

*ICL-ISRAEL CHEMICALS LTD.*  כימיקלים לישראל בע"מ

# **Periodic Report**

## **Description of Corporate Activity**

**For the Period Ended December 31, 2006**

Translation from Hebrew. The binding version is the original Hebrew version.

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# **DESCRIPTION OF CORPORATE ACTIVITY FOR THE YEAR ENDED DECEMBER 31, 2006**

## **Chapter 1 – General**

The Board of Directors of Israel Chemicals Ltd. (hereinafter the “**Company**”) is honored to present this description of corporate activity as of December 31, 2006, which encompasses a description of the corporation and the development of its business activities as they occurred during 2006 (hereinafter the “**Report Period**”). This report has been prepared in accordance with the Securities Regulations (Periodic and immediate reports), 5730 – 1970. The financial statements in this report are stated in US dollars according to its value as of December 31, 2006 (“**dollar**”).

Facts that appear in this report “as of the date of the report” are current as of March 27, 2007, unless otherwise stated.

The materiality of the information included in this periodic report, including the description of material transactions, has been evaluated from the Company’s perspective. In some cases the description has been expanded in order to give a broad picture of the described issue.

This report is presented as part of the Company’s periodic report for 2006 and assuming that the remaining portions of the periodic report are present before the reader.

In this report, unless otherwise implied by context, the following terms will have the meanings detailed below:

<b>ICL or “the Company</b>	Israel Chemicals Ltd., including its consolidated companies
<b>Segment</b>	A managerial division of ICL as described in section 2.1.3 and section 2.2 below.
<b>ICLFE</b>	ICL Fertilizers Europe – a unit within the ICL Fertilizers segment which coordinates the activities of ICL Fertilizers in Europe
<b>DSW</b>	Dead Sea Works Ltd. of the ICL Fertilizers segment
<b>Tami</b>	Tami (IMI) Research and Development Institute Ltd. – the central research institute of ICL, part of ICL Industrial Products segment.
<b>IP</b>	Iberpotash SA – a Spanish company of the ICL Fertilizers segment
<b>BKG</b>	A company in the ICL Performance Products segment, based in Germany
<b>CPL</b>	Cleveland Potash Ltd. – a UK company of the ICL Fertilizers segment
<b>Amfert</b>	Amsterdam Fertilizers B.V. a Dutch company of the ICL Fertilizers segment
<b>F&amp;C</b>	Fertilizers and Chemical Materials Ltd. – an ICL Fertilizers company
<b>ICL PP AMERICA</b>	The assets and operations acquired from Astaris
<b>Rotem</b>	Rotem Amfert Negev Ltd., of the ICL Fertilizers segment
<b>The Bromine Company</b>	Dead Sea Bromine Company Ltd. of the ICL Industrial Products segment
<b>DSM</b>	Dead Sea Magnesium Ltd., formerly of the ICL Metallurgy segment
<b>Israel Corp</b>	The Israel Corporation Ltd., which is the controlling shareholder of ICL
<b>PCS</b>	Potash Corporation of Saskatchewan Inc., a Canadian company, the largest potash producer in the world, which is an “interested party” of the Company
<b>Salt</b>	Unless otherwise specified – sodium chloride – NaCl
<b>FAO</b>	The Food And Agriculture Organization of The United Nations – an international food organization
<b>ISO</b>	The International Management standard in various fields
<b>“Responsible Care”</b>	An international program of chemical industry companies for the advancement of health, safety and the environment
<b>“HACCP”</b>	Hazard Analysis and Control Point - A system of rules and monitoring of risk analysis and pollution prevention in the food industry, developed by the U.S. Food and Drug Administration

<b>EMAS</b>	Eco-Management and Audit Scheme – a voluntary initiative of the European Union for measurement of environmental performance beyond the minimum legal standards for the participating companies
<b>REACH</b>	Registration, Evaluation and Authorization of Chemicals – a framework within the European Union – see sections 4.1.15, 4.2.16, and 4.3.16 of the report
<b>USDA</b>	U.S. Department of Agriculture
<b>OSHA</b>	Standards published by the US Federal Occupational Safety & Health Administration Agency.
<b>Dollar</b>	U.S. dollar
<b>N</b>	The element nitrogen, one of the three main plant nutrients
<b>P</b>	The element phosphorus, one of the three main plant nutrients
<b>K</b>	The element potassium, one of the three main plant nutrients
<b>Potash</b>	KCl, used as the plant's main source of potash
<b>Phosphate</b>	Phosphate rock that contains the element phosphorus (one of the three primary elements of a plant) measured in units of P <sub>2</sub> O <sub>5</sub>
<b>Fertecon</b>	A professional publication in the fertilizer field
<b>USDA</b>	United States Department of Agriculture
<b>CRU/ British Sulfur</b>	A professional research and analysis institute – dealing with, among others, the chemical industry, fertilizers, mining and extraction
<b>IFA</b>	The International Association of Fertilizer Manufacturers

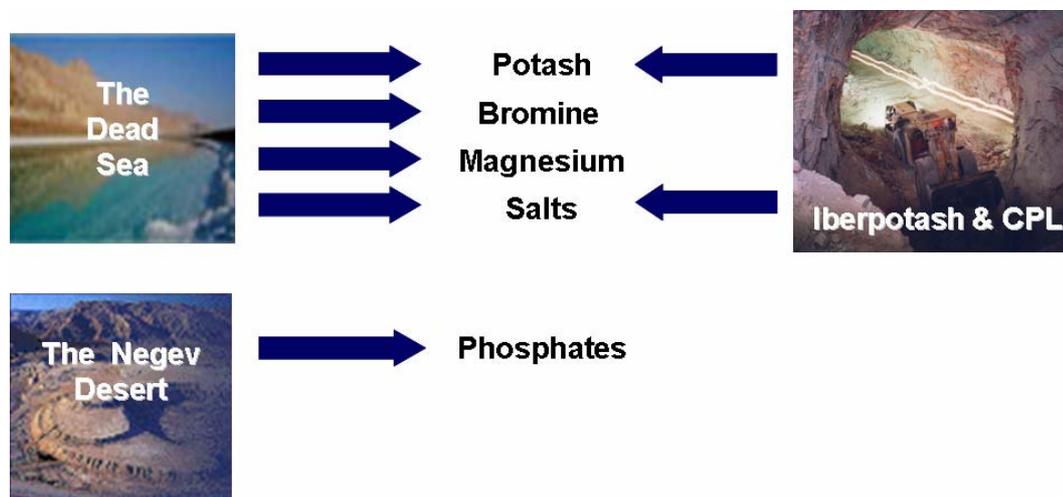
## Chapter 2 – Description of the General Development of the Corporation’s Business

### 2.1 General

#### 2.1.1 General description

ICL is a multinational company that operates mainly in the areas of fertilizers and specialty chemicals, in four segments – fertilizers, industrial products, performance products and metallurgy.<sup>1</sup>

ICL’s operations are based primarily on natural resources – potash, bromine, magnesium and sodium chloride from the Dead Sea and phosphate rock from the Negev Desert, all on the basis of concessions and licenses from the State of Israel. Operations are based as well as on potash and salt mines in England and Spain under leases and concessions from the competent authorities in those countries. ICL is active in the production of these minerals, in their sale throughout the world, and also in the development, manufacture and marketing of downstream products based primarily on these raw materials.



ICL has a prominent position in the potash and bromine markets. Potash is a core component of fertilizers. The bromine serves a wide range of applications, primarily as a basic ingredient of flame retardants. ICL’s products are used primarily in the areas of agriculture, electronics, food products, oil and gas drilling, water purification and desalination, and in the detergent, paper, cosmetics, pharmaceutical, automotive and aluminum industries. ICL has decades of accumulated experience in most of its businesses.

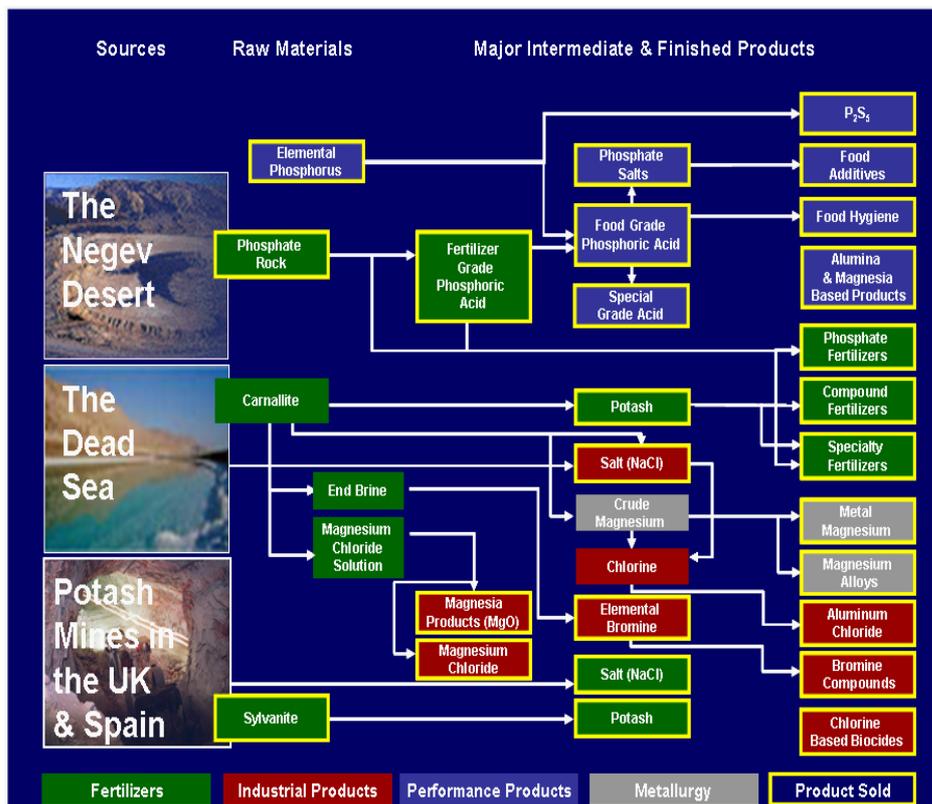
ICL has direct access to most of the raw materials required for its activities, at low cost and high quality, by virtue of the exclusive concession granted to ICL by the state of Israel for extraction of minerals from the Israeli side of the dead sea, in return for payment of royalties to the state (for details, see section 4.1.15 below). The costs of production of the potash and bromine that are extracted from the dead sea by ICL are relatively lower than the costs of other producers in the world who do not have access to the dead sea.

ICL’s main production facilities are based in Israel, Germany, the United States, Holland, Spain, England, China Brazil, and France. Furthermore, ICL has production facilities in Austria, Belgium, Turkey, Argentina, and Australia.

ICL’s operations outside of Israel are primarily in the production of products that are complimentary to or are based on ICL’s operations in Israel or related fields. Approximately 94% of ICL’s production is sold outside of Israel.

The activities of ICL’s facilities are integrated with one another, in terms of both supply of raw materials and whereby frequently one facility utilizes by-products of another facility to produce end-products (for example, bromine is produced by utilizing the bromine present in the by-product streams from the evaporation ponds used to manufacture potash, etc.)

<sup>1</sup> For details about a change in the segment structure at ICL commencing in 2007, see Section 2.2.

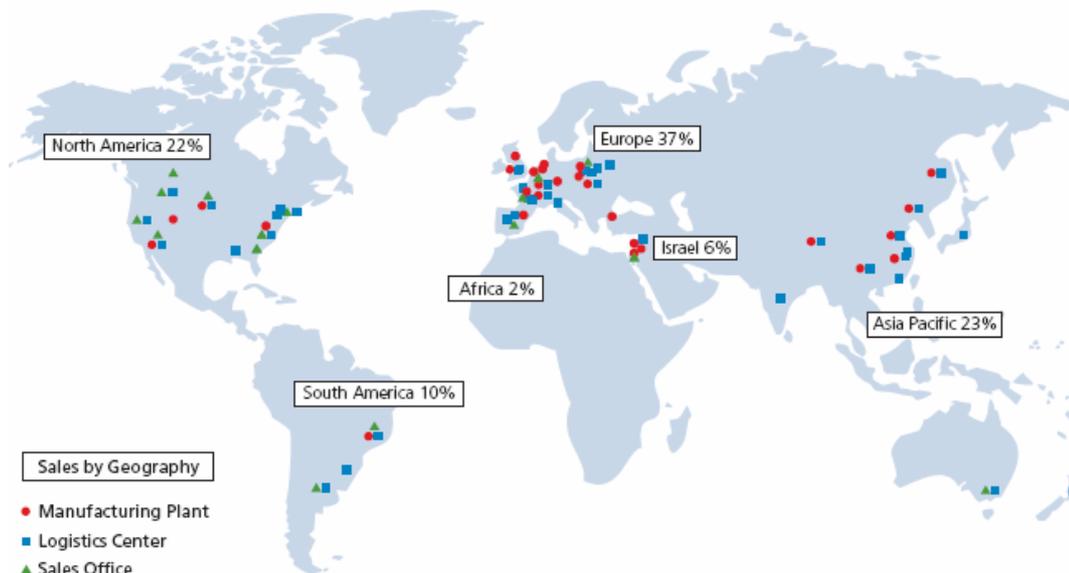


Approximately 6% of ICL's total sales occur in Israel. Regarding these sales, for some specific products, ICL and some of its companies have been declared a monopoly.

In 2006, approximately 48% of ICL's sales revenue arose from production activities taking place outside of Israel. Approximately 9% of the cost of sales of the products produced outside of Israel is attributable to raw materials supplied from Israel.

ICL has no material dependency on any single customer, supplier, or source of raw materials that are not included in the concessions granted to ICL.

The following chart shows the geographical distribution of ICL's sales in 2006:



### 2.1.2 The Company's competitive advantages

ICL believes that its business strength derives from the following competitive advantages:

- A. Direct access to natural resources - ICL has concessions for mineral production from the Dead Sea, for mining phosphate rock in the Negev Desert, and also concessions for

mining of potash and salt from underground mines in Spain and England. Around 39% of ICL's sales in 2006 were from products based on minerals that the Company produces from the Dead Sea. The Dead Sea is a vast and highly concentrated source of potash, bromine, magnesium and salt. The Dead Sea contains a supply of these raw materials that is, for all practical purposes, unlimited.

- B. Leading market positions – ICL has a leading position in the following product lines, and, in its estimation, its ranking in the world market is as follows:

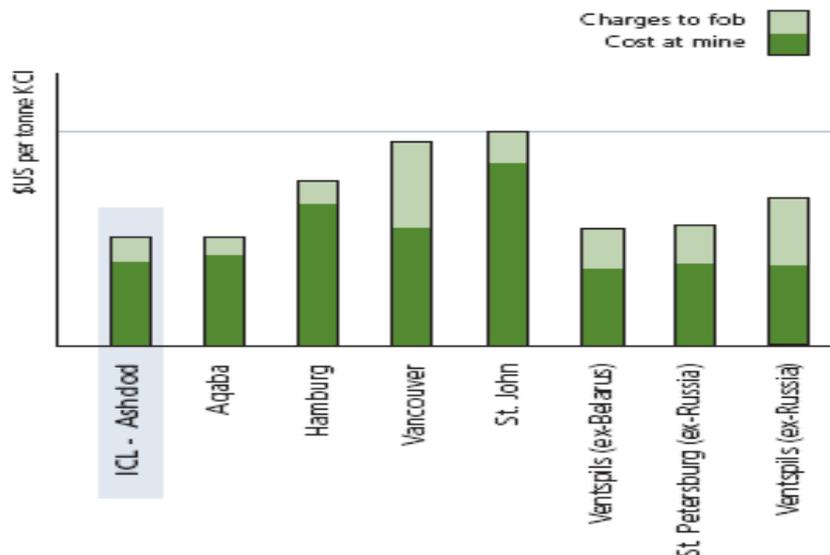
Product	Business Segment	Rank in International Market in 2006
Potash	ICL Fertilizer	Sixth
Bromine	ICL Industrial Products	First
Pure phosphoric acid	ICL Performance Products	First
Specialty phosphates	ICL Performance Products	First

Similarly, ICL has a leading position in a number of niche markets for specialty chemicals and specialty fertilizers.

- C. Low costs – ICL believes its business strength derives mainly from the location of ICL's facilities next to the Dead Sea, the relatively low cost of shipping from plant to customer, and the ability to integrate production processes, by-products and the Company's products to make the most of operational advantages.

- The relatively low production costs in Sdom derive primarily from the high concentration of minerals in the Dead Sea and the relatively low cost of their production compared with mining potash from underground deposits or extraction of bromine from less concentrated sources. In light of the fact that the Company produces and mines most of its principal raw materials on its own, the Company is less exposed to raw materials' price fluctuations than its competitors who purchase raw materials from third parties.

**COST OF POTASH PRODUCTION (\$ PER TON FOB)**



Source: British Sulphur / CRU (June 2005) (cost of production calculated for 2004 data, including royalties and mining taxes, not including depreciation and one-time expenses).

2. Production without dependence upon storage limitations - The hot and dry climate of the Dead Sea enables the Company to store, at particularly low cost, large quantities of potash in open areas. This advantage in storage capability enables the Company to produce continuously, without dependency on the fluctuations in the worldwide demand for potash.
  3. Relatively low shipping costs – ICL enjoys relatively low shipping costs due to the location of most of its facilities fairly close to seaports in Israel and worldwide. The location of ICL Fertilizers' facilities in Israel gives it a logistical advantage over some of its competitors. ICL's facilities are based in the Negev Desert, so it can ship its bulk products, through the Port of Ashdod towards Europe and South America and through the Port of Eilat towards Asia, Africa and Oceania. The Company has dedicated bulk-loading port facilities in Israel – in Ashdod and Eilat; and in Europe – in Barcelona (Iberpotash); Amsterdam; Ludwigshafen (AMFERT); and Teesside, England (CPL).
  4. Synergies - ICL benefits from synergies within the Company that reduce its production cost by, among other things, utilizing by-products and waste from one process as a raw material for another process. For example, the production of bromine is based on utilizing the bromine in the end brines resulting from potash production, where its concentration is higher than in the Dead Sea water. Magnesia is produced from brines rich in magnesium chloride that result as by-products from potash production in Sdom, and ICL Fertilizers uses a by-product of the process of producing metal magnesium (sylvinite) to produce potash, and ICL Industrial Products uses chlorine that is released by the process of producing metal magnesium, to produce bromine, etc.
- D. Manufacture of products with high added value - ICL efficiently utilizes various basic materials that are produced in its plants and turns them into downstream products with high added value. For example, ICL Fertilizers produces fertilizer-grade phosphoric acid from phosphate rock that it extracts from open-pit mines in the Negev Desert. ICL Performance Products further refines this acid into pure phosphoric acid that enables ICL Performance Products to manufacture phosphate salts, food additives and hygiene products.
- E. Significant entry barriers – ICL believes that entry of new competitors in many of its areas of business would be expensive and time-consuming. This is due to the high costs and relatively long timeframe needed for establishing production facilities of a nature similar to those of ICL, the special mining concessions that the Company holds, the intellectual property (proprietary knowledge, technologies and patents for various products and applications), and its international marketing and distribution systems.
- However, it should be emphasized that in some of the main areas of operation of the Company, existing manufacturers may well increase their production capacity.
- F. Relatively high cash flow from operations – In 2005 and 2006, the cash flow from operations of ICL was about \$491 million and \$347 million, respectively. ICL's high cash flows enable it to appropriately maintain and expand its production facilities, invest in infrastructure, establish new plants, take advantage of acquisition opportunities, distribute dividends to Company shareholders and to reduce its debt levels.
- G. Global presence with diversified businesses – ICL's international activities reduce its businesses' exposure to regional changes in different geographical areas. In addition to its geographical diversification, ICL has operations in four business lines that include a wide range of products, for use in different industries throughout the world. In 2006, the Company does not have any single customer that accounts for more than 10% of the total sales of the Company. This year, the volume of activities increased in North and South America compared with the prior year as a result of acquiring the operations of Astaris and Adicon towards the end of 2005 (see section 4.3.1).
- H. Company management – ICL's operations are managed by a management team with rich industry experience. ICL's Chief Executive Officer, most of the business segment managers and most of the senior vice presidents in the Company have more than 25 years of experience in ICL .

### 2.1.3 Corporate structure

The following chart describes the business segments of ICL in 2006:<sup>2</sup>

ICL Fertilizers	ICL Industrial Products	ICL Performance Products	ICL Metallurgy
<ul style="list-style-type: none"> <li>• Potash</li> <li>• Phosphate rock</li> <li>• Phosphoric acid (fertilizer grade)</li> <li>• Phosphate and compound fertilizers</li> <li>• Specialty fertilizers</li> <li>• Animal feed additives</li> </ul>	<ul style="list-style-type: none"> <li>• Bromine</li> <li>• Flame retardants</li> <li>• Brominated inorganic products</li> <li>• Agricultural chemicals</li> <li>• Water treatment biocides</li> <li>• Magnesia products</li> <li>• Chlorine based products</li> </ul>	<ul style="list-style-type: none"> <li>• Phosphoric acid (food grade)</li> <li>• Phosphate salts</li> <li>• Food additives</li> <li>• Food hygiene products</li> <li>• Performance products based on Alumina &amp; other chemicals</li> </ul>	<ul style="list-style-type: none"> <li>• Pure magnesium</li> <li>• Magnesium alloys</li> </ul>

### 2.1.4 Year of incorporation of the Corporation and corporate structure

ICL is a limited liability company established in 1968 as a government company.

In 1975 the shares of various development companies (including, among others, the Dead Sea Works, the companies today consolidated as Rotem Amfert Negev, the bromine companies, and Tami) were transferred from the State of Israel to ICL.

In 1992 the Israeli government decided to privatize ICL. In September 1992 the State published its tender prospectus, and at approximately the same time the shares of ICL were listed on the Tel-Aviv Stock Exchange Ltd. (hereinafter the “TASE”). Prior to its public share issuance, ICL issued to the State of Israel a special State share (the “**Special State Share**”) in ICL and its main Israeli subsidiaries (for rules of the **Special State Share** and the rights it affords the State, see section 5.8.2 of this report.).

In 1995 the State of Israel sold the controlling interest in ICL (representing approximately 24.9% of ICL’s shares) to the Israel Corporation, which was controlled at that time by the Eisenberg family. A majority of the ordinary shares held by the State in ICL were sold during the following years. In the year 2000, the State of Israel ceased to be an interest holder in ICL in terms of holding any ordinary shares in ICL, but it retained the Special State Share. In 1999 the Ofer Group acquired control of the Israel Corporation.

As part of ICL’s strategy, which was defined in 1999, ICL began an organizational process in order to achieve focused management of its core business activities, to make the most of the synergies between the Company’s various activities, to increase the efficiency of the various business units and to reduce operating costs. Within the framework of this process, in the period 1999-2001, ICL purchased all the minority interests in ICL’s publicly listed companies. Four management segments were defined and management teams were set up for these segments which are responsible for the management of all the business units in the segments. The division into segments corresponds to the new management concept of ICL and does not correspond necessarily to the legal structure of the Company. Correspondingly, the holding structure of the Company’s subsidiaries and representative offices around the world was reorganized.

Within the framework of the establishment of the business segments, ICL’s operations were as follows:

In the field of fertilizers, management and the network of marketing, sales, land transportation, sea shipping and loading facilities at the ports in Israel and Europe were consolidated, and ICL Fertilizers Europe was established in order to coordinate ICL Fertilizers’ activities in Europe.

In the framework of ICL Industrial Products, the management, marketing, sales and shipping in areas of industrial chemicals were consolidated in Israel and worldwide.

<sup>2</sup> For details of the legal structure of ICL, see the list at the appendix of the financial reports of the Company. For details about a change in the segment structure at ICL commencing from the beginning of 2007, see Section 2.2

Responsibility was transferred to ICL Performance Products, which as of November 2005 also includes the operations acquired from Astaris, for the general operations relating to pure phosphoric acid, which is manufactured in Israel. As a result, a unit was established that coordinates all of ICL's operations with regard to specialty phosphates. In addition, the Company has brought all of the administrative operations of ICL Performance Products under the control of the CEO of ICL Performance Products, Mr. Richard Kennedy, who was appointed in September 2006 as CEO of the segment (prior to this, he had been CEO of ICL Performance Products North America). Managers were also appointed for the various geographical units and areas of operation within the segment.

In North America,, the administrative activities of the various ICL segments were consolidated into a single central headquarters..

CEOs were appointed in China and Brazil in 2006, one as CEO of ICL China, responsible for all of ICL's operations in China, and the other as CEO of ICL Brazil, responsible for all of ICL's operations in Brazil.

As of the date of this report, all of the above-mentioned activities have been completed.

For additional details about the Company's strategy see Section 5.9 below.

As at the date of this Report, the persons with an interest in the Company by virtue of their shareholdings are:

Name	% Holding	% Holding (fully diluted) <sup>3</sup>
The Israel Corporation Ltd. <sup>4</sup>	52.19	51.76
Potash Corporation of Saskatchewan	10.05	9.97
Capital Research and Management Company	5.36	5.32

### 2.1.5 **Acquisition of material assets**

In 2006, no material assets were acquired by ICL.

### 2.1.6 **Changes in the management of the company's business**

During the period of this report there were no material changes in the manner of management of the Corporation's business.

## 2.2 **Areas of Activity**

ICL is a multinational company, primarily active in the areas of fertilizer and specialty chemicals, operating in four main business segments – fertilizers, industrial products, performance products and metallurgy. This division is made on a management/functional basis. There is no full correlation between the managerial and the legal structure. The following is a description of the business segments:

- A. **ICL Fertilizers** – ICL Fertilizers produces potash from the Dead Sea and extracts and produces potash and salt from underground mines in Spain and England. ICL Fertilizers refines potash into various grades and sells it worldwide. In addition, the segment uses a portion of its production of potash to manufacture compound fertilizers. In 2006 potash represented approximately 60% of the segment's sales.

In addition, ICL Fertilizers mines and processes phosphate rock from open-pit mines in the Negev Desert, and produces in Israel sulfuric acid, fertilizer-grade phosphoric acid, phosphate fertilizers,

<sup>3</sup> Presuming that the options for the Company's shares allotted on March 7, 2007 in accordance with the outline published by the Company on January 29, 2007 (see section 5.2E) are converted into shares, and less the shares held by a company consolidated with ICL.

<sup>4</sup> The Israel Corporation is a public company that is listed for trading on the Tel Aviv Stock Exchange (hereinafter: "TASE"). According to data provided to ICL by the Israel Corporation, Millennium Elad Investments Ltd. ("Millennium") holds approximately 47.3% of the Israel Corporation Ltd. The shareholders of Millennium are Mashat (Investments) Ltd. (a company controlled indirectly by a trust, the beneficiaries of which are Idan Ofer and his family) – 80% and Ofer (Ships Holding) Ltd. (a company held in equal shares by Ehud Angel and a company that is controlled by Eyal Ofer, Idan Ofer's brother). Idan Ofer and Ofer Ships also directly hold approximately 3.36% and 2.9% of the Israel Corporation Ltd. respectively.

compound fertilizers based primarily on potash and phosphate and specialty fertilizers. ICL Fertilizers also produces fertilizers in Holland, Germany and Belgium. In addition, ICL Fertilizers produces phosphate-based animal feed supplements in Turkey and in Israel.

ICL Fertilizers markets its products worldwide, primarily in Europe, Brazil, India, China, and Israel.

Commencing in 2007, the activities of Mifalei Tovala Ltd., which transports cargos mainly for the companies of ICL Israel, will be included as part of ICL Fertilizers, since most of its operations are the bulk transportation of ICL Fertilizers.

- B. ICL Industrial Products – ICL Industrial Products produces bromine from an end-brine that is created as a by-product of the production process of potash in Sdom and produces bromine-based compounds. As of 2006, ICL Industrial Products was the world's leading producer of bromine. In that year, ICL Industrial Products produced about 30% of the world's production of this product. During this year, ICL Industrial Products used approximately 80% of the bromine it produced for its own production of bromine compounds in its production facilities in Israel, Holland and China. Additionally, ICL Industrial Products produces various salt products, magnesia and chlorine (extracted together with caustic soda by electrolysis of salt which is created as a by-product of potash production, and which serves as a raw material in the segment's production processes).

ICL Industrial Products also manufactures chlorine-based industrial products in Israel and the United States.

ICL Industrial Products markets its products worldwide.

- C. ICL Performance Products - ICL Performance Products purifies some of the fertilizer-grade phosphoric acid produced by ICL Fertilizers, purchases pure phosphoric acid from other sources, and also produces thermal phosphoric acid and uses these acids to produce downstream products with high added value - phosphate salts, food additives, hygiene products, phosphorus derivatives and products for preventing the spreading of fires and for extinguishing them. ICL Performance Products also produces specialty products based on aluminum oxide (herein "alumina") and other raw materials. The lion's share of ICL Performance Products' production takes place at production facilities in Europe and specifically in Germany, the United States and Brazil, as well as in Israel, China and other countries. The products based on specialty phosphates represented approximately 80% of ICL Performance Products' sales in 2006.
- D. ICL Metallurgy – ICL Metallurgy produces and markets pure magnesium and magnesium alloys. The magnesium production is done in Sdom from carnallite that is extracted (during the potash production process) from the Dead Sea. ICL Metallurgy's magnesium products are used primarily in casting facilities to produce automotive parts and as a component in the aluminum alloy process in the aluminum industry. ICL Metallurgy's operations are conducted through a joint venture between ICL and Volkswagen AG of Germany.

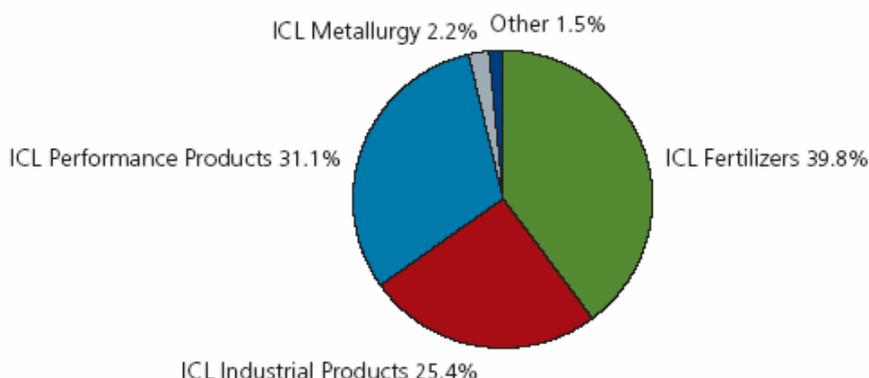
Sales in the metallurgy sector to external customers constitute only approximately 2.2% of ICL's operations and therefore, as of 2007, ICL Metallurgy will no longer be reported as an independent sector.

In addition to the business units described above, ICL has other operations that include water desalination (via a company that is 50% owned by ICL - IDE Desalination Engineering Ltd.) and land transportation (by the subsidiary "Mifalei Tovala Ltd." – hereinafter "Mifalei Tovala"). As noted above, commencing in 2007, other operations will include the results of DSM and will cease to include the results of Mifalei Tovala.

For further details about the Company's operations see section 5.3 below.

Below is a description of the distribution of ICL's sales in 2006 by business segment:

**Total sales in 2006 - \$ 3.258 billion<sup>5</sup>**



## **2.3 Capital Investment in the Corporation and Transactions in its Shares**

During the course of 2005 and 2006, the following changes occurred in the share capital of the Corporation:

- A. As a result of the conversion of all of the convertible debentures, 30,766,000 Ordinary Shares were issued in 2005.
- B. Within the framework of a compensation plan for senior managers, during 2005 and 2006, 643,000 and 699,200 Ordinary Shares of the Company (respectively) were issued free of charge. See Section 5.1(e).
- C. In 2006, following exercise of all the options of employees which were issued in 2003, the Company issued 20,951,668 Ordinary Shares.
- D. To the best of ICL's knowledge and according to reports it received from its shareholders, during 2006 no material transactions were executed in ICL's shares except as described below:

The controlling shareholder in ICL, the Israel Corporation Ltd., reported to ICL that in an off-the-floor transaction in 2006, it acquired 20,351,666 Ordinary Shares of ICL, which account for approximately 1.6% of the issued share capital of the Company. The details of the transaction:

Date	Number of shares	Share price (NIS)	Total consideration (NIS millions)
5.1.2006	16,951,666	19.02	322
11.4.2006	1,700,000	18.37	31.2
31.5.2006	1,700,000	19.29	32.8

## **2.4 Dividend Distribution**

### **2.4.1 Details regarding the distribution of dividends in the preceding two years:**

- A. On April 20, 2005, ICL distributed a cash dividend in the amount of \$35.9 million<sup>6</sup>.
- B. On September 21, 2005 ICL distributed a cash dividend in the amount of \$60 million<sup>6</sup>.
- C. On May 9, 2006, ICL distributed a cash dividend in the amount of \$90 million<sup>6</sup>.
- D. On September 19, 2006 ICL distributed a cash dividend in the amount of \$90 million<sup>6</sup>.

<sup>5</sup> For the purpose of this graph, the revenue data for the segments used for calculating the proportion of total revenue are after set-off of revenue from intra-segment sales.

<sup>6</sup> The sums, less the portion held by a consolidated company, are: 35.7, 59.8, 89.9 and 89.8 million respectively. See also Note 19E to the Financial Statements.

All of the dividends distributions noted above were made from profits and did not require court approval. The amounts are stated net. See also Note 19E to the financial statements.

On March 27, 2007, the board of directors of the Company resolved to pay a dividend in the sum of \$ 283.9 million (283.4 million net, less dividend paid for a consolidated company). The dividend is to be paid on April 25, 2007.

For details regarding covenants to banks for preservation of share capital, see section 5.4.5 below.

#### **2.4.2 Dividend distribution policy**

In 1998 the members of the Company's Board of Directors decided that as part of their considerations in determining the Company's dividend distribution policy, they would take into account the financial needs of the Company and also the interest of the shareholders in receiving dividends.

On 27, 2007, the board of directors of the Company decided to distribute the Company's net profit for 2006 as a dividend, after taking into account a dividend in the sum of \$ 90 million paid on September 19, 2006 for part of the profits of that year. As a result, on April 25, 2007, the sum of \$ 283.9 million (\$ 283.4 million net less the share of a consolidated company) will be paid as a dividend).

For subsequent years, ICL intends to pay a quarterly dividend in the sum of up to 70% of its net profits. Payment of the dividend, will depend on, among other things, on the Company's earnings, its investment plan its financial situation and various additional factors.

The following is a table of the dividend yields in recent years:

<b>Year</b>	<b>Dividend Yield (%)<sup>7</sup></b>
2001	3.99
2002	4.84
2003	4.48
2004	4.54
2005	3.59
2006	6.42

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<sup>7</sup> Dividend yield – the amount of the dividend per share distributed from the relevant year's profits, divided by the average price per share on the TASE during that year.

## Chapter 3 – Other Information

### 3.1 Financial Information Regarding the Corporation's Areas of Operations

A. The following table represents the Group's revenues by business segment:

2006 – in US \$ 000's										
	ICL Fertilizers				ICL Industrial Products	ICL Performance Products**	ICL Metallurgy	Other	Setoffs	Consolidated
	Potash	Phosphate	Setoffs	Total						
<b>1. Revenue</b>										
<b>A. Revenue from external sources</b>	791,368	504,170		1,295,538	827,289	1,011,050	73,168	51,116		<b>3,258,161</b>
<b>B. Revenue from sales to other segments</b>	133,715	64,725	(39,934)	158,506	10,556	16,867	19,418	35,321	(240,668)	
<b>C. Total</b>	925,083	568,895	(39,934)	1,454,044	837,845	1,027,917	92,586	86,367	(240,668)	<b>3,258,161</b>
<b>2. Costs</b>										
<b>A. Expenses that represent revenue by another segment of the Company</b>	34,612	30,316		64,928	61,881	59,895	53,644	320	(240,668)	
<b>B. Other costs</b>	645,338	527,331		1,130,767	567,075	882,111	74,740	76,156	(4,197)	
<b>C. Total</b>	679,950	557,647	(41,902)	1,195,695	628,956	942,006	128,384	76,476	(244,815)	<b>2,726,702</b>
<b>3. Operating Income</b>	245,133	11,248	1,968	258,349	208,889	85,911	(35,798)	9,891	4,217*	<b>531,459</b>
<b>4. Total assets as of December 31, 2006</b>	1,173,164	572,611	(26,213)	1,719,562	770,902	693,601	104,060	76,353	241,963	<b>3,606,441</b>
<b>5. Minority interest in revenues from external sources</b>					7,137	4,905	25,608			

\* Including costs not allocated to the segments.

2005 – in US \$ 000's										
	ICL Fertilizers				ICL Industrial Products	ICL Performance Products**	ICL Metallurgy	Other	Setoffs	Consolidated
	Potash	Phosphate	Setoffs	Total						
<b>1. Revenue</b>										
<b>A. Revenue from external sources</b>	927,851	465,855		1,393,706	794,294	666,543	80,795	50,663		<b>2,986,001</b>
<b>B. Revenue from sales to other segments</b>	136,273	82,700	(38,943)	180,030	11,181	10,445	22,035	36,865	(260,556)	
<b>C. Total</b>	1,064,124	548,555	(38,943)	1,573,736	805,475	676,988	102,830	87,528	(260,556)	<b>2,986,001</b>
<b>2. Costs</b>										
<b>A. Expenses that represent revenue by another segment of the Company</b>	39,095	21,681		60,776	63,801	78,659	56,640	680	(260,556)	
<b>B. Other costs</b>	691,384	511,433		1,164,867	587,775	543,323	55,140	79,382	(5,815)*	<b>2,424,672</b>
<b>C. Total</b>	730,479	533,114	(37,950)	1,225,643	651,576	621,982	111,780	80,062	(266,371)	<b>2,424,672</b>
<b>3. Operating Income</b>	333,645	15,441	(993)	348,093	153,899	55,006	(8,950)	7,466	5,815	<b>561,329</b>
<b>4. Total assets as of December 31, 2005</b>	1,036,919	589,218	(21,526)	1,604,611	725,699	657,839	109,606	62,503	163,684	<b>3,323,942</b>
<b>5. Minority interest in revenues from external sources</b>					8,001	6,118	28,278			

\* Including costs not allocated to the segments.

