subsidiaries.

- Regarding the breakdown of sales based on geographic area - see Note 23.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 33 - Segment Information (cont'd)

B. Business segments

| | Year ended | |
|--|----------------|-------|
| | 2004 | |
| | US\$ thousands | US\$ |
| | ----- | ----- |
| Sales by products | | |
| Plant protection products | 1,357,913 | 1 |
| Others (non-plant protection products) | 181,789 | |
| | 1,539,702 | 1 |
| | ===== | ===== |

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| | December 31, 2004 | | |
|---|--|------------------------|-------|
| | Assets utilized by the sector | Capital investments | ut |
| | US\$ thousands | US\$ thousands | US\$ |
| Segment assets and capital investments | | | |
| Plant protection products | 1,722,458 | 133,188 | 1 |
| Others (non-plant protection products) | 212,109 | 22,297 | |
| | ----- | ----- | ----- |
| | 1,934,567 | 155,485 | 1 |
| | ===== | ===== | ===== |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements

A. Material Differences between Israeli GAAP and US GAAP

The Company's consolidated financial statements conform with Israeli generally accepted accounting principles ("Israeli GAAP"), which differs in certain material respects from generally accepted accounting principles in the United States of America ("US GAAP") as described below:

1. Deferred taxes
 - a) Measurement differences

In accordance with Israeli GAAP:

Deferred taxes should be recognized in respect of differences related to assets and liabilities that result from translation of the local currency into the functional

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currency using historical exchange rates and that result from (1) changes in exchange rates or (2) indexing for tax purposes.

In accordance with US GAAP:

According to paragraph 9(f) of FAS No. 109, deferred tax liabilities or assets are not provided for differences related to assets and liabilities that are remeasured from the local currency into the functional currency and that result from (1) changes in exchange rates or (2) indexing for tax purposes.

b) Earnings from "Approved Enterprises"

Under the Israeli Law for the Encouragement of Capital Investments, 1959, an "approved enterprise" which chooses the "alternative benefits" track is exempt from income tax on undistributed profits.

In the event that a dividend is distributed out of tax-exempt earnings of the "approved enterprise" under the "alternative benefits" track, the distributing company will be subject to a 25% tax on the distributed earnings.

Furthermore, the shareholders will be liable for tax at the rate of 15%. However, if the shareholder is a company, that shareholder will be entitled to a 15% tax credit, if and when such dividend out of "approved enterprise" earnings is distributed to its shareholders.

In accordance with Israeli GAAP:

Deferred taxes should not be provided in respect of the undistributed tax-exempt earnings of an "approved enterprise" of subsidiaries, whose earnings have been reinvested and will not be distributed to their shareholders.

The Company has not provided deferred taxes in respect of undistributed tax-exempt earnings attributed to the "approved enterprise" of subsidiaries, which may be distributed, since it is the Group's policy not to initiate such a dividend distribution.

In accordance with US GAAP:

Deferred taxes should be provided on the excess of the financial statement carrying value over the tax basis of an investment in domestic subsidiary as the company does not have any means under local tax law to recover this difference in a tax-free manner.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

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Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Material Differences between Israeli GAAP and US GAAP (cont'd)

2. Share-based payments to employees

In accordance with Israeli GAAP:

No expense is recorded with respect to options granted to employees of the Company.

In accordance with US GAAP:

The Company issued stock appreciation rights that under APB 25 and FIN 28 should be accounted as variable options to employees relating to the future performance of work or services. In such cases, the benefit is charged to salary expense in the statement of income. The "benefit component" is measured as the difference between the market price of the share and the exercise price of the option at the end of each reporting period, and the proportional part of the period which has passed, in relation to amounts previously recorded at the beginning of that reporting period.

3. Financial derivatives

In accordance with Israeli GAAP:

The Company applies FAS 52, FAS 80 and EITF 90-17 to account for derivatives. Accordingly, the gains and losses on derivative instruments held for hedging purposes are recognized in the statement of income concurrently with gains or losses on the hedged assets. Certain derivative financial instruments, which are not intended for hedging purposes are presented in the balance sheet at their fair value. Changes in fair value are included in the statement of income in the period in which they occur.

