Annual Report 2006

BATM
Advanced Communications

2006

Annual Report
Financial Statements

DIRECTORS AND ADVISERS

Directors

P. Sheldon	Chairman, Non-executive
Dr. Z. Marom	Chief executive
O. Bar-Ner	Finance director
K. Gavish	Non-executive
Dr. D. Kaznelson	Non-executive
A. Zochovitzky	Non-executive

Registered Office

P.O.B.3737
Kfar Netter 40593
Israel

Company Number

520042813 – Registered in Israel

Auditors

Brightman Almagor & Co.
a member firm of
Deloitte Touche Tohmatsu
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Israel

Financial Advisers & Stock brokers

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Shore Capital
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Corporate Solicitors in Israel

Lipa Meir & Co.
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Corporate Solicitors in the UK

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Bankers

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Chairman's Statement

Financial Performance

I am delighted to report on a year that has seen the Company return to profitability in a significant way.

Revenue for 2006 was $73.5m (2005: $56.5m), an increase of 30.1%. Revenue for the second half of 2006 at $39.4m (H2 2005: $30.3m) broadly maintained the rate of increase achieved in the first half of the year.

Gross profit margin for 2006 was 42.3% (2005: 38.5%). Our margins have improved throughout 2006 as increased sales from our higher-margin software business replaced the declining revenues in our legacy business.

Selling, general and administrative expenses in 2006 were $14.5m (2005: $12.6m), representing 19.7% (2005: 22.3%) as a percentage of revenue. General and administrative expenses in 2006 include expenses of $400k related to the acquisition and relocation of Metrobility to Telco System's facilities and expenses of $357k related to the grant of stock options to employees.

Net R&D expense for 2006 amounted to $8.2m (2005: $9.9m) a decrease of 17.0%. This primarily relates to our software related development activities, where some of the costs have been allocated to Cost of Sales as a result of the growth in our software business. The balance represents the restructuring of our R&D team in the US.

Operating profit after amortisation of intangible assets for the year was $7.7m (2005: loss of $4.5m).

Net financial income in 2006 was $2.3m (2005: $1.7m). The increase is mainly due to higher interest rates, gains from the sale of marketable securities and higher cash balances.

Impairment of investments in 2006 amounted to $2.6m (2005: $294k). A significant portion (approximately $2.3m) of this is related to a loss on the sale of our shares in Lantech, a Taiwanese company acquired by BATM in 2001. The remainder represents our investment in Vidyatel, a small startup company that develops specialized video technology, which was fully expensed in 2006.

Net profit after amortisation of intangible assets and tax in 2006 amounted to $6.9m (2005: Loss $3.4m), resulting in a basic earnings per share of 1.77 cents (2005: Loss of 0.88 cents).

Our balance sheet remains strong and we ended 2006 with cash balances of $50.4m (H1 2006: $45.4m; year end 2005: $48.0m).The increase in cash compared to June 30, 2006 and December 31, 2005 is principally related to increased revenue and improved operating profit. 2006 end cash is comprised as follows: Cash and deposits up to three months duration of $15.4m; short-term investments up to one year of $31.6m; and long-term investments for more than one year of $3.4m. We continue to exercise a conservative investment strategy, maintaining most balances in bank deposits. Our balance sheet at December 31, 2006 also includes $1.8m of short-term notes payable and $1.9m of long-term notes payable relating to the acquisition of Metrobility during 2006.

Sales and Marketing

2006 saw us increase our direct relationships with Tier 2 customers such as Time Warner Telecom, as well as embarking on several large-scale, long-term projects with other new carriers. In addition, we have increased our global presence with activities in several new geographical markets, mainly in Asia, where previously we have not been active. We expect these activities to increase during 2007 and become a significant portion of our business in 2008.

Chairman's Statement

As reported in May, we have commenced a relationship with one of the world's largest suppliers of network equipment for mobile telecommunications and we believe that this relationship will secure business opportunities for the next several years.

We are optimistic that this trend of expanding business relationships will continue into 2007 and beyond with substantial revenue opportunities materialising in 2008.

Research and Development and New Products

R&D activities continue to enhance our product range for Carrier Ethernet solutions as we look to expand our Ethernet demarcation family, our integrated business solution and Advanced TCA offerings.

The acquisition of Metrobility increased our product portfolio for Ethernet transport and demarcation, and our focus now is to launch next generation products in 2007 that will deliver higher speed services, guarantee the quality of services and improve testing capabilities for operators.

The first half of 2007 will also see the launch of our integrated business solution in the North American market. This product allows carriers to provide both new and legacy services over IP networks. The product incorporates our latest IP software with interfaces to many of the standard telecom protocols and will enhance our direct channels position primarily in the US and subsequently in Europe and the Rest of the World.

In addition to new products to address our direct channels, we continue to invest in Advanced TCA technology. In co-operation with some of our largest customers we are developing the fastest, most advanced products in this field. Although our efforts are currently focused on existing OEM channels, we believe that this will lead to further contracts with new clients in the future.

Investment

At the end of the first half of 2006, we acquired Metrobility. Its products complement our offerings in both the US and South American markets. Metrobility has been fully integrated into our business during the second half of 2006 and relocated to our Telco Systems facilities in the U.S.

Following negotiations in late 2006, we agreed at the beginning of 2007 to sell our holdings in Lantech, a Taiwanese manufacturer of Ethernet switches, with consideration for our holding amounting to $700k. As the remaining book value of our holdings was approximately $3.0m, we have recognised the loss of approximately $2.3m in our 2006 income statement under Impairment of Investments.

Prospects

Our return to profitability in 2006 is vindication of the positive stance that the company took throughout the telecoms downturn and we are taking additional steps to improve further our operating performance for 2007 and beyond. Whilst the current phase of industry consolidation, which includes some of our major customers, means that there may be some uncertainty of visibility in the next few months, the current year has started well. In the medium and long term we believe the effects for the Company will continue to be positive. BATM continues to adapt and respond to the market in order to support our growth objectives. Together with a multi-year strategic plan and our new customer and channel relationships, we are committed to building on the success of 2006 and remain confident that our growth and profitability will continue.

Peter Sheldon
Chairman
24 May, 2007

Deloitte.

Brightman Almagor

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Independent Auditors' Report To the Shareholders of BATM Advanced Communications Ltd.

We have audited the accompanying consolidated balance sheets of **BATM Advanced Communications Ltd.** ("the Company") and its subsidiaries ("the Group") as at December 31, 2006 and 2005 and the related consolidated income statements, consolidated statements of changes in equity and consolidated cash flows statements of the Group for the years ended December 31, 2006 and 2005. These financial statements are the responsibility of the Company's management and Board of Directors. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards in Israel including those prescribed by the Auditors' (Mode of Performance) Regulations (Israel), 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management and Board of Directors, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position the Group as at December 31, 2006 and 2005, and the consolidated results of operations, changes in equity and the cash flows of the Group for the years ended December 31, 2006 and 2005 in accordance with International Financial Reporting Standards.

Brightman Almagor & Co.
Certified Public Accountants
A member firm of Deloitte Touche Tohmatsu
Israel, 24 May, 2007

Consolidated Income Statements

	Note	Year ended December 31, 2006 $'000	2005 $'000
Revenue	4	73,472	56,514
Cost of sales		(42,412)	(34,748)
Gross profit		31,060	21,766
Sales and marketing expenses		10,402	9,521
General and administration expenses		4,063	3,109
Research and development expenses		8,205	9,887
Other expenses		691	3,780
Total operating expenses		23,361	26,297
Operating profit (loss)		7,699	(4,531)
Investment revenue	8	1,906	1,535
Other gains	9	567	194
Finance costs	10	(201)	(51)
Impairment of Investments		(2,582)	(294)
Profit (loss) before tax		7,389	(3,147)
Tax	11	(504)	(276)
Profit (loss) for the year	6	**6,885**	**(3,423)**
Earnings (loss) per share (in cents)			
Basic	13	**1.77**	**(0.88)**
Diluted	13	**1.74**	**(0.88)**

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

Consolidated Statements of Changes in Equity

	Share Capital	Share Premium account	Revaluation reserve	Accumulated deficit	Total equity
	$'000s				
Balance as at 1 January 2005	1,177	397,549	-	(327,783)	70,943
Exercise of stock based options by employees	1	131			132
Grant of stock based options to employees		424			424
Decrease in fair value of available for sale investments			(219)		(219)
Net loss for the year				(3,423)	(3,423)
Balance as at 31 December 2005	**1,178**	**398,104**	**(219)**	**(331,206)**	**67,857**
Exercise of stock based options by employees	2	197			199
Grant of stock based options to employees		767			767
Increase in fair value of available for sale investments			158		158
Tax on items taken directly to equity			(40)		(40)
Released on disposal of available for sale investments			219		219
Net income for the year				6,885	6,885
Balance as at 31 December 2006	**1,180**	**399,068**	**118**	**(324,321)**	**76,045**

