2012 Annual Report Management Discussion and Analysis (the "Report")

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1. Market Overview and Operational Activities

General economic conditions

As a result of the ongoing uncertainty about the further course of the euro debt crisis, the economic and state budget risks in the U.S.A. and the significant economic weakening in emerging markets, economic development worldwide was affected from the second quarter of 2012. Global output has been depressed by a slowdown since the summer of 2011. This is still having an impact on major economic regions, even if to different extents. Imposed monetary and fiscal policies only calmed the situation temporarily, without solving the underlying structural problems. As a result, the few positive developments of economic data seen in the first quarter of 2012 could not be sustained. Also, during the summer, the debt crisis in the euro area drove the euro to new cyclical lows against the US dollar, before the euro was able to rebound from those lows after the European Central Bank announced that it will do everything necessary to stabilize the euro zone.

Economic growth in the euro zone slowed in 2012 mainly caused by the economic downturn in the southern European countries, which slipped into recession as a consequence of budget consolidation measures (so called “austerity”-measures). Whereas the northern countries, where levels of debt are somewhat lower, were able to post slight, albeit slower, economic growth in the first quarter, economic data from the second, third and fourth quarters showed that the mood in these countries also darkened markedly and most countries even recorded a shrinkage in the economic output in the last months of the year.

In its January 2013 “World Economic Outlook” (WEO), the International Monetary Fund (IMF) predicted a global growth at 3.2% in 2012 and 3.5% in 2013, 0.1 percentage points lower than in the October 2012 World Economic Outlook. Relative to the April 2012 forecasts published in the World Economic Outlook, the forecasts for 2013 growth have been revised from 2.0% down to 1.4% for advanced economies, and from 6.0% down to 5.5% for emerging market and developing economies. Output is expected to remain sluggish in advanced economies but still relatively solid in many emerging market and developing economies. Unemployment is likely to stay elevated in many parts of the world. And financial conditions will remain fragile, according to the IMF’s October 2012 Global Financial Stability Report (GFSR). These forecasts,

however, are predicated on two important assumptions: that there will be sufficient policy action to allow financial conditions in the euro area periphery to ease gradually and that recent policy easing in emerging market economies will gain traction. For the euro area, the IMF records a decline of 0.4% for 2012 and a decline of 0.2% for 2013. For the UK, a decline of 0.2% for 2012 is expected and a 1.0% growth for 2013 is projected. These assumptions are backed by the German Ifo Institute. According to its latest projections from December 2012, global economic output only increased weakly at a rate of 3.0% in 2012 and will continue its slow growth at a rate 3.3 % in 2013. The Ifo Institute expected a decline of 0.5% for 2012 and predicts a decline of 0.2% for the euro area in 2013.

Business Overview

Electronics Line 3000 Ltd. ("EL" or the "Company") is a pioneer in next-generation security solutions for the residential and small commercial markets. The Company designs and produces cutting-edge solutions for security and control of living and working environments. The EL line provides comprehensive security protection, as well as sophisticated system and home management functionality, for optimal comfort, safety and peace of mind. This new industry standard is further upgraded with enhanced remote management capabilities that give homeowners instant access to their system from anywhere in the world.

Upgrading Everyday Security

EL solutions enable new levels of control and maintenance in protected sites through the ELAS, a proprietary remote management server. The Company enjoys a unique market position in supplying ELAS-governed systems for the home and workplace, which provide the multiple benefits of a virtual security presence, convenient home automation, and energy efficiency, all customized by the end-user and/or the service provider.

EL's extensive product line includes both wired and wireless solutions. EL solutions offer enhanced detection and PSTN/IP/GSM/GPRS-based event reporting, along with advanced remote management tools. The back-office support and customized branding of EL solutions provide superior security with significant business benefits and market expansion potential.

Global Partnerships

Nearly three decades of cutting-edge leadership have earned EL a solid market position, allowing users worldwide to benefit from EL's ongoing development of upgraded security solutions. The Company maintains long-term partnerships worldwide.

EL has made emerging technology, user-friendly design and exceptional quality the benchmarks for serving its international network of clients and partners. Drawing on a tradition of pioneering expertise, EL specialists also provide security integration consultancy, installation service, training and technological support.

EL was established in 1982 and is headquartered in Israel. The Company is publicly traded on the Frankfurt Stock Exchange (ELN) and is part of the RISCO Group, an established leader in the international security market.

In March 2010 RISCO Ltd., ("Risco") a leading provider of integrated security solutions, acquired a controlling interest in the Company. RISCO Group intends to maintain the

Company's product offerings and independence in the market by growing it as RISCO Group's residential arm through product portfolio expansion into video and management solutions together with its major partners worldwide.

In order to increase the Company's global coverage and to have better penetration into new and existing markets, in August 2010, the Company entered into management and distribution agreements with Risco as Risco has the facilities to import, promote, sell, market and distribute the products in the territory (as defined in the agreement) and is willing to act as the supplier's non-exclusive distributor of the “Products in the Territory”.

The Company reorganized its sales force in order to achieve a better coverage in its target markets. Mr. Douglas Luscombe, the Company's CEO, was located in the UK and several new Regional Sales Managers (RSM) were assigned to cover the rest of Europe and the Russian markets.

The Company is well positioned in important markets around the world, in particular Northern and Western Europe and consistently strengthens its position in additional regions in Latin America, Asia Pacific and more. The Company’s brand is associated with high quality products and solutions.

The Company continues to develop and expand its marketing and sales capabilities with a focus on strategic customers and markets, while at the same time, providing more marketing and technical support to existing customers.

Products and Product Families

The Company offers an array of security solutions for every need. EL’s wireless control systems enable end-users to choose the level of control and monitoring they require using innovative remote solutions.

Advanced security detectors supply excellent interior and perimeter protection while safety detectors offer enhanced environmental and personal safety including: smoke, gas and water leak detection, panic buttons and much more.

The systems can be activated using a variety of local control devices such as keyfobs and keypads. EL also offers end-users and providers advanced remote management applications for comprehensive control over the system from any location.

Complementing accessories and add-ons include home automation modules, zone expanders, receivers, sirens and more for a complete security offering.

The EL Application Server (**ELAS**) is a 24/7 dedicated application server, which provides an answer to the growing demand for customer autonomy. The ELAS offers private remote access to EL security systems, allowing homeowners to easily check, activate, modify and communicate with their security system from anywhere in the world, through web-based or smartphone applications.

The sophisticated **iConnect** system, with its sleek design, serves as the command center for a residential and small commercial Security and Home Automation network.

Powered by the full range of ELAS remote management functions, iConnect effortlessly integrates remote signaling from end-users, monitoring stations, service providers and technicians. The ELAS enables remote programming and maintenance of the iConnect system by Internet or smartphones, built-in interface with PSTN/GSM/GPRS or PSTN/IP communication modules, configuration of email and SMS event notification to users, and much more.

The two-way wireless RF technology built into iConnect also enables the use of PIR Cameras with event triggered images, for verification to both the monitoring station and the end – users via web and Smartphone Applications. The compatible EL two-way peripherals communicate with the iConnect control panel and respond to RF signals with top-level data security. Designed for superior efficiency, the peripherals only respond to signals when the control panel is armed, and then they act with enhanced speed to minimize energy consumption and signal traffic congestion.

CommPact, named for its streamlined, space-saving design (21x15.2x4cm), offers cost effective security and connectivity, with all the essential functions of one-way wireless technology available in one small high-powered package.

The simple wireless installation and advanced remote management capabilities of CommPact provide an ideal value-for-money solution, which allows users to enjoy a complete sense of control and peace of mind.

CommPact's remote management is driven by the ELAS, which enables a virtual presence via video look-in on the premises. The advanced features include remote programming and maintenance of the CommPact system by Internet or smartphone, built-in interface with

PSTN/GSM/GPRS communication modules, configuration of email and SMS event notification to users, and stand-alone two-way audio capability.

An established, field-proven solution using one-way wireless FM technology, **Prime** features modular flexibility. Security, safety and comfort receive equal priority , with features that enable Home Automation .

The robust Prime system takes advantage of PSTN and/or GSM connectivity and is compatible with all of EL's wireless keypads and other peripherals. Service providers and end-users can customize Prime in all its essential functions: SMS event notifications, remote installation of software, upgrades, audio communication, range extension and more.

Business Strategy

The Company is engaged in the design, development, production, marketing and sales of next-generation security solutions for the residential and small commercial markets.

The Company's vision is to be a leading global provider of wireless security with remote management solutions for the mass residential and small commercial markets.

Key elements of the Company's growth strategy include:

- Continuing to position the Company's advanced 2 way wireless products as an innovative quality solution that reduces operating expenses for the service provider and increases functionality and control for the end user.
- Expanding and strengthening relationships with key target customers in order to sell to their customers the wireless security with remote management solutions.
- Providing a full range of market solutions – from standard, low cost solutions to high end, advanced solutions
- Increasing services which are available as part of the Company's platform for remote management solutions, including advanced video capabilities, remote management applications and more.
- Leveraging wireless technology and various platforms to develop new solutions.
- Invest in both short-term and long-term R&D in order to improve product design and lower production costs.

2. Operating and Financial Review for 2012

The financial statements of the Company as of December 31, 2012 have been prepared in accordance with the International Financial Reporting Standards (IFRS).

During the period from January 1 to December 31 of fiscal 2012 ("Reporting Period") an implementation of the Company's business plan has been put in place.

As part of that plan, the Company completed the development of its new product line (ELAS, iConnect Two-way-wireless and CommPact) put sales focus on distributing those in the market. The company outsourced its production activity and increased its operating expenses efficiency.

Earnings

The Company is facing internal and external challenges due to the recent developments in the global economy as well as from the implementation of the business plan. Global economic developments have affected the Company's 2012 and 2011 performances and results, its customers and suppliers and introduced new settings and opportunities for the future.

During the Reporting Period, the Company benefitted from the implementation of several streamlining measures, which had a positive effect on the Company's profitability. The major improvement of the gross margin was due to the Company´s decision to outsource its production activities to sub-contractors and to lower than expected operating costs during the reported period.

Additionally, during the reported period, new high margin products were launched, from which the Company expects further positive effects on the profitability in the upcoming quarters.

On November 28, 2011, the Company sold its UK subsidiary in a management buyout transaction. The reported 2012 financial figures apply to the Company's ongoing operations after the sale of the subsidiary, while in the comparable period ended at December 31, 2011, profit & loss of the subsidiary were consolidated with the ongoing operations.

In order to compare between the periods, the following table presents items of the profit & loss statement as of December 31, 2011, that were adjusted in regard to the sale of the subsidiary, and shows the earnings situation of the Company as if the subsidiary had been sold before January 1, 2011:

US dollars in thousands	12 months ended December 31, 2012	12 months ended December 31, 2011 (reported figures)	12 months ended December 31, 2011 (adjusted figures)
Revenues	14,331	24,164	18,152
Cost of Revenues	8,905	15,745	12,214
Gross Profit	**5,426**	**8,419**	**5,938**
% Gross Profit	**38%**	**35%**	**33%**
Operational cost and expenses:			
Research and development	1,349	1,733	1,733
Selling and marketing	1,556	2,878	1,463
General and administrative	1,678	1,977	1,573
Other (income) expenses	(402)	315	315
Total operating costs and expenses	**4,181**	**6,903**	**5,084**
Operational income	1,245	1,516	854
% Operational Income	9%	6%	5%
Finance Exp. Net.	166	354	351
Tax on Income	-	54	-
Gain from sale of subsidiary	-	1,224	-
Net income	**1,079**	**2,332**	**503**

The Company's revenues in the Reporting Period amounted to US$ 14.3 million, compared to adjusted US$ 18.2 million for the year ended December 31, 2011.

