AGILYSYS INC
Form DEF 14A
July 25, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

(Rule 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the

Securities Exchange Act of 1934

Filed by the Registrant x Filed by a Party other than the Registrant ¨

Check the appropriate box:

¨ Preliminary Proxy Statement

¨ **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

x Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to Section 240.14a-11c or Section 240.14a-12

AGILYSYS, INC.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

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¨ Fee paid previously with preliminary materials.

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(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

NOTICE OF 2014 ANNUAL MEETING OF SHAREHOLDERS

To be held on August 20, 2014

Please join us for the Agilysys, Inc. 2014 Annual Meeting of Shareholders to be held on Wednesday, August 20, 2014, at 8:30 a.m., local time, at the company s offices at 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005.

The purposes of the Annual Meeting are:

1. The election of the four director nominees named in the Proxy Statement to hold office for a two-year term expiring at the 2016 Annual Meeting of Shareholders;

2. To vote, on a non-binding advisory basis, to approve the compensation of our named executive officers set forth in the attached Proxy Statement;

3. To ratify the appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2015; and

4. To transact such other business as may properly come before the Annual Meeting or any adjournment or postponement thereof.

Shareholders of record at the close of business on July 3, 2014, are entitled to vote at the Annual Meeting. It is important to vote your shares at the Annual Meeting, regardless of whether you plan to attend. In addition to voting by mail, you may vote by telephone or Internet. Please refer to your enclosed proxy card and the Proxy Statement for information regarding how to vote by telephone or Internet. If you choose to vote by mail, please sign, date, and promptly return your proxy card in the enclosed envelope.

By Order of the Board of Directors,

Keith M. Kolerus

Chairman of the Board of Directors

July 25, 2014

Important Notice Regarding the Availability of Proxy Materials

for the Annual Meeting of Shareholders to be held on August 20, 2014.

The Proxy Statement and our Annual Report on Form 10-K for the

fiscal year ended March 31, 2014, are available at *www.agilysys.com*.

PROXY STATEMENT

2014 ANNUAL MEETING OF SHAREHOLDERS

August 20, 2014

ANNUAL MEETING INFORMATION

General Information

This Proxy Statement and the enclosed proxy card are being provided in connection with the solicitation by the board of directors of Agilysys, Inc., an Ohio Corporation (Agilysys, the Company, we, our, or us), to be used at the Annual Meeting of Shareholders to be held on August 2 2014, and any adjournments or postponements of the Annual Meeting. The Annual Meeting will be held at 8:30 a.m., local time, at the Company s offices at 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005. Our principal executive office is located at 425 Walnut Street, Suite 1800, Cincinnati, Ohio 45202. The purposes of the Annual Meeting are stated in the accompanying Notice. This Proxy Statement, the enclosed proxy card, and our Annual Report on Form 10-K for the fiscal year ended March 31, 2014 (2014 Annual Report), are first being mailed to shareholders and made available electronically on our website at *www.agilysys.com* beginning on or about July 25, 2014.

Record Date, Voting Shares, and Quorum

Shareholders of record of our common shares at the close of business on July 3, 2014, the Record Date, are entitled to notice of and to vote their shares at the Annual Meeting, or any adjournment or postponement of the Annual Meeting. On the Record Date, there were 22,617,212 common shares outstanding and entitled to vote at the Annual Meeting. Each share is entitled to one vote. The presence at the Annual Meeting, in person or by proxy, of the holders of a majority of the common shares outstanding at the close of business on the Record Date will constitute a quorum for the transaction of business at the Annual Meeting. We will include abstentions and broker non-votes in the number of common shares present at the Annual Meeting for purposes of determining a quorum. A broker non-vote occurs when a nominee holding shares for a beneficial owner has not received instructions from the beneficial owner and does not have discretionary authority to vote the shares. Our common shares are listed on the NASDAQ Global Select Market under the symbol AGYS. References within this Proxy Statement to our common shares or shares refer to our common shares, without par value, the only class of securities entitled to vote at the Annual Meeting.

How to Vote

If you are the record holder of common shares, you or your duly authorized agent may vote by completing and returning the enclosed proxy card in the envelope provided. This year, you may also vote by telephone or Internet. Telephone and Internet voting information is provided on your proxy card. A control number, located on the proxy card, is designed to verify your identity, allow you to vote your shares, and confirm that your voting instructions have been properly recorded. Please note the deadlines for voting by telephone, the Internet, and proxy card as set forth on the proxy card. If you vote by telephone or Internet, you need not return your proxy card. You may also attend the Annual Meeting and vote in person; however, we encourage you to vote your shares in advance of the Annual Meeting even if you plan on attending. If your common shares are held by a bank or broker, or any other nominee, you must follow the voting instructions provided to you by the bank, broker, or nominee. Although most banks and brokers offer voting by mail, telephone, and the Internet, availability and specific procedures will depend on their voting arrangements.

Unless revoked, common shares represented by a properly signed and returned proxy card (or other valid form of proxy), or as instructed via telephone or Internet, received in time for voting will be voted as instructed. If your proxy card is signed and returned with no instructions given, the persons designated as proxy holders on the proxy card will vote as follows:

FOR the election of each director nominee named herein (proposal 1);
FOR the approval, on a non-binding advisory basis, of the compensation of our named executive officers (proposal 2); and
FOR the ratification of the appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm (proposal 3).

The Company knows of no other matters scheduled to come before the Annual Meeting. If any other business is properly brought before the Annual Meeting, your proxy gives discretionary authority to the proxy holders with respect to such business, and the proxy holders intend to vote the proxy as recommended by our board of directors with regard to any such business, or, if no such recommendation is given, the proxy holders will vote in their own discretion.

Revocability of Proxies

You may revoke or change your vote at any time before the final vote on the matter is taken at the Annual Meeting by submitting to our Secretary a notice of revocation or by timely delivery of a valid, later-dated, duly executed proxy by mail, telephone, or Internet. You may also revoke or change your vote by attending the Annual Meeting and voting in person. If your shares are held by a bank, broker, or other nominee, you must contact the bank, broker, or nominee and follow their instructions for revoking or changing your vote.

Vote Required, Abstentions, and Broker Non-Votes

If a quorum is present at the Annual Meeting, for proposal 1 (election of directors), the nominees named herein for election as directors will be elected if they receive the greatest number of votes cast at the Annual Meeting present in person or represented by proxy and entitled to vote. Abstentions will have no effect on the election of directors. For proposal 2 (advisory vote on named executive officer compensation) and proposal 3 (ratification of independent registered public accounting firm), if a quorum is present, the affirmative vote of the holders of shares representing a majority of the common shares present in person or represented by proxy and entitled to vote will be required to approve each proposal. The effect of an abstention is the same as a vote against each proposal. If you hold your shares in street name and do not give your broker or nominee instruction as to how to vote your shares with respect to proposals 1 and 2, your broker or nominee will not have discretionary authority to vote your shares on proposals 1 and 2. These broker non-votes will have no effect on these proposals.

Cumulative Voting

Each shareholder has the right to vote cumulatively in the election of directors if the shareholder gives written notice not less than 48 hours before the Annual Meeting commences to our Chief Executive Officer or Secretary that he, she, or it wants its voting for the election of directors to be cumulative. In such event, the shareholder giving notice, or a representative of such shareholder, the Chairman, or the Secretary, will make an announcement about such notice at the start of the Annual Meeting. Cumulative voting means that the shareholder may cumulate his, her, or its voting power for the election of directors by distributing a number of votes, determined by multiplying the number of directors to be elected at the Annual Meeting times the number of such shareholder s shares. The shareholder may distribute all of the votes to one individual director nominee or distribute the votes among two or more director nominees, as the shareholder chooses. In the event of cumulative voting, unless contrary instructions are received, the persons named in the enclosed proxy will vote the shares represented by valid proxies on a cumulative basis for the election of the nominees named herein, allocating the votes among the nominees in accordance with their discretion.

Proxy Solicitation

The cost of solicitation of proxies, including the cost of preparing, assembling, and mailing the Notice, Proxy Statement, and proxy card, will be borne by us. In addition to solicitation by mail, arrangements may be made with brokerage houses and other custodians, nominees, and fiduciaries to send proxy materials to their principals, and we may reimburse them for their expenses in so doing. Our officers, directors, and employees may, without additional compensation, personally or by other appropriate means request the return of proxies.

Attending the Annual Meeting

All holders of our common shares at the close of business on the Record Date, or their duly appointed proxies, are authorized to attend the Annual Meeting. Cameras, recording devices, and other electronic devices will not be permitted at the Annual Meeting. If you hold your common shares through a bank, broker, or other nominee, you will need to bring a copy of the brokerage statement reflecting your share ownership as of the Record Date, or a legal proxy from your bank or broker, to attend the meeting.

Voting Results

Preliminary voting results will be announced at the Annual Meeting. Within four business days following the Annual Meeting, final results, or preliminary results if final results are unknown, will be announced on a Form 8-K filed with the Securities and Exchange Commission (SEC). If preliminary results are announced, final results will be announced on a Form 8-K filed with the SEC within four business days after the final results are known.

Company Information

Our 2014 Annual Report is being mailed with this Proxy Statement. These documents also are available electronically on our website at *www.agilysys.com,* under Investor Relations. Our 2014 Annual Report is not incorporated into this Proxy Statement and is not to be considered proxy solicitation material. If you wish to have additional copies of our 2014 Annual Report, we will mail copies to you without charge. Requests may be sent to our corporate services office at: Agilysys, Inc., Attn: Investor Relations, 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005, or you may request copies through our website, under Investor Relations. These documents have been filed with SEC and also may be accessed from the SEC s website at *www.sec.gov*. If you have any questions about the Annual Meeting or these proxy materials, please contact Investor Relations by telephone at 770-810-7948, or by email at *investorrelations@agilysys.com,* or through our website, under Investor Relations.

CORPORATE GOVERNANCE

Corporate Governance Guidelines

The Corporate Governance Guidelines (the Guidelines) adopted by our board of directors are intended to provide a sound framework to assist the board of directors in fulfilling its responsibilities to shareholders. Under the Guidelines, the board of directors exercises its role in overseeing the Company by electing qualified and competent officers and by monitoring the performance of the Company. The Guidelines state that the board of directors and its committees exercise oversight of executive officer compensation and director compensation, succession planning, director nominations, corporate governance, financial accounting and reporting, internal controls, strategic and operational issues, and compliance with laws and regulations. The Guidelines also state the board of directors policy regarding eligibility for the board of directors, including director independence and qualifications for director candidates, events that require resignation from the board of directors, service on other public company boards of directors, and stock ownership guidelines. The Nominating and Corporate Governance Committee annually reviews the Guidelines and makes recommendations for changes to the board of directors. The Guidelines are available on our website at *www.agilysys.com*, under Investor Relations.

Code of Business Conduct

The Code of Business Conduct adopted by our board of directors applies to all directors, officers, and employees of the Company and incorporates additional ethics standards applicable to our Chief Executive Officer, Chief Financial Officer, and other senior financial officers of the Company, and any person performing a similar function. The Code of Business Conduct is reviewed annually by the Audit Committee, and recommendations for change are submitted to the board of directors for approval. The Code of Business Conduct is available on our website at www.agilysys.com, under Investor Relations. The Company has in place a hotline available for use by all employees, as described in the Code of Business Conduct. Any employee can anonymously report potential violations of the Code of Business Conduct through the hotline, which is managed by an independent third party. Reported violations are promptly reported to and investigated by the Company. Reported violations are addressed by the Company and, if related to accounting, internal accounting controls, or auditing matters, the Audit Committee. In addition, we intend to post on our website all disclosures that are required by law or NASDAQ listing standards concerning any amendments to, or waivers from, any provision of the Code of Business Conduct.

Director Independence

NASDAQ listing standards provide that at least a majority of the members of the board of directors must be independent, meaning free of any material relationship with the Company, other than his relationship as a director. The Guidelines state that the board of directors should consist of a substantial majority of independent directors. A director is not independent if he fails to satisfy the standards for director independence under NASDAQ listing standards, the rules of the SEC, and any other applicable laws, rules, and regulations. During the board of directors annual review of director independence, the board of directors considers transactions, relationships, and arrangements, if any, between each director or a director s immediate family members and the Company or its management. In June 2014, the board of directors performed its annual director independence review and as a result of such review determined that each of Max Carnecchia, Jerry Jones, Michael A. Kaufman, Keith M. Kolerus, John Mutch, and Peter Sinisgalli qualify as independent directors. Mr. Dennedy is not independent because of his service as President and CEO of the Company.

Director Attendance

The board of directors held six meetings during fiscal year 2014, and no director attended less than 75% of the aggregate of the total number of board of director meetings and meetings held by committees of the board of directors on which he served. Independent directors meet regularly in executive session at board of director and committee meetings, and executive sessions are chaired by the chairman of the board or by the appropriate committee chairman. It is the board of directors policy that all of its members attend the Annual Meeting of Shareholders absent exceptional cause. All of the directors were in attendance at the 2013 Annual Meeting.

Shareholder Communication with Directors

Shareholders and others who wish to communicate with the board of directors as a whole, or with any individual director, may do so by sending a written communication to such director(s) in care of our Secretary at our Alpharetta, Georgia office address, and our Secretary will forward the communication to the specified director(s).

Committees of the Board

During fiscal year 2014, the board of directors had three standing committees: the Audit Committee, Compensation Committee, and Nominating and Corporate Governance Committee. At the end of the fiscal year and as of July 25, 2014, the members and chairman of each committee were as follows:

Director	Audit	Compensation	Nominating and Corporate Governance
Max Carnecchia			X
James H. Dennedy			
Jerry Jones	Chairman		X
Michael A. Kaufman		X	X
Keith M. Kolerus		X	Chairman
John Mutch*	X	X	
Peter Sinisgalli*	X	Chairman	

* Qualifies as an Audit Committee Financial Expert.

During fiscal year 2014 until November 2013, Robert A. Lauer served on the board as a member of the Compensation Committee and chairman of the Audit Committee, and Robert G. McCreary, III, served on the board as a member of the Nominating and Corporate Governance Committee. Mr. Andrew Cueva also served on the board as a member of the Nominating and Corporate Governance Committee and as chairman of the Compensation Committee until February 2014.

Committee Charters. The board of directors has adopted a charter for each committee, and each committee is responsible for the annual review of its respective charter. Charters for each committee are available on our website at *www.agilysys.com*, under Investor Relations.

Audit Committee. The Audit Committee held eight meetings during fiscal year 2014. The Audit Committee reviews with our independent registered public accounting firm the proposed scope of our annual audits and audit results, as well as interim reviews of quarterly reports; reviews the adequacy of internal financial controls; reviews internal audit functions; is directly responsible for the appointment, determination of compensation, retention, and general oversight of our independent registered public accounting firm; reviews related person transactions; oversees the Company s implementation of its Code of Business Conduct; and reviews any concerns identified by either the internal or external auditors. The board of directors determined that all Audit Committee members are financially literate and independent under NASDAQ listing standards for audit committee members. The board of directors also determined that Messrs. Mutch and Sinisgalli each qualify as an audit committee financial expert under SEC rules.

Compensation Committee. The Compensation Committee held four meetings during fiscal year 2014. The purpose of the Compensation Committee is to enhance shareholder value by ensuring that pay available to the board of directors, Chief Executive Officer, and other executive officers enables us to attract and retain high-quality leadership and is consistent with our executive pay philosophy. As part of its responsibility, the Compensation Committee oversees our pay plans and policies; annually reviews and determines all pay, including base salary, annual cash incentive, long-term equity incentive, and retirement and perquisite plans; administers our incentive programs, including establishing performance goals, determining the extent to which performance goals are achieved, and determining awards; administers our equity pay plans, including making grants to our executive officers; and regularly evaluates the effectiveness of the overall executive pay program and evaluates our incentive plans to determine if the plans measures or goals encourage inappropriate risk-taking by our employees. A more complete description of the Compensation Committee s functions is found in the Compensation Committee Charter. The board of directors determined that all Compensation Committee members are independent under NASDAQ listing standards for compensation committee members.

Our Legal and Human Resources Departments support the Compensation Committee in its work and, in some cases, as a result of delegation of authority by the Compensation Committee, fulfill various functions in administering our pay programs. In addition, the Compensation Committee has the authority to engage the services of outside consultants and advisers to assist it. The Committee engages compensation consultants to perform current market assessments when it believes that such an assessment would inform its decision making with respect executive compensation. The Compensation Committee did not engage a compensation consult to advise it in connection with setting compensation for the Named Executive Officers in fiscal year 2014. The Committee had previously engaged Towers Watson as its compensation consultant in 2012 and relied on its assessments in setting compensation for the Named Executive Officers in fiscal year 2013. Recently the Committee engaged Pearl Meyer & Partners as its compensation consultant, but it did not rely on its assessment in setting compensation for the Named Executive Officers in fiscal year 2014.

While the Compensation Committee directly retained Pearl Meyer & Partners and Towers Watson, in carrying out its assignments, Pearl Meyer & Partners and Towers Watson also interacted with our executive officers when necessary and appropriate, including our Chief Executive Officer, Chief Financial Officer, and our General Counsel, who provided data and insight on our compensation programs and business strategies. These executive officers attend Compensation Committee meetings when executive compensation, Company performance, and individual performance are discussed and evaluated by Compensation Committee members, and they provide their thoughts and recommendations on executive pay issues during these meetings and provide updates on financial performance, industry status, and other factors that may impact executive compensation. Decisions regarding the Chief Executive Officer s compensation were based solely on the Compensation Committee s deliberations, while compensation decisions regarding other executive officers took into consideration recommendations from the Chief Executive Officer. Only Compensation Committee members make decisions on executive officer compensation and approve all outcomes.

Nominating and Corporate Governance Committee. The Nominating and Corporate Governance Committee (Nominating Committee) held seven meetings during fiscal year 2014. The Nominating Committee assists the board of directors in finding and nominating qualified people for election to the board; reviewing shareholder-recommended nominees; assessing and evaluating the board of directors effectiveness; and establishing, implementing, and overseeing our governance programs and policies. The Nominating Committee is responsible for reviewing the qualifications of, and recommending to the board of directors, individuals to be nominated for membership on the board of directors. The board of directors has adopted Guidelines for Qualifications and Nomination of Director Candidates (Nominating Guidelines), and the Nominating Committee considers nominees using the criteria set forth in the Nominating Guidelines. At a minimum, a director nominee must:

- Be of proven integrity with a record of substantial achievement;
- Have demonstrated ability and sound business judgment based on broad experience;
- Be able and willing to devote the required amount of time to the Company s affairs, including attendance at board of director and committee meetings;
- Be analytical and constructive in the objective appraisal of management s plans and programs;
- Be committed to maximizing shareholder value and building a sound company, long-term;
- Be able to develop a professional working relationship with other directors and contribute to the board or directors working relationship with senior management of the Company;
- Be able to exercise independent and objective judgment and be free of any conflicts of interest with the Company; and
- Be able to maintain the highest level of confidentiality.

The Nominating Committee considers the foregoing factors, among others, in identifying nominees; however, there is no policy requiring the Nominating Committee to consider the impact of any one factor by itself. The Nominating Committee also will consider the board of directors current and anticipated needs in terms of number, diversity, specific qualities, expertise, skills, experience, and background. In addition, the Corporate Governance Guidelines state that the board of directors should have a balanced membership, with

diverse representation of relevant areas of experience, expertise, and backgrounds. The Nominating Committee seeks nominees that collectively will build a capable, responsive, and effective board of directors, prepared to address strategic, oversight, and governance challenges. The Nominating Committee believes that the backgrounds and qualifications of the directors as a group should provide a significant mix of experience, knowledge, and abilities that will enable the board of directors to fulfill its responsibilities.

The Nominating Committee will consider shareholder-recommended nominees for membership on the board of directors. For a shareholder to properly nominate a candidate for election as a director at a meeting of the shareholders, the shareholder must be a shareholder of record at the time the notice of the nomination is given and at the time of the meeting, be entitled to vote at the meeting in the election of directors, and have given timely written notice of the nomination to the Secretary. To be timely, notice must be received by the Secretary, in the case of an annual meeting, not less than 90 days nor more than 120 days prior to the anniversary of the previous year s annual meeting; provided, however, that if the date of the annual meeting is advanced more than 30 days prior to or delayed by more than 30 days after the anniversary of the preceding year s annual meeting, notice must be delivered not later than the close of business on the later of the 90th day prior to such annual meeting or the 10th calendar day following the day on which public disclosure of the date of such annual meeting is first made. In the case of a special meeting, timely notice must be received by the Secretary not later than the close of business on the 10th day after the date of such meeting is first publicly disclosed. A shareholder s notice must set forth, as to each candidate:

- Name, age, business address, and residence address of the candidate;
- Principal occupation or employment of the candidate;
- Class and number of shares that are owned of record or beneficially by the candidate;
- Information about the candidate required to be disclosed in a proxy statement complying with the rules and regulations of the SEC;
- Written consent of the candidate to serve as a director if elected and a representation that the candidate does not and will not have any undisclosed voting arrangements with respect to his actions as a director, will comply with the Company s Regulations and all other publicly disclosed corporate governance, conflict of interest, confidentiality, and share ownership and trading policies and Company guidelines;
- Name and address of the shareholder making such nomination and of the beneficial owner, if any, on whose behalf the nomination is made;
- Class and number of shares that are owned of record or beneficially by the shareholder and by any such beneficial owner as of the date of the notice;
- Representation that the shareholder or any such beneficial owner is a holder of record or beneficially of the shares entitled to vote at the meeting and intends to remain so through the date of the meeting;
- Description of any agreement, arrangement, or understanding between or among the shareholder and any such beneficial owner and any other persons (including their names) with respect to such nomination;
- Description of any agreement, arrangement, or understanding in effect as of the date of the shareholder s notice pursuant to which the shareholder, any such beneficial owner, or any other person directly or indirectly has other economic interests in the shares of the Company;
- Representation that the shareholder intends to appear in person or by proxy at the meeting to nominate the person or persons specified in the notice; and
- Representation whether the shareholder intends to deliver a proxy statement and/or form of proxy to holders of outstanding common shares and/or otherwise to solicit proxies in support of the nomination.

The Nominating Committee may request additional information from such nominee to assist in its evaluation. The Nominating Committee will evaluate any shareholder-recommended nominees in the same way it evaluates nominees recommended by other sources, as described above.

Board Leadership

The board of directors determined that having an independent director serve as Chairman of the Board is in the best interest of shareholders at this time. The structure ensures a greater role for our independent directors in the oversight of the Company and the active participation in setting agendas and establishing priorities and procedures for the board of directors. Pursuant to the board of directors Corporate Governance Guidelines, it is our policy that the positions of Chairman of the Board and Chief Executive Officer be held by different individuals, except as otherwise determined by the board of directors. Mr. Kolerus has served as Chairman of the Board since 2008.

Risk Oversight

Management is responsible for the day-to-day management of risks facing the Company, while the board of directors, as a whole and through its committees, is actively involved in the oversight of such risks. The board of directors role in risk oversight includes regular reports at board of director and Audit Committee meetings from members of senior management on areas of material risk to the Company, including strategic, financial, operational, and legal and regulatory compliance risks. Management regularly identifies and updates, among other items, the population of possible risks for the Company, assigns risk ratings, prioritizes the risks, assesses likelihood of risk occurrence, develops risk mitigation plans for prioritized risks, and assigns roles and responsibilities to implement mitigation plans. Risks are ranked by evaluating each risk s likelihood of occurrence and magnitude. The board of directors Compensation Committee, in consultation with management, evaluates our incentive plans to determine if the plans measures or goals encourage inappropriate risk-taking by our employees. As part of its evaluation, the Compensation Committee determined that the performance measures and goals were tied to our business, financial, and strategic objectives. As such, the incentive plans are believed not to encourage risk-taking outside of the range of risks contemplated by the Company s business plan.

Compensation Committee Interlocks and Insider Participation

None of the members of the Compensation Committee during fiscal year 2014 (Messrs. Cueva, Kaufman, Kolerus, Mutch and Sinisgalli) is or has been an officer or employee of the Company, has had any relationship with the Company required to be disclosed as a related person transactions and none of our executive officers served on the compensation committee (or other committee serving an equivalent function) or board of any company that employed any member of our Compensation Committee or our directors during fiscal year 2014.

DIRECTOR COMPENSATION

During fiscal year 2014, compensation for non-employee directors consisted of the following:

- $25,000 annual cash retainer for each non-employee director;
- $35,000 additional cash retainer for the Chairman of the Board;
- $7,500 additional cash retainer for the chairman of each of the Compensation and Nominating & Corporate Governance Committees;
- $10,000 additional cash retainer for the chairman of the Audit Committee;
- $10,000 additional cash retainer for each member of the Audit, Nominating & Corporate Governance, and Compensation Committees, including each chairman; and
- An award of restricted shares to each non-employee director valued at $70,000 on the grant date.

We also reimburse our directors for reasonable out-of-pocket expenses in connection with attendance at board of directors and committee meetings.

The fiscal year 2014 equity award for each director, other than for Messrs. Carnecchia and Sinisgalli, consisted of 5,654 restricted shares, based on a $12.38 grant date price, and was granted under the 2011 Stock Incentive Plan. The restricted shares vested on March 31, 2014, and provided for pro-rata vesting upon retirement prior to March 31, 2014. The grant was made in June 2013 to the then current non-employee directors; however,

Mr. Cueva declined the award given the significant ownership in the Company by his firm, MAK Capital. The award for each of Messrs. Carnecchia and Sinisgalli was made in November 2013 at the time of their first election to the board and, at the discretion of the board, was pro-rated at half the full-year director equity award value, consisting of 3,056 restricted shares based on an $11.45 grant date price. Their restricted shares also vested on March 31, 2014. As with Mr. Cueva, Mr. Kaufman declined an award upon his appointment to the board in February 2014 given the significant ownership in the Company by his firm, MAK Capital.

Our directors are subject to share ownership guidelines that require ownership of either (i) three times the director s respective annual cash retainer within two years of service and six times the director s respective annual cash retainer within four years of service; or (ii) 15,000 shares within the first two years following the director s election to the board of directors and 45,000 shares within four years of election. We pay no additional fees for board of director or committee meeting attendance.

Director Compensation for Fiscal Year 2014

Director	Fees Earned or Paid in Cash ($)(1)	Stock Awards ($)(2)	Total ($)
Max Carnecchia	17,500	34,991	52,491
R. Andrew Cueva	46,406		46,406
Jerry Jones	55,625	69,997	125,622
Michael A. Kaufman	5,223		5,223
Keith M. Kolerus	83,750	69,997	153,747
Robert A. Lauer	41,250	69,997	111,247
Robert G. McCreary, III	26,250	69,997	96,247
John Mutch	45,000	69,997	114,997
Pete Sinisgalli	19,531	34,991	54,522

(1) Fees are paid quarterly.
(2) Amounts in this column represent the grant date fair value of the restricted shares computed in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 718. As of March 31, 2014, the aggregate number of unexercised stock options held by each non-employee director was as follows: Mr. Kolerus, 15,000.

PROPOSAL 1

ELECTION OF DIRECTORS

At the Annual Meeting, shareholders will elect four Class B Directors for a term expiring at the 2016 Annual Meeting. The board of directors nominees for election are James H. Dennedy, Jerry Jones, Michael A. Kaufman, and John Mutch. Mr. Kaufman is a first-time nominee to the board. On February 18, 2014, the board named Mr. Kaufman to the board to fill the vacancy created when Mr. Cueva resigned as a director effective February 14, 2014. Mr. Cueva resigned from the board following his earlier resignation as a Managing Director of MAK Capital, our largest shareholder. The board believed that it was important to replace Mr. Cueva with another representative of MAK Capital given its substantial ownership of the Company, even though no agreement with MAK Capital or any other person requires MAK Capital to have a representative on the board. On this basis, Mr. Kaufman, the President of MAK Capital, was selected by the board to fill the vacancy in February and nominated by the board for election at the Annual Meeting.

Each nominee has indicated his willingness to serve as a director, if elected. A biography for each director nominee and our continuing directors follows and, if applicable, arrangements under which a director was appointed to the board of directors or information regarding any involvement in certain legal or administrative

proceedings is provided. Additional information about the experiences, qualifications, attributes, or skills of each director and director nominee in support of his service on the board of directors is also provided.