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

Consolidated Balance Sheets

	Note	December 31, 2006 $'000s	December 31, 2005 $'000s
Non-current assets			
Goodwill	14	2,284	-
Other intangible assets	15	4,556	1,088
Property, plant and equipment	16	9,185	9,296
Investments in other companies	18	1,001	3,388
Held to maturity investments		3,432	8,635
Deferred tax assets	23	735	649
		21,193	23,056
Current assets			
Inventories	20	13,176	10,445
Investments	19	31,612	17,773
Trade and other receivables	21	16,360	10,794
Cash and cash equivalents		15,363	21,560
		76,511	60,572
Total assets		**97,704**	**83,628**
Current liabilities			
Trade and other payables	24	16,748	13,605
Current tax liabilities		199	171
Provisions	25	2,116	949
		19,063	14,725
Net current assets		**57,448**	**45,847**
Non-current liabilities			
Long-term payables	24	1,901	-
Retirement benefit obligation	35	310	286
Long-term provisions	25	385	760
		2,596	1,046
Total liabilities		**21,659**	**15,771**
Net assets		**76,045**	**67,857**
Equity			
Share capital	26	1,180	1,178
Share premium account	27	399,068	398,104
Revaluation reserve	28	118	(219)
Accumulated Deficit	29	(324,321)	(331,206)
Total equity		**76,045**	**67,857**

The accompanying notes are an integral part of these financial statements.
The financial statements were approved by the board of directors and authorised for issue on 24 May, 2007. They were signed on its behalf by:

Dr. Z. Marom **O. Bar-Ner**

Consolidated Cash Flow Statements

	Note	Year ended December 31, 2006 $'000s	Year ended December 31, 2005 $'000s
Net cash from (used in) operating activities	31	3,760	(3,256)
Investing activities			
Interest received		1,551	4,042
Dividends received from available for sale investments		16	43
Proceeds on disposal of held to maturity investments		3,000	1,500
Proceeds on disposal of available-for-sale investments		8,956	6,359
Proceeds on disposal of deposits		13,000	39,193
Purchases of property, plant and equipment		(1,279)	(692)
Purchases of held to maturity investments		-	(3,423)
Purchases of available for sale investments		(7,657)	(5,041)
Purchases of deposits		(24,625)	(18,000)
Investment in a company		(200)	-
Acquisition of subsidiaries	30	(1,933)	(200)
Net cash from (used in) investing activities		(9,171)	23,781
Financing activities			
Repayments of borrowings		(985)	(250)
Proceeds on issue of shares		199	132
Net cash used in financing activities		(786)	(118)
Net increase (decrease) in cash and cash equivalents		(6,197)	20,407
Cash and cash equivalents at beginning of year		21,560	1,153
Cash and cash equivalents at end of year		**15,363**	**21,560**

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

Note 1 - General Information

BATM Advanced Communications Ltd. is a company incorporated in Israel under the Israeli Companies law. The address of the registered office is POB 3737, Kfar Neter 40593, Israel. The Company and its subsidiaries ("the Group") are engaged in the research and development, production and marketing of data communication products in the field of local and wide area networks and premises management systems.

These financial statements are presented in US dollars because that is the currency of the primary economic environment in which the Group operates. Foreign operations are included in accordance with the policies set out in Note 2.

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective:

IFRS 7	Financial Instruments: Disclosures; and the related amendment to IAS 1 on capital disclosures
IFRS 8	Opertaing Segments
IFRIC 10	Interim Financial Reporting and Impairment
IFRIC 11	Group and Treasury Share Transactions
IFRIC 12	Service Concession Arrangements

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Group except for additional disclosures when the relevant standards come into effect for periods commencing on or after 1 January 2007.

Note 2 - Significant Accounting Policies

Basis of accounting

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) for the first time. The disclosures required by IFRS 1 concerning the transition from Israeli GAAP to IFRS are given in Note 37.

The financial statements have been prepared on the historical cost basis, except for the revaluation of certain financial instruments. The principal accounting policies adopted are set out below.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. Control is achieved where the Company has the power to govern the financial and operating policies of an investee entity so as to obtain benefits from its activities.

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with those used by the Group.

All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Note 2 - Significant Accounting Policies (Cont.)

Business combinations

The acquisition of subsidiaries is accounted for using the purchase method. The cost of the acquisition is measured at the aggregate of the fair values, at the date of exchange, of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 are recognised at their fair value at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for resale in accordance with IFRS 5 Non Current Assets Held for Sale and Discontinued Operations, which are recognised and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognised as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognised. If, after reassessment, the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognised immediately in profit or loss.

Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Goodwill

Goodwill arising from consolidation represents the excess of the cost of acquisition over the Group's interest in the fair value of the identifiable assets and liabilities of a subsidiary, associate or jointly controlled entity at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised immediately in profit or loss and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary, associate or jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Goodwill arising from acquisitions before the date of transition to IFRS has been retained at the previous Israeli GAAP amounts subject to being tested for impairment at that date.

Note 2 - Significant Accounting Policies (Cont.)

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts, VAT and other sales-related taxes.

Sales of goods are recognised when goods are delivered and title has passed.

Revenue from long-term contracts is recognised in accordance with the Group's accounting policy on long-term contracts *(see below)*.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

Long-Term contracts

Where the outcome of a long-term contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date. This is normally measured by the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs, except where this would not be representative of the stage of completion. Variations in contract work, claims and incentive payments are included to the extent that they have been agreed with the customer.

Where the outcome of a long-term contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that it is probable will be recoverable. Contract costs are recognised as expenses in the period in which they are incurred.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. All of the Group's leases are classified as operating leases.

The Group as lessor

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

The Group as lessee

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Note 2 - Significant Accounting Policies (Cont.)

Foreign currencies

The individual financial statements of each Group company are prepared in the currency of the primary economic environment in which it operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each Group company are expressed in the US dollar, which is the functional currency of the Group, and the presentation currency for the consolidated financial statements.

In preparing the financial statement of the individual companies, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in profit or loss for the period. Exchange differences arising on the retranslation of non-monetary items carried at fair value are included in profit or loss for the period except for differences arising on the retranslation of non-monetary items in respect of which gains and losses are recognised directly in equity. For such non-monetary items, any exchange component of that gain or loss is also recognised directly in equity.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations (operations in foreign currencies) are translated at exchange rates prevailing on the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuate significantly during that period, in which case the exchange rates at the date of transactions are used. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such translation reserves, which were immaterial for all periods presented, are recognised as income or as expense in the period in which the operation is disposed.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Government grants

Government grants towards research and development costs are netted against related expenses over the periods necessary to match them with the related costs.

Operating profit

Operating profit is stated before investment revenues, other gains, finance cost and impairment of investments.

Note 2 - Significant Accounting Policies (Cont.)

Retirement benefit costs

Payments to defined contribution retirement benefit schemes are charged as an expense as they fall due. Payments made to state-managed retirement benefit schemes are dealt with as payments to defined contribution schemes where the Group's obligations under the schemes are equivalent to those arising in a defined contribution retirement benefit scheme.

For defined benefit schemes, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside profit or loss and presented in the statement of recognised income and expense.

Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost, and as reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to past service cost, plus the present value of available refunds and reductions in future contributions to the scheme.

Taxation

The tax expense represents the sum of the tax currently payable and deferred.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from the initial recognition of goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences arising on investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Note 2 - Significant Accounting Policies (Cont.)

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority.

Property, plant and equipment

Land and buildings held for use in the production or supply of goods or services, or for administrative purposes, are stated in the balance sheet on a historical cost basis, being the historical cost at the date of acquisition, less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

Properties in the course of construction for production, rental or administrative purposes, or for purposes not yet determined, are carried at cost, less any recognised impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Fixtures and equipment are stated at cost less accumulated depreciation and any recognised impairment loss.

Depreciation is charged so as to write off the cost or valuation of assets, other than land and properties under construction, over their estimated useful lives, using the straight-line method, on the following bases:

Buildings	2%
Fixtures and equipment	10%
Motor Vehicles	15%
Computers and Manufacturing equipment	10-33%

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in income.

Internally-generated intangible assets – research and development expenditure

Expenditure on research activities is recognised as an expense in the period in which it is incurred.

An internally-generated intangible asset arising from the Group's product development is recognised only if all of the following conditions are met:

- an asset is created that can be identified (such as software and new processes);
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Note 2 - Significant Accounting Policies (Cont.)