\*\* Including the operations acquired from Astaris from the date of acquisition

2004 – in US \$ 000's										
	ICL Fertilizers				ICL Industrial Products	ICL Performance Products**	ICL Metallurgy	Other	Setoffs	Consolidated
	Potash	Phosphate	Setoffs	Total						
<b>1. Revenue</b>										
<b>A. Revenue from external sources</b>	829,238	479,546		1,308,784	696,582	576,143	70,209	63,237		<b>2,714,955</b>
<b>B. Revenue from sales to other segments</b>	103,063	70,805	(26,773)	147,095	9,940	6,311	18,009	34,265	(215,620)	-
<b>C. Total</b>	932,301	550,351	(26,773)	1,455,879	706,522	582,454	88,218	97,502	(215,620)	<b>2,714,955</b>
<b>2. Costs</b>										
<b>A. Expenses that represent revenue by another segment of the Company</b>	33,881	16,406		50,287	54,209	65,411	44,679	1,034	(215,620)	
<b>B. Other costs</b>	667,432	521,053	(26,370)	1,162,115	589,361	470,000	46,800	90,927	1,384*	<b>2,360,587</b>
<b>C. Total</b>	701,313	537,459	(26,370)	1,212,402	643,570	535,411	91,479	91,961	(214,236)	<b>2,360,587</b>
<b>3. Operating Income</b>	230,988	12,892	(403)	243,477	62,952	47,043	(3,261)	5,541	(1,384)	<b>354,368</b>
<b>4. Total assets as of December 31, 2004</b>	946,380	583,592	(11,458)	1,518,514	748,429	362,600	136,474	56,556	236,699	<b>3,062,272</b>
<b>5. Minority interest in revenues from external sources</b>					8,485	5,882	24,573			

\* This figure in this table includes costs not attributed to the segments.

B. Explanation of changes and developments

For explanations of the changes and developments in the 2006 financial data, see sections 1.2 and 2 of the Directors' Report.

## **3.2 General Business Environment and Influence of External Factors on ICL**

3.2.1 ICL is a multinational company. Its financial results are affected by global economic trends, the changes in terms of trade and financing, and fluctuations of currency exchange rates. The demand for ICL's products is affected by, among other factors, the demand for basic agricultural products and by global economic conditions.

ICL is taking steps towards adapting its marketing and production policies to the global market conditions. ICL is focusing on improving cash flow, diversifying sources of financing and is committed to taking actions to improve efficiency and cost savings.

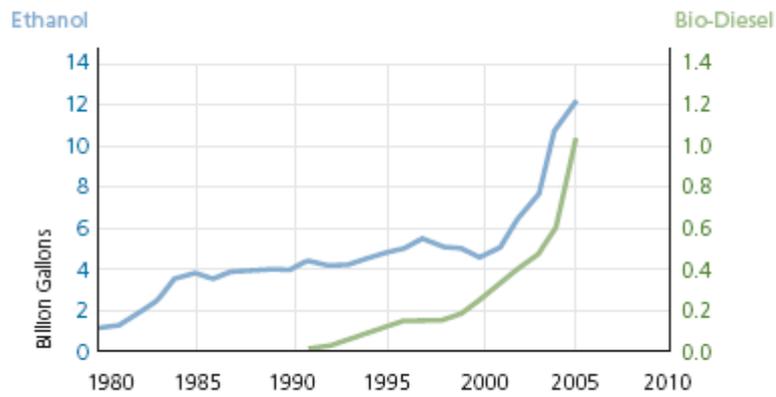
3.2.2 The Company has facilities that are located in Israel. As an Israeli corporation, the Company is affected by political, economic and security conditions prevalent in Israel. A number of countries, and various corporations and organizations still restrict their business relationships with Israeli companies although, as a result of the present geopolitical situation in Israel, their number is declining. This trend should improve ICL's ability to expand its business relationships with these countries and corporations and sell its products in these countries. A worsening geopolitical situation could harm business relationships with these countries and corporations.

3.2.3 The lion's share of ICL's revenues is in foreign currency, mainly US dollars and Euro. A portion of its operating expenses are in NIS. Therefore, a devaluation of the currency exchange rate of the NIS relative to the US dollar has a positive impact on ICL's profitability, and vice-versa. ICL has more revenues than expenses in Euro. Therefore, an appreciation of the exchange rate of the Euro relative to the US dollar has a positive impact on ICL's profitability. ICL hedges against some of these exposures.

3.2.4 Most of ICL's debt bears variable interest rates. Therefore, the Company is exposed to fluctuations in interest rates. The Company partially hedges against such exposure by using financial hedging instruments including financial derivatives. Regarding the amount of such hedging activities in 2006, see note 23B to the financial statements.

3.2.5 In the past few years, positive developments occurred in most of ICL's areas of business, as a result of global economic growth and improvements in the Company's target markets. For example, conditions in the global agricultural market, which significantly affect the demand for fertilizer, improved. In recent years there has been growth trend in the worldwide consumption of cereals (grains, rice, soy, corn etc.). The growth derives from the natural worldwide population growth, as well as a change in food consumption (an increase in meat consumption) as the result of increases in the standard of living primarily in the developing countries. In addition, in light of the sharp increases in energy prices, there is an increasing worldwide movement towards producing energy from agricultural sources. For example, global production of ethanol from corn and sugar has increased, since 2000, by almost 100%, and the production of biodiesel from soya and canola has increased almost fourfold since 2000. These trends have led significant increases in the prices of agricultural products and to increased cereal planting worldwide. Below are additional details:

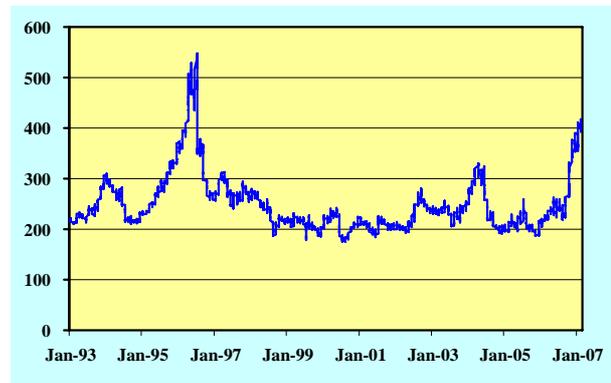
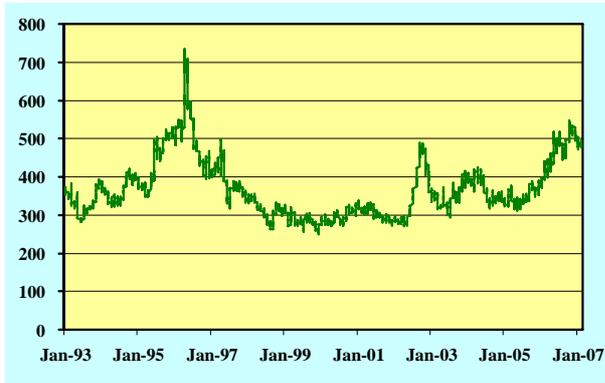
## Development of Ethanol and bio-diesel production over time



Source: Earth Policy Institute, Renewable Fuel Association

- **Wheat  
Prices  
(US¢/Bu)**

- **Corn  
Prices  
(US¢/Bu)**



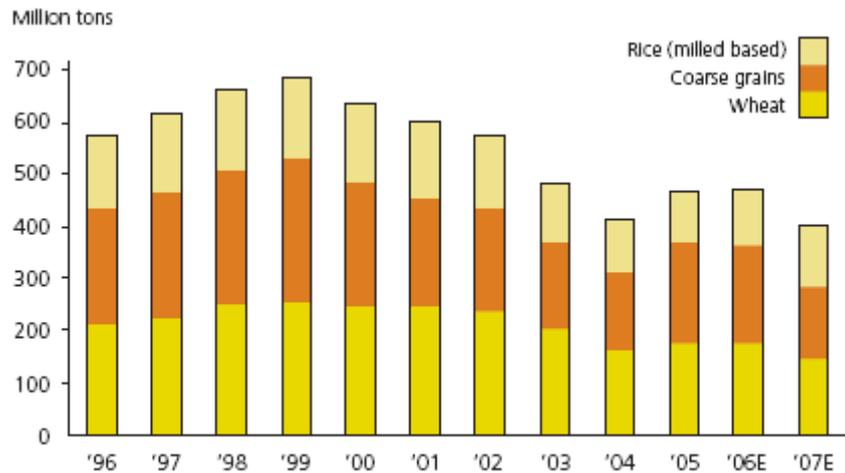
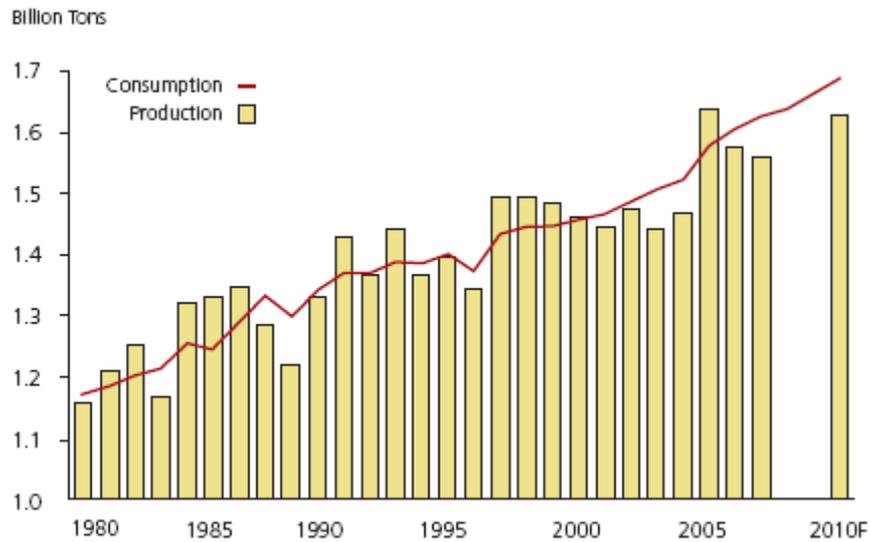
**Soya Prices  
(US¢/Bu)**



Source: Reuters

## World grain production and consumption

Source: USDA - [www.fas.usda.gov](http://www.fas.usda.gov)



Source: Food Outlook No. 2, December 2006 - FAO

- 3.2.6 Forecasts of the FAO as of January 2007 project an increase in corn crops in 2007, but in view of the use of corn for the production of ethanol as a fuel substitute, the forecast is for a decrease in global stocks of corn to their lowest in the past 11 years. Furthermore, according to the FAO forecast, wheat areas will increase, but here too, the projection is for a decrease in global stocks.<sup>8</sup>
- 3.2.7 The prolongation in 2006 of the price negotiations between the potash manufacturers and the Chinese and Indian customers, led to cessation of shipments to China by sea. In addition, a decision by other potash consumers to await the outcome of the negotiations with the Chinese, the ongoing weakness of the Brazilian market and the long European winter, resulted in a significant decrease in potash sales since the beginning of 2006 and in a corresponding increase in potash stocks. These factors led a number of large potash manufacturers to announce a reduction in production at their plants in order to match production to sales. At the end of July 2006, an agreement was signed with a large account in China for the sale of potash for the remainder of 2006, at an increased price, and shipments to that customer were resumed. In September 2006 an agreement was signed

<sup>8</sup> The information stated in this section, including the above Notes, includes forward-looking statements. This information is based upon the Company's market assessments and also upon statistics published by the World Food Organization. Actual results may materially differ from these projections as a result of changes in market conditions and/or production and/or grain supply relative to these projections, which may occur.

with the same customer, under which ICL Fertilizers will supply more than two million tons of potash over a period of three years, from January 2007 to December 2009. This agreement reflects a 30% increase in the quantity of potash compared with the earlier agreement with the same customer, which was to expire at the end of 2006. Under the new agreement, the potash prices will be determined by the parties at the beginning of each calendar year. In February 2007, an agreement was signed between ICL Fertilizers and the Chinese entities for the prices of potash during 2007.

In August and September 2006, ICL Fertilizers signed agreements with the largest accounts in India for the supply of more than 800,000 tons of potash over a period of nine months from August 2006 to April 2007.

Flooding in one of the mines of the Russian company Uralkali in 2006, compelled that company to close the mine which, according to external publications, has a production capacity of about 1.5 million tons and at the time of the flooding actually produced about 1.2 million tons annually.

Mosaic, a Canadian company, announced an increase in the percolation of brines in its principal mine in January 2007. As of the date of the report, the company gave notice that it was in control of the situation, that there were indications of a decrease in the percolation, which was not expected to affect its production quantities for the 2007 agricultural year (the agricultural year ends in May) beyond the additional operating expenses estimated by Mosaic at about \$30 - \$40 million.

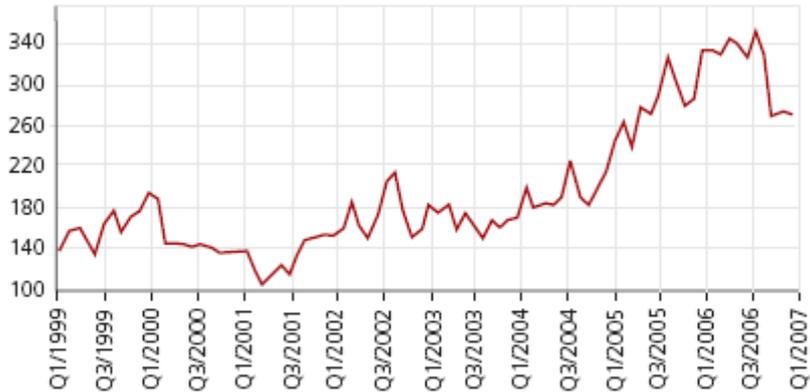
From the end of 2005, there was a reduction of 9% in the US production capacity for mono and di-ammonium phosphate (MAP/DAP). This reduction in capacity is the result of Mosaic shutting down plants which reduced production capacity by about 2 million tons of fertilizers (MAP/DAP/GTSP) and about 1.2 million tons of phosphoric acid in the first half of 2006. Prior to this, at the end of 2005, US Agri-Chem stopped production at two of its plants in the US and thereby reduced production capacity by about 560 thousand tons of MAP/DAP and by about 540 thousand tons of phosphoric acid.

- 3.2.8 The bromine market is affected to a large degree by the activity in the electronics and oil drilling industries, as well as limitations on use of methyl bromide as a result of the implementation of the Montreal Protocol (see section 4.2.16 below). The first half of 2006 was characterized by strong demand for flame retardants resulting from an increase in demand for electronics products. From the third quarter of 2006, the demand for flame retardants moderated even as production of some flame retardants in China increased. In the methyl bromide market, the trend of declining sales continued due to the restrictions of the Montreal Protocol. At the beginning of 2006, the increased demand for chemicals that serve the oil drilling industry continued, as a result of high oil prices, which led to the continuation of drilling operations worldwide on a similar level to 2005. In the main destination market in Mexico Bay, oil drilling operations were moderated in the second half of the year.
- 3.2.9 In the ICL Performance Products market, demand for products was positively affected by economic recovery in some of its target markets, but in contrast was negatively impacted by relatively low economic growth in Europe, which is its primary market.
- 3.2.10 At ICL Metallurgy, the downward price trend of magnesium metal products, which started in the last quarter of 2005, continued into the first half of 2006, and adversely affected the segment's results. In the third quarter of 2006, the trend reversed and a moderate rise was recorded in prices. The reversal was the result of a number of factors, mainly cancellation of the subsidy for magnesium exports from China, the announcement of closure of the magnesium production facilities of a Canadian company during 2007, and problems in the supply of magnesium from Russia due to floods in the region.
- 3.2.11 ICL's energy costs are affected mainly by prices of oil and its products in Israel and worldwide, and by the prices of electricity supplied by the Israel Electric Corporation and natural gas and electricity in other countries in which the Company's principal production facilities are located. In 2006 there was a further increase in fuel prices, in addition to the price increases in 2004-2005.

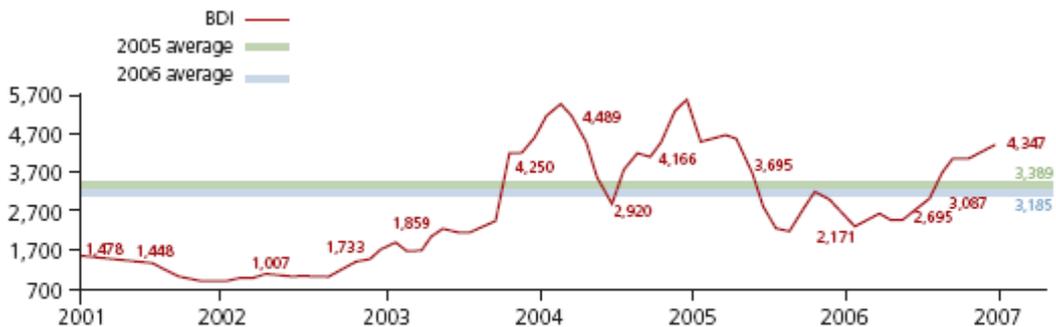
**Brent Oil Price Per Barrel (\$/barrel)**



**Mazut 1500 (\$/ton, Ashdod gate)**



3.2.12 Marine bulk shipping costs represent a significant component of expenses of ICL Fertilizers. In 2006 the trend of sharp volatility of bulk shipping prices continued. In the first half of 2006, bulk shipping prices dropped sharply, while in the second half of the year prices rose again. On average, prices during 2006 were slightly lower than the average in 2005, but remained relatively high compared with the past. In March 2007, there was a further rise in marine transportation costs. The closest measurement showing bulk shipping prices from Israel, representing the international average of transportation of dry bulk, is the BDI – Baltic Dry Index, published by an organization called the Baltic Exchange. The chart below shows the development of the index between 2001 and 2006.



Source: The Baltic Exchange - [www.bmti.de](http://www.bmti.de)

### **3.3 Sustainable Development Policy – Environmental and Safety Responsibility and Compliance with the Law**

ICL is committed, as policy, to the principles of sustainable development. In its activities for the promotion of the interests of the Company, ICL takes into consideration the effects of its activities on its shareholders, customers, suppliers, employees, the community and the environment in its areas of operation. ICL strive for a balance between economic, environmental and social needs and the needs of today's generation and future generations. ICL has invested and continues to invest considerable resources, both financial and administrative, as part of its policy for the principles of sustainable development, and believes that this is the right way to ensure its long-term success. Below are the principles that ICL promotes and by which it operates:

- ensuring the safety and health of its employees;
- affording respect to its employees, suppliers and customers<sup>9</sup>;
- strict adherence to appropriate production processes;
- a policy of environmental responsibility, with long-term efforts to minimize negative effects on the environment as far as possible;
- savings on energy, water and other natural resources, and the implementation of environment-friendly methods, with emphasis on savings in energy and natural resource inputs;
- promotion and leadership in transparency issues and compliance with stringent standards;
- promotion of multi-area internal compliance plans in ICL's companies in Israel and worldwide;
- implementation of a code of ethics for the Company, and its gradual assimilation as part of the values of ICL;
- ascertaining proper disclosure to investors and attentiveness to their requests and inquiries;
- ongoing contribution to the community and society in social involvement projects, focusing on the weaker segments of the population, especially children, in the areas of operation of ICL's companies.

These principles have led, for example, to the appointment of Board of Directors committees in the segments in Israel, with a mandate to discuss issues relating to ecology, security and safety, aided by outside consultants in the relevant fields. In addition, the Board of Directors of ICL appointed the CEO of ICL Fertilizers, Mr. Asher Greenbaum, to be in charge of all safety, ecology and security issues in the Company. Mr. Greenbaum reports directly to the Board of Directors from time to time, and the boards of directors of ICL and the segments and companies, maintain regular follow-up of activities in these areas.

#### **3.3.1 Environment and safety**

ICL's policy in the areas is to promote the following:

- Compliance with local and international standards, using the Best Available Technique.<sup>10</sup>
- Development of new products or new production lines approved by the Board of Directors of the Company, taking into account their effect on the environment.
- Development of products and processes that prevent, or at least minimize, the risks to humans and the environment.
- Safe use of the Company's products and customer participation throughout the chain of product life in plans for the prevention of environmental damage.
- Reduction of emissions, including from **diffused** sources.
- Energy saving.

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<sup>9</sup> Including employees employed by human resource companies. For specific arrangements see section 5.2F below.

<sup>10</sup> "Best Available Technique" is defined in law as follows: the best current available technology for preventing damage and nuisances and for preventing the pollution of water sources, which is in use and is economically feasible (Article 1 of the Business Licensing Regulations (Salt concentrations in industrial wastes), 5763-2003).

- Responsible use of natural resources.
- Increased and deeper re-use of waste and by-products of production processes, in order to recover most of the natural resources consumed in the production process.
- Cooperation with other manufacturers and with customers and users, for the development and implementation of means and methods that will promote safe products while preventing harm to the quality of the environment.
- Rehabilitation of mining and quarry sites.

For further details about related activities in the segments, see Sections 4.1.13, 4.2.14, 4.3.14 and 4.4.13.

### **3.3.2 Safety and health**

The Company's policy in these areas includes the following:

- Adoption of international safety standards and compliance with the safety standards applied worldwide.
- encouragement of a high and uncompromising level of awareness of safety and hygiene among employees and suppliers.
- Constant improvement in safety and health targets and their adoption, and striving for a "zero accidents" situation.
- Periodic inspections and risk assessment for everything relating to products and processes in the various plants.
- Promotion of a system of occupational medicine and preventive medicine,

For further details about related activities in the segments, see Sections 4.1.13, 4.2.14, 4.3.14 and 4.4.13.

### **3.3.3 The environment**

ICL is aware of the fact that the industrial production processes of some of its products, and the mining of the ores that are the basic raw materials for these products, affect the environment, and it is taking steps and will continue to take steps to prevent or to minimize damage and, where possible and appropriate, to rehabilitate such sites, in cooperation with the authorities, employees, suppliers and customers, as set out in this report.

ICL is aware that some of its products products that might be hazardous or cause harm, to some extent or another, to persons likely to be exposed to them – during the course of manufacture, transportation, storage or use of them. In addition, it is possible that some of these products have the potential of causing environmental damage, including with respect to waste water, emissions into the air, and waste generated during the course of manufacture. ICL takes all measures to prevent these hazards or to minimize them as much as possible

In 2006 the Company spent \$49 million on ecology-related issues. Of this sum, ICL invested about \$25 million in fixed assets for the prevention of environmental damage, and about \$24 million in current expenses for the same purpose.

In 2007, ICL has budgeted about \$80 million for these activities – about \$40 in fixed assets and \$40 million current expenses. From 2008 onwards, the Company foresees no reduction in requirements for these purposes.<sup>11</sup>

The policy of ICL is to take constant action to identify, develop and implement means of measuring and monitoring environmental implications while investing in the treatment of effluents, emissions and wastes, training employees and consumers (as necessary), cooperating with the authorities and many other activities. ICL companies work in full cooperation and coordination with the Ministry for Protection of the Environment.

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<sup>11</sup> The assessments for projected investments and expenses are forward-looking information and are based on existing legislation and standards, on the requirements of the authorities as known today for ICL Industrial products, and on the investment estimated by Company engineers. The realization of these assessments is uncertain. Any change in one of these assessments, including the estimate of the Company's engineers or in the implementation of the requirements of the authorities or the provisions of the laws, could lead to a different result.

As part of its implementation of this policy, ICL strives to –

- encourage a high level of awareness and of the environment and its preservation and compliance with the provisions of the law among managers, employees and consumers;
- apply the best means available<sup>12</sup>, technologically and economically, for dealing with the environmental aspects deriving from its activities;
- act in accordance with international standards for compliance with the standards in place around the world in the field of environment, as a basis for operations;
- implement an environmental management system, including ISO 14001, EMAS and Responsible Care;
- minimize the effects of production processes, storage, conveying and use of its products on humans and the environment;
- encourage the development and implementation of methods and processes for saving on energy and natural resources, with an emphasis on reducing and recycling production by-products, particularly industrial waste, use of solar energy and similar processes;
- reduce the emission of greenhouse gases, *inter alia* by transition to use of relatively clean gases and fuels;
- promote the production of products and relatively safe production processes for manufacture, use, recycling and removal;
- promote environment-friendly handling and use of products, and cooperation with both manufacturers and customers in this regard;
- provide customers with information and instruction for the Company's products, the correct and safe use of those products and how to prevent damage to the environment as a result of their use;
- to develop an open and informed dialog with officialdom, academia, business partners, neighboring plants, public bodies, and other "stakeholders" in these areas.

Further details regarding environmental issues are set out in section 3.3 and in Chapter 4 above (sections 4.1.13, 4.2.14, 4.3.14 and 4.4.13 above, for each segment).

### **3.3.4 Code of ethics and internal compliance programs**

The Board of Directors of ICL approved a code of ethics for the Company, which is initially being applied for ICL managers and specific groups of employees. The code of ethics sets appropriate rules of conduct for the Company and its employees based on ICL values. The five basic principles of the code are these:

- Respect for the law.
- Fair business practices.
- Respect for others – employees, suppliers, customers and service providers.
- Proper use and protection of Company assets.
- Work in accordance with the compliance program and procedures, as a basis for organizational excellence.

The code is intended also as a uniting framework for existing compliance programs in the Company, in the areas of securities, restrictive trade practices, safety, ecology and the prevention of sexual harassment. As of the date of the report, the senior managers of the Company have confirmed their personal commitment to fulfillment of the provisions of the code. During 2006, ICL introduced a training and assimilation process of the code among other employee populations in Israel and abroad, with the aim of encompassing all employees of all levels in the program. This process will be continued in 2007.

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<sup>12</sup> "Best Available Technique" is defined in law as follows: the best current available technology for preventing damage and nuisances and for preventing the pollution of water sources, which is used and is economically implementable (Article 1 of the Business Licensing Regulations (Salt concentrations in industrial wastes), 5763-2003).

ICL maintains a system of internal compliance to ensure that all relevant provisions of the law are upheld. It has been made clear to Company managers and suitable office-holders in ICL's companies that their managerial responsibilities include ensuring compliance with the law by the company in which they are officers. These matters are also regularly reviewed by the managements and boards of directors of the various companies. Among other actions taken, internal compliance plans were prepared and are implemented in matters such as restrictive trade practices, securities laws and the prevention of sexual harassment: day-long seminars are held for the relevant managers, and application of the provisions of the law is checked regularly.

For further details about the application of the internal compliance program in each segment, see Sections 4.1.15(e), 4.2.16(e), 4.3.15(e) and 4.4.14.4.

### **3.4 Corporate Governance**

ICL operates according to advanced principles of corporate governance, voluntarily applying rules designed to ensure checks and balances and to lead to good corporate governance. The following points are worthy of mention:

**Meetings of the Board of Directors and its supervision of the Company:** In 2006 the Board of Directors convened eight times. Every year, the Board discusses and approves the Company's strategy, as well as the five-year plan and the annual budget. The Finance Committee conducts a periodic review of the corporation's exposure to various financial risks. Investments in excess of a certain amount require the approval of the Board of Directors.

In addition to the Board of Directors of ICL, there are boards of directors for the segments in which the members of the ICL Board of Directors are members, as well as officers in ICL and other persons, including independent directors. These boards of directors, themselves or on committees dedicated to specific subjects (investments, safety, ecology and security, human resources, and others), convene regularly once every few weeks, and review the activities of the companies in the segment.

**The independence of the Board of Directors:** There is separation between the roles of the Chairman of the Board and the CEO. Officers who are directly subordinate to the CEO do not serve as directors in the Company.

**The qualifications and suitability of directors:** As of the date of the report, 11 out of the 12 members of the Board of Directors have accounting and financial expertise (see Section 7.1 of the Directors' Report). The directors are elected (excluding the outside directors, who are appointed by law for a period of three years) every year at the general Meeting. New directors receive suitable instruction about ICL and its operations. From time to time, the Board of Directors tours the Company's plants. Directors' remuneration is in accordance with the Companies Regulations (Rules for remuneration and expenses of an outside director), 5760-2000.

#### **Board of Directors control of certain actions of the Company:**

The Finance Committee and its actions: In the Company, the Finance Committee reviews the drafts of the quarterly financial statements prepared by the Company for publication, together with the Management and the outside auditors. All the members of the Board of Directors are invited to the meetings of the committee, which also discusses management of the Company's debt, financial hedging and other policies and other financial matters. In 2006, the Finance Committee convened six times.

The Audit Committee and its actions: ICL and the segments have audit committees. Most of the members of the audit committee at ICL are independent directors. ICL's audit committee is chaired by an outside director. In 2006 the committee convened 8 (eight) times.

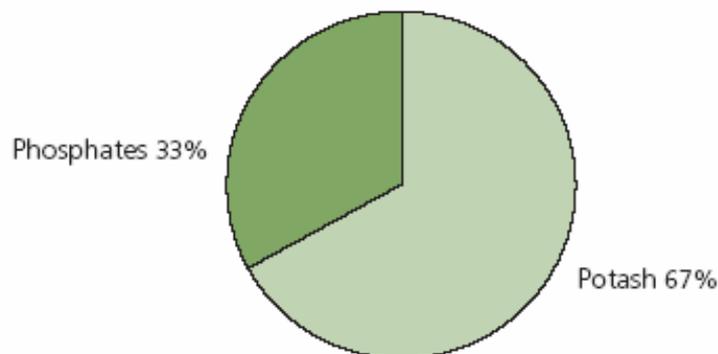
The audit committee is responsible, among other things, for the annual and multi-year internal audit plan, based on a risk survey conducted for ICL's companies in Israel and abroad. The audit committee oversees the efficacy of the Company's internal auditor and ensures that the auditor has access to the tools, sources and information required for performance of his functions, in accordance with the relevant standards. The audit committee and the board of directors have approved procedures and controls intended to detect and bring about the authorization and reporting of transactions with interested parties, as required. For additional details regarding the audit work done in ICL, see section 8.2 of the report of the board of directors.

## Chapter 4 – Description of the Corporation’s Business by Area of Activity

### 4.1 ICL Fertilizers

The following chart shows the external sales<sup>13</sup> of ICL Fertilizers, by product:

#### Total external sales for 2006 - \$ 1,296 million



#### 4.1.1 General information about ICL Fertilizers

ICL Fertilizers develops, manufactures, markets and sells fertilizers that are based primarily on potash (potassium chloride) and phosphate. In 2006, sales of ICL Fertilizers totaled \$1.45 billion, representing approximately 42% of the total sales of ICL (including sales to other segments of the Company). The major products of ICL Fertilizers are potash, phosphate rock, sulfuric acid (primarily used as a raw material in the production of phosphoric acid), fertilizer-grade phosphoric acid, phosphate fertilizers, compound fertilizers, specialty fertilizers, and phosphate-based feed additives for livestock. In 2006 ICL Fertilizers was the world’s sixth-largest producer of potash, and ranked second in sales in Western Europe.<sup>14</sup>

The Company’s primary manufacturing facilities: in Israel - Sodom (potash and salt), Mishor Rotem (phosphate rock, phosphoric acid, phosphate fertilizers and specialty compound fertilizers), the Oron and Zin sites (phosphate rock), Haifa (primarily liquid fertilizers for the local market); in Spain (potash and crude salt); in England (potash and crude salt); in Holland, (mainly fertilizers based on phosphate and potash, and also soluble fertilizers); in Germany, (fertilizers based mainly on phosphate and potash); in Belgium, (soluble fertilizers); and in Turkey, (phosphate-based products as animal feed additive).

Production and marketing activities for potash and phosphate fertilizers in Europe are coordinated by ICLFE, which was established to take advantage of synergies between ICL’s companies. In the Company’s estimation, ICL Fertilizers is today a “major player” in the European potash market.

ICLFE’s activities cover two potash production sites – one in Spain (IP) and one in England (CPL), the two Amfert sites for the production of fertilizers in Germany and Holland and the site for the production of animal feed additives (MCP and DCP) at Rotem Turkey. ICLFE’s headquarters are in Amsterdam, Holland.

<sup>13</sup> The term “external sales” refers to the segment’s sales to customers outside of the ICL Group (customers that are not other segments of ICL).

<sup>14</sup> Source: IFA, Fertecon

Details of ICL Fertilizers' operations sites are set out in the map below:



Potassium, phosphorus and nitrogen (K, P and N) constitute the three major nutrients required for plant growth. There are no substitutes for potassium and phosphorous. Each of the three major nutrients plays a different role in plant development. All of these three major plant nutrients are naturally present in soil in different concentrations, but continued growing of crops depletes soil of nutrients and therefore each must be replenished from external sources through the use of fertilizers.

Potash is a plant's primary source of potassium, and phosphate is a plant's primary source of phosphorous.

Potassium and phosphorus are vital for many of a plant's physiological processes, including strengthening cereal stalks, stimulating root development, leaf and fruit health, and accelerating the growth rate of crops. Without these elements, crops cannot achieve their growth potential. The agriculture industry strives to derive the greatest production from a given cultivated area. The more optimal the soil fertilization, the greater the yield and the better quality the harvest will be in a given area, and therefore there is a correlation between efficiencies (in terms of benefit per dollar invested) in the agriculture industry and fertilizer consumption.

ICL fertilizers is active mainly in the agriculture industry. This industry receives priority and support in many countries, particularly in the developing countries which are characterized by both population growth and growth in the standard of living, factors that lead to increases in food consumption and in fertilizer use. These markets, the largest of which are china, India and brazil, are ICL fertilizers' principal growth markets. Western Europe also represents a central market for ICL fertilizers, although this market is not growing.

The barriers to entry in the fertilizer industry are high due to the heavy investment required to establish production facilities for the basic minerals, which are used as raw materials for the fertilizer industry, and the relatively lengthy time periods required to establish these plants. Similarly, this industry requires appropriate concessions and proximity of production facilities to quarries.

In the past few years the fertilizer industry has undergone consolidation, which has reduced the number of suppliers in the industry. Similarly, various manufacturers and customers have entered into cooperation agreements and have established joint ventures. Standing out among these are the merger in 2004 between IMC Global and Cargill Crop Nutrition (both American companies), which created the fertilizer giant Mosaic, the purchase by the Canadian fertilizer giant PCS of holdings in ICL, APC (Arab Potash Corporation, of Jordan), SQM (Sociedad Quimica y Minera de Chile S.A, of Chile), and recently the acquisition of 20% of the largest manufacturer and distributor of fertilizers in china (Sinochem Hong Kong). There have also been divestitures of fertilizer facilities and companies, primarily in North and South America and in Europe. ICL also participated in this trend, as it acquired Iberpotash (a Spanish potash company) in 1998 (reaching 100% ownership in 2001) and Cleveland potash (a British potash company) in 2002. It should be further noted that in the potash market

additional demand is supplied by existing producers, either by de-bottlenecking or by expanding existing facilities. In 2005 a number of manufacturers announced projected expansions of their manufacturing capacities in the coming years. The company estimates that the expected increase in supply by existing manufacturers in the coming years, based on these suppliers' announcements regarding projected expansions, will not exceed the expected rate of growth of demand for potash, based on assessments regarding the average long-term rate of growth in demand for potash.<sup>15</sup> note also that in October 2006, the mine belonging to the Russian corporation Uralkali, the actual production of which was approximately 1.2 million tons of potash (the mine's production capacity was approximately 1.5 million tons), flooded. This flood appears to have put the mine out of production.

In January 2007, Mosaic gave notice of an increase in seepage of brines in its principal mine in Canada. As at the date of this report, the company has given notice that it is in control of the situation, that there are indications that the amount of seepage is reducing, and that there is not expected to be any adverse affect on its production quantities for the 2007 agricultural year (which ends in May) beyond the additional operating costs resulting from seepage, estimated by Mosaic at approximately 30 to 40 million dollars.

#### 1. Potash

- a. Potash is the common name for potassium chloride, which is the most common source of potassium for plants. Potassium is required for plant development, improves plant's ability to withstand disease, increases the yield, improves the quality and lengthens the shelf life of the crop. ICL Fertilizers sells potash for direct application as a fertilizer and to compound fertilizer manufacturers. ICL Fertilizers also uses potash
- b. ICL Fertilizers produces potash from the Dead Sea and from underground mines in Spain and England. The potash production process in Israel is based on separating the potash from carnallite. The carnallite, which is a compound of potassium chloride, sodium chloride (common salt) and magnesium chloride, precipitates in ponds located south of the Dead Sea, which contain brines drawn from the Dead Sea by means of one of the world's largest solar evaporation systems. The carnallite is transferred to the plants where the potash is separated from the common salt and the magnesium chloride in two parallel processes (known as "hot crystallization" and "cold crystallization").

Extraction of potash from underground mines in Spain and England is carried out on the basis of concessions and lease agreements. In these mines, sylvinit (a mixture of potash and salt) is mined with varying concentrations of potash. The potash is separated from the salt in production facilities situated adjacent to the mines.

In 2006, ICL Fertilizers produced approximately 5.1 million tons of potash, representing 10% of the worldwide production of potash.

- c. There is brine seepage in one of the dikes enclosing ICL Fertilizers' evaporation ponds which has caused damage to the layer sealing the dike. As a result, holes have been found in the dike itself and cracks have appeared along its length. Under certain circumstances, these holes and/or cracks might endanger the integrity of the dike. ICL Fertilizers, based on consultations with international experts in the field, has been taking and continues to take a variety of maintenance steps to retain the stability of the dike and to reinforce it, and is continually following these steps up in order to locate the development of malfunctions in the dikes.