THE BOARD OF DIRECTORS RECOMMENDS THAT SHAREHOLDERS VOTE FOR THE ELECTION OF MESSRS. DENNEDY, JONES, KAUFMAN AND MUTCH. PROXY CARDS RECEIVED BY THE COMPANY WILL BE VOTED FOR THE ELECTION OF MESSRS. DENNEDY, JONES, KAUFMAN AND MUTCH UNLESS THE SHAREHOLDER SPECIFIES OTHERWISE ON THE PROXY CARD.

DIRECTOR NOMINEES

(Class B Term to Expire in 2016)

James H. Dennedy	Age 48	Director since 2009

President and Chief Executive Officer of the Company since October 2011. Interim President and Chief Executive Officer since May 2011. Principal and Chief Investment Officer with Arcadia Capital Advisors, LLC, an investment management company making active investments in public companies, from April 2008 to May 2011. President and Chief Executive Officer of Engyro Corporation, an enterprise software company offering solutions in systems management, from January 2005 to August 2007. Previously a director of Entrust, Inc., I-many, Inc., and NaviSite, Inc. As a former President of a division of a publicly-held software company and as a Chief Executive Officer of a private software company, Mr. Dennedy has experience in the technology industry. In addition, Mr. Dennedy has extensive experience in investment strategy, capital structure, financial strategy, mergers and acquisitions, and significant public company leadership and board experience.

Jerry Jones	Age 58	Director since 2012

Chief Ethics and Legal Officer, Executive Vice-President of Acxiom Corporation, a marketing technology and services company, since 1999. Prior to joining Acxiom, Mr. Jones was a partner with the Rose Law Firm in Little Rock, Arkansas, where he specialized in problem solving and business litigation for 19 years, representing a broad range of business interests. Previously he was a director of Entrust, Inc. He is a 1980 graduate of the University of Arkansas School of Law and holds a bachelor s degree in public administration from the University of Arkansas. As the Chief Legal Officer of a technology company, Mr. Jones has extensive experience with legal, privacy, and security matters. He has also led the strategy and execution of mergers and alliances and international expansion efforts.

Michael A. Kaufman	Age 42	Director since 2014

Mr. Kaufman is the President of MAK Capital, a financial investment advisory firm based in New York, NY, which he founded in 2002. Mr. Kaufman holds a B.A. degree in Economics from the University of Chicago, where he also received his M.B.A. He also earned a law degree from Yale University. From 2013 to 2014 Mr. Kaufman served on the board of directors of Zygo Corporation (NASDAQ: ZIGO) and as a member of its compensation and corporate governance and nominating committees. As President of MAK Capital, the Company s largest shareholder, Mr. Kaufman is uniquely qualified to represent the interests of the Company s shareholders. Additionally, Mr. Kaufman s qualifications and experience include capital markets, investment strategy and financial management.

John Mutch	Age 58	Director since 2009

Founder and managing partner of MV Advisors LLC. Mr. Mutch founded MV Advisors in January of 2006 as a strategic block investment firm which provides focused investment and operational guidance to both private and public companies. MV Advisors current portfolio includes companies in the technology, active lifestyle and sports segments valued in excess of $100M. Mr. Mutch s career as an operating executive in the technology

includes serving as Chairman and Chief Executive Officer of BeyondTrust software from 2008 to 2013, as a Director and Chief Executive Officer of Peregrine Systems (Nasdaq: PRGS) from 2003 to 2005, and as a Director and Chief Executive Officer on HNC Software (Nasdaq: HNCS) from 1999 to 2002. Previously he spent eight years in a variety of executive sales and marketing positions at Microsoft Corporation. Mr. Mutch current serves on the board of directors of Steel Excel (Nasdaq: SXCL). Mr. Mutch holds a B.S. In Economics from Cornell University and an M.B.A. from the University of Chicago.

CONTINUING DIRECTORS

(Class A Term to Expire in 2015)

Max Carnecchia	Age 51	Director since 2013

President and Chief Executive Officer and a member of the board of directors of Accelrys, Inc., a provider of scientific business intelligence software, since June 2009. Prior to joining Accelrys, Mr. Carnecchia served as President of Interwoven, Inc., a content management software company, which was acquired by Autonomy Corporation plc in January 2009. Prior to joining Interwoven, Mr. Carnecchia served as Vice President of Global Sales of Xoriant Corporation, a software product development company, from April 2000 to January 2001 and as Vice President of Sales and Services of SmartDB Corporation, a provider of data integration toolkits for systems integrators and IT organizations, from September 1996 to February 2000. Mr. Carnecchia s more than two decades of high technology experience allows him to bring to the board of directors a broad understanding of the operational and strategic issues facing the Company.

Keith M. Kolerus	Age 68	Director since 1998

Chairman of the Board of Directors of the Company since October 2008. Retired Vice President, American Division, National Semiconductor, a producer of semiconductors and a leader in analog power management technology, from 1996 to February 1998. Mr. Kolerus served as Chairman of the Board of Directors of National Semiconductor Japan Ltd., from 1995 to 1998, and Chairman of the Board of Directors of ACI Electronics, LLC, from 2004 to 2008. Mr. Kolerus has extensive experience in engineering, global operations, private and public companies, software and hardware technology companies, government contracting, capital markets, financial management, and the technology industry. Mr. Kolerus prior experiences as a board chairman uniquely qualify him to lead the board of directors as its Chairman.

Peter F. Sinisgalli	Age 58	Director since 2013

Chief Executive Officer and a member of the board of directors of Eze Software Group, a provider of enterprise software for the investment management marketplace, since May 2014. Member of the board of directors of Manhattan Associates, a provider of supply chain management software, since March 2004. Mr. Sinisgalli served as Manhattan Associates president and chief executive officer from 2004 to 2012. Before joining Manhattan Associates, Mr. Sinisgalli spent a year at NewRoads, Inc., a privately held third-party fulfillment provider, where he held the position of president and chief executive officer. Prior to that, Mr. Sinisgalli spent six years at CheckFree Corporation, a Nasdaq-listed global leader in outsourced electronic processing services. His last position at CheckFree was president and chief operating officer. Mr. Sinisgalli spent 14 years at The Dun & Bradstreet Corporation where his last position was executive vice president and chief financial officer for Dun & Bradstreet Software.

EXECUTIVE OFFICERS

The following are biographies for each of our current, non-director executive officers. The biography for Mr. Dennedy, our President and Chief Executive Officer, and a director, is provided above.

Name	Age	Current Position	Previous Positions
Janine K. Seebeck	38	Senior Vice President, Chief Financial Officer and Treasurer since August 2013.	Vice President and Controller November 2011 to August 2013. Vice President of Finance, Asia Pacific, at PGi; from 2008 to April 2011. Vice President, Corporate Controller at Premiere Global Services, Inc. from 2002 to 2008.
Kyle C. Badger	46	Senior Vice President, General Counsel and Secretary since October 2011.	Executive Vice President, General Counsel and Secretary at Richardson Electronics, Ltd. from 2007 to October 2011. Senior Counsel at Ice Miller LLP from 2006 to 2007. Partner at McDermott, Will & Emery LLP from 2003 to 2006.
Larry Steinberg	46	Senior Vice President and Chief Technology Officer since June 2012.	Principal Development Manager, Microsoft Corporation from August 2009 to May 2012, and Principal Architect from June 2007 to July 2009; Founder and Chief Technology Officer of Engyro Corporation from March 1995 to May 2007.
Michael Buckham-White	43	Senior Vice President, Sales and Marketing since January 2014	Principal at We Engage Marketing, LLC consulting firm 2012 to 2013; Vice President of Analyst Relations/Strategic Communications 2010 to 2012 at PGi; Vice President/Director of Online Sales, Interactive Marketing, and Customer Insight & Analytics from 2006 to 2010 at Premiere Global Services, Inc.

BENEFICIAL OWNERSHIP OF COMMON SHARES

The following table shows the number of common shares beneficially owned as of July 3, 2014 by (i) each current director; (ii) our Named Executive Officers; (iii) all directors and executive officers as a group; and (iv) each person who is known by us to beneficially own more than 5% of our common shares.

Name	Common Shares	Shares Subject to Exercisable Options	Restricted Shares (1)	Total Shares Beneficially Owned (1)	Percent of Class (2)
Directors and Nominees					
Max Carnecchia	4,433		4,837	9,270	*
Jerry Jones	14,709		4,837	19,546	*
Michael A. Kaufman (3)	7,056,934			7,056,934	31.2
Keith M. Kolerus	118,002	15,000	4,837	137,839	*
John Mutch	49,087		4,837	53,924	*
Peter F. Sinisgalli	43,056		4,837	47,893	*
Named Executive Officers					
Kyle C. Badger	29,702	23,548	14,846	68,096	*
James H. Dennedy	140,518	68,962	67,071	276,551	1.2
Robert R. Ellis					*
Tony Ross	1,410	13,333	7,448	22,191	*
Janine Seebeck	13,303	11,544	11,632	36,479	*
Larry Steinberg	38,115	17,948	48,873	104,936	*
All directors and executive officers	7,415,043	150,335	177,647	7,837,636	34.4
Other Beneficial Owners					
MAK Capital One, LLC et al 590 Madison Avenue, 9th Floor New York, New York 10022	7,056,934 (4)				31.2
Capital Research Global Investors 333 South Hope Street Los Angeles, CA 90071	1,927,391 (5)				8.5
Dimensional Fund Advisors LP Palisades West, Building One 6300 Bee Cave Road Austin, Texas, 78746	1,797,110 (6)				8.0
RGM Capital, LLC 9010 Strada Stell Court, Suite 105 Naples, FL 34109	1,579,596 (7)				7.0
Black Rock, Inc. 40 East 52nd Street New York, New York 10022	1,408,148 (8)				6.2

(1) Beneficial ownership of the shares comprises both sole voting and dispositive power, or voting and dispositive power that is shared with a spouse, except for restricted shares for which individual has sole voting power but no dispositive power until such shares vest.

(2) * indicates beneficial ownership of less than 1% on July 3, 2014.

(3) Comprised entirely of shares beneficially owned by MAK Capital One L.L. C. Mr. Kaufman is the managing member of MAK Capital One L.L.C. and shares voting and dispositive power with respect to all of the shares.

(4) As reported on a Schedule 13D/A dated November 15, 2013. MAK Capital One LLC has shared voting and dispositive power with respect to all of the shares. MAK Capital One LLC serves as the investment manager of MAK Capital Fund LP (MAK Fund) and MAK-ro Capital Master Fund LP (MAK-ro Fund). MAK GP LLC is the general partner of MAK Fund and MAK-ro Fund. Michael A. Kaufman, managing member and controlling person of MAK GP LLC and MAK Capital One L.L.C., has shared voting and dispositive power with respect to all of the shares. MAK Fund has shared voting and dispositive power with respect to 3,424,973 shares. MAK-ro Fund has shared voting and dispositive power with respect to 1,859,675 shares.

Paloma International L.P. (Paloma), through its subsidiary Sunrise Partners Limited Partnership, and S. Donald Sussman, controlling person of Paloma, have shared voting and dispositive power with respect to 1,772,286 shares. The principal business address of MAK Capital One LLC, MAK GP LLC and Messrs. Kaufman and Cueva is 590 Madison Avenue, New York, New York 10022. The principal address of MAK Fund is c/o Dundee Leeds Management Services Ltd., 129 Front Street, Hamilton, HM 12, Bermuda. The principal business address of MAK-ro Fund is c/o Dundee Leeds Management Services Ltd., Waterfront Centre, 2nd Floor, 28 N. Church Street, P.O. Box 2506, Grand Cayman KY1-1104, Cayman Islands. The principal address of Paloma and Sunrise Partners Limited Partnership is Two America Lane, Greenwich, Connecticut 06836-2571. The principal business address for Mr. Sussman is 217 Commercial Street, Portland, Maine 04101.

On May 31, 2011, MAK Fund, Paloma and Computershare Trust Company, N.A. (the Trustee) entered into an Amended and Restated Voting Trust Agreement (the Revised Voting Trust Agreement) to clarify the effect on the voting trust created by the Voting Trust Agreement dated as of December 31, 2009, were the reporting persons (named above) to beneficially own one-third or more of the Company s outstanding voting securities as a result of a decrease in the total number of voting securities outstanding. In such event, regardless of the reporting persons economic interest in the Company, its voting power will be effectively limited to no more than 23% or 27% of the voting securities in the event of a shareholder vote on (i) a merger, consolidation, conversion, sale or disposition of stock or assets or other business combination which requires approval of two-thirds of the Company s voting power (a Strategic Transaction) or (ii) a transaction other than a Strategic Transaction which requires approval of two-thirds of the Company s voting power (an Other Transaction), respectively. In connection with a Strategic Transaction or Other Transaction, the reporting persons would continue to possess the total voting power only over a number of voting securities that would equal the total voting power it would possess were it to hold only one-third of the voting securities. The Revised Voting Trust Agreement will become effective if and when the number of shares owned by the reporting persons equals or exceeds one-third of the voting securities then outstanding as a result of a decrease in the total number of voting securities outstanding. Until such time, the Voting Trust Agreement will remain in full force and effect.

The Voting Trust Agreement provides that, for transactions requiring at least two-thirds of the voting power to approve, Trustee will vote shares as follows: (i) for a Strategic Transaction, vote shares that exceed 20% of the outstanding shares in favor of, against, or abstaining from voting in the same proportion as all other shares voted by shareholders (including reporting persons shares that do not exceed the 20% threshold); and (ii) for Other Transactions, vote shares that exceed 25% of the outstanding shares in favor of, against, or abstaining from voting in the same proportion as all other shares voted by shareholders (including reporting persons shares that do not exceed the 25% threshold). The Voting Trust Agreement terminates (i) if the vote necessary to approve all forms of transactions is lowered to the affirmative vote of holders of shares entitling them to exercise at least a majority of the voting power on the proposal to approve such transactions (from two-thirds); (ii) if MAK Fund and Paloma are no longer members of a group for purposes of Section 13(d) of the Securities Exchange Act, then the Voting Trust Agreement terminates with respect to any of MAK Fund and Paloma that beneficially owns not more than 20% of the outstanding shares; (iii) on February 18, 2020, or February 18, 2025 if MAK Fund continues to hold 20% of the outstanding shares; or (v) if another person or entity holds greater than 20% of the outstanding shares that are not subject to a similar voting agreement.

(5) As reported on a Schedule 13G dated February 6, 2014. Capital Research Global Investors has sole voting and dispositive power with respect to all of the shares.

(6) As reported on a Schedule 13G/A dated February 10, 2014. Dimensional Fund Advisors LP has sole voting power with respect to 1,766,747 shares and sole dispositive power with respect to 1,797,110 shares.

(7) As reported on a Schedule 13G dated February 12, 2014. RGM Capital, LLC has shared voting and dispositive power with respect to all of the shares. Robert G. Moses is the managing member of RGM Capital, LLC, and shares voting and dispositive power with respect to all of the shares.

(8) As reported on a Schedule 13G/A dated January 17, 2014. BlackRock, Inc. has sole voting power with respect to 1,368,065 shares and sole dispositive power with respect to all of the shares.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act requires the Company s directors and certain of its executive officers and persons who beneficially own more than 10% of the Company s common shares to file reports of and changes in ownership with the SEC. Based solely on the Company s review of copies of SEC filings it has received or filed, the Company believes that each of its directors, executive officers, and beneficial owners of more than 10% of the shares satisfied the Section 16(a) filing requirements during fiscal year 2014, with one exception. On March 31, 2013, restricted shares for Ms. Seebeck vested, and she opted to settle her tax obligation upon vesting with share withholding. The Form 4 to report such share withholding was filed on April 26, 2013.

COMPENSATION DISCUSSION AND ANALYSIS

Introduction

With the divestiture of the Technology Solutions Group (TSG) in August 2011, the Retail Solutions Group (RSG) in July 2013 and our United Kingdom business entity in March 2014, the Company has completed its transformation into a smaller, refocused Company operating as a pure play software-driven solutions provider to the hospitality industry. As discussed in the Compensation Discussion and Analyses contained in the Proxy Statements for our 2012 and 2013 Annual Meetings of shareholders, following the sale of TSG, the Company engaged new leadership in key executive positions with comparatively lower compensation arrangements to reflect the smaller, refocused Company. The Compensation Committee has since maintained the compensation programs put in place in fiscal year 2012 with even more emphasis on pay for financial performance and long-term incentives.

This Compensation Discussion and Analysis (the CD&A) describes our executive compensation philosophy and programs during fiscal year 2014. Executive compensation arrangements with our Named Executive Officers are governed by the Committee. In this CD&A, you will find detailed compensation information for our Named Executive Officers, which consist of our Chief Executive Officer (CEO), our Chief Financial Officer (CFO), our former CFO and our three other most highly compensated officers during fiscal year 2014, as listed below:

- James Dennedy, President and Chief Executive Officer
- Janine Seebeck, Senior Vice President, Chief Financial Officer and Treasurer
- Robert Ellis, former Senior Vice President, Chief Financial Officer, Chief Operating Officer and Treasurer
- Kyle Badger, Senior Vice President, General Counsel and Secretary
- Tony Ross, Vice President of Sales
- Larry Steinberg, Senior Vice President, Chief Technology Officer

Mr. Ellis employment with the Company ended on August 6, 2013. Ms. Seebeck was promoted to the CFO position on the same day from her previous position as Vice President and Controller. Mr. Ross is not an executive officer of the Company, and his compensation for fiscal year 2014 was not governed by the Compensation Committee. He is included as a Named Executive Officer because the Company had only four executive officers for a substantial portion of fiscal year 2014, and Mr. Ross was the next most highly compensated non-executive officer of the Company.

Compensation Highlights

Compensation Focus for Fiscal Year 2014. After considering the results of our 2013 vote on Named Executive Officer compensation, which confirmed the Company s philosophy and objectives relative to our executive compensation program, the Compensation Committee continued efforts to maintain reduced compensation expense and link executive pay to performance by:

- Establishing minimal base salary increases;
- Focusing annual incentive on significant improvements over fiscal year 2013 results; and
- Substantially increasing long-term incentives to reward increases in shareholder value.

Performance Linked Compensation. Our Compensation Committee set fiscal year 2014 compensation, including financial and business targets for performance-based compensation, for our Named Executive Officers to continue to emphasize pay for performance by setting annual cash incentive based on goals focused on significant improvements over fiscal year 2013 results for revenue and adjusted operating income.

Our CEO s targeted pay was approximately 74% performance-based, and between 50% and 64% for each of our other Named Executive Officers targeted pay was performance-based, tied directly to annual goals or long-

term equity awards, the value of which is tied directly to an increase in share price. As discussed below, targeted annual goals were primarily based on improvements over fiscal year 2013 results for revenue and adjusted operating income.

Our operating results for fiscal year 2014 significantly outperformed our plan. Total net revenue increased 7.7%, and adjusted operating income increased $8.1 million year over year to $3.4 million from an adjusted operating loss of $4.7 million in fiscal year 2013. As a result, annual incentive payouts ranged from 113% to 128% of target for the Named Executive Officers who received an annual incentive payout.

To further link pay to performance and emphasize long-term shareholder value creation, the Compensation Committee granted long-term equity incentive awards for fiscal 2014 that were substantially higher as a percentage of base salary over the prior year, including an increase of 5.3% for Mr. Dennedy and increases between 37.8% and 57.9% for the other Named Executive Officers, other than Mr. Ross.

Chief Executive Officer Compensation. Mr. Dennedy s compensation package for fiscal year 2014 continued to reflect the Compensation Committee s ongoing commitment to link pay to performance and to maintain reduced compensation costs, as evidence by the following for Mr. Dennedy:

- No increase in base salary from the prior year s base salary;
- No increase in annual cash incentive target from the prior year s annual cash incentive target;
- 50% of long-term incentive award, granted as stock-settled appreciation rights, is based entirely on share price improvement, and the balance, granted as restricted stock, is tied to share price;
- Annual incentive payout of 128% of targeted payout was earned based on the Company s results; and
- 74% of targeted compensation was variable pay, tied either to performance or share price improvement.

Chief Financial Officer Compensation. Ms. Seebeck was appointed our CFO in August 2013 during the second quarter of fiscal year 2014. Her initial compensation package was set significantly lower than her predecessor to achieve the Compensation Committee s goal of continuing to reduce compensation cost to reflect the smaller, refocused Company, with a base salary that was set 23% lower than her predecessor s salary and an annual incentive target that was set 48% lower.

Ms. Seebeck s compensation package for fiscal year 2014, upon her appointment as CFO, also continued to reflect the Compensation Committee s ongoing commitment to link pay to performance as evidence by the following for Ms. Seebeck:

- 50% of long-term incentive award, granted as stock-settled appreciation rights, is based entirely on share price improvement, and the balance, granted as restricted stock, is tied to share price;
- Annual incentive payout of 128% of targeted payout was earned based on the Company s results; and
- 50% of targeted compensation was variable pay, tied either to performance or share price improvement

At the beginning of the fiscal year, Mr. Ellis compensation was set similarly to the other Named Executive Officers, and included a 3.3% increase in base compensation and annual incentive target and a 37.8% increase in long-term equity incentive over the prior year. Upon Mr. Ellis resignation in August 2013, he received only the base compensation earned by him to that date. He did not receive any annual incentive compensation for fiscal year 2014, and all of the long-term equity awards granted to him in fiscal year 2014 were forfeited.

Compensation Philosophy, Objectives, and Structure

Our Compensation Committee adopted its pay philosophy, objectives, and structure for Named Executive Officers to achieve financial and business goals and create long-term shareholder value. Our Compensation Committee reaffirmed the pay philosophy, objectives, and structure for fiscal year 2014.

Compensation Philosophy and Objectives. Our Compensation Committee s pay philosophy is to pay a base salary and provide target annual cash incentives and long-term equity incentives, each at the 50th percentile of

comparative peer group compensation, and to annually review these compensation components based on peer group comparisons and tie compensation to our business strategy. The Compensation Committee s objective is to establish an overall compensation package to:

Reward the achievement of business objectives approved by our board of directors;
Tie a significant portion of compensation to the long-term performance of our common shares;
Provide a rational, consistent, and competitive executive compensation program that is well understood by those to whom it applies; and
Attract, retain, and motivate executives who can significantly contribute to our success.

Compensation Structure. Our compensation structure is comprised of:

Base Salary Base salary provides fixed pay levels aimed to attract and retain executive talent. Variations in salary levels among Named Executive Officers are based on each executive s roles and responsibilities, experience, functional expertise, relation to peer pay levels, competitive assessments, individual performance, and changes in salaries in the overall general market and for all employees of the Company. Salaries are reviewed annually by our Compensation Committee, and changes in salary are based on these factors and input from our CEO, other than for himself. None of the factors are weighted according to any specific formula. New salaries generally are based on the Compensation Committee s discretion and judgment but may be based on any of the above-mentioned relevant factors.

Annual Incentives Annual incentives provide cash variable pay for achievement of the Company s financial, strategic, and operational goals and individual goals, with target incentives set as a percentage of salary, designed to reward achievement of goals with an annual cash payment. Variations in incentive components and mix among Named Executive Officers are determined by our Compensation Committee and based on each executive s respective business unit or corporate goals and each executive s individual goals and corporate-wide initiatives, as well as market data, length of time in current role or similar role at another company, and recommendations from our CEO, other than for himself.

Long-Term Incentives Long-term incentives are variable, equity incentives designed to drive improvements in performance that build wealth and create long-term shareholder value by tying the value of earned incentives to the long-term performance of our common shares. Target incentives are set as a percentage of salary. Variations in awards among Named Executive Officers are determined by our Compensation Committee after a review of various factors, including recommendations based on market data, individual ability to influence results, length of time in current role or similar role at another company, and recommendations from our CEO, other than for himself.

Compensation Key Considerations

Annual Goal Setting. Annual goals for our Named Executive Officers are tied to our financial, strategic, and operational goals and include business specific financial targets relating to our goals. The annual incentive goals for each Named Executive Officer, other than Mr. Ross, are established by our Compensation Committee, with input from our CEO (other than for himself). At fiscal year-end, the Compensation Committee evaluates the performance of each Named Executive Officer and determines an appropriate award based on established goals, with input from our CEO (other than for himself) on individual goals. Our Compensation Committee establishes our CEO s annual incentive goals and determines his appropriate award based on established goals.

Variable Pay at Risk. Our philosophy drives the provision of greater at-risk pay to our Named Executive Officers, and variable pay at risk comprised approximately 74% of target annual compensation for our CEO and between 50% and 64% for other Named Executive Officers. Our Named Executive Officers have significant opportunities for long-term, equity-based incentive compensation, higher than for annual cash incentive compensation for each Named Executive Officer other than Mr. Ross, as our philosophy is to tie a significant portion of compensation to the long-term performance of our common shares. As a result, significant emphasis is placed on long-term shareholder value creation, thereby minimizing excessive risk taking by our executives.

Components of Compensation

Fiscal Year 2014

Competitive Market Assessments. The Compensation Committee did not commission a competitive market assessment in connection with setting Named Executive Officer compensation for fiscal year 2014. However, the Committee engaged Pearl Meyer & Partners as its compensation consultant during the fiscal year and received from them a competitive market assessment that evaluated compensation levels for the Company s top four executive positions, including Messrs. Dennedy, Badger and Steinberg and Ms. Seebeck. The assessments compared current compensation levels for these executives to published compensation data for comparable executives at a peer group determined by the Compensation Committee from a group recommended by Pearl Meyer & Partners. The peer group consisted of the following software and technology companies:

Company	**Ticker**	**GICS Sub Industry**	**Revenue $ in millions**	**Market Cap July 2013 $ in millions**
SPS Commerce Inc	SPSC	Internet Software & Services	$77	$977
E2open Inc	EOPN	Internet Software & Services	$75	$512
Support.com Inc	SPRT	Internet Software & Services	$72	$254
Sourcefire Inc	FIRE	Systems Software	$223	$2,377
Gigamon Inc	GIMO	Systems Software	$97	$1,054
Cyan Inc	CYNI	Systems Software	$96	$462
Qualys Inc	QLYS	Systems Software	$91	$507
XRS Corp	XRSC	Systems Software	$63	$30
Rally Software Development Corp	RALY	Systems Software	$57	$684
Synchronoss Technologies Inc	SNCR	Application Software	$274	$1,384
QAD Inc	QADA	Application Software	$252	$193
Bottomline Technologies Inc	EPAY	Application Software	$224	$1,100
Actuate Corp	BIRT	Application Software	$139	$352

Company	Ticker	GICS Sub Industry	Revenue $ in millions	Market Cap July 2013 $ in millions
PROS Holdings Inc	PRO	Application Software	$118	$916
Jive Software Inc	JIVE	Application Software	$114	$894
Ellie Mae Inc	ELLI	Application Software	$102	$620
BSQUARE Corp	BSQR	Application Software	$101	$31
American Software Inc	AMSWA	Application Software	$100	$224
Callidus Software Inc	CALD	Application Software	$95	$251
Model N Inc	MODN	Application Software	$84	$538
inContact Inc	SAAS	Alternative Carriers	$110	$453
		75th Percentile	*$118*	*$916*
		Median	*$100*	*$512*
		25th Percentile	*$84*	*$254*
Agilysys, Inc. (*pro forma FY14*)	AGYS	Application Software	$106	$257
percentile			*55*	*23*

Peer companies were selected based on industry relevance and comparability to the Company s revenue. As detailed below, Pearl Meyer & Partners assessment showed that the compensation in fiscal year 2014 for the four Named Executive Officers whose compensation was evaluated was generally aligned with the market median.

During fiscal year 2012, Towers Watson provided the Compensation Committee with two competitive market assessments, one in March and one in August, which updated the March assessment to adjust for expected revenues of the smaller Company after the closing of the TSG sale. The assessments evaluated compensation levels for the Company s top eight executive positions, including the Named Executive Officers. The assessments compared published survey compensation data for both general industry and the high technology services industry to current compensation levels for the Company s executives. Competitive compensation levels in these industries were gathered for base salary, annual incentive, total cash compensation, long-term incentive, and total direct compensation. The purpose of the assessments was to compare current market data to our then current compensation, which was based on prior benchmarking performed by the Company, where compensation levels were benchmarked to separate, defined peer group companies for corporate executives and each business unit executive. Towers advised that an assessment using the general and high technology services industries data provides more representative and relevant comparisons given the size of the Company.