Internally-generated intangible assets are amortised on a straight-line basis over their useful lives. Where no internally-generated intangible asset can be recognised, development expenditure is recognised as an expense in the period in which it is incurred.

Acquired intangible assets

Acquired intangible assets are measured initially at purchase cost and are amortised on a straight-line basis over their estimated useful lives.

Impairment of tangible and intangible assets excluding goodwill

At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the group estimates the recoverable amount of the cash-generating unit to which the asset belongs. An intangible asset with an indefinite useful life is tested for impairment annually and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised as an expense immediately, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials and, where applicable, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is determind on the “first-in–first-out” basis. Net realisable value represents the estimated selling price less all estimated costs of completion and costs to be incurred in marketing, selling and distribution.

Financial instruments

Financial assets and financial liabilities are recognised on the Group’s balance sheet when the Group becomes a party to the contractual provisions of the instrument.

Note 2 - Significant Accounting Policies (Cont.)

Trade receivables

Trade receivables are measured at initial recognition at fair value, and are subsequently measured at amortised cost using the effective interest rate method. Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. The allowance recognised is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate computed at initial recognition.

Investments

Investments are recognised and derecognised on a trade date where a purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at cost, including transaction costs.

At subsequent reporting dates, debt securities that the Group has the expressed intention and ability to hold to maturity (held-to-maturity debt securities) are measured at amortised cost using the effective interest rate method, less any impairment loss recognised to reflect irrecoverable amounts. An impairment loss is recognised in profit or loss when there is objective evidence that the asset is impaired, and is measured as the difference between the investment's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate computed at initial recognition. Impairment losses are reversed in subsequent periods when an increase in the investment's recoverable amount can be related objectively to an event occurring after the impairment was recognised, subject to the restriction that the carrying amount of the investment at the date the impairment is reversed shall not exceed what the amortised cost would have been had the impairment not been recognised.

Investments are classified as either held-for-trading or available-for-sale, and are measured at subsequent reporting dates at fair value. Where securities are held for trading purposes, gains and losses arising from changes in fair value are included in net profit or loss for the period. For available-for-sale investments, gains and losses arising from changes in fair value are recognised directly in equity, until the security is disposed of or is determined to be impaired, at which time the cumulative gain or loss previously recognised in equity is included in the profit or loss for the period. Impairment losses recognised in profit or loss for equity investments classified as available-for-sale are not subsequently reversed through profit or loss. Impairment losses recognised in profit or loss for debt instruments classified as available-for-sale are subsequently reversed if an increase in the fair value of the instrument can be objectively related to an event occurring after the recognition of the impairment loss.

All the Group investments are classified as held to maturity or available for sale. The Group currently has no held for trading investments.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and demand deposits, and other short-term highly liquid investments that are readily convertible to a known amount of cash and are subject to an insignificant risk of changes in value.

Financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the Group after deducting all of its liabilities.

Note 2 - Significant Accounting Policies (Cont.)

Bank borrowings

Interest-bearing bank loans and overdrafts are recorded at the proceeds received, net of direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs, are accounted for on an accrual basis in profit or loss account using the effective interest method and are added to the carrying amount of the instrument to the extent that they are not settled in the period in which they arise.

Trade payables

Trade payables are initially measured at fair value, and are subsequently measured at amortised cost, using the effective interest rate method.

Equity instruments

Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the directors' best estimate of the expenditure required to settle the obligation at the balance sheet date, and are discounted to present value where the effect is material.

Share-based payments

The Group has applied the requirements of IFRS 2 Share-based Payments. In accordance with the transitional provisions, IFRS 2 has been applied to all grants of equity instruments after 7 November 2002 that were unvested as of 1 January 2005.

The Group issues equity-settled share-based payments to certain employees. Equity-settled share-based payments are measured at fair value (excluding the effect of non market-based vesting conditions) at the date of grant. The fair value determined at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Group's estimate of shares that will eventually vest and adjusted for the effect of non market-based vesting conditions.

Fair value is measured by use of the Black-Scholes valuation model. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

Note 3 - Critical Accounting Judgements and Key Sources of Estimation Uncertainty

Critical judgements in applying the Group's accounting policies

In the process of applying the Group's accounting policies, which are described in Note 2, management has made the following judgements that have the most significant effect on the amounts recognised in the financial statements (apart from those involving estimations, which are dealt with below):

- Judgements with respect the non-capitalization of development expenses
- Judgements with respect to impairment of tangible and intangible assets

Note 3 - Critical Accounting Judgements and Key Sources of Estimation Uncertainty (Cont.)

Key sources of estimation uncertainty

The key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are with respect to provisions *(see Note 25)*.

Note 4 - Revenue

An analysis of the Group's revenue is as follows:

	Year ended December 31,	
	2006 $'000s	**2005 $'000s**
Sales of goods	67,033	54,690
Services	6,269	1,541
Property rental income	170	283
	73,472	**56,514**

Note 5 - Business and Geographical Segments

Business segments

The Group has no distinct business segments.

Geographical segments

The principle operations of the Group are located in Israel, Americas, Europe and the Far East. Manufacturing is carried out primarily in Israel and in the USA. The following table provides an analysis of the Group's sales by geographical market, irrespective of the origin of the goods/services. All numbers are in thousands of US dollars *(see table on page 18)*.

Note 5 - Business and Geographical Segments (Cont.)($'000s)

2006					
	Americas	Europe	Israel	Far East and Other	Total
Profit and Loss information					
Revenues	32,929	21,243	5,882	13,418	73,472
Gross Profit	13,921	8,980	2,487	5,672	31,060
Capital expenditure[1]	6,828	19	875	-	7,722
Depreciation and amortisation	1,230	9	1,050	-	2,289
Other non-cash expenses (income)	(235)	26	724	101	616
Balance sheet information					
Segment Assets	21,668	9,174	11,428	4,026	46,296
Segment Liabilities	11,811	557	8,955	336	21,659
Cashflow information	(1,727)	772	4,614	101	3,760

2005					
	Americas	Europe	Israel	Far East and Other	Total
Profit and Loss information					
Revenues	35,331	18,039	1,646	1,498	56,514
Gross Profit	13,607	6,948	634	577	21,766
Capital expenditure[1]	1,464	6	533	-	2,003
Depreciation and amortisation	3,223	10	926	-	4,159
Other non-cash expenses (income)	(324)	6	462	-	144
Balance sheet information					
Segment Assets	15,339	5,198	10,221	1,514	32,272
Segment Liabilities	9,219	667	5,740	145	15,771
Cashflow information	(6,501)	148	3,097	-	(3,256)

[1] Calculated on an accruals basis

Note 6 - Profit (loss) for the Year

Profit (loss) for the year has been arrived at after charging (crediting):

	Year ended December 31, 2006 $'000s	Year ended December 31, 2005 $'000s
Net foreign exchange losses (gains)	(107)	18
Research and development costs	9,389	10,810
Government grants	(1,184)	(923)
Depreciation of property, plant and equipment	1,598	1,463
Amortisation of intangible assets included in operating expenses	691	2,696
Impairment of investments	2,582	294
Cost of inventories recognised as expense	38,277	38,693
Staff costs *(see Note 7)*	15,108	12,713
Auditors' remuneration for audit services *(see below)*	128	120

Amounts payable to Brightman Almagor & Co. by the Company and its subsidiaries' undertakings in respect of non-audit services in 2006 were $20,000 (2005: $22,000).

In addition, payables in respect of non-audit services to others than the Company's auditors, for tax and internal audit services in 2006, were $13,000 and $11,000, respectively (2005: $5,000 and $5,000, respectively)

Note 7 - Staff Costs

The average monthly number of employees in 2006 (including executive directors) was 213 (2005:198).

	Year ended December 31, 2006 $'000s	Year ended December 31, 2005 $'000s
Their aggregate remuneration comprised:		
Wages and salaries	11,470	9,492
Social security costs	3,046	2,609
Other pension costs *(see Note 35)*	592	612
	15,108	**12,713**
Executive Directors' emoluments	**771**	**348**

Note 8 - Investment Revenue

	Year ended December 31,	
	2006 $'000s	2005 $'000s
Interest on bank deposits	**1,906**	**1,535**

Note 9 - Other Gains

	Year ended December 31,	
	2006 $'000s	2005 $'000s
Profit on disposal of available-for-sale investments	485	177
Increase (decrease) in the fair value of investments held at year end	(25)	35
Net foreign exchange gains (losses)	107	(18)
	567	**194**

Note 10 - Finance Costs

	Year ended December 31,	
	2006 $'000s	2005 $'000s
Interest on loans	**201**	**51**

Note 11 - Tax

	Year ended December 31,	
	2006 $'000s	2005 $'000s
Current tax	590	193
Deffered tax *(Note 23)*	(86)	83
	504	**276**

Taxation under various laws:

Israel

The Company and its Israeli subsidiaries are assessed under the provisions of the Income Tax Law (Inflationary Adjustments), 1985, pursuant to which the results for tax purposes are measured in Israeli currency in real terms in accordance with changes in the Israeli CPI. The Company has applied to the tax authorities with a request to measure its results for tax purposes in US dollars, starting from 2007.