The phenomenon of sinkholes is generated mainly by a lowering of the level of the Dead Sea, and is increasing in the Dead Sea area. Most of the sinkholes develop near the northern section of the Dead Sea, where ICL Fertilizers' operations are not great. A small number of sinkholes have also appeared in the area of the evaporation ponds, and in other places in the Dead Sea Works area. The development of a sinkhole under a dike could cause the dike to burst, causing loss of the solutions in the pond. ICL Fertilizers is working to locate the development of sinkholes in the area of the plant, and to fill them in when they appear.

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<sup>15</sup> The information stated in this section includes forward-looking statements. This information is based upon competitors' announcements and also upon statistics published by the United States Department of Agriculture. Actual results may materially differ from these projections as a result of changes in market conditions and/or production and/or grain consumption relative to these projections, which may occur.

## 2. Fertilizers and Phosphates

- a. Phosphorus, which is provided by fertilizers that are derived from phosphate rock, directly assists with a long list of plants' physiological processes, including production of sugars (including starch), photosynthesis, and energy transfer. Phosphorus strengthens cereal straw, stimulates root development, promotes flower formation and hastens the maturity of crops.
- b. The principal raw material used in production of phosphate products is phosphate rock. ICL Fertilizers mines phosphate rock from open-pit mines in the Negev Desert. During 2006, ICL Fertilizers produced approximately 2.9 million tons of phosphate rock. ICL Fertilizers has the capacity to produce approximately 4.5 million metric tons of phosphate rock annually. In 2006, ICL Fertilizers used approximately 90% of its phosphate rock production to manufacture phosphate fertilizers and phosphoric acid, which have greater added value. The balance of the phosphate rock was sold to external producers who manufacture phosphoric acid and fertilizers and as direct application fertilizer. ICL Fertilizers' policy is to shift the maximum possible portion of its phosphate-related sales away from the sale of phosphate rock as a raw material to the sale of higher value-added downstream products.

During 2005 and 2006, as part of a phosphate operations strategy project, ICL Fertilizers made investments in conjunction with a program to shift its sources of phosphate. This plan is intended to bring about a reduction in the costs of beneficiating and producing phosphate rock by adopting ecological improvements in the production process including a shutdown of the phosphate rock calcining facility in the Zin area of the Negev. The project ended in 2006. At the end of 2005, the Zin flash-calcining facility was shut down, and starting from the beginning of 2006, Rotem switched to a new work program with regard to sources of rock for production of acid, as planned.

- c. ICL Fertilizers uses phosphate rock to produce fertilizer-grade phosphoric acid and fertilizers, in addition to selling it as an end-product for direct applications and to manufacturers of acids and fertilizers. Phosphoric acid production also requires significant quantities of sulfur, which ICL Fertilizers purchases from third parties. ICL Fertilizers produces fertilizer-grade phosphoric acid, phosphate fertilizers, compound fertilizers and specialty fertilizers at its facilities in Israel. In addition, ICL Fertilizers has facilities for production of phosphate fertilizers and compound fertilizers in the Netherlands, Germany and Belgium, and a feed additives facility in Turkey.

Most of the compound fertilizers manufactured by ICL Fertilizers are based on the elements phosphorus and potassium. Some of the compound fertilizers also contain nitrogen, which ICL Fertilizers acquires from third parties and incorporates with the phosphorus and potassium. ICL Fertilizers also produces specialty fertilizers including liquid fertilizers and fully soluble fertilizers. ICL Fertilizers is active in developing downstream products based on phosphate rock, including phosphate fertilizers and compound and specialty fertilizers.

The specialty fertilizers manufactured by ICL Fertilizers are designed for use mainly in intensive agriculture. In the assessment of ICL Fertilizers, it is the leading worldwide producer of MKP (Mono Potassium Phosphate), which is a unique type of fully soluble fertilizer, which contains potash and phosphate and is used mainly in drip irrigation systems and also in foliar spray and in hydroponic greenhouses. As of 2006, the Company also produces the soluble fertilizer MAP (Mono Ammonium Phosphate) in a special facility, the output of which is intended to reach 10% or more of world-wide yields<sup>16</sup>.

These two products are produced in special processes developed by the Company, which are based on raw materials which ICL controls.

The Company's special fertilizers also include innovative fertilizers developed by the Company to meet the special requirements of customers, and which are being successfully produced in a semi-industrial demonstration facility. These are

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<sup>16</sup> The information contained in this section is based on the Company's assessment of current market conditions, and is forward-looking information. It might change, *inter alia*, due to changes in supply of fertilizers, including substitute products, as well as changes in demand or prices.

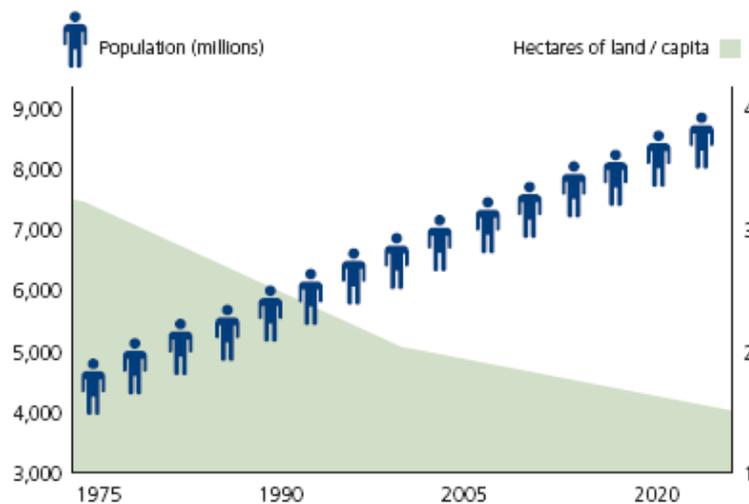
PeKacid and MagPhos, which are particularly acidic fertilizers, and Nutrivant, which is an NPK which contains a special surfactant for spraying foliage.

At the end of 2006, ICL Fertilizers completed construction of a facility for mixing various kinds of soluble NPK for the local and export markets.

### 3. Influence of external factors on ICL fertilizers<sup>17</sup>

There is inter-dependency between the amount of arable land, the amount of food required by the population, and use of fertilizers. As the amount of arable land declines and the population grows, there is a need to produce greater quantities of food in smaller areas (in other words – a greater yield of produce in a smaller given area). This situation requires increasingly greater use of fertilizers.

Global population growth and the process of urbanization which causes diminishing arable land per capita, are expected to cause growth in demand for fertilizers over time (see the chart below). In addition, the increase in the standard of living and the resulting changes in nutrition habits lead to an increase in consumption of meat, primarily in the developing countries. Consumption of fertilizer per nutrition unit of meat is higher than for that of a nutrition unit of produce. As a result, consumption of fertilizers has increased. In addition, due to high energy costs and the ecological effects of using certain fuels, there is a growing worldwide effort to move towards use of fuels that are produced from agricultural products. According to international agriculture and food agencies, the average annual long-term growth rate for fertilizers is projected to be 2-3%. Despite the long-term projections for growth in demand for fertilizers, in the short term demand for fertilizers is volatile and is affected by factors such as weather in the world's central agricultural growing regions, fluctuations in planting main crops, agricultural input costs, agricultural product prices and developments in biotechnology. Some of these factors are influenced by subsidies granted to farmers or to producers of inputs for agriculture in various countries, and by environmental regulations. In addition, currency exchange rates, legislation and international trade policies have an impact on the supply, demand and level of consumption of fertilizer worldwide. In spite of the volatility that can be caused in the short term as a result of these factors, the Company estimates that the policy of most countries worldwide is to ensure orderly and high-quality supply of food to the population, and thereby to encourage agricultural production, which should preserve the growth trend.



Source: FAO (Food and Agriculture Organization of the UN)

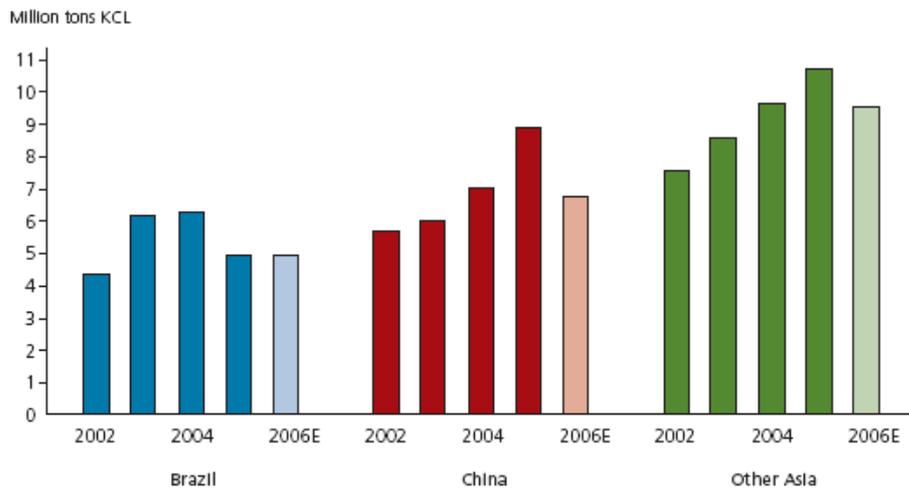
**Source: FAO (Food and Agriculture Organization of the UN)**

<sup>17</sup> The annual growth estimates of long term projected fertilizer consumption are considered forward-looking statements. The realization of these estimates cannot be certain and they are based on assumptions regarding population growth and reductions in farmland published by the FAO (the Food and Agriculture Organization of The United Nations) and based on estimates of the Company. Changes in growth of population and/or farmlands relative to these assumptions, in addition to changes in nutrition habits, will cause actual results to differ materially from the results projected or implied by this information.

During the past few years, changes have occurred in global agriculture that have significantly affected worldwide fertilizer demand. Heavy consumption of grains for food and for animal feed, which outpaced worldwide production, caused a decrease in cereal inventories. The increase in demand for fertilizers, including potash and phosphate fertilizers, brought about an increase in prices for these products in recent years. A partial contributor to the price increase was a rise in main production input prices for fertilizer producers. On the supply side, primarily with regard to potash, gaps between world - wide production capacity and actual production narrowed, mainly as a result of the increase in demand. In addition, the Company estimates that in the past few years there has been a trend of high demand for fertilizers in the developing countries such as Brazil, India, and China. Increased use of agriculture-derived fuel (Bio fuels) in recent years is likely to contribute as well to future growth in demand for fertilizers. Thus, for example, according to projections by the U.S. Department of Agriculture, increased consumption of corn for production of ethanol, which accounts for 15% of the corn consumption in the United States, has been one of the main growth catalysts for demand for corn (which is a primary source of demand for fertilizers) in recent years. Demand for “bio fuel” is growing by more than 20% annually and this trend is expected to continue as well. In spite of the above, it is not possible to predict the expected pace of these changes and their magnitude.<sup>18</sup>

In global terms the stable growth trend of potash demand has continued over time. Even when potash demand in a given year drops in a certain area of the world, it is likely to be offset by increased demand elsewhere, either in that year or thereafter.

### Potash Imports in Primary Countries



Source: Fertecon Potash Outlook 2006/3, IFA

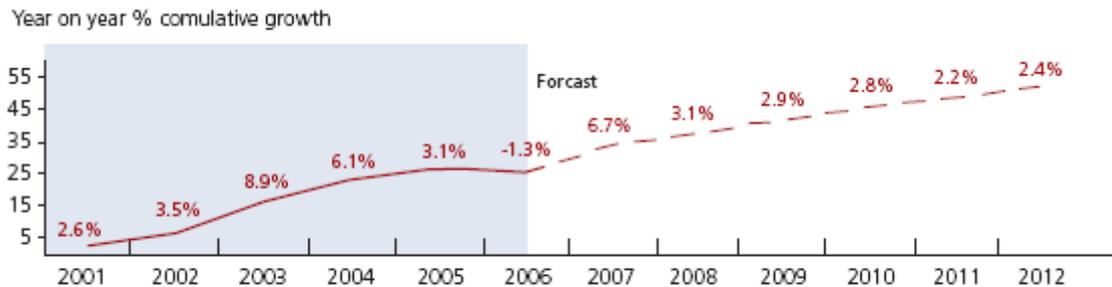
During the three-year period of 2002-2004, worldwide potash demand rose 20%. This growth in demand allowed most suppliers to reach their full production capabilities and even to open “bottlenecks” for purposes of increasing production. This occurred in parallel with significant price increases. In 2005, market demand returned to a lower growth rate than in past years. As of the date of this Report, projections are (see for example Fertecon) that the rate of growth in demand for potash in the coming years will continue to grow at an average of 2-3% annually, allowing suppliers to reach their full production capabilities while maintaining a balance between supply and demand in the next few years.<sup>19</sup>

<sup>18</sup> The information stated in this section includes forward-looking statements based upon projections of the United States Department of Agriculture. These projections may not be realized, in whole or in part, and they are dependent among other things upon fluctuation of the global economy, the rate of food production, fluctuations in supply and demand for various production components, industrial and agricultural developments, the worldwide trade balance specifically between the developed and developing countries, the impact of currency exchange rates and others.

<sup>19</sup> The information stated in this section and the accompanying graph includes forward-looking statements based upon various projections in professional publications, such as Fertecon. These projections may not be realized, in whole or in part, and they are dependent among other things upon fluctuation of the global economy, climate conditions, the rate of food production, fluctuations in supply and demand for various production components, industrial and

In 2006, there was a slow-down in trade in potash following two years of record demand. The trading year commenced with some hesitation due to the negotiations between BPC - the Russian / Belorussian company and Chinese customers, which were drawn out until July 2006, and this caused a delay in sales to China and India. Another negative factor in the demand for potash was caused by a weakening of the agriculture market in Brazil. Recovery in this market took place following the execution of agreements in China and India during the fourth quarter of the year, and a recovery of the Brazilian market as a result of increased seed prices.

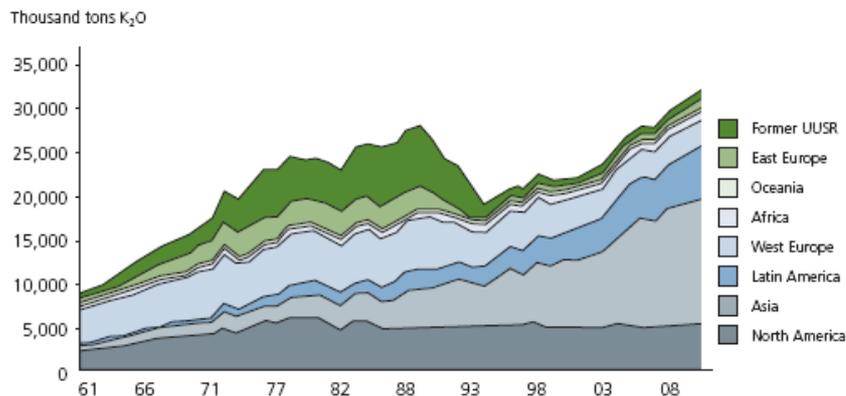
The following is a graphical description of the current projections regarding the growth rate for worldwide potash demand<sup>20</sup>:



Source: Fertecon Potash Outlook 2006/3

Past data shows that the trend of growth in demand for potash has been constant since the mid-Nineties with the main growth concentrated in Asia and Latin America. There is stable demand in North America and Europe. The distribution is described below<sup>21</sup>:

#### Potash Consumption Over Time in Various Countries



Source: Fertecon Potash Outlook 2006/3 (forecast); FAO STAT data, 2005 (actual)

agricultural developments, the worldwide trade balance specifically between the developed and developing countries, the impact of currency exchange rates and others.

<sup>20</sup> The information set out in this section and in the Graph accompanying it includes forward-looking information which is based on various estimates in professional publications. These estimates might not come to fruition or might only come to partial fruition, and are dependent, *inter alia*, upon fluctuations in the world economy, upon climactic conditions, upon the rate of food production, upon fluctuations in demand and supply for various production inputs, upon developments in agriculture and industry, upon the world trade balance in particular between developed and developing countries, upon the effects of exchange rates, etc.

<sup>21</sup> The information set out in this section and in the graph accompanying it includes forward-looking information which is based on various estimates in professional publications. These estimates might not come to fruition or might only come to partial fruition, and are dependent, *inter alia*, upon fluctuations in the world economy, upon climactic conditions, upon the rate of food production, upon fluctuations in demand and supply for various production inputs, upon developments in agriculture and industry, upon the world trade balance in particular between developed and developing countries, upon the effects of exchange rates, etc.

4. ICL Fertilizers' operations are subject to various legislative and regulatory limitations.

For details see section 4.1.15 below.

5. Quantitative data regarding production and sales, in thousands of tons:

	Production		Sales*	
	2006	2005	2006	2005
Potash	5,086	5,263	3,912	4,721
Fertilizers	1,614	1,636	1,656	1,671
Phosphate rock	2,949	3,236	421	365

\* To external customers

#### 4.1.2 **Products and services**

ICL Fertilizers manufactures fertilizers and raw materials for the fertilizer industry and for application by end customers. The raw materials produced by the Company are potash (potassium chloride), phosphate rock, sulfuric acid and phosphoric acid, which are used in the production of phosphate fertilizers and compound fertilizers or for direct application. The compound fertilizers are products that contain various formulations of potash, phosphorus and nitrogen, which are the vital nutrients for crops, and are used for application by the end user.

#### 4.1.3 **Breakdown of revenues and profitability of products and services**

The following is an analysis of the revenue and gross profit according to product:

	Year	Revenues (\$ million)*	% of ICL Revenues*	Gross profit (\$ million)	Gross profit (% of revenues)
Potash	2006	925.1	26.4	410.9	44.4
	2005	1,064.1	32.8	519.2	48.8
	2004	932.3	31.8	416.9	44.7

\* For purposes of this table, revenue figures for the product group and for ICL used in calculation of percentage figures are before setoff of revenue among business segments.

In 2006, there was a fall in revenues from sales of potash as a result of a reduction in the quantity of potash sold to China and India, flowing from the late conclusion of contracts for sale to those destinations, due to the lengthy duration of negotiations as aforesaid. The drop in quantities sold was set off in part by an increase in the average price.

	Year	Revenues (\$ million)*	% of ICL Revenues*	Gross profit (\$ million)	Gross profit (% of revenues)
Fertilizers and phosphates	2006	568.9	16.3	126.9	22.3
	2005	548.5	16.9	114.4	20.9
	2004	550.4	18.8	120.1	21.8

\* For purposes of this table, revenue figures for the product group and for ICL used in calculation of percentage figures are before setoff of revenue among business segments.

The increase in revenues in 2006 stems from an increase in quantities of phosphate rock and phosphoric acid sold to external customers and from an increase in the selling price of fertilizers and acid. This effect was set off in part by a reduction in the quantities of the fertilizers sold.

#### 4.1.4 **New products**

ICL Fertilizers is exploring new markets for its fertilizer products, including markets in Asia. ICL Fertilizers continues to develop innovative and advanced fertilizer products.

During the course of 2006, ICL fertilizers completed the process of running-in a facility in Mishor Rotem in the Negev desert for production of technical-grade map (mono ammonium phosphate). This product is a compound of phosphorus and nitrogen and serves primarily as a fertilizer for irrigation agriculture that is fully soluble and has many additional quality

characteristics. The process of manufacturing map has high synergies with the company's existing production processes. ICL fertilizers manufactures additional types of fully soluble fertilizers and markets the soluble fertilizers independently and through joint venture with other international producers of specialty fertilizers. In addition, ICL fertilizers is diligently developing new products in this area of soluble fertilizers.

In this context, an innovative potassium phosphate fertilizer has been developed, with a very high ph (2.2) – PeKacid, on the basis of which the company is now investing in developing the combination of this fertilizer with additional micro-elements. The company also developed a series of NPK fertilizer mixtures which have a special surfactant that is designed for foliar spraying.

#### 4.1.5 **Customers**

##### A. Dependence on single customer

ICL Fertilizers does not have any single customer that accounted for more than 10% of the total sales of ICL.

##### B. Geographical distribution of external sales

	2006		2005		2004	
	%	\$ million	%	\$ million	%	\$ million
Israel	11	144	10	139	9	124
North America	1	15	1	20	1	16
South America	20	260	19	264	24	314
Europe	39	508	39	546	42	552
Asia	23	300	25	348	18	231
Rest of World	6	69	6	76	6	72

The decrease in sales in Europe was attributable to a decrease in quantities sold in Europe, due to the low level of demand and due to an increase in the quantities sold by other suppliers from Russia in this market.

The relative decrease in sales in Asia was due to the late conclusion of sale contracts in China and India due to the lengthy duration of the negotiations on the sale contracts for this year.

The relative increase of sales in South America is attributable to demand in the Brazilian market, which continued beyond the end of the traditional season in September / October, and due to high levels of demand in Argentina. In all, sales throughout the year were similar to sales in the previous year.

#### 4.1.6 **Marketing and distribution**

The primary markets of ICL Fertilizers are Brazil, India, China, Israel, France, Spain, England and Germany. ICL Fertilizers sells its fertilizer products primarily via a network of its own sales offices as well as sales agents throughout the world. Most of ICL Fertilizers' sales are not transacted by means of long-term contracts or orders, but rather via current orders close to the date of supply. Consequently, the concept of a backlog has no meaning for ICL Fertilizers. ICL Fertilizers ships its products from Israel to customers overseas by ships (mainly bulk ships) that it leases in the marketplace (via the "Negev Star" company) and loads using dedicated facilities in the ports of Ashdod and Eilat.

In addition, ICL Fertilizers maintains dedicated bulk loading facilities in Barcelona (IP), in Amsterdam and in Ludwigshafen (Amfert) and in Teesside (CPL).

#### 4.1.7 **Competition**

##### A. Conditions of competition in areas of activity and tackling competition

###### 1) General.

The main competitive factor in the field of fertilizers is the product price. The price is based on the cost of production and terms of supply and demand in the market. For this reason companies located in proximity to sources of raw materials, ports and

customers benefit from competitive advantages. In the estimation of ICL Fertilizers, its cost of producing potash in Israel is among the lowest in the world. In addition, its relative proximity to the Asian and Western European markets and advantages in costs of shipping to the Brazilian market, afford ICL Fertilizers a logistical advantage over other large fertilizer exporters that are active in these markets. Additional factors that affect competition include product quality and service.

2) Potash

ICL Fertilizers is an important player in the potash market. In 2006 ICL Fertilizers ranked sixth in size among potash producers worldwide, and was the second-largest in Western Europe. The six leading worldwide manufacturers in this industry produce approximately 80% of the global potash production<sup>22</sup>.

In 1992, the European Union imposed protective levies to prevent sales at dumping prices on the import of potash from Belarus, Russia and the Ukraine. These regulations were in effect until May 2005. In November 2005 and in December 2006, the directorship of the European Union in the context of a review proceeding, decided to reduce the anti-dumping protective levies on potash that is produced by the two Russian manufacturers, and in parallel reached agreement with those manufacturers, pursuant to which the manufacturers committed to maintain minimum prices and an annual quota of sales that are not subject to levies. The Company believes that this will not have a material negative impact on ICL Fertilizers in the next few years, in light of the growing global demand for potash. The potential harm to sales in Europe as a result of the increase in quantities of sale of Russian potash will be set off by a redirection of sales to other worldwide markets in which relatively higher prices are prevalent<sup>23</sup>.

3) Fertilizers and Phosphates

The phosphate fertilizer market is extremely competitive. Among the competitors are international companies and government companies. This market is divided among many producers. ICL Fertilizers' share in the worldwide market is relatively small, though in Western Europe ICL Fertilizers is a leading producer and supplier of compound fertilizers based on phosphorus and potassium.

As noted above, the primary competitive factor in the phosphate fertilizer market is price. Additional factors that are less significant are product quality and new products that provide unique solutions.

ICL Fertilizers has no relative advantage with respect to cost of production of most of its phosphate fertilizers, except that due to its geographic location, logistical synergies with its potash operations in Israel, and its relative proximity to customers, ICL Fertilizers has logistical advantages over a number of other producers. For this reason ICL Fertilizers' strategy is to continue to develop production and sales of downstream products with higher added value, including specialty fertilizers. In addition, ICL Fertilizers is focused on markets where it has a logistical advantage. ICL Fertilizers is also working towards increasing sales in locations such as Australia that have "opposite seasons", thereby increasing the spread of its sales over the year.

B. Main competitors in the field of fertilizers

1) Potash

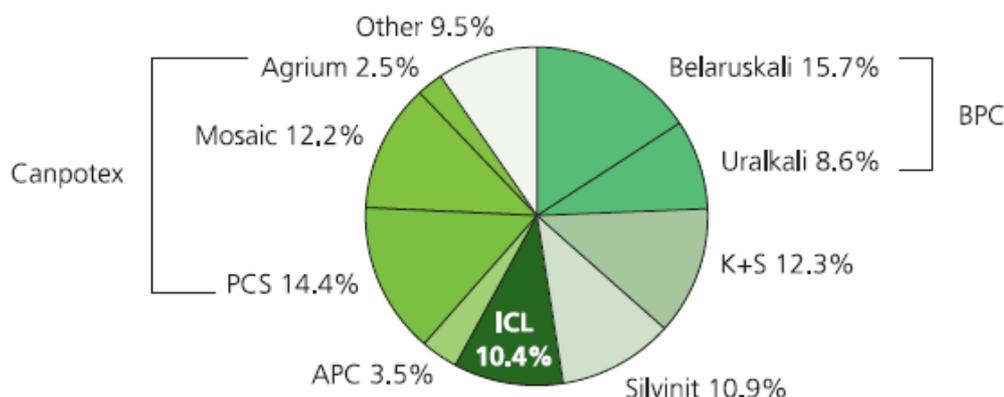
The significant competitors of ICL Fertilizers in the area of potash are: Potash Corporation of Saskatchewan (US and Canada), Mosaic (US and Canada), Belaruskali (Belarus), KS (Germany), Uralkali (Ukraine), Silvenit (Russia) and Arab Potash Company Ltd. (Jordan).

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<sup>22</sup> Source: Fertecon

<sup>23</sup> The Company's projection mentioned above regarding the effect of the removal of the anti-dumping levies on ICL's results constitute forward-looking statements, and are based on the Company's projections regarding the global status of demand and export of potash. The realization of these projections is uncertain. If the demand for potash drops, or alternatively exports rise, results will differ materially from the results projected or implied by this information.

Production of potash by ICL Fertilizers and competitors in 2006 was as follows:



**Canpotex – The export association of the Saskatchewan potash producers (Canada).**

**BPC – The export association of Belaruskali and Uralkali**

**Source: Fertecon 2005, Company reports and ICL Fertilizers data.**

## 2. Fertilizers and Phosphates

There are many phosphate production facilities located in many countries including the United States, Morocco, China, Russia, Jordan and Tunisia. The main producers whose product areas are more relevant to the competitive environment of the Company are: Mosaic (US), Potash Corporation of Saskatchewan (US), Office Cherrifienne de Phosphate (Morocco), Group Chimique Tunisienne (Tunisia), Prayon S.A. (Europe) and Roullier Group (Europe).

### C. Approach for tackling competition

ICL Fertilizers holds an advantage, as noted above, in its low production cost of potash in Sodom. In addition, ICL Fertilizers works very actively to enhance its competitive strengths. These activities include processes to realize efficiencies and exploit advantages of scale, technological improvements in production processes, development of specialty niche markets, and development of products that respond to special customer needs and downstream products (including specialty fertilizers and soluble fertilizers) for which competition is relatively low. In addition, ICL Fertilizers capitalizes upon logistical advantages that it possesses relative to its competitors. ICL Fertilizers has the ability to utilize seaports in the Mediterranean Sea, the Red Sea and Europe for delivery to its various markets. In certain markets, ICL Fertilizers is able to combine an assortment of products for an individual market or customer, which provides it with an advantage vis-à-vis various customers, whereby ICL Fertilizers can ship its bulk products on larger ships and as a result at a lower cost per ton.

In addition, the combination of production facilities in a number of different locations worldwide and diverse logistical options, enable the Company to respond to customer needs and to be flexible with regard to delivery timetables and quantities.

#### 4.1.8 Seasonality

The seasonal nature of demand for ICL Fertilizers' products gives rise generally to quarterly sales volatility, as sales levels in the second and third quarters are generally higher than sales in the first and fourth quarters. This year, the sharp fluctuations in the third and fourth quarters stemmed, as aforesaid, from the delay in concluding contracts in China and India, which affected all of the demand for potash around the world during the first half of the year.

The following is a breakdown of revenues by quarter for 2004-2006, in millions of dollars:

	1 <sup>st</sup> Quarter	2 <sup>nd</sup> Quarter	3 <sup>rd</sup> Quarter	4 <sup>th</sup> Quarter
2006	281	358	393	422
2005	381	428	398	366
2004	334	363	373	386*

\* Revenues in the fourth quarter of 2004 were exceptionally higher than other quarters primarily as a result of price increases for potash and other fertilizers.

Production at the plants remains at similar levels throughout the year, so that in the first and fourth quarters inventories accumulate which are subsequently used to respond to customer demand in the second and third quarters. The demand for raw materials (fine potash, phosphate rock, and phosphoric acid) which ICL Fertilizers sells to the fertilizer industry is relatively less volatile and is generally stable throughout the year.

#### **4.1.9 Production capacity**

ICL's production capability is based on the nominal hourly output of the various plants, multiplied by potential hours of operation per year.

##### **A. Potash**

ICL Fertilizers' annual production of potash in 2006 was 5.1 million tons (approximately 10% of the total global production). The total potential annual production capacity of ICL Fertilizers in the field of potash is approximately 6 million tons. Due to commercial considerations, the Company is examining increasing its production in Israel, in the near future, at the expense of a reduction of production at its facilities in Europe<sup>24</sup>.

During 2005, the Company began an investment in Evaporation Pond 3 at the Dead Sea, the purpose of which is to increase its production capacity for carnallite by converting part of the Pond area from salt precipitation to carnallite production, the equivalent of approximately 250,000 tons of potash. This investment is expected to be completed in 2008.

##### **B. Fertilizers and phosphates**

In 2006, ICL Fertilizers produced approximately 2.9 million tons of phosphate rock. ICL Fertilizers has annual production capacity of approximately 4.5 million tons of phosphate rock. The Company uses 90% of its annual production of phosphate rock as a raw material for the production of downstream products.

In 2006, ICL Fertilizers produced approximately 1.6 million tons of phosphate fertilizers and compound fertilizers which represent nearly the full production capacity for phosphate fertilizers and compound fertilizers of ICL Fertilizers.

#### **4.1.10 Research and development**

##### **A. Research and development activities and results**

ICL Fertilizers' research and development activities during the period of this report focused on the following topics:

- 1) Adaptation of types of phosphate rock to production of phosphoric acid and its downstream products.
- 2) Development of alternative methods for increasing potash raw materials production capability in Sodom.
- 3) Development of new products in the area of soluble fertilizers.
- 4) Quality improvement among its offered products.
- 5) Development of processes for exploiting phosphate deposits, thought till now to be uneconomical for the purpose of production of phosphoric acid.
- 6) Research in the area of environmental protection, including research to reduce the amount of effluent on site at Rotem.
- 7) Potential impact of the Dead Sea Canal on the production in Sodom.

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<sup>24</sup> The Company's assessment as aforesaid regarding its intention to increase its potential production capacity in Israel at the expense of a reduction of its potential production capacity at its facilities in Europe is forward-looking information, which is based on the Company's assessments of the state of demand and supply for potash around the world. The realization of these assessments is uncertain. If demand for potash increases, or supply decreases, the outcomes could be different from those estimated or implied from this information.

B. Research and development expenses

ICL Fertilizers' research and development expense in the report period was approximately \$2.8 million.

4.1.11 Raw materials and suppliers

A. Primary raw materials used in the field of fertilizers

1) Potash

ICL Fertilizers manufactures and produces the basic raw materials for production of potash – carnallite in Israel and sylvinitite in Spain and England. The other primary components it uses for production of potash, as noted, are heavy fuel (natural gas in Spain and England), industrial water and maintenance supplies.

2) Phosphate rock

The primary raw material used in production of ICL Fertilizers' phosphate products is phosphate rock. Phosphate rock is extracted from open-pit mines in a number of locations in the Negev Desert. ICL Fertilizers also sells phosphate rock as an end-product.

3) Phosphoric and sulfuric acids

ICL Fertilizers manufactures fertilizer-grade phosphoric acid at its facilities in Israel. Phosphoric acid is produced from phosphate rock and sulfuric acid, which is also produced in Israel. Sulfuric acid is produced from sulfur.

In 2006, ICL Fertilizers consumed approximately 660,000 tons of sulfur. The sulfur was purchased from a number of external sources in Russia, Germany, Kazakhstan, Italy and Israel.

4.1.12 Working capital

A. Raw material inventory policy

ICL Fertilizers itself produces most of the raw materials used in its production processes. The raw materials acquired from external sources are mainly sulfur and a few other components (nutrients) for production of compound fertilizers.

The primary raw material for potash production is located in evaporation ponds in Sodom and underground mines in England and Spain. The phosphate is mined from open-pit mines in the Negev Desert.

The Company maintains sulfur, phosphate and other auxiliary material inventories in quantities that take into account the projected level of production based on consumption characteristics, supply dates, distance from the supplier and other logistical considerations.

B. Finished product inventory policy

ICL Fertilizers' strategy is to maintain adequate inventory to ensure orderly supply to customers in consideration of the customers' distance from the production sites and their requirements for inventory availability.

In Sodom there is a relative advantage of virtually unlimited storage capability. Thanks to the dry climate in Sodom potash can be stored in piles in open areas. Therefore the potash production in the production facilities in Sodom is not necessarily dependant on the rate of sales. Product that is not sold is stored in open areas within the area of the plant. The storage advantage in Sodom enables ICL Fertilizers to produce potash continuously also in Spain and England while the main potash inventory of ICL Fertilizers is held in Sodom. In 2006, due to the delay in signing potash sale agreements in China and India, and a reduction in sales as a result, ICL Fertilizers accumulated surplus potash inventory. In the assessment of ICL Fertilizers, this surplus inventory will be sold by 2009<sup>25</sup>.

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<sup>25</sup> The information set out in this section includes forward-looking information. The Company's ability to sell the surplus inventory depends, inter alia, on the demand for fertilizers, their prices, competition from other producers, availability

Regarding phosphate fertilizers, ICL Fertilizers' strategy is to produce in an optimal manner which enables ICL Fertilizers to choose the preferred alternatives among selling fertilizer-grade phosphoric acid, phosphate fertilizers, compound fertilizers, or producing pure phosphoric acid. The strategy of maintaining inventories is set accordingly.

C. Credit policy

ICL Fertilizers extends credit terms to its clients according to customary practices in their locations. The group's sales are generally covered by trade credit risk insurance or by letters of credit from banks with high credit ratings.

In 2006, average days of credit extended to customers rose in relation to the previous year as a result of a change in the mix of sales targets.

December 31, 2006		
	Average credit level (\$ millions)	Average credit days
Customers*	218	55
Suppliers	152	66

\* Figures for customers' receivables and average days of credit exclude customers whose obligations have been sold through a securitization transaction as described in section 5.4.3 below and customers whose receivables have been discounted through other arrangements.

**4.1.13 Environmental matters**

A. General

ICL Fertilizers acts diligently and constantly endeavors to minimize its impact on the environment. The Company operates in the framework of the ISO 14001 environmental standard and the Responsible Care program and its plants have adopted internal compliance programs regarding environmental matters. The Board of Directors of ICL Fertilizers monitors environmental protection issues on an ongoing basis and has even appointed a special subcommittee for oversight of these matters. ICL Fertilizers also has an internal compliance mechanism in place with respect to environmental issues.

ICL Fertilizers restores mining sites both during mining and after the mining is complete. ICL Fertilizers also restores areas of mining clay and wadi loam in the area of Sodom. At the Zin Oron and Mishor Rotem mining sites, financing for restoration of the mines is provided by the Phosphate Mines Restoration Fund and financing for the quarry sites in Sodom is provided by the Dead Sea Sites Restoration Fund; in both cases the funds are financed by ICL Fertilizers.

In the framework of the Responsible Care program, in the beginning of 2005 the Company established a Community Advisory Panel (CAP), consisting of senior executives of the Dead Sea Works, residents of the area near the plants, and representatives of the hotels in Sodom. The panel deals with environmental problems that concern the residents and with cooperative activities. In this context, some 900,000 sqm was allocated to farmers from Neot Hakikar, a monitoring station was set up in communities at the instruction of the Ministry for the Environment, a course on environmental issues for residents has been started, visits have been conducted for residents at the ICL Fertilizers sites, and for management of the facilities at the various communities.

ICL Fertilizers runs a training program for employees on the topic of environmental matters in the various companies, in an effort to raise the Company's employees' awareness of and participation in matters of environmental matters. This activity includes targeted training for professional teams, seminars for employees on the topic of environmental protection, emergency staff drills for handling hazardous materials, courses on environmental protection for foremen and shift managers, a course for

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of land transport to the ports, in the ports as well as availability of ocean-going vessels, and the volumes of potash produced and sold by ICL Fertilizers potash plants in Israel and outside of Israel.

engineers and a course for operators, and training is also held for work managers to be environmental protection trustees.

Below is a list of actions taken by ICL Fertilizers during the past year:

1) Air Quality

Reduction of airborne emissions from point sources, including shutdown of the flash-calcination facility on the Zin site (at the end of 2005). In Sodom, installation of scrubbers on the potash furnaces has been completed.

The Company's multi-year program for reduction of airborne emissions from non-point sources is continuing.

The Company continues to take actions to reduce dust emissions resulting from the production process by Amfert in Holland.