During fiscal year 2013, the Compensation Committee believed that the Towers Watson assessments performed in fiscal year 2012, without any update, remained useful for purposes of determining Named Executive Officer compensation, and, as a result, the Compensation Committee did not request or review any additional assessments in fiscal year 2013 or when setting compensation in fiscal 2014.

Tally Sheets. Our Compensation Committee analyzes tally sheets at the beginning of the fiscal year to review overall compensation and pay mix for each Named Executive Officer. Tally sheets include a three-year look-back of total compensation, including annual cash compensation, long-term incentive awards granted and earned, and benefits and perquisites. Tally sheets also include a cumulative inventory of equity grants by fiscal year, including the value of outstanding equity at the Company s current stock price and the value received for prior vesting and exercises of equity. The tally sheets bring together, in one place, all elements of Named Executive Officers actual compensation and information about wealth accumulation so that our Compensation Committee can analyze the individual elements and mix of compensation and the aggregate total amount of annual and accumulated compensation. Tally sheets are also used by the Compensation Committee to evaluate

internal pay equity among the Named Executive Officers and to determine the impact of employment termination or change of control events. In support of the philosophy of rewarding future performance, the Compensation Committee does not consider prior pay outcomes in setting future pay levels. Rather, tally sheets are used by the Compensation Committee to review compensation as compared to expectations, and our Compensation Committee determined that annual compensation set for our Named Executive Officers for fiscal year 2014 was consistent with expectations and with the established compensation philosophy and pay mix guidelines driven by that philosophy.

Fiscal Year 2014 Compensation

Salary. For fiscal year 2014, salary comprised 26% of total target compensation for our CEO and between 36% and 50% for our other Named Executive Officers. Mr. Dennedy s salary remained the same in fiscal year 2014 as in fiscal year 2013. Messrs. Badger and Ellis received cost of living increases recommended by the CEO of 4% and 3.3% respectively. Since Messrs. Badger, Ellis and Steinberg had been first hired by the Company during fiscal year 2012 or 2013, the Compensation Committee considered the competitive market assessments provided by Towers Watson in fiscal year 2012 in determining the initial salaries for the newly hired Named Executive Officers, as well as their previous salary levels and prior experience, and in determining fiscal year 2013 salaries for all the Named Executive Officers. The Compensation Committee also considered the assessments provided by Towers Watson in setting Ms. Seebeck s salary upon her promotion to the CFO role in August 2013. Mr. Ross salary for fiscal year 2014 was set by the CEO.

Annual Incentives. For fiscal year 2014, annual goals were set at the beginning of the fiscal year. The discussion below, which specifically relates to the table below under Fiscal Year 2014 Payouts, provides details regarding fiscal year 2014 annual incentive performance metrics, levels, and payouts for the Named Executive Officers.

Performance Metrics. The Compensation Committee set financial performance metrics for fiscal year 2014 annual incentives to require target level improvements over fiscal year 2013 results of then continuing operations. The target level for revenue was set at an $8.5 million, or 8.7%, improvement over fiscal 2013 results; and the target level for adjusted operating income was set at a $5.2 million improvement over a loss of $4.7 million in fiscal 2013. These levels were set based on the Company s overall operating plan and expected growth and operating improvements. Target level improvements over fiscal year 2013 results for adjusted operating income were significant because the Company had negative adjusted operating income in fiscal year 2013. Adjusted operating income is calculated as operating income excluding amortization of intangibles, stock based compensation expense and non-recurring charges. The Company believes adjusted operating income is a profitability measure and a key driver of value, focusing on sales, product mix, margins, and expense management. Adjusted operating income was selected as an annual goal component for all Named Executive Officers given the desire to balance sales and margins, as both are manageable by our Named Executive Officers. The Compensation Committee deemed positive adjusted operating income so important that no payout on financial performance measures would be earned if adjusted operating income was less than $250,000.

Performance percentages for payouts (with proportionate payouts between the target and maximum achievement levels) were based on varying levels of achievement of fiscal year 2014 budgeted results, as set forth below. Additional detail about threshold and maximum incentives are disclosed in the Grants of Plan-Based Awards for Fiscal Year 2014 table.

	Threshold		Maximum	
Component	Payout (% of target incentive)	Required Achievement of Performance Measures (%)	Payout (% of target incentive)	Required Achievement of Performance Measures (%)
Revenue	90	98.2	150	104
Adjusted Operating Income	90	50.0	150	550

The Compensation Committee believed that the plan involved moderate difficulty at the threshold level, a high degree of difficulty at the 100% target level, given continuing competition and pricing pressure in the market, and significant difficulty at the maximum level, requiring significant improvement over fiscal year 2013 results, in each case relative to future expectations at the time the levels were set. Threshold levels were based on achievement necessary to successfully execute a minimum level of the operating plan.

MBO s. In addition to objective performance metrics, management by objective goals (MBOs) comprised 50% of the annual incentive of Named Executive Officers other than Messrs. Dennedy and Ellis and Ms. Seebeck. However, MBOs could only be earned in the event that threshold adjusted operating income targets were achieved in order to place greater weight on objective performance metrics. MBOs represent individual performance-based goals, with both quantitative and qualitative measures, relative to individual responsibilities and emphasize the importance of specific tasks and company-wide initiatives. The Compensation Committee believed that MBOs were appropriate for executives whose impact on shareholder value was less direct than the CEO and CFO. The Compensation Committee has discretion in deciding whether each MBO was achieved and in determining the level of achievement, and thus payout, for the MBO components. Achievement of MBOs results in a payout ranging from a minimum of 80% for partial achievement to 100% for maximum achievement, and Named Executive Officers are eligible for proportionate payouts between the minimum and maximum achievement levels. There is no payout for MBOs below the minimum achievement level. Consistent with the other elements of compensation, MBOs were established at the beginning of year when the outcome for the fiscal year was substantially uncertain. Fiscal year 2014 MBO goals and payout allocations for the Name Executive Officers were as follows:

Executive	MBO	% of MBOs
Kyle C. Badger	Improve Legal Department service levels	33
	Develop templates and processes for corporate acquisitions	33
	Complete data privacy legal education and create a cross-department working group to review emerging data privacy issues	33
Tony Ross	Achieve 93% of North American gross profit target	40
	Ensure 25% of outside sales representatives attain 100% of quota	20
	Deliver sales expense plan within 3% of budget	20
	Capture 60 new logo businesses within North America	20
Larry Steinberg	Provide online training and curriculum to all engineers for improvement of the skills necessary to their role	20
	End FY 14 3% under your departments budget	20
	Deliver IG 4.4.3 release candidate in Oct 2013 on time with high quality	10
	Deliver IG Mobile 2.0 release candidate in July 2013 on time with high quality	10
	Deliver Visual One 8.5.1 general availability in November 2013 on time with high quality based on successful release candidate sites	10
	Deliver Analytics 2.0 pilot in August 2013 and 2.0 release candidate in February 2014 on time with high quality	10
	Deliver rGuest PMS on time with high quality, as defined in public release dates	20

Weight differences between initiatives among the Named Executive Officers corresponded to importance of each initiative in respect of the overall Company operating plan.

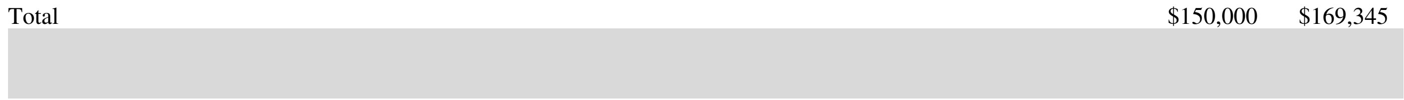
Annual Incentive Levels. For all Named Executive Officers, fiscal year 2014 target annual incentives were set as a percentage of salary. Target annual incentives were set at 85% of salary for Mr. Dennedy and 75% for Mr. Ellis, as opposed to approximately 50-60% of salary for other executives, substantially the same as the prior fiscal year when their percentage was raised in order to increase the performance-based nature of their total compensation due to their greater ability to influence corporate goals and initiatives. Ms. Seebeck s target annual incentive was set at 50% of salary upon her promotion to the CFO role. Mr. Ross target annual incentive was significantly higher, at 95% of salary, due to the nature of his role managing sales for the Company. Annual incentives comprised 23% of total target compensation for Mr. Dennedy, and between 21% and 25% for our other Named Executive Officers, other than Mr. Ross whose target annual incentive was 42% of total target compensation. Target annual incentives for all the Named Executive Officers were set at substantially the same

level as the prior fiscal year when, as with salaries, target levels were adjusted based on competitive market assessments provided by Towers Watson in fiscal year 2012 and used for determining fiscal year 2013 levels. The 2012 survey data indicated that 2013 target annual incentive percentages of salary were aligned with the market median, and total target cash compensation (salary and annual incentive) was in the competitive range for the positions evaluated, ranging from 21% below to 16% above market median. Mr. Dennedy s annual incentive as a percentage of salary was reduced from 100% to 88% in 2013 to set his total target cash compensation in line with market median and further reduced to 85% in 2014 to partially offset an increase in his long-term incentives. The competitive market assessment provided by Pearl Meyers & Partners during fiscal year 2014 indicated that the fiscal year 2104 target annual incentive values ranked between the 50th and 75th percentile and that total target cash compensation (salary and annual incentive) ranked approximately at the market median, with Mr. Dennedy and Mr. Badger positioned between the 50th and 75th percentile and Ms. Seebeck and Mr. Steinberg positioned between the 25th and 50th percentile.

Fiscal Year 2014 Payouts. The chart below sets forth the fiscal year 2014 annual incentive opportunity for each Named Executive and the components, weightings, and actual annual incentive payouts based on the Compensation Committee s review of the achievement of the performance measures. Only 99% of the revenue target was achieved resulting in a payout of 94% of target incentive under the plan. 671% of the adjusted operating income target was achieved, but this resulted in a payout of only 150% of target incentive, the maximum amount under the plan. The attainment by each Named Executive Officer of their respective MBOs is reflected in the table below.

			Performance Metrics			Annual Incentive	
	Target Incentive as a % of salary	**Component**	**Weight**	**Target**	**Actual (1)**	**Target**	**Payout**
James H. Dennedy	85%	Revenue	40%	$106.9M	$105.9M	$140,000	$132,278
		AOI	60%	$0.5M	$3.4M	$210,000	$315,000
Total						$350,000	$447,278
Janine Seebeck	50%	Revenue	40%	$106.9M	$105.9M	$48,000	$45,352
		AOI	60%	$0.5M	$3.4M	$72,000	$108,000
						$120,000	$153,352
Robert R. Ellis	75%	Revenue	40%	$106.9M	$105.9M	$93,000	$0
		AOI	60%	$0.5M	$3.4M	$139,500	$0
Total						$232,500	$0
Kyle C. Badger	50%	Revenue	20%	$106.9M	$105.9M	$26,000	$24,566
		AOI	30%	$0.5M	$3.4M	$39,000	$58,500
		MBO	50%			$65,000	$65,000
Total						$125,000	$148,066
Tony Ross	95%	Revenue	20%	$106.9M	$105.9M	$33,000	$30,264
		AOI	30%	$0.5M	$3.4M	$49,500	$74,250
		MBO	50%			$82,500	$82,500
Total						$165,000	$187,014
Larry Steinberg	60%	Revenue:	20%	$106.9M	$105.9M	$30,000	$28,345
		AOI	30%	$0.5M	$3.4M	$45,000	$67,500
		MBO	50%			$75,000	$73,500

Total	$150,000	$169,345



(1) Adjusted operating income (AOI) is a non-GAAP measure. A reconciliation of operating loss, a GAAP measure, for fiscal year 2014 to adjusted operating income is as follows:

(In thousands)	**2014**
Operating Loss	$ (6,896)
Share-based compensation expense	2,119
Amortization of intangibles	6,414
Asset impairments and related charges	327
Restructuring, severance and other charges	1,392
Adjusted operating income	3,356

In addition to the amounts noted above, in fiscal year 2014 Ms. Seebeck and Mr. Badger received a discretionary bonus of $25,000 each from the Compensation Committee, upon the recommendation of the CEO, related to their work in connection with the RSG transaction.

Long-Term Incentives. As with the annual incentives, the Compensation Committee approved fiscal year 2014 long-term incentive (LTI) awards at the beginning of year when the outcome for the fiscal year was substantially uncertain. LTI awards to Named Executive Officers consisted of stock-settled appreciation rights (SSARs) and restricted shares, both with three-year vesting schedules, pursuant to the Company s shareholder-approved 2011 Stock Incentive Plan. The Compensation Committee considered various LTI award alternatives. While annual incentives targeted specific performance goals, the focus on LTI awards was to link compensation directly to shareholder gains and to improve retention of key management during the Company s time of transition. SSARs provided the direct link between compensation and shareholder gains in a less dilutive manner than with stock options, and the three-year vesting schedule also enhances retention. Restricted shares also tie compensation to shareholder gains and highly bolster retention over the vesting period.

LTI awards comprised 52% of total target compensation for Mr. Dennedy to directly link a significant portion of his pay, when combined with his annual incentive, to performance and comprised between 25% and 43% for our other Named Executive Officers. In setting LTI awards for the Named Executive Officers other than the CEO, the Compensation Committee received input and recommendations from our CEO regarding each Named Executive Officer s relative ability to influence results. Target levels were substantially increased over the prior year for all the Named Executive Officers other than the CEO and Mr. Ross in order to further link pay to performance and emphasize long-term shareholder value creation, as described above. The competitive market assessment provided by Pearl Meyers & Partners indicated that fiscal year 2104 LTI values were below the market median, ranging from 1% lower than the market median for Mr. Dennedy and between 24% and 33% below the market median for Messrs. Badger and Steinberg and Ms. Seebeck.

The Compensation Committee set the 2014 LTI awards for each Named Executive Officer as follows:

Name	**Percent of Salary (%)**	**Total LTIP Value ($)**	**SSARs Granted (#)**	**Restricted Shares Granted (#)**
James H. Dennedy	200	800,000	50,188	32,310
Janine K. Seebeck	50	120,000	7,734	4,985
Robert R. Ellis	100	310,000	19,448	12,520
Kyle C. Badger	69	180,000	11,292	7,270
Tony Ross	35	59,500		4,806
Larry Steinberg	120	300,000	18,821	12,116

All SSARs and restricted shares vest in one-third increments on March 31, 2014, 2015 and 2016. Other than certain SSARs granted to Ms. Seebeck, the SSARs were granted at an exercise price of $12.38 (the closing price

of the common shares on the grant date), have a seven-year term, and are settled in common shares upon exercise. Ms. Seebeck was originally granted 5,019 SSARs at the $12.38 exercise price; she received an additional grant of 2,715 SSARs at an exercise price of $11.40 upon her promotion to CFO.

Additional Compensation Executive Benefits. We provide executive benefits to our Named Executive Officers including additional life and long-term disability insurance plans. From time to time, Named Executive Officers also may participate in supplier sponsored events. Executive benefits are further described in the Summary Compensation Table. We believe these benefits enhance the competitiveness of our overall executive compensation package. We have, however, limited executive benefits offered to reduce compensation costs. Additionally, welfare benefits offered to our Named Executive Officers are the same level of benefits offered to all Company employees, except that we pay for the cost of physicals to promote the health and well-being of our executives.

Employment Agreements and Change of Control

The material termination and change of control provisions of various agreements are summarized below for each Named Executive Officer and are covered in more detail in the Termination and Change of Control table and accompanying discussion.

Employment Agreements. All of the Named Executive Officers other than Mr. Ross recently entered into employment agreements with the Company effective July 22, 2014, all with substantially the same terms. Mr. Ellis employment agreement terminated in September 2013. The new employment agreements all have three year terms expiring July 21, 2017. Under the employment agreements, upon termination without cause, we must pay severance equal to one year s salary and target annual incentive and a lump sum amount equal to the executive s total premium for one year of COBRA continuation coverage under the Company s health benefit. If the executive s position is changed such that his or her responsibilities are substantially lessened (a change in position), the executive may terminate his or her employment if the Company fails to materially cure such condition within 30 days following notice of such condition by the executive, and the termination will be deemed to be a termination without cause and the executive is entitled to his or her severance benefits. None of the Named Executive Officers with employment agreements is entitled to excise tax gross-up payments. In consideration of the severance benefits, each employment agreement contains a 12-month post-termination non-solicitation provision, an indefinite confidentiality provision, and a 12-month post-termination non-compete provision. In the event that any of these Named Executive Officers are terminated without cause or for a change of position in the 24 months following a change of control of the Company, the Named Executive Officer is entitled to severance pay equal to two year s salary and target annual incentive and a lump sum amount equal to the executive s total premium for one year of COBRA continuation coverage under the Company s health benefit.

Our Compensation Committee believes that the terms of these employment agreements enhance our ability to retain our executives and contain severance costs by providing reasonable severance benefits competitive with market practice. Severance costs are contained by limiting pay to one year in the absence of a change of control, limiting personal benefits, not providing accelerated vesting for awards under the agreements, and narrowly defining a voluntary termination that triggers severance benefits. Severance payments in the event of a change of control are subject to a double trigger such that severance benefits are provided only upon a combination of a change of control and a qualified termination. Additionally, the Company benefits greatly from the non-competition, non-disclosure, and non-solicitation clauses contained in the employment agreements.

Mr. Ross is subject to the Company s U.S. Severance Pay Policy. Under the policy, Mr. Ross is eligible to receive severance pay based on position and full years of service, and in exchange for signing a release of claims, in the event that his employment is terminated by the Company for a reason other than for cause. As a vice president, on March 31, 2014, Mr. Ross was eligible for severance pay equal to 41 weeks of his base salary and applicable health benefits for the same period. Mr. Ross is also eligible under the policy to receive up to three months of outplacement assistance. None of the other Named Executive Officers are eligible for severance under the policy.

Accelerated Vesting. None of the employment agreements discussed above provide for accelerated vesting of equity. Under our 2011 Stock Incentive Plan, the only plan for which any of the Named Executive Officers have unvested equity, vesting is accelerated upon the actual occurrence of a change of control for all SSARs and restricted shares (including performance shares). The Compensation Committee believes that during a change of control situation, a stable business environment is in the shareholders best interests, and accelerated vesting provisions provide stability. The accelerated vesting provisions are applicable to all employees who receive equity awards, not just executive management.

Additional Compensation Policies

Clawback Recoupment of Bonuses, Incentives, and Gains. Under the Company s clawback policy, if the board of directors determines that our financial statements are restated due directly or indirectly to fraud, ethical misconduct, intentional misconduct, or a breach of fiduciary duty by one or more executive officers or vice presidents, then the board of directors will have the sole discretion to cancel any stock-based awards granted and to take such action, as permitted by law, as it deems necessary to recover all or a portion of any bonus or incentive compensation paid and recoup any gains realized in respect of equity-based awards, provided recoveries cannot extend back more than three years. Additionally, under Section 304 of the Sarbanes-Oxley Act, if we are required to restate our financial statements due to material noncompliance with any financial reporting requirements as a result of misconduct, our CEO and CFO must reimburse us for any bonus or other incentive-based or equity-based compensation received during the 12 months following the first public issuance of the non-complying document, and any profits realized from the sale of our securities during those 12 months.

Stock Ownership Guidelines. To underscore the importance of strong alignment between the interests of management and shareholders, the board of directors approved stock ownership guidelines for directors and executives, with our CEO having the highest ownership requirement. Director and executive compensation is designed to provide a significant opportunity to tie individual rewards to long-term Company performance. The objective of our stock ownership guidelines is to support this overall philosophy of alignment and to send a positive message to our shareholders, customers, suppliers, and employees of our commitment to shareholder value. Each director and executive officer is expected to maintain minimum share ownership of either: (i) a multiple of base salary or director annual retainer listed below, or (ii) the number of shares listed below:

	Multiple of Director Annual Retainer and Executive Base Salary		Number of Shares	
Title	**2 Years**	**4 Years**	**2 Years**	**4 Years**
Director	3x	6x	15,000	45,000
CEO	2.5x	5x	125,000	250,000
Senior Vice President	0.5x	2x	15,000	75,000
LTIP Participants		0.5x	2,500	15,000

Stock ownership that is included toward attainment of the guidelines includes (i) shares held of record or beneficially owned, either directly or indirectly; (ii) shares acquired upon exercise of stock options or SSARs; (iii) vested restricted or deferred shares; (iv) phantom or deferred share units held in a deferred compensation plan; and (v) shares or deferred shares acquired by dividend reinvestment. Directors and executives are expected to attain the specified target ownership levels within both two and four years from the later of the effective date of this policy or becoming a director or an executive, and remain at or above that level until retirement. Annually, the board of directors reviews progress toward achieving these ownership levels. Director and executives who have not attained the specified ownership guidelines will be required to hold 75% of shares acquired upon exercise of stock options and SSARs or vesting of performance or restricted shares until they meet their target ownership level. If ownership guidelines are not met within two and four years, our Compensation Committee has the right to pay an executive s annual incentives in shares until ownership guidelines are achieved.

Impact of Tax and Accounting Considerations. In general, the Compensation Committee considers the various tax and accounting implications of the pay mechanisms used to provide pay to our Named Executive Officers, including the accounting cost associated with long-term incentive grants, when determining compensation. Section 162(m) of the Internal Revenue Code generally prohibits any publicly held corporation from taking a federal income tax deduction for pay to the chief executive officer and the three other highest compensated executive officers (other than the chief financial officer) in excess of $1 million in any taxable year. Exceptions are made for certain qualified performance-based pay. It is the Compensation Committee s objective to maximize the effectiveness of our executive pay plans in this regard. The pay instruments used, including salaries, annual incentives, and equity, are tax deductible to the extent that they are performance-based or less than $1 million for such Named Executive Officer in a given year. However, the Compensation Committee retains discretion to pay compensation that is not tax deductible in situations where it believes such compensation is appropriate.

COMPENSATION COMMITTEE REPORT

The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis required by Item 402(b) of Regulation S-K with the Company s management. Based on that review and discussion, the Compensation Committee recommended to the board of directors that the Compensation Discussion and Analysis be included the Company s 2014 Annual Report on Form 10-K for the fiscal year ended March 31, 2014 and the Proxy Statement for its 2014 Annual Meeting of Shareholders.

The Compensation Committee of the Board of Directors

Pete Sinisgalli, Chairman

Michael A. Kaufman

Keith M. Kolerus

John Mutch

RELATIONSHIP WITH COMPENSATION COMMITTEE CONSULTANT

During fiscal year 2014, the Compensation Committee retained Pearl Meyer & Partners as compensation consultant for executive compensation matters. All fees paid to Pearl Meyer & Partners in fiscal year 2014 were for executive compensation consultation.

EXECUTIVE COMPENSATION

Summary Compensation Table

The following table and related notes provide information regarding fiscal year 2014 compensation for our Named Executive Officers, including our CEO and CFO and the other three most highly compensated executive officers whose total compensation exceeded $100,000 for fiscal year 2014.

Summary Compensation Table for Fiscal Year 2014

Name and Principal Position	Year	Salary ($)(1)	Bonus ($)(2)	Stock Awards ($)(3)	Option Awards ($)(3)	Non-Equity Incentive Plan Compen-sation ($)(4)	Non-qualified Deferred Compen-sation Earnings ($)	All Other Compen-sation ($)(5)	Total ($)
James H. Dennedy	FY14	400,000		399,998	400,129	447,278		32,760	1,680,038
	FY13	415,385		379,997	380,309	509,784		20,481	1,705,956
President and Chief Executive Officer	FY12	286,600		311,640		369,045		10,780	978,065
Janine K. Seebeck	FY14	218,490	25,000	59,995	60,015	153,352		11,505	528,347
Senior Vice President, Chief Financial Officer and Treasurer									
Robert R. Ellis	FY14	160,231		154,998	155,051			9,299	479,530
Former Senior Vice President,	FY13	290,934		85,499	85,566	327,718		11,186	800,903
Chief Operating Officer, Chief Financial Officer and Treasurer	FY12	131,705		123,199	81,335	88,591		3,520	428,350
Kyle C. Badger	FY14	258,462	25,000	90,003	90,027	148,066		12,091	623,619
Senior Vice President, General Counsel and Secretary	FY13	259,615		62,500	62,548	153,921		37,796	576,380
Tony Ross	FY14	174,231		59,498		187,014		12,676	433,419
Vice President, Sales									
Larry Steinberg	FY14	246,154		149,996	105,052	169,345		10,969	726,468
	FY13	205,962	39,550	574,750	95,660	148,972		7,646	1,072,540

Senior Vice President, Chief
Technology Officer

(1) For Mr. Ellis, 2014 salary is through August 2014. For Mr. Steinberg, 2013 salary is from start date through March 31, 2013.
(2) For Ms. Seebeck and Mr. Badger, amount consists of discretionary bonus related to the RSG transaction. For Mr. Steinberg, amount consists of hiring bonus.
(3) Stock Awards include grants of restricted shares and performance shares. Option Awards include SSAR grants. Amounts disclosed do not represent the economic value received by the Named Executive Officers. The value, if any, recognized upon the exercise of a SSAR will depend upon the market price of the shares on the date the SSAR is exercised. The value, if any, recognized for restricted and performance shares will depend upon the market price of the shares upon vesting. In accordance with SEC rules, the values for restricted and performance shares and SSARs are equal to the aggregate grant date fair value for each award computed in accordance with FASB ASC Topic 718. The values for restricted and performance shares are based on the closing price on the grant date. The values for SSARs are based on the Black-Scholes option pricing model. A discussion of the assumptions used in determining these valuations is set forth in Note 14 of the Notes to Consolidated Financial Statements of the Company s 2014 Annual Report. For Stock

Awards, the amounts shown represent grants of restricted shares to each Named Executive Officer as part of the executive s annual long-term equity grant and for Mr. Steinberg in 2013 includes grants of restricted shares as a long-term inducement award upon his hire.

(4) Amounts represent annual incentive payments received for 2014, 2013 and 2012 based on pre-set incentive goals established at the beginning of each fiscal year and tied to the Company s financial, strategic, and operational goals.

(5) All other compensation includes the following compensation, calculated based on the aggregate incremental cost to the Company of the benefits noted:

All Other Compensation for Fiscal Year 2014

Name	401(k) Company Match ($)	Executive Life Insurance ($)	Relocation ($)(a)	Severance ($)	Gross-ups ($)	All Other ($)(b)	Total ($)
J. Dennedy	12,376	1,651	16,800			1,933	32,760
J. Seebeck	10,682	430				393	11,505
R. Ellis	8,655	574				71	9,299
K. Badger	10,307	937				847	12,091
T. Ross	9,923	2,066				687	12,676
L. Steinberg	9,101	985				882	10,969

(a) Mr. Dennedy is reimbursed for temporary housing near the Company s corporate offices.

(b) Consists of executive long-term disability coverage.

Grants of Plan-Based Awards

The following table and related notes summarize grants of equity and non-equity incentive compensation awards to our Named Executive Officers for fiscal year 2014. All equity awards were made under the Company s 2011 Stock Incentive Plan.

