ELBIT VISION SYSTEMS LTD.

(An Israeli Corporation)

2007 CONSOLIDATED FINANCIAL STATEMENTS

ELBIT VISION SYSTEMS LTD.

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Deloitte

Brightman Almagor
1 Azrieli Center
Tel Aviv 67021
P.O.B. 16593, Tel Aviv 61164
Israel

Tel: +972 (3) 608 5555
Fax: +972 (3) 609 4022
info@deloitte.co.il
www.deloitte.com

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and
Shareholders of Elbit Vision Systems Ltd.

We have audited the accompanying consolidated balance sheets of Elbit Vision Systems Ltd. ("the Company") and its subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2007. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2007 and 2006 and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles.

Brightman Almagor & Co.

Brightman Almagor & Co.
Certified Public Accountants
A member firm of Deloitte Touche Tohmatsu

Tel Aviv, Israel
March 31, 2008

ELBIT VISION SYSTEMS LTD.

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands

	Note	December 31 2007	December 31 2006
A s s e t s			
CURRENT ASSETS:			
Cash and cash equivalents		2,189	1,060
Restricted deposit (short term)	14	540	688
Accounts receivable:	15a		
Trade (net of allowance for doubtful account 2007- $677 ,2006- $936)		4,738	3,198
Other		1,428	603
Inventories	4	5,299	3,968
T o t a l current assets		14,194	9,517
INVESTMENTS AND LONG-TERM RECEIVABLES:			
Severance pay fund	8	1,623	1,891
Other long-term receivables and investment	5	231	1,066
		1,854	2,957
PROPERTY AND EQUIPMENT, net of accumulated depreciation and amortization	6	490	455
OTHER ASSETS, net of accumulated amortization			
Goodwill		3,529	2,363
Other intangible assets	7	3,439	4,098
		6,968	6,461
T o t a l assets		23,506	19,390

The accompanying notes are an integral part of the financial statements

ELBIT VISION SYSTEMS LTD.

CONSOLIDATED BALANCE SHEETS (Cont.)

U.S. dollars in thousands

	Note	December 31 2007	December 31 2006
Liabilities and shareholders' equity			
CURRENT LIABILITIES:			
Credit from banks	15c	4,967	4,713
Current maturities of loan from shareholder	9a	-	160
Short term loan from banks	9a	-	2,015
Accounts payable and accruals:			
Trade		3,220	3,502
Deferred income	2i	2,082	1,617
Other	15b	2,629	3,583
T o t a l current liabilities		12,898	15,590
LONG-TERM LIABILITIES:			
Loans and other liabilities (net of current maturities)	9	1,000	-
Loans from Related Parties (net of current maturities)	9	-	609
Accrued severance pay	8	2,008	2,190
T o t a l long-term liabilities		3,008	2,799
COMMITMENTS AND CONTINGENT LIABILITIES	10		
T o t a l liabilities		15,906	18,389
SHAREHOLDERS' EQUITY:	11		
Share capital – ordinary shares of NIS 1 par value ("Ordinary Shares");			
Authorized – 60,000,000 Ordinary Shares as of December 31, 2007			
60,000,000 ordinary shares as of December 31, 2006			
Issued and outstanding:			
December 31, 2007 – 50,791,382 Ordinary shares			
December 31, 2006 – 29,516,314 Ordinary shares		10,629	5,091
Additional paid-in capital		28,249	25,846
Accumulated deficit		(31,278)	(29,936)
T o t a l shareholders' equity		7,600	1,001
T o t a l liabilities and shareholders' equity		23,506	19,390

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

ELBIT VISION SYSTEMS LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS

U.S. dollars in thousands (except per share data)

	Note	Year ended December 31, 2007	2006	2005
REVENUES:				
Sale of products		18,690	14,527	15,428
Services rendered		3,173	2,470	4,151
		21,863	16,997	19,579
COST OF REVENUES:	15d			
Cost of products sold		9,382	10,367	9,422
Cost of services rendered		1,926	1,869	2,211
		11,308	12,236	11,633
GROSS PROFIT		10,555	4,761	7,946
RESEARCH AND DEVELOPMENT COSTS – NET	15e	3,313	2,562	2,039
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES:				
Marketing and selling		4,885	4,149	3,583
General and administrative		1,338	1,870	1,127
Reorganization expenses		-	200	-
OPERATING INCOME (LOSS)		1,019	(4,020)	1,197
**FINANCIAL EXPENSES - **NET	15f	(1,081)	(1,332)	(437)
INCOME (LOSS) BEFORE OTHER INCOME (EXPENSES)		(62)	(5,352)	760
OTHER INCOME (EXPENSES)	15g	(1,277)	(5)	7
INCOME (LOSS) BEFORE TAXES ON INCOME		(1,339)	(5,357)	767
TAXES ON INCOME	12d	3	5	4
INCOME (LOSS) FOR THE YEAR FROM CONTINUING OPERATIONS		(1,342)	(5,362)	763
LOSS FROM OPERATIONS OF DISCONTINUED COMPONENT	3a	-	(180)	(152)
NET LOSS ON DISPOSAL OF DISCONTINUED OPERATION	3a	-	(551)	-
INCOME (LOSS) FOR THE YEAR		(1,342)	(6,093)	611
EARNING (LOSS) PER SHARE FROM CONTINUING OPERATIONS:	2m			
Basic		(0.034)	(0.186)	0.029
Diluted		(0.034)	(0.186)	0.026
LOSS PER SHARE FROM DISCONTINUED OPERATIONS:	2m			
Basic		-	(0.026)	(0.006)
Diluted		-	(0.026)	(0.005)
EARNING (LOSS) PER SHARE:	2m			
Basic		(0.034)	(0.212)	0.023
Diluted		(0.034)	(0.212)	0.021
WEIGHTED AVERAGE NUMBER OF SHARES USED IN COMPUTATION OF EARNING (LOSS) PER SHARE – BASIC (IN THOUSANDS)		39,393	28,778	26,500
DILUTED (IN THOUSANDS)		39,393	28,778	28,421

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

ELBIT VISION SYSTEMS LTD.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Share capital		Receipts on account of shares to be allotted	Additional paid-in Capital*	Other comprehensive income	Accumulated deficit	Total shareholders' equity
	Number of shares	Amount					
	In thousands		U.S. dollars in thousands				
BALANCE – DECEMBER 31, 2004	25,682	3,863	70	22,535	132	(24,454)	2,146
CHANGES DURING 2005:							
Net income for the year						611	611
Currency translation differences					(43)		(43)
Total comprehensive income							568
Employee stock options exercised and paid	82	18		(1)			17
Receipts on account of shares to be allotted			105				105
Issuance of share capital and warrants (note 11a)	815	607	(175)	766			1,198
Warrant exercised and paid (note 11a,11b)	183	41		24			65
BALANCE – DECEMBER 31, 2005	26,762	4,529	-	23,324	89	(23,843)	4,099
CHANGES DURING 2006:							
Loss for the year						(6,093)	(6,093)
Currency translation differences					(89)		(89)
Total comprehensive income							(6,182)
Employee stock options exercised and paid	182	40		(1)			39
Issuance of share capital and warrants (notes 3b,11a)	2,441	494		1,606			2,100
Beneficial conversion feature (note 9a(3))				900			900
Warrant exercised and paid	131	28		17			45
BALANCE – DECEMBER 31, 2006	29,516	5,091	-	25,846	-	(29,936)	1,001
CHANGES DURING 2007:							
Loss for the year						(1,342)	(1,342)
Issuance of share capital and warrants (note 11a)	21,275	5,538		2,403			7,941
BALANCE – DECEMBER 31, 2007	50,791	10,629	-	28,249	-	(31,278)	7,600

* Net of share issuance costs.

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

ELBIT VISION SYSTEMS LTD.
CONSOLIDATED STATEMENTS OF CASH FLOWS
U.S. dollars in thousands

	Year ended December 31,		
	2007	**2006**	**2005**
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (Loss)	(1,342)	(6,093)	611
Adjustments to reconcile net income (loss) to net cash provided by or used in operating activities:			
Depreciation and amortization	1,241	1,411	886
Amortization of discount on loan from shareholder	1,212	285	-
Loss from disposal of property	-	48	7
Loss from disposal of discontinued operation	-	551	-
Liability for employee rights upon retirement	(182)	118	55
Changes in operating assets and liabilities:			
Decrease (increase) in trade accounts receivable (including non-current portion)	(1,540)	283	(1,013)
Decrease (increase) in other accounts receivable	(465)	443	(168)
Increase (decrease) in trade account payable	(282)	1,003	29
Deferred income	465	(897)	1,725
Other	(965)	(2,212)	(1,523)
Decrease (increase) in inventories	(1,331)	591	123
Net cash provided by (used in) operating activities	(3,189)	(4,469)	432
CASH FLOWS FROM INVESTING ACTIVITIES:			
Acquisition of subsidiary consolidated for the first time (a)	-	-	-
Disposal of subsidiary (b)	-	120	-
Purchase of property and equipment	(296)	(130)	(222)
Long-term receivables	400	(101)	7
Redemption of (investment in) restricted deposit	148	1,122	(1,042)
Proceeds from disposal of property and equipment	38	30	16
Funds severance pay	268	(258)	(244)
Net cash provided by (used in) investing activities	558	783	(1,485)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Issuance of share capital and warrants - net of issuance costs	4,521	964	-
Short-term credit from bank – net	(761)	2,281	797
Proceeds from exercise of options and warrants	-	77	187
Retirement of long-term loan from shareholder	-	(27)	-
Proceeds from long-term loans from shareholder	-	1,556	-
Proceeds from long-term loans from bank	-	547	1,454
Short-term credit paid to Cornell Capital Partners L.P. – net	-	(1,449)	(1,719)
Net cash provided by financing activities	3,760	3,949	719
TRANSLATION DIFFERENCES ON CASH BALANCES OF CONSOLIDATED SUBSIDIARY	-	(89)	(2)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,129	174	(336)
BALANCE OF CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,060	886*	1,222*
BALANCE OF CASH AND CASH EQUIVALENTS AT END OF YEAR	2,189	1,060	886*
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION - cash paid during the year for:			
Interest paid - net	704	415	295
Income taxes paid – net	3	5	4

* Including cash and cash equivalents from discontinuing operation.

