ORAD HI-TEC SYSTEMS LTD. AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2005

U.S. DOLLARS IN THOUSANDS

INDEX

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REPORT OF INDEPENDENT AUDITORS

To the Shareholders of

ORAD HI-TEC SYSTEMS LTD.

We have audited the accompanying consolidated balance sheets of Orad Hi-Tec Systems Ltd. ("the Company") and its subsidiaries as of December 31, 2005 and 2004 and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2005. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We did not audit the financial statements of certain wholly-owned subsidiaries, whose assets constitute 6% and 7% of total consolidated assets as of December 31, 2005 and 2004, respectively, and whose revenues constitute 10%, 15% and 6% of total consolidated revenues for the years ended December 31, 2005, 2004 and 2003, respectively. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for those companies, is based solely on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2005 and 2004, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

Tel-Aviv, Israel
March 12, 2006

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

CONSOLIDATED BALANCE SHEETS

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

	December 31, 2004	December 31, 2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 4,752	$ 5,338
Restricted cash	750	500
Trade receivables (net of allowance for doubtful accounts of $ 443 and $ 378 at December 31, 2004 and 2005, respectively)	4,154	3,754
Other accounts receivable and prepaid expenses	910	719
Inventories	3,646	2,817
Work in process, net of advances from customers	1,063	466
Total current assets	15,275	13,594
SEVERANCE PAY FUND	773	817
PROPERTY AND EQUIPMENT, NET	2,195	1,914
Total assets	$ 18,243	$ 16,325
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Trade payables	$ 1,761	$ 1,262
Deferred revenues	741	1,201
Other accounts payable and accrued expenses	3,280	4,182
Total current liabilities	5,782	6,645
ACCRUED SEVERANCE PAY	1,103	1,173
SHAREHOLDERS' EQUITY:		
Share capital:		
Ordinary shares of NIS 0.01 par value:		
Authorized - 27,000,000 shares as of December 31, 2004 and 2005; Issued and outstanding - 10,750,726 shares as of December 31, 2004 and 10,790,621 shares as of December 31, 2005	28	28
Additional paid-in capital	75,241	75,281
Foreign currency translation adjustments	(547)	(547)
Accumulated deficit	(63,364)	(66,255)
Total shareholders' equity	11,358	8,507
Total liabilities and shareholders' equity	$ 18,243	$ 16,325

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

March 12, 2006		
Date of approval of the financial statements	Avi Sharir Director and Chief Executive Officer	Ehud Ben Yair Chief Financial Officer

CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Year ended December 31,		
	2003	2004	2005
Revenues:			
Sales	$ 15,439	$ 15,728	$ 14,485
Long-term development contracts	-	-	916
Total revenues	15,439	15,728	15,401
Cost of revenues:			
Cost of sales	5,608	6,188	5,287
Cost of long-term development contracts	-	-	1,047
Total cost of revenues	5,608	6,188	6,334
Gross profit	9,831	9,540	9,067
Operating expenses:			
Research and development, net	3,502	2,844	2,300
Sales and marketing	8,296	8,224	6,813
General and administrative	2,700	2,388	2,529
Amortization of deferred share compensation results from business combination	784	-	-
Total operating expenses	15,282	13,456	11,642
Operating loss	5,451	3,916	2,575
Financial income (expenses), net	433	189	(316)
Other expenses, net	333	148	-
Loss before minority interest in losses of a subsidiary	5,351	3,875	2,891
Minority interest in losses of a subsidiary	199	-	-
Net loss	$ 5,152	$ 3,875	$ 2,891
Basic and diluted net loss per share	$ 0.49	$ 0.36	$ 0.27
Weighted average number of shares used in computing basic and diluted net loss per share (in thousands)	10,582	10,698	10,781

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share data

	Number of outstanding Ordinary shares	Share capital	Additional paid-in capital	Warrants	Deferred share compensation	Foreign currency translation adjustments	Accumulated deficit	Total
Balance as of January 1, 2003	10,562,280	$ 28	$ 74,682	$ 425	$ (784)	$ (547)	$ (54,337)	$ 19,467
Comprehensive loss:								
Net loss	-	-	-	-	-	-	(5,152)	(5,152)
Total comprehensive loss								(5,152)
Amortization of deferred share compensation	-	-	-	-	784	-	-	784
Issuance of shares related to acquisition of Xync GmbH	88,446	*) -	-	-	-	-	-	*) -
Expiration of warrants	-	-	425	(425)	-	-	-	-
Balance as of December 31, 2003	10,650,726	28	75,107	-	-	(547)	(59,489)	15,099
Comprehensive loss:								
Net loss	-	-	-	-	-	-	(3,875)	(3,875)
Total comprehensive loss								(3,875)
Compensation expenses in respect of share options whose terms have been modified	-	-	38	-	-	-	-	38
Issuance of shares upon exercise of employee share options	100,000	*) -	96	-	-	-	-	96
Balance as of December 31, 2004	10,750,726	28	75,241	-	-	(547)	(63,364)	11,358
Comprehensive loss:								
Net loss	-	-	-	-	-	-	(2,891)	(2,891)
Total comprehensive loss								(2,891)
Issuance of shares upon exercise of employee share options	11,250	*) -	9	-	-	-	-	9
Issuance of earn-out shares	28,645	*) -	31	-	-	-	-	31
Balance as of December 31, 2005	10,790,621	$ 28	$ 75,281	$ -	$ -	$ (547)	$ (66,255)	$ 8,507