Grants of Plan-Based Awards for Fiscal Year 2014

		Estimated Future Payouts Under Non-Equity Incentive Plan Awards ($)(1)			Estimated Future Payouts Under Equity Incentive Plan Awards ($)			All Other Stock Awards: Number of Shares of Stock	All Other Option Awards: Number of Securities Underlying Options	Exercise or Base Price of Option Awards	Grant Date Fair Value of Stock and Option Awards
Name	Grant Date	Threshold ($)	Target ($)	Maximum ($)	Threshold (#)	Target (#)	Maximum (#)	(#)(2)	(#)(3)	($/share)	($)(4)
James H. Dennedy	6/4/2013	315,000	350,000	525,000							
	6/4/2013							32,310			12.38
	6/4/2013								50,188	12.38	7.97
Janine K. Seebeck	6/4/2013	108,000	120,000	180,000							
	6/4/2013							3,231			12.38
	6/4/2013								5,019	12.38	7.97
	8/7/2013							1,754			11.40
	8/7/2013								2,715	11.40	7.37
Robert R. Ellis	6/4/2013	209,250	232,500	348,750							
	6/4/2013							12,520			12.38
	6/4/2013								19,448	12.38	7.97
Kyle C. Badger	6/4/2013	123,500	130,000	162,500							
	6/4/2013							7,270			12.38
	6/4/2013								11,292	12.38	7.97
Tony Ross	4/1/2013	156,750	165,000	206,250							
	6/4/2013							4,806			12.38
Larry Steinberg	6/4/2013	142,500	150,000	187,500							
	6/4/2013							12,116			12.38
	6/4/2013								18,821	12.38	7.97

(1) Amounts shown in the columns under Estimated Future Payouts Under Non-Equity Incentive Plan Awards represent fiscal year 2014 annual threshold, target, and maximum cash-based annual incentives granted under the annual incentive plan. Total threshold, target, and maximum payouts were conditioned on achievement of weighted goals based on revenue and adjusted operating income and achievement of individual MBOs as applicable for each Named Executive Officer. Fiscal year 2014 payouts for each Named Executive Officer pursuant to these awards are shown in the Summary Compensation Table above in the column titled Non-Equity Incentive Plan Compensation. Further explanation of potential and actual payouts by component is set forth in the Compensation Discussion and Analysis Annual Incentives.

(2) The share amounts shown represent grants of restricted shares to each Named Executive Officer as part of the executive s annual long-term equity grant and for Mr. Steinberg includes grants of restricted shares as a long-term inducement award upon his hire.

(3) The share amounts represent SSARs granted at the fair market value of the shares on the grant date as fiscal year 2014 long-term incentive awards. The SSARs are exercisable in thirds beginning on March 31, 2014. All SSARs have a seven-year term.

(4) The dollar amount shown for each equity grant represents the grant date fair value of the SSARs and restricted shares, calculated in accordance with FASB ASC Topic 718. The actual value, if any, recognized upon the exercise of a SSAR or vesting of restricted shares will depend upon the market price of the shares on the date the SSAR is exercised or restricted shares vest.

Outstanding Equity Awards

The following table and related notes summarize the outstanding equity awards held by the Named Executive Officers as of March 31, 2014.

Outstanding Equity Awards at 2014 Fiscal Year-End

		Option Awards				Stock Awards	
		Number of Securities Underlying Unexercised Options (#)					
Name (1)	Grant Date	Exercisable	Unexercisable (2)	Option Exercise Price ($)	Option Date Expiration	Number of Shares of Stock That Have Not Vested (#)(3)	Market Value of Shares of Stock That Have Not Vested ($)(4)
James H. Dennedy	6/12/2012	52,233	26,117 (a)	7.46	6/12/2019	21,540 (a)	288,636
	6/4/2013	16,729	33,459 (a)	12.38	6/4/2020	16,980 (a)	227,532
Janine K. Seebeck	11/7/2011	5,152		8.31	11/7/2018		
	6/12/2012	3,814	1,907 (b)	7.49	6/12/2019	1,240 (b)	16,616
	6/4/2013	1,673	3,346 (b)	12.38	6/4/2020	2,154 (b)	28,864
	8/7/2013	905	1,810 (b)	11.40	8/7/2020	1,170 (b)	15,678
Robert R. Ellis							
Kyle C. Badger	10/31/2011	11,194		8.49	10/31/2018		
	6/12/2012	8,590	4,296 (c)	7.46	6/12/2019	2,793 (c)	37,426
	6/4/2013	3,764	7,528 (c)	12.38	6/4/2020	4,847 (c)	64,950
Tony Ross	6/12/2012	13,333	6,667 (d)	7.46	6/12/2019		
	6/4/2013					3,204 (d)	42,934
Larry Steinberg	5/9/2012	11,675	5,838 (e)	8.64	5/9/2019	45,811 (e)	613,867
	6/4/2013	6,273	12,548 (e)	12.38	6/4/2020	8,078 (e)	108,245

(1) For Mr. Ellis, all unvested SSARs were forfeited upon separation, and unexercised SSARs expired 90 days after separation.
(2) As of March 31, 2014, the vesting schedule for the time-vested SSARs was as follows:
- (a) 42,846 on March 31, 2015 and 16,730 on March 31, 2016
- (b) 4,485 on March 31, 2015, and 2,578 on March 31, 2016
- (c) 8,060 on March 31, 2015, and 3,764 on March 31, 2016
- (d) 6,667 on March 31, 2015
- (e) 12,112 on March 31, 2015, and 6,274 on March 31, 2016

(3) As of March 31, 2014, the vesting schedule for the time-vested stock awards was as follows:
- (a) 27,750 on March 31, 2015, and 10,770 on March 31, 2016
- (b) 2,902 on March 31, 2015, and 831 on March 31, 2016
- (c) 5,216 on March 31, 2015, and 2,424 on March 31, 2016
- (d) 1,602 on March 31, 2015, and 1,602 on March 31, 2016

(e) 14,395 on March 31, 2015; 887 on May 9, 2015; 4,039 on March 31, 2016; and 17,728 upon the successful development and sale of our next generation property management system

(4) Calculated based on the closing price of the shares on March 31, 2014 of $13.40 per share.

Option Exercises and Stock Vested

The following table and related notes summarize the exercise of stock options and/or SSARs and the vesting of other stock awards by the Named Executive Officers during fiscal year 2014.

Option Exercises and Stock Vested for Fiscal Year 2014

	Option Awards		Stock Awards	
Name	**Number of Shares Acquired on Exercise (#)**	**Value Realized on Exercise ($)**	**Number of Shares Acquired on Vesting (#)(1)**	**Value Realized on Vesting ($)(2)**
James H. Dennedy			27,749	371,837
Janine K. Seebeck			4,651	62,323
Robert R. Ellis	16,576	71,128		
Kyle C. Badger			8,772	117,545
Tony Ross			1,602	21,467
Larry Steinberg			14,394	192,880

(1) Includes partial vesting of time-vested restricted shares granted in 2012 and 2013.

(2) The value realized on vesting of stock awards is determined by multiplying the number of shares underlying the stock awards by the closing price of the shares on the vesting date of the awards.

Termination and Change of Control

The following table and discussion summarize certain information related to the total potential payments which would have been made to the Named Executive Officers in the event of termination of their employment with the Company, including in the event of a change of control, effective March 31, 2014, the last business day of fiscal year 2014. Mr. Ellis is omitted from the table because his employment with us ended prior to the end of the fiscal year. Mr. Ellis is not entitled to any compensation from us in the event of a change of control.

Employment Agreements. The Named Executive Officers other than Mr. Ross are each a party to an employment agreement with the Company. Mr. Ellis employment agreement terminated in September 2013. Under the employment agreements, if we terminate any of these remaining Named Executive Officers employment without cause, he or she will receive his base salary and applicable health benefits for 12 months and his or her target annual incentive following termination. If the Company changes his or her position such that his or her compensation or responsibilities are substantially lessened, he or she may terminate his or her employment within 30 days of the change in position and will receive his or her severance benefits. If he or she is terminated for cause or voluntarily terminates his or her employment for any reason other than a change in position, he or she is prohibited for a one-year period following termination (the Noncompetition Period) from being employed by, owning, operating, controlling, or being connected with any business that competes with the Company. If any of these executives other than Mr. Ross is terminated without cause or terminates his or her employment due to change in position, we may, in our sole discretion, elect to pay his or her severance benefits for all or any part of the Noncompetition Period, which payments are in lieu of the severance payments and benefits coverage described above and, so long as we make such payments, he or she will be bound by the non-competition provisions described above. Each executive s agreement also contains an indefinite non-disclosure provision for the protection of the Company s confidential information and one-year non-solicitation and non-compete provisions.

Following the end of the fiscal year, the Company entered into new employment agreements with each of Messrs. Dennedy, Badger and Steinberg and Ms. Seebeck. The new employment agreements update the definition of the Company s business for purposes of the non-compete provisions, provide that such non-compete provisions are applicable regardless of the reason for termination of employment, and provide the Company with

an opportunity to cure any condition that results in change of position for the executive. Additionally, under the new employment agreements, upon termination without cause, the Company must pay severance equal to one year s salary and target annual incentive, and a lump sum amount equal to the executive s total premium for one year of COBRA continuation coverage under the Company s health benefit; and in the event that any of these Named Executive Officers are terminated without cause or for a change of position in the 24 months following a change of control of the Company, the Named Executive Officer is entitled to severance pay equal to two year s salary and target annual incentive and a lump sum amount equal to the executive s total premium for one year of COBRA continuation coverage under the Company s health benefit. These enhanced severance benefits in the event of termination following a change of control are not reflected in the following table because such agreements were not in effect at the end of the fiscal year.

Severance Policy. Mr. Ross is subject to the Company s U.S. Severance Pay Policy. Under the policy, Mr. Ross is eligible to receive severance pay based on position and full years of service, and in exchange for signing a release of claims, in the event that his employment is terminated by the Company for a reason other than for cause. As a vice president, on March 31, 2014, Mr. Ross was eligible for severance pay equal to 41 weeks of his base salary and applicable health benefits for the same period. Mr. Ross is also eligible under the policy to receive up to three months of outplacement assistance. None of the other Named Executive Officers are eligible for severance under the policy.

Termination and Change of Control

Voluntary Termination or Termination for Cause ($)(1)	**James Dennedy**	**Janine Seebeck**	**Kyle Badger**	**Tony Ross**	**Larry Steinberg**
Base Salary and Incentive					
Accelerated Vesting					
Termination without Cause or by Employee for Change in Position ($)(1)					
Base Salary and Incentive	750,000	360,000	390,000	137,981	400,000
Health Insurance (2)	13,139		13,236	13,052	13,236
Accelerated Vesting					
Total	763,139	360,000	403,236		413,236
Change of Control ($)(3)					
Base Salary and Incentive					
Health Insurance					
Accelerated Vesting/SSARs (3)	189,263	18,361	33,197	39,602	40,588
Accelerated Vesting/Stock (3)	516,168	61,158	90,871	42,934	722,113
Total	705,431	75,519	124,068	82,536	762,701
Death or Disability ($)(4)					
Accelerated Vesting/SSARs (3)	189,263	18,361	33,197	39,602	40,588
Accelerated Vesting/Stock (3)	516,168	61,158	90,871	42,934	722,113
Total	705,431	75,519	124,068	82,536	762,701

(1) For the Named Executive Officers other than Mr. Ross, cause is defined as (i) breach of employment agreement or any other duty to the Company, (ii) dishonesty, fraud, or failure to abide by the published ethical standards, conflicts of interest, or material breach of Company policy, (iii) conviction of a felony crime or crime involving misappropriation of money or other Company property, (iv) misconduct, malfeasance, or insubordination, or (v) gross failure to perform (not including failure to achieve quantitative targets). Mr. Dennedy has 30 days to cure a breach of his employment agreement, any duty to the Company, or a material breach of Company policy. A change in position is the substantial lessening of compensation or responsibilities. After a change in position, the executive has 30 days to notify the Company of his or her

termination of employment. A voluntary termination includes death, disability, or legal incompetence. For Mr. Ross, cause is as determined by the Company, and he is not eligible for severance based on a change in position.

(2) Health Insurance consists of health care and dental care benefits. The amount reflects 12 months of benefits for the Named Executive Officers that participate in the Company s plans. These benefits have been calculated based on actual cost to us for fiscal year 2014.

(3) SSARs and restricted shares vest upon a change of control. For SSARs (except as qualified below) the value of accelerated vesting is calculated using the closing price of $13.40 per share on March 31, 2014 less the exercise price per share for the total number of SSARs accelerated. The potential payment from the accelerated SSARs includes only the proceeds from the exercise of SSARs with an exercise price less than $13.40 since there would be no proceeds upon the exercise of underwater SSARs. The value of restricted shares upon vesting reflects that same $13.40 closing price. Values represent potential vesting under a hypothetical change of control situation on March 31, 2014.

(4) All SSARs and restricted shares vest upon death or disability.

EQUITY COMPENSATION PLAN INFORMATION

The following table provides certain information with respect to all of the Company s equity compensation plans in effect as of March 31, 2014.

	Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans
Equity compensation plans approved by shareholders (2000 Stock Option Plan for Outside Directors and 2000, 2006, and 2011 Stock Incentive Plans)	944,335	13.17	2,047,205
Equity compensation plans not approved by shareholders			
Total			

PROPOSAL 2

ADVISORY VOTE REGARDING EXECUTIVE COMPENSATION

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act) and SEC rules require us to allow our shareholders to vote, on a non-binding, advisory basis, on whether to approve the compensation of our Named Executive Officers as disclosed in this Proxy Statement, in accordance with the SEC s compensation disclosure rules. As described more fully in our CD&A section of this Proxy Statement, our compensation programs applicable to our Named Executive Officers are designed to retain executives who can significantly contribute to our success, reward the achievement of specific annual and long-term goals and strategic objectives, and tie a significant portion of compensation to the long-term performance of our shares to align executive pay and shareholders interests. The Compensation Committee continually reviews the compensation programs for our Named Executive Officers to ensure the alignment of our executive compensation structure with our shareholders interests and market practices. As a result of this review, the Compensation Committee:

- Established minimal base salary increases for fiscal year 2014;
- Focused annual incentives on significant improvements over fiscal year 2013 results; and
- Structured long-term incentives to reward increases in shareholder value.

We are asking shareholders to approve our Named Executive Officers compensation as described in this Proxy Statement. Currently, we ask shareholders to vote on such compensation annually. This vote is not intended to address any specific item of compensation, but rather the overall compensation, and the philosophy, objectives, and structure applicable to such compensation. This advisory vote is not binding on the Company, the

Compensation Committee, or our board of directors; however, we value the opinions of our shareholders and to the extent there is any significant vote against this proposal, we will consider our shareholders concerns and evaluate whether any actions are necessary to address those concerns. Accordingly, we are asking our shareholders to vote FOR the following resolution at the Annual Meeting:

RESOLVED, that the Company s shareholders approve, on an advisory basis, the compensation of the Named Executive Officers, as disclosed in the Company s Proxy Statement for the 2014 Annual Meeting of Shareholders pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including the Compensation Discussion and Analysis and the discussion under Executive Compensation, including the 2014 compensation tables and the related disclosure and narratives to those tables.

THE BOARD RECOMMENDS THAT SHAREHOLDERS VOTE FOR PROPOSAL 2. PROXY CARDS RECEIVED BY THE COMPANY WILL BE VOTED FOR PROPOSAL 2 UNLESS THE SHAREHOLDER SPECIFIES OTHERWISE ON THE PROXY CARD.

AUDIT COMMITTEE REPORT

The Audit Committee oversees the Company s financial reporting process on behalf of the board of directors. The Audit Committee s activities are governed by a written charter adopted by the board of directors, the Amended and Restated Audit Committee Charter, which is available at the Company s website *www.agilysys.com*. The Audit Committee currently consists of three directors, all of whom are independent in accordance with the rules of the NASDAQ Stock Market, Section 10A(m) of the Securities Exchange Act of 1934, and the rules and regulations of the SEC. The board has determined that Directors John Mutch and Peter Sinisgalli each qualify as an audit committee financial expert as defined by the SEC.

Management has the primary responsibility for the Company s financial statements and the reporting process, including the system of internal controls over financial reporting. PricewaterhouseCoopers LLP (PwC), the Company s independent registered public accounting firm, audits the annual financial statements prepared by management and expresses an opinion on whether those financial statements conform with United States generally accepted accounting principles, and also audits the internal controls over financial reporting and management s assessment of those controls. The Audit Committee hires the Company s independent registered public accounting firm and monitors these processes.

In carrying out its responsibilities, the Audit Committee has reviewed and has discussed with the Company s management the Company s 2014 audited financial statements. Management represented to the Audit Committee that the Company s financial statements were prepared in accordance with United States generally accepted accounting principles. In addition, the Audit Committee discussed with the Company s financial management and independent registered public accounting firm the overall scope and plans for the audit. The Audit Committee also met with the independent registered public accounting firm, with and without management present, to discuss the results of the audit, their evaluation of the Company s internal controls over financial reporting, including both the design and usefulness of such internal controls, and the overall quality of the Company s financial reporting.

The Audit Committee has discussed with the independent registered public accounting firm the matters required to be discussed by Statement on Auditing Standards No. 114, The Auditor s Communication With Those Charged With Governance.

The Audit Committee has also received annual written disclosures from PwC regarding their independence from the Company and its management as required by the applicable requirements of the Public Company Accounting Oversight Board regarding the independent accountant s communications with the Audit Committee concerning independence, has discussed with the independent registered public accounting firm their independence, and has considered the compatibility of non-audit services with the registered public accounting firm s independence.

Based on the review and discussions referred to above, the Audit Committee recommended to the board of directors that the Company s 2014 audited financial statements be included in the Company s 2014 Annual Report and Form 10-K for the fiscal year ended March 31, 2014.

Submitted by the Audit Committee of the Board of Directors as of June 3, 2014

Jerry Jones, Chairman

John Mutch

Peter Sinisgalli

PROPOSAL 3

RATIFICATION OF APPOINTMENT OF

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

By NASDAQ and SEC rules, appointment of the Company s independent registered public accounting firm (Independent Accountant) is the direct responsibility of the Audit Committee, and the Audit Committee has appointed PwC as our Independent Accountant for the fiscal year ending March 31, 2015.

Shareholder ratification of the selection of PwC as our Independent Accountant is not required by our Amended Code of Regulations or otherwise; however, the board of directors has determined to seek shareholder ratification of that selection to provide shareholders an avenue to express their views on this important matter. If our shareholders fail to ratify the selection, the Audit Committee will seek to understand the reasons for the vote against ratification and will take those views into account in this and future appointments. Even if the selection is ratified, the Audit Committee in its discretion may direct the appointment of a different Independent Accountant at any time during the year if it is determined that such a change would be in the best interests of the Company and our shareholders. Representatives of PwC are expected to be present at the Annual Meeting, have the opportunity to make a statement if they desire to do so and be available to respond to appropriate questions.

THE BOARD RECOMMENDS THAT SHAREHOLDERS VOTE FOR THE RATIFICATON OF PWC AS OUR INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM. PROXY CARDS RECEIVED BY THE COMPANY WILL BE VOTED FOR PROPOSAL 3 UNLESS THE SHAREHOLDER SPECIFIES OTHERWISE ON THE PROXY CARD.

The Audit Committee reviewed the fees of PwC, our Independent Accountant for fiscal years 2014 and 2013. Fees for services rendered by PwC for fiscal years 2014 and 2013 were:

Fiscal Year	Audit Fees ($)	Audit-Related Fees ($)	Tax Fees ($)	All Other Fees ($)
2014	528,180		41,000	60,000
2013	633,400	103,000		

Audit Fees consist of fees billed for professional services provided for the annual audit of our financial statements, annual audit of internal control over financial reporting, review of the interim financial statements included in quarterly reports, and services that are normally provided in connection with statutory and regulatory filings. Audit-Related Fees generally include fees for employee benefits plan audits, business acquisitions, and accounting consultations. Tax Fees include tax compliance and tax advice services. All Other Fees generally relate to services provided in connection with non-audit acquisition activities.

The Audit Committee adopted an Audit and Non-Audit Services Pre-Approval Policy (the Policy) to ensure compliance with SEC and other rules and regulations relating to auditor independence, with the goal of safeguarding the continued independence of our Independent Accountant. The Policy sets forth the procedures and conditions pursuant to which audit, review, and attest services and non-audit services to be provided to the Company by the our Independent Accountant may be pre-approved. The Audit Committee is required to pre-approve the audit and non-audit services performed by our Independent Accountant to assure that the provision

of such services does not impair independence. Unless a type of service to be provided has received pre-approval as set forth in the Policy, it will require separate pre-approval by the Audit Committee before commencement of the engagement. Any proposed service that has received pre-approval but which will exceed pre-approved cost limits will require separate pre-approval by the Audit Committee. All audit, non-audit, and tax services were pre-approved by the Audit Committee during fiscal years 2014 and 2013.

RELATED PERSON TRANSACTIONS

All related person transactions with the Company require the prior approval or ratification by our Audit Committee. The board of directors adopted Related Person Transaction Procedures to formalize the procedures by which our Audit Committee reviews and approves or ratifies related person transactions. The procedures set forth the scope of transactions covered, the process for reporting such transactions, and the review process. Covered transactions include any transaction, arrangement, or relationship with the Company in which any director, executive officer, or other related person has a direct or indirect material interest, except for business travel and expense payments, share ownership, and executive compensation approved by the board of directors. Transactions are reportable to the Company s General Counsel, who will oversee the initial review of the reported transaction and notify the Audit Committee of transactions within the scope of the procedures, and the Audit Committee will determine whether to approve or ratify the transaction. Through our Nominating Committee, we make a formal yearly inquiry of all of our executive officers and directors for purposes of disclosure of related person transactions, and any such newly revealed related person transactions are conveyed to the Audit Committee. All officers and directors are charged with updating this information with our internal legal counsel.

OTHER MATTERS

The Board is not aware of any matter to come before the Annual Meeting of Shareholders other than those mentioned in the accompanying Notice. If other matters properly come before the Annual Meeting, the persons named in the accompanying proxy card intend, to the extent permitted by law, to vote using their best judgment on such matters.

SHAREHOLDER PROPOSALS

Shareholders who, in accordance with SEC Rule 14a-8, wish to present proposals for inclusion in the proxy materials to be distributed in connection with the 2015 Annual Meeting of Shareholders must submit their proposals so that they are received by our Secretary at our at our Alpharetta office, located at 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005, no later than the close of business on April 22, 2015. Each proposal submitted should be accompanied by the name and address of the shareholder submitting the proposal and the number of common shares owned. If the proponent is not a shareholder of record, proof of beneficial ownership should also be submitted. All proposals must be a proper subject for action and comply with the proxy rules of the SEC.

In order for a shareholder to bring a matter properly before the 2015 Annual Meeting present (other than a matter brought pursuant to SEC Rule 14a-8), the shareholder must comply with the requirements set forth in our Regulations, including: (i) be a shareholder of record at the time notice of the matter is given and at the time of the meeting, (ii) be entitled to vote at the meeting, and (iii) have given timely written notice of the matter to the Secretary. A shareholder s notice of a matter the shareholder wishes to present at the 2015 Annual Meeting (other than a matter brought pursuant to SEC Rule 14a-8), must be received by our Secretary at our Alpharetta office, located at 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005, no earlier than April 22, 2015, and no later than May 22, 2015.

Any shareholder entitled to vote at the Annual Meeting on August 20, 2014 may make a request in writing and we will mail, at no charge, a copy of our 2014 Annual Report, including the financial statements

and schedules required to be filed with the SEC pursuant to Rule 13a-1 under the Exchange Act, for the most recent fiscal year. Written requests should be directed to Agilysys, Inc., Attn: Investor Relations, 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005.

Please sign and return your proxy card promptly, or vote via the Internet or telephone. For your convenience a return envelope is enclosed requiring no additional postage if mailed in the United States.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This Proxy Statement and other publicly available documents, including the documents incorporated herein and therein by reference, contain, and our officers and representatives may from time to time make, forward-looking statements within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements can be identified by words such as: anticipate, intend, plan, goal, seek, believe, project, estimate, expect, strategy, future, likely, may, should, will and similar references to statements are not guarantees of future performance and involve risks, uncertainties, and assumptions that are difficult to predict. These statements are based on management s current expectations, intentions, or beliefs and are subject to a number of factors, assumptions, and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. Factors that could cause or contribute to such differences or that might otherwise impact the business include the risk factors set forth in Item 1A of our Annual Report for the fiscal year ended March 31, 2014. We undertake no obligation to update any such factor or to publicly announce the results of any revisions to any forward-looking statements contained herein whether as a result of new information, future events, or otherwise.

Electronic Voting Instructions

Available 24 hours a day, 7 days a week!

Instead of mailing your proxy, you may choose one of the voting methods outlined below to vote your proxy.

VALIDATION DETAILS ARE LOCATED BELOW IN THE TITLE BAR.

Proxies submitted by the Internet or telephone must be received by 1:00 am Eastern Time on August 20th, 2014.

Vote by Internet

Go to **www.investorvote.com/AGYS**

Or scan the QR code with your smartphone

Follow the steps outlined on the secure website

Vote by telephone

Call toll free 1-800-652-VOTE (8683) within the USA, US territories & Canada on a touch tone telephone

Follow the instructions provided by the recorded message

Using a black ink pen, mark your votes with an X as shown in this example. Please do not write outside the designated areas. X

q **PLEASE FOLD ALONG THE PERFORATION, DETACH AND RETURN THE BOTTOM PORTION IN THE ENCLOSED ENVELOPE.** q

Proposals The Board of Directors recommends a vote FOR all the nominees listed in Proposal 1 and FOR Proposals 2 and 3.

A

If cumulative voting is in effect, the Proxy holders intend to cumulate votes for the election of all or any one or more of the Board of Directors nominees, James H. Dennedy, Jerry Jones, Michael A. Kaufman and John Mutch. THIS PROXY CARD GIVES THE PROXY HOLDERS FULL DISCRETIONARY AUTHORITY TO VOTE CUMULATIVELY AND TO ALLOCATE VOTES AMONG MESSRS. DENNEDY, JONES, KAUFMAN AND MUTCH, UNLESS AUTHORITY TO VOTE FOR ANY OF THEM IS WITHHELD, IN WHICH CASE NO VOTES REPRESENTED BY THIS PROXY CARD WILL BE CAST FOR ANY DIRECTOR FOR WHOM AUTHORITY TO VOTE IS SO WITHHELD.

1. ELECTION OF FOUR CLASS A MEMBERS OF THE BOARD OF DIRECTORS TO HOLD OFFICE FOR A TWO-YEAR TERM EXPIRING AT THE 2016 ANNUAL MEETING;

01 James H. Dennedy 02 Jerry Jones 03 Michael A. Kaufman 04 John Mutch

.. **Mark here to WITHHOLD vote from all nominees.**

.. **Mark here to vote FOR all nominees.**

.. **For All Nominees EXCEPT** - To withhold a vote for one or more nominees, mark the box to the left and the numbered box(es) to the right corresponding to the director(s) listed above.

01 02 03 04

.. ..

	For	**Against**	**Abstain**
2. Approval, on a non-binding advisory basis, the compensation of our named executive officers set forth in the attached Proxy Statement.	..	..	..
3. Ratification of the appointment of PricewaterhouseCoopers LLP as our independent registered public accounting firm for the fiscal year ending March 31, 2015.	..	..	..

4. In their discretion, the proxies are authorized to vote upon such other business as may properly come before the Annual Meeting or any adjournments thereof.

B **Non-Voting Items**

Change of Address Please print new address below.

C **Authorized Signatures This section must be completed for your vote to be counted. Date and Sign Below**

Please sign exactly as your name appears above. If signing as attorney, executor, administrator, trustee or guardian, please give full title as such; and if signing for a corporation, please give your title. When shares are in the names of more than one person, each must sign.

Date (mm/dd/yyyy) Please print date below. Signature 1 Please keep signature within the box. Signature 2 Please keep signature within the box.

/ /

q **PLEASE FOLD ALONG THE PERFORATION, DETACH AND RETURN THE BOTTOM PORTION IN THE ENCLOSED ENVELOPE.** q

Proxy Card Agilysys, Inc. Annual Meeting of Shareholders August 20, 2014

This proxy is solicited on behalf of the Board of Directors

The undersigned hereby appoints James H. Dennedy, Keith M. Kolerus and Kyle C. Badger, and each of them, as proxy holders and attorneys, with full power of substitution, to appear and vote all of the Common Shares of Agilysys, Inc. which the undersigned shall be entitled to vote at the Annual Meeting of Shareholders of Agilysys, to be held on Wednesday, August 20, 2014 at Agilysys offices at 1000 Windward Concourse, Suite 250, Alpharetta, Georgia 30005 at 8:30 a.m., local time, and at any adjournments thereof, hereby revoking any and all proxies heretofore given.

When properly executed, this proxy will be voted in the manner directed by the signed shareholder(s); if no direction is made, this proxy will be voted FOR all nominees in proposal 1 and FOR proposals 2 and 3.