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

CONSOLIDATED STATEMENTS OF CASH FLOWS (Cont.)

	2006
	U.S. dollars in thousands
(a) Acquisition of subsidiary consolidated for the first time, see also note 3:	
Assets and liabilities of the subsidiary at date of acquisition:	
Working capital (excluding cash and cash equivalents)	(1,033)
Fixed assets	59
Long-term receivables	12
Other assets	1,514
Long-term loans and other liabilities	(9)
Goodwill arising on acquisition	-
	543
Less:	
Issuance of share capital and warrants (see c 2) hereafter)	(543)
	-

	2006
	U.S. dollars in thousands
(b) Disposal of subsidiary	
Assets and liabilities of the subsidiary at date of disposal:	
Working capital (excluding cash and cash equivalents)	346
Fixed assets	(284)
Long-term receivables	(193)
Other assets	(148)
Long-term loans and other liabilities	232
Goodwill	(1,039)
	(1,086)
Less:	
Future proceeds from selling the subsidiary	966
	(120)

(c) Supplementary information on financing activities not involving cash flow:

1) $ 1,168,000 worth of shares were released from escrow and $ 1,970,000 long term loan from shareholders were converted into share capital (see Notes 9 a.(2),(3) and 11 a.4),5)).
2) During 2006 part of the acquisition of the subsidiary was made through issuance of share capital in an amount equivalent to $ 543,000.

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

NOTE 1 - GENERAL

Elbit Vision Systems Ltd. (the "Company") is an Israeli corporation, which, together with its subsidiaries (the "Group"), is principally engaged in the design, development, manufacturing and marketing automatic vision and ultrasonic inspection and quality monitoring systems, and rending services related to those systems.

Elbit Vision Systems Inc. ("EVS Inc.") incorporated in Delaware U.S.A. and Elbit Vision Systems B.V. ("EVS BV") incorporated in the Netherlands are wholly-owned subsidiaries, engaged in the selling and marketing of the Company's products worldwide.

In June 2004, the Company expanded its activities and entered into new fields of operations through the acquisition of 70% of Yuravision Co. Ltd.'s ("Yuravision") shares, a South Korean developer of visual inspection software and systems for the microelectronics industry and display industries. This investment was sold during December 2006 and therefore presented as discontinued operation in the financial statements (see Note 3a).

In September 2004, the Company also completed the acquisition of the entire shareholding of ScanMaster Systems (IRT) Ltd. ("ScanMaster Ltd."), an Israeli company and IRT ScanMaster System Inc. ("ScanMaster Inc."), a new Hampshire corporation (collectively - "ScanMaster"). ScanMaster is engaged in the development, manufacturing and marketing of equipment for the ultrasonic inspection of industrial parts and components for the automotive and transportation industries, the metal industry as well as applications for aircraft and jet engine inspection.

In February 2006, the Company acquired business, assets and liabilities of Panoptes Ltd.("Panoptes") and ScanMaster Ltd. acquired 100% of the shares of Panoptes.
Panoptes Ltd. is principally engaged in the design, development, manufacturing and marketing automatic vision and quality monitoring systems for surface inspection, especially textiles, glass fabric and technical woven materials (see Note 3b).

As to Business and Geographical segments – see Note 17.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES:

The consolidated financial statements are prepared in accordance with accounting principles generally accepted ("GAAP") in the United States of America.

a. Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting years. Actual results could differ from those estimates.

Estimates and assumptions which, in the opinion of management, are significant to the underlying amounts included in the financial statements and for which it would be reasonably possible that future events or information could change those estimates include: (i) impairment assessments of goodwill and long-lived assets; (ii) realization of deferred income tax assets; and (iii) provisions for obsolete and slow moving inventory, These estimates are discussed further throughout the accompanying notes.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

b. Functional Currency and Financial Statements in U.S. Dollars

The currency of the primary economic environment in which operations of the Company and its subsidiaries are conducted is the U.S. dollar (the "dollar").

Virtually all sales by the Company and its subsidiaries are made outside Israel in non-Israeli currencies, mainly the dollar. Most purchases of materials and components are made in dollars or in Israeli currency under contracts linked to the dollar. In addition, most marketing and service costs are incurred outside Israel, primarily in dollars, through the Company's wholly-owned non-Israeli subsidiaries. Thus, the functional currency of the Company and its subsidiaries is the dollar.

Transactions in currencies other than each company's functional currency are translated based on the average currency exchange rates in accordance with the principles set forth in Statement of Financial Accounting Standards ("SFAS") No. 52, "Foreign Currency Translation". All gains and losses from translation of monetary balance sheet items and transactions denominated in currencies other than the functional currency are recorded in the statements of income as financial income, net as they arise.

c. Principles of consolidation

The consolidated financial statements include the financial statements of the company and its wholly-owned subsidiaries.

All material inter-company transactions and balances have been eliminated.

d. Cash Equivalents

Cash equivalent consist of short-term highly liquid investments, that are readily convertible into cash with original maturities when purchased of three month or less.

e. Allowance for doubtful accounts

The allowance for doubtful accounts has been made on the specific identification basis.

f. Inventories

Inventories are stated at the lower of cost or market. Cost is determined as follows:
Raw materials and spare parts - on moving average basis.
Product in process and finished products – on basis of production costs.

Inventories are written-down for estimated obsolescence, based on assumptions about future demand and market conditions.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

g. Property and equipment

(1) Property and equipment are stated at cost . Depreciation is calculated by the straight-line method over the estimated useful lives of assets, as follows:

	%
Machinery and equipment	10-33 (mainly 33%)
Office furniture and equipment	6-20
Vehicles	15-20

Leasehold improvements are amortized by the straight-line method over the term of the lease, or the estimated useful life of the improvements, whichever is shorter.

(2) **Impairment of long-lived assets** – Impairment examinations and recognition are performed and determined based on the provisions of FASB Statement No. 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets*" ("SFAS 144"). SFAS 144 requires that long-lived assets and certain identifiable assets held for use be reviewed for impairment on a periodic basis, or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of an asset to be held and used is determined by a comparison of the carrying amount of the asset and the amount of undiscounted future net cash flows to be generated by the asset or assets group. In the event that an asset is considered to be impaired, an impairment charge is recorded in the amount by which the carrying amount of the asset exceeds its estimated fair value.

h. Other assets- Goodwill and Intangible Assets

(1) Goodwill

Under FASB Statement No. 142, "*Goodwill and Other Intangible Assets*" ("SFAS 142"), goodwill is not amortized to earnings, but rather is subject to periodic testing for impairment, at the reporting unit level, at least annually or more frequently if certain events or indicators of impairment occur. Impairment is the condition that exists when the carrying amount of goodwill exceeds its implied fair value. Measurement of an impairment loss is an estimate, performed based on the following: If the fair value of the reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired. If the carrying amount of the reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. The Group uses the discounted cash flow method to determine the fair value of the reporting unit. The Company's reporting units consist of reportable segments; goodwill is allocated to the Non-destructive automated inspection segment (see also Note 17).

The Company has designated December 31 of each year as the date on which it will perform its annual goodwill impairment test. No impairment resulted from the annual review performed in the year 2007.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

h. Other assets- Goodwill and Intangible Assets (Cont.)

(2) Other intangible assets

These assets are amortized by the straight-line method over their estimated useful lives. Annual rates of amortization are as follows:

	%
Technology	10;20
Customer relations	10;20
Distribution network	10
Brand name	8.33

The backlog is amortized according to revenues, which are derived from specific orders.

i. Revenue recognition:

1) Sale of products:

a. General

Revenues from sales of products and supplies are recognized when an arrangement exists, delivery has occurred and title passed to the customer, Group's price to the customer is fixed or determinable and collectibility is reasonably assured.