The decrease in revenues was mainly due to the change in the Scandinavian market, where a long-term customer relationship was discontinued because of an M&A transaction of the client, the postponement of orders from a major customer following overstock with the client warehouse and general adverse market conditions.

The Cost of Goods sold amounted to US$ 8.9 million (~62%) compared to adjusted US$ 12.2 million (67%) in the comparable year.

The gross profit for the Reporting Period amounted to US$ 5.4 million (38% of the revenues) compared to adjusted US$ 5.9 million (33% of the revenues) in 2011. The margin increase resulted from efficiency gains and the use of outsourcing partners. Also, new high margin products were launched while old and low margin products were ceased.

The Company employs management service agreements with Risco Ltd. in order to assist it in the following fields: (i) sales administration services; (ii) IT and computerized systems; (iii) Finance management and accounting; (iv) human resources; (v) directors and consulting services; (vi) legal and company secretarial services.

The research and development expenses amounted to US$ 1.3 million during the Reporting Period, compared to adjusted US$ 1.7 million in the comparable year. Research and Development expenses included the amortization of US$ 100,000 production files that were previously capitalized as intangible assets, while the related product (CommPact) was under development.

The selling and marketing expenses amounted to US$ 1.6 million during the Reporting Period, compared to adjusted US$ 1.5 million for the comparable period of last year.

The general and administrative expenses amounted to US$ 1.7 million during the Reporting Period, compared to adjusted US$ 1.6 million in the comparable year.

Other income amounted to US$ 402,000 from the reversal of provisions during the Reporting Period, compared to US$ 315,000 other expenses (adjusted and reported) for the comparable period of last year.

Total operating expenses for the Reporting Period amounted to US$ 4.2 million, compared to adjusted US$ 5.1 million in the comparable year. The decrease in operating expenses is mainly due to operational efficiency, expense savings, and the implantation of the management service agreement between Risco and the Company as mentioned above.

The net profit for the Reporting Period amounted to US$ 1.1 million, compared to adjusted net profit of US$ 0.5 million in the comparable year.

The Company continues to develop and expand its marketing and sales capabilities with a focus on strategic customers, while at the same time, providing more marketing and technical support to existing customers due to the tough economic situation in certain countries.

The Company entered into distribution agreements with Risco, as Risco has the facilities to import, promote, sell, market and distribute the certain products in certain territories (as defined in the agreement) and is willing to act as EL's non-exclusive distributor of those products in the respective territories.

On October 10, 2012 the Company approved an amendment to the distribution agreement with Risco. According to the amendment, the Company will also have the option to distribute Risco products.

The Company's Financial Position

The Company's cash and cash equivalents as of December 31, 2012 (hereinafter: "the Reporting Date") were US$ 0.8 million, compared to US$ 1.7 million on December 31, 2011. The decrease is mainly due to cash used in financing activities, especially the repayment of a bank loan in the amount of US$ 1.2 million. This was compensated with cash provided by operating activity in the amount of US$ 0.6.

The Company's trade receivables on the Reporting Date were US$ 0.7 million, compared to US$ 2.0 million on December 31, 2011.

The Company's prepaid expenses, other accounts receivables, advance payments to suppliers and income tax receivables on the Reporting Date were US$ 0.2 million, compared to US$ 1.9 million on December 31, 2011.

The Company's inventories on the Reporting Date were US$ 4.0 million compared to US$ 1.4 million on December 31, 2011.

Net investment in property, plant and equipment, in the Reporting Period amounted to US$ 0.6 million, compare to a US$ 0.5 million investment on December 31, 2011.

The short term credit balance from banks on the Reporting Date amounted to US$ 0.3 million, compared to US$ 1.2 million on December 31, 2011.

The Company's trade payables as of the Reporting Date were US$ 2 million compared to US$ 2.8 million on December 31, 2011.

Other current liabilities, accrued expenses and income tax payable were US$ 0.8 million, compared to US$ 1 million last year.

Long term loans were US$ 180,000 on the Reporting Date compared to US$ 0.5 million on December 31, 2011.

Financial Ratios	December 31, 2012	December 31, 2011
Current Ratio	1.8	1.4
Quick Ratio	0.5	1.1

As of the Reporting Date, the Company complies with bank covenants.

The Company's total equity as of the Reporting Date was US$ 3.7 million, corresponding in an equity ratio of 51.5%, compared to US$ 2.5 million (29.0%) as of December 31, 2011.

Cash Flow

During the Reporting Period, net cash provided by operating activities was US$ 617,000 compared to net cash used in operating activities of US$ 255,000 during the comparable year.

During the Reporting Period, net cash used in investing activities was US$260,000 compared to net cash provided by investing activities of US$ 1.8 million in fiscal 2011.

Investment activities during 2011 include proceeds from sales of a subsidiary in total amount of US$ 2.1 million.

During the Reporting Period, cash used in financing activities amounted to US$ 1.2 million, compared to US$ 0.9 million during the fiscal year of 2011.

During fiscal 2012, the Company repaid loans' principals in the amount of US$ 1.2 million.

Employees

The number of employees increased from 31 as of December 31, 2011 to 34 as of December 31, 2012.

3. Risks and Opportunities

Risks related to the Company

Dependence on Sub-contractors

The Company depends on sub-contractors in production and in research and development services. In the event that the relationship with any of the sub-contractors is terminated, the Company may incur a delay in developing new products and in producing and supplying its products until such time as the Company is able to locate and establish a relationship with alternative sub-contractor(s) or alternatively, perform such work in-house. Additional time would be needed before such new sub-contractor(s) or internal personnel could render effective development services and prepare production files previously provided by the original sub-contractor(s). This time delay could affect the Company's ability to producing products, launch new products or introduce new versions of products in a timely manner which could adversely affect the Company's market share. In addition, any arrangement with a new sub-contractor or a decision to perform any such work in-house may increase the Company's costs and affect its gross margins.

The Dependence on Integrators, Service Providers, Distributors and Installers of Systems

Currently, the Company does not typically sell its solutions to end users. The Company's traditional customers are integrators, service providers, distributors and installers of systems. Therefore, the Company is dependent, and has little control over, the customers who are, in fact, third-party installers of the Company's products. The Company has virtually no contact with end users of the product. The customers are responsible for the most part, for the sale, installation and technical support of the Company's products in relations to the

end user. Due to this extended channel of distribution, the business results of the Company could be significantly harmed through changes in the business conditions of the customers which are beyond the ability of the Company to control. Installation and/or service problems could arise that might affect the sale of products to end users and because the Company does not perform the installation or service of its products at the end user facility, it might be difficult for the Company to positively impact or resolve such issues between the customer and the end user. Furthermore, the Company may not be able to preserve its current relationships or to develop new relationships with different customers. Any such change in its relationships with customers is liable to significantly harm the business affairs of the Company, affect the Company's sales, its financial condition and business results.

Dependence on Key Customers

The Company's sales to its largest four customers accounted (excluding sales to related parties) for approximately 45% of its total revenues during the year 2012 and approximately 43% of its total revenues during 2011. The Company does not have long-term purchase contracts with its customers, and sales arrangements with some of these customers do not have minimum purchase requirements. The Company cannot assure that these major customers or any other customer will continue to purchase its products at all or in the same volumes or on the same terms as they have in the past. Their failure to do so may significantly reduce the Company's revenues.

Changes in Exchange Rates

The Company is exposed to exchange rate fluctuations between the U.S. dollar and other currencies, which may negatively affect its earnings. A substantial majority of the Company's revenues are denominated in U.S. dollars; however, a significant portion of the expenses associated with the Company's Israeli operations, including personnel, are incurred in NIS. The Company cannot predict any future trends in the exchange rates of the NIS against the U.S. dollar. In addition, exchange rate fluctuations in currency exchange rates in countries other than Israel where the Company operates may also negatively affect the Company's earnings. These currencies currently include the Euro and the British Pound.

The Company has established certain hedging policies to protect itself against the impact of currency fluctuations going forward.

Intellectual Property

Critical to the Company's future is the Company's ability to protect its proprietary technology. The Company relies on a combination of patent, copyright, trademark and trade secret laws in order to protect its intellectual property rights..

The process of seeking patent protection can be long, expensive and sometimes unsuccessful. Therefore, the Company has chosen to file for protection of its intellectual property in certain selected markets, although not in all markets in which the Company sells its products. There can be no assurance that the Company's pending or future patent applications will result in patents being issued or that the Company's existing patents or any future patents which may be granted will provide meaningful protection or commercial

advantages to the Company. A patent only provides partial protection to intellectual property, as much depends on the climate of enforcement within the country granting the patent. In addition, any issued patent may be challenged, invalidated or legally (or illegally) circumvented by third parties, and the Company cannot be certain that its patents will be upheld as valid, be enforceable or prevent the development of competitive products. Moreover, the Company sells and markets its products in some countries; e.g., China, with potentially weak enforcement of intellectual property rights. If competitors are able to develop, manufacture and sell products that directly compete with the Company's products, the Company's sales and gross margins could be adversely affected.

In addition, competitors could purchase one of the Company's systems and attempt to replicate some or all of the competitive advantages the Company derives from its development efforts or design a product based on the Company's protected proprietary technology or develop their own competitive technologies that fall outside of the Company's protected intellectual property rights. If the Company's intellectual property is not adequately protected against use by competitors and other third parties, its competitive position could be eroded and its business could be adversely affected.

In addition to the risks of third-party infringement of the Company's intellectual property, there is also the risk that the Company may inadvertently and innocently infringe on the intellectual property of a third party, which would expose the Company to possible patent infringement claims which are often lengthy and costly disputes. The Company may be required to obtain licenses from third parties or otherwise redesign its products so as not to utilize such intellectual property, which may be uneconomical or otherwise impossible.

Risks Pertaining to Product Liability and Product Warranty

The products developed by the Company may contain latent defects that may only be discovered after the products have been installed and are in use. Such defects could cause a reduction in customers' satisfaction, harm the reputation of the Company or create a need to introduce costly changes to the product. In addition, the Company could be exposed to potential product liability claims. This could involve significant costs to the Company. Although the Company has a Corporate General Liability insurance policy, this policy does not cover costs the Company may incur to change the product, and there is no guarantee that the Company's insurance policy will fully cover any and all types of claims pertaining to product liability or afford coverage to the full extent of such claims that may be filed against the Company.

The Company provides a limited product warranty for the use and operation of its products, many of which also contain components manufactured by third parties. In effect, the Company is warranting components which it does not manufacture. This could give rise to a situation whereby the Company provides a more extensive warranty on these third party components than the Company receives from such third party manufacturers, thus creating some warranty exposure for the Company.

Marketing and Product Risk

The Company spends significant time and money to understand the needs of the market; however, the Company may misjudge market needs. The Company may design products and solutions that do not meet market demands or are not priced correctly or are not delivered to the market in a timely manner. For example, the Company may develop complementary products for its security solution with remote management capabilities which the market deems not to be necessary. If this happens, the Company's costs would increase without a corresponding increase in revenues. This may have a negative impact on the Company's operations and its financial condition.