Note 11 - Tax (Cont.)

The Company and its subsidiaries are assessed for tax purposes on an unconsolidated basis.

The Company is an "industrial company" as defined in the Israeli Law for the Encouragement of Industry (Taxes) 1969, and, as such, is entitled to certain tax benefits, mainly increased depreciation rates, the right to claim public issuance expenses and the amortization of patents and other intangible property rights as a deduction for tax purposes.

The production facilities of the Company have been granted "approved enterprise" status for several separate programs under the Law for the Encouragement of Capital Investments, 1959, as amended. Under this law, income attributable to each of these programs (in a manner prescribed in such law and its regulations) is fully exempt from tax for eight to ten years.

Such period of benefits commences on the first year in which the enterprise generates taxable income (The expiry date of the period of benefits is limited to the earlier of twelve years from commencement of production or fourteen years from the date of the approval.) The period of benefits of the first program commenced in 1992 and ended in 2000.

One of the Israeli subsidiaries has also been granted an Approved Enterprise status for the construction of the Company's plant at Yokneam, on terms similar to the above mentioned.

In the event of a distribution of a cash dividend out of tax-exempt income, as mentioned above, the Company (or the subsidiary who has also been granted with an Approved Enterprise status) will be liable to corporate tax at a rate of 10%-25% (depending on the percentage of foreign shareholders in the Company's equity), in respect of the amount distributed. The Company and the subsidiary currently have no plans to distribute dividends from tax-exempt income.

The above tax benefits are conditioned upon fulfillment of the requirements stipulated by the aforementioned law and the regulations promulgated there under, as well as the criteria set forth in the certificates of approval. In the event of failure by the Company or the subsidiary to comply with these conditions, the tax benefits could be canceled, in whole or in part, and the Company or the subsidiary would be required to refund the amount of the canceled benefits, plus interest and certain inflation adjustments.

On July 25, 2005 an amendment to the Israeli tax law was approved by the Israeli Parliament which reduces the tax rates imposed on Israeli companies to 31% for 2006; this amendment states that the corporate tax rate will be further reduced in subsequent tax years as follows: in 2007 29%, in 2008 27%, in 2009 26% and thereafter 25%.

The Company has received final tax assessments for the years up to and including the 2002 tax year. The subsidiaries have not been assessed for tax since their incorporation.

The United States of America

Since acquisition, Telco Systems has incurred losses for tax purposes. In addition, in accordance with U.S. tax law, Telco Systems made an election to amortize a substantial part of the excess cost paid by the Company in its acquisition over a period of 15 years. This has resulted in tax loss carry-forwards which may be expire before been utilized. Accordingly the future use of these benefits is uncertain. Other US subsidiaries are assessed for tax purposes on a consolidated basis with Telco Systems. No deferred tax asset has been recognised in respect of such losses.

Other jurisdictions

Taxation for other jurisdictions is calculated at the rates prevailing in the respective jurisdictions.

Note 11 - Tax (Cont.)

The charge for the year can be reconciled to the profit per the income statement as follows:

	Year ended December 31,	
	2006 $'000s	2005 $'000s
Profit (loss) before tax:	**7,389**	**(3,147)**
Tax at the Israeli corporation tax rate of 31% (2005: 34%)	2,291	(1,070)
Tax exempt income	(2,000)	-
Losses for which no assets were recorded	-	1,146
Other differences	213	200
Tax expense for the year	**504**	**276**

The effective tax rate for 2006 was 6.8% resulting mainly from the Company's benefits under the Approved Enterprise Program.

Note 12 - Dividends

No dividend was proposed or paid by the Company in financial years 2006 or 2005.

Note 13 - Earnings (loss) per Share

The calculation of the basic and diluted earnings (loss) per share is based on the following data:

	Year ended December 31,	
	2006	2005
Earnings for the purposes of basic and diluted earnings (loss) per share ($'000s)	**6,885**	**(3,423)**
Number of shares		
Weighted average number of ordinary shares for the purposes of basic earnings per share	389,467,186	388,578,761
Effect of dilutive potential ordinary shares:		
Share options	5,274,077	-
Weighted average number of ordinary shares for the purposes of diluted earnings per share	**394,741,263**	**388,578,761**

Note 14 - Goodwill

Goodwill acquired in a business combination is allocated, at acquisition, to the cash generating units (CGUs) that are expected to benefit from that business combination. At 31 December 2006 the goodwill of $2,284,000 was allocated to the acquisition of Metrobility *(see Note 30)*. An impairment charge of $2,475,000 was recorded in 2005 in respect of the balance at 1 January 2005 from the Acquisition of Telco Systems.

The Group tests goodwill annually for impairment, or more frequently if there are indications that it might be impaired.

The recoverable amounts of the CGUs are determined from value in use calculations. The key assumptions for the value in use calculations are those regarding the discount rates, growth rates and expected changes to selling prices and direct costs during the period. Management estimates discount rates using pre-tax rates that reflect current market assessments of the time value of money and the risks specific to the CGUs. The growth rates are based on industry growth forecasts. Changes in selling prices and direct costs are based on past practices and expectations of future changes in the market.

Note 15 - Other Intangible Assets

	Customer Relationships $'000s	Core Technology $'000s	Other $'000s	Total $'000s
Cost				
At 1 January 2005	-	-	-	-
Additions	1,311	-	-	1,311
At 31 December 2005	1,311	-	-	1,311
Additions	-	-	-	-
Acquired on acquisition of a subsidiary	2,300	1,420	439	4,159
At 31 December 2006	3,611	1,420	439	5,470
Amortisation				
At 1 January 2005	-	-	-	-
Charge for the year	223	-	-	223
At 31 December 2005	223	-	-	223
Charge for the year	544	101	46	691
At 31 December 2006	767	101	46	914
Carrying amount				
At 31 December 2006	**2,844**	**1,319**	**393**	**4,556**
At 31 December 2005	**1,088**	**-**	**-**	**1,088**

Other intangible assets are amortised over their estimated useful lives, which range from 5 to 7 years.

Note 16 - Property, Plant and Equipment ($'000s)

	Land and buildings	Plant and equipment	Motor Vehicles	Furntiure and fittings	Leashold Improvements	Total
Cost						
At 1 January 2005	8,637	10,089	19	1,039	126	19,910
Additions	-	664	-	28	-	692
Acquisition of subsidiary	-	439	-	4	-	443
Disposals	-	(15)	-	(11)	-	(26)
At 31 December 2005	8,637	11,177	19	1,060	126	21,019
Additions	-	990	16	42	231	1,279
Acquisition of subsidiary	-	1,859	17	17	16	1,909
At 31 December 2006	8,637	14,026	52	1,119	373	24,207
Accumulated depreciation						
At 1 January 2005	1,622	7,925	6	625	108	10,286
Charge for the year	388	1,001	3	69	2	1,463
Eliminated on disposals	-	(15)	-	(11)	-	(26)
At 31 December 2005	2,010	8,911	9	683	110	11,723
Charge for the year	462	1,034	3	55	44	1,598
Acquisition of subsidiary	-	1,651	17	17	16	1,701
At 31 December 2006	2,472	11,596	29	755	170	15,022
Carrying amount						
At 31 December 2006	**6,165**	**2,430**	**23**	**364**	**203**	**9,185**
At 31 December 2005	**6,627**	**2,266**	**10**	**377**	**16**	**9,296**

Note 17 - Subsidiaries

A list of the direct and indirect investments in subsidiaries, including the name, country of incorporation, percent of ownership interest is presented below.