*) Represent an amount lower than $ 1.

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,		
	2003	**2004**	**2005**
Cash flows from operating activities:			
Net loss	$ (5,152)	$ (3,875)	$ (2,891)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation	1,534	1,091	623
Amortization of deferred share compensation	784	-	-
Compensation expense in respect of share options whose terms have been modified	-	38	-
Decrease in trade receivables, net and other accounts receivable and prepaid expenses	510	890	591
Decrease in inventories	262	234	591
Decrease (increase) in work in process, net of advances from customers	(825)	277	597
Increase (decrease) in trade payables, other accounts payable and accrued expenses and accrued severance pay, net	(88)	(592)	429
Increase in deferred revenues	34	217	460
Other	1	28	31
Net cash provided by (used in) operating activities	(2,940)	(1,692)	431
Cash flows from investing activities:			
Purchase of property and equipment	(156)	(298)	(231)
Proceeds from sale of property and equipment	32	88	127
Decrease (increase) in restricted cash	(23)	(227)	250
Net cash provided by (used in) investing activities	(147)	(437)	146
Cash flows from financing activities:			
Short-term bank credit, net	(30)	-	-
Payment of long-term bank loan	(116)	(16)	-
Issuance of shares upon exercise of employee share options	-	96	9
Net cash provided by (used in) financing activities	(146)	80	9
Increase (decrease) in cash and cash equivalents	(3,233)	(2,049)	586
Cash and cash equivalents at beginning of year	10,034	6,801	4,752
Cash and cash equivalents at end of year	$ 6,801	$ 4,752	$ 5,338
Supplemental disclosure of cash flows activities:			
Cash received during the year for:			
Interest, net	$ 94	$ 62	$ 109

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

NOTE 1:- GENERAL

Orad Hi-Tec Systems Ltd. ("the Company") was incorporated in 1993. The Company and its subsidiaries provide innovative real-time video processing technologies for TV broadcasting, internet, production studio and sports events. The Company also develops and markets high-end three dimensional graphical computer platforms for the visual simulation and virtual reality markets.

The Company operates through its wholly-owned subsidiaries in the United States, France, Poland, Germany, the Netherlands, the United Kingdom, Spain, Israel and Hong-Kong. During 2004, the Company became a sole owner of its Hong-Kong subsidiary (previously held 60% of the subsidiary's shares). These subsidiaries are engaged in the development, selling and marketing of the Company's products. The Company sells its products directly and through its subsidiaries and its distribution networks worldwide.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP").

a. Use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

b. Financial statements in U.S. dollars:

A majority of the revenues of the Company and its subsidiaries are generated in U.S. dollars ("dollar"). In addition, a substantial portion of the Company's and its subsidiaries' costs are incurred in dollars. A substantial portion of the Company's funds are held in U.S. dollars. The Company's management believes that the dollar is the currency of the primary economic environment in which the Company and its subsidiaries operate. Thus, the functional and reporting currency of the Company and its subsidiaries is the dollar.

Accordingly, monetary assets, and liabilities and transactions in currencies other than the dollar are remeasured into U.S. dollars in accordance with Statement of Financial Accounting Standards No. 52, "Foreign Currency Translation" ("SFAS No. 52"). All transactions gains and losses from the remeasurement are reflected in the consolidated statements of operations as financial income or expenses, as appropriate.

c. Principles of consolidation:

The consolidated financial statements include the accounts of the Company and its subsidiaries. Intercompany balances and transactions have been eliminated upon consolidation.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

d. Cash equivalents:

Cash equivalents are short-term highly liquid investments that are readily convertible to cash with original maturities of three months or less.

e. Restricted cash:

Restricted cash is primarily invested in highly liquid deposits, which are used as a security for sales agreements and office lease agreements.

f. Inventories:

Inventories are stated at the lower of cost or market value. Inventory write-offs are provided to cover risks arising from slow-moving items, technological obsolescence, excess inventories and discontinued products.

Cost is determined as follows:

Raw materials, parts and supplies - by the moving average method.