PLEASE COMPLETE, DATE AND SIGN THIS PROXY CARD AND RETURN IT IN THE ENCLOSED POSTAGE-PAID ENVELOPE.

Important Notice Regarding Internet Availability of Proxy Materials for the Annual Meeting to be held on August 20, 2014: The Notice of Annual Meeting of Shareholders and Proxy Statement are available on our website at www.agilysys.com. 38,717 27,964

Selling and marketing	52,022	43,376	37,576
General and administrative	15,087	19,920	13,877
Amortization of intangible assets	132	130	186
Impairment of investment	1,554	-	-
Impairment of goodwill and intangible assets	-	57,110	-
Restructuring and other charges	2,787	3,573	12,040
Acquisition related expenses	-	-	2,622
Total operating costs and expenses	122,372	162,826	94,265
Operating loss	(9,587)	(90,486)	(32,807)
Other (loss) income			

	731	(7,000)	-
Financial income (expenses), net	1,668	(99)	(1,015)
Loss before tax	(7,188)	(97,585)	(33,822)
Taxes on income	-	894	-
Net income (loss)	$(7,188)	$(98,479)	$(33,822)

	Year Ended December 31,		
	2009	2010	2011
	(As a percentage of sales)		
Statement of Operations Data:			
Sales			
Products	88.9	87.7	86.2
Services	11.1	12.3	13.8
Total Sales	100.0	100.0	100.0
Cost of sales			
Products	46.3	49.5	50.1
Services	6.1	12.9	12.5
Write-off of excess inventory and provision for inventory purchase commitments	1.6	2.4	1.4
Inventory write-off related to bankruptcy of a customer	-	-	3.8
Gross margin	46.0	35.2	32.2
Operating costs and expenses:			
Research and development, gross	22.3	20.3	17.1
Less – grants and participations	1.6	1.5	2.3
Research and development, net	20.7	18.8	14.8
Selling and marketing	21.2	21.1	19.8
General and administrative	6.2	9.7	7.3
Amortization of intangible assets	0.1	0.1	0.1
Impairment of investment	0.6	-	-
Impairment of goodwill and intangible assets	-	27.7	-
Restructuring and other charges	1.1	1.7	6.3
Acquisition related expenses	-	-	1.4
Total operating expenses	49.9	79.1	49.7
Operating loss	(3.9)	(43.9)	(17.5)
Other (loss) income	0.3	(3.4)	-
Financial income (expenses), net	0.7	(0.1)	(0.5)
Loss before tax	(2.9)	(47.4)	(18.0)
Taxes on Income	-	0.4	-
Net (loss)	(2.9%)	(47.8%)	(18.0%)

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Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Sales. Sales in 2011 were approximately $190.0 million, a decrease of approximately 7.7% compared to sales of approximately $205.8 million in 2010. In 2011, BreezeMAX revenues totaled approximately $141.4 million or 74.4% of total revenue, compared to approximately $147.5 million or 71.9% of total revenue in 2010, a decrease of approximately 4.1% compared to the 2010 BreezeMAX revenues. The decrease of our total sales in 2011 resulted primarily due to the continuous unfavorable general economic conditions, which influenced some of our clients, and the intense competition which we faced, in particular by Chinese vendors. Our revenues in 2011 from non-WiMAX broadband wireless products were approximately $48.6 million, a decrease of approximately 16.4% compared to sales of approximately $58.2 million in 2010.

Sales in Europe, the Middle East and Africa reached approximately 42.5% of our sales in 2011 and totaled approximately $80.8 million, which represents a decrease of approximately 26.4% compared to our 2010 sales in these regions which were approximately $109.9 million or 53.4% of our sales. Sales in Central and Latin America accounted for 14.9% of our sales in 2011 compared to 13.1% of our sales in 2010. Sales in North America accounted for approximately 24.7% of our sales in 2011, compared to 23.1 % in 2010. Sales in Asia Pacific accounted for approximately 17.9% of our sales in 2011 compared to approximately 10.5% in 2010 in this region.

In 2010 and 2011, no customer accounted for more than 10% of our revenues. Because of the nature of our agreements and the associated large initial payments due, the identity of major customers generally varies from quarter to quarter and we do not believe that we are materially dependent on any one specific customer or any specific small number of customers.

Cost of sales. Cost of sales for products and services consists primarily of cost of components, product manufacturing and assembly, labor, overhead and other costs associated with production. Cost of sales was approximately $118.9 million in 2011, compared to cost of sales of approximately $128.6 million in 2010. Cost of sales as a percentage of sales are consistent between 2010 and 2011 at 62.5%.

Write-off of excess inventory and provision for inventory purchase commitments. We periodically assess our inventories valuation in accordance with obsolete and slow-moving items based on revenue forecasts and technological obsolescence. If inventories on-hand exceed our estimates or become obsolete, this would result in a charge to our statement of operations and a corresponding reduction in our inventory and shareholders' equity. Changes in demand for our products and in our estimates for demand create changes in provisions for obsolete inventory. As part of our ordinary course of business we evaluate, on a quarterly basis, our actual inventory needs versus our sales projections and write-off excess inventory and un-cancelable purchase commitments from our suppliers and subcontractors. As a result, we record charges related to the write-off of excess inventory and accrued a provision for inventory purchase commitments of new materials and components that we had purchased or committed to purchase in anticipation of forecasted sales that we did not consummate. Primarily as a result of the decrease of our sales, our write-off of excess inventory and our accrual of a provision for inventory purchase commitments decreased and amounted in the aggregate to approximately $2.6 million for the year ended December 31, 2011 compared to approximately $4.9 million for the year ended December 31, 2010.

Inventory utilization. We perform periodically an inventory evaluation model in order to align our inventory levels to the market conditions and anticipated customer demand. In each of 2011 and 2010, approximately $0.4 million of inventory previously written-off consistent with our inventory evaluation model was used as components in our regular production course and was sold as finished goods to end users. The sales of these related manufactured products were reflected in our revenues without increasing the cost of sales in the period the inventory was utilized. This inventory utilization increased our gross margin by 0.2% in 2011 and by 0.2% in 2010.

If the demand for our products suddenly and significantly decreased, or if there were a higher incidence of inventory obsolescence because of rapidly changing technology, standardization and customer requirements, we could be required to increase our write-off of excess inventory, and our gross margin could be adversely affected. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times compared to the risk of inventory obsolescence. However, if the demand for our products increases beyond our expectations following write-down of inventory, we may further utilize our written down inventory. Such utilization may contribute to our gross margin in future periods. We cannot predict the likelihood of utilizing previously written-off inventory in future operations.

Research and development expenses, net. Gross research and development expenses consist primarily of employee salaries, development-related raw materials and subcontractors, and other related costs partially offset by research and development funding. Gross research and development expenses were approximately $32.4 million in 2011, a decrease of approximately 22.3% compared to gross research and development expenses of approximately $41.7 million in 2010. This decrease was primarily attributable to the restructuring plans that the Company implemented during 2011 and 2010. Gross research and development, as a percentage of sales was 17% in 2011, compared to 20.3% in 2010. Grants and other participations for funding approved research and development projects totaled approximately $4.4 million in 2011 and $3.0 million in 2010. Research and development expenses, net, were approximately $28.0 million in 2011, compared to approximately $38.7 million in 2010.

Selling and marketing expenses. Selling and marketing expenses consist primarily of costs relating to compensation attributable to employees engaged in selling and marketing activities, promotion, advertising, trade shows and exhibitions, travel and related expenses. Selling and marketing expenses were approximately $37.6 million in 2011, a decrease of approximately 13.4% compared to selling and marketing expenses of approximately $43.4 million in 2010. This decrease was primarily attributable to the restructuring plan that the company implemented during 2011 and 2010. Selling and marketing expenses as a percentage of sales were 19.8% in 2011 compare to 21.1% in 2010.

General and administrative expenses. General and administrative expenses consist primarily of compensation costs for administration, finance and general management personnel, office maintenance, insurance costs, professional fees and other administrative costs. General and administrative expenses were approximately $13.9 million in 2011, a decrease of approximately 30.3% compared to general and administrative expenses of approximately $19.9 million in 2010. This decrease is related primarily to the $3.6 million that the Company recorded in 2010 for doubtful accounts and for the restructuring plan that the Company implemented during 2011 and 2010. General and administrative expenses as a percentage of sales decreased to 7.3% in 2011 from 9.7% in 2010.

Amortization of intangibles assets. As a result of our merger and acquisition activity of Wavion Inc. during November 2011, we had annual amortization charges of approximately $0.2 million recorded in 2011 compared to $0.1 million in 2010 related to the prior year's acquisition.

Impairment of investment. During 2011 and 2010 the Company did not book any impairment of investment.

Impairment of goodwill. During 2011 the Company did not book any impairment of goodwill compared to 2010, when the Company incurred impairment of goodwill in amount of $57.1 million. For further information regarding these charges, see Item 5.– "A Critical Accounting Principles —Goodwill".

Restructuring costs. During 2011 and 2010, we implemented separate restructuring plans including the layoff of approximately 194 employees in 2011 and approximately 160 employees in 2010 as well as the vacating of certain leased premises. As a result, we recorded a restructuring charge of approximately $12.0 million in 2011 and approximately $3.6 million in 2010, which primarily consists of employees' termination benefits, lease abandonment and repayment of grants.

Financial expenses, net. Financial expenses, net, were $1.0 million in 2011, compared to financial expenses, net, of approximately $0.1 million in 2010. The increase in financial expenses is attributed mainly to the inflation in the currency change between the Dollar and other currencies and interest on the Long Term Loan that the Company took from Silicon Valley Bank (SVB).

Other loss. During 2011 the Company did not book other loss compared to 2010, when the Company incurred impairment of short term investment in an amount of $7.0 million, resulting from purchasing from one of our customers subordinated convertible promissory notes (See note 6 to our consolidated financial statements).

Net loss. In 2011, net loss was approximately $(33.8) million, compared to a net loss of approximately $(98.5) million in 2010.

Year Ended December 31, 2010 Compared to Year Ended December 31, 2009

Sales. Sales in 2010 were approximately $205.8 million, a decrease of approximately 16.1% compared to sales of approximately $245.2 million in 2009. In 2010, BreezeMAX revenues totaled approximately $147.5 million or 71.9% of total revenue, compared to approximately $179.0 million or 73.0% of total revenue in 2009, a decrease of approximately 17.6% compared to the 2009 BreezeMAX revenues. The decrease of our total sales in 2010 resulted primarily due to the postponement of some WiMAX projects as a result of the unfavorable general economic conditions, which influenced some of our clients, and delays in allocating spectrum in several countries as well as the intense competition which we faced, in particular by Chinese vendors. Our revenues in 2010 from non-WiMAX broadband wireless products decreased approximately 12.7% compared to the previous year.

Sales in Europe, the Middle East and Africa reached approximately 53.4% of our sales in 2010 and totaled approximately $109.9 million, which represents a decrease of approximately 26.2% compared to our 2009 sales in this region which were approximately $148.7.million or 60.7% of our sales. Sales in Central and Latin America accounted for 13.1% of our sales in 2010 compared to 18.5% of our sales in 2009. Sales in North America accounted for approximately 23.1% of our sales in 2010, compared to 9.5 % in 2009. The main reason for the increase in our sales in North America was due a deployment to a large customer which we performed in 2010. Sales in Asia Pacific accounted for approximately 10.5% of our sales in 2010 compared to approximately 11.4% in 2009 in this region.

In 2010, no customer accounted for more than 10% of our revenues, compared to 2009, when one customer accounted for more than 15% of revenues.

Cost of sales. Cost of sales was approximately $128.6 million in 2010, compared to cost of sales of approximately $128.5 million in 2009. Cost of sales as a percentage of sales increased to approximately 62.5% in 2010 from approximately 52.4% in 2009. This increase is primarily attributable to the change in the mix of the products that comprised our revenues in 2010. As the market continues to move towards standardization and more players enter into this market making it more competitive for us, and as we shift the mix of products that comprise our revenues, such as an increase in the volume of lower-margin third party products and turnkey projects, our cost of sales as a percentage of sales increased.

Write-off of excess inventory and provision for inventory purchase commitments. Primarily as a result of the decrease of our sales, our write-off of excess inventory and our accrual of a provision for inventory purchase commitments increased and amounted in the aggregate to approximately $4.9 million for the year ended December 31, 2010 compared to approximately $4.0 million for the year ended December 31, 2009.

Inventory utilization. In 2010 and 2009, approximately $0.4 million and $0.6 million, respectively, of inventory previously written-off consistent with our inventory evaluation model was used as components in our regular production course and was sold as finished goods to end users. The sales of these related manufactured products were reflected in our revenues without increasing the cost of sales in the period the inventory was utilized. This inventory utilization increased our gross margin by 0.2% in 2010 and by 0.2% in 2009.

Research and development expenses, net. Gross research and development expenses were approximately $41.7 million in 2010, a decrease of approximately 23.8% compared to gross research and development expenses of approximately $54.7 million in 2009. This decrease is primarily attributable to the restructuring plans that the Company implemented during 2010 and 2009. Gross research and development, as a percentage of sales was 20.3% in 2010, compared to 22.3% in 2009. Grants and other participations for funding approved research and development projects totaled approximately $3.0 million in 2010 and $3.9 million in 2009. Research and development expenses, net, were approximately $38.7 million in 2010, compared to approximately $50.8 million in 2009.

Selling and marketing expenses. Selling and marketing expenses were approximately $43.4 million in 2010, a decrease of approximately 17% compared to selling and marketing expenses of approximately $52.0 million in 2009. This decrease is primarily attributable to the cost reduction plan that the Company implemented during 2010. Selling and marketing expenses as a percentage of sales was 21.1% in 2010 compare to 21.2% in 2009.

General and administrative expenses. General and administrative expenses were approximately $19.9 million in 2010, an increase of approximately 32% compared to general and administrative expenses of approximately $15.1 million in 2009. This increase is related primarily to the $3.6 million addition to the company’s provision for doubtful accounts. General and administrative expenses as a percentage of sales increased to 9.7% in 2010 from 6.2% in 2009.

Amortization of intangibles assets. As a result of our merger and acquisition activity in prior years, we had annual amortization charges of approximately $0.1 million recorded in each of 2010 and 2009.

Impairment of investment. During 2010 the Company did not book any impairment of investment compared to $1.6 million in 2009.

Impairment of goodwill. During 2010, the Company incurred impairment of goodwill in amount of $57.1 million. For further information regarding these charges, see Item 5.– “A Critical Accounting Principles —Goodwill”.

Restructuring costs. During 2010 and 2009, we implemented separate restructuring plans including the layoff of approximately 160 employees in 2010 and approximately 90 employees in 2009 as well as the vacating of certain leased premises.

As a result, we recorded a restructuring charge of approximately $3.6 million in 2010 and approximately $2.8 million in 2009, which primarily consists of employees' termination benefits, lease abandonment and repayment of grants.

Financial income, net. Financial expense, net, was $0.1 million in 2010, a decrease of approximately 105.9% compared to financial income, net, of approximately $1.7 million in 2009. The decrease in financial income is attributed mainly to decreased yields on investments compared to the previous year due to the decrease in our investment balances and the global interest rates.

Other loss. During 2010, the Company incurred impairment of short term investment in an amount of $7.0 million, resulting from purchasing from one of our customers subordinated convertible promissory notes (See note 6 to our consolidated financial statements), compared to a net income in 2009 of $0.7 million, which was received as additional proceeds in connection with the LGC transaction (under which we sold our CMU to LGC Wireless, Inc. during November 2006).

Net loss. In 2010, net loss was approximately $(98.5) million, compared to a net loss of approximately $(7.2) million in 2009.

Impact of Inflation and Currency Fluctuations –

A devaluation of the U.S. dollar against the NIS has a direct influence on the U.S. dollar cost of our operations. The majority of our sales, and part of our expenses, are denominated in dollars. However, a significant portion of our expenses, primarily labor expenses, is denominated in NIS unlinked to the U.S. dollar. Inflation in Israel and/or the devaluation of the dollar in relation to the NIS has the effect of increasing the cost in dollars of these expenses and has a negative effect on our profitability.

Because exchange rates between the NIS and the U.S. dollar fluctuate continuously, exchange rate fluctuations as recently experienced in Israel and especially larger periodic devaluations or revaluations, will have an impact on our profitability and period-to-period comparisons of our results of operations. The effects of foreign currency re-measurements are reported in our consolidated financial statements in the statement of operations.

To protect against exchange rate fluctuations, we have instituted several foreign currency hedging programs. These hedging activities consist of cash flow hedges of anticipated NIS payroll and forward exchange contracts to hedge certain trade payables in NIS. In 2011, the majority of the cash flow hedges were effective. For more information, see "Item 11—Qualitative and Qualitative Disclosures About Market Risk".

The following table presents information about the rate of inflation in Israel, the rate of devaluation or appreciation of the NIS against the U.S. dollar, and the rate of inflation of Israel adjusted for the devaluation:

Year ended December 31,	Israeli inflation rate %	Israeli devaluation (appreciation) rate %	Israeli inflation adjusted for devaluation (appreciation)%
2007	3.4	(9.0)	12.4
2008	3.8	(1.1)	4.9
2009	3.9	(0.7)	4.6
2010	2.7	(6.0)	8.7
2011	2.2	7.7	(5.5)

We cannot assure you that we will not be materially and adversely affected in the future if the devaluation (appreciation) of the NIS against the U.S. dollar continues or, that in the event the dollar appreciates against the NIS, the inflation in Israel exceeds the devaluation of the NIS against the dollar or if the timing of the devaluation lags behind inflation in Israel.

For a discussion of certain policies or factors relating to our being an Israeli company and our location in Israel, see "Item 3—Key Information—Risk Factors—Risks Related to Our Location in Israel".

B.LIQUIDITY AND CAPITAL RESOURCES

The following sections discuss the effects of changes in our balance sheets, cash flows and commitments on our liquidity and capital resources.

Balance Sheet and Cash Flows

Total cash, cash equivalents, short-term and long-term marketable securities and deposits were $64.4 million as of December 31, 2011, a decrease of approximately $18.9 million or 22.7% from $83.3 million at December 31, 2010. Total cash, cash equivalents, short-term and long-term marketable securities and deposits as of December 31, 2010 reflected a decrease of approximately $35.2 million or 29.7% from $118.5 million at December 31, 2009.

Total cash and cash equivalents as of December 31, 2011 were $57.8 million, a decrease of $3.5 million or 5.8% from $61.3 million at December 31, 2010. Total cash and cash equivalents as of December 31, 2010 were $61.3 million, a decrease of $7.8 million or 11.3% from $69.1 million at December 31, 2009.

Our operating activities used cash of approximately $18.0 million, $22.4 million and $15.5 million in 2011, 2010 and 2009, respectively. The cash flows used in operating activities for 2011 consisted primarily of adjusted net loss (net loss as adjusted for non-cash activities, including stock-based compensation expenses, depreciation of fixed assets and amortization of intangibles assets) plus an increase in long term trade receivable and decrease in trade payables, offset by a decrease in inventories, a decrease in accounts receivable, a decrease in other accounts receivable and prepaid expenses and an increase in other accounts payable and accrued expenses. The cash flows used in operating activities for 2010 consisted primarily of adjusted net loss (net loss was adjusted for non-cash activities, including impairment of goodwill and short term investment, stock-based compensation expenses, depreciation of fixed assets) plus an increase in inventories, an increase in other accounts receivable and prepaid expenses and a decrease in other accounts payable and accrued expenses, offset by an increase in trade payables and a decrease in trade receivables. The cash flows used in operating activities for 2009 consisted primarily of net loss adjusted for non-cash activities, including stock-based compensation expenses, depreciation of fixed assets and impairment of investments in affiliates plus a decrease in other accounts receivable and prepaid expenses and a decrease in inventories, fully offset by an increase in trade receivables, a decrease in trade payables and a decrease in other accounts payable and accrued expenses.

Our cash used in investing activities was approximately $12.5 million in 2011. In 2010 and 2009 our investing activities provided cash of approximately $14.5 million and $20.5 million, respectively. In 2011, our investing activities consisted mainly of the acquisition of Wavion ($24.6 million), investments in bank deposits $4.9 million, and fixed assets. In 2011, our cash used in investing was mainly attributable to our investment in Wavion and investments in bank deposits and fixed assets, which were partially offset by proceeds from the maturity of marketable securities and proceeds from maturity of bank deposits. In 2010, our investing activities provided proceeds from the maturity of marketable securities and proceeds from the maturity of bank deposits, which were partially offset by investments in bank deposits, marketable securities and fixed assets and investment in convertible promissory notes of one of our customers. In 2009, our investing activities provided proceeds from the maturity of marketable securities, proceeds from maturity of bank deposits, as well as the remaining proceeds from the LGC transaction (under which we sold our cellular mobile unit to LGC Wireless, Inc. during November 2006) which were partially offset by investments in bank deposits, marketable securities and fixed assets.

Capital expenditures were approximately $3.3 million, $5.0 million and $7.2 million in 2011, 2010 and 2009, respectively. These expenditures principally financed the purchase of research and development equipment and manufacturing equipment.

Our financing activities provided cash of approximately $27 million in 2011, $0.1 million in 2010 and $0.4 million in 2009. In 2011, the amount attributable to receipt of the Long Term Loan that the Company received from SVB related to the purchase of Wavion during the year, offset by a repayment of a long term loan that was received by Wavion in the past. In 2010 and 2009, the amount of cash provided was attributable to proceeds from the issuance of shares in connection with the exercise of employees' options in the amount of approximately $0.1 million and $0.4 million, respectively.

We expect that cash provided or used by operations may fluctuate in future periods as a result of a number of factors, including fluctuations in our operating results, shipment timing, accounts receivable collections, inventory management, and the timing of other payments and investments.

Accounts Receivable, Net. Accounts receivable, net was $48.3 million and $49.9 million as of December 31, 2011 and 2010, respectively. The decrease in the accounts receivable balance in 2011 was mainly a result of the global economic slowdown, aggressive competition and the crunch in the global capital markets offset by increasing of the net accounts receivable due to the acquisition of Wavion Inc. DSOs as of December 31, 2011, 2010 and 2009 were 106 days, 89 days and 97 days, respectively. Our DSOs in 2011 ranged between 80 and 125 days and we expect that our DSOs will further increase to a range of between 90 to 120 days during 2012 as a result of our customers requesting more favorable payment terms from as a result of increased competition.

Inventories. Inventories were $36.2 million as of December 31, 2011 compared to $56.1 million as of December 31, 2010. This decrease of inventory was mainly due to the usage of our inventory for sales during 2011 and due to an inventory write-off related to the bankruptcy of a customer. Inventories consist of raw materials, work in process and finished goods and inventories at customer sites that are not yet recognized as revenues. Inventory management remains an area of focus as we balance the need to maintain strategic inventory levels to ensure competitive lead times against the risk of inventory obsolescence because of rapidly changing technology and customer requirements. We are focusing our operational efforts to increase inventory turns in order to enhance our responsiveness to future customers' needs and market changes. Our inventory turns were approximately 3.3 times in 2011 and approximately 2.3 times in 2010.

Credit Facility

Long Term Loan. For a discussion of our Long Term Loan, please see the Section entitled "Item 10 Additional Information – Material Contracts."

WORKING CAPITAL –

Our working capital was approximately $62.0 million as of December 31, 2011 compared to $110.0 million as of December 31, 2010 and $132.8 million as of December 31, 2009.

Commitments

Leases. We lease office space in several locations worldwide. Rent expense totaled $5.3 million, $6.4 million and $6.8 million in 2011, 2010 and 2009, respectively. We also lease certain computers under operating lease agreements which expire in 2014. Computer leasing expenses totaled $0.5 million, $0.5 million and $0.2 million in 2011, 2010 and 2009, respectively. We also lease various motor vehicles under operating lease agreements, which expire in 2014. Motor vehicles lease expenses were $3.6 million, $3.0 million and $1.9 million in 2011, 2010 and 2009, respectively. The vast majority of the motor vehicle leases expenses are charged back to our employees.

Future annual minimum lease payments under all non-cancelable operating leases as of December 31, 2011 were as follows (in thousands):

	Rental of premises	Lease of computers	Lease of motor vehicles
2012	$ 3,657	$ 143	$ 1,133
2013	1,463	43	638
2014	130	6	235
2015	28	-	-
	$ 5,278	$ 192	$ 2,006

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The following table of our material contractual obligations as of December 31, 2011 summarizes the aggregate effect that these obligations are expected to have on our cash flows in the periods indicated (in thousands)

Contractual Obligations	Payments due by period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Rental Lease	$5,278	$3,657	$1,621	$ -	$ -
Motor Vehicle Lease	2,006	1,133	873	-	-
Computers Lease	192	143	49	-	-
Severance pay and long term employee liabilities	1,173	-	1,173	-	-
Long Term Loan	30,000	12,813	17,187	-	-
Long term accrued expenses	547	-	547	-	-
Other long-term liabilities	6,425	-	6,425	-	-
Total	$45,621	$17,746	$27,875	$ -	$ -

Royalties. We participated in programs (from InnoWave, Clariton Networks and Wavion) sponsored by the OCS of the Israeli Government for the support of research and development activities. We are obligated to pay royalties to the OCS amounting to 3.5% of the sales of the products and other related revenues generated from certain research and development projects, up to 100% of the amount granted by the OCS. The obligation to pay these royalties is contingent upon actual sales of the products, and in the absence of such sales, no payment is required. We did not receive grants-bearing royalties from the OCS during the years 2006 until 2011. As a result of the 2011 acquisition of Wavion , we assumed Wavion's grant-bearing royalties from the OCS, and such royalties have been recognized as a liability associated with the acquisition.

During 2011, we paid or accrued royalties to the OCS in the amount of $0.2 million. As of December 31, 2011, the aggregate contingent liability to the OCS amounted to $23.6 million.

Treasury stock. As of December 31, 2011, we repurchased an aggregate of 5,246,772 ordinary shares, which appear on our balance sheet as treasury stock, pursuant to our two repurchase programs, the 2002 repurchase program and the 2008 repurchase program, as stipulated below. In October 2008, following the approval of our board of directors and the receipt of a court approval, we were authorized to use up to $30 million of our available cash to repurchase our shares. Through December 31, 2011 we repurchased under this second repurchase program 1,449,999 ordinary shares at a weighted average price of approximately $3.44 per share for an aggregate of $5.0 million. We have not repurchased any shares in 2010 and 2011. See Item 16E "Purchases of Equity Securities by the Issuer and Affiliated Purchasers" for additional information.

Under the Company's first repurchase program in 2002, our board of directors authorized a share repurchase of up to $9 million of our ordinary shares. Under this 2002 repurchase plan, we had repurchased until December 31, 2003 3,796,773 ordinary shares at a weighted average price per share of approximately $2.07 for an aggregate of $7.9 million. Since then we have not utilized the remainder of this re-purchase program.

FUTURE NEEDS –

We believe our cash balances and investments and governmental research and development grants will be sufficient to satisfy our working capital needs, repayment of amounts under our Long Term Loan, capital expenditures, investment requirements, stock repurchases, commitments, future customer financings, and other liquidity requirements associated with our existing operations through at least the next twelve months. We believe that the most strategic uses of our cash resources include working capital, strategic investments to gain access to new technologies, acquisitions and financing activities. There are no transactions, arrangements and other relationships with unconsolidated entities or other persons that are reasonably likely to materially affect liquidity or the availability of our requirements for capital resources. However, if our operations do not generate cash to the extent currently anticipated by us, or if we grow more rapidly than currently anticipated, it is possible that we will require more funds than anticipated. We expect that these sources will continue to finance our operations in the long term, and will be complemented, if required, by private or public financing.

Effective Corporate Tax Rate

Income derived by Alvarion Ltd. is generally subject to the regular Israeli corporate tax rate.

Until December 31, 2003, the regular tax rate applicable to income of Israeli companies (which are not entitled to benefits due to "Approved Enterprise," as described below) was 36%. In June 2004 and in July 2005, the "Knesset" (Israeli parliament) passed amendments to the Income Tax Ordinance (No. 140 and Temporary Provision), 2004 and (No. 147), 2005, respectively, which determined, among other things, that the corporate tax rate is to be gradually reduced to the following tax rates: 2006 - 31%, 2007 - 29%, 2008 - 27%, 2009 - 26% and 2010 - 25%.