International Markets

The Company sells its products globally, primarily in Northern & Western Europe, Latin America and Asia. As a result of operating internationally, the Company may face the following risks due to its international operations, any one of which may affect sales or the Company's profitability:

- Changes in governmental requirements and regulations and differences in various countries' requirements;
- Difficulty in collecting accounts receivables;
- Differences in customs in each country;
- Differences in taxation in different countries;
- Political and/or economic instability;
- Disruption in trade caused by civil disturbances and/or war;
- Local labor strikes that affect the Company's ability to sell or deliver products in a particular country; and
- Weakening economies in target markets.

Risks Related to the industry

Changes in Prices of Raw Materials

The raw materials of the Company (mainly electronic, metal and plastic components) are purchased from various suppliers throughout the world. The capacity, supply and demand for such raw materials is subject to cyclical forces and market factors as well and may fluctuate significantly and as a result, the Company may have limited ability to control its costs in securing raw materials. In addition, prices of raw materials may be subject to fluctuation. The Company cannot assure that it will be able to pass on to customers the increased costs associated with the procurement of raw materials. To the extent that increases in costs of raw materials cannot be passed on to customers or there is a delay in passing on the increased costs to customers, the Company is likely to absorb the increase in the cost of raw materials which may materially reduce its margin of profitability.

Delay or Discontinuation in the Supply Finished products

Currently, the Company receives sales forecasts from the majority of its customers. Based on these sales forecasts and incoming orders, the Company purchases finished goods from it

subcontractors needed for sale. The Company generally maintains a sufficient inventory of long lead-time items in order to meet its sales forecasts schedule.

The Company may choose to maintain inventories of products that exceed what is necessary for the short term in order to have a small buffer stock to compensate for shortages or cessation in the supply of components. In such an event, the Company will incur additional costs to maintain this excess inventory, which could affect its gross margins.

Competition and Pressure to Develop New Products

The Company operates in a competitive market environment. Competition, whether direct or indirect, may adversely affect the income and profits of the Company through pressure exerted on prices, the loss of market share or other factors. Some of the Company's current and potential competitors are large companies or conglomerates that have vast resources (including capabilities in the fields of finance, technology, production, marketing and distribution), including, for example, UTC , Tyco, Bosch and Honeywell.

In addition, new competitors, such as service providers, utility companies, cable companies, and non-security distributors, may enter into the competitive market in which the Company operates.

The Company's products deal with evolving technology. The Company must continually invest in product development in order to stay on the cutting edge of technology in its market and secure its market position. The Company's sales may be affected by newer technologies offered by competitors that are not available from the Company.

Risks Related to Israel

Chief Scientist

Certain of the Company's products are developed using financing, in part, provided by the Chief Scientist of the Israel Ministry of Industry and Trade (the "Chief Scientist"), who is responsible for implementing the Israeli government's policy regarding the support and encouragement of industrial research and development.

The participation of the Chief Scientist in R&D expenses is based on certain conditions, unless the Chief Scientist approves a different arrangement .In the event the Company does not comply with the terms of the Chief Scientist grants, the Company may be required to return the grants, which may have a material adverse effect on the Company.

Security, Political and Economic Instability in Israel

The principal offices of the Company are located in Israel. Accordingly, security, political and economic conditions in Israel may directly affect the Company's business. Over the past several decades, a number of armed conflicts have occurred between Israel and its Arab neighbors. Any hostilities involving Israel or the interruption or curtailment of trade between Israel and its present trading partners could adversely affect the Company's operations. However, the ongoing hostilities and violence, future armed conflicts, political developments in other countries in the region or continued or increased terrorism, could disrupt the Company's operations or make conducting the Company's operations in Israel more difficult.

Any of these factors could have the effect of increasing the Company's costs, adversely affecting the Company's financial results and the expansion of the Company's business and delaying deliveries to Customers.

Furthermore, several countries continue to restrict business with Israel, in general, and with Israeli companies, in particular, and this may limit the Company's ability to make sales to these countries. These boycotts and embargos may have an adverse impact on the operations, financial condition or the further expansion of the Company's business.

4. Events after the end of the reporting period

After the end of the Reporting Period, one of the Company's customers claimed reimbursement for the costs he incurred in connection with the upgrade of a product version. The company chose to record the full provision of $265,000 as part of the estimated upgrade cost.

In January 2013 and as a result of the company's strong financial position, the company's bank approved to remove the floating charges.

In March 2013, the audit committee approved the nomination of Mrs. Sharon Sheep as a company director in the Board of Directors.

5. Information on the stock

The issued share capital of the company is NIS 68,564,240 and consists of 13,712,848 ordinary shares at NIS 5.00 par value each. All shares have the same voting rights and dividend claims.

There are no shares in the company with special rights according rights of control.

Under the provisions of German securities trading legislation, every investor whose proportion of the voting rights in the company reaches, exceeds or falls below certain thresholds as a result of the purchase or sale of shares or in any other way must notify the company and the Federal Financial Supervisory Authority (BaFin) thereof. The lowest threshold for such disclosures is 3%. Risco Ltd. currently holds more than 50% of the Company's share capital.

Restrictions on the voting rights of shares could result from statutory provisions. The Company's Board of Directors is not aware of any other restrictions on the exercise of voting rights or the transfer of shares.

The Company's shares are listed in the Prime Standard segment of the Frankfurt Stock exchange.

UPGRADING EVERYDAY SECURITY

6. Outlook

Looking ahead to the business year, the Company expects an increase in revenues of 25% to approximately US$ 18 million, mainly from its strategic customers and markets, in particular, Northern and Western Europe, and from the new product line (ELAS, iConnect 2 way and CommPact). With the increasing revenue, the Company also anticipates a continuously improving earnings situation.

The Company launched a pilot of its cloud-based solution, www.MyELAS.com, among a small group of customers, enabling them to independently register their wireless alarm systems to the cloud and thereby monitor and control their premises as well as receiving images from the motion detector cameras. In addition, customers can manage their installer base via the web admin application.

The Company expects that these new services, in addition to the Smartphone applications for iPhone and Android, will help increase sales of the iConnect and CommPact panels.

The Company continues focusing on its Two-way-wireless iConnect product line and its PIR camera detector with a built-in camera for video verification, in addition to the release of new complimentary products such as the two-way repeater for extending the detectors' range and the two-way vibration detector, all sustaining market expansions and increased sales.

Responsibility Statement

To the best of our knowledge and in accordance with the applicable reporting principles for financial reporting, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company, and the management report of the Company includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal opportunities and risks associated with the expected development of the Company for the remaining months of the financial year.

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Douglas Luscombe	Moshe Alkelai
CEO	Chairman of the Board

Rishon Le Zion, March 21, 2013

ELECTRONICS LINE 3000 LTD.

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2012

U.S. DOLLARS IN THOUSANDS

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of

ELECTRONICS LINE 3000 LTD.

We have audited the accompanying consolidated financial statements of Electronics Line 3000 Ltd. and its subsidiaries ("the Group"), which comprise the consolidated statements of financial position as of December 31, 2012 and 2011, and the consolidated income statements, consolidated statements of comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows for each of the two years then ended, and a summary of significant accounting policies and other explanatory information.
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Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects the financial position of the Group as of December 31, 2012 and 2011, and its financial performance and cash flows for each of the two years then ended, in accordance with International Financial Reporting Standards.

Tel-Aviv, Israel
March 14, 2013

KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

U.S. dollars in thousands

	Note	December 31, 2012	December 31, 2011
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	5	803	1,687
Trade receivables	6	658	2,017
Other accounts receivable	7	170	1,912
Inventories	8	4,042	1,423
Total current assets		5,673	7,039
NON-CURRENT ASSETS:			
Property, plant and equipment:	9		
Cost		4,251	13,858
Less - accumulated depreciation		3,642	13,334
Property, plant and equipment, net		609	524
Intangible assets	10	303	403
Deferred taxes	16e	498	483
Security deposits		17	80
Total non-current assets		1,427	1,490
Total assets		7,100	8,529

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

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

U.S. dollars in thousands

	Note	December 31, 2012	December 31, 2011
LIABILITIES AND EQUITY			
CURRENT LIABILITIES:			
Short-term credit from banks	11	351	1,244
Trade payables	12	1,956	2,796
Other current liabilities	13	811	925
Total current liabilities		3,118	4,965
NON-CURRENT LIABILITIES:			
Loans from banks	14	179	527
Employee benefit liabilities, net	15	143	140
Other long-term liabilities	17c	-	426
Total non-current liabilities		322	1,093
EQUITY:	18		
Share capital		15,933	15,933
Additional paid-in capital		6,584	6,474
Accumulated deficit		(18,857)	(19,936)
Total equity		3,660	2,471
Total liabilities and equity		7,100	8,529

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

March 14, 2013			
Date of approval of the financial statements	Moshe Alkelai Chairman of the Board	Douglas Luscombe President and CEO	Sharon Sheep Responsible for finance

CONSOLIDATED INCOME STATEMENTS

U.S. dollars in thousands, except per share data

	Note	Year ended December 31, 2012	Year ended December 31, 2011
Revenues	20	14,331	24,164
Cost of revenues	21	8,905	15,745
Gross income		5,426	8,419
Operating costs and expenses:			
Research and development	22	1,349	1,733
Selling and marketing	23	1,556	2,878
General and administrative	24	1,678	1,977
Other expenses (income), net	25	(402)	315
Total operating costs and expenses		4,181	6,903
Operating income		1,245	1,516
Financial income	26a	-	51
Financial expenses	26b	166	405
Gain from sale of subsidiary	17c	-	1,224
Income before taxes on income		1,079	2,386
Taxes on income	16b	-	54
Net income		1,079	2,332
Net income per share (basic and diluted)	27	0.08	0.18

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

U.S. dollars in thousands

	Year ended December 31,	
	2012	**2011**
Net income	1,079	2,332
Other comprehensive loss:		
Adjustments arising from translating financial statements of foreign operations	-	(6)
Amounts transferred to the income statement for sale of foreign operation	-	(1,407)
Total other comprehensive loss	-	(1,413)
Total comprehensive income	1,079	919

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

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

U.S. dollars in thousands

	Share capital	Additional paid-in capital	Foreign currency translation reserve	Accumulated deficit	Total equity
Balance as of January 1, 2011	10,933	6,453	1,413	(22,268)	(3,469)
Net income	-	-	-	2,332	2,332
Other comprehensive income:					
Financial statements of foreign operations	-	-	(6)	-	(6)
Amounts transferred to the income statement for sale of foreign operation	-	-	(1,407)	-	(1,407)
Total other comprehensive loss	-	-	(1,413)	-	(1,413)
Total comprehensive income	-	-	(1,413)	2,332	919
Issuance of share capital	5,000	-	-	-	5,000
Cost of share-based payments	-	21	-	-	21
Balance as of December 31, 2011	15,933	6,474	-	(19,936)	2,471
Net income and comprehensive income	-	-	-	1,079	1,079
Cost of share-based payments		110			110
Balance as of December 31, 2012	15,933	6,584	-	(18,857)	3,660