Name of subsidiary	Country of incorporation	Ownership interest	Date of acquisition
Telco Systems Inc.	United States of America	100%	April 2000
Integral Access Inc.	United States of America	100%	July 2005
Critical Telecom Inc.	Canada	100%	September 2006
Metrobility Optical Systems Inc.	United States of America	100%	June 2006
Telco Asia Pacific Limited*	Singapore	100%	March 2006
Netwiz	Israel	100%	January 1999
B.T.T.*	Israel	100%	March 1999
B.A.T.M. land*	Israel	100%	December 1994
BAT-NET*	Israel	100%	January 1996
B.A.T.M. Germany*	Germany	100%	June 1998
B.A.T.M. England*	United Kingdom	100%	April 1994
B.A.T.M. France*	France	100%	May 2000
B.A.T.M. Iberia*	Iberia	100%	September 2003

* Incorporated by the Company

Note 18 - Investment in Other Companies

	December 31,	
	2006 $'000s	2005 $'000s
Netstar Technology Corporation (Lantech) (1)	700	3,087
Lynx Photonic Networks Inc.	301	301
	1,001	**3,388**

(1) Following negotiations in late 2006, The Company agreed, at the beginning of 2007, to sell its holdings in Lantech, a Taiwanese manufacturer of Ethernet switches, with consideration for our holding expected to amount to approximately $700,000. As a result, the Company recognised the loss of $2,387,000 in its 2006 income statement under Impairment of Investments.

Note 19 - Investments

Investments presented as current assets include interest-bearing deposits of $30,589,000 at 31 December 2006 (2005: $13,211,000).

Note 20 - Inventories

	December 31,	
	2006 $'000s	2005 $'000s
Raw materials	6,762	4,640
Work-in-progress	809	640
Finished goods	5,605	5,165
	13,176	**10,445**

Note 21 - Other Financial Assets

Trade and other receivables

	December 31,	
	2006 $'000s	2005 $'000s
Amount receivable for the sale of goods	14,763	9,463
Participation in research and development:		
Government of Israel	459	353
VAT	214	275
Tax authorities	22	30
Prepaid expenses and other debtors	902	673
	16,360	**10,794**

The average credit period taken on sales of goods is 45 days. No interest is charged on the receivables. An allowance has been made at 31 December 2006 for estimated irrecoverable amounts from the sale of goods of $389,000 (2005: $1,077,000). This allowance has been determined by reference to past default experience.

The directors consider that the carrying amount of trade and other receivables approximates their fair value.

Bank balances and cash comprise cash held by the Group and short-term bank deposits with an original maturity of three months or less. The carrying amount of these assets approximates their fair value.

Credit risk

The Group's principal financial assets are bank balances and cash, trade and other receivables and investments.

The Group's credit risk is primarily attributable to its trade and receivables. The amounts presented in the balance sheet are net of allowances for doubtful receivables. An allowance for impairment is made where there is an identified loss event which, based on previous experience, is evidence of a reduction in the recoverability of the cash flows.

The Group has no significant concentration of credit risk, with exposure spread over a large number of counterparties and customers.

Note 22 - Derivative Financial Instruments

The Group has not used derivatives financial instruments in 2006 and 2005.

Note 23 - Deferred Tax Assets

The following are the major deferred tax assets recognised by the Group and movements thereon during the current and prior reporting period *(see also Note 11)*.

	Deferred development costs $'000s	Depreciation differences $'000s	Retirement benefit obligations $'000s	Total $'000s
At 1 January 2005	172	237	323	732
Credit (charge) to income	(93)	54	(44)	(83)
At 31 December 2005	79	291	279	649
Credit to income	24	32	30	86
At 31 December 2006	**103**	**323**	**309**	**735**

Note 24 - Other Financial Liabilities

Trade and other payables

	December 31, 2006 $'000s	December 31, 2005 $'000s
Trade creditors	8,967	8,041
Salary accruals	2,015	1,954
Related parties	371	341
VAT	6	7
Other creditors and accruals	2,740	3,262
Liability in regard an acquisition of a subsidiary (Metrobility) (1)	2,649	-
	16,748	**13,605**

Trade creditors and accruals principally comprise amounts outstanding for trade purchases and ongoing costs. The average credit period taken for trade purchases is 60 days.

The directors consider that the carrying amount of trade payables approximates to their fair value.

(1) The liability of $2,649,000 comprise of $1,801,000, bears annual interest of 5%, maturity date June 2007 and of $848,000, bears annual interest of 12%, the payment is on a monthly basis ending December 2007.

Note 24 - Other Financial Liabilities (Cont.)

Long- term payables

Liability of $1,901,000 for the acquisition of Metrobility in 2006, bears annual interest of 5%, maturity date June 2008.

Note 25 - Provisions

	Warranty provision $'000s	Contingent consideration resulting from the acquisition of subsidiary $'000s	Tax $'000s	Total $'000s
At 31 December 2005	769	940	-	1,709
Additional provision in the year	-	-	600	600
Utilisation of provision	9	-	-	9
On acquisition of subsidiary	257	110	-	367
Payment during the year	-	(184)	-	(184)
At 31 December 2006	**1,035**	**866**	**600**	**2,501**
Included in current liabilities				2,116
Included in non-current liabilities				385
				2,501

The warranty provision represents management's best estimate of the Group's liability under warranties granted on the Group's products, based mainly on past experience.

Note 26 - Share Capital

Ordinary shares of NIS 0.01 each (number of shares)		
	2006	**2005**
Authorised:	**1,000,000,000**	**1,000,000,000**
Issued and fully paid:	**389,677,837**	**388,961,117**

The Company has one class of ordinary shares which carry no right to fixed income.

Note 27 - Share Premium Account

	Share premium $'000s
Balance at 1 January 2005	397,549
Premium arising on issue of equity shares	131
Stock options granted to employees	424
Balance at 31 December 2005	398,104
Premium arising on issue of equity shares	197
Stock options granted to employees	767
Balance at 31 December 2006	**399,068**

Note 28 - Revaluation Reserve

	Revaluation reserve $'000s
Balance at 1 January 2005	-
Decrease in fair value of available-for-sale investments	(219)
Balance at 31 December 2005	(219)
Increase in fair value of available-for-sale investments	158
Tax on items taken directly to equity	(40)
Released on disposal of available-for-sale investments	219
Balance at 31 December 2006	**118**

Note 29 - Accumulated Deficit

	Accumulated deficit $'000s
Balance at 1 January 2005	(327,783)
Net loss for the year	(3,423)
Balance at 31 December 2005	(331,206)
Net profit for the year	6,885
Balance at 31 December 2006	**(324,321)**

Note 30 - Acquisition of Subsidiaries

On 29 June 2006, the Group acquired 100% of the issued share capital of Metrobility Optical Systems Inc. ("Metrobility") for a consideration of $6,100,000. Metrobility is a manufacturer of intelligent demarcation equipment that enables optical Ethernet services in metropolitan area networks. This transaction has been accounted for by the purchase method of accounting.

Note 30 - Acquisition of Subsidiaries (Cont.)

Metrobility	Book value $'000s	Fair value adjustments $'000s	Fair value $'000s
Net assets acquired			
Property, plant and equipment	208	(44)	164
Inventories	1,715	(517)	1,198
Trade and other receivables	1,451	32	1,483
Cash and cash equivalents	149	-	149
Trade and other payables	(1,139)	(721)	(1,860)
Bank loans	(985)	-	(985)
Provisions	(70)	(187)	(257)
	1,329	**(1,437)**	(108)
Other Intangible Assets			4,120
Goodwill			2,284
Total consideration			**6,296**
Satisfied by:			
Cash			1,863
Directly attributable costs			260
Consideration recorded as liability			4,173
			6,296
Net cash outflow arising on acquisition			
Cash consideration			6,296
Cash and cash equivalents acquired			(149)
			6,147

Metrobility contributed $5,900,000 revenue and $300,000 to the Group's profit before tax for the period between the date of acquisition and 31 December 2006.

If the acquisition of Metrobility had been completed on the first day of the 2006 financial year, Group revenues for that year would have been $78,800,000 and Group profit would have been $6,100,000.

On July 2005 the Group acquired the net assets of Integral Access Inc, a US corporation, for a cash consideration of $200,000. The acquisition agreement contains a contingent consideration to be paid by the Company based on the performance of the operations acquired. Based on management estimation at the date of the acquisition, it is probable that the Company will be required to pay an additional amount of $940,000. Accordingly such amount has been included as part of the purchase price paid for the acquired operations and as a liability in this financial statements. Integral Access is involved in next generation access equipment for the delivery of integrated business services by service providers. This transaction has been accounted for by the purchase method of accounting.

Note 30 - Acquisition of Subsidiaries (Cont.)

Integral Access	$'000s
Net asset acquired	
Property, plant and equipment	443
Inventories	737
Trade and other receivables	649
Trade and other payables	(1,137)
Bank loan	(250)
Provisions	(613)
	(171)
Other Intangible Assets	1,311
Total consideration	1,140
Less- consideration recorded as liability	(940)
Total cash consideration	**200**

For the period from January 1, 2005 to July 31, 2005 (date of acquisition) Integral Access's revenues and net loss amounted to $4,800,000 and $6,400,000 respectively ($3,474,000 and profit of $130,000 respectively for the period from the date of the acquisition to December 31, 2005).