In July 2009, the Knesset passed the Law for Economic Efficiency (Amended Legislation for Implementing the Economic Plan for 2009 and 2010), 2009, which prescribes, among others, an additional gradual reduction in the rates of the Israeli corporate tax and real capital gains tax starting 2011 to the following tax rates: 2011 - 24%.

In December 5, 2011, the Knesset (Israel's Parliament) passed a law for changing the tax burden (the Law), which cancels, among others, the gradual reduction in the corporate tax rates in Israel. In addition, the corporate tax in Israel will be increased to 25% starting in 2012. Accordingly, the real capital gains tax rate will increase to 25%. There was no effect on the Company as a result of the above mentioned changes.

As described below, several of our manufacturing facilities have been granted "Approved Enterprise" status under the Law for the Encouragement of Capital Investments, 1959, as amended, or the Investment Law, and, consequently, are eligible, subject to compliance with specified requirements, for tax benefits beginning when such facilities first generate taxable income.

According to the provision of the law, we have elected the "alternative benefits" track provisions of the Investment Law, pursuant to which we have waived our right to grants and instead receive a tax benefit on undistributed income derived from the "Approved Enterprise" program. The tax benefits under the Investment Law may not be available with respect to income derived from products developed and manufactured outside of Israel or developed or manufactured in Israel but outside of the Approved Enterprises mentioned above and may be affected by the current location of our facilities in Israel. The relative portion of taxable income that should be allocated to each Approved Enterprise and expansion is subject to the fulfillment of covenants with the tax authorities.

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Several of our facilities have been granted Approved Enterprise status:

(i) Nazareth Facilities: On December 31, 1997, our production facilities in Nazareth were granted Approved Enterprise status. Subject to compliance with applicable requirements, the income derived from the Nazareth Approved Enterprise is tax exempt for a period of 10 years.

The periods of tax benefits with respect to Nazareth Approved Enterprises will commence with the first year in which we earn our taxable income and exhaust our accumulated tax loss carry forwards. The period of tax benefits for the Approved Enterprises are subject to limits of the earlier of 12 years from the commencement of production or 14 years from receiving the approval (these limits do not apply to the exemption period). The period of benefits for Nazareth plan expired in 2009.

(ii) Status Expansion of Nazareth and Migdal Ha-emek: In 2000, we received approval of our application for an expansion of our Approved Enterprise status with respect to our Nazareth facility. This expansion included, among other things, our Carmiel facility, which during 2004 was relocated to Migdal Ha-emek. The income derived from this Approved Enterprise is tax-exempt for a period of 10 years. The relative portion of taxable income that should be exempt for a 10-year period is subject to final covenants with the tax authorities. The 10-year period of benefits will commence with the first year in which we earn taxable income. The period of benefits for this expansion plan will expire in 2012.

(iii) Or Yehuda / Tel Aviv Facilities: In 1997, Floware submitted a request for Approved Enterprise status of its production facility in Or Yehuda. This request was approved. After the merger, Floware's enterprise was relocated into our facilities in Tel Aviv. The income derived from this Approved Enterprise is tax exempt for a period of two years and thereafter will be subject to a reduced tax rate between 10% and 25% for an additional period of five to eight years. The actual number of years and tax rate depends upon the percentage of the non-Israeli holders of our share capital. The period of benefits will commence with the first year that we earn taxable income. The period of benefits for this plan has expired in 2011.

In order to maintain eligibility for the above programs and benefits, we must meet specified conditions stipulated by the Investment Law, regulations published there-under and the letters of approval for the specific investments in "Approved Enterprises." In the event of failure to comply with these conditions, any benefits that were previously granted may be canceled, and we may be required to refund the amount of the benefits, in whole or in part, including interest.

If these retained tax-exempt profits are distributed they would be taxed at the corporate tax rate applicable to such profits as if we had not elected the alternative system of benefits, currently between 10% - 25% for an "Approved Enterprise." As of December 31, 2011, our accumulated deficit does not include tax-exempt profits earned by our "Approved Enterprise."

On April 1, 2005, tax benefits under the amendment to the Investment Law came into effect (the "Amendment") and has significantly changed the provisions of the Investment Law. The Amendment limits the scope of enterprises that may be approved by the Investment Center. The Investment Center is a statutory body in Israel responsible for providing certain grants and/or tax benefits subject to certain criteria and limitations. These criteria set for the approval of a facility as a "Privileged Enterprise," include a generally required provision that at least 25% of the Privileged Enterprise's income must be derived from export. Additionally, the Amendment enacted major changes concerning the manner in which tax benefits are awarded under the Investment Law so that companies no longer require the Investment Center's approval in order to qualify for tax benefits. However, the Amendment provides that terms and benefits that were included in any certificate of approval which was already granted will remain subject to the provisions of the law as they were on the date of such approval.

In December 2010, the "Knesset" (Israeli Parliament) passed the Law for Economic Policy for 2011 and 2012 (Amended Legislation), 2011, which prescribes, among others, amendments in the Law for the Encouragement of Capital Investments, 1959 ("the Law"). The amendment became effective as of January 1, 2011. According to the amendment, the benefit tracks in the Law were modified and a flat tax rate applies to the Company's entire preferred income. The Company will be able to elect to apply (the waiver is irrevocable) the amendment and from then on it will be subject to the amended tax rates that are: 2011 and 2012 - 15% (in development area A - 10%), 2013 and 2014 - 12.5% (in development area A - 7%) and in 2015 and thereafter - 12% (in development area A - 6%).

Status Expansion of our Production Facilities: Under the Amendment, in 2005 and 2007, we submitted an expansion request for additional “Privileged Enterprise” approval regarding our production facilities. A portion of the income derived from this “Privileged Enterprise” will be tax-exempt for a period of 10 years and the rest will be taxed at a reduced rate of 10% to 25% (depending on the percentage of foreign investment in the Company). The 10-year period of benefits will commence with the first year in which we earn taxable income.

Our Israeli company had no taxable income since inception nor any profit under our Approved or Privileged Enterprise plans.

As of December 31, 2011, Alvarion Ltd. had an available tax loss carry forward amounting to approximately$206 million, which may be carried forward, in order to offset taxable income in the future, for an indefinite period; the Israeli subsidiary has an available tax loss carry forward amounting to approximately $38.5 million.

As of December 31, 2011, the U.S. subsidiaries had approximately $42.3 million in US federal net operating loss carry forward for income tax purposes, which can be carried forward and offset against taxable income for 20 years and expire between 2012 and 2031. The state tax losses carry forwards of the U.S. subsidiaries are approximately $14.3 million and this balance will expire between 2012 through 2018.

The state and federal tax loss carry forwards per income tax returns filed included uncertain tax positions that were taken in prior years. Due to the application of ASC 740-10, the filed net operating losses are greater than the net operating loss deferred tax asset which was recognized for financial statement purposes.

Utilization of U.S. net operating losses may be subject to substantial annual limitations due to the “change in ownership” provisions (“annual limitations”) of the Internal Revenue Code of 1986, as amended and similar state provisions. The annual limitation may result in the expiration of net operating losses before utilization.

Because we have more than one “Approved Enterprise", and/ or “Privileged Enterprise” our effective tax rate in Israel will be a weighted combination of the various applicable tax rates. We are likely to be unable to take advantage of all tax benefits in Israel for an Approved Enterprise, which would otherwise be available to us, because a portion of our operations may be considered by the Israeli tax authorities as generated in areas that are defined as non-Approved or non-Privileged Enterprise areas.

Our effective corporate tax rate may substantially exceed the Israeli tax rate. Our France, Romania, Brazil, Hong-Kong, Singapore, Japan, Mexico, Poland, Israel, Uruguay, Spain, UK, South-Africa, Italy, Argentina, Ecuador, Costa Rica, India, Chile, Indonesia, Taiwan and Philippines subsidiaries will generally each be subject to applicable federal, state, local and foreign taxation, and we may also be subject to taxation in other jurisdictions where we own assets, have employees or conduct activities. Because of the complexity of these local tax provisions, it is not possible to anticipate the actual combined effective corporate tax rate that will apply to us.

Government Grants –

Under an arrangement entered during 2003 with the OCS in Israel’s Ministry of Industry and Trade we participate in new OCS programs under which we are eligible to receive grants for research and development projects without any royalty repayment obligations, excluding OCS programs grants resulting from InnoWave’s former operations, Clariton and Wavion which were not included in this arrangement.

In addition to these grants, we obtain grants from the OCS to fund certain other research and development projects as part of our participation in the MAGNET Consortium. These grants do not bear any royalty repayment obligations. The MAGNET Program in the OCS sponsors innovative generic industry-oriented technologies to strengthen the country's technological expertise and enhance competitiveness.

We also participate in certain governmental programs in Spain and in Romania, which finance certain local research and development projects.

In addition we participate in the BuNGEE (researching for high capacity density deployments targeting 1Gbs/km^2) and Flavia (Flexible Architecture for Virtualizable wireless future Internet access) projects, which are a consortium of commercial companies and academy institutes from Europe and Israel.

All of these programs provide grants without any royalty obligations. The programs are expected to last between two and three years. If we are unable to meet the terms of these programs we may be required to return the grants received.

Recently Issued Accounting Standards –

Impact of recently issued Accounting Standards:

In May 2011, the FASB issued ASU 2011-04 Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs, codified in ASC 820 "Fair Value Measurement". The guidance requires an entity to provide a consistent definition of fair value to ensure that the fair value measurement and disclosure requirements are similar between U.S. GAAP and International Financial Reporting Standards. The guidance changes certain fair value measurement principles and enhances the disclosure requirements particularly for Level 3 fair value measurements, and will become effective for the Company beginning January 1, 2012. The Company does not expect the adoption of this new guidance to have a material impact on its financial statements.

In June 2011, the FASB issued ASU 2011-05 Presentation of Comprehensive Income, codified in ASC 220 "Comprehensive Income". The guidance requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The guidance also eliminates the option to present the components of other comprehensive income as part of the statement of equity. In December 2011, the FASB issued ASU 2011-12, deferring the effective date for amendments outlined in ASU 2011-05, but the remainder of its provisions will become effective for the Company beginning January 1, 2012. The Company is still evaluating whether to present other comprehensive income in a single continuous statement of comprehensive income or in two separate but consecutive statements.

In September 2011, the Financial Accounting Standards Board, or FASB issued ASU 2011-08, Testing Goodwill for Impairment, codified in ASC 350 "Intangibles – Goodwill and Other". The revised accounting standard update intended to simplify how an entity tests goodwill for impairment. The amendment will allow an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity no longer will be required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. This accounting standard update will be effective for the Company beginning January 1, 2012. The Company does not expect the adoption of this new guidance to have a material impact on its financial statements.

C.RESEARCH AND DEVELOPMENT, PATENTS AND LICENSES –

Our product development plans are market driven and address the major, fast-moving trends that influence the wireless industry. We believe that our future success will depend upon our ability to maintain technological competitiveness, to enhance our existing products and to introduce on a timely basis new commercially viable products addressing the demands of the broadband wireless access market. Accordingly, we devote, and intend to continue to devote a significant portion of our personnel and financial resources to research and development. As part of the product development process, we seek to maintain close relationships with current and potential distributors, other resellers and end users, strategic partners and leaders in industry segments in which we operate to identify market needs and define appropriate product specifications.

As of December 31, 2011, our research and development staff consisted of 225 full time employees. Our research and development is conducted at our facilities in Israel, Romania and Spain. We occasionally use independent subcontractors for portions of our development projects.

Our gross research and development expenses were approximately $32 million or 17% of sales in 2011, $42 million or 20% of sales in 2010 and $55 million or 22% of sales in 2009. The Government of Israel and other jurisdictions for funding-approved research and development projects reimbursed us for approximately $3.9 million in 2009, $3.0 million in 2010 and $4.4 million in 2011.

D.TREND INFORMATION -

See "—Operating Results—2011 Highlights" and "Item 3—Key Information—Risk Factors".

E.OFF-BALANCE SHEET ARRANGEMENTS

None.

F.TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

See "—Liquidity and Capital Resources—Working Capital—Commitments".

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES –

A.DIRECTORS AND SENIOR MANAGEMENT

The following table lists the name, age and position of each of our directors and executive officers as of March 31, 2012:

Name	Age	Position
Amnon Yacoby	61	Chairman of the Board of Directors (1)(4)(5)
Dan Yalon	39	Director (1)
Professor Raphael Amit	64	Director(1)(2)(3)(4)
Robin Hacke	52	Director (1)(2)(3)(5)
Tali Aben	48	Director (1)(5)
Doron Inbar	62	Director (1)(3) (4) (5)
Ng Eng Ho	58	Director (1)
Eran Gorev	47	Chief Executive Officer and President (6)
Lior Shemesh	42	Chief Financial Officer
Mohammad Shakouri	49	Corporate Vice President, Innovation and Marketing
Elli Yaniv	59	President, Operations and Infrastructure Division
Gadi Bahat	48	Chief Business Officer
Tal Meirzon	46	Chief Operating Officer
Assaf Katan	41	Corporate Vice President, Strategy & Business Development
Anat Mogilevsky	37	Corporate Vice President, Human Resources

(1) “Independent Director” under rules of the SEC, NASDAQ Marketplace Rules and the Israeli Companies Law (see explanation below).

(2) “External Director” within the meaning of the Israeli Companies Law (see explanation below).

(3) Member of our audit committee.

(4) Member of our compensation committee.

(5) Member of our nominating and corporate governance committee.

(6) Mr. Gorev will leave the Company and will be replaced by Mr. Hezi Lapid, effective May 6, 2012. Mr. Lapid most recently served as Chairman and CEO of Axerra Networks, a provider of carrier network equipment. Prior to joining Axerra, he headed multiple business units as an executive of ECI Telecom Ltd. from 1995 until 2003. He also served as CEO of C. Mer Industries, a global system integrator delivering turn-key solutions for wireless networks. Mr. Lapid holds a B.Sc. in Electrical Engineering from Ben-Gurion University and a M.Sc. in Management and Information Sciences from Tel Aviv University.

Mr. Amnon Yacoby has served as a member of our board of directors since our merger with Floware in August 2001. In October 2011, he was appointed as the Chairman of the Board of Directors. Mr. Yacoby founded Floware and served as its Chief Executive Officer and as a member of its board of directors until its merger with us. Following our merger with Floware until the end of 2001, Mr. Yacoby served as our co-Chief Executive Officer. In 2004, Mr. Yacoby founded Aternity, Inc. and serves as its Chairman and CEO. In 1987, Mr. Yacoby founded RAD Network Devices Ltd., a developer of data networking devices, and served as its president and Chief Executive Officer until 1995. From 1972 to 1986, he served in the Israel Defense Forces’ Electronic Research Department in various positions, most recently as head of the department. He twice received the Israel Security Award. Mr. Yacoby holds B.Sc. and M.Sc. degrees in Electrical Engineering from the Technion – Israel Institute of Technology.

Professor Raphael Amit has served as one of our external directors since September 2003. He serves on the audit and on the compensation committees. Prior to joining our board of directors, Professor Amit served as Chairman of the board of directors of Creo Products Inc (NASDAQ: CREO until May 2005). Professor Amit has been the Robert B. Goergen Professor of Entrepreneurship and a Professor of Management at the Wharton School of the University of Pennsylvania since July 1999. Professor Amit also serves as the Academic Director of Wharton's Goergen Entrepreneurial Management Programs. Prior thereto, Professor Amit was the Peter Wall Distinguished Professor at the Faculty of Commerce and Business Administration, University of British Columbia (UBC), where he was the founding director of the W. Maurice Young Entrepreneurship and Venture Capital Research Center. From 1983 to 1990, Professor Amit served on the faculty of the J.L. Kellogg Graduate School of Management at Northwestern University, where he received the J.L. Kellogg Research Professorship and the Richard M. Paget Research Chair in Business Policy. Professor Amit holds B.A. and M.A. degrees in Economics from the Hebrew University and a Ph.D. in Management from the Northwestern University's J.L. Kellogg Graduate School of Management. Professor Amit has served as a consultant to a broad range of organizations in North America and Europe on strategic, entrepreneurial management and new venture formation issues.

Ms. Robin Hacke was appointed as one of our external directors upon our merger with Floware in August 2001. Ms. Hacke served as a member of Floware's board of directors from its initial public offering in August 2000 and was appointed as an external director of Floware in December 2000. In September 2007, Ms. Hacke became Director of Capital Formation at Living Cities, a funding collaborative of foundations and financial institutions. Since August 2003, Ms. Hacke has been the Managing Director of Pentaport Venture Advisors Inc., a company that advises investment companies, including Portview Communications Partners LP. From 1990 to 2002, Ms. Hacke served as the Chief Executive Officer of HK Catalyst Strategy and Finance Ltd., a company that Ms. Hacke founded that provided advisory services to investment companies and high-tech enterprises. From 1986 to 1990, Ms. Hacke held various management positions at Aitech Ltd., an Israeli start-up company. Prior to that, Ms. Hacke was an investment banker at Shearson Lehman Brothers in New York. Ms. Hacke holds an A.B. magna cum laude degree from Harvard-Radcliffe College and an MBA degree from Harvard Business School.

Mr. Doron Inbar has served as a member of our board of directors since September 2009. Mr. Inbar is a Venture Partner at Carmel Ventures, an Israeli-based venture capital fund. He serves as Chairman of C-nario Ltd. a digital signage company. As chairman of Enure Networks Ltd. and an active chairman at Archimedes Global Ltd., a private health provision and insurance company providing its services in the CIS countries. In addition Mr. Inbar serves as independent director on the board of Maccabi Dent Ltd., the largest chain of dental service clinics in Israel. Prior to joining Carmel Ventures in 2006, Mr. Inbar served as President and Chief Executive Officer of ECI Telecom Ltd., having served as President from November 1999 and Chief Executive Officer from February 2000. Mr. Inbar joined ECI Telecom in 1983 and during his first eleven years with ECI, he served in various positions at its wholly-owned U.S. subsidiary, ECI Telecom, Inc., including Executive Vice President and General Manager. In July 1994, Mr. Inbar returned to Israel to become Vice President, Corporate Budget, Control and Subsidiaries of ECI Telecom Ltd. In June 1996, Mr. Inbar was appointed Senior Vice President and Chief Financial Officer, and he became Executive Vice President in January 1999. Mr. Inbar holds a bachelors degree in economics and business administration from Bar-Ilan University, Israel.

Mr. Ng Eng Ho has served as a member of our board of directors since September 2009. Mr. Eng Ho is the Executive Director of Audelia Pte Ltd., an investment and management consultancy company he founded in November 2007. Prior to founding Audelia Pte Ltd. Mr. Eng Ho served as Executive Vice President (Operations) at ST Technologies Telemedia Pte Ltd., a subsidiary of Temasek Holdings, since December 2005, and as the Deputy President Director of ST Telemedia's Indonesian subsidiary, PT Indosat Tbk, from January 2003 through December 2005. Prior to that, Mr. Eng Ho was Managing Director of Keppel Telecommunications & Transportation Ltd, (Keppel T&T) from July 1998 to September 2002, after serving in various positions at Keppel T&T and its subsidiaries from September 1990 through June 1998. Prior to joining Keppel T&T, Mr. Eng Ho was a career officer in the Singapore Armed forces from 1973 through 1990. Mr. Eng Ho received his Bachelor of Science (Telecomm System Engineering) degree (Honors) from the Royal Military College of Science, UK.

Ms. Tali Aben was appointed as a member of our board of directors in November 2011. Since 2008, she has been advising international investors on opportunities within the Israeli high-tech sector. Ms. Aben also serves as an external director of Attunity Ltd. and Vizrt Ltd. (two publicly traded companies), as well as several privately-held companies and non-profit organizations. Previously, Ms. Aben was a General Partner with Gemini Israel Funds, a venture capital firm, which she joined in 1994. At Gemini, she funded and supported many successful companies, including Verisity, Jacada, Abirnet, Business Layers, Servicesoft, nLayers and others. Her focus has been primarily on software companies, expanding in 2007 to include cleantech companies. Ms. Aben holds a B.Sc. in Mathematics and Computer Science and an MBA, both from Tel Aviv University.

Mr. Dan Yalon was appointed as a member of our board of directors in February 2012. Since 2007, Mr. Yalon has served as the Chief Strategy Officer of NICE Systems (NASDAQ: NICE). As a member of NICE's executive leadership team, Mr. Yalon was responsible for strategy formulation and execution, and for strategic alliances building growth strategies which were successfully executed organically and inorganically. Prior to joining NICE in 2007, Mr. Yalon was Head of Strategy and New Business Initiatives at Amdocs (NYSE: DOX), where he led all corporate strategy activities – defining and executing growth engines. His career also includes several years as a strategy consultant with US-based Monitor Group and with Israeli firm POC Hi-Tech. Mr. Yalon holds an LL.B. and a Bachelor degree in Management from the Hebrew University of Jerusalem and is a graduate of Harvard Business School's Advanced Management Program (AMP).

Mr. Eran Gorev was appointed as our President and Chief Executive Officer in December 2009. Prior to his appointment, he served from 2005 until 2009 as President and CEO of NICE Systems Inc., the company's operation in the Americas, and from 2008 until 2009 as NICE's Chief Business Officer, responsible for driving the company's global business. Prior to NICE Systems, Mr. Gorev worked for Amdocs from 1996 until 2004, where he was President of the North America Major Clients Division responsible for the company's business with some of North America's leading communication service providers and media companies, and Corporate Vice President and Head of Worldwide Sales, responsible for leading global sales and business development activities. Mr. Gorev holds an LLB degree from Tel-Aviv University and a joint MBA degree from the Kellogg School of Management, at Northwestern University, and the Recanati School of Business Administration, at Tel-Aviv University.

Mr. Lior Shemesh became our Chief Financial Officer in January 2011, after serving for two years as our Vice President of Finance. Prior to this, he served as Vice President of Finance at Veraz Networks, a provider of softswitch, media gateway and digital compression solutions from May 2003 to October 2008. Before joining Veraz, Mr. Shemesh worked for ECI Telecom, a networking infrastructure provider, from April 2000 to May 2003 as the company Controller, and later as Associate Vice-President of Finance of the Broadband Division. Mr. Shemesh is a Certified Public Accountant in Israel and holds a B.A. in Accounting and Economics, and an M.B.A from Bar-Ilan University.

Dr. Mohammad Shakouri was appointed as our Corporate Vice President of Innovation and Marketing in March 2008 and assumed his new role as of April 1, 2008. Dr. Shakouri joined us in February 2001 and has extensive experience in wireless communication systems and fiber optic networks. Dr. Shakouri serves as a Vice President of WiMAX Forum, a member of WiMAX Forum board of directors, advisory board for the Wireless Communication Alliance and is an IEEE MTT-SVC 2004 chairman. Prior to joining Alvarion, Dr. Shakouri worked at Lucent Technologies where he was responsible for managing, building and developing network solutions for European and South American broadband wireless markets. Before joining Lucent, he spent fourteen years in technical and management positions with Hewlett Packard developing microwave and fiber optic communication components and systems. He co-founded the wireless systems division, where he was responsible for the engineering team developing low-cost residential digital wireless systems for U.S. and Asian markets. Dr. Shakouri earned his doctorate in electrical engineering from Stanford University on Subpicosecond GaAs Wafer Probe Systems.

Mr. Gadi Bahat joined Alvarion as President of the Customer Business Division in October, 2010, with global responsibility for regional operations and activities. Mr. Bahat came to Alvarion after successfully leading Olista (a provider of customer experience analytics solutions that enable mobile and broadband operators to increase the success of their service offerings) for two years as CEO and board member, until the company was acquired in May 2010. Prior to joining Olista in September 2008, Mr. Bahat spent over a decade with Comverse, where he held a number of executive management positions including EMEA Group President, International Group President and World Group President. He was also a member of Comverse’s Executive Management team, and was responsible for a P&L of more than $500 million. Before joining Comverse in August 1995, Mr. Bahat held a number of Product Management/Marketing positions at Scitex and RAD Data Communications. Mr. Bahat holds a B.Sc. in Electrical Engineering from the Technion Israel Institute of Technology, and an MBA from Tel-Aviv University.

Tal Meirzon currently holds the position of COO for Alvarion. Prior to Alvarion, Mr. Meirzon was the CEO for Wavion Networks leading the company to a front line position in the carrier-grade Wi-Fi market. In November 2011, Mr. Meirzon played a pivotal role in facilitating Alvarion’s acquisition of Wavion Networks. Prior to this, Mr. Meirzon held various executive positions at Gilat Satellite Networks for 13 years, serving as the General Manager of Gilat’s Wireless Business Unit. In addition he held roles as VP Marketing and Business Development, where he managed Gilat's expansion into new markets. Mr. Meirzon holds a B.Sc in Electrical Engineering and an MBA in Technology Management and Marketing, both from the Tel Aviv University.

Elli Yaniv joined Alvarion as the Corporate VP of Operations in September 2011. Previously, Mr. Yaniv was VP of Operations for more than four years at Gilat Satelites Network. From 1994 until 2005 Mr. Yaniv was with Flextronics in a variety of global management roles including management of the global semiconductor division. Prior to Flextronics, Mr. Yaniv held a number of executive positions in several hi-tech Israeli companies, including the establishment of Intel’s first fabrication plant in Israel. Mr. Yaniv holds a M.Sc. in Industry and Management Engineering from the Technion Israel Institute of Technology, and an MBA from Tel-Aviv University.

Assaf Katan joined Alvarion in October 2010 as VP Business Development and became a member of Alvarion’s management team in January 2012. Prior to joining Alvarion, Mr. Katan spent two and a half years as VP Marketing and Business Development at Media Layers, a start-up in the Mobile Advertising space. He previously spent five years at Comverse in various corporate marketing and business development positions, where he initiated and led the company's entry into the mobile content domain, and a team leader at Shaldor, Israel's leading strategy consulting firm. Mr. Katan holds a B.A. in Psychology and Business Administration from the Tel Aviv University.

Anat Mogilevsky joined Alvarion as the Corporate Vice President of Human Resources in November 2011. Prior to Alvarion, Ms. Mogilevsky headed the Human Resources department for 3 years at RADVISION. From 2005 to 2009, Mr. Mogilevsky held a number of roles in Human Resources at Alvarion, including serving as the Director of Training and Organizational Development. Prior to Alvarion, Ms. Mogilevsky served in Human Resources department of the R&D and Operations Divisions at Teva Pharmaceutical Industries. Ms. Mogilevsky holds a B.A. in Sociology and M.A. in Labor Studies from Tel Aviv University.

There are no family relationships between any of our directors and executive officers.

B.COMPENSATION OF DIRECTORS AND OFFICERS –

The aggregate direct labor costs associated with all of our directors and executive officers as a group (24 persons) for the year ended December 31, 2011 (including persons who served as executive officers and directors during 2011 and did not serve in such capacity as of December 31, 2011) was approximately $3.9 million, which included, with respect to the executive officers, payments made pursuant to bonus plans and with respect to certain executive officers, payments made pursuant to their separation agreements. This amount also includes approximately $507,000 that was set aside or accrued to provide pension, retirement, social security or similar benefits. The amount does not include amounts expended by us for vehicles made available to our officers; expenses, including business travel, professional and business association dues and expenses; reimbursements to directors and officers; and other fringe benefits commonly reimbursed or paid by companies in Israel. Our directors received an aggregate of approximately $287,112 in cash compensation in 2011.

From time to time, we grant options and awards under our equity incentive plans (described below under Share Ownership) to our executive officers and directors.

Option grants to directors (including the chairman of our board of directors) who are not executive officers are made pursuant to an automatic option grant program. Non-employee directors who are elected or re-elected to our board of directors are granted upon each of their election or re-election, an option to purchase 30,000 ordinary shares for the term for which they are elected or re-elected. The options vest in equal quarterly installments over the term of election or re-election, commencing at the end of the third month following the date of election or re-election. All options to our non-employee directors pursuant to the automatic option grant program are granted at an exercise price equal to 100% of the closing price of the ordinary shares on the NASDAQ Global Select Market on the last trading day immediately preceding the date of the election or re-election.