2) Liquid Effluents

- In Spain, a multi-year program is underway to relocate salt piles while paying close attention to the issue of wastewater drainage and handling of sludge
- Waste recycling by ICL Fertilizers, whereby ICL Fertilizers removes metals, used oils and other disposable materials for recycling. In England the Company operates a backfill project with partial funding by the European Union, whose purpose is to inject part of the process by-products back into the mine instead of dumping them at sea.
- At the Dead Sea Works, technology for secondary treatment of sanitary effluent is being investigated jointly with the Ministry for the Environment. The pilot facilities will be tested during the course of 2007, and selection of the technology is expected to end by the end of 2008<sup>26</sup>.
- Continued progress of a master plan for methods of collecting liquids at Rotem.

B. Future material capital expenditures for environmental matters

During 2006, ICL Fertilizers invested a total of \$12.3 million in the acquisition of property, plant and equipment for prevention of environmental hazards and recorded \$10.7 million as a current expense. During 2007, ICL Fertilizers is expected to invest approximately \$20 million in property, plant and equipment and to incur similar current expenses to those incurred in 2006 for these purposes. In ICL Fertilizers' estimation, there is not expected to be a decrease in the level of these expenses in subsequent years.<sup>27</sup>

In January 2007, the Ministry for Protection of the Environment notified Tamar Local Council that it was about to add conditions to the business license of Dead Sea Works, relating to the power station, to take effect on January 1, 2008. Since the new requirements are even more stringent than the current ones, mainly on the matter of emissions of nitric oxide, ICL Fertilizers will be compelled to invest in the purchase of treatment equipment in order to comply with the new standards. ICL Fertilizers estimates the cost of the required investment in equipment for compliance with the requirements at about \$7 million, plus current operating inputs. ICL Fertilizers is considering investment in upgrading the existing power station, which will result, among

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<sup>26</sup> The information contained in this section is forward-looking and is based on existing statutes and standards, on the requirements of various authorities known at present and on engineering assessments with respect to the technology of the solution that the Company's engineers are currently in possession of. The realization of these estimates cannot be certain. Any change in any of these estimates, including any change in the estimates made by the Company's engineers, technological difficulties or the solution being tested, or in industrial implementation of it, or any change in implementation of the requirements of the authorities or the provisions of the law might bring about different results from the above.

<sup>27</sup> The Company's projections regarding the projected costs and/or expenses in the area of environmental matters constitute forward-looking statements, and are based on legislation and regulation currently in effect, on governmental requirements known to ICL Fertilizers and on investment estimates made by Company engineers. The realization of these estimates cannot be certain. Any change in governmental requirements or current legislation and regulations or the Company's estimates may cause materially different results in the Company's costs or expenses in this regard.

other things, in compliance with the standard for nitric oxide emissions. ICL Fertilizers has requested discussions with the Ministry for Protection of the Environment to coordinate the schedule for the alternative it decides on. At this stage, talks with the Ministry have not yet commenced, and therefore the final schedule is not yet known.

#### **4.1.14 Safety and health**

Some of ICL Fertilizers' products, as well as the raw materials and production processes, involve various levels of risks to persons who might be exposed to them. ICL Fertilizers must comply with the safety standards and requirements prescribed, in part, under local law, and in part under international and local standards. There is a trend towards updating these requirements and making them stricter, as a result of which, various investments might be required.

ICL Fertilizers is continually making special investments in setting up and improving its safety and health measures, with the aim of preventing accidents and continually taking care of employees in the segment, and of persons in and around the facilities and the products.

The boards of directors of ICL Facilities, the safety committees in the segment and the committees that operate at the facilities, periodically examine safety achievements and events, and the extent to which targets set in light of ICL Fertilizers' safety policy are met. In 2006, the ICL Fertilizers' Safety Committee met 4 times. ICL Fertilizers has a safety and health compliance plan and effects internal checking processes in order to ensure compliance with legal requirements and ICL's guidelines.

ICL Fertilizers is in advanced stages of implementation of the ISO 18001 Safety Management standard. As at the date of this report, all of the production facilities and services at Sodom, and all of the facilities at the Mishor Rotem and Zafir sites have received certification. ICL Fertilizers' facilities in the Netherlands are about to receive certification under the standard.

ICL Fertilizers has a training and compliance system set up in order to encourage a high and uncompromising level of awareness of safety and health among employees and contractors operating on its premises, including, *inter alia*, programs such as *Bamah* – Conduct-Based Safety, and the coordination and operation of ICL's Safety and Health Excellence Center. Safety and health goals are set periodically, with the aim of constantly improving safety and health goals, and implementation of such with the aim of achieving zero accidents. Employee protection means include, *inter alia*, protections on equipment and facilities and at work sites, protective measures for employees, procedures and training, appointing safety commissioners and safety teams, and investigating accidents and near-accidents.

In the area of health, there is an industrial health and preventative medicine system which includes, *inter alia*, periodic checks and risk assessments with respect to products and processes in facilities.

The transportation of chemical products around the world requires the implementation of appropriate transportation and storage measures. Transportation Enterprises Ltd., a subsidiary of ICL (which, as of January 1, 2007, is part of the ICL Fertilizers segment), transports a large portion of the dangerous materials and it has transportation equipment including dedicated tankers (isotankers) for this purpose. Transportation Enterprises has a safety system headed by a Safety Officer. There is also a system at ICL (in the ICL Industrial Products segment) for treating exceptional occurrences in the transportation of dangerous substances, which can be used, as necessary, by all of the ICL companies.

#### **4.1.15 Limitations on and regulation of the Corporation**

##### **A. Concessions and Permits**

Following is a brief description of restrictions in law or legal arrangements, related to the operations of the corporation, which could have significance implications for ICL.

##### **1) Dead Sea Concession Law (1991)**

According to the Dead Sea Concession Law, (1961) (hereinafter the "**Concession Law**"), as amended in 1986, ICL Fertilizers was granted a concession to commercially exploit the resources of the Dead Sea and to lease the ground required for its plants for a term that will expire on March 31, 2030, with the right of first refusal for a period after the concession's expiration. As consideration for the concession, ICL Fertilizers pays royalties to the Israeli government, calculated at

the rate of 5% of the value of the products ex works, excluding certain expenses, as well as leasing fees.

As of 2010, the government can demand renegotiation of the level of royalties, for quantities exceeding 3 million tons of potash produced and sold in any given year starting from that year onward, provided that the amount of the royalties for such surplus is to be no more than 10% of the value of the potassium chloride at the factory gate, less certain expenses.

On the basis of the Concession Law and the concession agreement, Dead Sea Works, a division of ICL Fertilizers, granted a sub-concession to Dead Sea Bromine, a division of ICL Industrial Products to produce bromine and bromine compounds from the Dead Sea, whose term also extends until 2030.

## 2) Phosphate mining

Rotem has mined phosphate in the Negev Desert for over fifty years. This mining is done through concessions for mining phosphate, granted from time to time by the State by authority of the Mining Ordinance. In June 2002 Rotem received three concessions covering Rotem Field (valid until the end of 2021), Tzafir Field (valid until the end of 2021), and Effeh Field (valid until the end of 2013).<sup>28</sup> With respect to its mining of phosphate, Rotem is obligated to pay royalties to the State according to the formula set forth in the Mining Regulations.

The validity of the concessions granted to Rotem is contingent upon mining permit agreements ("Permits") between Rotem and the Israel Lands Administration regarding the areas covered by the concessions. Rotem signed a final negotiated draft of the Permits and paid usage fees to the Administration as required and in accordance with the Permits, in September 2003.<sup>29</sup> The Administration has not yet returned the countersigned Permits, but is acting in accordance with their letter and spirit, and Rotem believes, according to a legal opinion of Rotem's legal counsel, that the Administration is obligated to the terms of the Permits.

With respect to the Hatrurim phosphate field, the Supervisor of Mines at the Ministry of Infrastructure gave notice of his intention to grant Rotem a mining concession, after it receives a mining permit by the Israel Lands Administration. The ILA has delayed granting the permit<sup>30</sup>.

Mining and quarrying activities require a permit specific to a given area within the framework of a zoning plan, according to the Planning and Construction Law, 5725 – 1965. These plans are updated, as needed, from time to time. As of the date of this Report, various applications have been submitted to the planning authorities. Plan applications that were submitted by Rotem for extending the implementation stages past 2005, relating to a plan from 1991 that target the Tzafir area (Zin – Oron) for mining and quarrying, was approved in its majority, and the implementation stages were extended for four years, until 2009. In parallel, Rotem was asked to prepare a new descriptive plan and detailed plans regarding a portion of the mine fields.

## 3) ICL Fertilizers' European concessions

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<sup>28</sup> These concessions replaced a prior concession from 1995, which combined a permit from the Israel Lands Administration, which was granted for the Rotem and Tzafir Fields, with minor changes in boundaries compared with the 2002 concessions, and whose term was until April 2005.

<sup>29</sup> The Israel Lands Administration has not yet returned signed copies of the Permits to Rotem, and in so doing has granted the request of the Ministry of Finance, stemming from a dispute regarding the amount of royalties payable from Rotem to the Treasury. A representative of the Treasury recently demanded payment of additional royalties for the period from 1995 to 2001, of about \$7.7 million, in addition to interest and linkage differences. Rotem believes this demand is baseless. Recently, Rotem and the State reached an agreement to refer the dispute between them to mediation, which has not yet commenced. According to a legal opinion of Rotem's legal counsel, the mining permits that it signed, and that are even being observed by both parties, are in full force and effect as of the date of Rotem's signature in September 2003, and on that date the mining permits from 2002 also took effect, and replaced the preceding permit from 1995.

<sup>30</sup> Here too, the ILA has acted in accordance with the request of the Ministry of Finance as a result of the abovementioned dispute regarding royalties. On March 25, 2007, the representative of the Accountant General informed the ILA that the Accountant General agrees to grant the mining permit for a period of one year until April 1<sup>st</sup>, 2008.

In Spain, ICL Fertilizers has been granted mining concessions based on Spanish legislation enacted in 1973. Pursuant to the legislation, the regional government in Catalonia issued special mining regulations, which granted IP, an ICL Fertilizers company, separate concessions for each of the 126 different sites relevant for its current and future mining operations. Some of the concessions expire between 2007 and 2009, but they are renewable. The remainder of the concessions is for terms lasting at least 50 more years. Under these concessions IP is obligated to pay a fixed amount of 0.35 Euro per dunam per year. The total royalties paid in 2006 were approximately 29 thousand Euros.

CPL's mining concession is based on approximately 113 mining leases and concessions for extracting various minerals, in addition to numerous easements and rights of way from private owners of land under which CPL operates or, in the case of mining underneath the North Sea, granted by the Crown Estate. The terms of all of these leases, concessions, easements and rights of way extend until 2015-2038.

- 4) For details of royalties the company pays under these concessions, see note 18B of the Financial Statements.

**B. Business licenses and toxic substance permits**

Valid business licenses have been issued for the sites of the business segment's plants, in accordance with legal requirements in their jurisdictions. In addition, ICL Fertilizers has a toxic substance permit under the Hazardous Materials Law (1993), and also a permit for pumping wastewater into the Dead Sea under the Prevention of Sea Pollution from Land-Based Sources Law (1988). These permits are current and require renewal from time to time.

**C. Outline plan and building permits**

Pursuant to special legislation with respect to the Dead Sea concession<sup>31</sup>, enacted in 1994 and 1995, the provisions of the Planning and Building Law were applied to the Dead Sea Works under the concession, subject to special provisions set out in the aforesaid legislation. These laws stated that any work done by March 2004 would be deemed to have been performed in accordance with the Planning and Building Law, and they also defined a list of particular projects which could be set up under a special brief procedure, deemed to have been approved under planning and building laws. The Company is operating in accordance with the zoning plan and the detailed plans for its facilities at Sodom. To date, a detailed plan has been approved for part of the land covered by the facilities (known as Area E at Sodom) for the Sodom – Zefa Conveyor Belt, and for the P-88 pumping station.

**D. Price monitoring under the Commodities and Services Monitoring Law (1957)**

- 1) Fertilizer prices – Selling prices of fertilizer-grade phosphoric acid for local Israeli customers, as well as the fertilizers sold in Israel, usually by F&C, are regulated under the Monitoring of Commodity and Service Prices Law (1996).

The quantity of these products sold in Israel by ICL Fertilizers is not material to ICL.

- 2) For further information regarding the declaration of ICL and its subsidiaries as a monopoly in certain fields in Israel see section 5.8 below.

**E. Standards and quality control**

ICL Fertilizers has a comprehensive quality control system. Each company in this business segment has its unique aspects (described below), but there are three central common issues:

- ISO 9000 quality management certification;
- All ICL Fertilizers plants in Israel are participants in the international Responsible Care program.

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<sup>31</sup> The Dead Sea Concession (Planning and Building) (Temporary Provisions for Particular Works) Law, 5754-1994 and the Dead Sea Concession (Legislative Amendments) Law, 5755-1995.

- In most of ICL Fertilizers' plants advanced quality control methodologies are implemented, such as: deployment of quality improvement staff, Six Sigma, and information management; also, its main facilities have a comprehensive system of internal quality checks, in which there are also various competitions between units. Here is a list of quality control procedures by plant:

1) Sodom Facility

All of the manufacturing and services facilities in Sodom have ISO 9001 management certification. The potash production facility in Sodom has ISO 14001 management certification for environmental quality.

All of the service and production facilities in Sodom have 18001 safety management certification.

2) Mishor Rotem and Tzafir Facility

These facilities have ISO 9001 management certification and they have ISO 14001 management certification for environmental quality and 18001 safety management certification.

A number of products have been approved as suitable for use as raw materials for the food industry and have HACCP certification.

3) Holland

ICL Fertilizers' facilities in Holland have the ISO 9001 quality management certification and ISO 14001 management certification for environmental quality, and are in the process of receiving 18001 safety management certification. AMFERT's white acid facility operates under the HACCP standard.

4) England

ICL Fertilizers' facilities in England have the ISO 9001 quality management certification and ISO 14001 management certification for environmental quality. Similarly, environmental control is conducted through EMAS (Eco-Management and Audit Scheme)<sup>32</sup>

5) Spain

ICL Fertilizers' facilities in Spain are in the process of receiving ISO 14001 management certification for environmental quality and ISO 90001 quality management certification.

6) Haifa

ICL Fertilizers' facilities at Kiryat Ata have the ISO 9001 quality management certification and ISO 14001 management certification for environmental quality.

7) Turkey

ICL Fertilizers' facilities in Turkey have the ISO 9001 quality management certification.

F. Compliance Programs

ICL Fertilizers has adopted compliance programs with regard to various topics including sexual harassment, antitrust, securities, safety and ecology.

G. Increase in water level in Pond 150

As part of the evaporation process, salt that precipitates to the bed of one of the evaporation ponds in Sodom, one of the sites of ICL Fertilizers, creates a salt layer of approximately 20 centimeters annually. Since the amount of raw material that is produced is affected by the volume of the brines in the Pond, it is necessary to preserve a fixed brine volume in the pond. To this end, the water level of the pond is raised by approximately 20 centimeters annually. In order to increase the level of the pond, ICL Fertilizers has to raise the dike that borders the pond every so often.

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<sup>32</sup> Refers to a European program, according to which the Company's environmental quality data are confirmed by a third party. The Company's environmental quality report which was verified by EMAS, was approved by the authorities with no requirement for further review.

The Ein Boqeq and Hamei Tamar Hotels and other facilities and infrastructure are located on the banks of the pond. Raising the water level of the pond above a certain level is likely to cause structural damage to the foundations and the hotel buildings situated close to the water's edge and to other infrastructure on the shoreline of the pond, depending on the height to which the water level is raised and the location of the relevant hotel or infrastructure.<sup>33</sup>

The above-mentioned situation requires the establishment of defenses for the hotels and infrastructure. Such protections are divided into two stages. The first is the stage of temporary defenses, which are supposed to provide protection pending the implementation of a permanent solution. The second stage is that of the permanent solution which is supposed to provide protection until the end of the current concession period (i.e. 2030).

Temporary defenses: In the first stage – that of the temporary defenses – three such defenses have been constructed so far, in the vicinity of the Moriah Hotel, in the area of Hamei Zohar and in the Ein Boqeq region. The levels of a number of infrastructures have also been raised. Each of the defenses were erected by putting up a dike near the relevant hotels, and these are called “Adjacent Defenses”. In the Ein Boqeq region, a system is also being installed for lowering the ground water, and this is due to be completed during 2007. There are also pumping systems in the Hamei Zohar area.

As at the date of publication of this Report, the temporary defense intended for the Nirvana Hotel, which is mainly the erection of a system to keep the groundwater level low, respective to the hotel, is also being set up.

Since the assessment is that the permanent solution will not be complete before 2015, it will be necessary to implement additional temporary defenses during the period leading up to that date. As we have seen, erection of the first temporary defenses (for the Nirvana Hotel) is supposed to end in 2007, and additional defenses are supposed to be in place by the end of 2008. This matter is being handled by the Government of Israel which imposed it on the Ministry of Tourism. It is uncertain whether the erection of these protections will be completed on time. There might be delays in the timetables due to failure to obtain the permits required by law to perform the necessary works on time. Failure to complete a protection on time might cause damage to the hotels and/or significant financial damage to the Company.

With respect to the permanent solution, in 2004, the government ordered the Ministry of Tourism to evaluate three alternatives for a permanent solution. The harvesting alternative, which is based on harvesting the salt precipitated in the pond from the floor of the pond in order to keep the water level constant; an alternative of moving some of the hotels and the Lagoon Alternative. Pursuant to the Lagoon Alternative, another dike would be erected in the pond which would separate the portion near the hotels, where the water level would remain static, from the rest of the pond, where the level would rise each year. A committee set up by the government recommended the Lagoon Alternative.

As at the date of this Report, the government has given notice that in its assessment, the tests (which are being done by a team set up by the Ministry of Tourism) to decide which alternative will be implemented, will be completed in another three years.

In 2006, the Dead Sea Hotels Union filed a petition to the High Court of Justice. It requested that the Court order the State to abandon the hotel removal alternative; to decide within three months which of the other two remaining alternatives (harvest or lagoon) would be implemented; that the permanent solution be completed no later than the end of 2007; and to declare that the hotels would not bear any expense relating to the permanent solution. An interim injunction (which has not been awarded at this stage) was also requested prohibiting the raising of the water level in Pond 5 above the level planned for the end of 2008.

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<sup>33</sup> As far back as 1971 it was widely known, including to the various authorities, that the water level in Pond 150 will rise annually by approximately 20 centimeters. Most of the hotels signed a document in which they acknowledge their awareness of the rising water level and that they will take this matter into account in the planning and construction of the hotels, and that they will bear the costs of building barriers and they shall have no claim against DSW with respect to the raising of the water level.

The High Court ruled that the State must submit a timetable for implementation of the defenses and this was done in respect of both the temporary protections and the permanent solution. In an additional ruling, the High Court held that there is a “need for special, constant and unwavering diligence” in handling the matter, and that it is important that budget decisions and statutory processes relating to the temporary defenses and the permanent solution be advanced with the relevant persons taking into account the time factor. At the end of February 2007, the State submitted a notice to the Supreme Court which states that there are delays in actual performance compared with the timetable which the State announced to the court.

With respect to financing, in terms of the temporary defenses that are currently being implemented, the Arrangements Law of 2002<sup>34</sup> provides that the financing is to be divided such that the State is to bear ½ and each of the Tamar Regional Council, the Company and the Hotels would bear 1/6. No decisions have been made regarding financing arrangements for other temporary defenses or regarding the permanent solution. On December 24, 2006, the government decided “to budget up to NIS 70 million with permission to make an undertaking under the budget of the Ministry of Tourism for the purpose of contracting in order to test the viability of the long-term alternatives for protecting the hotel area at Ein Boqeq – Hamei Zohar.; to budget up to NIS 30 million with permission to make an undertaking under the budget of the Ministry of Tourism for the purpose of planning and performing urgent protection works at the Ein Boqeq – Hamei Zohar area.” And that “the Minister of Finance will make regulations within 45 days setting out the financing arrangements between the various partners with respect to completion of Dead Sea defenses, including the methods to be used for budgeting such.” (all as set out in the decision). As at the date of this Report, no such regulations have been made. DSW is of the opinion that it is not required to bear the costs of these protections.

In the above petition to the High Court and in the responses given under it by the State<sup>35</sup>, the Tamar Regional Council and the Company, the State contended that the time had not yet arrived to deal with the question of financing (either of the additional temporary defenses or of the permanent solution). The others, including the Company, expressed the position that the State must bear the funding of these protections.

#### H. The Dead Sea Water Level and the Sea Canal

The water level of the Dead Sea (its northern section) drops about one meter each year. The decreasing water level is accompanied by a shrinking of the sea area and other phenomena such as creation of sinkholes, underground holes and deepening of the river courses that flow to the Dead Sea. The falling water level stems from the policies of the Jordanian, Syrian and Israeli governments to utilize the water resources of the Dead Sea catchment area. The extraction of the Sea’s salts by plants in Israel and Jordan also contributes somewhat to the drop in the water level. According to a study performed on behalf of the government<sup>36</sup> (the “Default Choice Report”), utilizing the water sources and the activities of the plants prevent approximately 1.25 billion cubic meters annually of water which used to flow into the Dead Sea from flowing into it, being exploited instead. Maintaining the current depth and surface area of the water would require an additional inflow of 650 million cubic meters per year.

In 2003 the Israeli government decided to evaluate a number of alternatives for the future of the Dead Sea, including a sea canal from the Mediterranean Sea, a sea canal from the Red Sea, restoring potable water inflow by returning a significant portion of the natural water sources, as well as checking the Default Choice - on the assumption that the current situation persists.

At a later stage the Jordanian government initiated the evaluation of the alternative of a canal from the Red Sea to the Dead Sea. The pilot project is being financed by the

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<sup>34</sup> Chapter 7, Section 22 of the Arrangements for the State Economy Law (Legislative Amendments to Attain Budget Goals and Economic Policy for 2002), 5732-2002, and the Arrangements for the State Economy Regulations (Legislative Amendments to Attain Budget Goals and Economic Policy for 2002) (Tools for Financing Protections for the Dead Sea Shoreline), 5732-2002.

<sup>35</sup> The response to the High Court of Justice was given by the State prior to the government decision of December 24, 2006 referred to above.

<sup>36</sup> Policy Paper for the Future of the Dead Sea, March 2004

World Bank. To the best of ICL Fertilizers' knowledge, the World Bank prepared a document whose purpose is to define the tests needed to be performed prior to reaching a decision. The pilot project is being led by an oversight committee with members from Jordan, the Palestinian Authority, Israel and the World Bank.

According to Articles in the press, it has been resolved that in a few months, the process of choosing the companies that will perform the feasibility and environmental impact studies will commence. The testing process will take about two years, and an affirmative decision regarding the project will require the consent of all of the member countries (Israel, Jordan and the Palestinian Authority). DSW is unable to determine how probable implementation of the project will be.

A drop in the water level means that the Company is required to draw the water from a greater depth, which requires investment and increased electricity expenses for DSW. According to the Default Choice Report, it is estimated that even if it will be decided to build a Sea Canal, it will take at least 15 years for its construction to be completed.<sup>37</sup>

Bringing water from the Red Sea or the Mediterranean Sea would impact the constitution of the water in the Dead Sea and the level of evaporation, and therefore the quantity of raw materials that can be produced in the Dead Sea Works' evaporation ponds. It is projected that bringing water from the Red Sea or the Mediterranean Sea would cause a layer of light, low-mineral water to float on the upper level of the sea, the creation of gypsum and development of microorganisms.

The strength of this impact, if any, is dependant upon a number of variables such as – the type of water that would be brought, the annual quantity, the future water level, and rate of precipitation of the gypsum and the creation of the microorganisms. Today, before these impacts have been scientifically investigated, it is difficult to establish the impact of the Sea Canal on production in the evaporation ponds as well as the other environmental impacts in the Dead Sea area.

I. Limits on Cadmium in phosphate fertilizers

Phosphate rock, which ICL mines, contains cadmium in various concentrations. Cadmium is considered to have a deleterious effect on the environment. Most countries to which ICL sells phosphate fertilizers do not presently limit quantities of cadmium in fertilizer. The European Union has been conducting, for some time, a series of public hearings prior to enacting regulations, limiting the maximum concentration of cadmium permitted in phosphate fertilizers anywhere within the countries that are European Union members. According to a published draft of these regulations, the regulations, if imposed, would come into effect gradually over a period of five to fifteen years. A number of European countries have already imposed limits on quantities of cadmium in fertilizer. However, these cadmium limitations generally do not currently prohibit sales of phosphate fertilizers containing cadmium above such limits. Instead, they require payment of a penalty for selling nonconforming products. Some of ICL Fertilizers' fertilizer products exceed these cadmium limits. ICL Fertilizers intends to adapt its use of raw materials in fertilizer production to concentrations that will comply with the cadmium limits imposed by the proposed European Union regulations.<sup>38</sup>

J. Law Regarding European Chemical Registration (The REACH Directive)

A statute covering the framework for licensing and evaluation of chemicals in the European Union (known as "REACH") was approved by the European Parliament and the Council of Ministers in December 2006, and shall come into force as of June 1, 2007. The statute applies to chemicals already on the market, as well as to new chemicals. Pursuant to this legislation, manufacturers on the common market and importers of chemicals or of chemicals that are contained in certain products shall be required to submit dossiers contain detailed information of every substance or chemical compound manufactured or imported into Europe, in quantities of more than one ton per

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<sup>37</sup> A drop in water level of 15-20 additional meters, is therefore the minimum projection. This is because of the timetable required to understand environmental implications, and collect data, for project planning and approval (specific to a multi-lateral project), raising funds and realizing the broad range of activities required by this matter." The Default Choice Report, page 4.

<sup>38</sup> The information contained in this section includes forward-looking statements. The information is based on the Company's plans and is subject to the results of decisions made by these countries.

year (the amount and content of the information depends on the volume of production and/or sales in Europe, and the nature of the product in terms of its effect on health and the environment). Some of the products will undergo risk evaluation based on the information that is submitted, and others will only be able to be sold in the future under an appropriate permit. Such a permit will only be granted on the basis of quantified evidence relating to management of the product with regard to health and environmental aspects, the lack of appropriate alternatives, and a socio-economic evaluation. For certain enduring, environmentally toxic substances, the permit will only be granted on the basis of a socio-economic evaluation and on condition that an alternative development plan is submitted, in order to encourage a transition to use of less hazardous substance.

The statute will be implemented gradually, between 2007 and 2022, under the supervision of the new European Chemicals Agency (ECHA), which is expected to commence work in 2008.

Implementation of REACH will cause ICL additional costs in the field of licensing, control and implementation of product stewardship programs with customers, and might increase the prices of raw materials. Another possible risk caused by REACH legislation is reduction in usage of a product / material, or removal of certain products from the European market. Likewise, there will be products and compounds that require investment in alternative research and development due to the need to remove certain components from use in the European market. ICL Fertilizers is preparing to implement the provisions of this statute.

#### **4.1.16 Legal proceedings**

##### **A. Pending proceedings regarding the Kishon River**

- 1) The production site of Fertilizers and Chemical Materials Ltd., a company in the ICL Fertilizers segment (hereinafter “**F&C**”) borders the Kishon River. For decades F&C along with many other entities, municipalities and plants, has diverted wastewater to the Kishon River.
- 2) On May 29, 2001, a class action was filed against F&C and other defendants, in Magistrates Court in Haifa under the Prevention of Environmental Nuisances Law (Civil Actions) (1992). The State of Israel and dozens of plants were joined to the action as third-party defendants. The action claims that the defendants polluted the Kishon River. The plaintiffs asked the court to order the defendants to cease the pollution of the Kishon River and to restore the Kishon River to the state it was in prior to the discharge of the waste. F&C, other defendants, the Kishon River Authority and the State of Israel filed a motion for dismissal of the action, on the grounds, among other things, that the State and other defendants have taken, and presently take, steps to remove and prevent environmental hazards, that the currently diverted wastewater is not polluted, and that on these grounds there is no basis for a class action under the abovementioned law. These motions to dismiss have been heard but no ruling has yet been issued.

The vast majority of the causes of action raised in the claim have not yet been brought before the Supreme Court for resolution. Nevertheless, with regard to the abovementioned action, the Company believes, based on the opinion of its legal counsel, that it has good defenses to these claims and therefore it has not included a reserve in its financial statements.

- 3) Between 2001 and 2005, seven lawsuits were filed against F&C and eight additional defendants (including the State of Israel) in Haifa District Court by 50 individuals (or their heirs or dependants), most of them fishermen who had worked, according to the claims, in the Kishon’s fishing harbor. The plaintiffs claim that the diversion of wastewater into the Kishon caused them to suffer from cancer (and other diseases). Dozens of plants and government entities were also joined as third-party defendants to these lawsuits. Because these claims are for physical injury, the plaintiffs are not required to quantify the amounts sought as damages. Nine of the claims have been set aside by consent and therefore the damages claimed are NIS 138 million (and an additional NIS 3 million for pending claims which overlap the principal damage) as of the date the claims were filed, in addition to interest and index-linkage differentials from the date of the disease or of the date of filing of the claim, as well as punitive damages, expenses for treatments and

third party assistance which, to a small extent, have not been quantified, attorneys' fees and costs.

As of the date of this Report, these cases are in the stages hearing evidence. First, the court is deliberating the question of the causative relationship in the narrow sense, meaning the connection between the substances alleged to have been in the fishing harbor and the plaintiffs' injuries. These actions involve highly complex fact patterns spanning decades and involving over one hundred parties (plaintiffs, defendants and third parties), and constitute a precedent-setting case, both in terms of the nature of the claim and the division of responsibility among the defendants and third parties.

It can be said, with the necessary caution and subject to the abovementioned information, that F&C has good defenses to these claims, based on expert opinions presented by F&C and other defendants. These defenses include: (a) a higher cancer rate is not apparent among the fishermen, (b) most of their ailments can be attributed to personal risk factors (primarily the fact that over 90% of the plaintiffs are smokers) as well as natural illness, and (c) the circumstances of the claimed exposure are not known to cause the plaintiffs' diseases.

Notwithstanding the foregoing, in accordance with the evaluation of its legal advisors, and in light of the factual and legal complexity of these proceedings, the initial stage in which they are pending, and the multitude of parties involved, the Company cannot estimate its exposure with regard to these claims and no reserve has been included in the financial statements.

- 4) In April, June and July 2004, three lawsuits were filed against four defendants in Haifa District Court by 93 former soldiers (as well as heirs and dependants). The plaintiffs combined with an earlier claim by a former soldier and his wife, claiming that contact with toxic substances in the Kishon River caused them severe physical injury. The soldiers claim total damages (in the nominal sum, as at the date of submission of the claim) of approximately NIS 268 million (approximately \$64 million) as quantifiable special/general damages, approximately NIS 84 million in dependant damages (approximately \$20 million, some of which overlap with the special damages), and NIS 141 million (approximately \$33 million) in punitive damages (all of these amounts are as at the date of submission of the lawsuit), other primary damages not quantified in the claim (including loss of future livelihood, medical expenses, in some cases loss of salary for years lost from work, etc., since the claims are claims for personal injury, the plaintiffs are not required to provide a precise quantification the entire sum claimed), and interest and linkage differentials, attorneys' fees and costs. The defendants joined third parties including F&C as well as dozens of plants and government entities, including the State of Israel. As at the date of this report, one of the plaintiffs has revoked his claim (in the sum of NIS 7 million) which was set aside by consent, and 12 others have given notice to the court that they are considering withdrawing their claims.

These cases are in the initial hearing stages. Consequently, the factual information regarding the plaintiffs and the nature of their alleged exposure is mostly not known to the defendants and third-party defendants, including F&C. These actions involve highly complex fact patterns spanning decades and involving hundreds of parties (plaintiffs, defendants and third parties), and constitute a precedent-setting proceeding, both in terms of the nature of the claim and the division of responsibility among the defendants and third parties. It is likely, with the necessary caution and subject to the abovementioned information, that some of F&C's defenses to the claims described in sub-section 3 above will also serve to defend F&C with regard to these claims. Notwithstanding the foregoing, in accordance with the evaluation of its legal advisors, and in light of the factual and legal complexity of these proceedings, the initial stage in which they are pending, and the multitude of parties involved, the Company cannot estimate its exposure with regard to these claims and no reserve has been included in the financial statements.

In 2004, a lawsuit was filed against defendants including F&C by Israel Shipyards claiming that direct and indirect corrosion damage had been caused to its floating dock and its locks by the Kishon River's waters, in the nominal sum of approximately NIS 21 million. In 2006, the statement of claim was amended in light of the fact that the floating dock had been sold, and the sum of the claim was reduced to a nominal sum of approximately NIS 20 million. In these claims notices

of third-party defendants were served on additional parties. F&C claimed that it acted in accordance with appropriate permits issued by the authorized agencies and that the substances it diverted into the Kishon did not cause the alleged damage. The Company believes, based on the opinion of its legal counsel, that it has good defenses to these claims. Therefore no reserve has been included in the financial statements.

B. Soil and ground water pollution – Spain

In February 2004 a consolidated company of ICL was informed that a Prosecutor of Environmental Crimes of in Catalonia, Spain, instituted a criminal proceeding in which it filed a brief in the Magistrate's Court in Messarat, Spain, against the former and current managers of an ICL Fertilizers company that operates mines in Spain, claiming that the managers violated local legislation and caused groundwater contamination due to seepage of salt waste from the salt mounds which have been a by-product of the potash plants over many years, in part before ICL Fertilizers acquired the company. The court has also been asked to issue an order prohibiting further salt waste dumping. If this request is granted, the Company will not be able to continue to produce potash at this facility until the problem is solved. As of the date of this report, no such order had been issued. ICL Fertilizers believes, based of legal opinion and counsel, that the probability of this order being issued at this stage is low.

ICL Fertilizers has two potash production facilities in Spain. During the potash production process salt is produced which is stored in piles. There is no use for most of the salt. ICL Fertilizers is required from time to time to obtain permits to create these piles. The ICL fertilizers plant in Sallent has a permit to pile salts which will suffice, according to current storage methods and production rates, for approximately an additional year of production. ICL Fertilizers is working to receive a permit for expanding the dumping area for the salt. If this permit is not received, it may limit the quantities that may be produced at that facility in the future.

**4.1.17 Goals and business strategy**<sup>39</sup>

A. ICL Fertilizers' strategy is intertwined with the trends in the field of fertilizers and includes the following elements:

- 1) Expansion of potash production capacity in order to take advantage of the inherent advantages of this market and to participate in this market's growth.
- 2) Broadening production of downstream products based on phosphate rock, while utilizing existing infrastructure and improving utilization of the current plants.
- 3) Development of the specialty fertilizers field and expansion of its product offering, primarily in the area of soluble fertilizers, while developing new and innovative products and starting to produce products that are not currently products of ICL Fertilizers.
- 4) Constant improvement of product quality.

B. Principal projects planned or undertaken by the Corporation

- 1). The Company is continuing with a project to expand potash production capacity in its raw materials system in Sodom, which began in 2005, and it intends to expand the production capacity of its facilities in Sodom as well.
- 2) During the year, the project to adapt the phosphate rock and downstream product production systems to the existing phosphate rocks found in the phosphate mines in Israel was completed.
- 3) ICL Fertilizers today operates a power plant for producing electricity in Sodom, and purchases electricity from the Israel Electric Co.

On October 24, 2004 the Dead Sea Works, a division of ICL Fertilizers, received approval in principle from the Minister of National Infrastructure for grant of a license to produce electricity with power and heat plants (co-generation) with total

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<sup>39</sup> ICL Fertilizers' plans and strategies, as described in this section 4.1.16, reflect the strategies of ICL Fertilizers as of the date of this report, and are forward-looking statements and are based on ICL Fertilizers' projections. These plans and projections may change, in whole or in part, from time to time. There can be no certainty regarding the accomplishment of these plans or the success of these strategies.

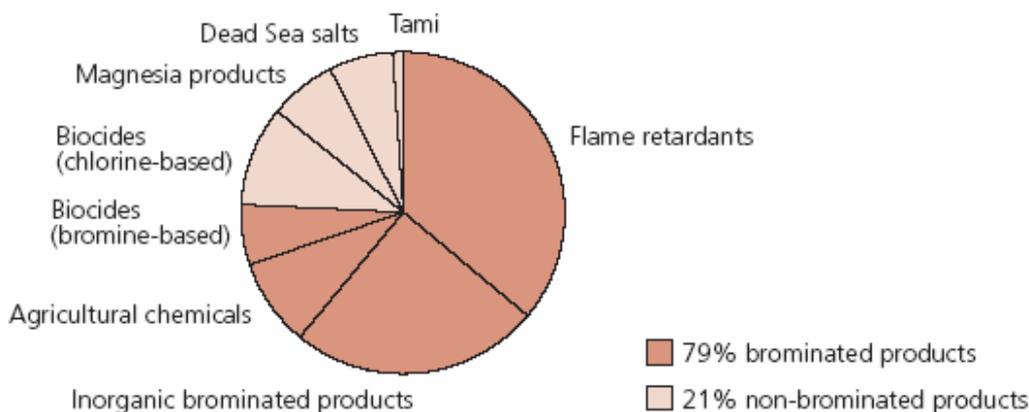
production of between 400 and 700 megawatts. On August 31, 2006, DSW received a production license as aforesaid. The license is conditional upon DSW's compliance with a series of milestones. On February 28, 2007, DSW gave notice that it wishes, at this stage, to receive a license for a 400 megawatt station. Beyond that, up to 700 megawatts, there is not yet any solution regarding infrastructure for transmission of electricity from Sodom to the center of the country, and such a solution is not expected to come into being in the coming years. Therefore, at this stage, the size of the station has been set at a maximum of 400 megawatts.

- 4) During the course of the year, CPL purchased new, cheaper technology for transporting the ore in the mining process in its mines in England. Initially, a single machine was purchased which is being used for experimentation and as a pilot. If the technology is proven to be successful, other machines of the same kind might also be purchased.