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,	
	2012	**2011**
Cash flows from operating activities:		
Net income	1,079	2,332
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Adjustments to profit or loss items:		
Depreciation and amortization	273	480
Loss (gain) from sale of property, plant and equipment	2	(28)
Increase (decrease) in employee benefit liabilities, net	3	(99)
Cost of share-based payments	110	21
Taxes on income	-	54
Financial expenses, net	128	384
Gain from sale of subsidiary	-	(1,224)
	516	(412)
Changes in operating asset and liability items:		
Decrease (increase) in trade receivables	1,359	(1,033)
Decrease (increase) in other accounts receivable	1,735	(796)
Decrease (increase) in inventories	(2,619)	2,081
Decrease in security deposits	63	-
Decrease in trade payables	(840)	(396)
Decrease in other long-term liabilities	(426)	(775)
Decrease in other current liabilities	(114)	(859)
	(842)	(1,778)
Interest paid	(128)	(384)
Income taxes paid	(8)	(13)
	(136)	(397)
Net cash provided by (used in) operating activities	617	(255)
Cash flows from investing activities:		
Purchase of property, plant and equipment	(274)	(315)
Proceeds from sale of equipment	14	62
Proceeds from sale of investments in previously consolidated subsidiaries (a)	-	2,091
Net cash provided by (used in) investing activities	(260)	1,838

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,	
	2012	2011
Cash flows from financing activities:		
Decrease in short-term bank credit, net	-	(1,243)
Receipt of long-term loans from banks	-	1,054
Receipt of short-term loans from related parties	-	1,183
Repayment of long-term loans from banks	(1,241)	(1,865)
Net cash used in financing activities	(1,241)	(871)
Exchange differences on balances of cash and cash equivalents of foreign operations	-	(8)
Increase (decrease) in cash and cash equivalents	(884)	704
Cash and cash equivalents at beginning of year	1,687	983
Cash and cash equivalents at end of year	803	1,687
Significant non-cash transactions:		
Conversion of shareholders' debt into shares	-	5,000
(a) Proceeds from sale of investments in previously consolidated subsidiaries:		
The subsidiaries' assets and liabilities at date of sale:		
Working capital (excluding cash and cash equivalents)	-	2,024
Property, plant and equipment	-	1,379
Deferred taxes	-	(349)
Non-current liabilities	-	(780)
Foreign currency translation reserve transferred to the income statement	-	(1,407)
Gain from sale of subsidiaries	-	1,224
	-	2,091

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

NOTE 1:- GENERAL

a. Electronics Line 3000 Ltd. ("the Company") was incorporated in Israel in December 2002.

The Company's shares are publicly traded on the Prime Standard, a market operated by the Frankfurt Stock Exchange.

b. The Company is engaged in the design, development, production, marketing and sale of electronic security with remote management solutions, and complementary products for the mass residential and small commercial markets. These solutions can be monitored and enable remote management of the premises for security, and automation and video application. The registered office of the Group is located at 14 Hachoma Street, Rishon LeZion, Israel

c. Definitions:

In these financial statements:

The Company	- Electronics Line 3000 Ltd.
The Group	- The Company and its investees.
Subsidiaries	- Companies that are controlled by the Company (as defined in IAS 27(2008)) and whose accounts are consolidated with those of the Company.
Investees	- Subsidiaries.
Related parties	- As defined in IAS 24.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

The following accounting policies have been applied consistently in the financial statements for all periods presented, unless otherwise stated.

a. Basis of presentation of the financial statements:

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").
The Company's financial statements have been prepared on a cost basis, except for: financial assets and liabilities (including derivatives) which are presented at fair value through profit or loss.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company has elected to present profit or loss items using the function of expense method.

The preparation of the financial statements requires management to make critical accounting estimates as well as exercise judgment in the process of adopting significant accounting policies. The matters which required the exercise of significant judgment and the use of estimates, which have a material effect on amounts recognized in the financial statements, are specified in Note 3 below.

b. Consolidated financial statements:

The consolidated financial statements comprise the financial statements of companies that are controlled by the Company (subsidiaries). Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity. The effect of potential voting rights that are exercisable at the end of the reporting period is considered when assessing whether an entity has control. The consolidation of the financial statements commences on the date on which control is obtained and ends when such control ceases.

The financial statements of the Company and of the subsidiaries are prepared as of the same dates and periods. The consolidated financial statements are prepared using uniform accounting policies by all companies in the Group. Significant intragroup balances and transactions and gains or losses resulting from intragroup transactions are eliminated in full in the consolidated financial statements.

c. Functional currency, presentation currency and foreign currency:

1. Functional currency and presentation currency:

The presentation currency of the financial statements is the U.S. dollar

The Group determines the functional currency of each Group entity, and this currency is used to separately measure each Group entity's financial position and operating results.

When an investee's functional currency differs from the Company's functional currency, that investee represents a foreign operation whose financial statements are translated into the Company's functional currency so that they can be included in the consolidated financial statements.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Assets and liabilities are translated at the closing rate at the end of each reporting period. Goodwill arising from the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities on the date of acquisition of the foreign operation are treated as assets and liabilities of the foreign operation and are translated at the closing rate at the end of each reporting period. Profit or loss items are translated at average exchange rates for all the relevant periods. All resulting translation differences are recognized as a separate component of other comprehensive income (loss) in equity under "foreign currency translation reserve".

Upon the full or partial disposal of a foreign operation resulting in loss of control in the foreign operation, the cumulative gain (loss) from the foreign operation which had been recognized in other comprehensive income is transferred to profit or loss. Upon the partial disposal of a foreign operation which results in the retention of control in the subsidiary, the relative portion of the cumulative amount recognized in other comprehensive income is reattributed to non-controlling interests.

2. Transactions, assets and liabilities in foreign currency:

Transactions denominated in foreign currency are recorded upon initial recognition at the exchange rate at the date of the transaction. After initial recognition, monetary assets and liabilities denominated in foreign currency are translated at the end of each reporting period into the functional currency at the exchange rate at that date. Exchange rate differences, other than those capitalized to qualifying assets or recorded in equity in hedges, are recognized in profit or loss. Non-monetary assets and liabilities measured at cost in foreign currency are translated at the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currency and measured at fair value are translated into the functional currency using the exchange rate prevailing at the date when the fair value was determined.

3. Index-linked monetary items:

Monetary assets and liabilities linked to the changes in the Israeli Consumer Price Index ("Israeli CPI") are adjusted at the relevant index at the end of each reporting period according to the terms of the agreement. Linkage differences arising from the adjustment, as above, other than those capitalized to qualifying assets or recorded in equity in hedges, are recognized in profit or loss.

d. Cash equivalents:

Cash equivalents are considered as highly liquid investments, including unrestricted short-term bank deposits with an original maturity of three months or less from the date of acquisition.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

e. Short-term deposits:

Short-term bank deposits are deposits with an original maturity of more than three months from the date of acquisition. The deposits are presented according to their terms of deposit.

f. Allowance for doubtful accounts:

The allowance for doubtful accounts is determined in respect of specific debts whose collection, in the opinion of the Company's management, is doubtful. The Company also recognizes a provision for groups of customers that are collectively assessed for impairment based on their credit risk characteristics. Impaired debts are derecognized when they are assessed as uncollectible.

g. Inventories:

Inventories are measured at the lower of cost and net realizable value. The cost of inventories comprises costs of purchase and costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated selling costs. The Company periodically evaluates the condition and age of inventories and makes provisions for slow moving inventories accordingly.

Cost of inventories is determined as follows:

Purchased products and raw materials - using the weighted average cost method or using the "first-in, first-out" method.

The Company periodically evaluates the condition and age of inventories and makes provisions for slow-moving inventories accordingly.

h. Revenue recognition:

Revenues are recognized in profit or loss when the revenues can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Company and the costs incurred or to be incurred in respect of the transaction can be measured reliably. In cases where the Company acts as an agent or as a broker without being exposed to the risks and rewards associated with the transaction, its revenues are presented on a net basis. Revenues are measured at the fair value of the consideration received less any trade discounts, volume rebates and returns.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Following are the specific revenue recognition criteria which must be met before revenue is recognized:

Revenues from the sale of goods:

Revenues from the sale of goods are recognized when all the significant risks and rewards of ownership of the goods have passed to the buyer and the seller no longer retains continuing managerial involvement. The delivery date is usually the date on which ownership passes.

Revenues from services:

Revenues from services are recognized by reference to the stage of completion at the end of the reporting period. The stage of completion is measured based on the proportion of actual labor hours incurred to the estimated total labor hours for the entire contract. Where the contract outcome cannot be measured reliably, revenue is recognized only to the extent that the expenses incurred are recoverable.

Customer discounts:

Customer discounts given at the end of the year and in respect of which the customer is not obligated to comply with certain targets, are recognized in the financial statements proportionately as the sales entitling the customer to said discounts are made.

Customer discounts for which the customer is required to meet certain targets, such as a minimum amount of annual purchases (either quantitative or monetary), an increase in purchases compared to previous periods, etc. are recognized in the financial statements in proportion to the purchases made by the customer during the year that qualify for the target, provided that it is expected that the targets will be achieved and the amount of the discount can be reasonably estimated.

i. Taxes on income:

Taxes on income in profit or loss comprise current and deferred taxes. Current or deferred taxes are recognized in profit or loss, except to the extent that the tax arises from items which are recognized directly in other comprehensive income or in equity. In such cases, the tax effect is also recognized in the relevant item.

1. Current taxes:

The current tax liability is measured using the tax rates and tax laws that have been enacted or substantively enacted by the end of reporting period as well as adjustments required in connection with the tax liability in respect of previous years.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

2. Deferred taxes:

Deferred taxes are computed in respect of temporary differences between the carrying amounts in the financial statements and the amounts attributed for tax purposes.

Deferred taxes are measured at the tax rates that are expected to apply when the asset is realized or the liability is settled, based on tax laws that have been enacted or substantively enacted by the end of the reporting period. Deferred taxes in profit or loss represent the changes in the carrying amount of deferred tax balances during the reporting period, excluding changes attributable to items recognized in other comprehensive income or in equity.

Deferred tax assets are reviewed at the end of each reporting period and reduced to the extent that it is not probable that they will be utilized. Temporary differences (such as carryforward losses) for which deferred tax assets had not been recognized are reviewed at the end of each reporting period and a respective deferred tax asset is recognized to the extent that their utilization is probable.

Taxes that would apply in the event of the disposal of investments in investees have not been taken into account in computing deferred taxes, as long as the disposal of the investments in investees is not probable in the foreseeable future. Also, deferred taxes that would apply in the event of distribution of earnings by investees as dividends have not been taken into account in computing deferred taxes, since the distribution of dividends does not involve an additional tax liability or since it is the Company's policy not to initiate distribution of dividends from a subsidiary that would trigger an additional tax liability.

All deferred tax assets and deferred tax liabilities are presented in the statement of financial position as non-current assets and non-current liabilities, respectively. Deferred taxes are offset in the statement of financial position if there is a legally enforceable right to offset a current tax asset against a current tax liability and the deferred taxes relate to the same taxpayer and the same taxation authority.

j. Property, plant and equipment:

Property, plant and equipment are measured at cost, including directly attributable costs, less accumulated depreciation, accumulated impairment losses and any related investment grants and excluding day-to-day servicing expenses. Cost includes spare parts and auxiliary equipment that are used in connection with plant and equipment.

A part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item is depreciated separately.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Depreciation is calculated on a straight-line basis over the useful life of the assets at annual rates as follows:

	%	Mainly %
Machinery and equipment	10 - 15	10
Motor vehicles	15	15
Office furniture and equipment	6 - 33	33
Leasehold improvements	see below	

Leasehold improvements are depreciated on a straight-line basis over the shorter of the lease term (including the extension option held by the Group and intended to be exercised) and the expected life of the improvement.