Products in process and finished products:
Raw materials, parts and supplies - by the moving average method.
Subcontracting costs - on the basis of actual costs.

g. Property and equipment:

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is calculated by the straight-line method over the estimated useful lives of the assets at the following annual rates:

	%
Computers and peripheral equipment	20 - 33
Office furniture and equipment	6 - 15
Motor vehicles	15
Leasehold improvements	Over the shorter of the term of the lease or the life of the asset

The Company leases under operating leases computers and peripheral equipment, mobile broadcasting and demonstrating units ("leased equipment") to its customers. Leased equipment is stated at cost, net of accumulated depreciation. Depreciation is calculated by the straight-line method over the estimated useful lives of the assets (three years).

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

h. Impairment of long-lived assets:

The Company's and its subsidiaries' long-lived assets are reviewed for impairment in accordance with Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS No. 144"), whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the future undiscounted cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. As of December 31, 2005, no impairment losses have been identified.

i. Revenue recognition:

The Company and its subsidiaries generate revenues mainly from sales of systems, software licenses, development contracts and from operating leases of equipment. The Company and its subsidiaries also generate revenues from maintenance and support, training and installation.

The Company and its subsidiaries implement Statement of Position No. 97-2, "Software Revenue Recognition" ("SOP No. 97-2"), as amended. Revenues from systems sales are recognized upon delivery of the system or upon installation at the customer site, where applicable, provided that collection is probable, the system fee is fixed or determinable and persuasive evidence of an arrangement exists. In cases where a significant installation is required after the delivery of the system, revenues from the system are deferred until the installation occurs. Revenues in arrangements with multiple deliverables are recognized under the “residual method” when Vendor Specific Objective Evidence ("VSOE") of fair value exists for all undelivered elements, no VSOE exists for the delivered elements, and all other revenue recognition criteria are satisfied. The Company's and its subsidiaries' VSOE used to allocate the sales price to maintenance, support and training is based on renewal ratio or the price charged when these elements will be sold separately.

Revenues from development contracts are recognized based on SOP No. 81-1, "Accounting for Performance of Construction Type and Certain Production Type Contracts", using contract accounting on the completed-contract method or when applicable, as specific milestones are met. A provision for estimated losses on uncompleted contracts is recorded in the period in which such losses are first identified, in the amount of the estimated loss on the entire contract. As of December 31, 2005, a provision for losses in the amount of $ 200 was recorded.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Maintenance and support revenue included in multiple element arrangements is deferred and recognized on a straight-line basis over the term of the maintenance and support agreement.

Revenues from training and installation included in multiple element arrangements are recognized at the time they are rendered.

Revenues from operating leases of equipment are recognized ratably over the lease period, in accordance with Statement of Financial Accounting Standards No. 13, "Accounting for Leases" ("SFAS No. 13").

The Company and its subsidiaries generally do not grant a right of return to their customers.

Deferred revenue includes amounts received from customers but not recognized as revenues.

j. Warranty costs:

The Company offers a one year warranty for all of its systems. Provision for warranty costs is provided at the time revenues are recognized, for estimated material costs during the warranty period based on the Company's experience.

k. Research and development costs:

Research and development costs are charged to the statement of operations as incurred.

l. Non-royalty-bearing-grants:

Non-royalty-bearing grants from the European Union for funding of approved research and development projects are recognized at the time the Company is entitled to such grants, on the basis of the costs incurred. These grants are presented as a reduction of research and development expenses. During the years 2003, 2004, 2005, the Company received grants in the amount of $ 0, $ 0 and $ 141, respectively.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

m. Royalty-bearing grants:

Royalty-bearing grants from the Government of Israel for funding of approved research and development projects are recognized at the time the Company is entitled to such grants, on the basis of the costs incurred. These grants are presented as a reduction of research and development expenses. During the years 2003, 2004, 2005, no development grants were received.

n. Income taxes:

The Company and its subsidiaries account for income taxes in accordance with Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS No. 109"). This Statement prescribes the use of the liability method whereby deferred tax assets and liabilities are determined based on the differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company and its subsidiaries provide a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value.

o. Concentrations of credit risks:

Financial instruments that potentially subject the Company and its subsidiaries to concentrations of credit risk consist principally of cash and cash equivalents, restricted cash, work in process, net of advances from customers and trade receivables.

Cash and cash equivalents and restricted cash are mainly invested in U.S. dollars with major banks in Luxemburg and in Israel. Management believes that the financial institutions that hold the Company's investments are financially sound and, accordingly, minimal credit risk exists with respect to these investments.

Work in process, net of advances from customers is derived from long term development contracts. The Company performs ongoing credit evaluations of its customers. A provision for estimated losses on uncompleted contracts is recorded in the period in which such losses are first identified, in the amount of the estimated loss on the entire contract.