During 2011, we granted all of our directors and executive officers as a group (24 persons) (including persons who served as directors and executive officers during 2011 and did not serve in such capacity as of December 31, 2011) options to purchase an aggregate of 480,000 of our ordinary shares at exercise prices ranging from $ 0.003 to $0.95, with expiration dates ranging from November 1, 2017 to December 21, 2021.

As of December 31, 2011, our directors and executive officers (including persons who served as executive officers and directors during 2011 and did not serve in such capacity as of December 31, 2011) held outstanding options to purchase an aggregate of 6,031,998 ordinary shares, at exercise prices ranging from $ 0.003 to $15.40 with expiration dates ranging from May 8, 2012 to December 21, 2021.

We currently pay each of our non-executive directors (other than the Chairman of our board of directors who provides executive services to Alvarion and is paid separately for those services) an annual fee of $25,000 for the services he or she provides to Alvarion, which annual fee includes payment for the board and committee meetings attended by such director during the year. In addition, each of the chairs of the Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee is paid an additional annual fee of $25,000.

C. BOARD PRACTICES –

Appointment of Directors and Terms of Office

Our board of directors currently consists of seven members. Under our articles of association, our board of directors is to consist of between 4 and 10 members. Our directors are elected by our shareholders at an annual general shareholders meeting. Our directors generally commence the terms of their office at the close of the annual general shareholders meeting at which they are elected and, other than our external directors, serve in office until the close of the third annual general shareholders' meeting following the meeting at which they are elected, and may be re-elected by the shareholders. Annual general shareholders meetings are required to be held at least once every calendar year, but not more than 15 months after the last preceding annual general shareholders meeting. In the intervals between the annual general meetings of the shareholders, our shareholders or our board of directors may appoint new directors to fill any vacancy created in our board of directors, except for vacancies of an external director.

The terms of office of the directors, including compensation, must be approved, under the Israeli Companies Law, by the audit committee, the board of directors and the general meeting of the shareholders.

Pursuant to a recent amendment to the Israeli Companies Law that took effect in 2011, compensation arrangements for executive officers who are not directors require the approval of the audit committee and the board of directors. The approval of the audit committee may be substituted with the approval of the compensation committee, provided that the compensation committee complies with all the requirements prescribed by the Israeli Companies Law regarding composition of the audit committee. If the compensation arrangement is an immaterial amendment to an existing compensation arrangement of an officer who is not a director, the approval of the audit committee is sufficient.

The term of office of Messrs. Inbar, Yalon and Eng Ho will expire at our 2012 annual general meeting of the shareholders; and the term of office of Mr. Yacoby will expire at our 2013 annual general meeting of the shareholders. The term of office of Ms. Aben will expire at our 2014 annual general meeting of the shareholders. The terms of office of our external directors, Ms. Hacke and Professor Amit, expire in August 2013 and September 2012, respectively, as described below.

Service Contracts of Directors

None of our directors has the right to receive any benefit upon termination of his or her office or any service contract he or she may have with us.

External Directors

We are subject to the provisions of the Israeli Companies Law. Under the Israeli Companies Law, companies incorporated under the laws of Israel whose shares have been offered to the public in or outside of Israel are required to appoint at least two directors who qualify as external directors under the Israeli Companies Law. At least one of the external directors is required to have "financial and accounting expertise" (unless another member of the audit committee, who is an independent director under the NASDAQ Marketplace Rules, has "financial and accounting expertise") and any other external director must have "accounting and financial expertise" or "professional expertise," as such terms are defined by regulations promulgated under the Israeli Companies Law. Our board of directors has determined that Professor Amit has "financial and accounting expertise" and Ms. Hacke has "professional expertise".

A person may not serve as an external director if at the date of the person's election or within the prior two years the person is a relative of the company's controlling shareholder, or the person or his or her relatives, partners, employers, supervisors or entities under the person's control, have or had any affiliation with us or with a controlling shareholder or relatives of a controlling shareholder, and, in the case of a company without a controlling shareholder or a shareholder holding at least 25% of the voting rights, any affiliation, at the time of election, to the chairman of the board of directors, the chief executive officer, an interested party or the company's most senior finance officer. Under the Israeli Companies Law, the term affiliation includes:

- an employment relationship;
- a business or professional relationship maintained on a regular basis;
- control; and
- service as an office holder.

In addition, a person may not serve as an external director:

- if the person or his or her relatives, partners, employers, supervisors or entities under the person's control, maintains a business or professional relationship, even if such relationship is not on a regular basis, other than a negligible business or professional relationship, or
- if the person received compensation as an outside director in excess of the amounts permitted by the Israeli Companies Law and regulations thereunder.

An "office holder" is defined as any managing director, general manager, chief executive officer, executive vice president, vice president, or any other person assuming the responsibilities of any of these positions regardless of that person's title, or any director or any manager directly subordinate to the general manager. Each person listed in the table under "Director and senior management" in Item 6.A. above is an office holder. A "relative" is defined as a spouse, sibling, parent, grandparent or descendent, or a spouse's descendant, sibling or parent or the spouse of any of the foregoing. An "interested party" is defined as a holder of 5% or more of our shares or voting rights, any person or entity that has the right to nominate or appoint at least one of our directors or our general manager, or any person who serves as one of our directors or as our general manager.

A person may not serve as an external director if that person’s position or other business creates, or may create, a conflict of interest with the person’s responsibilities as an external director or may otherwise interfere with such person’s ability to serve as a director. If at the time any external director is to be elected all members of the board of directors that are not controlling shareholders or their respective relatives are of the same gender, then the external director to be elected must be of the other gender. There is also a restriction on interlocking boards of directors: a director of a company may not be elected as an external director of another company if, at that time, a director of the other company is acting as an external director of the first company.

Under the Israeli Companies Law, each committee of a company’s board of directors is required to include at least one external director, except for the audit committee, which requires that all external directors be members of such committee, including one external director serving as the chair of the audit committee. The term of office of an external director is three years and may be extended for additional three year terms. However, Israeli companies listed on certain stock exchanges outside Israel, including the NASDAQ Global Select Market, such as our company, may appoint an external director for additional unlimited terms of three years each subject to certain conditions. Such conditions include the determination by the audit committee and board of directors that, in view of the director’s professional expertise and special contribution to the company’s board of directors and its committees, the appointment of the external director for an additional term is in the best interest of the company. An external director can be removed from office only under very limited circumstances.

The external directors must be elected by the majority of the shareholders in a general meeting, provided that either (i) the shares voting in favor of the external director's election includes at least a majority of the shares of non-controlling shareholders or shareholders who have a personal interest in the election of the external directors (excluding a personal interest that is not related to a relationship with the controlling shareholders), or (ii) the total shares of non-controlling shareholders voted against the election does not represent more than two percent of the total voting rights in the company.

Until the lapse of two years from the termination of office, the company, a controlling shareholder and entities under the company's control may not grant the external director or any of his or her relatives, directly or indirectly, any benefit, or engage the external director or his or her relatives as an office holder of the company, of a controlling shareholders or of an entity under the company's control, and may not employ or receive services from the external director or any of his or her relatives, either directly or indirectly, including through a corporation controlled by that person. The restriction on a relative that is not the spouse or child of the external director is limited to one year from the termination of office instead of two years.

Ms. Robin Hacke and Professor Raphael Amit qualify as our external directors under the Israeli Companies Law. We have appointed the external directors to the committees of our board of directors as required by the Israeli Companies Law.

Independent Directors

NASDAQ Listing Rules require that the board of directors of a NASDAQ-listed company have a majority of independent directors, each of whom satisfies the "independence" requirements of NASDAQ, and its audit committee must have at least three members and be comprised only of independent directors, each of whom satisfies the respective "independence" requirements of NASDAQ and the SEC. Our board of directors has determined that each of Professor Amit, Ms. Hacke, Ms. Aben, Mr. Yalon, Mr. Yacoby, Mr. Inbar, and Mr. Ng Ho qualifies as an independent director under the requirements of NASDAQ, and that each of Professor Amit, Ms. Hacke, and Mr. Inbar (who serve on our audit committee) qualifies as an independent director under the requirements of the SEC and NASDAQ.

Under the Israeli Companies Law, an Israeli company, whose shares are publicly traded, may elect to adopt a provision in its articles of association pursuant to which a majority of its board of directors (or a third of its board of directors in the case the company has a controlling shareholder) will constitute individuals complying with certain independence criteria prescribed by the Israeli Companies Law, as well as certain other recommended corporate governance provisions. We have not included such provisions in our articles of association since our board of directors complies with the independence requirements and the corporate governance rules of NASDAQ and the Securities and Exchange Commission regulations. However, as described above, a majority of our board of directors and all the members of our audit committee consist of directors that comply with the independence criteria prescribed by the Israeli Companies Law.

Committees of the Board of Directors

Our board of directors has established an audit committee, a compensation committee and a nominating and corporate governance committee.

Audit Committee

Pursuant to the Israeli Companies Law and the NASDAQ Listing Rules, the board of directors of a public company must appoint an audit committee. The responsibilities of the audit committee include monitoring the management of the Company's business and suggesting appropriate courses of action, as well as classifying and approving related party transactions and extraordinary transactions, reviewing the internal auditors audit plan, establishing and monitoring whistleblower procedures, reviewing and recommending on board members compensation and other matters as required by Israeli law and NASDAQ rules. The audit committee must be comprised of at least three directors, including all the external directors (including one external director serving as the chair of the audit committee). Our audit committee assists the board of directors in fulfilling its responsibilities to ensure the integrity of our financial reports, serves as an independent and objective monitor of our financial reporting process and internal controls systems, including the activities of our independent auditor and internal audit function, and provides an open avenue of communication between the board of directors and the independent auditors, internal auditor and financial and executive management.

The audit committee may not include the chairman of the board, or any director employed by us, by a controlling shareholder or by any entity controlled by a controlling shareholder, or any director providing services to us, to a controlling shareholder or to any entity controlled by a controlling shareholder on a regular basis, or any director whose income is primarily dependent on a controlling shareholder, and may not include a controlling shareholder or any relatives of a controlling shareholder. Individuals who are not permitted to be audit committee members may not participate in the committee's meetings other than to present a particular issue. However, an employee who is not a controlling shareholder or relative may participate in the committee's discussions but not in any vote, and the company's legal counsel and corporate secretary may participate in the committee's discussions and votes if requested by the committee.

The members of our audit committee are Professor Amit, Ms. Hacke and Mr. Inbar each of whom is an independent director under the requirements of the SEC, NASDAQ and the Israeli Companies Law. Professor Amit qualifies as an "audit committee financial expert" for purposes of the rules of the SEC. As stated above, Ms. Hacke and Professor Amit qualify as external directors under the Israeli Companies Law.

Compensation Committee

The compensation committee of our board of directors consists of Mr. Yacoby, Professor Amit and Mr. Inbar. Our board of directors has adopted a compensation committee charter setting forth the responsibilities of the committee, which include:

- reviewing and recommending to the board of directors for its determination all compensation arrangements of our chief executive officer and chief financial officer;
- reviewing and determining all compensation arrangements of our other executive officers, including our corporate vice presidents and division presidents; and
- overseeing our equity incentive plans and cash incentives and deferred compensation plans.

Nominating and Corporate Governance Committee

The nominating and corporate governance committee of our board of directors consists of Ms. Hacke, Mr. Yacoby, Mr. Inbar and Ms. Aben. Our board of directors has adopted a nominating and corporate governance committee charter setting forth the responsibilities of the committee, which include:

- seeking and recommending to the board of directors the nomination of qualified candidates for election to the board of directors;

- recommending to the board of directors the directors that shall serve on each committee of the board of directors;
- leading and monitoring a process to assess the effectiveness of the board of directors;
- developing and recommending to the board of directors a set of corporate governance guidelines, periodically reviewing such guidelines and recommending changes; and
- overseeing the evaluation of the board of directors.

Internal Auditor

The Israeli Companies Law also requires the board of directors of a public company to appoint an internal auditor recommended by the audit committee. The role of the internal auditor is to examine, among other things, whether the company's acts comply with applicable law and orderly business procedure. The internal auditor may be an employee of the company but may not be an interested party or office holder, a relative of an interested party or office holder, or a member of the company's independent accounting firm or its representatives. Our current internal auditor, Mr. Eyal Weitzman, has served in this position since February 2006.

Fiduciary Duties and Approval of Related Party Transactions

Fiduciary Duties. The Israeli Companies Law codifies the fiduciary duties that office holders, which under the Israeli Companies Law include directors and executive officers, owe to a company. An office holder's fiduciary duties consist of a duty of care and a duty of loyalty.

The duty of care requires an office holder to act with the level of care that a reasonable office holder in the same position would apply under the same circumstances. This includes the duty to use reasonable means to obtain information regarding the advisability of a given action submitted for his approval or performed by him by virtue of his position, and all other relevant information material to these actions.

The duty of loyalty requires an office holder to act in good faith and for the company's benefit, including to avoid any conflict of interest between the office holder's position in the company and any other position held by him or his personal affairs, and prohibits any competition with the company, or the exploitation of any business opportunity of the company in order to receive personal advantage for himself or others. This duty also requires disclosing to the company any information or documents relating to the company's affairs that the office holder has received as a result of his position as an office holder. A company may approve any of the acts mentioned above provided that all the following conditions apply: the office holder acted in good faith and neither the act nor the approval of the act prejudices the good of the company and the office holder disclosed the essence of his personal interest in the act, including any substantial fact or document, a reasonable time before the date for discussion of the approval. A director is required to exercise independent discretion in fulfilling his or her duties and may not be party to a voting agreement with respect to his or her vote as a director. A violation of these requirements is deemed a breach of the director's duty of loyalty.

Disclosure of Personal Interest. The Israeli Companies Law requires that an office holder promptly disclose to the company any personal interest that he or she may have and all related material information known to him or her, in connection with any existing or proposed transaction by the company. "Personal interest", as defined by the Israeli Companies Law, includes a personal interest of any person in an act or transaction of the company, including a personal interest of a person's relative or of a corporation in which that person or a relative of that person is a 5% or greater shareholder, a holder of 5% or more of the voting rights, a director or general manager, or in which he or she has the right to appoint at least one director or the general manager, and includes shares for which the person has the right to vote pursuant to a power-of-attorney. "Personal interest" does not apply to a personal interest stemming merely from holding shares in the company.

The office holder must make the disclosure of his or her personal interest no later than the first meeting of the company's board of directors that discusses the particular transaction. This duty does not apply to the personal interest of a relative of the office holder in a transaction unless it is an "extraordinary transaction". The Israeli Companies Law defines an "extraordinary transaction" as a transaction that is not in the ordinary course of business, not on market terms or is likely to have a material impact on the company's profit, assets or liabilities.

Approval of Compensation of Office Holders. Under the recent amendment to the Israeli Companies Law that took effect in 2011, compensation arrangements for officers who are not directors require the approval of the audit committee and the board of directors. The approval of the audit committee may be substituted with the approval of the compensation committee, provided that the compensation committee complies with all the requirements prescribed by the Israeli Companies Law regarding composition of the audit committee. If the compensation arrangement is an immaterial amendment to an existing compensation arrangement of an officer who is not a director, the approval of the audit committee is sufficient. Arrangements regarding the compensation of directors require the approval of the audit committee, the board and the shareholders, in that order.

Approval of Other Transactions with Office Holders. The Israeli Companies Law provides that a transaction with an office holder or a transaction in which an office holder has a personal interest requires board approval, unless the transaction is an extraordinary transaction or the articles of association provide otherwise. Our articles of association do not provide otherwise. The transaction may not be approved if it is adverse to our interest. If the transaction is an extraordinary transaction, or if it concerns exculpation, indemnification, insurance or compensation of an office holder, then the approvals of our audit committee and board of directors are required, except if the compensation arrangement is an immaterial amendment to an existing compensation arrangement of an officer who is not a director, in which case the approval of the audit committee is sufficient. Exculpation, indemnification, insurance or compensation of a director also requires shareholder approval.

Any person who has a personal interest in a matter that is considered at a meeting of the board of directors or the audit committee generally may not be present at such meeting or vote on such matter unless a majority of the board of directors or the audit committee has a personal interest in the matter, or if such person is invited by the chairman of the board of directors or audit committee, as applicable, to present the matter being considered. If a majority of the board of directors or the audit committee has a personal interest in the transaction, shareholder approval is also required.

Controlling Shareholder – Disclosure and Approval

The Israeli Companies Law imposes on a controlling shareholder of a public company the same disclosure requirements described above as it imposes on an office holder. For this purpose, a "controlling shareholder" is any shareholder who has the ability to direct the activities of a company, including any shareholder that holds 25% or more of the voting rights if no other shareholder owns more than 50% of the voting rights in the company. Two or more shareholders with a personal interest in the approval of the same transaction are deemed to be one shareholder.

Approval of the audit committee, the board of directors and our shareholders, in that order, is required for:

- extraordinary transactions, including a private placement, with a controlling shareholder or in which a controlling shareholder has a personal interest; and

- the terms of compensation or employment or engagement of a controlling shareholder or his or her relative, as our officer holder or employee or as a service provider to the company, including through a company controlled by a controlling shareholder.

Shareholder's approval must include the majority of shares voted at the meeting. In addition to the majority vote, the shareholder approval must satisfy either of two additional tests:

- the majority includes at least a majority of the shares voted by shareholders who have no personal interest in the transaction; or

- the total number of shares, other than shares held by the disinterested shareholders, that voted against the approval of the transaction does not exceed 2% of the aggregate voting rights of our company.

Generally, the approval of such a transaction may not be for more than three years. However, an extraordinary transaction, including a private placement with a controlling shareholder or in which a controlling shareholder has a personal interest that does not concern the terms of compensation or employment or engagement of a controlling shareholder or his or her relative, as an officer holder or employee of our company or as a service provider to the company, the transaction may be approved for a longer period if the audit committee determines that the approval of the transaction for a period of longer than three years is reasonable under the circumstances.

Duties of Shareholders

Under the Israeli Companies Law, a shareholder has a duty to act in good faith and in a customary manner towards the company and other shareholders, and to refrain from abusing his or her power in the company, including when voting in a shareholders meeting or in a class meeting on matters such as the following:

- An amendment to the company’s articles of association;
- An increase in the company’s authorized share capital;
- A merger; or
- Approval of related party transactions that require shareholder approval.

In addition, any controlling shareholder, any shareholder who knows that he or she possesses the power to determine the outcome of a shareholders meeting or a shareholders class meeting and any shareholder who has the power to prevent the appointment of an office holder, is under a duty to act with fairness towards the company. The Israeli Companies Law does not define the substance of this duty of fairness, except to state that the remedies generally available upon a breach of contract will also apply in the event of a breach of the duty to act with fairness, taking into account the position in the company of those who breached the duty of fairness.

Exculpation, Insurance and Indemnification of Directors and Officers

Indemnification of Office Holder

Our articles of association provide that, to the extent permitted by the Israeli Companies Law, we may indemnify our office holders for the following liabilities or expenses incurred by an office holder as a result of an act done by him or her in his or her capacity as an office holder:

- a financial liability imposed on him or her in favor of another person by a court judgment, including a settlement, judgment or an arbitrator’s award approved by a court;

- reasonable costs of litigation, including attorney’s fees, expended as a result of an investigation or proceeding instituted against the office holder by a competent authority, provided that such investigation or proceeding was concluded without the filing of an indictment against the office holder or the imposition of any financial liability in lieu of criminal proceedings, or was concluded without the filing of an indictment against the office holder and a financial liability was imposed on the office holder in lieu of criminal proceedings with respect to a criminal offense in which proof of criminal intent is not required or in connection with a financial sanction; and

- reasonable litigation expenses, including attorneys’ fees, expended by an office holder or charged to him or her by a court, in a proceeding filed against him or her by the company or on its behalf or by another person, or in a criminal charge from which he or she was acquitted, or in a criminal charge of which he or she was convicted of a crime which does not require a finding of criminal intent.

- a financial obligation imposed upon an Office Holder and reasonable litigation expenses, including attorney fees, expended by the Office Holder as a result of an administrative proceeding instituted against him. Without derogating from the generality of the foregoing, such obligation or expense will include a payment which the Office Holder is obligated to make to an injured party as set forth in Section 52(54)(a)(1)(a) of the Securities Law, and expenses that the Office Holder incurred in connection with a proceeding under Chapters H'3, H'4 or I'1 of the Securities Law, including reasonable legal expenses, which term includes attorney fees.

The Israeli Companies Law and our articles of association provide that, subject to certain limitations, we may undertake to indemnify an office holder of the company retrospectively, and may also undertake in advance to indemnify an office holder of the company, provided the undertaking is limited to events which the board of directors believes can be anticipated at the time of such undertaking, in light of the company’s activities as conducted at such time and is in an amount or based on criteria that the board of directors determines is reasonable under the circumstances and, provided, further, that such undertaking lists the events which the board of directors believes can be anticipated in light of the company’s activities as conducted at such time, and the amount or criteria that the board determines is reasonable under the circumstances.

Insurance of Office Holders

Our articles of association provide that, to the extent permitted by the Israeli Companies Law, we may obtain insurance to cover any liabilities imposed on an office holder as a result of an act done by him or her in his or her capacity as an office holder, in any of the following:

- a breach of his or her duty of care to us or to another person;
- a breach of his or her duty of loyalty to us, provided that he or she acted in good faith and had reasonable grounds to assume that his or her act would not prejudice us; and
- any financial liability imposed upon him or her in favor of another person.
- a payment which the Office Holder is obligated to make to an injured party as set forth in Section 52(54)(a)(1)(a) of the Securities Law and expenses that the Office Holder incurred in connection with a proceeding under Chapters H'3, H'4 or I'1 of the Securities Law, including reasonable legal expenses, which term includes attorney fees.

Exculpation of Office Holders

In addition, our articles of association provide that, to the extent permitted by the Israeli Companies Law, we may exculpate an office holder in advance from liability, in whole or in part, for damages resulting from a breach of his or her duty of care to us.

Limitations on Exculpation, Indemnification and Insurance

These provisions are specifically limited in their scope by the Israeli Companies Law, which provides that a company may indemnify or insure an office holder against a breach of duty of loyalty only to the extent that the office holder acted in good faith and had reasonable grounds to assume that the action would not prejudice the company. In addition, a company may not indemnify, insure or exculpate an office holder against a breach of duty of care if committed intentionally or recklessly (excluding mere negligence), or committed with the intent to derive an unlawful personal gain, or for a fine or forfeit levied against the office holder in connection with a criminal offense.

We have obtained directors' and officers' liability insurance for the benefit of our office holders to the full extent permitted by the Israeli Companies Law.

We entered into indemnification agreements with each of our directors and office holders in the form approved by our audit committee, board of directors and shareholders. The indemnification agreements provide that we will indemnify an office holder for any expenses incurred by the office holder in connection with any claims (as these terms are defined in the agreement) that fall within one or more categories of indemnifiable events listed in the agreement, related to any act or omission of the office holder and director while serving as our office holder (or serving or having served, at our request, as an employee, consultant, office holder or agent of any of our subsidiaries, or any other corporation or partnership). In addition, under these agreements, we exempt and release our office holders from any and all liability to us related to any breach by them of their duty of care to us, to the maximum extent permitted by law.

D.EMPLOYEES –

As of December 31, 2011, we had 542 employees, of whom 225 were engaged in research and development, 46 in operations, 212 in sales and marketing, and 59 in administration and management.

Of our full-time employees, as of December 31, 2011, 361 were located in Israel, 23 in the United States and 158 at our other branch offices, which offices are listed in "Item 4—Information on the Company—Organizational Structure."

As of December 31, 2010, we had 715 employees, of whom 286 were engaged in research and development, 84 in operations, 280 in sales and marketing, and 65 in administration and management. Of our full-time employees, as of December 31, 2010, 429 were located in Israel, 43 in the United States and 243 at our other branch offices, which offices are listed in "Item 4—Information on the Company—Organizational Structure."

As of December 31, 2009, we had 877 employees, of whom 394 were engaged in research and development, 110 in operations, 306 in sales and marketing, and 68 in administration and management. Of our full-time employees, as of December 31, 2009, 566 were located in Israel, 42 in the United States and 269 at our other branch offices.

We consider our relations with our employees to be good and have never experienced any strikes or work stoppages. Substantially all of our employees have employment agreements, and none are represented by a labor union.

We are subject to labor laws and regulations in Israel and in other countries where our employees are located. Although our Israeli employees are not parties to any collective bargaining agreement, we are subject to certain provisions of collective bargaining agreements among the Government of Israel, the General Federation of Labor in Israel and the Coordinating Bureau of Economic Organizations, including the Industrialists' Association, that are applicable to our Israeli employees by virtue of expansion orders of the Israeli Ministry of Industry, Trade and Labor. Israeli labor laws are applicable to all of our employees in Israel. Those provisions and laws principally concern the length of the work day, minimum daily wages for workers, procedures for dismissing employees, determination of severance pay and other conditions of employment.

We contribute funds on behalf of our employees to an individual insurance policy known as Managers' Insurance. This policy provides a combination of savings plan, insurance and severance pay benefits to the insured employee. It provides for payments to the employee upon retirement or death and secures a substantial portion of the severance pay, if any, to which the employee is legally entitled upon termination of employment. Each participating employee contributes an amount equal to 5% of such employee's base salary, and we contribute between 13.83% and 15.83% of the employee's base salary. Employees are also entitled, instead of or combined with the Manager's Insurance above, to a pension fund to which the employee contributes an amount ranging from 5% to 5.5% of such employee's base salary, and we contribute an amount equal to 14.83% of the employee's base salary. We also provide our employees with an Education Fund, to which each participating employee contributes an amount equal to 2.5% of the employee's base salary, and we contribute an amount of up to 7.5% of the employee's base salary. Both of the above contributions are limited to maximum amounts promulgated under the Israeli tax regulations which are tax exempt. We also provide our employees with additional health insurance coverage for instances of severe illnesses. Outside of Israel, we offer alternative local plans of pension, health insurance, and social security as provided under the applicable laws in such jurisdictions.

As an Israeli employer, Israeli law requires us to provide salary increases as partial compensation for increases in the Israeli consumer price index or as set by local law. Employees and employers also are required to pay predetermined sums, which include a contribution to provide a range of social security benefits.

Management Employment Agreements

We maintain written employment agreements with substantially all of our key employees. These agreements provide, among other matters, for monthly salaries, our contributions to Managers' Insurance or Pension Fund and an Education Fund, and severance benefits. All of our agreements with our key employees are subject to termination by either party upon the delivery of notice of termination as provided therein.

E.SHARE OWNERSHIP –

The following table sets forth certain information as of March 31, 2012 for (i) each of our executive officers and directors that beneficially owns more than 1% of our outstanding ordinary shares and (ii) our executive officers and directors as a group. The information in the table below is based on 62,403,424 ordinary shares outstanding as of March 31, 2012. Each of our outstanding ordinary shares has identical rights in all respects.

Name	Number of Ordinary Shares (1)	Percentage of Outstanding Ordinary Shares
Amnon Yacoby (2)	809,579	1.30 %
All directors and members of senior management as a group (15 persons)(3)	4,016,709	6.11 %

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(1) The number of ordinary shares beneficially owned includes the shares issuable pursuant to options that are exercisable within 60 days of March 31, 2012. Shares issuable pursuant to such options are deemed outstanding for computing the percentage of the person holding such options but are not outstanding for computing the holding percentage of any other person.

(2) Includes options to purchase 85,000 of our ordinary shares which are exercisable within 60 days of March 31, 2012. The options have a weighted exercise price of $6.14 with expiration dates ranging from May 8, 2012 until December 21, 2021.

(3) Includes options to purchase 3,291,130 of our ordinary shares which are exercisable within 60 days of March 31, 2012.

Except as set forth in the table above, none of our other directors or members of senior management listed above under "—Directors and Senior Management" held more than 1% of our outstanding shares as of March 31, 2012.

As of March 31, 2012, our directors and members of senior management who are currently engaged with the Company as listed above under "—Directors and Senior Management", as a group, held options to purchase 4,536,877 of our ordinary shares at a weighted average exercise price of $4.70 with expiration dates ranging from May 08, 2012 until December 21, 2021. The voting rights of our directors and members of senior management do not differ from the voting rights of other holders of our ordinary shares.