With respect to systems sold with installation requirements, the installation is not considered to be a separate earnings process; thus, revenue is recognized when all of the above criteria are met and installation is completed.

b. Acceptance clause, customers' support service and warranty

The Group distinguishes between revenue recognition in respect of revenue derived from automatic vision inspection products (sold by the Company) and ultrasonic inspection products (sold by ScanMaster).
The terms of the agreements between the Company and its customers are substantially different from the terms of the agreements between ScanMaster and its customers. Therefore, the revenue recognition accounting policy applied by each of the companies is different in this case. Set forth bellow are the main accounting policies applied by each of the companies:

The Company

In case that Company's agreement with the customer includes an "acceptance" clause, revenue recognition will take place after the Company receives the "acceptance certificate" from the customer. In some cases, the Company grants its customers a trial period, usually several months, in order to evaluate prototype of the system's performance. In case that the systems performance meets the customer's requirements, it purchases the system at the end of the trial period. The Company does not recognize sales revenue from products shipped to customers for trial until such products are actually purchased. Until purchased, these products are recorded as consignment inventory at the lower of cost or market.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

i. Revenue recognition (Cont.):

1) Sale of products (Cont.):

b. Acceptance clause, customers' support service and warranty

ScanMaster

ScanMaster's agreements with its customers usually include acceptance testing procedures clause ("ATP"). Each product of ScanMaster has standard performance specifications that are examined in the ATP; usually, the performance specifications are not customized for the specific needs of the customer. Also, unlike in the case of the company, ScanMaster does not grant its customers a trial period in the normal course of business. The agreements with the clients do not include the right of the clients to a refund in case the ATP is not to their satisfaction. However, the collection of the final payment from the customer (usually 10% out of the total consideration) is dependent upon receiving the signed ATP.

ScanMaster distinguishes between sales of new products, in respect of which ScanMaster has no past installation experience and sales of products, in installation of which the company is well experienced. In respect of sales of new products ScanMaster recognizes revenues only after the company receives the ATP from the customer. In respect of sales of other products, in the installation of which the company is well experienced, the ATP is only a formal procedure, and therefore, the installation of products is a sufficient requirement to recognize revenues.

ScanMaster provides for warranty costs at the same time as the revenue is recognized. The annual provision is calculated at rates of 0.5%-2% of the sales, based on past experience.

c. Right of return

The Group does not provide, in the normal course of business, a right of return to its customers. If uncertainties exist, such as the granting to the customer of a right of cancellation, revenue is recognized when the uncertainties are resolved.

d. Revenues from systems that require significant customization, integration and installation are recognized based on SOP 81-1 "Accounting for Performance of Construction - Type and Certain Production - Type Contracts", using contract accounting on the percentage of completion method, based on the relationship of actual labor costs incurred, to total labor costs estimated to be incurred over the duration of the contract. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract.

Arrangements that include professional services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. When services are considered essential, revenue under the arrangement is recognized using contract accounting.

When services are not considered essential, the revenue allocable to the software services is recognized as the services are performed.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

i. Revenue recognition (Cont.):

2) Services rendered

Service revenue in respect of the Group's products is recognized ratably over the contractual period, or as services are performed.

3) Deferred income

The deferred income balance as of December 31, 2007 and 2006 include amounts of revenues that were invoiced and cash was received, but deferred less applicable product and warranty costs.

j. Research and development

Research and development expenses net of third party grants, are expensed as incurred.
The Company has no obligation to repay the grants if sales are not generated.

k. Advertising expenses

Advertising expenses are expenses as in incurred. Advertising expenses for the years ended December 31, 2007, 2006 and 2005 were $ 428,000 $ 470,000, and $ 122,000, respectively.

l. Deferred income taxes

The company accounts for income taxes in accordance with FASB Statement No. 109, "Accounting for Income Taxes" ("SFAS 109"). Deferred income taxes are determined by the asset and liability method based on the estimated future tax effects attributable to temporary differences between income tax bases of assets and liabilities and their reported amounts in the financial statements, and to carryforwards for tax losses and deductions. Deferred tax balances are computed using the enacted tax rates to be in effect at the time when these differences are expected to reverse, as they are known at the balance sheet date.

Deferred tax assets and liabilities are classified as current or non-current according to the classification of the respective asset or liability, or the expected reversal date of the specific temporary difference, if not related to a specific asset or liability.

Valuation allowances in respect of deferred tax assets are established when it is more likely than not that all or a portion of the deferred income tax assets will not be realized.

m. Earning (loss) per share ("EPS")

Basic EPS is computed based on the weighted average number of shares outstanding during each year. 1,718,749 ordinary shares, which were issued and were placed in escrow were reflected in basic and diluted EPS shares for the years ended December 31, 2006 and 2005. Total common stock equivalents, related to options and warrants, 1,921,496 were reflected in diluted EPS for the year ended December 31, 2005. Total common stock equivalents, related to options and warrants 16,862,858, 9,322,308 and 8,716,907 shares for the years 2007 , 2006 and 2005, respectively, were excluded from EPS calculation, because the effect of such options and warrants is antidilutive.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

n. Stock-based compensation

In January 2006, the Company adopted SFAS No. 123(R), “Share-Based Payment” (“SFAS No. 123(R)”), using the modified prospective application method as its transition method. The Company recognizes $ 282,000 of compensation expenses in 2007 as a result of the application of SFAS 123 (R). Until the adoption of SFAS No. 123(R) the Company accounted for employees and directors stock-based compensation in accordance with Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees” (“APB 25”) and in accordance with FASB Interpretation No. 44 (“FIN 44”). Pursuant to these accounting pronouncements, the Company recorded compensation for stock options granted to employees and directors over the vesting period of the options based on the difference, if any, between the exercise price of the options and the market price of the underlying shares at that date.

Had compensation cost for the Company’s stock option plans been determined based on fair value at the grant dates for all awards made in 2005 in accordance with the provisions of SFAS No. 123 (“SFAS 123”), as amended by SFAS No. 148 “Accounting for Stock-Based Compensation” (“SFAS 148”), the Company’s pro forma net loss per share would have been as follows:

	Year ended December 31 2005 $ in thousands (except per share data)
Net income as reported	611
Less - stock-based employee compensation expense determined under fair value method	(559)
Pro forma net income	52
Earning per share:	
Basic - as reported	$ 0.023
Diluted - as reported	$ 0.021
Basic - pro forma	$ 0.002
Diluted - pro forma	$ 0.002

As to information about the stock option plans and assumptions used in calculating the pro forma information, see Note 11b.

o. Comprehensive income

In addition to income (loss), other comprehensive income includes exchange differences arising from the translation of the net investment in subsidiary.

p. Reclassification

Certain comparative figures have been reclassified to conform to the current year presentation.

q. Consentration of credit risk

As of December 31, 2007 and 2006, the Group held cash and cash equivalents and short-term bank deposits, most of which were deposited with major Israeli, European, and U.S. banks. The Company is of the opinion that the credit risk in respect of these balances is insignificant.

The Group performs ongoing credit evaluations of its customers for the purpose of determining the appropriate allowance for doubtful accounts. In respect of sales to customers in emerging economies, the Group requires letters of credit from banks.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

r. Recently issued accounting pronouncements:

1) In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" ("FAS 157"). FAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements; however, it does not require any new fair value measurements. FAS 157 is effective for fiscal years beginning after November 15, 2007 (January 1, 2008, for the Company). Earlier application is encouraged, provided that the reporting entity has not yet issued financial statements for that fiscal year, including any financial statements for an interim period within that fiscal year. The Company is currently evaluating the impact of the provisions of FAS 157 on its financial position and results of operations.

2) In February 2007, the FASB issued FASB No. 159, The Fair Value Option for Financial Assets and Financial Liabilities—Including an Amendment of FASB Statement No. 115. This standard permits an entity to choose to measure many financial instruments and certain other items at fair value. Most of the provisions in FASB No. 159 are elective; however, the amendment to FASB No. 115, Accounting for Certain Investments in Debt and Equity Securities, applies to all entities with available-for-sale and trading securities. The fair value option established by FASB No. 159 permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity will report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date. The fair value option: (a) may be applied instrument by instrument, with a few exceptions, such as investments otherwise accounted for by the equity method; (b) is irrevocable (unless a new election date occurs); and (c) is applied only to entire instruments and not to portions of instruments. FASB No. 159 is effective as of the beginning of an entity's first fiscal year that begins after November 15, 2007. The Company does not expect the adoption of FASB No. 159 to have a material impact on its consolidated financial statements.

3) In December 2007, the FASB issued FASB 141(R), "Business Combinations" of which the objective is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a business combination and its effects. The new standard requires the acquiring entity in a business combination to recognize all (and only) the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose to investors and other users all of the information they need to evaluate and understand the nature and financial effect of the business combination.

4) In December 2007, the FASB issued FASB 160 "Noncontrolling Interests in Consolidated Financial Statements--an amendment of ARB No.51" of which the objective is to improve the relevance, comparability, and transparency of the financial information that a reporting entity provides in its consolidated financial statements by establishing accounting and reporting standards by requiring all entities to report noncontrolling (minority) interests in subsidiaries in the same way--as equity in the consolidated financial statements. Moreover, Statement 160 eliminates the diversity that currently exists in accounting for transactions between an entity and noncontrolling interests by requiring they be treated as equity transactions.