## 4.2 ICL Industrial Products

The following chart details the external sales<sup>40</sup> of the industrial products business segment according to product:

External sales for 2006 – \$ 827 million



### 4.2.1 General information regarding ICL Industrial Products

- A. ICL's Industrial Products segment develops, manufactures markets and sells industrial products, principally based upon bromine, magnesia, chlorine and salts from the Dead Sea. In 2006, the net sales of the Industrial Products segment (including sales to other companies in the Company) totaled approximately \$838 million, representing approximately 24% (including sales to other segments of the Company), of ICL's total net sales for that year. Flame retardants, brominated products for industrial and agricultural uses and clear brines based on bromine for the oil and gas drilling industries represent a majority of the sales of this segment. Other products include biocides based on bromine and chlorine for water treatment, products based on magnesia (magnesium oxide), and products based on the Dead Sea salts. During 2006, ICL Industrial Products used internally approximately 80% of its annual elemental bromine production and sold the remainder in global markets.

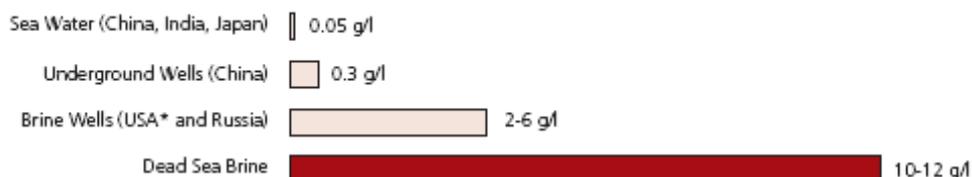
ICL Industrial Products' major manufacturing facilities are located in Israel in Sodom (production of bromine, Dead Sea salts and bromine compounds), in Ramat Hovav (production of bromine compounds) and in Mishor Rotem (magnesia production) in Terneuzen, Holland (production of bromine compounds), in the United States in West Virginia (production of chlorine-based biocides), in China through a joint venture in Liang Yong Yang (production of bromine compounds) and a joint venture in ShanDong (production of bromine compounds), and near Calais, France (production of specialty magnesia products and calcium compounds used as raw materials in health foods) – as shown in the chart below: .

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<sup>40</sup> The term "external sales" refers to the segment's sales to customers outside of the ICL Group (customers that are not other segments of ICL).



B. Bromine is an element from the halogen family known for its variety of uses in many industries. Bromine is a heavy, volatile, toxic, and corrosive liquid element with a sharp odor and reddish-brown hue. Bromine is used in the production of a range of bromine compounds. Bromine is found naturally in sea water, underground brine deposits and the Dead Sea. Its concentration varies depending upon its source. The Dead Sea is the source of the most highly-concentrated bromine<sup>41</sup>.



\* Arkansas – brine wells of Chemtura & Albemarle

Source: ICL Estimates

\*\* For a description of the process of bromine extraction from Dead Sea brine see section 4.2.12(1) below.

The feasibility of extracting bromine is the result of a number of considerations: finding a suitable bromine source; the bromine's concentration; availability of chlorine, which serves as a primary raw material in bromine's production; availability of suitable production technologies and special means of transportation of bromine and/or bromine compound production equipment that is able to take in the manufactured bromine.

The process for extracting bromine depends on the nature of its source and its concentration. The lower the concentration of bromine in the brines, the harder and more expensive it is to extract.

Most of the bromine produced worldwide is used as raw material for compounds with a wide range of uses.

C. The primary uses of ICL Industrial Products' products:

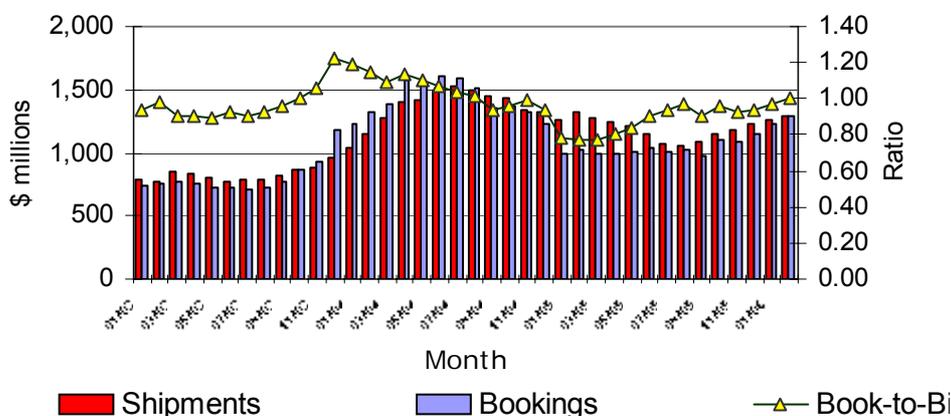
1) **Flame retardants** are used in many areas of the plastics and electronics industries, primarily for printed circuit boards in the electronics industry, electronic cables and plastic housings of electronic equipment. In addition, flame retardants are increasingly being used in the automotive, construction, furniture and textile industries. In the next few years, use of flame retardants is projected to rise along

<sup>41</sup> The information in this graph is based on the Company's internal estimates.

with the growth in the electronics industry and widening requirements and standards for flame retardants in additional fields.<sup>42</sup>

Below are details the book to bill ratio of semiconductors over recent years:

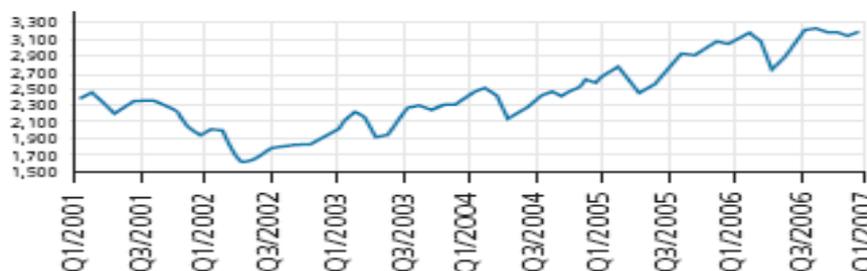
### Semiconductors Equipment Book to Bill Ratio (3 months average, %, \$billions)



Source: Semiconductors Trade Association

- 2) **Heavy drilling liquids** based on bromine (hereinafter “**clear brines**”) are used to balance pressure at a certain stage in drilling of oil and gas wells with high operating pressures. Use of these bromine-based clear brines around the world is growing due to the increase in oil and gas drilling in various parts of the world, including in new oil fields, such as in Western Africa and the former Soviet Union.

The following chart shows the number of oil drilling rigs operating in the world over time:



Source: Baker Hughes

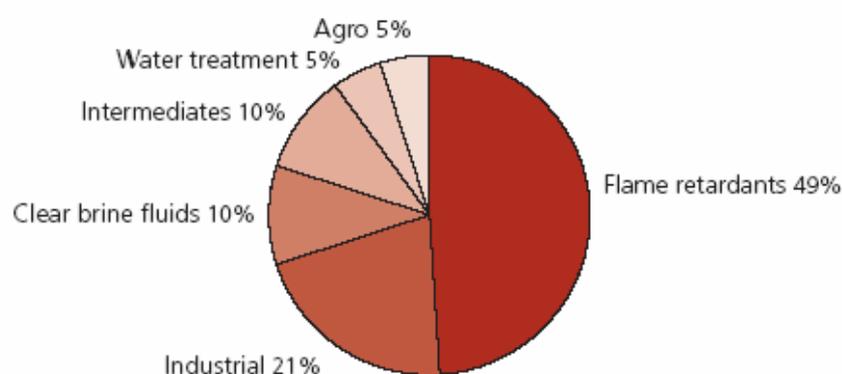
- 3) **Soil and space fumigation products**, primarily **methyl bromide** which is used for soil fumigation and acts mainly against nematodes (microscopic roundworms) and soil fungus that damage plant roots. In addition, methyl bromide is used in space fumigation against agents that damage stored produce, primarily in dry agricultural produce. It should be noted that since 1995 limitations have been enacted on the use of methyl bromide (which is suspected of damaging the ozone layer) and quantities used for soil fumigation are decreasing. Regarding the limitations on methyl bromide see section 4.2.16(a)(3) below. ICL Industrial Products intends to try to remain active in

<sup>42</sup> Projections regarding the projected growth in use of flame retardants constitute forward-looking statements, and are based on the Company's projections regarding the growth of the electronics industry and on the Company's evaluations regarding the ramifications of current and pending regulation in various countries regarding required use of flame retardants. The realization of these estimates cannot be certain. If these markets do not grow, or regulatory trends change, materially different results than those stated above may occur.

the field of soil fumigation products by offering a new product that is under development. In addition, ICL Industrial Products will continue to sell methyl bromide for other applications where production and sales quantities are not limited, as well as for “critical uses” in soil fumigation as determined from time to time.

- 4) **Bromine- and chlorine-based biocides** are used primarily for various types of water treatment. Use of these products has grown annually, driven by increased pollution of worldwide water sources and adoption of environmental regulations for purifying and disinfecting sewage. Bromine- and chlorine-based biocides produced by ICL Industrial Products are used in swimming pool and spa water treatment, cooling towers, paper production systems (patented) and the cleaning and sanitizing markets.
- 5) **Calcined and specialty magnesia products** are used in various industries, primarily in the transformer industry, rubber, and as a mineral supplement in pharmaceutical and food products. In the past, the Company manufactured sintered magnesia, which it sold as a raw material for the production of refractory bricks and other shaped parts that line kilns used in the manufacture of steel. Due to the competition from China in the area of sintered magnesia, ICL Industrial Products has ceased manufacturing this product and instead is focusing on the manufacture and sale of calcined and specialty magnesia products.
- 6) **Products based on chlorine from the Dead Sea** include primarily magnesium chloride (flakes and pellets), used for de-icing roads and dust control on dirt roads, as well as in the textile and cosmetics industries. ICL Industrial Products manufactures a wide range of types of sodium chloride (common salt) used for food, as salt for water softening, electrolysis for the electrochemical industry, de-icing roads and other uses. Additional products include anhydrous aluminum chloride, used primarily as a catalyst in the organic chemical industry, and pure potash, which is high-quality potash used for metal coating processes and in the food and pharmaceutical industries.

#### Worldwide Uses for Bromine Compounds in 2006



Source: Estimates of ICL

#### D. General Business Environment and Influence of External Factors

The bromine market is affected by the level of activity in the electronics and oil drilling industries, as well as limitations on use of methyl bromide, as a result of the enactment of the Montreal Protocol (see section 4.2.16 below). 2006 was characterized by strong demand for flame retardants during the first half of the year, and reduced demand as of the third quarter of the year. In addition, there was an increase in TBBA production (the largest Bromine-based flame retardant) in China. The trend of decreasing methyl bromide sales continued due to the limitations imposed by the Montreal Protocol.

On the other hand, there was an increase in demand in the market for chemicals used in oil drilling resulting from increased oil prices which gave rise to increased drilling operations. Despite the decrease in quantities sold of some of these products, compared with 2005 sales, which were mainly a result of a change in the Company's customer mix, increases in selling prices of most of the products sold by ICL Industrial

Products brought about an overall increase in revenues for 2006. In 2006, the average sale prices of the products sold on the market for chemicals used in oil drilling increased as a result of termination of a long-term contract with low prices, at the end of 2005. At the same time, there was a decrease in sales quantities of clear brines for oil drilling because contracts with two large customers were not renewed.

Along with the increase in selling prices noted above, however, the prices of a portion of the raw materials used by ICL Industrial Products in its production processes have also risen in parallel. During 2006, the price of energy also rose, impacting the segment's production costs and specifically the cost of producing magnesia-based products.

In 2006, profitability improved in the area of bromine- and chlorine-based biocides for water treatment. In the area of chlorine-based biocides, ICL Industrial Products benefited from penetration to new customers who are closer to the end user. In bromine based biocides, ICL Industrial Products benefited from the increased growth of "Fuzzicide," (this biocide is a unique product for this segment, based on bromine and used for the treatment of water for paper factories). Sales of Fuzzicide also increased in 2006. This is due to the product's innovation and efficiency, making it possible to use it more efficiently and cost-effectively than other products.

ICL Industrial Products' products are exposed to competition (for details regarding competition see section 4.2.7 below) and are subject to restrictions in various countries (for details on these restrictions see section 4.2.16). ICL Industrial Products' facilities operate in accordance with environmental protection regulations in their various countries (for details regarding environmental matters see section 4.2.14 below).

#### 4.2.2 **Products and services**

The following are the main product categories of ICL Industrial Products:

<b>Principal Products</b>	<b>Primary Applications</b>	<b>Primary End Markets</b>
Brominated Flame Retardants	Flame retardant plastic additives	Printed circuits, thermoplastics, engineering polymers, textiles, foams and rubber
Magnesium - Hydroxide Flame Retardants	Plastic additives	Cables and additional uses in the plastics industry
Elemental Bromine	Raw Material for Industry	Pharmaceutical and rubber industries, Bromine compounds producers and oxidants
Inorganic Bromine Compounds	Photographic paper and film, oxidizing agents, chemical intermediates, and oil and gas field fluids	Photography, oil and gas drilling and textiles
Organic Bromine Compounds	Insecticides, solvents for chemical synthesis and chemical intermediates	Pharmaceutical, Agrochemical, rubber and dyes
Soil and Space Fumigation	Applied to soil and space for pest and disease control	Agriculture, space and quarantine fumigation
Chlorinated and Brominated Biocides for Water Treatment	Chemicals for disinfection and sanitizing drinking water, industrial water and sewage	Pools, spa, cooling towers, industrial water treatments, cleaners and sanitizers and paper plants
Calcined and Specialty Magnesia	Magnesia compounds, vulcanization control, transformer steel, antacid medication, mineral supplements in food and pharmaceutical products	Chemical, rubber, adhesives, food, nutrient-enhanced products, and pharmaceuticals
Dead Sea salts	De-icing and dust control on dirt roads, food industry, chlorine production, cosmetics and catalysts	Municipalities and households, food preservation, water softening, cosmetics and the chemical industry

#### 4.2.3 Detail of sales and profitability of products and services

The following is an analysis of the revenue and gross profit according to product:

	Revenues (\$ million)*	% of ICL Revenues*	Gross profit (\$ million)	Gross profit (% of revenues)
2006	837.8	23.9	356.4	42.5
2005	805.5	24.8	299.8	37.2
2004	706.5	24.1	205.7	29.1

\* For purposes of this table, revenue figures for the product group and for ICL used in calculation of percentage figures include revenue among business segments.

#### 4.2.4 New products

ICL Industrial Products is involved in the development of innovative products in its areas of activity and discovery of new applications for existing products. During the period of this report, ICL Industrial Products spent about \$13 million on new product development and support and improvement of existing manufacturing processes.

#### 4.2.5 Customers

##### A. Dependence on single customer

ICL Industrial Products does not have any single customer that accounted for more than 10% of the total sales of ICL.

##### B. Breakdown of sales according to geographical market

	1-12/2006		1-12/2005		1-12/2004	
	\$ millions	%	\$ millions	%	\$ millions	%
<b>Israel</b>	42	5%	40	5%	36	5%
<b>North America</b>	258	31%	211	27%	193	28%
<b>South America</b>	17	2%	15	2%	13	2%
<b>Europe</b>	237	29%	232	29%	200	29%
<b>Asia</b>	256	31%	272	34%	238	34%
<b>Rest of the world</b>	17	2%	24	3%	17	2%

##### C. Developments that occurred in the geographical areas

In 2006 ICL Industrial Products' sales grew in North America, mainly as a result of biocide sales. The downturn in Asia stems mainly as a result of a reduction in sales of bromine in China.

#### 4.2.6 Marketing and distribution

ICL Industrial Products' primary markets are Western Europe, the United States, China, Japan and Taiwan. ICL Industrial Products sells its products primarily through a network of sales offices, agents and distributors throughout the world. Most of ICL Industrial Products' sales are not transacted by means of long-term contracts or orders, but rather via current orders close to the date of supply. Consequently, the concept of a backlog has no meaning for ICL Industrial Products.

In addition, ICL Industrial Products has framework agreements with specific customers, through which the customer can purchase up to previously-agreed maximum quantities of product during the term, on the basis of which the customer issues purchase orders to ICL Industrial Products from time to time.

#### 4.2.7 Competition

##### A. Conditions of competition in the industrial products segment and primary competitors

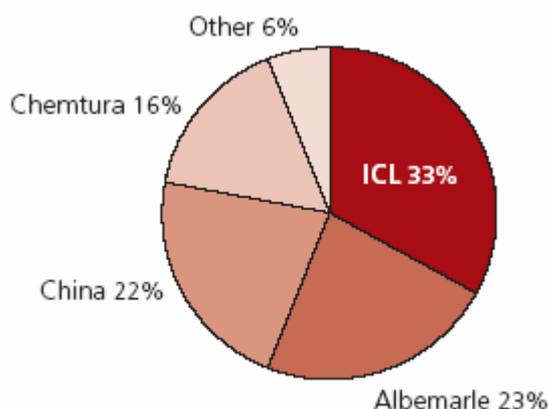
ICL Industrial Products is the world's leading producer of elemental bromine, accounting for approximately one-third of world output. ICL Industrial Products estimates that in 2006 it, together with its two main competitors, Chemtura Corporation (hereinafter

“Chemtura”) (which is the result of the merger in 2005 of Great Lakes Chemicals Corp. and Crompton)<sup>43</sup> and Albemarle Corporation (hereinafter “Albemarle”), accounted for approximately 75% of the worldwide production of bromine and approximately 70% of the production of bromine compounds. Chemtura and Albemarle produce bromine primarily from underground brine sources in the U.S. Albemarle also has a joint venture with a Jordanian company to produce bromine and bromine compounds. This joint venture that started operations in November 2002 is located on the Jordanian side of the Dead Sea that has access to the same source of raw materials that ICL Industrial Products has. Chemtura purchases bromine and bromine compounds from ICL Industrial Products under long-term contracts. Prior to 2006, Albemarle also purchased bromine under a long-term agreement for one of its facilities. The facility, including the bromine purchase agreement, was recently sold by Albemarle.

It should be noted that the Dead Sea is a source of relatively low-cost bromine and that the supply of these bromine raw materials from the Dead Sea is, for all practical purposes, unlimited.

ICL Industrial Products has a market-leading position in the fields of biocides, magnesia and other salts, with regard to certain niche products.

#### Production capacity of bromine manufacturers in 2006



(1)

Sources: ICL projections, US Bureau of Mines, Arkansas Oil & Gas Commission publications

#### B. Approach for tackling competition

Its relatively low production cost of bromine affords ICL Industrial Products a competitive advantage. Bromine production requires a complex logistical system based on a fleet of special containers (isotanks) specifically designed to transport bromine. One of the advantages of ICL Industrial Products is having the largest fleet of isotanks in the world, which enables it to transport relatively large quantities of bromine around the world. A widespread worldwide marketing network and a range of high-quality products, combined with a technical support system that works closely with customers afford ICL Industrial Products a good competitive position in its markets. In China, for example, ICL Industrial Products’ network includes two production facilities in partnership with local manufacturers, a bromine containers farm, and sales and technical support networks. In Holland ICL Industrial Products has a bromine compound production facility, which gives it a competitive advantage in Europe.

In the field of bromine compounds, competition is characterized by offering higher quality products, and better customer service and support. ICL Industrial Products has long-term relationships with its customers.

#### 4.2.8 Seasonality

ICL Industrial Products operations are not characterized by regular seasonal fluctuations. However, amounts sold of some of its products fluctuate between the various seasons.

<sup>43</sup> In 2005 Great Lakes merged with Crompton, a U.S. company, to form Chemtura, a corporation that operates in the fields of plastics and fuel additives, water treatment chemicals and agricultural products. Chemtura is a leading company in the field of plastics additives.

Agricultural products are characterized by relatively high sales in the second and third quarters. Biocides for swimming pools are characterized by relatively lower sales in the fourth quarter. Salts for de-icing are characterized by relatively higher sales in the first and fourth quarters. The net impact of these diverse seasonal differences on ICL Industrial Products is insignificant.

#### **4.2.9 Production capacity**

ICL Industrial Products' potential production capacity is based on the various plants' nominal hourly output multiplied by the potential operation hours in a given year.

The potential production capacity for bromine is approximately 240,000 tons. ICL Industrial Products is in the process of expanding the potential production capacity of its bromine facilities in Sodom. In 2008, further expansion of the bromine production facilities in Sodom are expected to be completed, which will increase production capacity to 280,000 tons. The potential annual production capacity for bromine compounds is 300,000 tons. Regarding bromine compounds, in some of its facilities ICL Industrial Products produces more than one product. Therefore, production capacity is dependant upon the range of products produced by each plant from time to time. In 2006, the Company manufactured 179,000 tons of bromine and 246,000 tons of bromine compounds.

The production capacity for chlorine-based biocides is approximately 30,000 tons. Annual production in 2006 was 30,000 tons.

#### **4.2.10 Research and development**

##### **A. Research and development activities and results**

The principal research and development activities conducted by ICL Performance Products during the period of this report are as follows:

- 1) Development of innovative products in the Company's main areas of activity.
- 2) Searching for new uses for existing products.
- 3) Improving product quality and lowering production costs by changing and improving processes.
- 4) Ecologic research for improvement of the wastewater treatment system, reduction of airborne emissions and solid waste.
- 5) Research in the area of construction materials in order to overcome problems of accelerated wear and tear of building materials, corrosion prevention, equipment adaptation, and tests in accelerated aging.

##### **B. Investment in research and development**

ICL Industrial Products' total research and development expenses for the period of this report were approximately \$13 million, for which approximately \$0.5 million was received in grants. For information on the repayment of these grants, see notes 18(a)(5) and 21B in the Company's financial statements.

#### **4.2.11 Intangible assets – Patents and trademarks**

ICL Industrial Products believes that protecting its intellectual property is a cornerstone of protecting and developing its business activities. Its intellectual property is an asset that ICL Industrial Products manages in an active and ongoing manner.

Over the years, ICL Industrial Products has, in various countries, approximately 152 registered patents and an additional approximately 118 patent applications that are in various stages of evaluation throughout the world. As of December 31, 2006 these patents protect a relatively small portion of ICL Industrial Products' products.

During 2006, 30 patent applications by ICL Industrial Products were granted.

#### **4.2.12 Raw materials and suppliers**

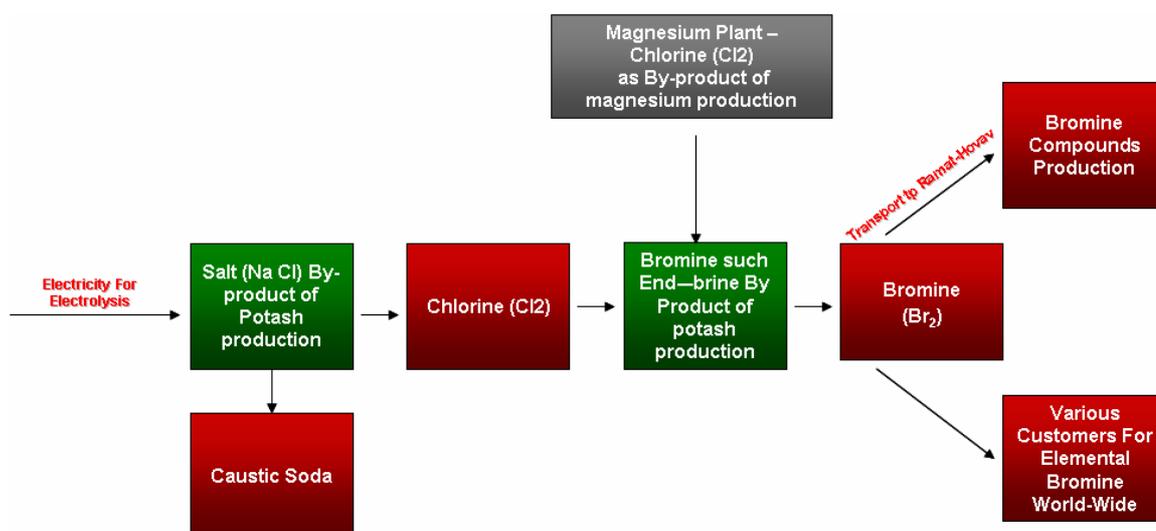
The following describes the principal raw materials used by the industrial products segment for production of its products:

#### A. Bromine and its compounds

Elemental bromine is produced from the end brines (salt solutions) that result from the processes carried out to produce potash from carnallite. The brine is pumped to ICL Industrial Products' plant in Sodom, where bromine is produced in an oxidation process using chlorine.

The chlorine is produced by electrolysis of sodium chloride and as a by-product of the magnesium production process of ICL Metallurgy. The electrolysis facility and the magnesium plant are located next to the bromine facility in Sodom. The sodium chloride used in the electrolysis process is a by-product of the potash production in Sodom.

ICL Industrial Products uses elemental bromine to manufacture bromine compounds at its facilities in Israel, the Netherlands and China. ICL Industrial Products sells the balance of its elemental bromine to third parties. Most bromine compounds are manufactured by chemical processes involving bromine together with a range of other raw materials, of which the most important are Bisphenol A, used to manufacture the flame retardant TBBA.



#### B. Magnesia

Some of the brine that remains after the production of potash is rich in magnesium chloride. This brine is pumped to ICL Industrial Products' facilities at Mishor Rotem in the Negev Desert. At these facilities, in a process utilizing magnesium chloride and other materials, magnesia (magnesium oxide) is produced. The magnesia is further processed into several grades of magnesia.

#### C. Chlorine-based biocides

ICL Industrial Products produces these products at its facilities in the United States. For production of chlorine-based disinfection products, (biocides), ICL Industrial Products purchases chlorine, urea and caustic soda from local manufacturers.

#### D. Dead Sea salts

Dead Sea salts are manufactured at a facility in Sodom. The production starts from materials and brines produced as by-products of potash production. For example, magnesium chloride flakes are produced from brines rich in magnesium chloride that remain after potash is separated from carnallite. Various types of sodium chloride are also extracted from the salt that remains after potash is separated from carnallite.

### 4.2.13 Working capital

#### A. Raw material inventory policy

ICL Industrial Products itself produces the bromine used in its bromine compound production and also acquires a small amount of the bromine required for these compounds from China. It acquires the Dead Sea brines used as central raw materials in its production of bromine, magnesia and Dead Sea salts from ICL Fertilizers. Chlorine

is acquired from ICL Metallurgy and from ICL Industrial Products' chlorine facility. ICL Industrial Products also purchases raw materials from external suppliers, notably Bisphenol A and other chemicals required for production processes.

ICL Industrial Products maintains raw material inventories in quantities that take into account the projected level of production based on consumption characteristics, supply dates, distance from the supplier and other logistical considerations.

B. Finished product inventory policy

ICL Industrial Products' policy is to maintain adequate inventory to ensure orderly supply to customers in consideration of the customers' distance from production centers and their requirements for inventory availability, and in conjunction with optimization of the inventory's storage costs. Therefore, portions of finished product inventories are held in storage facilities in the destination countries.

C. Credit policies

ICL Industrial Products extends credit terms to its clients according to customary practices in their locations. The group's sales are generally covered by trade credit risk insurance or by letters of credit from banks with high credit ratings.

	December 31, 2006	
	Average credit level (\$ millions)	Average credit days
Customers*	87	38
Suppliers	74	50

\* Figures for customers' receivables and average days of credit exclude customers whose obligations have been sold through a securitization transaction as described in section 5.4.3 below and customers whose obligations have been discounted through other arrangements.

4.2.14 Environmental matters

A. General

During the past few years ICL Industrial Products has focused on research and engineering activities and projects to create new ecological systems and improve existing ones. In addition, under the auspices of the Board of Directors of the segment, a special committee of the Board of Directors for ecological and safety matters oversees ICL Industrial Products' activities regarding environmental quality and directs the segment's environmental policies. Likewise, ICL Industrial Products has an internal compliance program for environmental matters.

Under the framework of the Responsible Care program, ICL Industrial Products initiated the establishment of a public forum with representatives of the community and environmental groups three years ago. This is the first forum of its kind established in Israel and based on its success other similar forums have been established. In this forum, the Company presents with full transparency, public education is conducted and information is passed to the general public.

ICL Industrial Products runs a training program for employees on the topic of environmental matters in the various companies, in an effort to raise the Company's employees' awareness of and participation in matters of environmental matters. This activity includes targeted training for professional teams, focusing on employees on the production floor. In the framework of this training, courses for environmental protection trustees are conducted including environmental quality training in the training packages of the various units.

Below is a list of principal actions taken by ICL Industrial Products:

1. Air Quality

- Investments were made in the production facilities in order to improve recycling of solvents and other organic materials, and absorption via active charcoal, in order to achieve reduction of the amount of these materials emitted into the air.

- As a result of ICL Industrial Products' many activities regarding environmental quality, there was a significant reduction in 2006 in the amount of organic solvents emitted from the plants' stacks.
- Investment was made in monitoring and detection systems, in order to ascertain that there are no deviations in the plant's operation and emission systems. In addition, additional sensors were installed to detect bromine and chlorine leakage.
- The local Ramat Hovav Industrial Authority set up a number of stations to measure air quality throughout Ramat Hovav.
- For details on the system planned for collecting emissions from stacks, see item C below.

## 2. Wastewater

- ICL Industrial Products is in the process of running-in a new facility in Ramat Hovav for biological treatment of the facilities' wastewater, in which it has invested \$7 million.
- Biological wastewater treatment is the most prevalent technology for reducing organic degradable substances in wastewater. The biological treatment is done with micro-organisms that feed on the organic substances found in the wastewater and thereby cause them to substantially decrease in quantity. The process is limited to bio-degradable substances. (in this regard see section (b) below).
- ICL Industrial Products continued operations in 2006 on its production facility in order to reduce the amounts of organic and solid wastes in the wastewater, to separate the various wastewater streams and to achieve a general reduction in the amount of wastewater.
- Operation of a special laboratory for monitoring and analyzing wastewater quality was commenced.

## B. Material impact of rulings regarding environmental matters

1. In May 2004, plants in Ramat Hovav, including an ICL Industrial Products plant, received notice regarding changes in their business licenses with respect to treatment of waste water. Under the notice, each facility was required to move over to independent treatment, with the aim of reaching zero liquid waste in the future.

On October 10, 2004, all of the plants in Ramat Hovav, along with the Manufacturers' Association, filed an administrative appeal in the district court in Be'er Sheva against the Ministry of Environment to void the abovementioned requirements.

It was agreed, with the consent of the Court, that the dispute be referred to mediation. Following the mediation proceedings and opinions, the parties reached an agreement to the effect that the solution for waste removal at Ramat Hovav will continue to be by use of evaporation ponds and that the conditions of the business license will be amended accordingly. On December 14, 2006, a mediation agreement was signed between the Ministry for the Environment, the Manufacturers Association of Israel, facilities at Ramat Hovav (including ICL Industrial Products facilities) and Sustainable Development for the Negev (a Registered Association). The agreement was authorized by the District Court and was given the force of an order by consent on December 28, 2006, the conditions of which were incorporated in the business license for ICL Industrial Products' Ramat Hovav facilities. The updated conditions of the business license were transmitted to the facility on January 31, 2007. Under the agreement and the conditions of the license, treatment of wastewater (including removal) shall be the sole responsibility of each facility. Set-up of the biological treatment plant was to be completed by December 31, 2006, at which point operation of them would commence. Values for the wastewater leaving the treatment facilities were prescribed. As of the beginning of 2008, the pumping of wastewater into the Council's central treatment system will not be permitted. The wastewater from the facilities will be removed to the evaporation pools and reservoirs that are operated

and managed by the Council, until the end of 2009. After that date, independent removal systems will be operated under the management of each facility, and wastewater pumping into the current system shall be prohibited. Each facility is to meet the permanent wastewater values by no later than the beginning of 2010.

Pursuant to the new conditions of the license, the facilities submitted a plan for setting up an independent removal system, and for conducting a risk survey for the independent removal system including the sediment solids in it.

Under the agreement, the parties agreed to commence accelerated negotiations regarding air emissions both from new and existing facilities, as well as diffused emissions, and prevention of pollution and odor hazards, on the basis of international standards. The parties have commenced such negotiations.

2. Pursuant to the requirements of the Ministry of the Environment, which were sent to ICL Industrial Products as a draft of the Ramat Hovav business license on December 12, 2004, the facility must treat existing and future waste using one of the following processes: a thermal bromine recovery process, solid stabilization, or removal to suitable treatment facilities that exist outside of Israel. As at the date of this report, these conditions have not yet come into force. ICL has made a provision in its financial statements that it believes to be adequate for the removal of this historical waste. For details of the treatment facility for this waste see item C below.
3. In July 2004 an epidemiological study was published by Ben Gurion University, which was commissioned by the Ministry of Health, regarding disease and death rates from various diseases within a radius of 20 kilometers of Ramat Hovav (a chemical industrial zone with 17 plants, among them an ICL Industrial Products plant), compared to other areas outside this radius. According to the survey, in most cases no connection was found between disease and death rates and residence within or outside the radius of Ramat Hovav and residence downwind of the prevailing winds from the site. In some cases, the opposite relationship was found. Regarding some of the diseases that were tested in the survey, a higher rate of disease and death was found in towns closer to Ramat Hovav relative to the control group, while with regard to others, the rate of disease or death was actually lower relative to the control group. The study report notes that during the course of the study other factors among the population that may have been relevant with regard to disease or death were not investigated, and it therefore notes that it is not capable of establishing a causative relationship between proximity to Ramat Hovav and disease or death. In addition, the study did not check the airborne concentration of chemicals in any of the surveyed locations, and therefore it has no evidence to reach any specific conclusion regarding any of the plants in Ramat Hovav.

C. Future material capital expenditures for environmental matters

For years, ICL Industrial Products has invested in prevention of environmental harm.

During 2006, ICL Industrial Products invested a total of approximately \$10.4 million in the acquisition of property, plant and equipment for prevention of environmental harm and recorded approximately \$2 million as a current expense for waste removal and research on issues related to prevention of environmental harm.

In 2007, ICL Industrial Products expects to invest approximately \$20 million in property, plant and equipment and record approximately \$12 million as a current expense for similar purposes. Due to the escalation in environmental protection requirements, the scope of these expenses is expected not to decline in the years 2008 and onward. The following are the principal facilities which ICL Industrial Products intends to set up during 2008.<sup>44</sup>

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<sup>44</sup> Projections regarding the capital expenditures and expenses constitute forward-looking statements, and are based on legislation and regulation currently in effect, on governmental requirements known to ICL Industrial Products and on investment estimates made by Company engineers. The realization of these estimates cannot be certain. Any change in these estimates, including changes in the estimates made by the Company's engineers or changes in adoption of governmental requirements or legal rulings may cause different results than those stated above.

- ICL Industrial Products is currently designing a future facility for treatment both of historical waste and current waste. This facility will employ thermal breakdown of the waste, restoring bromine from it as HBR so that it can be recovered as a raw material. The facility is planned to be set up during 2008, subject to the receipt of building permits. The planned investment by ICL Industrial Products, upon an initial estimation, is around 25 million dollars.
- ICL Industrial Products is currently planning to collect emissions from the stacks of its facilities and to break down residual organic matter using catalytic oxidation technology. The system is designed to enable a reduction of approximately 99% in concentrations of the organic substances currently emitted. The system is planned to commence operation during the course of 2008, subject to the receipt of building permits. The planned investment by ICL Industrial Products, upon an initial estimation, is around 13 million dollars.

#### **4.2.15 Safety and health**

Some of ICL Industrial Products' products, as well as the raw materials and production processes, involve various levels of risks to persons who might be exposed to them. ICL Industrial Products must comply with the safety and health standards and requirements prescribed, in part, under local law, and in part under international and local standards. There is a trend towards updating these requirements and making them stricter, as a result of which, various investments might be required.

ICL Industrial Products is continually investing in safety measures, with the aim of preventing accidents and whilst continually taking care of employees in the segment, and persons in and around the facilities and products.

The board of directors of ICL Industrial Products, the safety committees in the segment and the committees that operate at the facilities, periodically examine safety achievements and events, and the extent to which targets set in light of ICL's safety policy are met. In 2006, the ICL Industrial Products' Safety Committee met 6 times. ICL Industrial Products has a compliance program in the field of safety, and has internal checking processes for ensuring compliance with requirements.

ICL Industrial Products is in advanced stages of implementation of the ISO 18001 Safety Management standard. As at the date of this report, the facilities at Ramat Hovav, Sodom and Mishor Rotem in Israel, and Bromchemie in the Netherlands, have been certified under the standard.

ICL Industrial Products has a training and compliance program for encouraging a high and uncompromising level of awareness of issues of safety and health among its employees and suppliers, including, *inter alia*, programs such as *Nassah* (Operative Risk Management). Safety and health goals are set periodically, with the aim of constantly improving safety and health goals, and implementation of such with the aim of achieving zero accidents. Employee protection means include, *inter alia*, protections on equipment and facilities and at work sites, protective measures for employees, procedures and training, appointing safety commissioners and safety teams, and investigating accidents and near-accidents.

In the area of health, there is an industrial health and preventative medicine system which includes, *inter alia*, periodic checks and risk assessments with respect to products and processes in facilities.

The segment is responsible for the ICL program for dealing with exceptional occurrences in transportation of dangerous substances.

#### **4.2.16 Limitations on and regulation of the Corporation**

##### **A. Subjection of activities to specific laws**

##### **1. Sub-concession**

The Bromine Company is the holder of a sub-concession granted under the Concession Law. The primary concession granted by the Concession Law is held by DSW (for details regarding this concession see section 4.1.14 above). This sub-concession was granted to the Bromine Company in 1962 and as of today, is valid until 2030.