In accordance with US GAAP:

All derivative instruments are recognized as either assets or liabilities in the balance sheet and are measured at fair value. Changes in the fair values of derivative instruments are recognized currently in earnings since the specific hedge accounting criteria are not met.

4. Goodwill

In accordance with Israeli GAAP:

Goodwill is amortized over its economic life but no more than 20 years. Goodwill is examined for a decrease in value where there are indications that there has been a permanent decrease in the value of the goodwill.

In accordance with US GAAP:

Goodwill balances is not amortized but is examined by means of an impairment test carried out at least once a year on a fixed date in

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accordance with the directives in FAS 142, where in the first year of implementation the impairment test was on January 1, 2002.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Material Differences between Israeli GAAP and US GAAP (cont'd)

4. Goodwill (cont'd)

In accordance with US GAAP: (cont'd)

A two-step impairment test is used to identify potential goodwill impairment and measure the amount of a goodwill impairment loss to be recognized (if any). The first step of the goodwill impairment test, used to identify potential impairment, compares the fair value of a reporting unit with its carrying amount, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, including goodwill, the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired, thus the second step of the impairment test is unnecessary. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test shall be performed to measure the amount of impairment loss, if any.

The second step of the goodwill impairment test, used to measure the amount of impairment loss, compares the implied fair value of reporting unit goodwill with the carrying amount of that goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss shall be recognized in an amount equal to the excess.

5. Stock options issued by investee companies

In accordance with Israeli GAAP:

The Investor is required to create a provision for losses, which it may incur from the dilution of its holdings in investee companies, when it is probable that the securities will be converted.

In accordance with US GAAP:

A loss of the parent company resulting from the dilution of its holdings, because of securities being converted is recorded only at the time of the conversion.

6. Capitalization of licensing costs

In accordance with Israeli GAAP:

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Certain costs incurred by the Company in connection with the registration process to obtain licenses to sell products in various jurisdictions are capitalized.

In addition, amounts which are paid by the Company to the original registrant as data compensation costs only after the EPA issues a registration to the Company are also capitalized.

The capitalized licensing costs are amortized over the expected benefit period.

In accordance with U.S. GAAP:

The costs incurred by the Company in connection with the registration process to obtain licenses to sell products in various jurisdictions are deemed development costs under U.S. GAAP and are expensed as incurred.

The amounts paid by the Company to the original registrant as data compensation costs only after the EPA issues a registration to the Company are capitalized and amortized over the expected benefit period.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Material Differences between Israeli GAAP and US GAAP (cont'd)

7. Dividend Declared after the Balance Sheet Date

In accordance with Israeli GAAP:

Dividends declared subsequent to the balance sheet date are reflected as a deduction of retained earnings.

In accordance with US GAAP:

Dividends declared subsequent to the balance sheet date are deducted from retained earnings in the period in which the dividend was declared.

8. Liabilities for employee severance benefits

In accordance with Israeli GAAP:

Amounts funded by purchase of insurance policies and by deposits with recognized severance pay funds are deducted from the related severance pay liability, which is then presented at a net amount.

In accordance with US GAAP:

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The amounts funded would be presented as other long-term assets and the amount of the liability would be presented under long-term liabilities.

9. Convertible debentures

In accordance with Israeli GAAP:

If a conversion of the debentures is expected, the debentures are presented in the balance sheet in a separate category between "long-term liabilities" and "shareholders' equity", whereas, if the conversion of the debentures is not expected they are presented in the balance sheet as part of "long-term liabilities".

In accordance with US GAAP:

All convertible debentures are presented in the balance sheet as part of "long-term liabilities".

10. Contingent consideration

In accordance with Israeli GAAP:

Contingent consideration in respect of acquisition of investee companies is recorded as part as the purchase cost when it is expected to be paid.