Both FASB 141(R) and FASB 160 are effective for fiscal years beginning after December 15, 2008. The Company does not believe that adoption of these standards will have any impact on its financial statements.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

s. Initial adoption of new standards:

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109" (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing the recognition threshold a tax position is required to meet before being recognized in the financial statements. It also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006 and was adopted by the Company in 2007. The adoption of FIN 48 did not have a material impact on its consolidated results of operations and financial condition.

NOTE 3 - CONSOLIDATED SUBSIDIARIES

a. Acquisition and Disposal of Yuravision

On December 2, 2003, the Company signed a term sheet (the validity of which was extended on February 16, 2004) to acquire 100% of the shares of Yuravision (as to the nature of operation of Yuravision, see Note 1).

Pursuant to the term sheet, through June 30, 2004, the Company entered into a series of purchase agreements with some of Yuravision's shareholders. Under those agreements, the Company purchased 51% of Yuravision's shares for an aggregate amount of $ 1,014,000, in cash and has a legal commitment to purchase additional 19% of Yuravision shares.

The total cost of acquisition amounted to $ 1,484,000 (including legal fees and other direct costs of $ 134,000, and the aggregate fair value of the warrants issued to Yuravision's shareholder of $ 30,000).

On December 1, 2006, the Company executed an agreement with a Korean corporation for the sale of Yuravision shares in consideration for $950,000, or the Purchase Price, plus the purchase from the Company of its right to receive from Yuravision repayment of an $800,000 loan, or the Loan Amount in consideration for the full value of the loan. Half of the Purchase Price was paid upon the closing of the transaction on December 15, 2006, and the remaining half of the Purchase Price will be payable no later than December 1, 2008. The purchaser has undertaken to pay the Company half of the Loan Amount by no later than December 1, 2008 and the remaining half, or the Outstanding Payment, by no later than May 1, 2009.

The Company have received a stand by letter of credit from the purchaser guaranteeing payment of the Loan Amount.

Consideration for assignment of the Loan was subject to reduction in the event that certain key employees of Yuravision terminated their employment; provided that the Korean corporation was unable to find replacements using the services of an employment agency. Subsequently, all of the key employees terminated their employment with Yuravision, however, the Company claimed that the Korean corporation did not diligently use the services of the employment agency in order to find replacements. Following protracted negotiations,
On January 28, 2008 the Company entered into a modification agreement amending the December 1, 2006 agreement with the Korean corporation. Pursuant to the modification agreement the Loan Amount was reduced from $800,000 to $460,000, without any further obligation by the Korean corporation for the reduced amount of $340,000. The payment terms of the loan were changed so that the Korean corporation paid to the Company $360,000 on February 4, 2008 and was required to pay the remaining $100,000 owed under the loan by January 28, 2009. The terms for the payment of the purchase price were not changed.

NOTE 3 - CONSOLIDATED SUBSIDIARIES (cont.)

a. Acquisition and Disposal of Yuravision (cont.)

Yuravision is classified as discontinued operation in the consolidated financial statements and its results of operation and financial position are separately reported for all periods presented. Summarized financial information for Yuravision is as follows:

	Year ended December 31	
	2006	2005
	$ in thousands	
Revenues	707	1,212
Cost of revenues	345	590
Gross profit	362	622
Research and development costs, net	207	154
Marketing and selling expenses	48	182
General and administrative expenses	319	438
Operating loss	(212)	(152)
Financial expenses	(66)	(34)
Other income	98	34
Net loss of discontinued operation	(180)	(152)

b. Acquisition of Panoptes Ltd.

In February 2006, the Company acquired business, assets and liabilities of Panoptes Ltd., and its subsidiary acquired 100% of the shares of Panoptes Ltd. Panoptes Ltd. is principally engaged in the design, development, manufacturing and marketing automatic vision and quality monitoring systems for surface inspection, especially textiles, glass fabric and technical woven materials.

The total consideration of acquisition of Panoptes Ltd. amounted to $ 622,000 (including estimated direct transaction costs amounting to $ 79,000). The Company issued 800,000 ordinary shares amounted to $ 543,000 and , subject to certain instances, will pay cash royalties equaling 3.5% of sales of EVS optical inspection systems between January 2006 and the end of December 2008 to Ma'aragim Panoptes' controlling shareholder (see Note 10a5)).

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition:

	At January 1, 2006 ($ in thousands)
Long-term receivables	12
Property, plant, and equipment	59
Intangible assets	1,514
Total assets acquired	1,585
Current liabilities	(954)
Long-term liabilities	(9)
Total liabilities assumed	(963)
Net assets acquired	622

Of the $ 1,514,000 of acquired intangible assets, $ 1,025,000 were assigned to current technology, which represents patent and other intellectual properties (5 years useful life); $ 489,000 were assigned to customer relations (5 years useful life).

NOTE 4 – INVENTORIES

	December 31	
	2007	**2006**
	$ in thousands	
Raw materials	2,341	1,330
Spare parts	621	566
Work in process	1,482	861
Finished products*	855	1,211
	5,299	3,968

* Mainly systems in trial by customers (see Note 2i).

The balances are net of write-down of $463,000 and $1,467,000 as of December 31, 2007 and 2006, respectively.

NOTE 5 – OTHER LONG-TERM RECEIVABLES AND INVESTMENT

	December 31	
	2007	**2006**
	$ in thousands	
Deposits on leased vehicle (see also Note 10b2))	70	39
Investment (1)	61	61
Future proceeds from selling the Yuravision	100	966
	231	1,066

(1) On July 22, 2004, the Company converted a convertible loan that had been granted to Micro Components Ltd. ("MCL") into 197,217 ordinary shares of MCL. As of December 31, 2007 the Company holds 4% of MCL's ordinary shares.

NOTE 6 - PROPERTY AND EQUIPMENT

a. Comprised as follows:

	December 31	
	2007	**2006**
	$ in thousands	
Machinery and equipment	2,791	2,660
Leasehold improvements	254	216
Office furniture and equipment	418	296
Vehicles	62	184
	3,525	3,356
Less - accumulated depreciation and amortization	3,035	2,901
	490	455

b. Depreciation and amortization expenses totaled $ 222,000, $ 191,000, and $254,000, in the years ended December 31, 2007, 2006 and 2005, respectively.

NOTE 7- OTHER INTANGIBLE ASSETS

	Gross carrying amount December 31		Accumulated amortization December 31	
	2007	2006	2007	2006
	U.S. dollars in thousands		U.S. dollars in thousands	
Technology	2,828	2,828	1,000	625
Customer relations	1,599	1,599	566	357
Distribution network	338	338	113	79
Brand name	489	489	136	95
Backlog	414	414	414	414
	5,668	5,668	2,229	1,570

Amortization expenses totaled $ 659,000 $ 669,000, and $ 436,000, in the years ended December 31, 2007, 2006, and 2005, respectively.

Estimated amortization expense for the following years, subsequent to December 31, 2007:

	$ in thousands
Year ended December 31:	
2008	669
2009	669
2010	669
2011	366
2012	366

NOTE 8- ACCRUED SEVERANCE PAY, NET

a. The Company's liability for severance pay is calculated in accordance with Israeli law based on the latest salary paid to employees and the length of employment in the Company.
Part of the liability is funded through individual insurance policies.
The policies are assets of the company and, under labor agreement subject to certain limitation, they may be transferred to ownership of the beneficiary employees.

b. A U.S. subsidiary provides defined contribution plan for the benefit of its employees. Under this plan, contributions are based on specific percentages of pay.

c. Severance pay and defined contribution plan expenses were $ 14,000, $ 165,000, and $ 291,000 in the years ended December 31, 2007, 2006, and 2005, respectively. The earnings on the amounts funded were $ 52,000, $ 102,000, and $ 54,000 for the years ended December 31, 2007, 2006, and 2005, respectively.

NOTE 9 – LONG-TERM LIABILITIES – LOANS AND OTHER

a. Composed as follows:

	December 31	
	2007	**2006**
	$ in thousands	
Loans from banks(1)	1,000	2,015
Other liabilities:		
Loans from shareholders(2),(3)	-	769
	1,000	2,784
Less – current maturities:		
From banks	-	2,015
From shareholder (2)	-	160
	-	2,175
	1,000	609

(1) In August 2005 the Company entered into an agreement with bank Mizrahi, pursuant to which the Company received in 2005 a credit line for the aggregate amount of $ 2,000,000. The credit line is secured by a first ranking floating charge on all the Company's assets and all the assets of ScanMaster (see Note 11d).
In June 2007 the Company terminated the abovementioned agreement and entered into a new agreement with bank Leumi for a credit line amounted to $ 2,500,000.

(2) During 2003, the Company and Elbit Ltd. (a shareholder), reached an agreement, whereby the Company’s debt to Elbit Ltd. of $ 400,000 and accrued interest thereon that was due in 2003, will have the following terms:

a. The loan will bear annual interest of Libor+2% (formerly Libor+0.5%) payable quarterly.

b. The loan is repayable in quarterly installments of $ 40,000 each, commencing in the third quarter of 2003, but only if the cash flows provided by Company’s operating activities in the quarter preceding the payment exceeds $ 50,000.