The useful life, depreciation method and residual value of an asset are reviewed at least each year-end and any changes are accounted for prospectively as a change in accounting estimate.
Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognized. An asset is derecognized on disposal or when no further economic benefits are expected from its use. The gain or loss arising from the derecognition of the asset (determined as the difference between the net disposal proceeds and the carrying amount in the financial statements) is included in profit or loss when the asset is derecognized.

k. Intangible assets:

Expenditures relating to internally generated intangible assets, excluding capitalized development costs, are recognized in profit or loss when incurred. After initial recognition, intangible assets are carried at their cost less any accumulated amortization and any accumulated impairment losses.

Intangible assets with a finite useful life are amortized over their useful life and reviewed for impairment whenever there is an indication that the asset may be impaired. The amortization period and the amortization method for an intangible asset are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for prospectively as changes in accounting estimates. The amortization of intangible assets with finite useful lives is recognized in profit or loss.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Gains or losses arising from the derecognition of an intangible asset are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in profit or loss.

The useful life of intangible assets is as follows:

	Years
Product files	5

Research and development expenditures:

Research expenditures are recognized in profit or loss when incurred. An intangible asset arising from a development project or from the development phase of an internal project is recognized if the Company can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale; the Company's intention to complete the intangible asset and use or sell it; the Company's ability to use or sell the intangible asset; how the intangible asset will generate future economic benefits; the availability of adequate technical, financial and other resources to complete the intangible asset; and the Company's ability to measure reliably the expenditure attributable to the intangible asset during its development.

The asset is measured at cost less any accumulated amortization and any accumulated impairment losses. Amortization of the asset begins when development is complete and the asset is available for use. The asset is amortized over its useful life. Testing of impairment is performed annually over the period of the development project.

l. Impairment of non-financial assets:

The Company evaluates the need to record an impairment of the carrying amount of non-financial assets whenever events or changes in circumstances indicate that the carrying amount is not recoverable. If the carrying amount of non-financial assets exceeds their recoverable amount, the assets are reduced to their recoverable amount. The recoverable amount is the higher of fair value less costs of sale and value in use. In measuring value in use, the expected future cash flows are discounted using a pre-tax discount rate that reflects the risks specific to the asset. The recoverable amount of an asset that does not generate independent cash flows is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in profit or loss.

An impairment loss of an asset, other than goodwill, is reversed only if there have been changes in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. Reversal of an impairment loss, as above, shall not be increased above the lower of the carrying amount that would have been determined (net of depreciation or amortization) had no impairment loss been recognized for the asset in prior years, and its recoverable amount. The reversal of impairment loss of an asset presented at cost is recognized in profit or loss.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The following criteria are applied in assessing impairment of these specific assets:

Development costs capitalized during the development period:

The impairment test is performed annually, on December 31, or more frequently if events or changes in circumstances indicate that there is an impairment

m. Financial instruments:

1. Financial assets:

Financial assets within the scope of IAS 39 are initially recognized at fair value plus directly attributable transaction costs, except for financial assets measured at fair value through profit or loss in respect of which transaction costs are recorded in profit or loss.

After initial recognition, the accounting treatment of financial assets is based on their classification as follows:

a) Financial assets at fair value through profit or loss:

This category includes financial assets held for trading (including derivatives) and financial assets designated upon initial recognition as at fair value through profit or loss.

Embedded derivatives are separated from the host contract and accounted for separately if: (a) the economic characteristics and risks of the embedded derivatives are not closely related to those of the host contract; (b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and (c) the combined instrument is not measured at fair value through profit or loss.

b) Loans and receivables:

Loans and receivables are investments with fixed or determinable payments that are not quoted in an active market. After initial recognition, loans are measured based on their terms at amortized cost less directly attributable transaction costs using the effective interest method and less any impairment losses. Short-term borrowings are measured based on their terms, normally at face value.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

2. Financial liabilities:

Financial liabilities within the scope of IAS 39 are classified as either financial liabilities at fair value through profit or loss, loans at amortized cost or derivatives designated as effective hedging instruments. The Group determines the classification of the liability on the date of initial recognition. All liabilities are initially recognized at fair value. Loans are presented net of directly attributable transaction costs.

After initial recognition, the accounting treatment of financial liabilities is based on their classification as follows:

a) Financial liabilities at amortized cost:

After initial recognition, loans, including debentures, are measured based on their terms at amortized cost less directly attributable transaction costs using the effective interest method. The amortization of the effective interest is recognized in profit or loss in the line item, "financing".

b) Financial liabilities at fair value through profit or loss:

Financial liabilities at fair value through profit or loss include financial liabilities classified as held for trading (including derivatives) and financial liabilities designated upon initial recognition as at fair value through profit or loss.

3. Derecognition of financial instruments:

a) Financial assets:

A financial asset is derecognized when the contractual rights to the cash flows from the financial asset expire or the Company has transferred its contractual rights to receive cash flows from the financial asset or assumes an obligation to pay the cash flows in full without material delay to a third party and has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A transaction involving factoring of accounts receivable and credit card vouchers is derecognized when the abovementioned conditions are met.

If the Company transfers its rights to receive cash flows from an asset and neither transfers nor retains substantially all the risks and rewards of the asset nor transfers control of the asset, a new asset is recognized to the extent of the Company's continuing involvement in the asset. When continuing involvement takes the form of guaranteeing the transferred asset, the extent of the continuing involvement is the lower of the original carrying amount of the asset and the maximum amount of consideration received that the Company could be required to repay.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

b) Financial liabilities:

A financial liability is derecognized when it is extinguished, that is when the obligation is discharged or cancelled or expires. A financial liability is extinguished when the debtor (the Group) discharges the liability by paying in cash, other financial assets, goods or services; or is legally released from the liability.

4. Impairment of financial assets:

The Group assesses at the end of each reporting period whether there is any objective evidence of impairment of a financial asset or group of financial assets as follows.

Financial assets carried at amortized cost:

Objective evidence of impairment exists when one or more events that have occurred after the initial recognition of the asset have a negative impact on the estimated future cash flows. Evidence of impairment may include indications that the debtor is experiencing financial difficulties, including liquidity difficulty and default in interest or principal payments. The amount of the loss recorded in profit or loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred) discounted at the financial asset's original effective interest rate (the effective interest rate computed at initial recognition). If the financial asset has a variable interest rate, the discount rate is the current effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account (see allowance for doubtful accounts above). In a subsequent period, the amount of the impairment loss is reversed if the recovery of the asset can be related objectively to an event occurring after the impairment was recognized. The amount of the reversal, up to the amount of any previous impairment, is recorded in profit or loss.

n. Provisions:

A provision in accordance with IAS 37 is recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. If the Group expects part or all of the expense to be reimbursed to the Company, such as in an insurance contract, the reimbursement is recognized as a separate asset only when it is virtually certain that it will be received by the Company. The expense is recognized in the income statement net of the reimbursed amount.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Following are the types of provisions included in the financial statements:

Legal claims:

A provision for claims is recognized when the Group has a present legal or constructive obligation as a result of a past event, it is more likely than not that an outflow of resources embodying economic benefits will be required by the Group to settle the obligation and a reliable estimate can be made of the amount of the obligation.

o. Employee benefit liabilities:

The Group has several employee benefit plans:

1. Short-term employee benefits:

Short-term employee benefits include salaries, paid annual leave, paid sick leave, recreation and social security contributions and are recognized as expenses as the services are rendered. A liability in respect of a cash bonus or a profit-sharing plan is recognized when the Group has a legal or constructive obligation to make such payment as a result of past service rendered by an employee and a reliable estimate of the amount can be made.

2. Post-employment benefits:

The plans are normally financed by contributions to insurance companies and classified as defined contribution plans or as defined benefit plans.

The Group has defined contribution plans pursuant to Section 14 to the Severance Pay Law under which the Group pays fixed contributions and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient amounts to pay all employee benefits relating to employee service in the current and prior periods. Contributions to the defined contribution plan in respect of severance or retirement pay are recognized as an expense when contributed concurrently with performance of the employee's services.

The Group also operates a defined benefit plan in respect of severance pay pursuant to the Severance Pay Law. According to the Law, employees are entitled to severance pay upon dismissal or retirement. The liability for termination of employment is measured using the projected unit credit method. The actuarial assumptions include rates of employee turnover and future salary increases based on the estimated timing of payment. The amounts are presented based on discounted expected future cash flows using a discount rate determined by reference to yields on Government bonds with a term that matches the estimated term of the benefit obligation.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

In respect of its severance pay obligation to certain of its employees, the Company makes current deposits in pension funds and insurance companies ("the plan assets"). Plan assets comprise assets held by a long-term employee benefit fund or qualifying insurance policies. Plan assets are not available to the Group's own creditors and cannot be returned directly to the Group.

The liability for employee benefits shown in the statement of financial position reflects the present value of the defined benefit obligation less the fair value of the plan assets, less past service costs.

Actuarial gains and losses are recognized in profit or loss in the period in which they occur.

p. Share-based payment transactions:

The Company's employees, other employees of the parent company and the Company’s director are entitled to remuneration in the form of equity-settled share-based payment transactions.

Equity-settled transactions:

The cost of equity-settled transactions with employees, employees of the parent company and its Director is measured at the fair value of the equity instruments granted at grant date. The fair value is determined using an acceptable option pricing model.

The cost of equity-settled transactions is recognized in profit or loss, together with a corresponding increase in equity, during the period which the performance is to be satisfied, ending on the date on which the relevant employees become fully entitled to the award ("the vesting period"). The cumulative expense recognized for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The expense or income recognized in profit or loss represents the change between the cumulative expense recognized at the end of the reporting period and the cumulative expense recognized at the end of the previous reporting period.

No expense is recognized for awards that do not ultimately vest.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

If the Company modifies the conditions on which equity-instruments were granted, an additional expense is recognized for any modification that increases the total fair value of the share-based payment arrangement or is otherwise beneficial to the employee/ employees of the parent company at the modification date.

If a grant of an equity instrument is cancelled, it is accounted for as if it had vested on the cancellation date, and any expense not yet recognized for the grant is recognized immediately. However, if a new grant replaces the cancelled grant and is identified as a replacement grant on the grant date, the cancelled and new grants are accounted for as a modification of the original grant, as described above.

q. Earnings (loss) per share:

Earnings per share are calculated by dividing the net income attributable to equity holders of the Company by the weighted number of Ordinary shares outstanding during the period. Potential Ordinary shares (convertible securities such as convertible debentures, warrants and employee options) are only included in the computation of diluted earnings per share when their conversion decreases earnings per share or increases loss per share from continuing operations. Potential Ordinary shares that are converted during the period are included in diluted earnings per share only until the conversion date and from that date in basic earnings per share. The Company's share of earnings of investees is included based on the earnings per share of the investees multiplied by the number of shares held by the company.

NOTE 3:- SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUPMTIONS USED IN THE PREPARATION OF THE FINANCIAL STATEMENTS

In the process of applying the significant accounting policies, the Group has made the following judgments which have the most significant effect on the amounts recognized in the financial statements:

a. Judgments:

- Determining the fair value of share-based payment transactions:

  The fair value of share-based payment transactions is determined using an acceptable option-pricing model. The model includes data as to the share price and exercise price, and assumptions regarding expected volatility, expected life, expected dividend and risk-free interest rate.