In accordance with US GAAP:

Contingent consideration is recorded as part of the purchase cost only when the payment probability is beyond any reasonable doubt which generally is the date that the contingency is resolved.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Material Differences between Israeli GAAP and US GAAP (cont'd)

11. Earnings per share:

In accordance with Israeli GAAP:

In accordance with Opinion No. 55 of the Institute of Certified Public Accountants in Israel, the dilutive effect of share options and convertible debentures is included in the computation of basic earnings per share only if their exercise or conversion is considered to be probable. Calculation of the probability is based on the ratio

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between the market price of the shares and the present value of the price of exercising the stock options into shares or the present value of the payments for conversion of the debentures into shares.

In accordance with US GAAP:

In accordance with FAS 128 "earnings per share" - basic earnings per share are computed on the basis of the weighted average number of shares outstanding during the year. Diluted earnings per share are computed on the basis of the weighted-average number of shares outstanding during the year, plus the dilutive potential effect of ordinary share options considered to be outstanding during the year using the treasury stock method.

12. Comprehensive income

In accordance with Israeli GAAP:

Presentation of comprehensive income and other comprehensive income is not required. In accordance with US GAAP:

An enterprise (a) classifies items of other comprehensive income by their nature in the financial statements and (b) presents the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in capital in the equity section of the balance sheet.

13. Purchase of minority shares of Agan

In accordance with Israeli GAAP:

The purchase of minority shares of Agan in May 1998 (Note 1B) was accounted according to recorded amounts.

In accordance with US GAAP:

Under FTB 85-5 the purchase of the minority shares was accounted at fair value.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

A. Material Differences between Israeli GAAP and US GAAP (cont'd)

14. Statements of cash flows

(a) Translation differences in respect of cash and cash equivalents

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In accordance with Israeli GAAP:

The statements shall report the effect of exchange rate changes on cash and cash equivalents balances held in foreign currencies, only in "autonomous foreign entities", in a separate part of the reconciliation of the change in cash and cash equivalents during the period.

In accordance with US GAAP:

The statements shall report the effect of exchange rate changes on all cash and cash equivalents balances held in foreign currencies as a separate part of the reconciliation of the change in cash and cash equivalents during the period.

(b) Securitization transaction (see Note 3)

In accordance with Israeli GAAP:

The securitization transaction was classified as a sale of trade receivables. Thus, cash flows, derived from that transaction, were classified as cash flows from operating activities.

In accordance with US GAAP:

Until June 30, 2003 the securitization transaction did not meet the criteria set out by FAS 140 for the classification as a sale of trade receivables and was classified as a secured borrowing. Therefore, cash flows derived from this transaction until June 30, 2003 were classified as cash flows from financing activities.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

- B. The effect of the material differences between Israeli and US GAAP on the financial statements
 - 1. Statements of income:
 - a) Net income:

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| | Year end | |
|---|----------|-------|
| | ----- | |
| | 2004 | US\$ |
| | ----- | ----- |
| Net income as reported, according to Israeli GAAP | 165,527 | |
| | ----- | |
| Deferred taxes (A1) | (15,861) | |
| Share-based payments to employees (A2) | (26,185) | |
| Financial derivatives (A3) | (10,374) | |
| Amortization of goodwill (A4) | 10,569 | |
| Stock option issues by investee companies (A5) | 1,760 | |
| Capitalization of licensing costs (A6) | (5,325) | |
| | ----- | |
| | 120,111 | |
| Income tax in respect of the above differences | 3,736 | |
| Minority interest in respect of the above differences | (109) | |
| | ----- | |
| Net income according to US GAAP | 123,738 | |
| | ===== | |

b) Earnings per ordinary share

| | Year end | |
|---|----------|-------|
| | ----- | |
| | 2004 | US\$ |
| | ----- | ----- |
| Basic earnings per ordinary share: | | |
| As reported according to Israeli GAAP | 0.39 | |
| | ===== | |
| As reported according to US GAAP | 0.32 | |
| | ===== | |
| Weighted average of number of shares and share equivalents according to US GAAP | 383,907 | |
| | ===== | |
| Fully diluted earnings per ordinary share: | | |
| As reported according to Israeli GAAP | 0.37 | |
| | ===== | |
| As reported according to US GAAP | 0.28 | |
| | ===== | |
| Weighted average of number of shares and equivalents according to US GAAP | 446,098 | |
| | ===== | |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