On June 21, 2007, the Company executed an agreement with Elbit Ltd., pursuant to this agreement Elbit Ltd. (i) converted the loan to the Company in the amount of $470,000 (including accrued interest) into 1,492,063 ordinary shares, at a price of $0.315 per share; and (ii) invested in the Company $250,000 in consideration for 793,651 ordinary shares at a price of $0.315 per share and received a 4 year warrant to purchase 396,825 ordinary shares at an exercise price of $0.45 per share.

NOTE 9 – LONG-TERM LIABILITIES – LOANS AND OTHER (cont.)

a. Composed as follows (cont.)

(3)In February 2006, the Company issued notes to Mivtach Shamir Holdings Ltd. ("Mivtach") for $3 million (half of which will be held in escrow until the occurrence of certain events). The notes were convertible at the option of Mivtach into 6,000,000 ordinary shares of EVS, at a price per share of $0.50. Repayment of the notes was in 30 equal monthly installments commencing two years after the notes issuance or on the date that Mivtach decides not to convert the notes, whichever is sooner. The Company also granted to Mivtach a two-year warrant to purchase 4,000,000 of the Company's ordinary shares at an exercise price of $0.50 per share, exercisable only if Mivtach converts the notes.

The Company allocated the proceeds received based on the respective fair values to the notes and the warrants. Consistent with provisions of EITF 98-5 and 00-27, the Company evaluated whether the notes contain a beneficial conversion feature ("BCF") and determined that all proceeds should be allocated to the BCF and the notes initially recorded at nil. The amount of discount is to be amortized over the term of notes.

As of December 31, 2006 the company recorded in its financial reports a long term loan of $ 342,000, representing the amortized discount to date.

. On June 21, 2007 the Company signed an agreement with Mivtach pursuant to which, Mivtach converted the full amount of the convertible notes into (a) 9,523,810 of the Company's ordinary shares; and (b) received a 4 year warrant to purchase 2,380,952 of the Company's ordinary shares at an exercise price of $0.45 per share. As a result of the conversion, the unamortized discount, created as a resullt of the allocation of the proceeds to the BCF, was accelerated and recognized in earnings.

b. The liabilities (net of current maturities) mature in the following years after the balance sheet dates:

	December 31	
	2007	**2006**
	$ in thousands	
2008	1,000	267
2009	-	-
2010	-	342
2011 and thereafter	-	-
	1,000	609

NOTE 10 - COMMITMENTS AND CONTINGENT LIABILITIES

a. Royalties

1) The Company is committed to pay royalties to the Government of Israel based on proceeds from sales of products in the research and development of which the Government participates by way of grants. At the time the grants were received, successful development of the related projects was not assured.

   In the case of failure of a project that was partly financed as above, the Company is not obligated to pay any such royalties.

   Under the terms of the Company's funding from the Israeli Government, royalties of 3%-5% are payable on sales of products developed from a project so funded, up to 100% of the amount of the grant received by the Company (dollar linked); as from January 1, 2001 - with the addition of an annual interest rate based on Libor.

   Royalty expenses to the Government of Israel totaled $ 266,000, $ 259,000 and $ 286,000 in the years ended December 31, 2007, 2006 and 2005 respectively and are included in the statements of operations among cost of revenues.

2) The Company and ScanMaster Ltd. are committed to pay royalties to the Government of Israel in respect of marketing expenses in which the Government participated by way of grants. At the time the grants were received, successful development of the related projects was not assured. In the case of failure of a project that was partly financed as above, the Company is not obligated to pay any such royalties. The royalties are payable at the rate of 4% of the increase in export sales, up to the amount of the dollar-linked grant received. No royalties were paid in the reported years to the Government of Israel.

   On November 7, 2007, the Company received a letter from the Ministry of Trade, Industry and Labor – Fund for the Encouragement of Marketing Abroad (the "Fund"), claiming that it had failed to pay royalties to the Fund since 1999 in the aggregate amount of $480,818. On November 21, 2007, the Company sent a letter to the Fund in which it stated that the Fund had not requested any of these royalties for many years despite the Company's written request to clarify the issue. In its letter the Company stated that a material amount of the royalties could no longer be claimed due to the operation of the statute of limitations and that in any event the Fund may be estopped from making at least part of the claims as a result of its non-response to the Company's inquiry. On December 18, 2007, the Company met with representatives of the Fund to discuss the issue. The Company have yet to receive a response to the meeting. The Company recorded an allowance of $ 90,000 on acount of this claim.

   The maximum royalty amount payable the Company expect to pay to the Government of Israel under 1 and 2 above ,at December 31, 2007 is approximately $ 1,092,000.

3) Effective upon its initial public offering on July 3, 1997, the Company agreed to pay Elbit Ltd. ("Elbit") royalties in an amount dependent upon the sales of the Company's vision system products in the textile, automotive and food industries.

   The royalties will in turn be paid in full by Elbit to the original developer of certain elements of the technology licensed by the Company from Elbit.

   In 2002, the Company and Elbit amended the abovementioned agreement, effective as of July 1, 2001; pursuant to the agreement the royalties would be paid directly to the developer, twice a year, at a rate of 0.9375%-1.5% of sales of certain products in the immediately preceding six months.

   The royalty expenses totaled $ 20,600 and $ 46,000 in the years ended December 31, 2006 and 2005, respectively, and are included in the statements of operations in cost of revenues.
   No expenses were recorded in the year ended December 31, 2007.

NOTE 10 - COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. Royalties (cont.)

4) ScanMaster Ltd. signed an agreement with a supplier, whereunder the supplier assisted Scanmaster Ltd. to complete a development of one of the Company's products. The supplier is also entitled to receive royalties from the product's sales. The royalty expenses in respect of royalties paid to the said supplier amounted to totaled $ 34,000 and $ 28,000 in the years ended December 31, 2007 and 2006, respectively, were included in the statements of operations in cost of revenues.

5) As part of acquisition of Panoptes Ltd. (see Note 3b.), the Company, subject to certain instances, will pay cash royalties equaling 3.5% of sales of EVS's optical inspection systems between January 2006 and the end of December 2008 to Ma'aragim Panoptes' controlling shareholder. The Company paid to Ma'aragim royalties $ 155,000 and $ 109,000 during the years ended December 31, 2007 and 2006, respectively .

b. Lease commitments

1) The premises occupied by the Company and certain subsidiaries are rented under various operating lease agreements. The lease agreements for the premises expire in 2009 with extended options for another 3 years.

Minimum lease commitments of the Company and the subsidiaries under the above leases, at rates in effect as of December 31, 2007, are as follows:

	$ in thousands
Year ending December 31:	
2008	485
2009	499
2010	513
	1,497

The rental payments for the premises in Israel, which constitute most of the above amounts, are payable in Israeli currency linked to the Israeli CPI.

Rental expenses totaled $ 331,000, $ 514,000, and $ 540,000 in the years ended December 31, 2007, 2006 and 2005, respectively.

2) The Company leases motor vehicles under long-term operating lease agreements. The lease agreements expire on various dates ending in 2008 – 2010 (with prior notice of cancellation clauses).

Minimum lease commitments of the Company under the above leases, at rates in effect on December 31, 2007, are as follows:

	$ in thousands
2008	379
2009	263
2010	98
	740

To secure the amounts due to the lessor, the Company has deposited a total of U.S. $ 69,000. The deposits are unlinked and presented among other receivables and long-term receivables.
Lease expenses in 2007, 2006 and 2005, amounted to $ 430,000, $ 299,000, and $ 298,000 respectively.

NOTE 10 - COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

c. Guarantees

As of December 31, 2007, the Company provided guarantees in the aggregate amount of $1,185,000 to its customers in order to secure the Company's commitments under its sales agreements. The guarantees are usually secured by cash advances received from the said customers.

NOTE 11 - SHAREHOLDER' EQUITY

a. Authorized, issued and outstanding shares

1) The Company's Ordinary Shares are traded in the United States on the OTC Bulletin Board market under the symbol EVSNF.OB.

2) In March 2004, the Company entered into a Standby Equity Distribution Agreement with Cornell. Pursuant to this agreement, the Company will be entitled to issue Cornell with put notices requiring it to purchase, six days following each put notice, a number of Company's ordinary shares with a value of up to $ 300,000 per put notice and up to an aggregate value of $ 10,000,000 over two years.

   The price per share payable by Cornell will be determined based on the minimum price of Company's shares during the five days period following Company's put notice to Cornell to purchase Company's shares. Under the said agreement, the Company agrees to pay Cornell commitment fees, which were defined as follows:

   a) For each notice, Cornell will deduct 5% from the price payable for Company's ordinary shares, as a commitment fee.

   b) Upon execution of the Agreement, the Company issued Cornell with 148,438 of its ordinary shares in an amount equal to $ 190,000.

   c) Upon the first to occur of (i) receipt by the Company of an aggregate of more than $5,000,000 from Cornell pursuant to the Agreement; and (ii) the first put notice to be provided by the Company following the first anniversary of the execution of the Agreement, the Company will issue to Cornell a number of its ordinary shares with a value of $ 150,000, calculated in accordance with the minimum closing bid price of Company shares on the public market on which its shares shall be traded at such time, on the day on which the Company is required to issue the ordinary shares.
   Through December 31, 2005, the Company repaid $ 2,129,000 of the Note in cash and $ 433,000 by the issuance of 869,946 shares to Cornell, as stipulated in the said agreement.