NOTE 3:- SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUPMTIONS USED IN THE PREPARATION OF THE FINANCIAL STATEMENTS (Cont.)

b. Estimates and assumptions:

The preparation of the financial statements requires management to make estimates and assumptions that have an effect on the application of the accounting policies and on the reported amounts of assets, liabilities, revenues and expenses. Changes in accounting estimates are reported in the period of the change in estimate.

The key assumptions made in the financial statements concerning uncertainties at the end of the reporting period and the critical estimates computed by the Group that may result in a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

- Legal claims:

  In estimating the likelihood of outcome of legal claims filed against the Company and its investees, the companies rely on the opinion of their legal counsel. These estimates are based on the legal counsel's best professional judgment, taking into account the stage of proceedings and legal precedents in respect of the different issues. Since the outcome of the claims will be determined in courts, the results could differ from these estimates.

- Deferred tax assets:

  Deferred tax assets are recognized for unused carryforward tax losses and deductible temporary differences to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

- Development costs:

  In testing impairment of development costs, management makes assumptions regarding the expected cash flows from the asset being developed, the discount rate and the expected period of benefits.

NOTE 4:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION

IAS 19 (Revised) - Employee Benefits:

The IASB made several changes to IAS 19, the principal of which are as follows:

- The remeasurement of the net defined benefit liability (formerly - actuarial gains and losses) are recognized in other comprehensive income t and not in profit or loss.
- The "corridor" approach which allowed the deferral of actuarial gains or losses has been eliminated.
- Income from the plan assets is recognized in profit or loss based on the discount rate used to measure the employee benefit liabilities. The return on plan assets excluding the aforementioned income recognized in profit or loss is included in the remeasurement of the net defined benefit liability.
- The distinction between short-term employee benefits and long-term employee benefits is based on the expected settlement date and not on the date on which the employee first becomes entitled to the benefits.
- Past service cost arising from changes in the plan is recognized immediately.

The Standard is to be applied retrospectively in financial statements for annual periods commencing on January 1, 2013, or thereafter. Earlier application is permitted.

The Company estimates that the Standard is not expected to have a material impact on its financial statements.

NOTE 5:- CASH AND CASH EQUIVALENTS

Composition by currency:

	December 31,	
	2012	2011
U.S. dollars	588	1,119
Euros	69	91
GBP	41	144
NIS	105	333
	803	1,687

NOTE 6:- TRADE RECEIVABLES

a. Composition:

	December 31, 2012	December 31, 2011
Open accounts	735	2,098
Checks receivable	-	3
	735	2,101
Less - allowance for doubtful accounts	77	84
Trade receivables, net	658	2,017

Impaired debts are accounted for through recording an allowance for doubtful accounts.

Trade receivables are non-interest bearing and are generally for 60-90 day terms.

b. The movements in the allowance for doubtful accounts were as follows:

	Individually impaired
At January 1, 2011	394
Charge for the year	8
Reversal of collected doubtful accounts	(33)
Derecognition of bad debts	(273)
Deconsolidated Company	(12)
At December 31, 2011	84
Charge for the year	7
Reversal of collected doubtful accounts	(10)
Derecognition of bad debts	(4)
At December 31, 2012	77

c. An analysis of past due but not impaired trade receivables (allowance for doubtful accounts), trade receivables, net, with reference to reporting date:

	Neither past due nor impaired	Past due but not impaired				Total
		< 30 days	30 - 60 days	60 -90 days	> 90 day	
December 31, 2012	220	348	23	5	62	658
December 31, 2011	1,337	615	32	26	7	2,017

NOTE 7:- OTHER ACCOUNTS RECEIVABLE

	December 31,	
	2012	2011
Prepaid expenses	42	110
Advances to suppliers	4	1,412
Government authorities	96	390
Other receivables	28	-
	170	1,912

NOTE 8:- INVENTORIES

	December 31,	
	2012	2011
Finished products	3,086	1,270
Raw materials	352	-
	3,438	1,270
Inventory in transit	604	153
	4,042	1,423

The provisions for slow-moving inventories as of December 31, 2012 and 2011 are $ 1,288 and $ 1,579, respectively.

NOTE 9:- PROPERTY, PLANT AND EQUIPMENT

a. Composition and movement:

	Building	Installations and leasehold improvements	Machinery and equipment	Motor vehicles	Office furniture and equipment	Total
Cost:						
Balance at January 1, 2011	1,392	5,915	5,013	72	3,515	15,907
Acquisitions during the year	-	-	201	12	102	315
Disposals during the year	-	-	(787)	(44)	-	(831)
Currency translation differences	10	-	-	-	-	10
Deconsolidated company	(1,402)	-	-	-	(141)	(1,543)
Balance at December 31, 2011	-	5,915	4,427	40	3,476	13,858
Assets fully depreciated and no longer in use	-	(5,905)	(3,736)	(40)	(146)	(9,827)
Acquisitions during the year	-	-	257	-	17	274
Disposals during the year	-				(54)	(54)
Balance at December 31, 2012	-	10	948	-	3,293	4,251
Accumulated depreciation:						
Balance at January 1, 2011	36	5,736	4,906	56	3,186	13,920
Provision during the year	27	170	42	11	129	379
Disposals during the year	-	-	(771)	(26)	-	(797)
Currency translation differences	(1)	-	-	(1)	(1)	(3)
Deconsolidated company	(62)	-	-	-	(103)	(165)
Balance at December 31, 2011	-	5,906	4,177	40	3,211	13,334
Assets fully depreciated and no longer in use	-	(5,905)	(3,736)	(40)	(146)	(9,827)
Provision during the year		1	96	-	76	173
Disposals during the year	-	-	-	-	(38)	(38)
Balance at December 31, 2012	-	2	537	-	3,103	3,642
Depreciated cost at December 31, 2012	-	8	411	-	190	609
Depreciated cost at December 31, 2011	-	9	250	-	265	524

NOTE 9:- PROPERTY, PLANT AND EQUIPMENT (Cont.)

b. In 2010 and 2011 the Company accelerated the depreciation expenses in respect to leasehold improvements and machinery and equipment over the expected useful period, which is due to the Company's decision to vacate the buildings of the Company's plant and administration and the decision to cease self manufacturing.

As a result of the depreciation acceleration, the Company recorded in 2011 an expense in the approximate amount of $ 131.

NOTE 10:- INTANGIBLE ASSETS

Internal development costs of production files that have been capitalized are composed as follows:

	December 31,	
	2012	**2011**
Cost:		
As of January 1	504	504
Amortizations	(201)	(101)
As of December 31	303	403

The intangible assets became available for use in 2011 and are being depreciated over a period of 5 years.

NOTE 11:- SHORT-TERM CREDIT FROM BANKS

a. Composition:

	Annual interest rate *)	December 31,	
		2012	**2011**
	%		
Current maturities of long-term loans (see note 14)	LIBOR + 3.5	351	1,244

b. Liens:
As of the balance sheet date the Company has two floating charges (a non specific lien on all assets of the Company on which there is no previous specific lien) on its assets in favor of one of the Company’s banks.
After the balance sheet date, in January, 2013, the Company removed one of the floating charges.

NOTE 12:- TRADE PAYABLES

	December 31, 2012	December 31, 2011
Open accounts	1,956	2,794
Checks payable	-	2
	1,956	2,796

Trade payables are non-interest bearing and generally have terms of 60-90 days.

NOTE 13:- OTHER CURRENT LIABILITIES

	December 31, 2012	December 31, 2011
Accrued expenses	155	193
Accrued salaries and related expenses	270	249
Onerous contract	-	405
Others	386	78
	811	925

NOTE 14:- LOANS FROM BANKS

a. Composition:

	Average interest rate (1)	December 31, 2012	December 31, 2011
	%		
U.S. dollars	LIBOR + 1.7 (2)	-	884
U.S. dollars	LIBOR + 3.5 (2)	530	887
		530	1,771
Less - current maturities		351	1,244
		179	527

NOTE 14:- LOANS FROM BANKS (Cont.)

(1) As of December 31, 2012, the effective interest rate is equal to the average interest rate.

(2) As of December 31, 2012, three-months LIBOR is 0.3% (2011 - 0.58%).

b. In May 2011 the Company entered into agreement with its main bank regarding new covenant as follows:

- Tangible equity to balance sheet ratio – at least 20% as of December 31, 2012 and onwards.

- Debt to EBITDA ratio - will not be more than 4 as of December 31, 2012 and December 31, 2013 and will not be more than 3 as of December 31, 2014 and onwards.

- Operating profit - a positive operating profit in each four consecutive quarters starting from January 1, 2011.

As of December 31, 2012 the Company is meeting its bank covenants.

c. According to their original contractual terms, the long-term loans are repayable in future years, as follows:

	December 31, 2012
First year - 2013	351
Second year - 2014	179
	530

NOTE 15:- EMPLOYEE BENEFIT LIABILITIES, NET

Employee benefits consist of short-term benefits and post-employment benefits.

Post-employment benefits:

According to the labor laws and Severance Pay Law in Israel, the Company is required to pay compensation to an employee upon dismissal or retirement or to make current contributions in defined contribution plans pursuant to Section 14 to the Severance Pay Law, as specified below. The Company's liability is accounted for as a post-employment benefit. The computation of the Company's employee benefit liability is made in accordance with a valid employment contract based on the employee's salary and employment term which establish the entitlement to receive the compensation.

The post-employment employee benefits are normally financed by contributions classified as defined benefit plans or as defined contribution plans, as detailed below.

a. Defined contribution plans:

Section 14 to the Severance Pay Law, 1963 applies to part of the compensation payments, pursuant to which the fixed contributions paid by the Group into pension funds and/or policies of insurance companies release the Group from any additional liability to employees for whom said contributions were made. These contributions and contributions for compensation represent defined contribution plans.

	Year ended December 31,	
	2012	**2011**
Expense in respect of defined contribution plans	81	97

b. Defined benefit plans:

The Company accounts for that part of the payment of compensation that is not covered by contributions in defined contribution plans, as above, as a defined benefit plan for which an employee benefit liability is recognized and for which the Company deposits amounts in central severance pay funds and in qualifying insurance policies.

NOTE 15:- EMPLOYEE BENEFIT LIABILITIES, NET (Cont.)

1. Expenses recognized in the statement of income:

	Year ended December 31,	
	2012	2011
Current service cost	16	17
Interest cost on benefit obligation	24	57
Expected return on plan assets	(18)	(48)
Net actuarial loss recognized in the year	1	180
Total employee benefit expenses	23	206
Actual return on plan assets	36	(2)

2. The plan assets, net:

	December 31,	
	2012	2011
Defined benefit obligation	570	565
Fair value of plan assets	(427)	(425)
Total liabilities, net	143	140

3. Changes in the present value of defined benefit obligation:

	2012	2011
Balance at January 1,	565	2,015
Interest cost	24	57
Current service cost	16	17
Benefits paid	(66)	(1,557)
Net actuarial loss	19	86
Exchange differences	12	(53)
Balance at December 31,	570	565

NOTE 15:- EMPLOYEE BENEFIT LIABILITIES, NET (Cont.)

4. Plan assets:

a) Plan assets comprise assets held by a long-term employee benefit fund and qualifying insurance policies.

b) The movement in the fair value of the plan assets:

	2012	2011
Balance at January 1,	425	1,776
Expected return	18	48
Benefits paid	(43)	(1,261)
Net actuarial gain (loss)	18	(94)
Exchange differences	9	(44)
Balance at December 31,	427	425

5. The principal actuarial assumptions used are as follows:

	December 31,	
	2012	2011
Discount rate	4%	4.4%
Future salary increase	5%	5%

NOTE 16:- TAXES ON INCOME

a. Tax laws applicable to the Company:

1. Income Tax (Inflationary Adjustments) Law, 1985:

According to the law, until 2007, the results for tax purposes were adjusted for the changes in the Israeli CPI.