Pursuant to the sub-concession:

- DSW grants the Bromine Company a sub-lease with respect to areas used by the Bromine Company.
- The Bromine Company has the exclusive right to extract bromine and bromine compounds from the Dead Sea.
- The Bromine Company's receipt of concentrated brine used for its extraction of elemental bromine is provided for.
- ICL Industrial Products pays the State royalties in accordance with the terms of the sub-concession, in the amount of 5% of its revenues from sales of products it extracts in accordance with the sub-concession, as well as lease payments for the areas leased under the sub-lease.

## 2. Limitations on the use of bromine-based flame retardants

In various countries of the world a review is being conducted regarding possible limitations on use of bromine-based flame retardants. Below are details resulting from the main proceedings known to the business segment as of the date of this report: Agencies of the European Union continue to evaluate the risks of the flame retardants HBCD and TBBA. In 2006, TBBA completed its health risk assessment without any restrictions. The environmental risk assessment is expected to end in 2007.

Further to the trend in the European Union regarding examinations of the possibility of restricting the use of bromine-based flame retardants, agencies of the European Union conducted a risk assessment process regarding DECA, a bromine-based commercial flame retardant (which is currently on the market). This product contains 97% pure DECA, the rest being a substance called NONA. In a decision dated October 13, 2005, based on the above risk evaluation, the executive committee of the Agencies of the European Union announced that DECA had been removed from the list of prohibited substances, according to the directive of the European Union regarding hazardous substances in electronics products (ROHS). Recently, the Agencies expressed an opinion to the effect that the decision to remove commercial DECA from the list of prohibited substances relates only to pure DECA, without the auxiliary substance NONA. ICL Industrial Products is on a joint forum with other large manufacturers of DECA which is attempting to convince the European Union not to restrict use of NONA-containing DECA for some of the applications currently in use. Additionally, ICL Industrial Products has instituted legal steps against the above decision, due to the fact that the Agencies of the European Union are not prepared to alter their opinion. On August 24, 2006, the government of Sweden announced a prohibition on use of DECA in textile products, furniture and cables, to come into force as of January 1, 2007. England and France objected to the Swedish legislation. Spokespersons for the European Market Commission have announced that in their view, the prohibition contravenes the laws of the common market, and therefore, the option of referring it to the European Court is being examined.

In Europe, a regulatory process is in place to evaluate the risks of the HBCD flame retardant, and the results of the evaluation will be discussed in the first half of 2007.

In California, a law was passed that will remove the flame retardants Penta and Octa (neither one manufactured by the industrial products segment) from use beginning in 2008, and regarding DECA scientific monitoring will be conducted by a state legislative committee. As of the date of this report, a number of state legislatures in the United States were considering draft legislation in various stages regarding bromine-based flame retardants, including various suggested regulations, ranging from imposition of limitations of the use of DECA, to marking products that contain DECA to future prohibition of its use. In Canada, a draft regulation classifying DECA as a toxic substance is being considered by environmental agencies. As of today, ramifications regarding sale of this material in Canada are not known, and the matter could result in a reporting obligation. ICL Industrial Products has other products that could be used as substitutes for some of DECA's uses.

## 3. Montreal Protocol

In conjunction with the "Montreal Protocol" regarding substances that deplete the Ozone Layer (the "**Montreal Protocol**"), which Israel is a party to, (and which was also

adopted in internal Israeli legal regulations referred to below), the production and consumption of methyl bromide for soil fumigation and the fumigation of merchandise and crops not for quarantine purposes or pre-shipment, have been reduced.

Under the Protocol, beginning in 2005, methyl bromide for soil fumigation may only be sold in the developed countries for "critical uses" approved by the parties to the Protocol from time to time. In Western Europe, the member countries voluntarily decided to reduce the amounts to a level representing 60% of the amount approved in 2006. In the USA, the EPA decided to on a reduction of about 20% compared with 2006 in the quotas for soil fumigation.

Beginning January 1, 2005 amounts of methyl bromide that can be sold for soil fumigation and volume fumigation not for the purposes of quarantine or pre-shipment to developing countries were reduced by 20%. This cap will be in effect until 2015 and thereafter the amount will fall to zero, except for "critical uses" as the parties may approve under the accord from time to time.

Methyl bromide has other uses which are defined as exempt uses which are not restricted as to production and consumption quantity, including pre-shipment and quarantine treatment referred to above, and use for production of other materials, the methyl bromide being consumed in its entirety during the process of production of the other material (feedstock).

The expected reduction in sales due to implementation of the provisions of the Montreal Protocol in 2007 are estimated by the Company at approximately \$ 11 million, and the operating profit lost as a result is estimated by the Company at approximately \$ 7 million<sup>45</sup>.

ICL Industrial Products intends to remain active in the field of soil fumigation even after use of methyl bromide is prohibited as noted above. Therefore, in recent years, ICL Industrial Products has dedicated efforts to develop and market substitutes and products complementary to methyl bromide in this market.

4. In March, 2004, the Regulations on Hazardous Substances (Adoption of Montreal Protocol Regarding Hazardous Substances that Endanger the Ozone Layer) (2004), became effective, which enforce the directives of the Montreal Protocol in Israel. As a result of these regulations, ICL Industrial Products is required to obtain an annual license for export of methyl bromide. In August 2005 the regulations were amended, establishing that the Ministry of Agriculture's Plant Protection and Monitoring Services Authority would coordinate the use of methyl bromide in Israel. The Authority published guidelines that set forth the division of permitted quantities for "critical uses," effective as of January 1, 2006.
5. Pursuant to the adoption of the Beijing Amendment to the Montreal Protocol by Israel on April 15, 2004, limitations on the production, sale and export of Chlorobromomethane (CBM) were added to the additional terms and conditions in the business license of Bromine Compounds. ICL Industrial Products anticipates that these limitations will not have a material impact upon its operations.

B. Business License

The sites on which ICL Industrial Products' plants operate have valid business licenses in accordance with legal

requirements. In addition, ICL Industrial Products has a toxic substance permit under the Hazardous Materials Law (1993), which is currently valid and must be renewed each year, and also a permit for pumping wastewater into the Dead Sea under the Prevention of Sea Pollution from Land-Based Sources Law (1988), These permits are current and require renewal from time to time.

C. Product Regulation and Registration

The following is additional information regarding limitations and regulatory supervision on the activities of ICL Industrial Products:

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<sup>45</sup> The information in this section is forward looking information. The estimated results might change, *inter alia* due to fluctuations in demand and supply of both these products and substitute products, if any, in regulation, implementation in different countries, and costs.

1. Insecticides (including soil fumigation) – In most countries of the world, this material and any product containing this material, must be registered prior to import or sale in that country. Sale is restricted according to the level of hazard (disease) and the crop for which the permit was granted in that country. The permit is generally for a limited time and needs to be renewed in order to continue selling.
2. Water treatment (biocides) – In a number of countries this material and every product containing this material must be registered, prior to import or sale in that country. Sale is limited to those commercial uses for which the permit is received in a given country. The permit is generally for a limited time and needs to be renewed in order to continue selling. In 2000, the Biocide Directive went into effect in the EU, which requires licensing of every new biocide before it starts to be sold, and also implemented a process of re-licensing every biocide on the market. During 2007-2008 ICL Industrial Products will continue to invest in licensing its products that are sold in Europe, including submitting files for renewing licenses for existing biocides.
3. Chemicals – Certain chemicals cannot be sold for certain purposes in certain countries. Certain bromine compounds are subject to trade restrictions according to use.
4. Montreal Protocol - An international accord that imposes supervision and limitations on production, see section 4.2.16(a)(3) above.
5. European Chemical Registration (The REACH Directive)

A statute covering the framework for licensing and evaluation of chemicals in the European Union (known as “REACH”) was approved by the European Parliament and the Council of Ministers in December 2006, and shall come into force as of June 1, 2007. The statute applies to chemicals already on the market, as well as to new chemicals. Pursuant to this legislation, manufacturers on the common market and importers of chemicals or of chemicals that are contained in certain products shall be required to submit dossiers contain detailed information of every substance or chemical compound manufactured or imported into Europe, in quantities of more than one ton per year (the amount and content of the information depends on the volume of production and/or sales in Europe, and the nature of the product in terms of its effect on health and the environment). Some of the products will undergo risk evaluation based on the information that is submitted, and others will only be able to be sold in the future under an appropriate permit. Such a permit will only be granted on the basis of quantified evidence relating to management of the product with regard to health and environmental aspects, the lack of appropriate alternatives, and a socio-economic evaluation. For certain durable, environmentally toxic substances, the permit will only be granted on the basis of a socio-economic evaluation and on condition that an alternative development plan is submitted, in order to encourage a transition to use of less hazardous substance.

The statute will be implemented gradually, between 2007 and 2022, under the supervision of the new European Chemicals Agency (ECHA), which is expected to commence work in 2008.

Implementation of REACH will cause ICL additional costs in the field of licensing, control and implementation of product stewardship programs with customers, and might increase the prices of raw materials. Another possible risk caused by REACH legislation is reduction in usage of a product / material, or removal of certain products from the European market. Likewise, there will be products and compounds that require investment in alternative research and development due to the need to remove certain components from the European market. ICL Industrial Products is preparing to implement the provisions of this statute.

#### D. Standards and quality control

ICL Industrial Products has a advanced and comprehensive quality control system. Each company in this business segment has its unique aspects (described below), but there are three central common issues:

- ISO 9001 management certification;

- All ICL Industrial Products plants in Israel are participants in the international Responsible Care program.

In addition to the above:

The research and development, engineering and information systems units of ICL Industrial Products also have ISO 9001 design certification. The analytical laboratory of the research unit also has ISO 17025 certification for 8 effluent testing methods.

The plants in Ramat Hovav, Sodom and Bromchemie have 18001 safety management certification and ISO 14001 management certification for environmental quality.

The Bromine Compounds company has adopted advanced quality control methodologies such as: deployment of quality improvement staff, Six Sigma, information management; HACCP (Hazard Analysis Critical Control Point), which is a methodology adopted in order to prevent intrusion of contaminants into a product. Also, its main facilities have a comprehensive system of internal quality checks, in which there are also various competitions between units.

The magnesia plant complies with GMP-13 criteria for livestock (Good Manufacturing Practice). The plant has received HACCP certification from the Israel Standards Institute and has also been certified for GMP for food by the Israeli Ministry of Health. The plant is in advanced stages of compliance with the requirements of pharmaceutical GMP. The plant has 18001 certification and is in advanced stages of obtaining Israeli Standard ISO 14001 certification.

ICL Industrial Products' research institute, which provides research services to other ICL segments as well, has an advanced quality control system which has ISO 9001 certification. Both of the Company's laboratories are certified under ISO 17025 laboratory certification. In addition, both of the laboratories meet the GLP (Good Laboratory Practice) criteria. The research institute also has a quality system that complies with the GMP requirements for pilot and mini-pilot programs, in accordance with customer needs. The research institute also has ISO 14001 management certification for environmental quality. The plant is in advanced stages of preparation for Israeli Standard 18001.

The business unit for Dead Sea salts has ISO 14001 management certification for environmental quality as well as 18001 safety management certification and is in the initial stages of satisfying the criteria of GMP in its pure potash production facility. The pure potash facility received HACCP certification in January 2007.

#### E. Internal Compliance

ICL Industrial Products' companies are implementing an internal compliance program regarding: sexual harassment, restrictive trade practices, securities law, safety and ecology.

#### 4.2.17 Legal proceedings

##### Plantation workers' claim

Beginning in 1994 three subsidiaries within ICL Industrial Products (hereinafter in this section the "**subsidiaries**") were joined in a lawsuit as third-party defendants by American companies that had been sued in United States courts (including two class actions in Hawaii) by over 30,000 former employees of banana plantations (mainly in Central America, the Caribbean islands, Africa and the Philippines). The plaintiffs claimed to have been injured by exposure to chemical substances produced by a number of manufacturers, including large chemical companies, and supplied to banana growing companies (together, the "**defendants**"), over the course of approximately thirty years (1960-1990). Many of these cases were transferred by the American courts to courts in the countries of the plaintiffs' residence. In most of these claims the subsidiaries were listed as direct defendants.

During the period that these proceeding were being held most of the plaintiffs reached settlements with most of the defendants. The settlements provide that the subsidiaries are deemed to be a settling party and are released from the settled claims. At this time it is not possible to predict the impact of these settlements on the indemnification and participation claims filed against the subsidiaries. It should be noted that there are claims of over 5,000 plaintiffs (probably even more) that are not parties to the abovementioned settlement agreements. The subsidiaries claim that they have no responsibilities or obligations towards the plaintiffs and that there is not even jurisdiction over the subsidiaries in these cases.

In the opinion of ICL Industrial Products, the quantities of substances provided by the companies in the segment to the relevant countries, and during the relevant period were, if at all, small compared with the quantities of substances supplied by the other manufacturers. All of these claims are for bodily injury and therefore, the sums are not set out in the statements of claim.

ICL Industrial Products cannot, at this stage, assess whether and to what extent the subsidiaries might be exposed to liability in these proceedings, due to the uncertainty involved in these proceedings, and therefore, no provision was made in respect of them in the financial statements.

In the opinion of ICL Industrial Products, at the relevant date, they had sufficient insurance coverage regarding the subject of the claims, but there appears to be some dispute with some of the insurers regarding this coverage and its scope. If the plaintiffs succeed in their claims against all or some of the defendants and the defendants succeed in their claims against the subsidiaries, the sum the subsidiaries are obligated to pay may exceed the scope of the coverage recognized by the insurers<sup>46</sup>.

#### **4.2.18 Goals and business strategy**<sup>47</sup>

The following sets forth the primary goals and business strategy of ICL Industrial Products:

- A. Establishing and strengthening its business position in the bromine and bromine compound market in China by leveraging the production and marketing infrastructure established in China in recent years.
- B. Increasing vertical integration among the segment's operations (chemicals for swimming pools and chlorine salt products) by establishing appropriate distribution channels.
- C. Development of new uses for existing products.
- D. Raising the proportion of specialty products in the mix of products sold by ICL Industrial Products.
- E. Maintaining current products while gradually adapting them to changing regulatory requirements, which change from time to time.
- F. Achievement of operational excellence and improvement of competitive capability through operational efficiencies throughout the supply chain.
- G. Development of new market-specific products and applications containing bromine, so that they may serve as growth catalysts for increased worldwide demand from bromine.
- H. Evaluation of mergers and acquisitions of other companies in the field including the possibility of horizontal expansion.

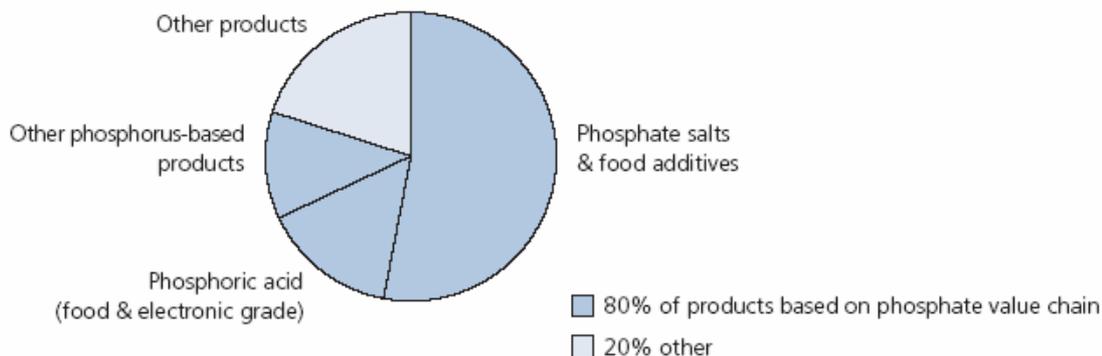
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<sup>46</sup> Subject to objections raised by one of the above insurers recently with respect to the calculation of its portion, as a result of which, apparently, there will be an insubstantial reduction of the portion borne by the insurers, the balance to be absorbed by ICL Industrial Products.

<sup>47</sup> ICL Industrial Products' plans and strategies, as described in this section 4.2.17, reflect the strategies of ICL Industrial Products as of the date of this report, are based on the projections of ICL Industrial Products as of the date of this report, and are in part forward-looking statements. It should be noted that if the Company's projections or strategies change regarding its area of activity, legislation and regulation or requirements of the authorities, these plans and projections may change, in whole or in part, from time to time and that these can be no certainty regarding the accomplishment of these plans or the success of these strategies.

### 4.3 ICL Performance Products

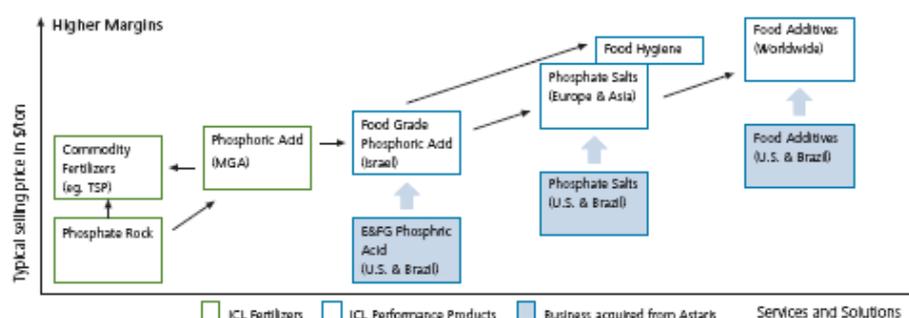
The following chart details the external sales<sup>48</sup> of the Performance Products business segment according to product:



#### 4.3.1 General information regarding ICL Performance Products

- A. ICL Performance Products is the most prominent example of ICL's implementation of its strategy of increasing its production of downstream products with higher added value. ICL Performance Products develops, produces, markets and sells a broad range of phosphate-based and alumina-based products and other industrial performance products. In 2006 ICL Performance Products revenues totaled \$1,028 million (including sales to ICL's other business segments), representing approximately 29% of ICL's revenues in that year. Approximately 80% of ICL Performance Products' external sales are of phosphoric acid of various grades (technical, food, electronics and poly phosphoric acid) and its downstream products. These products are based partially on phosphate rock that is mined by ICL Fertilizers in the Negev Desert in Israel and partially on phosphorus (P<sub>4</sub>) and phosphoric acid that are purchased from third parties.

The following chart describes how ICL Performance Products is part of ICL's strategy to manufacture downstream products with higher added value based on phosphate rock.



ICL Performance Products are designed for a long list of uses and industries, and primarily for the food, detergent, metallurgy, electronics, footwear, paper, pharmaceutical and metallurgy industries and for water treatment, for the concrete industry and fire retardant worldwide.

- B. In November 2005, ICL Performance Products acquired substantially all of the assets and operations of Astaris LLC in North America and Brazil (see section 4.3.1 above). The acquired operations complement the activities of ICL Performance Products prior to the acquisition and represent many synergies with current activities. In July 2005, ICL Performance Products purchased Adicor, a Brazilian company. Adicor manufactures

<sup>48</sup> The term "external sales" refers to the segment's sales to customers outside of the ICL Group (customers that are not other segments of ICL).

and supplies additives for the food industry in Brazil. Towards the end of 2006, ICL effected a reorganization of management in the Performance Products segment. A new CEO, Mr. Richard Kennedy, was appointed to this segment. In the past, he had acted as CEO of ICL Performance Products North America. Managers were also appointed for the various geographical units and areas of operation within the segment. This reorganization was part of the process of merging Astaris's operations into those of the Group.

- C. Part of the operations of the Performance Products segment is in the field of fire retardants for forests and open spaces (the fire safety field), mainly in the USA. Fire safety products are used against fires, mainly, in forests and open spaces, whilst the fire is burning, by spreading the products using aircraft. On January 2, 2007, ICL Performance Products acquired the assets and operations of a company called Fire-Trol, which operates in this field and has significant presence mainly in Canada and Europe. This acquisition is a strategic acquisition for ICL Performance Products in the field of fire safety, in geographical terms, as well as with respect to the products that the Group offers.

In addition, during 2006 the activities of a German company, Lactis Hygiene GmbH were acquired. This company is active in industrial hygiene. Also a joint venture was established in India to manufacture and market additives for the leather industry.

During the course of 2006, two of the companies of ICL Performance Products were divested – a company in Portugal which dealt in the field of thermoplastics for the footwear industry and the German Philopharm company, which dealt with pharmaceutical products.

- D. The activities of ICL Performance Products are divided into the following categories:

1) **Pure Phosphoric acid (technical grade, food-grade acid, electronics-grade acid and poly phosphoric acid)** – ICL Performance Products is one of the world's leading manufacturer of pure phosphoric acid. The Company manufactures and markets phosphoric acid of varying grades, primarily for the food industry. ICL Performance Products' product mix includes specialized acids with high added value that are used in the electronics and construction industries.

2) **Phosphate salts and food additives** - ICL Performance Products manufactures and markets products with high added value, including phosphate salts, produced in Germany, the United States, Brazil and China, which are primarily based on phosphoric acid. These products are designed for diverse uses, including treatment of metals, detergents, toothpastes, food additives and others. ICL Performance Products mainly uses phosphate salts that it produces as raw material to manufacture food additives in many countries. Food additives contribute to the appearance, texture, taste and preservation of food. ICL Performance Products' food additives target the processed meat, fish and seafood markets, the cheese and milk products markets and the baked goods industry.

3) **Other Phosphate-based products** – The primary market for these products are:

**Hygiene products** – a range of disinfectant and cleaning materials for various uses in the foodservice industry, including products for cleaning dairies, farms, industrial kitchens and other types of food facilities. ICL Performance Products maintains manufacturing facilities in France, Germany and Austria. Some of these products are based primarily on clean phosphoric acid that is produced in Israel.

**Fire retardant products** – the Company is one of the world's leading manufacturers of phosphate-based fire retardant products, which are used primarily to fight forest fires. These materials are produced in the United States.

**P<sub>2</sub>S<sub>5</sub>** – is used as a primary ingredient in lubricating oil additives and insecticides.

4) **Other Products** - ICL Performance Products manufactures a wide range of products that are not phosphate-based. Among these are the following products:

**Thermoplastic products (Rhenoflex)** - ICL Performance Products develops, manufactures and markets unique, environmentally-friendly, patent-protected thermoplastic products for reinforcing the front and rear of shoes and production of other leather goods such as handbags, briefcases, etc. Thermoplastic materials are plastic materials that can be molded with heat. Among ICL Performance

Products' customers are some of the leading manufacturers of quality footwear in the world. These manufacturing facilities are located in Germany, France and China.

**Chemicals for Water and Paper (Alumina Compounds, Paper & Water Chemicals – APW)** – ICL Performance Products manufactures and markets a wide range of alumina compounds and other chemicals (polymers) for the paper industry and other industries, cement additives and chemicals for treatment of industrial and drinking water. Production facilities are based primarily in Germany.

**Pharma-Cosmetics-Gypsum (PCG)** – ICL Performance Products manufactures and markets raw materials and products for the pharmaceutical and cosmetics industries and also manufactures synthetic plaster for the medical, dental and hobby industries. Production facilities are based in Germany and China.

- E. ICL Performance Products manufactures its products mainly in its facilities in Germany, the United States, Brazil, France, China, England, Argentina, Austria and Australia. In Mishor Rotem in Israel, ICL Performance Products manufactures pure phosphoric acid by means of purifying fertilizer-grade phosphoric acid produced by ICL Fertilizers. Likewise, ICL Performance Products manufactures “thermal” phosphoric acid in the US by utilizing elemental phosphorous and the segment also acquires purified phosphoric acid from third parties.

ICL Performance Products' plants outside of Israel utilize raw materials obtained from ICL's operations in Israel and other sources. For details regarding ICL Performance Products' products see section 4.3.2 below.

The global distribution of ICL Performance Products' specialty phosphates is as follows:



F. General Business Environment and Influence of External Factors

The general global economic recovery brought about an increase in demand for certain products of ICL Performance Products. On the other hand, the strengthening of the Euro against other foreign currencies during recent years, increased imports from China and the appearance of new manufacturers has harmed the Company's ability to compete. In addition, an increase in prices for raw material and energy that serve this industry brought about an increase in production costs.

#### 4.3.2 Products and services

The following are the main product categories of ICL Performance Products:

Principal Products	Primary Applications	Primary End Markets
<b>Specialty Phosphate-based Products</b>		
Pure Phosphoric Acid	Metal treatment, cleaners, food additives and phosphate salts	Metal treatment, food and beverages
	Electronics	Semiconductors, flat screens and printed circuits
Phosphate Salts	Treatment and conditioning	Detergents, toothpastes, food, metal treatment, leather, ceramics, and textile
Food Additives	Functional modification of food products	Food, mainly processed meats and cheese, dairy products, baked goods and beverages
Food Hygiene Products	Cleaning and disinfection	Dairies, and meat and dairy industries
Fire retardant products	Fire retardant	Local authorities, etc., particularly in North America
P <sub>2</sub> S <sub>5</sub>	Lubricating oil additives and Insecticide products	Automotive and Agricultural industries
Polyphosphoric acid	Asphalt additives	Roadworks industry
<b>Other products</b>		
Water Treatment Chemicals	Conditioning of cooling water and water for boilers, industrial water and drinking water	Industrial water treatment
Paper Chemicals	Chemicals for paper strength and paper surface quality	Paper industry
Alumina Compounds	Setting accelerators, Rheological additives	Building industry
Alumina and Magnesia Compounds	Antacid and antiperspirant active ingredients	Pharmaceuticals and cosmetics
Synthetic Gypsum	Casting and molding	Dental uses, medical, jewel making, hobby and ceramics
Thermoplastic Materials	Heel and toe reinforcement for shoes	Footwear

#### 4.3.3 Details of sales and profitability of products and services

The following is an analysis of the revenue and gross profit according to segment:

	Revenues (\$ million)*	% of ICL Revenues*	Gross profit (\$ million)	% of gross profit as a % of revenues
2006	1,027.9	29.4	279.2	27.2
2005	677.0	20.9	196.7	29.1
2004	582.5	19.9	178.5	30.6

\* For purposes of this table, revenue figures for the product group and for ICL used in calculation of percentage figures include revenue among business segments.

#### 4.3.4 New products

ICL Performance Products is involved in the development of innovative products in its areas of activity. In addition ICL Performance Products develops new formulations for existing products in order to adapt them as much as possible to the specific needs of its customers.

#### 4.3.5 Customers

##### A. Dependence on single customer

ICL Performance Products does not have any single customer that accounted for more than 10% of ICL's total sales.

##### B. Breakdown of sales according to geographical markets:

	1-12/2006		1-12/2005		1-12/2004	
	\$ millions	%	\$ millions	%	\$ millions	%
Israel	4	0	3	1	3	1
North America	409	40	105	16	57	10
South America	49	5	26	4	17	3
Europe	418	41	416	62	393	68
Asia	98	10	80	12	72	12
Rest of the world	33	4	36	5	34	6

The relative growth of sales in North America was primarily a result of the fact that 2006 was the first full year of inclusion of the North American operations acquired by ICL performance Products (the Astaris operations), which were acquired in November 2005. The growth in Asia was primarily a result of ICL Performance Products' focus on this market, and the shifting of markets from other countries towards Asia, for example the footwear manufacturing market. The sales growth in Europe resulted from a growth in activity, primarily in Russia.

#### 4.3.6 Marketing and distribution

ICL Performance Products sells its products mainly to industrial and commercial customers in Europe, North America, South America and Asia. ICL Performance Products' marketing network is based primarily on an extensive internal marketing organization and, to a lesser extent, on external distributors and selling agents. To market and sell many of its performance products effectively, ICL Performance Products' marketing personnel work closely with customers in order to tailor the products to the customers' needs. ICL Performance Products is not dependent on external marketing pipelines.

A significant portion of ICL Performance Products' products are proprietary and have brand names well-recognized in their relevant markets, including Fibrisol, Brifisol, Joha, Tari, Rhenoflex, Anti-Germ, Py-Ran, Nutrifos, Levn-Lite, and Phos-chek.

Most of ICL Performance Products' sales are conducted according to agreements with terms of less than one year, and via spot orders placed close to the date of supply. In addition, ICL Performance Products has framework agreements with specific customers, through which the customer can purchase up to previously-agreed maximum quantities of product during the term, on the basis of which the customer issues purchase orders to ICL Performance Products from time to time.

#### 4.3.7 Competition

##### A. Conditions of competition in areas of activity

Competition in the performance products segment centers on product characteristics, price, quality, service and the ability to address customers' needs. In this segment ICL Performance Products has many competitors, which vary from product to product.

ICL Performance Products has a leading position in the field of pure phosphoric acid and its downstream products.

##### B. Names of significant competitors

ICL Performance Products' competitors are large and mid-size international chemical companies, which have manufacturing and marketing presences in various countries, as well as regional companies that reap the benefits of being local manufacturers in a regional marketplace. In every field, many companies compete with ICL Performance Products by offering similar or substitute products.

Despite the presence of many Chinese manufacturers in the area of phosphate products, their ability to compete during 2006 as well as in the near future on a large scale is limited due to the Chinese electricity shortage in certain areas, the lower quality of their products and logistics difficulties<sup>49</sup>.

Among the primary competitors of ICL Performance Products (other than the Chinese manufacturers) in each field are:

##### 1. In the field of phosphate based products

- a. Pure phosphoric acid, phosphate salts and food additives – ICL Performance Products' main competitors are: Thermphos International BV, Chemische Fabrik Budenheim KG, Innophos Inc., Prayon, PCS, Thai Polyphosphates, Haifa Chemicals Ltd. and various Chinese producers.
- b. Hygiene products - The main competitors in Central Europe are: Ecolab Inc., and Johnson Wax.
- c. P<sub>2</sub>S<sub>5</sub> – ChemTrade Logistics Company

##### 2. In the field of other products.

- a. In the field of paper chemicals - the primary competitors of ICL Performance Products are: BASF AG, Hercules, Kemira Oy, Ciba and Eka Nobel.
- b. In the field of water - the primary competitors of ICL Performance Products are: Nalco Company, The Henkel Group, and GE Water Technologies (GE Betz).
- c. In the field of PCG - the primary competitors of ICL Performance Products are: Reheis Inc. and Summit in the area of antiperspirant, SPI Pharma in the area of pharmaceutical products, and GC Corporation in the field of gypsum.
- d. In the field of Rhenoflex – ICL Performance Products' main competitor is Texon, UTOP (a Taiwanese company), and Chinese manufacturers (on the Chinese market).

##### C. Approach for tackling competition:

ICL Performance Products addresses competition through the following activities:

- Maintaining a close connection with customers in order to respond to unique customer needs.

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<sup>49</sup> The information stated in this section includes forward-looking statements based upon the projections of the Company. It is possible that actual results may vary depending upon changes in the Chinese economy.

- Technical support and service.
- In certain cases, by tailoring specialty formulations to customer needs and in other cases manufacture of a wide range of products in order to create differentiation between segment's products and those of its competitors.
- Establishment and acquisition of manufacturing and marketing networks in various countries in order to reap the special benefits of being a local producer.
- Development of specialty markets in which ICL Performance Products has a relative advantage.
- Filing of patents and trademarks for specialty products.
- Reduction of production costs.
- Using purified and thermal phosphoric acid from own production and third parties.
- Developing and providing technical expertise in its areas of activity.
- Maintaining long established relationships with customers based on adapted proprietary knowledge and experience in its areas of activity.

#### 4.3.8 **Seasonality**

ICL Performance Products' operations are not characterized by significant seasonal fluctuations.

#### 4.3.9 **Production capacity**

ICL Performance Products' potential production capacity is based on the various plants' minimum hourly output multiplied by the potential operation hours in a given year.

	<b>Production (thousands of tons)</b>	<b>Production capacity (thousands of tons)</b>
Pure Phosphoric Acid (in terms of P <sub>2</sub> O <sub>5</sub> )	174	380 <sup>50</sup>
Phosphate salts and food additives	378	424
Other phosphate-based products	42	94
Other products	244	325

In addition, the potential production capacity of phosphoric acid by Fosbrasil, a company 44% owned by ICL Performance Products, is 70,000 tons per year. The Company also acquires phosphoric acid from third parties.

#### 4.3.10 **Research and development**

##### A. **Research and development activities and results**

The principal research and development activities conducted by ICL Performance Products during the period of this report are as follows:

In the field of pure phosphoric acid, phosphate salts and food additives –

1. Development of innovative products in the area of phosphate salts and food additives in order to strengthen ICL Performance Products' position in the markets in which it is active.
2. Development of products that assist in prolonging shelf life of food products.
3. Development of innovative products that address new customer needs.
4. Improvement of quality and characteristics of the special acids sold to the electronics and construction industries.
5. Improvement of manufacturing processes.

In other fields-

<sup>50</sup> Part of the consideration of utilizing production capacity for thermal phosphoric acid depends upon the economic feasibility of importing phosphorus (P<sub>4</sub>).

1. Development of new thermoplastic products based on ICL Performance Products patents.
2. Improvement of the water treatment product line.
3. Development of innovative products for the paper industry.
4. Improvements of pharmaceutical, cosmetics and gypsum products.
5. Development of additives for building industry.

B. Investment in research and development

ICL Performance Products' total research and development expenses for the period of this report were approximately \$ 14 million.

**4.3.11 Intangible assets – patents and trademarks**

ICL Performance Products believes that protecting its intellectual property is a cornerstone of protecting and developing its business activities. ICL Performance Products has, in various countries, approximately 1,570 registered trademarks and approximately 420 registered patents.

**4.3.12 Raw materials and suppliers**

The primary raw material for manufacture of phosphate salts and food additives is pure phosphoric acid, which is produced by purifying fertilizer-grade phosphoric acid as well as by a thermal process from elemental phosphorus (P<sub>4</sub>). ICL Performance Products obtains fertilizer-grade phosphoric acid from ICL Fertilizers and also obtains P<sub>4</sub> and purified phosphoric acid from external manufacturers.

ICL Performance Products has long-term supply contracts with suppliers of P<sub>4</sub> and phosphoric acid that guarantee it orderly supply of these raw materials.

In addition to pure phosphoric acid, ICL Performance Products uses hundreds of other raw materials, which it purchases from many suppliers. The raw material with the greatest total cost is caustic soda.

Except as noted above, ICL Performance Products is not dependent on any individual supplier or source of raw materials.

**4.3.13 Working capital**

A. Raw material inventory policy

ICL Performance Products holds raw material inventories in quantities that take into account expected production levels on the basis of consumption characteristics, delivery dates, distance from the supplier and other logistical considerations.

B. Finished product inventory policy

ICL Performance Products' strategy is to maintain adequate inventories to ensure orderly supply to customers in consideration of the customers' distance from the manufacturing locations and their requirements for inventory availability, and in conjunction with optimization of the inventory's storage costs. Therefore, portions of finished product inventories are held in storage facilities in the destination countries.

C. Credit policies

ICL Performance Products extends credit terms to its clients according to customary practices in their locations. The Company's sales are generally covered by trade credit risk insurance or by letters of credit from banks with high credit ratings.

Below are details regarding the average credit level and average credit days:

	December 31, 2006	
	Average credit level (\$ millions)	Average credit days
Customers*	92	54 days
Suppliers	71	34 days

\* Figures for customers' receivables and average days of credit exclude customers whose obligations have been sold through a securitization transaction as described in section 5.4.4 below and customers whose obligations have been discounted through other arrangements.

#### 4.3.14 **Environmental matters**

##### A. General

ICL Performance Products diligently and constantly endeavors to minimize its impact on the environment and ensures its compliance with relevant legal requirements regarding environmental protection. In this context, ICL Performance Products also has an internal compliance program for environmental issues.

##### B. Future material capital expenditures for environmental matters<sup>51</sup>

The total amount of capital expenditures in plant and equipment 2006 by ICL Performance Products relating to environmental matters stood at approximately \$1.7 million. Current expenses in 2006 stood at approximately \$ 5.5 million.

According to ICL Performance Products' estimates, the total capital expenditures and current expenses relating to environmental matters in 2007 are anticipated to be approximately \$ 12 million. The scope of these expenses is expected not to decline in the years 2007 and onward.

#### 4.3.15 **Safety and health**

Some of ICL Performance Products' products, as well as the raw materials and production processes, involve various levels of risks to persons who might be exposed to them. ICL Performance Products must comply with the safety standards and requirements prescribed, in part, under local law, and in part under international and local standards. There is a trend towards renewing these requirements and making them stricter, as a result of which, various investments might be required.

ICL Performance Products is continually making special investments in setting up and improving its safety and health measures, with the aim of preventing accidents and continually taking care of employees in the segment, and of persons in and around the facilities and the products.

The boards of directors of the companies in the ICL Performance Products segment periodically examine safety achievements and events, and the extent to which targets set in light of the Company's safety policy are met. Management of the facilities conducts follow-ups of safety issues on an ongoing basis. ICL Performance Products has a safety and health compliance plan and effects internal checking processes in order to ensure compliance with legal requirements and ICL's guidelines.

OSHA principles are implemented in most ICL Performance Products facilities in Europe and the USA.

ICL Performance Products has a training and compliance program for encouraging a high and uncompromising level of awareness of safety and health issues among its employees and contractors operating on its premises. Safety and health goals are set periodically, with the aim of constantly improving safety and health goals, and implementation of such with the

<sup>51</sup> Projections regarding the projected costs and expenses constitute forward-looking statements, and are based on legislation and regulation currently in effect, on governmental requirements known to ICL Performance Products and on investment estimates made by Company engineers. The realization of these estimates cannot be certain. Any change in these estimates, including changes in the estimates made by the Company's engineers or changes in adoption of governmental requirements or legal rulings may cause different results than those stated above.

aim of achieving zero accidents. Employee protection means include, *inter alia*, protections on equipment and facilities and at work sites, protective measures for employees, procedures and training, appointing safety commissioners and safety teams, and investigating accidents and near-accidents.

In the area of health, there is an industrial health and preventative medicine system which includes, *inter alia*, periodic checks and risk assessments with respect to products and processes in facilities.