- B. The effect of the material differences between Israeli and US GAAP on the financial statements (cont'd)
2. Balance sheet:

| | December 31, 2004 | | | Dece |
|--|-------------------|-------------|---------|-------------|
| | As reported | Adjustments | US GAAP | As reported |
| | US\$ thousands | | | US |
| Other receivables(1) | 77,219 | 5,323 | 82,542 | 54,538 |
| Long-term investments, loans and receivables (4) | 22,070 | 15,957 | 38,027 | 18,044 |
| Intangible assets after amortization(2) (3) (6) (10) | 527,420 | 26,161 | 553,581 | 448,402 |
| Other payables(3) (5) | 192,405 | 14,685 | 207,090 | 150,541 |
| Deferred taxes, net(1) | 54,354 | 8,674 | 63,028 | 43,778 |
| Employee severance benefits, net(4) | 26,709 | 15,957 | 42,666 | 24,774 |
| Minority interest(7) (12) | 18,756 | (1,981) | 16,775 | 6,436 |
| Capital reserve(8) (9) (10) | (2,568) | 128,993 | 126,425 | (5,393) |
| Proposed dividend subsequent to balance sheet date(11) | 12,700 | (12,700) | - | 7,200 |
| Retained earnings((1)2) | 345,841 | (106,187) | 239,654 | 229,914 |
| Shareholders' equity | 874,495 | 10,106 | 884,601 | 693,541 |

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- (1) Change in deferred taxes.
- (2) Reversal of systematic amortization related to goodwill.
- (3) Reconciliation of additional goodwill related to contingent consideration.
- (4) Reconciliation of deposits funded in respect of severance pay.
- (5) Recognition of all derivatives at fair value.
- (6) Capitalization of licensing costs.
- (7) Elimination of provisions for potential losses resulting from dilution of holding in investee companies.
- (8) Share options issued to employees.
- (9) Cumulative foreign currency translation adjustments with respect to GAAP differences.
- (10) Purchase of minority shares of Agan.
- (11) Dividend declared subsequent to balance sheet date.
- (12) Effects of the reconciliation to US GAAP.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

B. The effect of the material differences between Israeli and US GAAP on the financial statements (cont'd)

3. Comprehensive income

"Comprehensive income" consists of the change, during the current period, in Company's shareholder equity that does not derive from shareholders' investments or from the distribution of income to shareholders.

Comprehensive income include two components - net income and other comprehensive income. Net income is the earning stated in the statement of operations and other comprehensive income include amounts recorded directly to shareholders' equity that do not derive from transactions with shareholders.

| Year ended December 31 | |
|------------------------|------|
| 2004 | 2003 |
| US\$ thousands | |

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| | | |
|--|---------|--------|
| Net income according to US GAAP | 123,738 | 56,071 |
| | ----- | ----- |
| Other comprehensive income, net of nil tax: | | |
| Adjustments from translation of financial statements of investee companies | 2,825 | 1,886 |
| | ----- | ----- |
| Total comprehensive income | 126,563 | 57,957 |
| | ===== | ===== |

4. Statements of cash flows

| | Year ended December | |
|---|---------------------|-----------|
| | 2004 | 2003 |
| | US\$ thousands | |
| | ----- | |
| Net cash flows generated by operating activities: | | |
| According to Israeli GAAP | 215,653 | 249,240 |
| Effect of change in exchange rate on cash (A14a) | (1,997) | (5,434) |
| Classification of securitization transaction (A14b) | - | (48,226) |
| | ----- | ----- |
| According to US GAAP | 213,656 | 195,580 |
| | ===== | ===== |
| Net cash flows generated by financing activities: | | |
| According to Israeli GAAP | (82,033) | (155,926) |
| Classification of securitization transaction (A14b) | - | 48,226 |
| | ----- | ----- |
| According to US GAAP | (82,033) | (107,700) |