   Through June 2006, the Company issued Cornell with 1,433,527 of its ordinary shares in an amount equal to $ 569,000.

   On February 17, 2006, the Company repaid all outstanding amounts owed to Cornell, and have thus fulfilled all of it obligations toward them under the Promissory Note. Following repayment of the Promissory Note, all ordinary shares and advance notices held in trust to guarantee the loan were returned to the Company, and the floating charge on its assets was removed.

NOTE 11 - SHAREHOLDER' EQUITY (cont.)

a. Authorized, issued and outstanding shares (cont.)

3) In June 2007 the Company completed the April Investment with a group of Israeli institutional investors, or the Israeli Investors, for the purchase of its 9,465,544 ordinary shares for $0.315 per share, of an aggregate price of $2,981,646. Pursuant to the transaction, the investors were also issued warrants to purchase 4,732,774 of the Company's ordinary shares at an exercise price per share of $0.45, exercisable for a period of 4 years.

4) On June 21, 2007, following the approval of the Company's board of directors and the Company's audit committee, the Company executed an agreement with Elbit Ltd., or the Elbit Agreement. This agreement was approved by the Company's shareholders in a meeting held on July 31, 2007. Pursuant to this agreement Elbit Ltd.(i) converted an existing loan to the Company in the amount of $470,000 (including accrued interest up until March 31, 2007) into 1,492,063 ordinary shares, at a price of $0.315 per share; and (ii) invested $250,000 in consideration for 793,651 of the Company's ordinary shares at a price of $0.315 per share and received a 4-year warrant to purchase 396,825 of the Company's ordinary shares at an exercise price of $0.45 per share. At consummation the Company paid all interest accrued on the loan between April 1, 2007 and the closing date.

5) On February 21, 2006, the Company consummated the Mivtach Agreement. Pursuant to the agreement, Mivtach Shamir Hidings Ltd. ("Mivtach") provided the Company with a two-year $3 million loan, which Mivtach Shamir was entitled at its sole discretion, for a period of 24 months following the provision of the loan, to convert into 6,000,000 of the Company's ordinary shares, at a price per share of $0.5 (half the loan was being held in escrow subject to the completion of a certain milestone, or conversion of the loan). The interest on the loan was repaid on a quarterly basis. Mivtach was also granted a two-year warrant to purchase 4,000,000 of the Company's ordinary shares at an exercise price of $0.5 per share, exercisable only if the loan was converted. On February 21, 2006, Mivtach assigned their right to receive shares from the Company, under the convertible loan and warrant, to M S N D Real Estate Holding Ltd. ("M.S.N.D."). On June 21, 2007 the Company executed an agreement with M.S.N.D., which was approved by the Company's shareholders in a meeting held on July 31, 2007, pursuant to which, the Mivtach Agreement was amended, or the Amendment Agreement. Pursuant to the Amendment Agreement, the terms of the Mivtach Agreement and the loan therein, were amended, such that in consideration for M.S.N.D.'s undertaking to convert the full loan amount by no later than August 1, 2007 (a) Mivtach will be issued with 9,523,810 of ordinary shares; and (b) Mivtach will receive a 4-year warrant to purchase 2,380,952 of the Company's ordinary shares at an exercise price of $0.45 per share. Mivtach also agreed to waive its rights to exercise at least 3,000,000 ordinary shares issuable under the Mivtach Agreement, agreeing to exercise no more than 1,000,000 ordinary shares issuable under the Amendment Agreement, which warrants expired on February 21, 2008. Following consummation the Amendment Agreement M.S.N.D, has become a holder of more than 25% of the Company's issued and outstanding share capital.

M.S.N.D. also completed the purchase of 2,939,192 of the Company's ordinary shares from three of the founders of ScanMaster, in accordance with the provisions of a share purchase agreement.

NOTE 11 - SHAREHOLDER' EQUITY (cont.)

b. Share option plans:

1) The plans:

(a) In February 1996, the Company's board of directors adopted the Company's Employee Share Option Plan (1996) (hereafter – The 1996 Plan). Under the 1996 plan, 565,720 options can be granted to directors, employees and consultants of the Company and its subsidiaries. Each option can be exercised into one ordinary share of the Company.
The 1996 plans was valid for ten years and expired in February 2006, except for option awards outstanding on that date.

Under the 1996 Plan, options usually vest as follows: 50% - two years after the effective date of grant; 75% - after three years; and 100% - after four years.

(b) In April 2000, the board of directors of the Company adopted the Employee Share Option Plan (2000) (hereafter – The 2000 Plan).

Under the 2000 plan, options to purchase an aggregate of 4,500,000 ordinary shares are available to be awarded to employees, directors or consultants of the Company or any of its subsidiaries.
Under the 2000 plan, options usually vest over a period of three or four years from the date of grant, in equal parts each year.

The 2000 Plan is valid for ten years and will expire on April 3, 2010, except for options outstanding on that date.

(c) In November 2003, the Board of Directors of the Company adopted the Employee Share Option Plan (2003) (hereafter – The 2003 Plan).

Under the 2003 plan, options to purchase an aggregate of 2,000,000 ordinary shares are available to be awarded to employees, directors or consultants of the Company or any of its subsidiaries.

Under the 2003 plan, options usually vest over a period of four years from the date of grant, in equal parts each year.
The 2003 Plan is valid for ten years and will expire on November 30, 2013, except for options outstanding on that date.

(d) In March 2006, the Board of Directors of the Company adopted the Employee Share Option Plan (2006) (hereafter – The 2006 Plan).

Under the 2006 plan, options to purchase an aggregate of 2,000,000 ordinary shares are available to be awarded to employees, directors or consultants of the Company or any of its subsidiaries.

Under the 2006 plan, options usually exercisable over a period up to ten years following the date of grant, if not exercised earlier, or 6 months after termination of the employee, will generally vest as to 25-33% commencing the beginning of the second year after the grant and as to an additional 25-33% in each of the remaining years thereafter, assuming continuous employment with the Company through such periods.

NOTE 11 - SHAREHOLDER' EQUITY (cont.)

b. Share option plans (cont.):

1) The plans (cont.):

The 2006 Plan is valid for ten years and will expire in March, 2016, except for options outstanding on that date.

The exercise price of options granted under the 1996, 2000 and 2003 plans is to be not less than 85% of the fair market value of the ordinary share on the date of grant. All of the outstanding options from the 1996, 2000 and 2003 plan are to expire no later than 10 years following the date of grant.

Through December 31, 2005, options to purchase 474,848 shares were exercised. The proceeds from the exercise amounted to $ 102 thousands.

During 2006 options to purchase 183,797 shares were exercised. The proceeds from the exercise amounted to $ 43 thousands.

During 2007 no options were exercised.

The 2000, 2003 and 2006 plans are subject to the terms stipulated by Section 102 of the Israeli Income Tax Ordinance. Inter alia, these terms provide that the Company will be allowed to claim, as an expense for tax purposes, the amounts credited to the employees as a benefit in respect of shares or options granted under the plan.

The amount allowed as an expense for tax purposes, at the time the employee utilizes such benefit, is limited to the amount of the benefit that is liable to tax as labor income, in the hands of the employee; all being subject to the restrictions specified in Section 102 of the Income Tax Ordinance.

The aforementioned expense will be recognized in the tax year that the benefit is credited to the employee.

2) Options granted to employees:

(a) A summary of the status of the above plans in respect of options granted to employees and directors of the Company and its subsidiaries as of December 31, 2007, 2006 and 2005, and changes during the years ended on those dates, is presented below:

	Year ended December 31					
	2007		2006		2005	
	Number	Weighted average exercise price	Number	Weighted average exercise price	Number	Weighted average exercise price
Options outstanding at beginning of year	4,888,686	$ 0.83	4,551,596	$ 0.86	4,406,138	$ 0.88
Changes during the year:						
Granted (1)	350,000	0.42	777,500	0.69	625,000	0.51
Exercised	-	-	(183,797)	0.21	(82,250)	0.21
Forfeited	(228,334)	1.19	(256,613)	1.21	(397,292)	0.69
Options outstanding at end of year	5,010,352	0.79	4,888,686	0.83	4,551,596	0.86
Options exercisable at year end	3,962,739	$ 0.85	3,663,176	$ 0.90	3,147,401	$ 0.97
Weighted average fair value of						

options granted during the year (2)	$ 0.35	$ 0.64	$ 0.37

NOTE 11 - SHAREHOLDER' EQUITY (cont.)

b. Share option plans (cont.):

2) Options granted to employees (cont.):

(1) Options granted in 2007, 2006 and 2005 were granted with exercise price that was at market value or above.