In February 2008, the "Knesset" (Israeli parliament) passed an amendment to the Income Tax (Inflationary Adjustments) Law, 1985, which limits the scope of the law starting 2008 and thereafter. Since 2008, the results for tax purposes are measured in nominal values, excluding certain adjustments for changes in the Israeli CPI carried out in the period up to December 31, 2007. Adjustments relating to capital gains such as for sale of property (betterment) and securities continue to apply until disposal. Since 2008, the amendment to the law includes, among others, the cancellation of the inflationary additions and deductions and the additional deduction for depreciation (in respect of depreciable assets purchased after the 2007 tax year).

NOTE 16:- TAXES ON INCOME (Cont.)

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

   The Company has the status of an "industrial company", as implied by this law. According to this status and by virtue of regulations published thereunder, the Company is entitled to claim a deduction of accelerated depreciation on equipment used in industrial activities, as determined in the regulations issued under the Inflationary Law.

b. Tax rates applicable to the Company

1. The Israeli corporate tax rate was 25% in 2010, 24% in 2011 and 25% in 2012.

   A company is taxable on its real (non-inflationary) capital gains at the corporate tax rate in the year of sale. A temporary provision for 2006-2009 stipulates that the sale of an asset other than a quoted security (excluding goodwill that was not acquired) that had been purchased prior to January 1, 2003, and sold by December 31, 2009, is subject to corporate tax as follows: the part of the real capital gain that is linearly attributed to the period prior to December 31, 2002 is subject to the corporate tax rate in the year of sale as set forth in the Israeli Income Tax Ordinance, and the part of the real capital gain that is linearly attributed to the period from January 1, 2003, through December 31, 2009, is subject to tax at a rate of 25%.

   On December 5, 2011, the Israeli Parliament (the Knesset) passed the Law for Tax Burden Reform (Legislative Amendments), 2011 ("the Law") which, among others, cancels effective from 2012, the scheduled progressive reduction in the corporate tax rate. The Law also increases the corporate tax rate to 25% in 2012. In view of this increase in the corporate tax rate to 25% in 2012, the real capital gains tax rate and the real betterment tax rate were also increased accordingly.

   The effect of the abovementioned change on the financial statements is immaterial.

2. The principal tax rates applicable to the subsidiaries whose place of incorporation is outside Israel are:

   Company incorporated in England - tax at the rate of 26% in 2011.

c. Tax assessments:

   The Company has not received final tax assessments since its incorporation, however, the assessments of the Company are deemed final through 2008.

NOTE 16:- TAXES ON INCOME (Cont.)

d. Deferred taxes:

The deferred taxes are reflected in the statement of financial position as follows:

	December 31, 2012	December 31, 2011
Non-current assets	498	483

Deferred tax assets are computed at an average tax rate of approximately 25% and 24% for 2012 and 2011, respectively.

The Company recorded deferred tax assets, principally for tax loss carryforwards and also for other temporary differences, as of December 31, 2012 and 2011 in the amount of $ 498 and $ 483, respectively (see e below). The deferred tax assets were recorded based on the Company's management best estimation of realization of these losses and temporary differences in the foreseeable future.

e. Changes in deferred taxes:

	Year ended December 31, 2012	Year ended December 31, 2011
Balance at the beginning of the year	483	112
Change during the year	15	34
Adjustment of deferred tax balances following change in exchange rate	-	(12)
Deconsolidation Company	-	349
Balance at the end of the year	498	483

NOTE 16:- TAXES ON INCOME (Cont.)

f. Taxes on income included in statements of income:

	December 31,	
	2012	2011
Current taxes	-	88
Deferred taxes	-	(34)
	-	54

g. Theoretical tax:

The reconciliation between the tax expense, assuming that all the income and expenses, gains and losses in the statement of income were taxed at the statutory tax rate and the taxes on income recorded in profit or loss is as follows:

	Year ended December 31,	
	2012	2011
Income before taxes on income	1,079	2,386
Taxes computed at statutory tax rate of 25% (2011- 24%)	270	573
Increase (decrease) in tax due to:		
Non-deductible expenses	20	12
Exempt income	-	(338)
Cost of share-based payments	28	5
Utilization of previously unrecognized tax losses and other items *)	(318)	(198)
	-	54

*) Including differences in the basis of measurement (U.S.$ - NIS) - amount represents the difference resulting from the basis of measurement for income tax purposes in Israel (calculated based on the New Israeli Shekel) and the measurement currency of the Company (the U.S. dollars).

NOTE 16:- TAXES ON INCOME (Cont.)

h. Carryforward losses for tax purposes:

The Company's carryforward losses for tax purposes as of December 31, 2012 and 2011 amount to approximately $ 15,936 and $ 16,253, respectively. With respect to tax losses carryforward of approximately $ 13,944 and $ 14,321, no deferred tax asset was recognized as of December 31, 2012 and 2011, respectively.

NOTE 17:- COMMITMENTS AND CONTINGENT LIABILITIES

a. Royalties:

1. The Company is obligated to pay royalties of 2%-3.5% of the revenues from products in the development of which the Chief Scientist participated. The royalties are limited to the amount of the grant received, linked to the U.S dollar. Total grants received as of December 31, 2012 and 2011 amounted to approximately $ 1,670. The balance of contingent royalties is approximately $ 1,238. Since the Company does not manufacture and sell the products for which it had received the grants, it does not expect to pay additional royalties in the future, therefore no liability was included in the financial statements.

   Under the conditions of an agreement for participation by the Bi-National Fund for Research and Development ("BIRD") in joint R&D programs between the Group and a U.S. company, BIRD granted grants to the Group. In consideration for this grant, BIRD is entitled to royalties of between 2.5% and 5% of the gross sales of products resulting from this research, up to the amount of the grant, linked to the U.S dollar. Thereafter, BIRD will be entitled to royalties of 2.5% of sales up to an additional amount equaling half of the grant received. On January 1, 2003, the benefits and the obligations deriving from this agreement were transferred to the Company from Metis. The grants received by the Company and the balance of contingent royalties as of December 31, 2012 and 2011 amounted to approximately $ 340. It was also agreed with BIRD that should one of the companies register a patent on a product developed, the Group will also pay royalties to BIRD at the rate of 1.5% of the gross sales of the product resulting from the research, for the duration of the patent.

   Since the Company does not manufacture and sell the products for which it had received the grants, it does not expect to pay additional royalties in the future, therefore no liability was included in the financial statements.

NOTE 17:- COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

b. Operating leases:

The Company entered into agreements with Metis to lease the plant and administration building until 2021 and 2024, respectively. The Company had an option to cancel the part of the leases in 2011 and 2014, respectively. The rent was linked to the higher of the change in Israel's CPI or the exchange rate of the NIS in relation to the U.S. dollar. Certain of the leases have escalation clauses.

During 2010 following the Company's decision to vacate its plant and administration buildings, the Company recognized the remaining obligation of lease expenses.

In February 2011, the Company utilized its option and canceled the lease agreement for 2 out of 4 floors in the plant building, as agreed.

In December 2011, the Company and the administration building landlord signed settlement agreement terminating the lease agreement immediately.

In June 2012, the Company and the plant landlord signed a settlement agreement terminating the lease agreement immediately. According to the settlement agreement the Company paid the landlord $ 292 to remove any future claims regarding the rental payments. During the reported period the Company recorded other income in the amount of $ 404.

As of the balance sheet date, the Company has no obligation regarding any future lease payments related to the administration and the plant buildings.

c. Sale of subsidiary:

On November 28, 2011, the Company sold its UK subsidiary in a Management Buyout transaction.

Under the Management Buyout agreement, the Company receives a consideration of GBP 1.8 million which was paid in cash at the closing date.

NOTE 18:- EQUITY

a. The share capital is composed as follows:

	December 31, 2012		December 31, 2011	
	Authorized	Issued and outstanding	Authorized	Issued and outstanding
	Number of shares			
Ordinary shares of NIS 5 par value each	50,000,000	13,712,848	50,000,000	13,712,848

The authorized share capital of the Company is NIS 250,000,000 comprised of 50,000,000 authorized Ordinary shares, par value NIS 5 each.

b. Stock Option Plan:

1. In June 8, 2005, the Company's Board of Directors adopted a share option plan according to which up to 290,735 options exercisable into Ordinary shares of the Company may be granted to officers, directors, employees and consultants of the Group.

2. In May 9, 2006, the BOD resolved to increase the number of shares available for option grants under the June 2005 share option plan up to 500,000 options.

3. In June 14, 2011 additional allocation of 330,000 options to the Company's CEO, directors and top management of Risco Ltd., the controlling shareholders, was approved by the audit committee and the board of directors. The final approval by the Company's share holders was received on October 10, 2011.

4. In July 2012, the nomination of certain director, who was previously granted options, was terminated. Consequently, 50,000 options were forfeited

   Measurement of the fair value of equity-settled share options:

   The Company uses the Binomial model when estimating the grant date fair value of equity-settled share options. The measurement was made at the grant date of equity-settled share options since the options were granted to employees.

   The following table lists the inputs to the binomial model used for the fair value measurement of equity-settled share options for the above plan:

Dividend yield	0%
Expected volatility of the share prices	77.3%
Risk-free interest rate	1.89%
Expected life of share options	10 years
Share price	€ 1.010

NOTE 18:- EQUITY (Cont.)

Based on the above inputs, the fair value of the options was determined at $ 212 (€ 164) at the grant date.

The options granted will expire 10 years after the date of grant and vest over a period of 3 years. The exercise price of the options granted is € 1.5.

The expected life of the share options is based on historical data and is not necessarily indicative of the exercise patterns of share options that may occur in the future.

The expected volatility of the share prices reflects the assumption that the historical volatility of the share prices is reasonably indicative of expected future trends.

4. Movement during the year:

The following table illustrates the number and weighted average exercise prices (WAEP) of, and movements in, share options during the years:

	Year ended December 31,			
	2012		2011	
	Number of options	WAEP (U.S.$)	Number of options	WAEP (U.S.$)
Share options outstanding at beginning of year	541,181	3.25	216,059	5.32
Share options granted during the year	-	-	330,000	1.94
Share options forfeited during the year	(50,000)	1.94	(4,878)	6.59
Share options outstanding at end of year	491,181	3.38	541,181	3.25
Share options exercisable at end of year	294,768	4.18	201,435	5.22

5. During 2012 and 2011, the employment of certain officers and employees of the Company, who were previously granted options, was terminated. Consequently, 50,000 and 4,878 of the options were forfeited, respectively.

Total expenses of share-based payments amounted to $ 110 and $ 21 for 2012 and 2011, respectively.

NOTE 19:- FINANCIAL INSTRUMENTS

a. The financial assets and financial liabilities in the statement of financial position are classified by groups of financial instruments pursuant to IAS 39:

	December 31,	
	2012	2011
Financial assets:		
Financial assets at fair value through profit or loss:		
Derivatives	27	-
Loans and receivables	658	2,017
Financial liabilities:		
Financial liabilities measured at amortized cost	2,641	5,573
Financial liabilities at fair value through profit or loss:		
Derivatives	-	18

b. Financial risks factors:

The Company's activities expose it to various financial risks such as market risk (foreign exchange risk and interest rate risk), credit risk and liquidity risk. The Company comprehensive risk management plan focuses on activities that reduce to a minimum any possible adverse effects on the Group's financial performance.