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 34 - Material Differences Between Israeli and US GAAP and their Effect on the Financial Statements (cont'd)

B. The effect of the material differences between Israeli and US GAAP on the financial statements (cont'd)

4. Statements of cash flows (cont'd)

Translation differences in respect of cash balances of autonomous foreign investee companies:

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| | Year ended December | |
|--|---------------------|-------|
| | 2004 | 2003 |
| | US\$ thousands | |
| Translation differences in respect of cash balances: | | |
| According to Israeli GAAP | - | - |
| Effect of change in exchange rate on cash (A14a) | 1,997 | 5,434 |
| According to US GAAP | 1,997 | 5,434 |

Note 35 - Events (Unaudited) Subsequent to the Date of the Independent Auditors' Report

1. Subsequent to the date of the Independent Auditors' Report and proximate to July 13, 2005, NIS 5,359 thousand par value debentures (Series A) were converted into 539 thousand of the Company's ordinary shares of NIS1 par value, and US\$ 133,650 thousand par value of the debentures that were allotted in March 2004 in a private placement to institutional investors (hereinafter - "The Debentures") were converted into 29,429 thousand shares of the Company's ordinary shares of NIS 1 par value. Furthermore, at the aforesaid period, 2,182 thousand options (Series 1) were exercised for 2,182 thousand of the Company's ordinary shares of NIS 1 par value.
2. Until December 31, 2004 it was not anticipated that The Debentures would be converted and accordingly they were presented according to their liability value as part of the long-term liabilities. Proximate to July 13, 2005, management of the Company believes that conversion of The Debentures is probable and accordingly the balance of The Debentures will be classified (together with the Series A debentures) at their liability value as a separate balance sheet item between the long-term liabilities and the shareholders' equity.
3. As described in Note 21B(3), on March 8, 2005, the Company's Board of Directors decided to adopt a new option plan for officers and employees of the Company and its subsidiaries. Pursuant to the plan, 14,900,000 option warrants exercisable into up to 14,900,000 ordinary shares of the Company of a par value of NIS 1 each were issued on March 14, 2005. Of these, 800,000 option warrants were issued to the CEO of the Company, 9,600,000 to the employees of the Company in Israel, 2,000,000 to the employees of the Company abroad and 2,500,000 were deposited with a trustee for future distribution.

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Makhteshim-Agan Industries Ltd.

Notes to the Financial Statements

Note 35 - Events (Unaudited) Subsequent to the Date of the Independent Auditors' Report (cont'd)

4. Subsequent to the date of the Independent Auditors' Report and proximate to July 13, 2005, Company employees exercised approximately 714 thousand options granted in April 2001 (as described in Note 21B(1)) for 493 thousand of the Company's ordinary shares of NIS 1 par value each.
5. Subsequent to the date of the Independent Auditors' Report and proximate to July 13, 2005, Company employees exercised approximately 166 thousand options granted in April 2003 (as described in Note 21B(2)) for approximately 119 thousand of the Company's ordinary shares of NIS 1 par value.
6. In May 2005, the Company's Board of Directors resolved to distribute an interim dividend, in the amount of US\$ 18.3 million, to be paid on September 1, 2005.

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Makhteshim-Agan Industries Ltd.

Appendix to the Financial Statements

Rate of Control and Ownership in Subsidiaries as at December 31, 2004

A. Domestic consolidated subsidiaries

Holding company

Investee company

Makhteshim-Agan Industries Ltd.

Makhteshim Chemical Works Ltd. (Makhteshim)
Agan Chemical Manufacturers Ltd. (Agan)
Lycored - Natural Products Industries Ltd. (Lycor)
Luxembourg Medicine Ltd.