#### **4.3.16 Limitations on and regulation of the Corporation**

Following is a brief description of restrictions in law or legal arrangements, related to the operations of the corporation, which could have significance implications for ICL.

##### **A. Subjection of activities to specific laws**

ICL Performance Products' activity is regulated by legislation which varies according to product and location. Due to the large number of products and countries, there is no specific legislation that has a unique substantial impact on ICL Performance Products.

##### **B. Business licenses**

The business segment's plants have valid business licenses in accordance with legal requirements in their jurisdictions.

##### **C. Standards**

###### **Chemical Licensing in Europe (REACH)**

A statute covering the framework for licensing and evaluation of chemicals in the European Union (known as "REACH") was approved by the European Parliament and the Council of Ministers in December 2006, and shall come into force as of June 1, 2007. The statute applies to chemicals already on the market, as well as to new chemicals. Pursuant to this legislation, manufacturers on the common market and importers of chemicals or of chemicals that are contained in certain products shall be required to submit dossiers contain detailed information of every substance or chemical compound manufactured or imported into Europe, in quantities of more than one ton per year (the amount and content of the information depends on the volume of production and/or sales in Europe, and the nature of the product in terms of its effect on health and the environment). Some of the products will undergo risk evaluation based on the information that is submitted, and others will only be able to be sold in the future under an appropriate permit. Such a permit will only be granted on the basis of quantified evidence relating to management of the product with regard to health and environmental aspects, the lack of appropriate alternatives, and a socio-economic evaluation. For certain durable, environmentally toxic substances, the permit will only be granted on the basis of a socio-economic evaluation and on condition that an alternative development plan is submitted, in order to encourage a transition to use of less hazardous substance.

The statute will be implemented gradually, between 2007 and 2022, under the supervision of the new European Chemicals Agency (ECHA), which is expected to commence work in 2008.

Implementation of REACH will cause ICL additional costs in the field of licensing, control and implementation of product stewardship programs with customers, and might increase the prices of raw materials. Another possible risk caused by REACH legislation is reduction in usage of a product / material, or removal of certain products from the European market. Likewise, in ICL Performance Products' assessment, it is reasonable that there will be products and compounds that will require investment in research and development of alternatives, due to some components being removed from the European market. ICL Performance Products is preparing to implement the provisions of this statute.

D. Standards and quality control

ICL Performance Products has a comprehensive and advanced quality control system.

- All of its plants have ISO 9001 management certification;
- ICL Performance Products meets the requirements of GMP in its food grade facilities (pure phosphoric acid, phosphate salts, and food additives) and hygiene products for the food industry.

E. Internal compliance

ICL Performance Products has adopted compliance programs with regard to antitrust, securities, prevention of sexual harassment, safety and ecology.

**4.3.17 Goals and business strategy**

ICL Performance Products seeks to increase its revenues, profitability and cash flow primarily through the following<sup>52</sup>:

- A. Focus on markets with high growth potential, primarily Asia, South America and Eastern Europe.
- B. Capture of new market share by means of acquisitions and partnerships.
- C. Expansion of areas of operation into complimentary fields.
- D. Intensification of cooperation with customers for development of new products.
- E. Investment in research and development of new products and technologies.
- F. Reduction of costs to preserve and strengthen competitive capabilities in principal markets.
- G. Exploiting additional synergies presented by the Astaris acquisition.

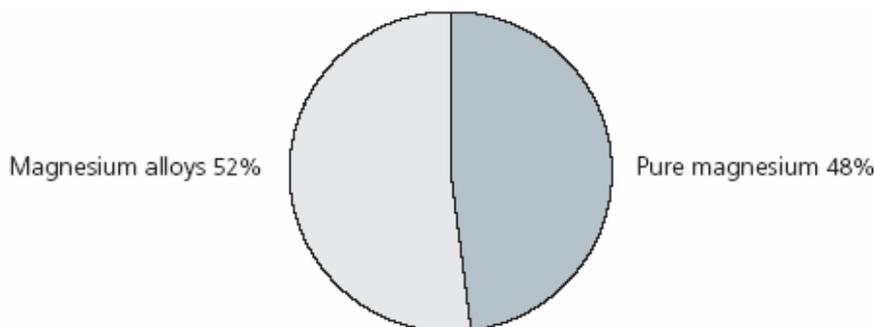
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<sup>52</sup> The strategic intentions of ICL Performance Products, as stated in this section 4.3.16, reflect the strategy of ICL Performance Products at this time, and are in part forward-looking statements that are based on current estimations of the area of operations and the Company's condition, which may change, in whole or in part, from time to time. There can be no certainty regarding the realization of ICL Performance Products' intentions or strategies.

## 4.4 ICL Metallurgy

The following chart details the 2006 external sales<sup>53</sup> of the metallurgy business segment according to product:

**Total External Sales for 2006 - \$73 millions**



### 4.4.1 ICL Metallurgy

#### A. General

ICL Metallurgy is a joint venture for the manufacture and marketing of magnesium, established by ICL together with Volkswagen under the name Dead Sea Magnesium Ltd. ICL holds approximately two-thirds of the joint venture and Volkswagen holds the balance.

ICL Metallurgy manufactures, markets and sells pure magnesium and magnesium alloys. In 2006, ICL Metallurgy's net sales (including sales to other ICL companies) totaled approximately \$92.6 million, representing about 2.6% of ICL's total net sales for that year.

Carnallite (a triple salt consisting of potassium chloride, sodium chloride and magnesium chloride), extracted from the Dead Sea as part of the potash production process, contains highly concentrated magnesium chloride. During electrolysis, magnesium is separated from the carnallite, creating magnesium metal and two by-products, chlorine gas and sylvinit (a double salt consisting of potassium chloride and sodium chloride). The sylvinit, which retains the carnallite's potash and salt after removal of the magnesium, is returned to the potash production process. The chlorine is used as a raw material mainly in the production of bromine in ICL Industrial products' bromine facility in Sodom. Sales of this segment amount to approximately 2.2% of the total sales of ICL. Accordingly, it was resolved that as of 2007, the results of this field will not be presented as a separate segment, but rather, will be included under "other".

#### B. General Business Environment and Influence of External Factors

Magnesium is considered one of the lightest construction metals. Among magnesium's main characteristics is a good strength- weight ratio, relative to other, substitute metals, notably steel and aluminum. The metal's primary use is in the following industries: Aluminum, where it is used as a primary alloy in aluminum production, steelmaking, where it is used as an auxiliary material for extracting sulphur from steel, and the magnesium alloy casting industry where it is primarily used for manufacturing automotive parts. In addition, there are other industries that use the metal where magnesium is used on a small scale.

Demand for magnesium products derives mainly from demand for the end-products described above.

In recent years, due to ongoing price erosion, several Western producers of magnesium have been forced to cease production.

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<sup>53</sup> The term "external sales" refers to the segment's sales to customers outside of the ICL Group (customers that are not other segments of ICL).

ICL Metallurgy's customers fall into two primary categories as noted above, the aluminum industry and the casting industry, mainly for the automotive market. Levels of demand for ICL Metallurgy's products derive mainly from demand for the end-products in these industries. The price downturn which commenced in the final quarter of 2005 continued during the first half of 2006, and affected the Company's results for the entire year. The continued increase in energy prices also had an adverse effect on the Company's results. During the third quarter, and towards the end of 2006, the trend reversed, due to a number of factors which brought about an improvement in sale prices on the market in Europe and the USA. The main factors which caused the price increase included cancellation of the subsidy for magnesium exports from China, difficulties in supplying magnesium alloys from China to Europe, notice that the Canadian magnesium manufacturer was closing its magnesium production plant in 2007 and problems with the supply of magnesium from Russia as a result of floods in that area.

#### **4.4.2 Products and services**

ICL Metallurgy manufactures, markets and sells pure magnesium and magnesium alloys in ingot form weighing between 8 and 23 kilograms, and also in T bars in weights chosen by the customer. In addition, as part of the magnesium manufacturing process, two by-products, chlorine and sylvinitite, are produced by the Company.

Pure magnesium serves primarily as a component of aluminum alloying in the aluminum field. In addition, this magnesium is used as an auxiliary material in the steelmaking industry.

Magnesium alloys are primarily used in the magnesium product pressure-casting industry. Magnesium's low weight relative to other metals, and the element's strength, serve as the primary basis for its use in the worldwide automotive parts casting industry.

Chlorine is a by-product created during the magnesium production process and is used primarily by ICL Industrial Products in its production of bromine and bromine compounds.

Sylvinitite is a by-product created during the magnesium production process and is used in the potash production process by ICL Fertilizers.

This use of by-products as raw materials for production of other products of the Company is just an example of the synergies that exist among the segments.

ICL Metallurgy's sales in the domestic market primarily consist of chlorine and sylvinitite to other subsidiaries of ICL.

#### **4.4.3 Breakdown of revenues and profitability of products and services**

The following is an analysis of the revenue and gross profit according to product:

	Revenues (\$ million)*	% of ICL Revenues*	Gross profit (\$ million)	% of gross profit
2006	92.6	3	(26.6)	(28.6)
2005	102.8	3	(0.2)	(0)
2004	88.2	3	5.3	6

\* For purposes of this table, revenue figures for the product group and for ICL used in calculation of percentage figures include revenue among business segments.

#### **4.4.4 New products**

The Company develops new magnesium alloy products through ICL Metallurgy's dedicated Metallurgy Research Institute (MRI). During the past few years ICL Metallurgy has developed a number of alloys used primarily in the automotive industry. These alloys have been offered in the past two years by ICL Metallurgy to a number of manufacturers of automobiles and automobile parts. These manufacturers are engaged in the process of getting the various alloys approved for use in various parts they produce. The process of approving alloys for use in producing automotive parts can take a number of years. During 2006, the Company continued to supply a new magnesium alloy to a customer with which it had reached an agreement at the beginning of 2005, for use in the manufacture of a certain part in one of its automobiles, and to manufacture a part for another consumer product. In addition the Company continued to sell new alloys in small quantities to an automobile parts manufacturer for testing and approval of its product by automobile manufacturers.

#### 4.4.5 **Customers**

##### A. Dependence on single customer

ICL Metallurgy does not have any single customer that accounted for more than 10% of the total sales of the Company.

##### B. Geographical distribution of sales in the segment

	1-12/2006		1-12/2005		1-12/2004	
	\$ millions	%	\$ millions	%	\$ millions	%
Israel	2.2	3	1.0	1	0.4	-
North America	33.7	46	52.6	65	32.5	46
South America	32.1	44	26.4	33	33.4	48
Europe	0.6	1	0.7	1	2.8	4
Asia	4.5	6	-	-	1.1	2
Rest of the world	33	4	36	5	34	6

The following are the developments that occurred in the geographical areas:

The drop in sales in North America in 2006 was the result of a reduction in sales volumes, and a reduction in sales prices in this market. On the other hand, the increase in sales in Europe stems from a shifting of quantities of the Company's sales into the European market. Part of the effect of the increase in sales quantities was set off as a result of the decrease of the sales prices in Europe compared with 2005 price.

#### 4.4.6 **Marketing and distribution**

ICL Metallurgy's sales and marketing efforts are coordinated via sales offices located in Israel and the United States with a direct staff of sales professionals. In addition, ICL Metallurgy has sales representatives and agents in key strategic markets including Germany, the United States, Italy, France, Taiwan, Spain, Japan, Sweden and Korea.

ICL Metallurgy relies on warehouses located in strategic areas of the world for its product distribution. ICL Metallurgy ships products in containers by sea from its central warehouse in Israel to three major warehouses located in Antwerp, New Jersey and Illinois. ICL Metallurgy stores inventory in these warehouses to ensure timely deliveries to meet customers' needs. ICL Metallurgy also uses direct shipments to customers.

Most of ICL Metallurgy's sales are not transacted by means of long-term contracts or orders, but rather via current orders close to the date of supply.

#### 4.4.7 **Competition**

##### A. Conditions of competition in the segment

ICL Metallurgy's market is extremely competitive. The Company has a number of Western, Chinese and Russian competitors. Competition in this area has intensified since 1995 as many Chinese manufacturers entered the market. The entrance of these Chinese manufacturers and the intensification of competition noted above caused magnesium prices to decline by approximately 50% between 1995 and 2000.

According to industry sources, the Chinese manufactured more than 500,000 tons of magnesium in 2006. ICL Metallurgy has a production capacity of about 34,000 tons of magnesium per year.

During recent years there has been a significant reduction in magnesium production in Western countries, as many manufacturers, including manufacturers in the United States, Canada, France and Norway ceased production.

During 2006, Norsk Hydro, the leading manufacturer in the industry, announced its intention to cease magnesium production operations at its facilities in Canada, as of the third quarter of 2007. This announcement, together with announcements regarding floods in the area of the magnesium production plant in Russia caused a change in the price reduction trend in the USA from the third quarter onwards. Contemporaneous with this announcement, it was announced that protective customs that were imposed upon

a Chinese manufacturer had been cancelled. An appeal against this decision has been filed. To date, the effect of this cancellation on the US market has not been considerable.

Other factors of competition in this segment, in addition to the customer's purchase price, include quality and specifications of products, and compliance with chemical standards in accordance with customer needs. The competition also necessitates offering technical support for customers in the area of casting of magnesium alloys, reliability of product supply and availability of products for just-in-time delivery to customers' locations.

**B. Names of significant competitors**

According to industry publications, the primary competitors are a large number of Chinese manufacturers (approximately 90), of which about 10 have a production capacity of more than 15,000 tons a year, the rest being smaller. Together, these manufacturers exported more than 300,000 tons out of China in 2006, constituting more than 65% of the worldwide consumption outside of China. Additional competitors of ICL Metallurgy are Avisma and Solikams (Russia), who together represent approximately 6% of the worldwide production capacity, US Magnesium (USA) – approximately 9% and Norsk Hydro (Canada) – approximately 10%. As stated above, Norsk Hydro has, in the meantime, announced that it will be closing its plant next year.

**C. Approach for tackling competition**

ICL Metallurgy addresses competition through the following activities:

Maintaining high quality control supervision for production of ICL Metallurgy products; availability of its products close to customers' production facilities, and provision of technical guidance and support by expert professionals in the area of casting. In addition, ICL Metallurgy capitalizes on its advantages in research and development capabilities, for ongoing development of innovative, complex alloys for the casting industry, mainly for the automotive industry. These alloys, which have special properties and require special expertise to produce, distinguish ICL Metallurgy from most of the other manufacturers and improve its competitive position versus the competition in the field.

**4.4.8 Production capacity**

ICL Metallurgy's potential production capacity is based on daily output of an electrolysis cell multiplied by the potential number of cells and the number of days in a given year.

In 2006 ICL Metallurgy manufactured approximately 24,500 tons of magnesium. Its potential annual production capacity is approximately 34,000 tons of magnesium.

**4.4.9 Research and development**

**A. Research and development activities and results**

ICL Metallurgy operates a center for dedicated research and development in Be'er Sheva. The center includes a staff of engineers and researchers, advanced laboratories and equipment for research and development of pure magnesium and magnesium alloy products as well as new magnesium production processes. During the past few years ICL Metallurgy developed a number of innovative magnesium alloys with special properties that grant them a relative advantage over existing alloys. The employees and engineering staff are available to provide services to customers in order to provide assistance and response to technical difficulties regarding production at the customers' facilities.

**B. Investment in research and development**

ICL Metallurgy constantly participates in research and development programs sponsored by the Chief Scientist of Israel, in research programs of the European Union (currently in its Fifth and Sixth projects) and is also participating in a joint project of the Chief Scientist with other countries. ICL Metallurgy's total research and development expense during the period of this report was approximately \$1.7 million, excluding grants.

#### 4.4.10 **Intangible assets**

##### Patents

ICL Metallurgy believes that protecting its intellectual property is a cornerstone of protecting and developing its business activities and competitive position. ICL Metallurgy has six registered and approved patents in various jurisdictions worldwide. Four are in the area of innovative magnesium alloys and two cover production processes.

#### 4.4.11 **Raw materials and suppliers**

##### A. Primary raw materials used in the metallurgy segment

The primary raw materials used in magnesium production are: carnallite, energy (mainly electricity), lime and aluminum.

1. Carnallite – ICL Metallurgy acquires carnallite from ICL Fertilizers' facility in Sodom. ICL Metallurgy dries the carnallite using special dryers. The dry carnallite is melted at high temperatures and is transferred to electrolysis cells. In these cells, carnallite is separated from metal magnesium, chlorine gas and sylvinit. After this stage the melted magnesium is transferred to the casting facilities, where the magnesium is molded into ingots and magnesium alloys. ICL uses the chlorine by-product in its production of bromine and other chemicals at ICL Industrial Products' facilities. The sylvinit is transferred to ICL Fertilizers for its production of potash.
2. Energy – ICL Metallurgy uses large amounts of electricity mainly from the power plant at ICL Fertilizers' facility in Sodom. ICL Metallurgy acquires the balance of its electricity from the national electricity grid. In addition ICL Metallurgy uses heavy fuel purchased in Israel.
3. Lime – lime is used as a means to neutralize gases during the production process. The lime is acquired from a third party in Israel under a long term contract.
4. Aluminum – Aluminum is used as a raw material in the production of magnesium alloys. In addition, small amounts of other metals are used in the production of magnesium alloys.

#### 4.4.12 **Working capital**

##### A. raw material inventory policy

ICL Metallurgy maintains raw material inventories in quantities that take into account the supplier locations and supply times.

##### B. Finished product inventory policy

ICL Metallurgy maintains inventory in warehouses in Israel and overseas in close proximity to its customers. Maintaining these inventories is intended to ensure orderly supply to customers in consideration of the customers' distance from production centers and their requirements for inventory availability.

##### C. Credit policy

December 31, 2006		
	Average credit level (\$ millions)	Average credit days
Customers*	7.9	36 days
Suppliers	3.6	76 days

\* Figures for customers' receivables and average days of credit exclude customers whose obligations have been discounted through various arrangements.

#### 4.4.13 **Environmental matters**

##### 4.4.13.1 **General**

ICL Metallurgy acts diligently and constantly endeavors to minimize its impact on the environment. The Company operates in the framework of Responsible Care and its plants have adopted internal compliance programs regarding environmental protection. In addition, during the year, ICL Metallurgy completed

the process of receiving the ISO 14001 management certification for environmental quality. Furthermore, ICL Metallurgy has an internal compliance program for environmental issues.

Consequently, ICL Metallurgy has invested significant resources over the years in the area of environmental protection. Among other things, these include equipment for gas neutralization and treatment of hazardous substances created during the magnesium manufacturing process and for improving particulate emissions. In this context, ICL Metallurgy completed the building and running-in of a unit that extracts chlorine from gases produced during the magnesium extraction process. The recovered chlorine is sold to ICL Industrial Products for the production of bromine.

#### **4.4.13.2 Material environmental protection capital expenditures<sup>54</sup>**

During 2006 ICL Metallurgy invested a total of about \$300,000 in the acquisition of property, plant and equipment for prevention of environmental harm and recorded approximately \$5.6 million as a current expense.

In 2007, ICL Metallurgy projects total capital expenditures and current expense similar to those of 2006. Due to the escalation in environmental protection requirements, the scope of these expenses is expected not to decline in the years 2008 and onward.

#### **4.4.14 Safety and health**

Some of ICL Metallurgy's products, as well as the raw materials and production processes, involve various levels of risks to persons who might be exposed to them. The production process includes work with metals at high temperatures (approx. 700° C), electrolysis of hot solutions and the generation of chlorine gas. ICL Metallurgy must comply with the safety standards and requirements prescribed, in part, under local law, and in part under international and local standards. There is a trend towards updating these requirements and making them stricter, as a result of which, various investments might be required.

ICL Metallurgy makes continual and special investments in setting up and improving its safety measures, with the aim of preventing accidents and continually taking care of employees in the segment, and of persons in and around the facilities and the products.

The board of directors of ICL Metallurgy and the safety committee at the facility periodically examine safety achievements and events, and the extent to which targets set in light of the Company's safety policy are met. In 2006, the ICL Metallurgy's Safety and Health Committee met twice. ICL Metallurgy has a safety compliance plan and effects internal checking processes in order to ensure compliance with legal requirements and ICL's guidelines.

ICL Metallurgy is in advanced stages regarding the obtaining of certification under Israeli Safety Management Standard 18001 – see section 4.4.15.3 below.

ICL Metallurgy has a training and compliance program for encouraging a high and uncompromising level of awareness of safety and health among employees and contractors on the facility's premises, including, *inter alia*, assessments regarding implementation of a program such as *Bamah* – Conduct-Based Safety. Safety and health goals are set periodically, with the aim of constantly improving safety and health goals, and implementation of such with the aim of achieving zero accidents. Employee protection means include, *inter alia*, protections on equipment and facilities and at work sites, protective measures for employees, procedures and training, appointing safety commissioners and safety teams, and investigating accidents and near-accidents.

In the area of health, there is an industrial health and preventative medicine system which includes, *inter alia*, periodic checks and risk assessments with respect to products and processes at the facility.

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<sup>54</sup> Projections regarding the capital expenditures and expenses constitute forward-looking statements, and are based on legislation and regulation currently in effect, on governmental requirements known to ICL Metallurgy and on investment estimates made by Company engineers. The realization of these estimates cannot be certain. Any change in these estimates, including changes in the estimates made by the Company's engineers or changes in adoption of governmental requirements or legal rulings may cause different results than those stated above.

#### **4.4.15 Limitations on and regulation of the Corporation**

Following is a brief description of restrictions in law or legal arrangements, related to the operations of the corporation, which could have significance implications for ICL.

##### **4.4.15.1 Subjection of activities to specific laws**

ICL Metallurgy operates under a sub-lease granted to it by Dead Sea Works, which is part of the ICL Fertilizers segment, under the authority of the Dead Sea Concession Law (1961) and with the consent of the State. This sub-lease expires on March 31, 2030. Under the current terms agreed upon by the Israeli government, ICL Metallurgy is obligated to pay royalties for its products extracted from the Dead Sea, based on the value of the carnallite consumed in the metallic magnesium manufacturing process. The Israeli government has the right to re-evaluate the royalty terms for magnesium beginning in 2006. As at the date of this report, no such request has been received. For 2006, ICL Metallurgy's royalties to the Israeli Government were \$354,000.

##### **4.4.15.2 Permits**

The site where ICL Metallurgy's plant operates has a valid business license in accordance with legal requirements. In addition, ICL Metallurgy has a toxic substance permit under the Hazardous Materials Law (1993), which is currently valid and must be renewed each year, and also a permit for pumping wastewater into the Dead Sea under the Prevention of Sea Pollution from Land-Based Sources Law (1988). These permits are in force but require renewal from time to time.

##### **4.4.15.3 Standards and quality control**

All of ICL Metallurgy's production and services facilities in Sdom have ISO 9001 management certification.

During 2006, ICL Metallurgy completed the process for receiving ISO 14001 management certification for environmental quality, and received such certification.

During 2006, ICL Metallurgy commenced the process of receiving certification under Israeli Standard 18001 for safety management. Recent investigations done at the end of 2006 show that the certification is due to be received during the first quarter of 2007.

##### **4.4.15.4 Compliance Programs**

The Company has adopted compliance programs with regard sexual harassment, antitrust, securities, safety and ecology.

#### **4.4.16 Goals and business strategy**<sup>55</sup>

ICL Metallurgy's strategy derives from its need to achieve a competitive advantage in the competitive market in which it operates. Therefore ICL Metallurgy's strategy is directed in the following areas:

- A. Continuing to develop innovative alloys with improved properties for use in the automotive industry, in partnership with automobile manufacturers around the world.
- B. Testing and development of magnesium wrought alloys.
- C. Improved partnerships with customers.
- D. Improvement of cash flow.

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<sup>55</sup> ICL Metallurgy's plans and strategies, as described in this section 4.4.15, reflect the strategies of ICL Metallurgy as of the date of this report, and are forward-looking statements and are based on ICL Metallurgy's projections regarding market conditions, completion of research and development regarding alloys and their applications, and establishment of a facility for pumping gas to Sodom and transporting gas. These can be no certainty regarding the accomplishment of these plans or the success of these strategies and they may change, in whole or in part, from time to time.

- E. Migration to use of gas – ICL Metallurgy’s magnesium plant is an energy-intensive plant. The State of Israel, via the Israel Natural Gas Lines Ltd., is in the process of constructing a pipeline for transporting gas to Sodom. According to estimates that have been provided to the Company, the pipeline will be completed by the end of 2007. Discussions held by the Company regarding agreements for acquiring gas have not yet evolved into a gas supply agreement. The Company estimates that if and when it switches to use of natural gas, this will bring about a decrease in production costs.<sup>56</sup>

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<sup>56</sup> The information includes forward-looking statements. The date of the pipeline’s completion is based on forecasts given to the Company by the Gas Pipeline Company. The Company’s projections regarding decrease in costs is based on the Company’s estimates regarding the difference between prices of the crude oil that the Company currently uses as compared with the price of gas that the Company expects to be included in the gas supply agreement.

## Chapter 5 – Additional General Corporate Information

### 5.1 Property, Plant and Equipment

ICL's main manufacturing facilities are located in Israel, Germany, Holland, Spain, England, the United States, China, and France. In addition, ICL has manufacturing facilities in Austria, Belgium, Turkey, Brazil, Argentina and Australia. The following is a detailed description of the primary manufacturing and logistic facilities and seaports used in ICL's activities:

Country	Location	Main Characteristics	Owned/leased	Size in dunam
Israel	Sodom	Solar evaporation ponds; pumping facilities; manufacturing and transportation facilities for: potash, bromine, chlorine, magnesium chloride brines and solids, sodium chloride, metal magnesium, and aluminum chloride; power plant	Leased under the Concession Law until 2030	30,140
	Mishor Rotem	Phosphate mines and manufacturing and transportation facilities for: phosphate rock, sulfuric acid, fertilizer-grade phosphoric acid, phosphate fertilizers, compound and specialty fertilizers, pure phosphoric acid, and magnesia products	Leases expiring between 2028 and 2041 Regarding magnesia facilities – leased until 2019 with option to lease for 49 subsequent years	3,580
	Tzafir (Zin and Oron)	Phosphate mines and manufacturing and transportation facilities for phosphate rock	Leases expiring between 2017 and 2024	950
	Ramat Hovav	Bromine compound manufacturing and transportation facilities	Leases expiring between 2024 and 2048	4,760
	Kiryat Ata	Manufacturing, storage and transportation facilities for liquid fertilizers and chemicals; research laboratory	Leases expiring between 2046 and 2049	670
	Ashdod Port	Warehouses and loading and unloading facilities for bulk and liquids	Leased until 2016	201
	Eilat Port	Warehouses and loading and unloading facilities for bulk	Leased until 2014	20
Germany	Ludwigshafen	Manufacturing facilities for various chemicals and compound fertilizers; warehouses and port facilities	Mostly owned (the balance leased until 2012)	810
	Ladenburg	Manufacturing facilities for pure phosphoric acid, phosphate salts, food additives and various chemicals	Owned	150

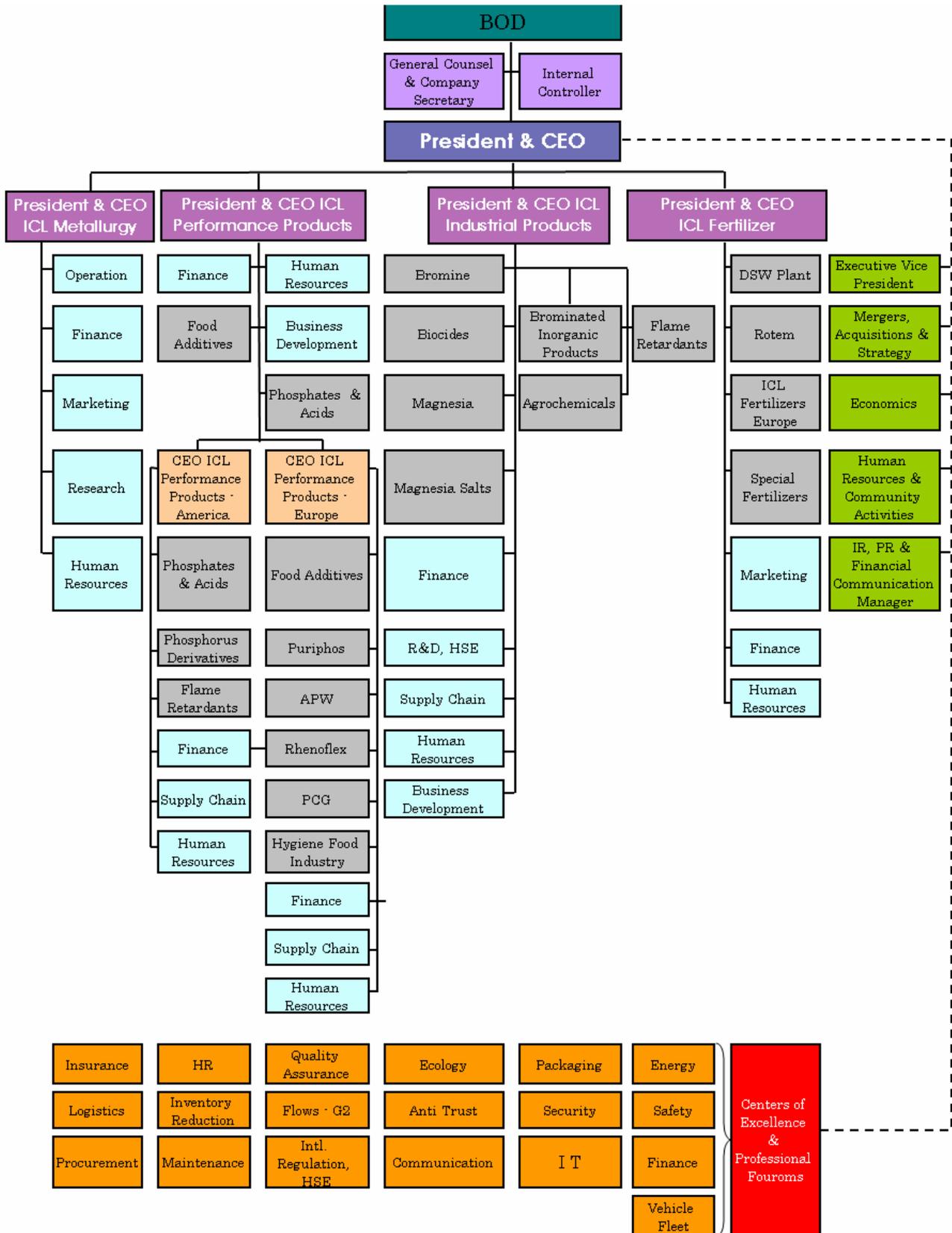
Country	Location	Main Characteristics	Owned/leased	Size in dunam
	Viernheim /Eppelheim	Manufacturing facilities for phosphate salts and food additives	7.5 owned, the rest leased	13
	Memmingen	Manufacturing facilities for hygiene products	Owned	13
Holland	Terneuzen	Manufacturing facilities for bromine compounds; warehouses	Mostly owned (the balance leased until 2007)	120
	Amsterdam	Manufacturing facilities for phosphate and compound fertilizers; warehouses and port facilities	Mostly owned (the balance leased until 2007)	120
Spain	Catalonia	Potash and salt mines; manufacturing facilities for potash and sodium chloride; warehouses	Owned	4,505
	Barcelona	Warehouses and port facilities for bulk loading and unloading	Facilities and equipment are owned. Land is owned by the port.	13
England	Cleveland	Potash and salt mines; manufacturing facilities for potash and sodium chloride; warehouses	Owned	1,580
	Teesside	Warehouses and port facilities for loading and unloading	Leased until 2014	87.6
	London	Food additive production plant	Lease until 2010 with option for another 20 years	approx. 1.5
United States	West Virginia	Manufacturing facilities for biocides (water treatment chemicals)	Mostly owned	210
	Lawrence Kansas	Manufacturing facilities for pure phosphoric acid and phosphate salts	Owned	133
	St. Louis Missouri	Manufacturing facilities for pure phosphoric acid and phosphate salts	Owned	77
	Carteret New Jersey	Manufacturing facilities for pure phosphoric acid and phosphate salts	Owned	69
	Ontario California	Manufacturing of phosphate salts	Leased until 2012	14
China	ShanDong Province	Manufacturing facilities for bromine compounds; warehouses; offices	Leased until 2049	Approx. 64.3
	LYG	Manufacturing facilities for bromine compounds, warehouses, offices	Leased until 2056	33

Country	Location	Main Characteristics	Owned/leased	Size in dunam
	Jiangsu Province	Manufacturing facilities for phosphate salts, alumina salts and products for the aluminum and paper industries	Leased until 2012	Approx. 12
	Kunming	Manufacturing facilities for phosphate salts	Lease	27
	Shanghai	Manufacturing facilities for phosphate salts and food additives	Lease	3
	Jiangyin	Manufacturing facilities for cosmetic active ingredients and thermoplastic materials for the shoe industry	Long-term lease	67
France	Caffiers near Calais	Manufacturing facilities for magnesia products and calcium carbonate (Scoralite); warehouses; offices	Owned	42
	Faucogneiy	Manufacturing facilities for various chemicals	Owned	6
	Vaas	Manufacturing facilities for ICL Performance Products hygiene products	Owned	24
Austria	Neumarkt	Manufacturing facilities hygiene products	Part owned and part leased	12
Australia	Melbourne	Manufacturing facilities for food additives	Leased	7
Brazil	San Jose Dos Compos	Manufacturing of phosphate salts	Leased	10
	Sao Bernado do Campo (Sao Paulo)	Manufacturing of phosphate salts and food additives	Leased	28

In addition, the Company maintains plants and logistics facilities in other locations throughout the world, as well as office buildings in Israel and overseas, that are both owned and leased.

## 5.2 Human Resources

A. The following chart represents the organizational chart of ICL:



ICL's Board of Directors directs the Company's policy and supervises the Chief Executive Officer's execution of his duties. The Chief Executive Officer heads the Company, assisted by a management team that includes the segment managers, the Executive Vice President, Chief Financial Officer, Vice President of Economics, Vice President of Mergers, Acquisitions and Strategy, Vice President Human Resources who is in charge, *inter alia*, of: Community Activities, Press Relations and IT, General Counsel and Corporate Secretary, and Investor Relations and Financial Communications Manager.

Each segment has its own management team, which includes the segment manager as well as vice presidents in the areas of operations, business unit managers, marketing, finance and human resources.

In addition, within the Group there are inter-company centers of excellence in various fields headed by experts in each field from the various segments, who coordinate these centers in addition to their ongoing responsibilities. These centers assist the ICL headquarters and its segments with management and supervision of their fields of responsibility.

B. Breakdown of employed personnel

As of December 31, 2006, ICL employed 9,307 employees. Of these, 33 are employees of the Company (Israel Chemicals Ltd.) and the balance are employed by the various subsidiaries.

The following details relate to the Company's employees.\*

1. Breakdown of employees by area of activity:

	2006	2005
Manufacturing	7,360	7,265
Marketing and Sales	745	759
Management and Administration	885	887
Research and Development	317	325
<b>Total Employees</b>	<b>9,307</b>	<b>9,236</b>

\* In the tables above and below regarding human resources – for partially consolidated companies, the number of employees included from each company reflects the percentage of consolidation of that company.

2. Breakdown of employees by segment:

	2006	2005
ICL Fertilizers	4,452	4,453
ICL Industrial Products	2,018	2,017
ICL Performance Products	2,172	2,094
ICL Metallurgy	345	350
Other (includes employees of IDE, Mifalei Tovala and ICL management)	320	322
<b>Total Employees</b>	<b>9,307</b>	<b>9,236</b>

3. Geographic breakdown of employees:

	2006	2005
Israel	4,675	4,680
Germany	1,042	1,088
Spain	916	871
England	817	861
Holland	238	240
United States	776	719
China	291	237
Brazil;	81	91
Others	471	446
<b>Total Employees</b>	<b>9,307</b>	<b>9,236</b>

C. Significant changes regarding employees

As of December 31, 2006 ICL had 9,307 employees, compared with 9,236 employees on December 31, 2005, an increase of 71 employees. The workforce increase was primarily in the ICL Performance Products segment due mainly to an increase in operations in this segment in China. In Germany, the decrease in human resources stemmed from sale of the operations of Philopharm, which was part of the ICL Performance Products segment. The increase in human resources in Spain stemmed from a change in the shift method used in Iberpotash's mine. The reduction in human resources in England stemmed from a rationalization plan implemented by the Company.

D. Investment in employee training and education

ICL continually invests in training and educating the Company's workforce. ICL takes pride in the fact that most of its managers rose from within the Company. ICL has established an internal training center for education purposes, which acts in a few central areas – management development training, professional colloquium events, seminars and courses – and coordinates the concepts and preparations for discussions on organizational topics common to ICL companies. The management of the center consists of representatives from the various segments.

In addition, both within and outside the frame of the training center, periodic training is conducted in the areas in which ICL has internal compliance programs: restrictive trade practices, securities law, safety, ecology and prevention of sexual harassment.

E. Employee incentive program

1. On January 28, 2007 (the "Effective Date"), the board of directors of ICL approved an outline under which office holders and other senior employees of the Company and of companies under its control in and out of Israel would be offered 12,900,000 options. Out of this sum, 2,200,000 options were allotted to the CEO]. Each option affords a right to receive one ordinary share in the Company by way of transfer or allotment, in return for payment of an exercise price of NIS 25.59 (the base price for the shares at the beginning of the day of trading on which the resolution was passed), linked to the CPI and subject to adjustments (the "Exercise Supplement"). Alternatively, and at the Company's discretion, it shall be entitled to transfer or allot shares in the sum of the difference between the share price upon exercise, and the Exercise Supplement. The option warrants are not negotiable or transferable.