The Company's management oversees the risks in accordance with the policies approved by the Board.

1. Market risks:

a) Foreign exchange risk:

The Company operates in a large number of countries and is exposed to foreign exchange risk resulting from the exposure to different currencies. Foreign exchange risk arises on forward commercial transactions, recognized assets and liabilities that are denominated in a foreign currency other than the functional currency. Accounting department is responsible for managing the net position of each foreign currency by the use of forward exchange contracts and other hedging tools.

Management's policy is to hedge between 40% and 70% of forecasted transactions in every principal currency over the next 12 months.

NOTE 19:- FINANCIAL INSTRUMENTS (Cont.)

The Company has forward foreign currency contracts and cylinder transactions to manage some of its transactions exposure to fluctuations in exchange rates. These forward foreign currency contracts and cylinder transactions are not designated as cash flow, fair value or net investment hedges and are entered into the periods consistent with the periods of currency transaction exposure. Such derivatives do not qualify for hedge accounting.

As of December 31, 2012 and 2011, the Company's monetary liabilities in NIS exceeded monetary assets by $ 372 and $ 2,149, respectively.

As of December 31, 2012 and 2011, the Company's monetary assets in Euro exceeded monetary assets by $ 136 and $ 291, respectively.

As of December 31, 2012 and 2011, the Company's monetary assets in GBP exceeded monetary assets by $ 235 and $ 917, respectively.

b) Interest rate risk:

The Group is exposed to the risk of changes in the market interest rates on long-term loans with floating interest rates.

2. Credit risk:

The Company monitors and reduces its credit risk by using a policy to ensure collection through sales of its products to wholesalers with an appropriate credit history and by insuring the customers who received a credit line.

Credit risk may arise from the exposure of holding several financial instruments with a single entity or from entering into transactions with several groups of debtors with similar economic characteristics whose ability to discharge their obligations will be similarly affected by changes in economic or other conditions. Factors that have the potential of creating concentrations of risks consist of the nature of the debtors' activities, such as their business sector, the geographical area of their operations and the financial strength of groups of borrowers.

The Company regularly monitors the credit extended to its customers. The Company provides an allowance for doubtful accounts based on the factors that affect the credit risk of certain customers, past experience and other information.

3. Liquidity risk:

The Group monitors its risk to a shortage of funds using a monthly and daily budget tool.

The Company’s objective is to maintain a balance between continuity of funding and flexibility through the use of bank overdrafts and bank loans.

NOTE 19:- FINANCIAL INSTRUMENTS (Cont.)

The maturities of the financial liabilities of the Company are for one year, except for the bank loans. The long-term loans are repayable in future years based on contractual undiscounted payments, as follows:

	December 31, 2012
First year - 2013	2,462
Second year - 2014	179
	2,641

c. Fair value:

The carrying amount of cash and cash equivalents, trade receivables, other accounts receivable, credit from banks, trade payables and other accounts payable approximate their fair value.

d. Classification of financial instruments by fair value hierarchy:

The financial instruments presented in the balance sheet at fair value are with similar characteristics using the following fair value hierarchy which is determined based on observable market data (valuation techniques which use inputs that are not based on observable market data).

Financial assets measured at fair value:

	December 31,	
	2012	2011
Financial assets at fair value through profit or loss:		
Derivatives	27	-

Financial liabilities measured at fair value:

	December 31,	
	2012	2011
Financial liabilities at fair value through profit or loss:		
Derivatives	-	18

NOTE 19:- FINANCIAL INSTRUMENTS (Cont.)

e. Sensitivity tests relating to changes in market factors:

	December 31,	
	2012	**2011**
Sensitivity test to changes in the NIS exchange rate:		
Gain (loss) from the change:		
Increase of 5% in the NIS rate	(82)	(204)
Decrease of 5% in the NIS rate	82	204
Sensitivity test to changes in the Euro exchange rate:		
Gain (loss) from the change:		
Increase of 5% in the Euro rate	7	15
Decrease of 5% in the Euro rate	(7)	(15)
Sensitivity test to changes in the GBP exchange rate:		
Gain (loss) from the change:		
Increase of 5% in the GBP rate	12	46
Decrease of 5% in the GBP rate	(12)	(46)

NOTE 20:- REVENUES

	Year ended December 31,	
	2012	**2011**
Foreign:		
Europe	12,115	22,363
Americas	550	458
Other countries	1,634	1,316
	14,299	24,137
Domestic - Israel	32	27
	14,331	24,164
Includes sales to one major customer	2,652	5,007

NOTE 21:- COST OF REVENUES

	Year ended December 31,	
	2012	2011
Purchases and changes in raw materials	10,604	11,747
Labor	432	1,157
Manufacturing and other expenses	499	689
Depreciation	96	147
	11,631	13,740
Changes in inventories of finished products and work-in-progress	(2,726)	2,005
	8,905	15,745

NOTE 22:- RESEARCH AND DEVELOPMENT EXPENSES

	Year ended December 31,	
	2012	2011
Salaries and related expenses	557	707
Amortization	100	101
Consulting fees	630	827
Other	62	98
	1,349	1,733

NOTE 23:- SELLING AND MARKETING EXPENSES

	Year ended December 31,	
	2012	2011
Salaries and related expenses	900	1,840
Advertising	100	330
Foreign travel and transportation	188	338
Other	368	370
	1,556	2,878

NOTE 24:- GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended December 31,	
	2012	2011
Salaries and related expenses	644	678
Management and consulting fees	427	324
Depreciation	75	111
Other	532	864
	1,678	1,977

NOTE 25:- OTHER EXPENSES, NET

	Year ended December 31,	
	2012	2011
Capital loss (gain) on sale of property, plant and equipment	2	(27)
Onerous contract	-	211
Accelerated depreciation (see Note 9b)	-	131
Other income (see Note 17b)	(404)	-
	(402)	315

NOTE 26:- FINANCIAL INCOME AND EXPENSES

	Year ended December 31,	
	2012	2011
a. Financial income:		
Foreign exchange differences	-	40
Other	-	11
	-	51
b. Financial expenses:		
Bank borrowings, net	128	387
Other	38	18
	166	405

NOTE 27:- NET PROFIT (LOSS) PER SHARE

The following reflects the net loss and share data used in the basic and diluted net loss per share computations:

	Year ended December 31, ,	
	2012	2011
Profit attributable to Ordinary shares for computing basic and diluted net loss per share	1,079	2,332
Weighted average number of Ordinary shares for computing basic net profit (loss) per share	13,712,848	13,002,848
Adjusted weighted average number of Ordinary shares for computing diluted profit (loss) per share	13,712,848	13,002,848

In the calculation of the diluted net profit per share for the years ended December 31, 2012 and 2011, all share options were not taken into account because of the anti-dilutive effect.

NOTE 28:- BALANCES AND TRANSACTIONS WITH RELATED PARTIES

a. Balances with related parties:

	December 31,	
	2012	2011
Trade payables – Parent company (Risco)	(1,048)	(2,437)
Trade receivable – Fellow subsidiary	194	-
Key management personnel (including directors)	(26)	(40)

b. Transactions with related parties:

	December 31,	
	2012	2011
Manufacturing services agreement (see d 2 below):		
Raw material sales *)	(115)	(2,306)
Purchases of finished goods	4,571	4,299
Management service agreement (see d 1 below)	300	300
Interest due from line of credit (see d 4 below)	-	25
Research and development services (see f below)	592	747
Distribution agreement (see d 3 below)	(1,989)	-
Key management personnel (including directors)	223	251

*) Based on Company's cost used for manufacturing.

NOTE 28:- BALANCES AND TRANSACTIONS WITH RELATED PARTIES (Cont.)

c. On July 10, 2012 the Company's audit committee and board of directors approved a settlement agreement with the Company's previous management. According to the settlement agreement, the Company paid its previous management an amount of $ 86 to remove any future claims regarding to management's services provided according to past service agreement.

d. After approval by the Company's audit committee, the shareholders, in a special general meeting on August 12, 2010, approved the agreement that the Company had entered into with Risco, which includes the following:

1. Management services agreement - Risco is willing to exert its efforts and utilize its professional connections in order to assist the Company in the following fields: (i) sales administration services; (ii) IT and computerized systems; (iii) finance management and accounting; (iv) human resource; (v) directors and consulting services; (vi) legal and company secretarial services.

   The Company shall pay Risco for all services rendered by it under this agreement, payable not less often than monthly and in accordance with the Company's normal and reasonable payment payroll practices regarding service providers, an annual gross amount of $ 300. The annual amount shall be adjusted on a yearly basis in accordance with the change in the Company's revenues from sales compared to the revenue from sales of the preceding year, but in any event shall not be less than the base amount.

2. Manufacturing services agreement – the Company wishes to retain Risco services for the purpose of manufacturing certain products of the Company, on a non-exclusive basis. Prices shall be provided by the service provider, and agreed on by the parties.

3. Distribution agreement - Risco has the facilities to import, promote, sell, market and distribute the products in the territory (as defined in the agreement) and is willing to act as the supplier's non-exclusive distributor of the products in the territory. The distributor and supplier intend that the transfer prices for the products, shall be, in the aggregate for all products for each calendar year, at arm's length prices.

4. The Company received a line of credit, in the amount of up to $ 6,500 from Risco. Any amount taken by the Company from the line of credit shall bear an annual interest of LIBOR+2.5%, charged on a quarterly basis. As of December 31, 2011, the Company converted the credit line to equity as part of Private placement for Risco, see e below.

NOTE 28:- BALANCES AND TRANSACTIONS WITH RELATED PARTIES (Cont.)

e. In a private placement effected on March 14, 2011, the Company issued 3,550,000 Ordinary shares of the Company to the controlling shareholder, Risco Ltd., at a price per share of NIS 5.00, for a total consideration of NIS 17,750 thousand (approximately $ 5,000) which was to through conversion of outstanding credit line to equity. The private placement was approved in a special general meeting of the Company's shareholders that took place on February 16, 2011.

f. After approved by the Company's audit committee and the Company's shareholders, on June 16, 2011, the Company had entered into an R&D service agreement with a service provider controlled by the controlling shareholder of the Company's largest and controlling shareholder.

g. After approved by the Company's audit committee, the shareholders, in a special general meeting on October 10, 2012 approved an amendment to the Distribution agreement with Risco (see d 3 above). According to the amendment the Company will have the option to distribute Risco products.

NOTE 29:- GEOGRAPHIC INFORMATION

Revenues reported in the financial statements derive from the Company's country of domicile (Israel) and foreign countries based on the location of the customers, are as follows:

	Year ended December 31,	
	2012	**2011**
Israel	32	27
Europe	12,115	22,363
Other foreign countries	2,184	1,774
	14,331	24,164

The carrying amounts of non-current assets (property, plant and equipment and intangible assets) in the Company's country of domicile (Israel) and in foreign countries based on the location of the assets, are as follows:

	December 31,	
	2012	**2011**
Israel	579	927
Foreign countries	333	-
	912	927

NOTE 30:- SIGNIFICANT EVENTS AFTER THE REPORTED PERIOD

After the reported period, one of the Company's customers claimed reimbursement for the costs he incurred in connection with the upgrade of product version. The Company decided to record the full provision of $265K as part of the estimated upgrade cost.

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