(2) The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model in 2007 and 2005 and the Binomial lattice model in 2006, with the following weighted average assumptions:

	Year ended December 31		
	2007	**2006**	**2005**
Dividend yield	0%	0%	0%
Expected volatility	140%	102%	70%
Risk-free interest rate	4.15%	4.7%	4.84%
Expected life - in years	6	6	4

. Dividend yield - Management used an expected dividend yield based primarily on past experience applicable as of the grant date.

Expected volatility - Management estimated volatility based on the historical volatility of the Company's ordinary shares, being the only traded financial instrument of the Company, using in most cases daily observations of the Company's price share to determine the standard deviation.

Risk free interest rate - The risk-free interest rate is based on the implied yield in effect at the time of each option grant, based on U.S. Treasury zero-coupon bond issued with equivalent remaining terms.

Management estimates forfeiture rates at the date of grant, which are adjusted in subsequent periods if the actual forfeiture rates differ from those initially estimated. Management uses historical data to estimate pre-vesting option forfeiture rates and records share-based compensation expense only for those awards that are expected to vest.

NOTE 11 - SHAREHOLDERS' EQUITY (Cont.)

b. Share option plans (Cont.):

2) Options granted to employees (Cont.):

(b) The following table summarizes certain information about options granted to employees and directors of the Company which were outstanding and exercisable under the above plans as of December 31, 2007:

	Options outstanding		Options exercisable	
Exercise prices	Number outstanding at December 31, 2007	Weighted average remaining contractual life	Number exercisable at December 31, 2007	Weighted average remaining contractual life
$		Years		Years
1.68	110,000	1.00	110,000	1.00
1.25	727,500	6.24	727,500	6.24
1.20	44,000	6.95	44,000	6.95
1.17	523,639	2.41	523,639	2.41
1.00	166,027	4.58	166,027	4.58
0.85	136,500	5.90	136,500	5.90
0.83	15,000	5.96	15,000	5.96
0.80	300,334	6.79	300,334	6.79
0.78	400,000	8.15	-	-
0.75	625,000	6.59	625,000	6.59
0.70	25,000	7.98	16,667	7.98
0.68	153,197	5.90	153,197	5.90
0.50	600,000	7.98	400,004	7.98
0.48	295,100	4.21	295,100	4.21
0.40	290,000	9.62	30,716	8.42
0.37	30,000	9.12	-	-
0.36	272,750	3.06	272,750	3.06
0.35	30,000	9.30	-	-
0.28	120,000	8.97	-	-
0.20	125,453	5.62	125,453	5.62
0.15	20,852	4.58	20,852	4.58
	5,010,352	6.08	3,962,739	5.40

c. Dividends

In the event the Company declares cash dividends, such dividends will be paid in Israeli currency. Under current Israeli regulations, any cash dividend in Israeli currency paid in respect of ordinary shares purchased by non-residents of Israel with non-Israeli currency may be freely repatriated in such non-Israeli currency, at the rate of exchange prevailing at the time of conversion.

d. Options issued to consultants

In May 2005, the Company issued to advisors 50,000 warrants, fully vested with an exercise price of $1 and 125,000 with vesting period of a three years and an exercise price of $0.8.

In September 2005, the Company issue 571,429 warrants, fully vested to bank Mizrahi with an exercise price of $0.77 and immediate vesting in favor of loan agreement (see also Note 9). During November 2006, the Company's board of directors approved to change the exercise price to $0.5.

All those warrants were granted above market value and the Company recorded expenses according to SFAS 123.

NOTE 12 - TAXES ON INCOME

a. Corporate taxation in Israel

1) Measurement of results for tax purposes under the Income Tax (Inflationary Adjustments) Law, 1985 (the "Inflationary Adjustments Law")

   Under the Inflationary Adjustments Law, results for tax purposes are measured in real terms, having regard to the changes in the Israeli Consumer Price Index (hereafter – CPI). The Company and ScanMaster Ltd. are taxed under this law.

   On February 26, 2008 the Income Tax (Inflationary Adjustments) Law (Amendment no. 20) (Limitation for period of application), 2008 (the"Amendment") passed in a third calling in the Knesset. According to the amendment, the application of the Inflationary Law will cease in the tax year of 2007, and beginning in 2008 the instructions of the law will no longer apply, except for transaction period instructions which have the purpose of preventing distortions in the calculations of taxes.

   In accordance with the Amendment, beginning in the year 2008, no calculations for inflationary adjustments of revenues for tax purposes will be made . In addition,there will be no adjustments to the Israeli CPI for fixed assets' depreciations and carryforward tax losses for the period beginning January 1, 2008.

   As explained in Note 2, the financial statements are measured in dollars. The difference between the changes in the Israeli CPI and in the exchange rate of the dollar relative to Israeli currency, both on annual and cumulative bases, creates a difference between taxable income and income reflected in these financial statements.

   Paragraph 9(f) of FAS 109, "Accounting for Income Taxes", prohibits the recognition of deferred tax liabilities or assets that arise from differences between the financial reporting and tax bases of assets and liabilities that are measured from the local currency into dollars using historical exchange rates, and that result from changes in exchange rates or indexing for tax purposes. Consequently, the abovementioned differences were not reflected in the computation of deferred tax assets and liabilities.

2) Tax rates

   a) The income of the Company and ScanMaster Ltd. (other than income from "approved enterprises", see b. below) are taxed at the regular rate. For 2007 the corporate tax rate was 29% and it will gradually decrease from 27% in 2008 through 25% in 2010.

   b) Non Israeli subsidiaries

   Subsidiaries that are incorporated outside of Israel are assessed for tax under the tax laws in their countries of residence. The principal tax rates applicable to subsidiaries outside Israel are as follows:
   Company incorporated in the USA – tax rate of 39%.
   Company incorporated in tne Netherlands – tax rate of 20 %.

NOTE 12 - TAXES ON INCOME (cont.)

b. Tax benefits under the Law for the Encouragement of Capital Investments, 1959 (hereinafter – the law)

Under the law, by virtue of the "approved enterprise" status granted to investments in certain assets the Company and ScanMaster Ltd. are entitled to various tax benefits.

1) The main tax benefits available to the Company and ScanMaster Ltd. are:

(a) Reduced tax rates:

(i) The Company

Tax exemption during the period of benefits – 10 years – commencing in the first year in which the Company earns taxable income from the approved enterprises (provided that the maximum period to which it is restricted by the law has not elapsed).

The Company has four approved enterprises; the benefit periods commenced in 1994, 1995, 1997 and 2004, respectively.

The periods of benefits for the first, second and third approved enterprise expired in 2003, 2004 and 2006, respectively.

In the event of distribution of cash dividends from income, which was tax exempt as above, the Company would have to pay 25% tax in respect of the amount distributed. The amount distributed for this purpose includes the amount of the tax that applies as a result of the distribution.

(ii) ScanMaster Ltd.

Tax exemption during the period of benefits – 7 years – commencing in the first year in which the Company earns taxable income from the approved enterprises (provided that the maximum period to which it is restricted by the law has not elapsed).

Tax exemption on income from approved enterprises in respect of which the companies have elected the "alternative benefits" (involving waiver of investment grants); the length of the exemption period is four years, after which the income from these enterprises is taxable at the rate of 25% for three years.

ScanMaster Ltd. has three approved enterprises; the benefit periods in respect of the first and second enterprises commenced in 1994 and 1997, respectively.
The period of tax benefits in respect of the first approved enterprise has expired.

The period of tax benefits in respect of the second approved enterprise will expire in 2008. The third approved enterprise has not yet been activated.

In March 2004 ScanMaster Ltd. received a warning from the Investment Center that the instrument of approval of the second approved enterprise might be cancelled. ScanMaster Ltd. plans to appeal the Investment Center's decision in the near future. ScanMaster Ltd. has not utilized its tax benefits in respect of this enterprise. In case that the said approved enterprise will be cancelled, the Company estimates that it will not be required to be subject to penalties.

NOTE 12 - TAXES ON INCOME (cont.)

b. Tax benefits under the Law for the Encouragement of Capital Investments, 1959 (hereinafter – the law) (cont.)

(b) Accelerated depreciation

The Company is entitled to claim accelerated depreciation in respect of equipment used by the approved enterprises during five tax years.

(c) Conditions for entitlement of the benefits

The entitlement to the above benefits is conditional upon the Company fulfilling the conditions stipulated by the above law, regulations published there under and the certificate of approval for the specific investments in approved enterprises. In the event of failure to comply with these conditions, the benefits may be canceled, and ScanMaster Ltd. and the Company may be required to refund the amount of the benefits, in whole or in part, with the addition of linkage differences to the Israeli CPI and interest.

In the event of distribution of cash dividends out of income, which was tax exempt as above, the companies would have to pay the 25% tax in respect of the amount distributed. For this purpose, the amount distributed includes the amount of the tax that applies as a result of the distribution.