Trade receivables are mainly derived from sales to customers located primarily in Europe, Asia, North America and South America. The Company performs ongoing credit evaluations of its customers. An allowance for doubtful accounts is determined with respect to those amounts that the Company and its subsidiaries have determined to be doubtful of collection.

As of December 31, 2004 and 2005, the Company and its subsidiaries have no significant off-balance-sheet concentration of credit risk such as forward exchange contracts, option contracts or other foreign hedging arrangements.

p. Severance pay:

The Company's liability for severance pay for its Israeli employees is calculated pursuant to the Israeli severance pay law based on the most recent salary of the employees multiplied by the number of years of employment, as of the balance sheet date. Employees are entitled to one month's salary for each year of employment or a portion thereof.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company's liability for all of its employees is fully provided by monthly deposits with insurance policies and by an accrual.

The deposited funds include profits accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfillment of the obligation pursuant to Israeli severance pay law or labor agreements. The value of the deposited funds is based on the cash surrender value of the insurance policies.

Severance expenses for the years ended December 31, 2004 and 2005, amounted to approximately $ 585 and $ 244, respectively.

q. Basic and diluted net loss per share:

Basic net loss per share is computed based on the weighted average number of Ordinary shares outstanding during each year. Diluted net loss per share is computed based on the weighted average number of Ordinary shares outstanding during each year, plus dilutive potential Ordinary shares considered outstanding during the year, in accordance with Statement of Financial Accounting Standards No. 128, "Earnings per Share" ("SFAS No. 128").

r. Fair value of financial instruments:

The carrying amounts of cash and cash equivalents, restricted cash, trade receivables, other accounts receivable and prepaid expenses, trade payables and other accounts payable and accrued expenses approximate their fair value due to the short-term maturity of such instruments.

s. Accounting for share-based compensation:

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and FASB Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation" ("FIN No. 44") in accounting for its employee share option plans. Under APB No. 25, when the exercise price of the Company's share options is less than the market price of the underlying share on the date of grant, compensation expense is recognized.

The Company adopted the disclosure provisions of Financial Accounting Standards Board Statement No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure" ("SFAS No. 148"), which amended certain provisions of SFAS No. 123 "Accounting for Stock Based Compensation" ("SFAS No. 123") to provide alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. The Company continues to apply the provisions of APB No. 25, in accounting for stock-based compensation.

Pro forma information regarding net loss and net loss per share is required by SFAS No. 123, and has been determined as if the Company had accounted for its employee share options under the fair value method of that Statement. The fair value for these options was estimated at the grant date using the Black and Scholes option pricing model with the following weighted average assumptions for the years ended December 31, 2003 and 2005 (no options were granted during 2004): risk-free interest rates of 1.50% and 4.36%, respectively, dividend yields of 0% for each year;

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

a volatility factor of the expected market price of the Company's Ordinary shares of 68% and 69%, respectively; a weighted-average expected life of the option of 4 years for each year. Weighted average fair values of options at their grant dates in 2003 and 2005 were $ 0.59 and $ 0.65, respectively. All options were granted with an exercise price equal to the fair market value at the date of grant.

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods.

Pro forma information under SFAS No. 123:

	Year ended December 31,		
	2003	**2004**	**2005**
Net loss as reported	$ (5,152)	$ (3,875)	$ (2,891)
Add: share-based compensation expense included in reported net loss	784	38	-
Deduct: share-based compensation expense determined under fair value method	(1,538)	(227)	(63)
Pro forma net loss	$ (5,906)	$ (4,064)	$ (2,954)
Basic and diluted net loss per share as reported	$ (0.49)	$ (0.36)	$ (0.27)
Pro forma basic and diluted net loss per share	$ (0.56)	$ (0.38)	$ (0.27)

On December 16, 2004, the FASB issued Statement No. 123 (revised 2004), "Share-Based Payment" ("SFAS No. 123(R)"), which is a revision of SFAS No. 123. Generally, the approach in SFAS 123(R) is similar to the approach described in Statement 123. However, SFAS No. 123 permitted, but not required, share-based payments to employees to be recognized based on their fair values while SFAS No. 123(R) requires all share-based payments to employees to be recognized based on their fair values. SFAS No. 123(R) also revises, clarifies and expands guidance in several areas, including measuring fair value, classifying an award as equity or as a liability and attributing compensation cost to reporting periods. SFAS 123 (R) will be effective for periods commencing January 1, 2006. SFAS No. 123(R) permits public companies to adopt its requirements using one of two methods:

(i) a "modified prospective" method in which compensation cost is recognized beginning with the effective date (a) based on the requirements of Statement SFAS No. 123(R) for all share-based payments granted after the effective date and (b) based on the requirements of SFAS No. 123 for all awards granted to employees prior to the effective date of SFAS No. 123(R) that remain unvested on the effective date.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

(ii) a "modified retrospective" method which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under SFAS No. 123 for purposes of pro forma disclosures.