The options are to vest in three installments – one third is to vest on January 27, 2008. The option warrants, or the shares obtained upon exercise thereof, if exercised, shall be blocked for an additional period, until January 27, 2009. Another third of the option warrants will vest on January 27, 2009; the option warrants or the shares obtained upon exercise thereof, if exercised, shall be blocked for an additional period, until January 27, 2010. The final third shall vest on January 27, 2010, and the option warrants or the shares obtained from exercise of them, if exercised, shall be blocked for an additional period, until January 27, 2011.

The option warrants for employees in Israel were allotted to the trustee under section 102 of the Income Tax Ordinance, under the capital gain track, and accordingly, the option warrants or the shares received from exercise thereof, as the case may be, will be held by the trustee for an obstruction period of two years from the date of allotment.

2. On March 27, 2006, the Board of Directors of the Company approved an incentive plan for the senior managers in the framework of which it approved the private placement of up to 700,000 shares of the Company to the senior managers of the Company and its subsidiaries. Of this, 175,000 shares are to be issued to the Chief Executive Officer. The shares will be issued for no consideration to a trustee, according to section 102 of the Israeli income tax law [new version] and its regulations after April 20, 2006, subject to the approval of the TASE to list the shares for trading and will be blocked for a year from their allotment.

F. Employment benefits and agreements

ICL employees in Israel are employed pursuant to collective employment agreements, senior ICL personal employment agreements and personal agreements. The collective employment agreements are signed for specified terms and are renewed from time to time. In some of the subsidiaries of the Company, the original term of the collective employment agreement has lapsed. According to law, in the event a new collective employment agreement is not signed, the

terms of the original agreement are extended for a period of an additional year or for an unlimited term, as the case may be, unless one party gives the other notice of cancellation. As of the date of this report, no notice of cancellation had been given for any of the collective employment agreements referred to above.

As of the date of this report, at ICL Fertilizers' Dead Sea Works Ltd. subsidiary, there was a collective employment agreement in effect until the end of September 2006. As at the date of this report, negotiations are being held regarding extension of the employment agreement. At ICL Fertilizers' Rotem Amfert Negev subsidiary, there is a collective employment agreement in effect until the end of April 2007. At ICL Industrial Products' Dead Sea Bromine Ltd. subsidiary a collective employment agreement is in effect until the end of December 2007. At ICL Metallurgy's Dead Sea Magnesium subsidiary a collective employment agreement is in effect until the end of June 2007.

Senior employees in special positions and members of management are employed under personal agreements. These agreements are not limited by time and can be terminated with prior notice of a few months.

Local employees of ICL companies overseas are employed according to the employment terms prevalent in the countries in which they are employed. Most of the overseas employees of ICL, primarily in Germany, Holland, England and the United States, are employed under collective employment agreements.

A relatively limited number of the employees at ICL sites in Israel are employed by outsourced personnel agencies. In addition, the Group has contracted in Israel with subcontractors for provision of various services such as security, packaging, maintenance, cleaning etc. In accordance with the decision of the Board of Directors of ICL and its Israeli subsidiaries in October 2004, contractors who employ workers at ICL's plants in Israel are required to give employees working permanently for ICL, salary terms beyond those required by law. In this context, employers are obligated to grant these employees, in addition to current salary that must be at least 5% higher than the minimum wage stipulated by law, pension contributions, severance fund contributions, recuperation funds, appropriate uniforms, meals etc.

On October 24, 2004 the Board of Directors established supervision procedures for its subcontractors in order to ascertain whether they are granting their employees the compensation described above. As of the date of this report the Company is in the process of implementing this program.

For details regarding the severance fund, pension and early retirement see note 17 to the financial statements.

#### G. Rationalization plans

During the past few years, ICL has implemented, and intends to continue to implement in the future, processes to achieve efficiencies and cost-cutting. In this context the Company intends to continue to send employees to early retirement in 2007<sup>57</sup>.

#### H. Code of Ethics and Internal Compliance Programs

The Board of Directors of ICL approved a Code of Ethics for ICL – for details see section 3.3.4 above.

ICL maintains an internal compliance program in order to ensure adherence to relevant legal requirements. It is clarified to senior managers and other relevant officeholders, that, as part of their management responsibilities, they must ensure compliance with the legal requirements of the Company for which they serve. These matters are also regularly reviewed by the management and Boards of Directors of the various companies. Among other things, internal compliance programs have been prepared and implemented in the areas of antitrust, securities law, ecology, safety and prevention of sexual harassment; seminars have been held for managers and relevant employees in these areas and implementation of the legal requirements is checked regularly. For further details regarding the implementation of compliance in each segment, see sections 3.3 and 4.1.15(e), 4.2.16(e), 4.3.15(e) and 4.4.14.4

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<sup>57</sup> The information contained in this section is forward-looking information. The Company's ability to continue with its plan, and the extent of its success, are dependent, *inter alia*, upon personal consents obtained, if at all, with each and every employee, in meetings with committees and under the economic and tax circumstances in place at the appropriate time.

## **5.3 Investments in Other Consolidated Subsidiaries**

- A. ICL holds 50% of I.D.E. Technologies Ltd. (hereinafter "IDE"). IDE builds facilities for water desalination in Israel and worldwide. In addition, IDE built and operates a desalination facility for the Cyprus government and holds 50% of a venture for construction and operation of a desalination facility in Ashkelon, Israel. IDE's partners in this venture are Veolia Water SA (formerly Vivendi) and Elran (D.D.) infrastructure Ltd. The facility was completed and produces at an annual rate of over 100 million cubic meters of treated water.

On November 23, 2006, a subsidiary of IDE entered into a contract to plan, finance, set up and operate a seawater desalination facility at Hadera, using the BOT method, for around 100 million cubic meters a year. The shareholders of the subsidiary are IDE and Shikun Ve Binui Holdings Ltd., in equal shares.

- B. ICL holds all of the shares of Mifalei Tovala Ltd. Mifalei Tovala's primary activity is trucking of cargo, mainly for ICL subsidiaries. Mifalei Tovala has expertise in transport of hazardous materials.

## **5.4 Financing**

### **5.4.1 Financial situation and sources of financing**

ICL's strategy is to balance its sources of financing among various financial instruments, and between local and international financing entities.

In 2006 the Company's net financial obligations fell, and at the end of the period the Company's net financial obligations amounted to \$551.7 million, not including securitization, a decrease of \$51.5 million.<sup>58</sup> (for the consideration obtained from securitization, see section 5.4.3 below). The reduction in liabilities was a result of cash flows which were also used to finance a dividend in the sum of \$ 180 million.

ICL's primary financing sources are short- and long-term bank loans from international and Israeli banks. In parallel, the Company utilizes non-bank sources of short- and long-term financing in order to diversify its debt portfolio.

For details regarding the Company's financial situation and sources of financing, see section 3 of the Board of Directors' report.

### **5.4.2 Average interest rates**

For information regarding average interest rates on loans, see notes 12 and 15 to the financial statements.

Most of ICL's loans bear variable interest rates based on floating interest rate based on LIBOR for short terms of one to six months, plus a premium as defined in each loan agreement. Therefore, the Company's financing expenses are exposed to interest rate fluctuations. ICL partially reduces this exposure by means of financial instruments, including interest rate derivatives, which both float fixed interest rates and create protection against variable rates reaching certain levels, in order to adjust its actual interest rate structure to match its projections regarding anticipated developments in interest rates. A minority of loans bear fixed-rate interest for the duration of the loan.

For details regarding these transactions, see note 23 to the financial statements.

### **5.4.3 Sale of customer receivables through securitization transactions**

In July 2004 ICL and some of its subsidiaries joined in a securitization transaction whereby the companies will sell most of their receivables from customers, to an external company established for that purpose that is not owned or controlled by ICL. The securitization transaction was made with Rabobank covering a total amount of \$220 million. The term of this transaction with Rabobank is five years, subject to annual renewal of a back-up credit line provided for the transaction. As of December 31, 2006, the consideration received as a result of the sale of these receivables was \$220 million.

For further details regarding securitization transactions see Note 4(b) to the financial statements.

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<sup>58</sup> Net financial obligations – credit, short- and long-term debt from banks and other credit providers, less cash and short- and long-term deposits at financial and governmental institutions.

#### **5.4.4 Amount of credit received during the period of this report**

During the report period, no long-term loans were received.

#### **5.4.5 Limitations of the Company's ability to receive credit**

In connection with some of the financing transactions described above, the Company is obligated to maintain certain financial relationships within its consolidated balance sheet:

- A. The ratio of net financial liabilities to equity on the balance sheet may not be higher than 2.1.
- B. ICL's equity may not fall below \$700 million plus 25% of the cumulative annual net income for 2005 and onwards.
- C. The ratio of EBITDA, as defined in the financing agreements, to net interest expense must be at least 3.5.
- D. The ratio of net financial obligations to EBITDA, as defined above, must not exceed 4.5.
- E. The Company's subsidiaries' total financial indebtedness is limited to 10% of the total assets in the Company's consolidated balance sheet. In certain cases loans to subsidiaries are not included in this restriction.
- F. ICL's loan agreements are generally based on provisions standard in the respective market, with the inclusion of clauses regarding negative pledge, commitments to maintain at least 67% ownership of material subsidiaries, and the State of Israel continuing to hold the "Special State Share."

#### **5.4.6 The Company's revolving credit facilities and their terms**

ICL has access to unused three- to five-year credit facilities for the total amount of \$195 million from commercial banks. Borrowing costs, when these credit lines are utilized, are similar to the Company's other interest rates. During periods of non-utilization, the Company pays commitment fees.

#### **5.4.7 Credit rating of the Corporation**

The Company is rated AA by the "Maalot" rating agency.

### **5.5 Taxation**

For details regarding the ICL's tax situation see notes 2 and -16 of the financial statements.

### **5.6 Environmental Matters**

See section 3.3.2 above.

### **5.7 Safety**

The companies' boards of directors, and safety committees at the segments, companies and plants, periodically review safety events and accomplishments as well as achievement of objectives established in light of the Company's safety policy. A safety compliance program has been implemented among ICL companies, with the assistance of legal advice and periodic evaluation of compliance with legislation and internal procedures in every segment and subsidiary. The OSHAS 18001 safety management standard has been implemented in Bromine, Rotem and DSW companies within ICL in Israel. Investigation of workplace accidents on the basis of OSHA precedents is conducted at all ICL Israel companies as well as at most of the subsidiaries in Europe and the United States.

Safety-related activities within the ICL companies are conducted on a constant and ongoing basis, in accordance with relevant professional requirements and in light of ICL's goal to prevent and minimize accidents. During the past few years, the diligent effort throughout the Company towards improvement and excellence in the area of safety has been reflected in a reduction in the number of accidents and improvement of the workplace safety level and conditions.

Among the other activities in this area the following points should be noted: An ICL-wide forum was established on the topic of safety in which the safety personnel at the Israeli companies participate. In this forum ICL's policies and strategies are debated and events and activities are presented for updating among the companies. Employee representatives responsible for improvements present

original ideas for improving the safety level. Internal competitions are conducted for achievements in the area of safety, training sessions, certifications and internal drills are conducted to enrich the knowledge and preparation, among other things, in the context of a general collective training center within the Group. At the Company's plants, an advanced safety detection and protection systems have been acquired and installed. For further details see also section 3.3 above.

## **5.8 Limitations on and Regulation of the Corporation**

### **5.8.1 Restrictive trade practices**

Certain subsidiaries of ICL (and also ICL in those areas in which the subsidiaries have been declared) have been declared monopolies in Israel in the following areas: Manufacture and supply of potash, supply of phosphates and phosphoric acid, sulfuric acid, ammonia, chemical fertilizers, solid phosphoric fertilizers, bromine and bromine compounds. In light of their declarations as monopolies, the companies are subject to limitations set forth in Chapter 4 of the Restrictive Trade Practices Law, most significantly its prohibition to abuse their positions as monopolies. As of 2006, less than 7% of ICL's revenues derive from Israeli sales and therefore, in the Company's estimation, the abovementioned declaration does not have a material impact on ICL. For details regarding the internal antitrust compliance program of the Company see section 5.2(h) above.

### **5.8.2 Special state share**

The State of Israel holds a nontransferable Special State Share in ICL on order to preserve vital State interests. Any change in provisions requires approval of the State. The Special State Share grants the following rights:

A. **Limitation of transactions and other actions:** Sale or transfer of material assets of the company (in Israel), including certain types of changes in structure, relating to ICL 's assets and activities in Israel or granting any other rights in the above-mentioned assets, not in the ordinary course of the company's business, whether in one transaction or in a series of transactions, will be invalid without the approval of the holder of the Special State Share, who will have the right to oppose the transfer of a material asset as stated above, only if in its opinion such transfer is likely to harm one of the "vital State interests." Restrictions are similarly imposed on voluntary liquidation, merger and reorganization, excluding certain exceptional cases as enumerated in the Articles of Association.

B. **Limitations on acquiring shares:**

1. Any acquisition or holding of 14% or more of the issued share capital of the Company will not be valid with regards to the company without the approval of the holder of the Special State Share. In addition, any acquisition or holding of 25% or more of the issued share capital of the company (including increase of its holdings to 25%) will not be valid with regard to the company without the approval of the holder of the Special State Share, and even if in the past the approval of the holder of the Special State Share had been received for a ownership percentage less than 25%.
2. In addition to the above, the approval of the holder of the Special State Share will be required for any percentage of ownership of any shares whereby the holder is granted the right, ability or practical potential, to appoint, directly or indirectly, a number of directors of the company that represent half or more of the directors of the company, and will not be valid regarding the company as long as that approval has not been obtained, as noted above.

For purposes of this subsection (2) pledge and/or security interest in the shares of the company will be considered acquisition of shares.

C. **Right to information:** The right to receive information from the company, as provided in the Articles of Association. The Articles of Association also provide that the holder of the Special State Share will use this information only to exercise its rights under the Articles of Association for purposes of protecting the vital State interests.

The Articles of Association further impose a periodic reporting obligation to the holder of the Special State Share, regarding all transactions pertaining to assets approved by the board of directors during the three months prior to the date of the report, any changes in capital ownership and any voting agreements among the company's shareholders signed during that period.

- D. The following are “**vital State interests**” as defined in the Articles of Association for purposes of the Special State Share:
1. To preserve the character of the company and its subsidiaries Dead Sea Works Ltd., Rotem Amfert Negev Ltd., Dead Sea Bromine Company Ltd., Bromine Compounds Ltd. and Tami (I.M.I.) Research and Development Institute Ltd. (the Company and these subsidiaries are referred to here and hereinafter the “Companies”) as Israeli companies for whom the center of business and management is Israel.
  2. To monitor the control over minerals and natural resources, for purposes of their efficient development and utilization, including maximum application in Israel of the results of investment, research and development.
  3. To prevent acquisition of a position of influence in the Companies by hostile entities or entities likely to harm foreign relations or security issues of the State.
  4. To prevent acquisition of a position of influence in the Companies or management of the Companies, whereby such acquisition or management will create a situation of significant conflicts of interest likely to negatively impact one of the vital interests enumerated above.
- E. **ICL as an Israeli company:** The ongoing management and control over the business activities of the company must be in Israel. The majority of the members of the Board of Directors must be Israeli citizens and residents. In general, meetings of the Board of Directors must take place in Israel.
- F. **Full extent of rights:** Other than the rights enumerated above, the Special State Share will not grant the holder any rights pertaining to voting or capital.

The State of Israel also holds a Special State Share in the following ICL subsidiaries: Dead Sea Works Ltd. , Dead Sea Bromine Company Ltd., Rotem Amfert Negev Ltd., Bromine Compounds Ltd., Tami (I.M.I.) Research and Development Institute Ltd. and Dead Sea Magnesium Company Ltd. The rights granted by these shares according to the Articles of Association of these subsidiaries are identical to those rights enumerated above. The full provisions governing the rights of the Special State Share appear in the Articles of Association of ICL<sup>59</sup> and the Companies enumerated in subsection (d) above, and are available for the public’s review.

## 5.9 **Business Goals and Strategy**<sup>60</sup>

The Company’s goal is to maximize shareholder value over time. The Company’s strategy for achieving this goal was defined in 1999 and stands to this day. This strategy includes the following components:

A. Focus on managerial operational segments

ICL is based on a segmented management structure: ICL Fertilizers, ICL Industrial Products, ICL Performance Products and ICL Metallurgy<sup>61</sup>. These segments correspond to the ICL’s management approach and do not necessarily reflect the legal structure of the Company. In this context, management teams have been established in these segments, which are responsible for the management of the business units within the segments.

B. Enhancing penetration of international markets

ICL is focused on strengthening its penetration of international markets, specifically growth markets. The Chinese market is a notable example, which ICL has approached in recent years through a number of joint ventures for manufacture of products based on or complementary to products produced by ICL Industrial Products and ICL Performance Products as well as the

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<sup>59</sup> ICL’s Articles of Association are available on the website of the Israel Securities Authority and the TASE under “Company reports.”

<sup>60</sup> The Company’s plans and strategies, as described above, reflect the strategies of the Company as of the date of this report, are based on its current evaluations of its various eras of activity of the Company and the Company’s current situation, and may change, in whole or in part, from time to time. These can be no certainty regarding the realization of these plans or strategies.

<sup>61</sup> As set out above, as of 2007, ICL Metallurgy will not be considered an operations segment of ICL but will be under the category of “other”.

growth in net sales of ICL Fertilizers. In 2006 over 94% of ICL's sales were made outside of Israel, and furthermore approximately 48% of ICL's net sales came from its activities conducted outside of Israel. The location of ICL's facilities in Israel and Europe constitute logistical advantages for the Company versus most of the Company's competitors.

C. Expanding the range of higher value-added product offerings

Increasing production for sale of products with high added value, which are produced and marketed by ICL. In addition, ICL is striving to expand its product offering by custom-designing products to conform to customer requirements.

D. Taking full advantage of synergies

ICL takes advantage of potential synergies among its plants in an effort to increase its efficiency and competitiveness and reduce its costs of production. For these purposes, during 1999-2001 ICL acquired the minority stakes in its publicly-traded subsidiaries, which enabled it to exploit these synergies without harming other shareholders. The Company dedicated much of its attention to identifying potential synergies among its various plants and business segments. Synergy is manifested, among other things, by using waste and by-products of one process as raw material for another process. Decisions regarding investments or changes in manufacturing methods require evaluation of their impact on the abovementioned synergies.

E. Improving cash flow

ICL is focused on improving its cash flow as part of its strategic approach. In this context, cash flow is a central determinant in ICL and the segments' considerations in making management decisions.

F. Diversifying sources of financing

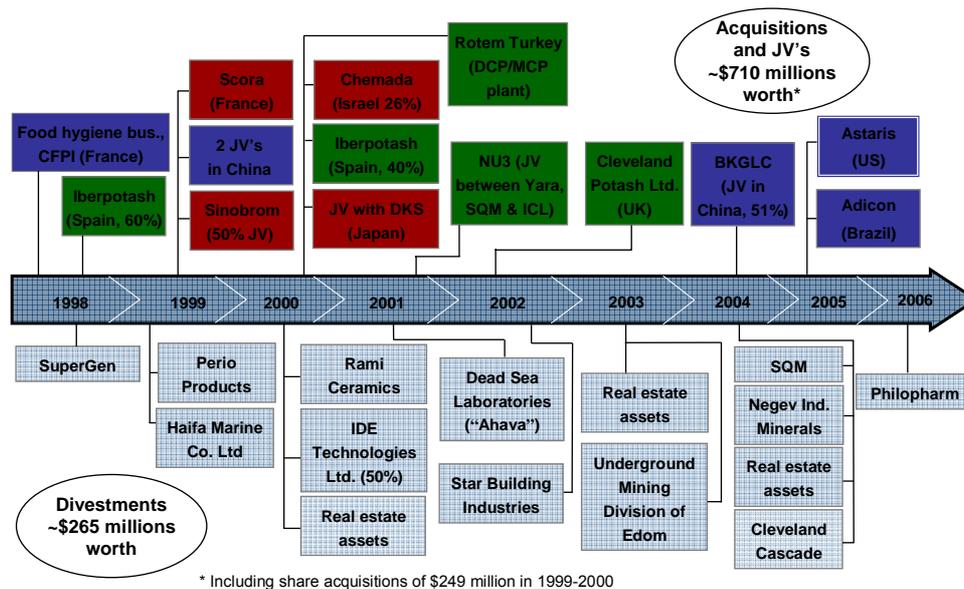
ICL seeks to diversify its sources of financing between bank and non-bank sources in order to increase the relative share of non-bank sources. The Group also seeks to diversify among domestic and international financing sources.

G. Expansion of core activities

ICL strives to continue to conduct research in the areas of potash, bromine and phosphate, in order to expand its market share and reduce its production costs. For example, in the past few years, ICL has invested approximately \$70 million in expanding DSW's potash production capacity by approximately 12.5%, and is also in the process of increasing raw material production capacity. In the area of Industrial Products, expansion of bromine production capacity in Sodom has been approved. The project is currently being set up. In the area of Performance Products, ICL acquired most of the assets and operations of Astaris and Fire Trol (see section 4.3.1C). ICL plans to increase its production capacity in other areas as well, while reducing production costs.

H. Mergers, acquisitions and strategic partnerships

ICL strives to locate and identify business acquisition opportunities, in order to expand its business through acquisitions of complementary technologies and various businesses. For example, the Company acquired two companies in Spain and England, Iberpotash and Cleveland Potash in 1998 and 2002, respectively, and acquired Astaris in North and South America in 2005. Beginning in 1998, the Company completed acquisitions and joint ventures with a total value of over \$500 million. ICL is interested in continuing to leverage its technological and operational know-how for acquisition of other businesses in order to maximize competitive advantages synergies and growth potential. In addition, ICL has divested non-core companies and business.



#### I. Measurements and Benchmarking

ICL utilizes advanced benchmarks when evaluating management decisions of ICL and its segments. These benchmarks are set in accordance with the Company's strategy to focus on increasing shareholder value and improving cash flow. Management's compensation takes into account their achievement of the milestones set in accordance with these benchmarks. In addition and in order to balance between management incentives and Company performance, the Company maintains management compensation programs based on option and share grants. These options and shares are "locked up" for various periods of time so that the managers' benefit is tied to the Company's performance during such periods.

As of the date of the balance sheet, ICL had taken various steps in furtherance of its strategy, including:

In the field of fertilizers, the network of marketing, ground transportation, sea shipping and loading facilities at the ports in Israel and Europe were consolidated, and ICL Fertilizers Europe was established in order to coordinate ICL Fertilizers' activities in Europe.

In the framework of ICL Industrial Products, the management and marketing in areas of industrial chemicals were consolidated in Israel and worldwide and ICL's research institute, Tami, was transferred into the management of ICL Industrial Products.

Responsibility was transferred to ICL Performance Products for the general operations relating to food-grade phosphoric acid, which is manufactured in Israel. In addition, a unit was established that coordinates all of the Company's activities with regard to specialty phosphates.

Management teams were established for these segments that are responsible for the management of the business units.

ICL acquired overseas businesses in its core areas of activity including potash companies in Europe, and established joint ventures in its areas of operations in various locations worldwide and particularly in China. In contrast, ICL divested operations totaling about \$265 million that were not in the core business areas of the Company.

## 5.10 Financial Information Regarding Geographical Segments

For information regarding geographical segments see note 25 to the financial statements.

## 5.11 Risk Factors<sup>62</sup>

### Macroeconomic risks:

#### 5.11.1 Currency exchange rate fluctuation

The multinational nature of ICL's activities exposes the Company to the impact of currency exchange rate fluctuation. ICL's financial statements are prepared in dollars. ICL's sales are made in a variety of currencies, primarily in dollars and euros. The portion of ICL's sales made in currencies other than the dollar exposes ICL to fluctuations in currency exchange rates of these currencies versus the dollar. Revenue and expenses of consolidated companies overseas, in the local non-dollar currency which is their functional currency, do not represent exposure. On the other hand, revenue and expenses of these companies in dollars expose these companies to fluctuations in currency exchange rates of the dollar versus their functional currencies.

A portion of ICL's expenses in Israel are incurred and paid in NIS. Therefore, ICL is exposed to strengthening of the currency exchange rate of the NIS relative to the dollar (appreciation of the NIS). Some of ICL's expenses outside of Israel (at non-autonomous companies) are incurred and paid in the local currency, specifically the euro. Therefore, ICL is exposed to strengthening of the currency exchange rate of the various currencies, specifically the Euro, relative to the dollar. ICL's strategy is to partially hedge against this exposure according to market conditions and projections regarding currency exchange rate developments.

For additional details regarding exposure to currency exchange rate volatility and the Company's hedging strategy see section 6 of the Board of Directors' report.

#### 5.11.2 Increase in interest rate and banking legislation

A portion of the Company's liabilities bear interest at variable rates. The Company is exposed to the risk of rising interest rates, which would increase its financing expenses and adversely affect its results.

The directives of the Supervisor of Banks regarding individual borrowers and borrowing groups may set limitations on the loans the Company can receive from Israeli banks. The Supervisor of Banks established limitations regarding the amount of credit of a group of borrowers relative to the banks' capital. ICL, the Israel Corporation, and the Ofer Group are considered one borrowing group. ICL today has the ability to borrow from overseas banks, and from non-bank institutions in Israel and overseas.

#### 5.11.3 War or acts of terror

War or acts of terror in the locations where the Company operates are likely to negatively impact the Company. This impact may manifest itself in production delays, distribution delays, loss of property, injury to employees, and appreciation of insurance premiums. In addition, the Company's plants are likely to be targets of terrorist acts due to the chemicals they store. The Company does not have property insurance against war or acts of terror, other than the State's insurance which covers only physical property damage, without accounting for reinstatement values.

It should be noted that since the construction of the Company's initial facilities in the 1950's, the Company has never suffered from any disturbances as the result of war or acts of terror mentioned above.

#### 5.11.4 Activities in various countries around the world

The Company is a multinational company exposed to economic, political and legislative conditions and risks in the countries in which the Company maintains facilities. The Company is exposed to a range of business risks and its success is dependant on, among other things, the Company's ability to contend with changes in these economic, political and legislative conditions. Legislative changes may increase the Company's expenses or may influence demand for its products. In addition, legislative changes, including, for example, in the area of taxation,

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<sup>62</sup> This section includes forward-looking information regarding risk factors, whose occurrence will negatively impact the Company's results. This information is based on estimations by the Company's management as of the date of this report regarding the Company, its area of activity and the market in general. Forward-looking information, as noted, is by definition uncertain information regarding the future, and in the event of a change in the estimations of the Company regarding these factors, in whole or in part, actual results will differ materially from those results projected or implied by this information.

intellectual property, import and manufacturing licenses, or environmental protection regulations, are likely to cause changes in plant costs and product demand.

#### **Industry risks:**

##### **5.11.5 Factors affecting sales of fertilizer products**

Sales of fertilizer products are subject to the influence of many factors that are beyond its control, including prices of agricultural products, government policies, weather and others.

1. Most of the fertilizer products of the Company are sold to growers of agricultural products. Fertilizer sales may be harmed as a result of decline in agricultural produce prices or other events that cause farmers to plant less and consequently reduce their use of fertilizers. Agricultural produce price decline leads to a drop in produced quantities and can cause a decrease in demand for fertilizers and lower prices. These phenomena are likely to affect the Company's business, its economic condition and the success of its future plans.
2. Government policies, and specifically, subsidy levels, may affect the amount of agricultural crops and as a result, sales of fertilizer products. As a rule, reducing agricultural subsidies or increasing subsidies to local fertilizer manufacturers, in a country to which ICL sells its products, will likely have a negative impact on ICL Fertilizers' business.
3. Weather may negatively impact sales of ICL Fertilizers' products. The agricultural industry is heavily affected by local weather conditions. Conditions such as heavy storms, long periods of drought, floods, or extreme seasonal temperatures are likely to affect the local crop's quality and yield and cause a reduction in the use of fertilizer. Loss of sales in an agricultural season in a target country as a result of weather-related events can cause sales to be lost for the whole year.

Reduction in crops due to price decline or changes in subsidy levels as stated above, are likely to have a short-term effect. In the long term, the need to feed the population will not allow for a prolonged decline in crops.

##### **5.11.6 Dependence on demand for end-products**

Sales of ICL Industrial Products' products are affected by various factors that are not within its control, including dependence upon electronics markets and legislative amendments in the areas of use of its products. For instance, a large proportion of ICL Industrial Products' products are sold for use as flame retardants. This area is subject to legislative amendment around the world, which can restrict certain uses of flame retardants. In this regard, see also section 4.2.16.2.

A large portion of ICL Industrial Products' products are used as intermediaries for end-products; for example a significant portion of the company's flame retardants are added to plastic components in electronic devices, including personal computers and televisions. Decline in demand for these consumer devices will likely negatively impact the sales of ICL Industrial Products.

##### **5.11.7 Dependence on factors beyond its control**

Sales of ICL Performance Products' products are influenced by factors that are outside of the its control. The Company has a high production component in Europe, and a large portion of its sales are effected in Europe in Euros. Some of the Company's competition are local manufacturers outside of Europe. The revaluation of the euro exchange rate vis-à-vis the dollar increases the competitive edge of these competitors.

##### **5.11.8 Subjection to legislative and licensing restrictions**

- A. ICL, as a company active in the field of industrial chemicals, is significantly affected by legal rulings and licensing authorities in the areas of environmental protection and safety. In recent years, there has been a significant increase in stringency of legislative directives and regulatory requirements in these areas, in Israel and throughout the world. Standards that will be adopted in the future are likely to affect ICL and change its methods of operation. In addition, some of the Company's licenses are for limited periods and require renewal from time to time. These permit renewals is not certain and it is possible that their renewal will be made dependant upon additional conditions. For further details see the subsections titled "Limitations on and regulation of the Corporation" in sections 4 and 5 above.

- B. Legislative changes throughout the world are likely to prohibit or restrict use of the Company's products, due to environmental protection, health or safety considerations. For example, certain countries have prohibited or restricted use of methyl bromide, due to its apparent effect on the Earth's ozone layer. For details regarding this restriction, see section 4.2.16(a)(3) above. In addition, in various countries in Europe and in the United States evaluations are being conducted which will or may result in the imposition of potential restrictions on the use of certain types of flame retardants based on bromine. For details see section 4.2.16(a)(2) above.

#### **5.11.9 Exposure relating to environmental protection and safety**

- A. From time to time the Company is exposed to legal proceedings, both civil and criminal, as a result of alleged environmental contamination caused by certain ICL facilities. For details regarding legal proceedings pending against the Company pertaining to environmental protection, see 4.1.15 above.

In addition, from time to time examinations and investigations are conducted by enforcement authorities in Israel and throughout the world. As of the date of this report, in the Company's estimation, material impacts on the Company's results are not anticipated from any of the current examinations or investigations currently being conducted.

- B. Furthermore, the Company is from time to time exposed to claims alleging physical or property damage, which may cause the Company financial harm. In addition, some of the manufacturing or marketing activities entail safety risks that ICL attempts to minimize, but is not able to eliminate. In various countries, such as the State of Israel, there is legislation that may cause responsibility to be placed on the Company without regard to its actual intent or negligence. Other laws place responsibility on defendants jointly and severally, sometimes also retroactively, and therefore can cause the Company to be liable for activities conducted jointly with others. The Company may also be found liable for claims regarding land that it mined or activities that the Company conducted within its premises, after such activities have ceased. Removal of waste from Company premises to unauthorized sites can expose the Company to claims. With regard to environmental matters, the Company has \$100 million in coverage for certain exposures.

#### **5.11.10 Third party liability and product liability**

The Company is exposed to risk of liability related to damage caused to third parties by its own operations or by its products. The Company has insurance coverage for third party liability in the amount of up to \$350 million per incident and for product liability in the amount of up to \$350 million for cumulative annual damage. There is no certainty that this insurance will fully cover all damage for such liability. Likewise, sale of faulty products by the Company might give rise to recall of products by the Company or by its customers which used the products. The costs of recall could be very high. These costs will not be covered by the Company's product liability coverage.

#### **5.11.11 Pensions and health insurance**

Some of the Company's employees in Israel and overseas have pension and health insurance arrangements that are the Company's responsibility. In return for some of these undertakings, the Company has monetary reserves that are invested in financial channels. Changes in life expectancy, changes in the capital market or changes in other parameters by which undertakings to employees and retirees are calculated, and statutory amendments could increase the Company's net undertaking for this item.

#### **5.11.12 Volatility**

A portion of the activities of ICL are characterized by volatility. This volatility is caused by entry of new products into the market, vendors exiting the market, changes in supply of the product and changes in demand. These fluctuations may harm the Company's profitability.

#### **Risk unique to the Company:**

#### **5.11.13 Concessions and permits**

Around 39% of ICL's sales in 2006 were of products based on minerals extracted by the Company from the Dead Sea in accordance with the Dead Sea Concession Law (1961). In addition, ICL extracts potash and sodium chloride in Spain and England pursuant to permits

and concessions in those countries. Furthermore, the Company mines phosphate rock from phosphate deposits in the Negev Desert in accordance with a concession from the State of Israel. Loss or impairment of these concessions would cause harm to the Company. For details regarding these concessions and permits see section 4.1.15(a).

#### **5.11.14 Natural Disasters**

The Company is exposed to natural disasters such as flooding, earthquake, and other natural disasters that may cause material damage to its business. The Company has insurance covering this exposure.

Some of ICL's plants in Israel are located on the African-Syrian Rift, a seismically active area.

In recent years sinkholes have been discovered in the area of the Dead Sea, which could cause harm to the plants.

In one of the Dead Sea evaporation ponds' dikes operated by a subsidiary of ICL Fertilizers, there is seepage of brines from within the pond and cracks have appeared in the dike. There is also a fear that sinkholes might appear in the dike. If the dike is breached, the Company might lose the solutions in the large evaporation pond. For additional details see section 4.1.1.

In the area of Sodom, where many of ICL's plants are located, there are occasional flash floods in the stream-beds. Heavy flash floods occurred in October 2004, causing property damage and loss of profits. The Company has insurance coverage that covers these types of damage, subject to payment of deductibles.

In 1999 there was flooding in the potash mine in England. The Company does not have property insurance for the underground property of the mine in England.

#### **5.11.15 Water level in Pond 150**

In conjunction with the evaporation process, salt is precipitating in evaporation pond number 150 at the Dead Sea (which is the central evaporation pond in the solar evaporation pond system) in a layer growing by approximately 20 centimeters per year. The precipitated salt causes a reduction in the volume of brine in the pond. In order to overcome this phenomenon, the water level of the pond must be raised. Failure to raise the water level as stated above will cause a reduction in the production capacity of ICL Fertilizers. For further details regarding the water level in pond 150 see section 4.1.15(f).

#### **5.11.16 Price of water and electricity**

The Company's phosphate facilities use large quantities of water purchased from the Mekorot Company at prices set by the government. If these prices rise significantly, the Company's costs will rise as well.

In Sodom, the Company obtains water from an independent system that is not part of the national water system. A shortage of water in the water sources in proximity to the plants, will force ICL Fertilizers to seek water sources located further away at higher cost.

The Company's plants in Israel and overseas consume large amounts of energy. Significant price increases for energy, or energy shortages, in Israel will affect production costs and/or quantities.

#### **5.11.17 The Sea Canal**

The State of Israel occasionally evaluates the possibility of constructing a canal from the Red Sea or the Mediterranean Sea to the Dead Sea, for purposes of energy production, desalination and raising the Dead Sea's water level. Such a canal would likely change the composition of the Dead Sea. Such a change in water composition might negatively impact the production of ICL plants. (On this topic see also section 4.1.15.)

#### **5.11.18 Labor disputes**

ICL from time to time experiences labor disputes, slowdowns and strikes. Most of ICL's employees are subject to collective agreements. Lengthy slowdowns or strikes at any of ICL's plants would likely cause non-supply of products that had already been ordered. In addition, due to the interdependency of the ICL plants, slowdowns or strikes in any one ICL plant is likely to have a material impact on the Company. The Company has insurance coverage against part of the cost of labor stoppages in the context of the Strike Fund of the Manufacturers' Association.

### 5.11.19 Dependence on seaports, transportation and loading in Israel

Approximately one-half of the net sales of the Company are sales of bulk products characterized by large quantities. Most of this production quantity is shipped from two seaports in Israel from dedicated facilities. It is not possible to ship large quantities in bulk from other facilities. Any significant mishap with regard to the seaport facilities or a strike of port workers would likely create difficulties in exporting goods overseas and harm sales.

The following are the Company's estimates of level of impact of these risk factors on the activities of ICL.

It should be noted that the Company's estimations of level of influence of a risk factor on the Company below reflect the level of influence of that risk factor assuming the risk factor occurs, and does not reflect any estimation of or give weight to the likelihood of occurrence of that risk factor. In addition, the order of appearance of the risk factors above and below is not according to the inherent risk of each factor or the likelihood of its occurrence.

	Level of influence of the risk factor on the Company		
	Low influence	Medium influence	High influence
<b>Macroeconomic risks</b>			
Currency exchange rate fluctuation	V		
Increase in interest rates and banking legislation	V		
War or acts of terror	V		
Activities in various countries around the world		V	
<b>Industry risks</b>			
Impacts on sales of fertilizers (product prices, government policies and weather)		V	
Impacts on sales of ICL Industrial Products products (product prices, government policies relating to use of flame retardants, etc.)		V	
Impact on sale of ICL Performance Products products			
Dependence on demand for end-products	V		
Subjection to legislative and licensing restrictions		V	
Exposure relating to environmental protection and safety		V	
Third party and product liability		V	
Changes in pension and health insurance calculation coefficients by companies overseas	V		
Seasonality and volatility	V		
<b>Special risks</b>			
Concessions and permits			V
Natural disasters	V*		
Water level in Pond 150	V		
Costs of water and energy		V	
Canal from the Red Sea or the Mediterranean Sea to the Dead Sea	V		
Labor disputes	V		
Dependence on seaports, transportation and loading in Israel		V	

\* Taking into account the Company's insurance coverage.