Accordingly, if the results of the operations of Integral Access had been consolidated in the Group's financial statements starting on January 1, 2005 the Group's consolidated revenues and loss for the year ended 31 december 2005 would have been $61,314,000 and $9,823,000 respectively.

On September 2006 the Group acquired the net assets of Critical Telecom Corporation Inc., a Canadian corporation, for a cash consideration of $70,000. The transaction has been accounted for by the purchase method of accounting.

Critical Telecom	$'000s
Net asset acquired	
Property, plant and equipment	44
Inventories	100
Trade and other receivables	81
Trade and other payables	(84)
	141
Other Intangible Assets	39
Total consideration	180
Less- consideration recorded as liability	(110)
Total cash consideration	**70**

Note 31 - Note to the Cash Flow Statement

	Year ended December 31	
	2006 $'000s	2005 $'000s
Operating profit (loss) from continuing operations	7,699	(4,531)
Adjustments for:		
Depreciation of property, plant and equipment	1,598	1,463
Stock options granted to employees	767	424
Amortisation of intangible assets	691	2,696
Increase in retirement benefit obligation	24	5
Decrease in provisions	(175)	(285)
Operating cash flows before movements in working capital	10,604	(228)
Increase in inventories	(1,433)	(2,283)
Increase in receivables	(4,007)	(366)
Decrease in payables	(1,184)	(297)
Cash generated by operations	3,980	(3,174)
Income taxes paid	(19)	(31)
Interest paid	(201)	(51)
Net cash from (used in) operating activities	**3,760**	**(3,256)**

Cash and cash equivalents (which are presented as a single class of assets on the face of the balance sheet) comprise cash at bank and other short-term highly liquid investments with a maturity of three months or less.

Note 32 - Contingent Liabilities

Royalties

The Company and one of its subsidiaries are committed to pay royalties to the Office of the Chief Scientist of the Government of Israel ("Chief Scientist") on proceeds from the sale of products for which the Chief Scientist has provided research and development grants. The royalties are capped at 100%-150% of the grants received (in dollar terms). The royalties payable are at a rate of 3%, for the first three years of product sales; 4%, for the following three years, and 5%, thereafter. The total amount of grants received, net of royalties paid or accrued, as at December 31, 2006 was $7,339,000 (December 31, 2005 - $6,769,000).

Total royalty expenses to the Chief Scientist for the years ended December 31, 2006 and 2005 were $231,000 and $555,000, respectively. These amounts are included in cost of sales.

Stamp duties

There is a potential exposure totalling approximately $2,000,000, relating to stamp duties connected with some placements made by the Company in the past. According to the advice of the Company's legal advisors, and in contrast to the position of the Companies' Registrar, an obligation to pay stamp duties arises only when a stamped document exists, and since the placements were not accompanied by a stamped issuance report, such obligation does not exist.
The Company has not provided for such an amount in its financial statements.

Note 33 - Operating Lease Arrangements

The Group as lessee

	Year ended December 31	
	2006 $'000s	2005 $'000s
Minimum lease payments under operating leases recognised in income for the year	**849**	**1,120**

At the balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	December 31,	
	2006 $'000s	2005 $'000s
Within one year	778	928
In the second to fifth years inclusive	2,572	1,939
After five years	26	323
	3,376	**3,190**

Operating lease payments represent rentals payable by the Group for certain of its office properties. Leases are negotiated for an average term of 6 years and rentals are fixed for an average of 6 years.

The Group as lessor

Property rental income earned during 2006 was $170,000 (2005: $283,000). The property held have committed tenants for the next two years.

At the balance sheet date, the Group had contracted with tenants for the following future minimum lease payments:

	December 31,	
	2006 $'000s	2005 $'000s
Within one year	139	55
In the second year	61	88
	200	**143**

Note 34 - Share-Based Payments

Equity-settled share option scheme

The Company has a share option scheme for all employees of the Group. Options are usually exercisable at a price equal to the average quoted market price of the Company's shares on the date of grant. The vesting period is between three to five years. Unexercised options expire ten years from the date of grant. Options are forfeited when the employee leaves the Group.

Options to certain management employees are exercisables at a price equal to the average quoted market price of the Company's shares less 10% on the date of grant.

Details of the share options outstanding during the year are as follows:

	2006		2005	
	Number of share options	Weighted average exercise price (in GBP)	Number of share options	Weighted average exercise price (in GBP)
Outstanding at beginning of period	13,390,124	0.7321	8,937,465	1.1450
Granted during the period	3,715,098	0.2684	5,546,655	0.1747
Forfeited during the period	(661,582)	2.6240	(666,592)	1.9906
Exercise during the period	(656,720)	0.1364	(427,404)	0.1703
Outstanding at the end of the period	**15,786,920**	**0.5664**	**13,390,124**	**0.7321**
Exercisable at the end of the period	**8,581,770**	**0.8639**	**6,665,755**	**1.2536**

The weighted average share price at the date of exercise for share options exercised during 2006 was 0.30 Great British Pounds ("GBP"). The options outstanding at 31 December 2006 had a weighted average exercise price of 0.5093 GBP, and a weighted average remaining contractual life of 5.59 years. In 2006, options were granted on March 1, June 7, June 14, August 30, September 10 and December 22. The aggregate of the estimated fair values of the options granted on those dates is $1,937,000. In 2005, options were granted on May 24, July 16 and September 10. The aggregate of the estimated fair values of the options granted on those dates is $1,766,000.

Note 34 - Share-Based Payments (Cont.)

The inputs into the Black-Scholes model are as follows:

	2006 $'000s	2005 $'000s
Weighted average share price	0.30	0.17
Weighted average exercise price	0.14	0.17
Expected volatility	56-99	56-58
Expected life	7	7
Risk-free rate	4.5%	4%-4.5%
Expected dividends	-	-

Expected volatility was determined by calculating the historical volatility of the Company's share price over the previous 1 year. The expected life used in the model has been adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioural considerations.

The Group recognised total expenses of $767,000 and $424,000 related to equity-settled share-based payment transactions in 2006 and 2005, respectively.

Note 35 - Retirement Benefit Obligation

Defined contribution schemes

The Group operates defined contribution retirement benefit schemes for all qualifying employees in Israel. The assets of the schemes are held separately from those of the Group in funds under the control of trustees. Where there are employees who leave the schemes prior to vesting fully in the contributions, the contributions payable by the Group are reduced by the amount of forfeited contributions.

The employees of the Group's subsidiaries in the United States are members of a state-managed retirement benefit scheme operated by the government of the Unites States. The subsidiary contributes a specified percentage of payroll costs to the retirement benefit scheme to fund the benefits. The only obligation of the Group with respect to the retirement benefit scheme is to make the specified contributions.

Defined benefit schemes

The Group operates defined benefit schemes for qualifying employees of its subsidiaries in Israel. This scheme provides severance pay provision as required by israeli law. No other post-retirement benefits are provided. The schemes are funded schemes.

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at 20 February 2007 by Alan Dubin F.S.A. Ltd., a member of the Institute of Actuaries. The present value of the defined benefit obligation, the related current service cost and past service cost were measured using the projected unit credit method.

The main assumptions used in the actuarial calculation were:

1. Discount rates at a range of 3.6% to 4.09% in 2006 (2005: 3.76% to 4.00%)
2. Expected rate of salary increases of 3.0%. Based on terms of the plans, the fair value of the defined benefit assets approximates it surrender value.

The Liability recognised in the balance sheet at 31 December 2006 was $310,000 (2005: $286,000).

Note 36 - Related Party Transactions

Remuneration of key management personnel

The remuneration of the directors, who are the key management personnel of the group, is set out below in aggregate for each of the categories specified in IAS 24 Related Party Disclosures. Further information about the remuneration of individual directors is provided in the audited part of the Directors' Remuneration Report on pages 45 to 46.

	2006 $'000s	2005 $'000s
Short-term employee benefits	705	312
Post-employment benefits	13	15
Other long-term benefits	22	19
Termination benefits	28	19
Share-based payment	243	127
	1,011	**492**

Directors' transactions

The Company granted to Ofer Bar-Ner, the CFO of the Company a loan in the amount of $50,000, linked to the Israeli consumer price index +4% per annum. The loan will become a non-refundable bonus provided he stays in the company's employ until at least January 1, 2008.

Note 37 - Explanation of Transition to IFRS

This is the first year that the Group has presented its financial statements under IFRS. The following disclosures are required in the year of transition. The last annual financial statements under Israeli GAAP were for the year ended 31 December 2005 and the date of transition to IFRSs was therefore 1 January 2005.