The Company is now evaluating which method to adopt. Therefore, the Company can not assess whether the adoption of SFAS No. 123(R) will have a material effect on its financial position and results of operations.

t. Impact of recently issued accounting standards:

In November 2004, the FASB issued Statement of Financial Accounting Standards No. 151, "Inventory Costs, an Amendment of ARB No. 43, Chapter 4" ("SFAS No. 151"). SFAS No. 151 amends Accounting Research Bulletin ("ARB") No. 43, Chapter 4, to clarify that abnormal amounts of idle facility expense, freight handling costs and wasted materials (spoilage) should be recognized as current-period charges. In addition, SFAS 151 No. requires that the allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The Company does not expect that the adoption of SFAS No. 151 will have a material effect on its financial position or results of operations.

In May 2005, the FASB issued Statement of Financial Accounting Standard No. 154 ("SFAS 154"), "Accounting Changes and Error Corrections", a replacement of APB No. 20, "Accounting Changes" and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements". SFAS 154 provides guidance on the accounting for and reporting of accounting changes and error corrections. APB No. 20 previously required that most voluntary changes in accounting principles be recognized by including in net income for the period of the change the cumulative effect of changing to the new accounting principle. SFAS 154 requires retroactive application to prior periods' financial statements of a voluntary change in accounting principles unless it is impracticable. SFAS 154 is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

u. Reclassification:

In 2005, certain amounts from prior years have been reclassified to conform to the current year's presentation. The reclassification had no effect on previously reported net loss or shareholders' equity.

U.S. dollars in thousands

NOTE 3: - OTHER ACCOUNTS RECEIVABLE AND PREPAID EXPENSES

	December 31, 2004	December 31, 2005
Government authorities	$ 356	$ 285
Prepaid expenses	255	264
Other	299	170
	$ 910	$ 719

NOTE 4:- INVENTORIES

	2004	2005
Raw materials	$ 1,146	$ 719
Products in process and finished products	2,500	2,098
	$ 3,646	$ 2,817

Inventory write-off provision expense recorded in 2003, 2004 and 2005 amounted to $ 381, $ 190 and $ 469, respectively. The write-offs are included in cost of revenues.

NOTE 5:- WORK IN PROCESS, NET OF ADVANCES FROM CUSTOMERS

	December 31, 2004	December 31, 2005
Work in process	$ 2,494	$ 1,923
Advances from customers	(1,431)	(1,257)
Provision for losses	-	(200)
	$ 1,063	$ 466

NOTE 6:- PROPERTY AND EQUIPMENT

	2004	2005
Cost:		
Computers and peripheral equipment	$ 7,415	$ 7,621
Office furniture and equipment	270	348
Motor vehicles	617	203
Leasehold improvements	2,357	2,340
	10,659	10,512
Accumulated depreciation:		
Computers and peripheral equipment	6,892	7,066
Office furniture and equipment	179	200
Motor vehicles	365	103
Leasehold improvements	1,028	1,229
	8,464	8,598
Depreciated cost	$ 2,195	$ 1,914

Depreciation expense amounted to $ 1,534, $ 1,091 and $ 623 for the years ended December 31, 2003, 2004 and 2005, respectively.

U.S. dollars in thousands

NOTE 7: - OTHER ACCOUNTS PAYABLE AND ACCRUED EXPENSES

	December 31,	
	2004	2005
Employees and payroll accruals	$ 876	$ 759
Accrued expenses	2,054	2,839
Government authorities	82	289
Warranty provision	225	250
Other	43	45
	$ 3,280	$ 4,182

NOTE 8:- COMMITMENTS AND CONTINGENT LIABILITIES

a. Royalty commitments:

1. Royalties to the Office of the Chief Scientist ("OCS"):

Under the Company's research and development agreements with the OCS and pursuant to applicable laws, the Company is required to pay royalties at the rate of 4.5% of sales of products developed with funds provided by the OCS, up to an amount equal to 100% of the OCS research and development grants received, linked to the dollar. The Company is obligated to repay the Israeli Government for the grants received only to the extent that there are sales of the funded products.

Royalties’ expenses amounted to $ 220, $ 197 and $ 217 for the years ended December 31, 2003, 2004 and 2005, respectively, relating to the repayment of such grants.

As of December 31, 2005, the Company had a contingent obligation to pay royalties in the amount of $ 2,576.

2. Royalty obligation to the Marketing Fund of the Government of Israel:

The Israeli Government, through the Fund for the Encouragement of Marketing Activities, awarded the Company grants for participation in foreign marketing expenses. The Company is committed to pay royalties at the rate of 4% of the increase in foreign sales, up to an amount equal to 100% of the grant received plus interest.