Makhteshim

Prisma Industries Ltd.
Negev Peroxide - Registered Partnership

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| | |
|---------------------------------------|--|
| Agan | Agan Aroma Chemicals Ltd. Agan Chemical Marketing Ltd. |
| Lycored | Bio-Dar Ltd. Dalidar Pharma Israel (1995) Ltd. |
| Luxembourg Medicine Ltd. | Isramedcom Ltd Luxvision Ltd. (formerly Curex Ltd.) |
| B. Foreign consolidated subsidiaries | |
| Makhteshim | Celsius Property B.V. (Celsius) |
| Agan | Fahrenheit Holding B.V. (Fahrenheit) |
| Lycored | Nutriblend International Sarl ALB Holdings UK |
| ALB Holdings UK | Nutriblend Ltd. |
| Makhteshim and Agan in equal parts | Makhteshim Agan Holding B.V. |
| Celsius | Irvita Plant Protection N.V. |
| Irvita Plant Protection N.V. | White Rock Insurance Company PCC Limited/Macell |
| Fahrenheit | Quena Plant Protection N.V. |
| Celsius and Fahrenheit in equal parts | Magan HB B.V. Aragonesas Agro S.A. Magan Argentina S.A. Proficol S.A. Proficol Andina N.V. |
| Magan HB B.V. | MAB Participacoes S/C Ltd. |
| MAB Participacoes S/C Ltd. | Milenia Participacoes S.A |
| Milenia Participacoes S.A. | Milenia Paraguay S.A. Emerald Agrochemical Company AVV Milenia Biotecnologia e Genetica Ltd. Milenia Agro Ciencias S.A. Defensa S.R.L. |
| Proficol S.A. | Proficol Venezuela S.A. |
| Proficol Andina N.V. | Rice Co. LLC (USA) |

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Makhteshim-Agan Industries Ltd.

Appendix to the Financial Statements

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B. Foreign consolidated subsidiaries (cont'd)

Holding company

Investee company

Makhteshim Agan Holding B.V

Makhteshim Agan Costa Rica S.A.
 Makhteshim Agan Espana S.A.
 Makhteshim Agan of North America Inc.
 Makhteshim Agan France S.A.R.L.
 Makhteshim Agan (UK) Ltd.
 Makhteshim Agan Romania S.R.L.
 Makhteshim Agan (Thailand) Ltd.
 Agricur Defensivos Agricolas Ltd.
 Makhteshim Agan Italia S.R.L.
 Makhteshim Agan South Africa PTY Ltd.
 Magan Korea Co. Ltd.
 Makhteshim Agan India Private Ltd.
 Makhteshim Agan Poland SP. zo.o
 Magan Holding Germany GmbH
 Makhteshim Agan Sweden AB
 Makhteshim Agan Portugal Ltd.
 Magan Japan Co. Ltd.
 Magan Italia S.R.L
 MA U.S. Holding Inc. (USA)

Agronica Australasia Pty
 Limited Australia

Magan Holding Germany GmbH

Feinchemie Schwebda GmbH
 Makhteshim Agan Deutschland GmbH

Feinchemi Schwebdan GmbH

FCS France S.A
 Feinchemi (UK) Ltd.

MA U.S. Holding Inc. (USA)

Farm Saver Group
 Control Solutions Inc.

Agronica Australasia Pty
 Limited Australia

Farmoz Pty Limited

C. Companies Proportionately Consolidated

Makhteshim Agan Industries

Biotec M.A.H. Management Ltd
 Biotec M.A.H. - Registered Partnership

Biotec M.A.H -
 Registered Partnership

Biotec Agro Ltd.

Makhteshim Agan Holdings B.V.

Alfa Agricultural Supplies S.A.

Fahrenheit

InnovAroma S.A.

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D. Affiliated companies

Makhteshim

Fibertec Fiberglass Ltd.

Makhteshim and Agan hold shares in other foreign companies which retain registration rights to certain products sold outside of Israel.

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