Note 37 - Explanation of Transition to IFRS (Cont.)

Reconciliation of equity at 1 January 2005 (date of transition to IFRS) ($'000s)

	Israeli GAAP	Effect of transition to IFRS	IFRS
Property, plant and equipment	10,587	(963)	9,624
Goodwill	2,475	-	2,475
Financial assets	3,098	-	3,098
Deferred tax assets	-	732	732
Investment in companies	3,688	-	3,688
Total non-current assets	19,848	(231)	19,617
Trade and other receivables	9,779	-	9,779
Inventories	7,425	-	7,425
Short term investments	46,478	-	46,478
Cash and cash equivalents	1,153	-	1,153
Total current assets	64,835	-	64,835
Total assets	**84,683**	**(231)**	**84,452**
Trade and other payables	13,223	5	13,228
Employee termination benefits	376	(95)	281
Total liabilities	13,599	(90)	13,509
Total assets less total liabilities	**71,084**	**(141)**	**70,943**
Share capital	1,177	-	1,177
Share premium account	397,549	-	397,549
Accumulated deficit	(327,658)	(125)	(327,783)
Foreign currency translation adjustment	16	(16)	-
Total equity	**71,084**	**(141)**	**70,943**

Note 37 - Explanation of Transition to IFRS (Cont.)

Reconciliation of equity at 31 December 2005
(date of last Israeli GAAP financial statements) ($'000s)

	Israeli GAAP	Effect of transition to IFRS	IFRS
Property, plant and equipment	10,477	(1,181)	9,296
Intangible assets	1,678	(590)	1,088
Financial assets	8,635	-	8,635
Deferred tax assets	-	649	649
Investment in companies	3,388	-	3,388
Total non-current assets	24,178	(1,122)	23,056
Trade and other receivables	10,794	-	10,794
Inventories	10,445	-	10,445
Short term investments	20,856	(3,083)	17,773
Cash and cash equivalents	18,477	3,083	21,560
Total current assets	60,572	-	60,572
Total assets	**84,750**	**(1,122)**	**83,628**
Interest-bearing loans			
Trade and other payables	14,011	(406)	13,605
Employee termination benefits	372	(86)	286
provision	1,909	(200)	1,709
Current tax liability	171	-	171
Total liabilities	16,463	(692)	15,771
Total assets less total liabilities	**68,287**	**(430)**	**67,857**
Share capital	1,178	-	1,178
Share premium account	397,680	424	398,104
Revaluation reserve	-	(219)	(219)
Accumulated deficit	(330,587)	(619)	(331,206)
Foreign currency translation adjustment	16	(16)	-
Total equity	**68,287**	**(430)**	**67,857**

Note 37 - Explanation of Transition to IFRS (Cont.)

Reconciliation of profit or loss for 2005 ($'000s)

	Israeli GAAP	Effect of transition to IFRS	IFRS
Revenue	56,514	-	56,514
Cost of sales	(34,530)	(218)	(34,748)
Gross profit	21,984	(218)	21,766
R&D expenses	(9,675)	(212)	(9,887)
Sales and marketing expenses	(9,505)	(16)	(9,521)
General and administration expenses	(2,908)	(201)	(3,109)
Finance income	1,510	219	1,729
Finance costs	(51)	-	(51)
Other expenses	(4,091)	17	(4,074)
	(24,720)	(193)	(24,913)
Loss before tax	(2,736)	(411)	(3,147)
Tax expense	(193)	(83)	(276)
Net loss	**(2,929)**	**(494)**	**(3,423)**

Financial Statements

The directors present their report together with the audited financial statements for the year ended 31 December 2006.

Principal Activities and Review of the Business

BATM's main activities are the research and development, production and marketing of data and telecommunication products in the field of local and wide area networks. The operations of the business are reviewed in full in the Chairman's Statement on pages 1-2.

Results and Dividends

The results of the year are set out in the consolidated profit and loss account. After providing $3,273,000 amortization of intangible assets for the year and a write down of one of the Company's investments, we recorded a profit of $6,885,000. No dividend is being declared for the year.

Directors

The following served as directors during the year.

Peter Sheldon FCA, (65), non-executive Chairman, is a Chartered Accountant and International Business Consultant. He is a former finance director of Hambros Bank and has held positions as Chairman and Director of a number of publicly quoted and private companies. During the year his term of office as Honorary President of a major UK Charity came to an end. He is a director of the British Israel Chamber of Commerce. His only other commercial appointment during the year was Chairman of Video Domain Technologies Ltd. a private Israeli video security company. He has been a member of the Board of BATM since 1998 and became Chairman in October 1999.

Dr. Dan Kaznelson, M.D., D.M.D. (65), Senior non-executive, is a Physician, a former Lecturer at The Tel-Aviv University, a self-educated Database Systems Analyst and Programmer, and a reserve Colonel in the Israel Defense Forces. He has held positions as Chairman and Director of a number of private and publicly quoted companies. He has been a member of the Board of BATM since 1996 and is at present Chairman of the Audit and Remuneration Committees.

Dr. Zvi Marom (52), Chief Executive Officer, founded BATM in 1992. He holds degrees in Engineering and Medicine. Prior to establishing BATM, he was the head of the Electronic faculty of the Israeli Open University and senior consultant to several industrial and academic institutions. He graduated in excellence from the naval academy and served in combat command posts. He was awarded the Techmark "Technology Man of the Year" award from the London Stock Exchange in 2000. He is currently a director of Shore Capital, a UK company.

Ofer Bar-Ner (42), Chief Financial Officer, joined BATM in 1999. From 1996 he was Chief Financial Officer of Silver Arrow LP, a subsidiary of Elbit Systems and EL-OP, and between 1989 and 1993 he was group manager in the finance Department of Elbit. He graduated in Industrial Engineering and Management from the Technion in Haifa and has an MBA and MA in accounting from Northeastern University in Boston, MA.

Ariella Zochovitzky (50), CPA, non-executive, is the general manager & partner of C.I.G. Capital Investments Group Ltd. She is currently a director of a number of public and private companies in Israel including Pension Funds at New Makefet, Inspire Investments Ltd., Elco Holdings Ltd and Gazit Inc. She has been a member of the Board of BATM since September 2004.

Koti Gavish (63), non-executive, is the Chief Executive Officer of Eihut Capital Market Ltd. He is currently a director of a number of public and private companies in Israel including Ratio Oil Exploration Ltd., Superior Cables Ltd., Spark Enterprise Ltd. and the Provident Funds of Bank Mercantil Discount Ltd. He has been a member of the Board of BATM since September 2004.

Compliance

The Board supports the principles of corporate governance outlined in the Combined Code on Corporate Governance (Code). This statement describes the manner in which the company has applied the principles set out in Section 1 of the code.

The directors consider that throughout the financial year the company has complied with the requirements of Section 1 of the Code, with the exception of A.1.2 in relation to matters specifically reserved for board decision, and A.1.4 in relation to the company secretary.

The Board

The Board generally meets every three months. This is in compliance with Israeli company legislation. There is not a formal schedule of matters specifically reserved to the Board for decision, as set out in A.1.2 of the Code, however, provisions in the Israeli company legislation set out the responsibilities and duties of and areas of decision for the Board. These provisions have been fully complied with.

The Board comprises six directors, four of whom are non-executive directors, under the chairmanship of Peter Sheldon. The Chief Executive is Dr. Zvi Marom. The senior non-executive director is Dr. Dan Kaznelson. All the directors are of a high calibre and standing. The biographies of all the members of the Board are set out on pages 40 & 41. Dr. Zvi Marom, Dr. Dan Kaznelson, Peter Sheldon and Ofer Bar-Ner hold shares in the company and their share holdings are set out on page 46. All the non-executive directors are independent of management and not involved in any business or other relationship, which could materially interfere with the exercise of their independent judgment.

The induction of newly elected directors into office is the responsibility of the senior independent director (presently Dr. Dan Kaznelson). The new directors receive a memorandum on the responsibilities and liabilities of directors as well as presentations of all activities of the company by senior members of management and a guided tour of the company's premises.

The CEO regularly invites all directors to visit the company premises and its manufacturing facilities. Once per month each director receives a "Flash report" on the company's activities, and information on the performance of the company and a report on the trading and quarterly results of the company are provided at every board meeting. Once per year a budget is discussed and approved by the Board for the following year. All directors are properly briefed on issues arising at Board meetings and any further information requested by a director is always made available.