Royalties’ expenses amounted to $ 43, $ 144 and $ 194 for the years ended December 31, 2003, 2004 and 2005, respectively, relating to the repayment of such grants.

As of December 31, 2005, the Company had a contingent obligation to pay royalties in the amount of $ 331.

U.S. dollars in thousands

NOTE 8:- COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

b. Operating leases:

The Company and its subsidiaries lease their facilities under various operating lease agreements, which expire on various dates. Aggregate minimum rental commitments under non-cancelable leases as of December 31, 2005, are as follows:

2006	$ 545
2007	446
2008	443
2009 and thereafter	1,447
	$ 2,881

Total rental expense for the years ended December 31, 2003, 2004 and 2005, amounted to $ 627, $ 695 and $ 565, respectively.

c. Liens:

As of December 31, 2005, fixed pledges on bank accounts in the amount of $ 500 were recorded to secure sales agreements and office lease agreements.

d. Litigation:

Claims have been lodged against the Company in respect of various matters in the ordinary course of business and legal proceedings in respect thereof are under way. The Company's management is of the opinion, based upon the opinions of the legal advisors handling the claims, that the likelihood of the claims to prevail is remote.

NOTE 9:- SHAREHOLDERS' EQUITY

The Company's shares are listed for trading on the Frankfurt Stock Exchange (Prime Standard) and on the Alternative Investment Market ("AIM") in the London Stock Exchange, both under the symbol "OHT".

a. Ordinary shares:

Ordinary shares confer upon their holders voting rights, the right to receive cash dividends, and the right to a share in excess assets upon liquidation of the Company.

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

NOTE 9:- SHAREHOLDERS' EQUITY (Cont.)

b. Employee share option plan:

1. In 1996, the Company approved an employee share option plan, which was expanded in 2000 and 2002. Under the expanded plan, 974,465 options to purchase Ordinary shares have been reserved for issuance. These options may be granted to directors, officers and employees of the Company and its subsidiaries and are mainly vested as follows: 50% after two years, 25% after the third year and 25% after the fourth year starting from the date of grant. If not exercised, the options will expire on the tenth anniversary of the date of grant. Any options, which are canceled or forfeited before expiration, become available for future grants.

   During 2003, the Company approved a new share option plan ("the 2003 Share Option Plan"). The Company's Board of Directors approved treating shares allotment under the 1996 Employee Share Option Plan as being reserved for allotment under the 2003 Share Option Plan.

   Total amount of options available for future grants as of December 31, 2005 amounted to 250,599.

2. A summary of the Company's options activity, and related information is as follows:

	Year ended December 31,					
	2003		2004		2005	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at the beginning of the year	531,384	$ 11.19	711,635	$ 8.09	455,934	$ 8.86
Granted	240,000	$ 1.17	-	$ -	25,000	$ 1.19
Exercised	-	$ -	(100,000)	$ 0.96	(11,250)	$ 0.88
Canceled or forfeited	(59,749)	$ 8.82	(155,701)	$ 10.40	(15,100)	$ 3.65
Outstanding at the end of the year	711,635	$ 8.09	455,934	$ 8.86	454,584	$ 8.81
Exercisable at the end of the year	309,208	$ 14.65	298,892	$ 12.83	366,251	$ 10.64

The following table summarizes information about options outstanding and exercisable as of December 31, 2005:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 9:- SHAREHOLDERS' EQUITY (Cont.)

Range of exercise price	Options outstanding as of December 31, 2005	Weighted average remaining contractual life (years)	Weighted average exercise price	Options exercisable as of December 31, 2005	Weighted average exercise price of options exercisable
$ 0.8 - 0.96	122,500	7.10	$ 0.94	72,500	$ 0.92
$ 1.19 - 1.77	88,000	6.67	$ 1.61	63,000	$ 1.77
$ 2.14 - 5.75	95,344	6.22	$ 2.56	82,011	$ 2.61
$ 9.08 - 11.71	38,522	2.32	$ 10.36	38,522	$ 10.36
$ 20.71 - 29.64	54,218	3.98	$ 21.53	54,218	$ 21.53
$ 33.18 - 34.95	56,000	4.13	$ 34.61	56,000	$ 34.61
	454,584	5.69	$ 8.81	366,251	$ 10.64

All of the options granted to employees officers and directors in 2003, and 2005 (no options were granted during 2004), have an exercise price equal to the fair market value of the share at date of grant. During 2004, the Company's Board of Directors determined to accelerate vesting for 100,000 options held by one of the Company's senior officers, who resigned from his job. Accordingly, the Company recorded compensation expense in respect of these options whose terms have been modified for a total compensation amount of $ 38.

c. Acquisition of Art Technologies GmbH ("Art"):