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

The Company and ScanMaster Ltd. are “industrial companies” as defined by this law and as such are entitled to certain tax benefits, consisting mainly of accelerated depreciation as prescribed by regulations published under the Inflationary Adjustments Law, amortization of patents and certain other intangible property, and the right to claim public issuance expenses.

d. Reconciliation of Income Taxes

Following is a reconciliation of the theoretical tax expense, assuming all income is taxed at the statutory corporate tax rate applicable to Israeli corporations, and the actual expense:

	Year ended December 31		
	2007	**2006**	**2005**
		$ in thousands	
Income (Loss) before taxes on income	(1,339)	(5,357)	767
Theoretical tax benefit on the above amount	(388)	(1,661)	261
Increase in taxes in respect of tax losses incurred in the reported year for which deferred taxes were not recorded (see f. below)	388	1,661	(261)
Other	3	5	4
Actual tax expense	3	5	4

Taxes on income included in the statement of operations relate to Company’s subsidiaries.

NOTE 12 - TAXES ON INCOME (cont.)

e. Deferred Taxes

1) The Company has approximately $ 30 million unutilized carryforward tax losses from prior years. Therefore, no current tax liability has been provided in 2007 and 2006.
Virtually all the Company's temporary differences are in respect of carryforward tax losses. The Company expects that during the period in which its tax losses are utilized, its income would be tax exempt, as described in b1) (a) above. Accordingly, no deferred tax assets have been included in these financial statements in respect of the Company's carryforward tax losses.

2) ScanMaster has unutilized carryforward tax losses from prior years, exceeding other temporary differences. Valuation allowance has been provided in full, for all deferred taxes relating to the above tax losses and temporary differences; Accordingly no tax benefits have been included in these financial statements, as follows:

	December 31, 2007	December 31, 2006
	$ in thousands	$ in thousands
Provision for vacation pay	87	94
Accrued severance pay	42	14
Carryforward tax losses	858	1,362
Research and development costs	417	218
Less – valuation allowance	(1,404)	(1,688)
	-	-

The deferred taxes are computed at the average tax rate of 25% - 27%.

f. Carryforward tax losses

Carryforward tax losses of the Company and its subsidiaries aggregate approximately $ 41 million at December 31, 2007.

g. Tax assessments

Final tax assessments have been received by the Company and ScanMaster Ltd. through the tax year 2002.

NOTE 13 – FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

a. General

The Company operates internationally, which gives rise to exposure to market risks, mainly from changes in foreign exchange rates.

b. Fair value of financial instruments

The fair value of financial instruments included in working capital is usually identical or close to their carrying amount. The fair value of long-term receivables also approximate the carrying amounts, since they bear interest at rates close to prevailing market rates.

NOTE 14 – LIABILITIES SECURED BY PLEDGES AND RESTRICTION PLACED IN RESPECT OF LIABILITIES

a. The Group has registered fixed charge on bank deposits in favor of certain banks. The bank deposits are used to secure a credit line granted to the Company by the banks, and as collateral for guarantees provided to its customers (see Note 2q).

As of December 31, 2007, the bank deposits amount to $ 540 thousands, out of which $ 182 thousands are linked to the dollar and $ 358 thousands are linked to the Euro; The deposits are for a period of one Month.

b. The Company and Scanmaster have registered floating charges on all of their assets in favor of banks (see Notes 9, 15c).

NOTE 15 – SUPPLEMENTARY INFORMATION:

	December 31	
	2007	**2006**
	$ in thousands	
a. Accounts receivable		
1) Trade – **allowance for doubtful accounts:**		
Balance at beginning of year	936	774
Charged to general and administrative expenses	(84)	174
Write-off of uncollectible amounts	(175)	(12)
Balance at end of year	677	936
2) Other:		
Employees	60	50
Prepaid expenses	378	181
Israeli Government departments and agencies	324	362
Receivables from selling the Yuravision	360	-
Advance to agent	275	-
Sundry	31	10
	1,428	603

NOTE 15 – SUPPLEMENTARY INFORMATION (Cont.)

b. Accounts payable and accruals – other:

	December 31	
	2007	2006
	$ in thousands	
Employees and employee institutions	535	645
Israeli Government departments and agencies	1,005	998
Provision for vacation and recreation pay	588	592
Provision for product warranty	218	259
Liability for commissions to agents	108	394
Accrued expenses and sundry	175	695
	2,629	3,583

c. Credit from banks

Composed as follows:

	% interest rate as of December 31, 2007	December 31	
		2007	2006
		$ in thousands	
Unlinked credit from bank	9	504	528
Short-term loans from banks:			
Linked to the dollar	8	3,793	3,223
Linked to the Euro	7	670	962
		4,967	4,713

In 2003, the Company entered into agreements for bank credit facilities, pursuant to which the Company may, from time to time, borrow an aggregate amount of up to $ 3,930,000. As of December 31, 2007 the Company uses $ 3,537,444 of the said credit; to secure the credit facilities, the Company registered a floating fixed charge on certain bank deposits in favor of the said banks (see Note 14).

d. Cost of revenues

	Year ended December 31		
	2007	2006	2005
	$ in thousands		
Industrial operations:			
Materials consumed	4,202	5,636	7,178
Payroll and related expenses	2,776	2,745	2,569
Subcontracted work	247	253	135
Depreciation and amortization	579	579	457
Other production expenses	1,873	2,267	1,736
Royalties (see Note 10a)	300	287	(490)
Increase in inventories	1,331	469	48
	11,308	12,236	11,633

NOTE 15 – SUPPLEMENTARY INFORMATION (cont.):

e. Research and development expenses:

Total expenses	3,454	2,707	2, 193
Less – grants and participations, see Note 10a1).	(141)	(145)	(154)
	3,313	2,562	2,039

f. Financial income (expenses)

	Year ended December 31		
	2007	2006	2005
	$ in thousands		
Income:			
Interest in respect of bank Deposits and securities	62	44	46
Exchange differences	48	-	99
Other	-	9	-
	110	53	145
Expenses:			
Interest			
In respect of liability to related parties	360	460	22
In respect of credit from banks	747	695	170
In respect of credit from Cornell	-	-	79
Exchange differences	-	215	124
Other	84	15	187
	1,191	1,385	582
	(1,081)	(1,332)	(437)

g. Other income (expenses)

	Year ended December 31		
	2007	2006	2005
	$ in thousands		
Write off of discount on convertible loan associated with beneficial conversion feature (see note 9a.(3))	(1,047)	-	-
Other	(230)	(5)	7
	(1,277)	(5)	7

NOTE 16 – RELATED PARTIES

	2007	2006	2005
	$ in thousands		
Marketing and selling	120	92	-
General and administrative	278	322	184
Financing expenses on long-term loan granted by shareholders - see Note 9a.	360	29	22
Other expenses	1,047	-	-

NOTE 17 - BUSINESS AND GEOGRAPHICAL SEGMENTS

a. General information:

1) Factors management used to identify the enterprise's reportable segments

The Company's reportable segments are strategic business units that offer different products and services. They are managed separately because each business requires different technology and marketing strategies. Most of the businesses were acquired as a unit, and the management at the time of the acquisition was retained.

2) Description of the types of products and services from which each reportable segment derives its revenues

Due to the acquisition in 2004, the internal organizational structure changed; consequently, the company has two reportable segments:

(a) Automatic Vision Inspection segment - design, develop, manufacture and marketing automatic vision inspection and quality monitoring systems, and rendering services related to those systems.

(b) Non-destructive Automated Inspection segment - develop, manufacture and market equipment for the ultrasonic inspection of industrial parts and components for the automotive and transportation industries, the metal industry as well as applications for aircraft and jet engine inspection.

Prior to June 2004, the Company operated only in one segment - the Automatic Vision Inspection segment.

b. Information about reported segment income or loss and assets:

Measurement of segment income or loss and segment assets
The accounting policies of the segments are the same as those described in the significant accounting policies. The Company evaluates performance based on profit or loss from operations before income taxes, not including non-recurring gains and losses and foreign exchange gains and losses.
The Company accounts for inter-segment sales and transfers as if the sales or transfers were to third parties, that is - at current market prices.

	Automatic Vision Inspection	Non-Destructive Automated Inspection	Total
	$ in thousands		
Year ended December 31, 2007:			
Revenues from unaffiliated customers	7,646	14,217	21,863
Total Consolidated revenues			21,863
Segment Operating income (loss)	(122)	1,356	1,234
Unallocated corporate expenses			(215)
Operating income			1,019
Segment assets	7,852	15,648	23,500
Other unallocated amounts			6
Consolidated assets at the year end			23,506
Expenditures for segment assets	186	110	296
Total depreciation and amortization	438	455	893

NOTE 17 - BUSINESS AND GEOGRAPHICAL SEGMENTS (cont.)

c. Geographic information

1) The Company's revenues by geographic areas (based on locaton of customers) are as follows:

	2007	2006	2005
	$ in thousands		
U.S.A.	6,341	4,178	6,163
Europe	7,756	7,370	4,389
Other (mainly Japan and China)	7,766	5,449	9,027
	21,863	16,997	19,579

2) The Company's long-lived assets by gegraphic areas are as follows:

	2007	2006
	$ in thousands	
Israel	7,437	6,887
U.S.A.	21	27
	7,458	6,914