Under Israeli law it is not a mandatory requirement for a company to have a secretary and the company does not therefore have a formally appointed secretary. However, Mr. Arthur Moher, who is also one of the company's legal advisers, provides the company with all the functions of company secretary and all the directors have access to Mr. Moher's services. The directors are therefore of the opinion that the spirit of A.1.4 of the Code has been complied with.

The directors may take independent professional advice at the company's expense in furtherance of their duties. Independent outside counsel is always present at Board meetings and Board committee meetings.

Relations with Shareholders

The company's management generally meets with the institutional shareholders after the publication of its interim and final financial statements. The Board supports the use of the annual general meeting to communicate with private investors.

Nominations Committee

The Board has a nominations committee which is chaired by Peter Sheldon. Individuals nominated as directors are elected by the shareholders in general meeting. Executive and non-executive directors are elected by the shareholder's General Meeting for a term of one year. Non-executive public "external" directors, as defined by Israeli Company Law are appointed and elected for a mandatory term of three years, which is renewable for a further term of three years. The re-appointment of a director must be approved by the shareholders in general meeting.

Directors' Remuneration

The Board has a Remuneration Committee, which is chaired by Dr. Dan Kaznelson. Information about the service contracts of the executive directors and the remuneration of directors is set out in the Remuneration Report on page 45 & 46.

Accountability and Audit

Auditors

Brightman Almagor & Co., a member firm of Deloitte Touche Tohmatsu, has expressed its willingness to continue in office and a resolution to re-appoint the firm will be proposed at the annual general meeting.

Audit Committee

The company has an Audit Committee, which consists of three out of the four non-executive directors, Dr. Dan Kaznelson (chairman), Mrs. Ariella Zochovitzky and Mr. Koti Gavish

The Audit Committee meets a minimum of twice a year and the internal and external auditors also attend the meetings. The Audit Committee adheres to the functions and requirements prescribed to it by the Israeli Companies Act and Israeli law. The Chairman of the Audit Committee maintains close contact with the company on a weekly basis.

The "Market Abuse Directive"

The Board of Directors has established a committee in order to study the draft "Market Abuse Directive" and to supervise the implementation of the guidelines laid down in the "Market Abuse Directive".

As of 1 January, 2006 the company complies of with these guidelines, including inter alia, the maintaining of "insider lists" of all individuals with access to inside information of the company.

Internal Control

The Board of directors has overall responsibility for ensuring that the company maintains adequate systems of internal control. To this end, in accordance with Israeli Company Law, the company retains the services of an independent external auditor. The internal auditor reports to the Audit Committee, and is responsible for ensuring that the company is run according to good corporate practice.

Risk management is currently reviewed on an ongoing basis by the Board as a whole. The key features of the financial controls of the company include a comprehensive system of financial reporting, budgeting and forecasting, and clearly laid down accounting policies and procedures. The Board of the company is furnished with detailed financial information on a monthly basis.

Statement of Directors' Responsibilities

After making enquiries, the Directors have a reasonable expectation that the Company and its subsidiaries have adequate resources to continue in operational existence for the foreseeable future. For this reason, they have adopted the going concern basis in preparing the financial statements.

Company law requires the Directors to prepare financial statements for each financial period, which give a true and fair view of the state of affairs of the Company and the Group, and of the profit and loss of the Group for the period. In preparing these financial statements, the Directors are required to: select suitable accounting policies and then apply them consistently; make judgments and estimates that are reasonable and prudent; state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Environmental Policy

The Directors recognize the importance of the Group adhering to clear environmental objectives.

Its environmental policy is to:

- Meet the statutory requirements placed on it;
- Adopt good environmental practice in respect of premises, product development and manufacturing, and consumption of resources;
- Aim to recycle as much of its waste products as it is economically practicable to do.

The Company is implementing the recommendations of ROHS (The Restriction of Hazardous Substances in Electrical and Electronic Equipment (ROHS) Directive (2002/95/EC), and as from the year 2006, all its products will be fully ROHS compatible

Directors' Remuneration

Remuneration Committee and Remuneration Report

The remuneration committee consists of three out of the four non-executive directors. As presently constituted, the committee consists of Dr. Dan Kaznelson, Mrs. Ariella Zochovitzky and Mr. Koti Gavish. Dr. Dan Kaznelson serves as chairman. The committee is responsible for recommendation to the board of the remuneration strategy and policy of the company for determining the short and long-term incentive pay structures for the executive directors. With the exception of the "public external" non-executive directors who serve for a period of three years in accordance with Israeli company law, all directors have to be re-elected by the shareholders at AGM, if proposed for re-election.

In accordance with Israeli company law, the Board recommends and the general meeting of the Company is asked to approve, the remuneration of the executive and non-executive directors of the company, after it has been first approved by the company's Remuneration Committee. The remuneration of the executive and non-executive directors of the company for the year ended 31 December 2005 was as follows:

Executive Directors in 2006

Dr. Zvi Marom – CEO – earned a basic salary of $200,000 and social benefits as are normally granted by employers in Israel. An annual profit share bonus, based on the rate of increase in net profit of each year, is also payable, the terms having been approved at the Company's AGM on 25, May 2005. A bonus of $275,000 was accrued in respect of 2006 under this plan. A special bonus of $100,000 was paid in respect of 2005.

Ofer Bar-Ner – CFO – earned a basic monthly salary of NIS 35,000 and social benefits. In 2006, a loan of $50,000 was approved at the Company's AGM the loan will became a non-refundable bonus to Mr. Bar-Ner provided he stays in the company's employ until at least January 1 2008.

	2006	2005
	Salary and Benefits	Salary and Benefits
Dr. Zvi Marom	622	270
Ofer Bar-Ner	149	78

Non-executive Directors in 2006

The non-executive Chairman is remunerated at a rate of $18,000 per annum, plus $3,000 for each Board or other meeting attended. Dr. Dan Kaznelson is paid $9,000 per annum and $1,500 per meeting respectively. Mrs. Ariella Zochovitzky and Mr. Koti Gavish, the Public external Directors, were remunerated in accordance with Israeli Company Law provisions for such appointees. In addition they received a remuneration package of 200,000 share options each per annum, as approved by the Shareholders Annual Meeting at the time of their election as directors.

The Chairman's remuneration reflects both his responsibility and the fact that, as a resident of the UK, he has to travel to Israel for board meetings. These fees were arrived at by reference to fees paid by other companies of similar size and complexity and reflected the amount of time that non-executive directors are expected to devote to the company's activities during the year.

Directors' Remuneration

	2006 Fees	2005 Fees
Peter Sheldon	38	38
Dr. Dan Kaznelson	23	18
Daniel Goldman	-	3
Ariella Zochovitzky	10	10
Koti Gavish	10	10

Directors' Interest in Shares

The directors of the company are listed below together with their beneficial interests in the shares of the company at the beginning and end of the financial year.

	0.01 NIS Ordinary Shares fully paid 2006	0.01 NIS Ordinary Shares fully paid 2005
Dr. Zvi Marom	92,750,900	91,750,900
Dr. Dan Kaznelson	146,300	135,300
Peter Sheldon	300,000	100,000
Ofer Bar-Ner	158,600	58,600

Directors' Options (Accumulated)

	Number of options 2006	Number of options 2005
Dr. Zvi Marom (1)	2,700,000	2,700,000
Ofer Bar-Ner (2)	1,333,333	333,333
Ariella Zochovitzky (3)	600,000	400,000
Koti Gavish (4)	600,000	400,000

(1) The grant is of :

a: 400,000 options exercisable into 100,000 ordinary shares of the company per year commencing on July 1, 2000 and on July 1, of every subsequent year. Each option vests and is exercisable 24 months from the date of each grant, at a price equal to the then current market price less ten per cent.

b: 300,000 options granted at an exercise price of £0.20 per share these options will vest at a rate of 100,000 options annually on July 1st of each year commencing from July 1, 2004.

c: 2,000,000 options granted as follows: one million at an exercise price of £0.1625 per share these options will vest over 3 years commencing from December 31, 2005. The additional one million are performance linked incentive provided that the annual net profit of the company has increased by at least 15% as compared with the previous year and that the company has made a net profit in the relevant financial year, the exercise price is £0.1625 per share and will vest over 3 years commencing from December 31, 2005.

(2) The grant is of:

a: 333,333 options vested fully on January 1, 2004 at exercise price of £0.2648.

b: 1,000,000 options granted at an exercise price of £0.24 per share these options will vest over 3 years commencing from February 1, 2006.

(3) Exercise price of £0.1621 per share. These options will vest at a rate of 200,000 options annually on December 31 of each year commencing from December 31, 2004.

(4) Exercise price of £0.154 per share. These options will vest at a rate of 200,000 options annually on December 31 of each year commencing from December 31, 2004.

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