According to the purchase agreement with Art, the issuance of 57,290 Ordinary shares was conditional upon achieving certain revenue targets from the product developed by Art ("contingent shares"). During 2002, upon achievement of certain of the revenue targets, 28,645 of the contingent shares with a fair value of $ 54 were issued. During 2003 and 2004, certain of the revenue targets were not achieved in the prescribed time frame and therefore, the remaining 28,645 shares were not issued. However, the Company agreed to issue such shares during 2005, and accordingly, the remaining 28,645 shares with a fair value of $ 31 were issued.

d. Acquisition of Xync GmbH ("Xync"):

On November 16, 2000, the Company acquired all the outstanding shares of Xync, a German based corporation. The purchase agreement included a clause for the continued employment of most of the shareholders of Xync in the acquired company, for a period of thirty months, after the date of the acquisition, in exchange for additional restricted Ordinary shares of the Company, during the period. During 2003, all the restricted shares were released from trust. The Company recorded compensation expenses over the employment period.

Compensation expenses amounted to $ 784, $ 0 and $ 0 for the years ended December 31, 2003, 2004 and 2005, respectively.

e. Dividends:

Dividends, if any, will be paid in New Israeli Shekels ("NIS"). Dividends paid to shareholders outside Israel may be converted to U.S. dollars on the basis of the exchange rate prevailing at the date of the conversion. The Company does not intend to pay cash dividends in the foreseeable future.

NOTE 10:- INCOME TAXES

a. Domestic - Israeli income taxes:

1. Measurement of taxable income under the Income Tax (Inflationary Adjustments) Law, 1985:

   Results for tax purposes are measured in terms of earnings in NIS after certain adjustments for increases in the Israeli Consumer Price Index ("CPI"). As explained in Note 2b, the financial statements are measured in U.S. dollars. The difference between the annual change in the Israeli CPI and in the NIS/dollar exchange rate causes a further difference between taxable income and the income before taxes shown in the financial statements. In accordance with paragraph 9(f) of SFAS No. 109, the Company has not provided deferred income taxes on the difference between the functional currency and the tax basis of assets and liabilities.

2. Tax rates:

   On July 25, 2005, the Knesset (Israeli Parliament) approved the Law for the Amendment of the Income Tax Ordinance (No. 147), 2005, which prescribes, among others, a gradual decrease in the corporate tax rate in Israel to the following tax rates: in 2006 - 31%, in 2007 - 29%, in 2008 - 27%, in 2009 - 26% and in 2010 and thereafter - 25%. The amendment is not expected to have a material effect on the Company's financial position and results of operations.

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

   The Company's production facilities in Israel have been granted an "Approved Enterprise" status under the above law. Four expansion programs of the Company have been granted the status of an "Approved Enterprise". According to the provisions of such Israeli law, the Company has been granted an "Alternative Benefit" status, under which the main benefits are tax exemption and a reduced tax rate. Consequently, the Company's income derived from the "Approved Enterprise" is tax exempt for a period of two years and for an additional period of five to eight years is subject to a reduced tax rate of 20% - 25% (based on the percentage of foreign ownership in each taxable year).

   The Company completed implementation of its first, second and third expansion programs in 1996, 1999 and in 2000, respectively. The fourth program has not yet been completed.

   The period of tax benefits, detailed above, is subject to limits of the earlier of 12 years from the commencement of production, or 14 years from the approval date.

NOTE 10:- INCOME TAXES (Cont.)

The entitlement to the above benefits is conditional upon the fulfillment of the conditions stipulated by the above law, regulations published thereunder and the instruments of approval for the specific investments in "Approved Enterprises". In the event of failure to comply with these conditions, the benefits may be canceled and the Company may be required to refund the amount of the benefits, in whole or in part, including interest.

If the retained tax-exempt profits are distributed, they would be taxed at the corporate tax rate applicable to such profits as if the Company had not elected the alternative system of benefits, currently 20%-25% for an "Approved Enterprise". As of December 31, 2005, accumulated deficit included approximately $ 6,150 of tax exempt profits earned by the Company's "Approved Enterprises". The Company has decided not to distribute dividends out of such tax-exempt profits. Accordingly, no deferred income taxes have been provided on income attributable to the Company's "Approved Enterprise".

Income from sources other than the "Approved Enterprise" during the benefit period will be subject to the tax at the regular rate.

4. Tax benefits under the Law for the Encouragement of Industry (Taxes), 1969:

The Company is an "Industrial Company", as defined by this law and, as such, is entitled to certain tax benefits, mainly accelerated depreciation of machinery and equipment, as prescribed by regulations published under the Inflationary Adjustments Law and the right to deduct public issuance expenses and amortization of intangible property rights for tax purposes.

b. Tax assessments:

The Company has obtained final tax assessments from the Israeli Tax Authorities for the tax years through 2002.

NOTE 10:- INCOME TAXES (Cont.)

c. Stamp duty:

An amendment of the Stamp Duty on Documents Law, 1961, or the Stamp Duty Law, came into effect on June 1, 2003 determining, among other things, that the Stamp Duty on most agreements shall be paid by the parties that signed such agreement, jointly or severally, or by the party that undertook under such agreement to pay the Stamp Duty. The Stamp Duty Law determined that a document (or part thereof) that is signed in Israel or relates to an asset or obligation in Israel would be subject to a tax rate between 0.4% and 1% of the value of the subject matter of such document. The Company's management believes that an adequate provision to cover this exposure has been provided.

Under an order published in December 2005, said requirements to pay Stamp Duty were cancelled with respect to documents signed on or after January 1, 2006.

d. Net operating carryforward losses:

The Company has accumulated losses for tax purposes as of December 31, 2005, in the amount of approximately $ 12,900 which may be carried forward and offset against taxable income in the future for an indefinite period.

The carryforward losses of the Israeli subsidiary, amounting to approximately $ 650 as of December 31, 2005, can be utilized indefinitely.

Foreign:

The carryforward losses of the French subsidiary, amounting to approximately $ 11,900 as of December 31, 2005, can be utilized indefinitely.

The carryforward losses of the U.S. subsidiary, amounting to approximately $ 9,000 as of December 31, 2005, can be utilized mainly through 2017 to 2026. Utilization of U.S. net operating losses may be subject to the substantial annual limitation due to the "change in ownership" provisions of the Internal Revenue Code of 1986 and similar state provisions. The annual limitation may result in the expiration of net operating losses before utilization.

The carryforward losses of the Dutch subsidiary, amounting to approximately $ 5,300 as of December 31, 2005, can be utilized indefinitely.

The carryforward losses of the other subsidiaries amount to approximately $ 3,100 as of December 31, 2005. The majority of the carryforward losses can be utilized indefinitely.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

NOTE 10:- INCOME TAXES (Cont.)

e. Deferred income taxes:

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company and its subsidiaries deferred tax liabilities and assets are as follows:

	December 31,	
	2004	2005
Deferred tax assets in respect of operating loss carryforwards	$ 10,416	$ 10,147
Valuation allowance	(10,416)	(10,147)
Net deferred tax asset	$ -	$ -

Management currently believes that since the Company and its subsidiaries have a history of losses it is more likely than not that the deferred tax assets regarding the loss carryforwards will not be realized in the foreseeable future.

f. Reconciliation of the theoretical tax expense (benefit) to the actual tax expense (benefit):

In 2003, 2004 and 2005, the main reconciling items between the statutory tax rate of the Company and the effective tax rate (0%) are carryforward tax losses, for which a full valuation allowance was provided.

g. Loss before minority interest in losses of a subsidiary consists of the following:

	Year ended December 31,		
	2003	2004	2005
Domestic	$ 31	$ (2,342)	$ (2,031)
Foreign	(5,382)	(1,533)	(860)
	$ (5,351)	$ (3,875)	$ (2,891)

U.S. dollars in thousands

NOTE 11:- GEOGRAPHIC INFORMATION

The Company manages its business on the basis of one reportable segment.

a. Revenues classified by geographic destinations based on customer locations:

	Year ended December 31,		
	2003	2004	2005
Europe	$ 7,167	$ 8,332	$ 8,239
Asia	4,193	3,587	3,844
North America	1,594	1,381	1,234
South America	2,245	2,258	1,836
Other	240	170	248
	$ 15,439	$ 15,728	$ 15,401

b. Long-lived assets by geographic region:

	2003	2004	2005
Israel	$ 2,400	$ 1,806	$ 1,465
Europe	262	139	354
North America	17	102	39
Other	190	148	56
	$ 2,869	$ 2,195	$ 1,914

NOTE 12:- FINANCIAL INCOME (EXPENSES), NET

	Year ended December 31,		
	2003	2004	2005
Financial expenses:			
Foreign currency transaction adjustments, net	$ -	$ -	$ (379)
Bank charges	(65)	(61)	(45)
Interest on short-term bank credit	(5)	(1)	-
	(70)	(62)	(424)
Financial income:			
Foreign currency translation adjustments, net	404	188	-
Interest on bank deposits	99	63	108
	503	251	108
	$ 433	$ 189	$ (316)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands

NOTE 13:- TRANSACTIONS WITH RELATED PARTIES

The following related party transactions are included in the statements of operations:

	Year ended December 31,		
	2003	2004	2005
Revenues *)	$ 1,111	$ -	$ -
Sales and marketing *)	$ 131	$ -	$ -

*) Not a related party since January 1, 2004. The Company has become a sole owner of Orad North Asia.

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