Equity Incentive Plans –

As of December 31, 2011, a total of 34,886,495 ordinary shares have been reserved for issuance upon exercise of options granted to our employees, officers, directors and consultants pursuant to our share option plans. These ordinary shares have been reserved pursuant to our 2006 Global Share Based Incentive Plan (the "2006 Plan"), 2002 Global Share Option Plan (the "2002 Plan"), Key Employee Share Incentive Plan (1994), as amended, Key Employee Share Incentive Plan (1996), Key Employee Share Incentive Plan (1997), 1999 U.S. Stock Option Plan, interWAVE's 1994 Stock Option Plan, interWAVE's 1999 Stock Option Plan and Floware's Key Employee Share Incentive Plan (1996).

Options granted under the share option plans usually vest over a period of four years.

As of December 31, 2011, options to purchase 9,313,328 of our ordinary shares were outstanding under the share option plans, including options issued pursuant to the terms of the Floware merger and interWAVE amalgamation, at a weighted average exercise price of $4.83 per share. Unless a shorter period is specified in the notice of grant or unless the applicable share option plan has an earlier termination date, each of the outstanding options to purchase 9,313,328 of our ordinary shares expire between six and ten years from the date of grant. As of December 31, 2011, options to purchase 9,212,839 of our ordinary shares were available for issuance under the share option plans.

Pursuant to our 2006 Plan we may grant restricted share units, restricted shares, options and other equity awards to employees, directors, consultants, advisers and service providers of our Company and its subsidiaries. Initially, 1,500,000 ordinary shares were reserved for issuance upon the exercise of awards granted under the 2006 Plan. The number of ordinary shares available for issuance under the 2006 Plan is reset annually on April 1 of each year to equal 4% of our total outstanding shares as of the applicable reset date. As of December 31, 2011, options to purchase 5,968,196 of our ordinary shares were outstanding under the 2006 Plan.

The share option plans are administered by the board of directors which designates the optionees, dates of grant, vesting period and the exercise price of options. Each grantee is responsible for all personal tax consequences of the grant and the exercise of the options. Unless otherwise approved by our board of directors, employees usually may exercise vested options granted under the share option plans for a period of three months following the date of termination of their employment with us or any of our subsidiaries and options that have not vested on the date of termination expire. Under Israeli law, the issuance of options must be approved by our board of directors and the issuance of options to directors must be approved by the shareholders.

ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A.MAJOR SHAREHOLDERS -

As of March 31, 2012, we were not aware of any person who beneficially owned 5% or more of our outstanding ordinary shares. Each of our outstanding ordinary shares has identical rights in all respects.

Based on a review of the information provided to us by our transfer agent, as March 31, 2012, there were 58 holders of record of our ordinary shares, including 43 holders of record with a U.S. mailing address, including banks, brokers and nominees. As of March 31, 2012, these 43 holders of record with a U.S. mailing address held approximately 65,119,715 ordinary shares, representing approximately 96% of the aggregate 67,650,196 ordinary shares outstanding as of such date (excluding our treasury stock). Because these holders of record include banks, brokers and nominees (including one U.S. nominee company, CEDE & Co., which held approximately 96% of our outstanding ordinary shares as of such date), the beneficial owners of these ordinary shares may include persons who reside outside the United States.

To the best of our knowledge, we are not directly or indirectly owned or controlled by another corporation, by any foreign government or by any other natural or legal person or persons severally or jointly and currently there are no arrangements that may, at a subsequent date, result in a change in our control.

B.RELATED PARTY TRANSACTIONS

None.

C.INTERESTS OF EXPERTS AND COUNSEL

Not applicable.

ITEM 8. FINANCIAL INFORMATION FINANCE

A.CONSOLIDATED STATEMENTS AND OTHER FINANCIAL INFORMATION

The Financial Statements required by this item can be found at the end of this Annual Report, beginning on page F-1.

Legal Proceedings –

Initial Public Offering Securities Litigation.

On November 21, 2001, a purported Class Action lawsuit ("the Action") was filed against interWAVE (which merged into the Company in 2003), certain of its former officers and directors, and certain of the underwriters for interWAVE's initial public offering ("the IPO"). On April 19, 2002, the plaintiffs filed an amended complaint. The amended complaint alleged that the prospectus from interWAVE's IPO failed to disclose certain alleged improper actions by various underwriters for the offering, in violation of the Securities Act of 1933, as amended and the Securities Exchange Act of 1934, as amended ("the Exchange Act"). Similar complaints have been filed concerning more than 300 other IPOs; all of these cases have been coordinated as In re Initial Public Offering Securities Litigation, 21 MC 92. On October 8, 2002, the Court entered an Order of Dismissal as to all of the individual defendants in the IPO litigation, without prejudice. In 2007, a settlement that had been pending with the Court since 2004,was terminated by stipulation. After a ruling by the Second Circuit Court of Appeals in six "focus" cases in the coordinated proceedings (interWAVE is not one of the six test cases) made it unlikely that the settlement would receive final Court approval plaintiffs filed amended master allegations and amended complaints in the six test cases. In 2008, the Court denied the defendants' motion to dismiss the amended complaints.

This action has been resolved through a global settlement of the coordinated litigation. Under the settlement, the insurers pay the full amount of the settlement share allocated to the Company, and the Company bears no financial liability. InterWAVE, as well as the officer and director defendants who were previously dismissed from the Action pursuant to tolling agreements, have received complete dismissals from the case. On October 5, 2009, the Court entered an order granting final approval of the settlement. Although certain objectors filed appeals, by early 2012 all of those appeals had been withdrawn or dismissed and the settlement is now final.

Export Sales

Export sales constitute a significant portion of our sales. In 2011, export sales were approximately $189 million, constituting approximately 99.5% of our total sales. For a more detailed discussion regarding the allocation of our revenues by geographic regions based on the location of our customers, see “Item 5—Operating and Financial Review and Prospects—Operating Results.”

Dividend Policy

We have never declared or paid any cash dividend on our ordinary shares. We do not anticipate paying any cash dividend on our ordinary shares in the foreseeable future. We currently intend to retain all future earnings to finance operations and expand our business.

B.SIGNIFICANT CHANGES

Except as otherwise disclosed in this Annual Report, no significant change has occurred since December 31, 2011.

ITEM 9.THE OFFER AND LISTING

A.OFFER AND LISTING DETAILS

The following table sets forth the high and low sales prices for our ordinary shares as reported by the NASDAQ Global Select Market, in U.S. dollars, and as reported by the Tel Aviv Stock Exchange, in NIS, for each of the last five years:

	NASDAQ Global Select Market		Tel Aviv Stock Exchange	
Year	High	Low	High	Low
2007	$15.21	$ 6.03	NIS 59.76	NIS 26.54
2008	$9.69	$ 2.54	NIS 37.50	NIS 10.05
2009	$4.80	$2.36	NIS 19.00	NIS 10.23
2010	$4.28	$1.79	NIS 15.59	NIS 6.78
2011	$2.62	$0.83	NIS 9.24	NIS 3.10

The following table sets forth, for each of the full financial quarters in the years indicated, the high and low sales price for our ordinary shares as reported by the NASDAQ Global Select Market, in U.S. dollars, and as reported by the Tel Aviv Stock Exchange, in NIS:

	NASDAQ Global Select Market		Tel Aviv Stock Exchange	
2010	High	Low	High	Low
First Quarter	$ 4.28	$3.49	NIS 15.59	NIS 13.15
Second Quarter	$4.07	$2.00	NIS 14.96	NIS 7.60
Third Quarter	$2.36	$1.79	NIS 8.81	NIS 7.00
Fourth Quarter	$2.76	$1.84	NIS 10.44	NIS 6.78
2011	High	Low	High	Low
First Quarter	$2.62	$1.71	NIS 9.24	NIS 5.94
Second Quarter	$1.89	$1.15	NIS 6.48	NIS 4.00
Third Quarter	$1.67	$1.04	NIS 5.71	NIS 3.99
Fourth Quarter	$1.22	$0.83	NIS 4.27	NIS 3.10
2012	High	Low	High	Low
First Quarter	$1.27	$0.91	NIS 4.58	NIS 3.41

The following table sets forth the high and low sales price for our ordinary shares as reported by the NASDAQ Global Select Market, in U.S. dollars, and the Tel Aviv Stock Exchange, in NIS, for the most recent six months:

	NASDAQ Global Select Market		Tel Aviv Stock Exchange	
Month	High	Low	High	Low
October 2011	$1.22	$0.94	NIS 4.27	NIS 3.45
November 2011	$1.09	$0.83	NIS 3.97	NIS 3.14
December 2011	$1.03	$0.84	NIS 3.99	NIS 3.10
January 2012	$1.23	$0.94	NIS 4.55	NIS 3.45
February 2012	$1.27	$1.01	NIS 4.58	NIS 3.85
March 2012	$1.01	$0.91	NIS 3.82	NIS 3.41

As of March 31, 2012, the exchange rate of the NIS to the US$ was $1 to NIS3.715.

B.PLAN OF DISTRIBUTION

Not applicable.

C.MARKETS –

Our ordinary shares began trading on the NASDAQ Global Market on March 23, 2000 under the symbol "BRZE". Prior to that date, there was no market for our ordinary shares. On August 1, 2001, upon the completion of our merger with Floware and the change of our name to Alvarion Ltd., our symbol was changed to "ALVR". On August 1, 2001, our ordinary shares also began to trade on the Tel Aviv Stock Exchange. As of the date of this Annual Report, our ordinary shares trade on both the NASDAQ Global Select Market and the Tel Aviv Stock Exchange under the symbol "ALVR".

D.SELLING SHAREHOLDERS

Not applicable.

E.DILUTION

Not applicable.

F.EXPENSES OF THE ISSUE

Not applicable.

ITEM 10.ADDITIONAL INFORMATION -

A.SHARE CAPITAL

Not applicable.

B.MEMORANDUM AND ARTICLES OF ASSOCIATION –

We are registered under the Israel Companies Law as a public company with the name Alvarion Ltd. Our registration number with the Israeli Registrar of Companies is 51-172231-6.

The following is a summary description of certain provisions of our Memorandum of Association and Articles of Association.

Our Articles of Association permit us to engage in any lawful business. Our purpose, as set forth in Article 3 of our Articles of Association, is to operate in accordance with business considerations to generate profits (provided, however, that we may donate reasonable amounts to worthy causes, as our board of directors may determine in its discretion, even if such donations are not within the framework of business considerations).

Our Articles of Association permit us to enter into a business transaction with any of the directors of our Company or enter into a business transaction with a third party in which a director has a personal interest, subject to compliance with the Israeli Companies Law.

Our board of directors may, from time to time, in its discretion, cause us to borrow or secure the payment of any sum or sums of money for our purposes, on such terms and conditions as it deems appropriate.

Our authorized share capital consists of 120,080,000 ordinary shares, par value NIS 0.01 per share.

Shareholders are entitled to receive dividends or bonus shares, upon the recommendation of our board of directors and resolution of our shareholders. The shareholders entitled to receive dividends or bonus shares are those who are registered in the shareholders register on the date of the resolution approving the distribution or allotment, or on such later date, as may be determined in such resolution. Any right to a declared dividend by us to our shareholders terminates after seven years from our declaration of the dividend if such dividend has not been claimed by the shareholder within such time. After seven years, the unclaimed dividend will revert back to us.

Every shareholder has one vote for each share held by such shareholder of record. With certain exceptions, no shareholder is entitled to vote at any general meeting (or be counted as a part of the lawful quorum thereat), unless all calls and other sums then payable in respect of his shares have been paid.

A shareholder seeking to vote with respect to a resolution that requires that the majority of such resolution's adoption include at least a certain percentage of all those not having a personal interest (as defined in the Israeli Companies Law) in it, must notify us at least two business days prior to the date of the general meeting, whether or not he has a personal interest in the resolution, as a condition for his right to vote and be counted with respect to such resolution.

Upon our liquidation, the liquidator, with the approval of a general meeting of the shareholders, may distribute all or part of the property to our shareholders, and may deposit any part of such property with trustees in favor of the shareholders, as deemed appropriate by the liquidator.

Rights attached to our ordinary shares may be modified or abrogated by a resolution adopted at a general meeting of the shareholders by more than 50% of the issued shares of such a class, or an "ordinary majority," other than certain rights relating to the election of directors and liquidation that may be modified or abrogated only with the approval of more than 75% of the shareholders who are entitled to vote at the meeting.

An annual general meeting of our shareholders, or "annual meeting," must be held once in every calendar year, within a period of not more than 15 months from the preceding annual meeting, either within or outside of Israel. All general meetings of our shareholders other than annual meetings are called "extraordinary meetings." Our board of directors has discretion over when to convene an extraordinary meeting. However, our board of directors must convene an extraordinary meeting upon demand by: (i) the lesser of any two directors of our Company; or a quarter of the directors of our Company; or (ii) upon the demand of one or more shareholders holding alone or together at least (a) 5% of the issued share capital of our Company and 1% of the voting rights or (b) 5% of the voting rights. Our board of directors, upon demand to convene an extraordinary meeting, is required to announce the convening of the meeting within 21 days from the receipt of the demand, provided, however, that the date fixed for the extraordinary meeting may not be more than 35 days from the publication date of the announcement of the extraordinary meeting, or such other period as may be permitted by the Israeli Companies Law or the regulations thereunder.

Directors, other than external directors, are elected, and hold office from the close of the annual general shareholders' meeting at which they are elected, unless a later date is stated, until the third annual general shareholders' meeting following the meeting at which such directors were elected. See "Item 6 – Directors, Senior Management and Employees – Board Practices". Any director may be removed from office by way of a resolution adopted by the vote of the holders of 75% of the voting power represented at a meeting.

The shareholders who are entitled to participate and vote at a general meeting are those shareholders who are registered in our shareholders register on the date determined by our board of directors, provided that such date not be more than 40 days, nor less than 4 days prior to the date of the general meeting, except as otherwise permitted by the regulations under the Israeli Companies Law. Shareholders entitled to attend a general meeting are entitled to receive notice of such meeting at least 21 days prior to the date fixed for such meeting (or at least 35 days for those cases prescribed under the Israeli Companies Law).

The quorum required for a meeting of shareholders consists of at least two shareholders present in person or by proxy holding at least 33 1⁄3% of the voting power. A meeting adjourned for lack of a quorum will be adjourned to the same day in the next week at the same time and place, or any other time and place as the chairman of our board of directors may determine with the consent of the holders of a majority of the voting power represented at the meeting in person or by proxy. At the reconvened meeting, the required quorum consists of any two shareholders. The chairman of the board of directors presides as chairman at each of our shareholders meetings. The chairman of the meeting has neither an additional nor a casting vote.

There are no limitations imposed by our Articles of Association or the Israeli Companies Law on the right to own our shares including the rights of non-resident or foreign shareholders to hold or exercise voting rights of our shares, except with respect to subjects of countries which are in a state of war with Israel.

Certain provisions of Israeli corporate and tax law may have the effect of delaying, preventing or making more difficult a merger or other acquisition of our Company, as detailed in "Item 3—Key Information—Risk Factors—Risks Related to Our Location in Israel". Provisions of Israeli law may delay, prevent or make difficult a merger with or an acquisition of us, which could prevent a change of control and therefore depress the market price of our ordinary shares.

For example, the Israeli Companies Law provides that certain ownership thresholds in public companies may be crossed only by means of a tender offer made to all shareholders. A purchaser must conduct a special tender offer in order to purchase shares in publicly held companies if, as a result of the purchase, the purchaser would hold 25% or more of the voting rights of a company in which no other shareholder holds 25% or more of the voting rights, or the purchaser would hold more than 45% of the voting rights of a company in which no other shareholder holds more than 45% of the voting rights. A special tender offer is not required if: (i) the shares are acquired in a private placement that is approved by the shareholders with the knowledge that as a result the purchaser would hold more than 25% or 45% of the voting rights, as applicable, (ii) the purchaser reaches the 25% threshold by purchasing shares from a shareholder who held 25% or more of the voting rights immediately prior to the transaction, or (iii) the purchaser crosses the 45% threshold by purchasing shares from a shareholder who held more than 45% of the voting rights immediately prior to the transaction.

Under the Israeli Companies Law, a person may not purchase shares of a public company if, following the purchase, the purchaser would hold more than 90% of the company's shares or of any class of shares, unless the purchaser makes a tender offer to purchase all of the target company's shares or all the shares of the particular class, as applicable. If, as a result of the tender offer, either:

- the purchaser acquires more than 95% of the company's shares or a particular class of shares and a majority of the shareholders that did not have a personal interest accepted the offer; or
- the purchaser acquires more than 98% of the company's shares or a particular class of shares;

then, the purchaser automatically acquires ownership of the remaining shares. However, if the purchaser is unable to purchase more than 95% or more than 98%, as applicable, of the company's shares or class of shares, the purchaser may not own more than 90% of the shares or class of shares of the target company.

In addition, the Israeli Companies Law requires the parties to a proposed merger to file a merger proposal with the Israeli Registrar of Companies, specifying certain terms of the transaction. Each merging company's board of directors and shareholders must approve the merger. Shares in one of the merging companies held by the other merging company or certain of its affiliates are disenfranchised for purposes of voting on the merger. A merging company must inform its creditors of the proposed merger. Any creditor of a party to the merger may seek a court order blocking the merger, if there is a reasonable concern that the surviving company will not be able to satisfy all of the obligations of the parties to the merger. Moreover, a merger may not be completed until at least 50 days have passed from the time that the merger proposal was filed with the Israeli Registrar of Companies and at least 30 days have passed from the approval of the shareholders of each of the merging companies.

Our transfer agent and registrar is American Stock Transfer & Trust Company at 59 Maiden Lane, New York, New York 10038.

For additional information, see "Item 6—Directors, Senior Management and Employees—Board Practices."

C.MATERIAL CONTRACTS

1. Loan and Security Agreement with Silicon Valley Bank

On June 21, 2011, the Company entered into the Long Term Loan with SVB, whereby SVB provided a $30 million loan for the financing of the Wavion acquisition. As part of the transaction, the Company pledged all of its assets under a floating charge, and created a fixed charge on its IP rights and receivables. The Long Term Loan contains various provisions related to compliance with financial covenants, restrictive covenants, including negative pledges, and other customary commitments, contained in credit facility agreements of this type. The Long Term Loan amount consists of Facility A $25 million and Facility B $5 million.

Facility A will be repaid in thirty six (36) equal monthly installments each commencing on March 1st, 2012. The interest rate applicable to Facility A is LIBOR plus 4.75%, payable monthly starting December 1, 2011.

Facility B will be repaid in one (1) installment after thirty six (36) months following drawdown of the Long Term Loan. The interest rate applicable to Facility B is LIBOR plus 4.50%, payable monthly starting December 1, 2011.

As of April 1st, 2012 the Company was in breach of certain financial covenants set forth in the Long Term Loan but on April 25, 2012, it reached a general agreement with SVB for the grant of a temporary forbearance of the breached covenants and a modification of the terms of the Long Term Loan, which terms include (i) an increase of the interest rate applicable to Facility A and Facility B to LIBOR plus 5.85% and (ii) the repayment of approximately $7,000,000 of principal on the Long Term Loan in addition to its normal loan payments by July 2012.

Following the early repayment described above, the current outstanding balance under the Long Term Loan will be approximately US$ 20 million.

2. Acquisition of Wavion Inc.

In November 2011, the Company completed its purchase of 100% of the outstanding common shares of Wavion, Inc., for the sum of $28.4 million in cash, including the payment of an earn-out. Wavion is a provider of carrier grade outdoor Wi-Fi solutions, offering a variety of different products for Wi-Fi access and 3rd Generation cellular technologies (“3G”) off-load applications.

D.EXCHANGE CONTROLS

Non-residents of Israel who own our ordinary shares may freely convert all amounts received in Israeli currency in respect of such ordinary shares, whether as a dividend, liquidation distribution or as proceeds from the sale of the ordinary shares, into freely-repatriable non-Israeli currencies at the rate of exchange prevailing at the time of conversion (provided in each case that the applicable Israeli income tax, if any, is paid or withheld).

Since January 1, 2003, all exchange control restrictions on transactions in foreign currency in Israel have been eliminated, although there are still reporting requirements for foreign currency transactions. Legislation remains in effect, however, pursuant to which currency controls may be imposed by administrative action at any time.

The State of Israel does not restrict in any way the ownership or voting of our ordinary shares by non-residents of Israel, except with respect to subjects of countries that are in a state of war with Israel.

E.TAXATION

General

The following is a discussion of Israeli and U.S. tax consequences material to our shareholders. To the extent that the discussion is based on new tax legislation that has not been subject to judicial or administrative interpretation, the views expressed in the discussion might not be accepted by the tax authorities in question. The discussion is not intended, and should not be construed, as legal or professional tax advice and does not exhaust all possible tax considerations.

Shareholders and potential investors are urged to consult their own tax advisors as to the Israeli or other tax consequences of the purchase, ownership and disposition of ordinary shares, including, in particular, the effect of any foreign, state or local taxes.

Israeli Taxation

The following is a summary of the principal Israeli tax laws applicable to companies in Israel, with special reference to their effect on us, and certain Israeli government programs benefiting us. This section also contains a discussion of certain Israeli tax consequences to persons acquiring ordinary shares. This summary does not discuss all the acts of Israeli tax law that may be relevant to a particular investor in light of his or her personal investment circumstances or to certain types of investors subject to special treatment under Israeli law, such as traders in securities or persons that own, directly or indirectly, 10% or more of our outstanding voting share capital. To the extent that the discussion is based on new tax legislation which has not been subject to judicial or administrative interpretation, there can be no assurance that the views expressed in this discussion will be accepted by the tax authorities. This discussion should not be construed as legal or professional tax advice and is not exhaustive of all possible tax considerations.

General Corporate Tax Structure

Income derived by Alvarion Ltd. is generally subject to the regular Israeli corporate tax rate.

Until December 31, 2003, the regular tax rate applicable to income of Israeli companies (which are not entitled to benefits due to “Approved Enterprise,” as described below) was 36%. In June 2004 and in July 2005, the “Knesset” (Israeli parliament) passed amendments to the Income Tax Ordinance (No. 140 and Temporary Provision), 2004 and (No. 147), 2005, respectively, which determined, among other things, that the corporate tax rate was to be gradually reduced to the following tax rates: 2007 - 29%, 2008 - 27%, 2009 - 26%, 2010 - 25% and 2011 – 24%.

In July 2009, the Knesset passed the Law for Economic Efficiency (Amended Legislation for Implementing the Economic Plan for 2009 and 2010), 2009, which prescribes, among others, an additional gradual reduction in the rates of the Israeli corporate tax and real capital gains tax starting 2011 to the following tax rates: 2011 - 24%.

In December 5, 2011, the Knesset (Israel's Parliament) passed a law for changing the tax burden (the Law), which cancels, among others, the gradual reduction in the corporate tax rates in Israel. In addition, the corporate tax in Israel will be increased to 25% starting in 2012. Accordingly, the real capital gains tax rate will increase to 25%. There was no effect on the Company as a result of the above mentioned changes.

However, as detailed below, income derived in Israel from certain “Approved Enterprises” will enjoy certain tax benefits for a specific definitive period. The allocation of income derived from approved enterprises is dependent upon compliance of certain requirements with the Investment Law.

Our effective corporate tax rate may substantially exceed the Israeli tax rate. Our US, France, Romania, Brazil, Hong-Kong, Singapore, Japan, Mexico, Poland, Uruguay, Spain, UK, South-Africa, Italy, Argentina, Ecuador, Costa Rica, India, Chile, Indonesia, Taiwan and Philippines subsidiaries will generally each be subject to applicable federal, state, local and foreign taxation, and we may also be subject to taxation in other jurisdictions where we own assets, have employees or conduct activities. Because of the complexity of these local tax provisions, it is not possible to anticipate the actual combined effective corporate tax rate that will apply to us.

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Tax Benefits under the Law for the Encouragement of Industry (Taxes), 1969 –

The Law for the Encouragement of Industry (Taxes), 1969, generally referred to as the Industry Encouragement Law, provides several tax benefits for industrial companies. An industrial company is defined as a company resident in Israel, at least 90% of the income of which in a given tax year exclusive of income from specified government loans, capital gains, interest and dividends, is derived from an industrial enterprise owned by it. An industrial enterprise is defined as an enterprise whose major activity in a given tax year is industrial production activity.

Under the Law for the Encouragement of Industry (Taxes), 1969 (the "Industry Encouragement Law"), Industrial Companies are entitled to the following preferred corporate tax benefits, among others:

- deduction of purchase of know-how and patents and/or right to use a patent over an eight-year period for tax purposes;
- accelerated depreciation rates on equipment at the first five tax years of using the equipment and buildings; and
- deduction over a three-year period of expenses involved with the issuance and listing of shares on the Tel Aviv Stock Exchange or, on or after January 1, 2003, on a recognized stock market outside of Israel.

Eligibility for benefits under the Industry Encouragement Law is not contingent upon the approval of any governmental authority.

We believe that we currently meet the criteria to qualify as an Industrial Company within the definition of the Industry Encouragement Law. No assurance can be given that we will continue to qualify as an Industrial Company, or will be entitled to receive any benefits under the Industry Encouragement Law in the future.

Tax Benefits under the Law for the Encouragement of Capital Investments, 1959 –

Tax Benefits prior to the 2005 Amendment

The Law for Encouragement of Capital Investments, 1959, as in effect prior to April 1, 2005 which is referred to below as the Capital Investments Law, provides that capital investments in a production facility or other eligible assets may, upon application to the Israeli Investment Center of the Ministry of Industry, Trade and Labor, be designated as an "Approved Enterprise". Each certificate of approval for an Approved Enterprise relates to a specific investment program in the Approved Enterprise, delineated both by the financial scope of the investment and by the physical characteristics of the facility or the asset. An Approved Enterprise is entitled to certain benefits, including Israeli government cash grants, state-guaranteed loans and tax benefits.

Taxable income derived from an Approved Enterprise under the Capital Investments Law is subject to a reduced corporate tax rate of 25%. That income is eligible for further reductions in tax rates depending on the percentage of the foreign investment in our share capital. The tax rate is 20% if the foreign investment is 49% or more but less than 74%, 15% if the foreign investment is 74% or more but less than 90%, and 10% if the foreign investment is 90% or more. The lowest level of foreign investment during the year will be used to determine the relevant tax rate for that year. These tax benefits are granted for a limited period not exceeding seven years, or 10 years for a company whose foreign investment level exceeds 25%, (the "benefits period") from the first year in which the Approved Enterprise has taxable income, after the year in which production commenced (the "commencement year") (as determined by the Israeli Investment Center of the Ministry of Industry, Trade and Labor, or the Investment Center). The period of benefits may in no event, however, exceed the lesser of 12 years from the year in which the production commenced (as determined by the Investment Center) or 14 years from the year of receipt the letters of approved of Approved Enterprise status (please note that the years limitation does not apply to the exemption period).

An Approved Enterprise may elect to forego any entitlement to the grants otherwise available under the Capital Investments Law and, in lieu of the foregoing, may participate in an "Alternative Benefits Program." Under the Alternative Benefits Program, a company's undistributed income derived from an Approved Enterprise will be exempt from corporate tax for a period of between two and 10 years from the commencement year, depending on the geographic location of the Approved Enterprise within Israel, and the company will be eligible for a reduced tax rate of 10%-25% for the remainder of the benefits period. There can be no assurance that the current benefit programs will continue to be available, or that we will continue to qualify for benefits under the current programs.

We believe that our capital investments qualify to receive tax benefits as an Approved Enterprise, however no assurance can be given that such investments will be approved as in fact qualifying for such tax benefits by the Israeli tax authorities. Additionally, no assurance can be given that we will, in the future, be eligible to receive additional tax benefits under this law. For a discussion of the risks our business and prospects for growth face in connection with tax benefits under Israeli law, see "Risk Factors—If we fail to comply with these conditions in the future, the tax benefits received could be canceled and we could be required to pay increased taxes in the future. We could also be required to refund tax benefits, with interest and adjustments for inflation based on the Israeli consumer price index" and "Risk Factors—We currently contemplate that a portion of our products will be manufactured outside of Israel. This could materially reduce the tax benefits to which we would otherwise be entitled. We cannot assure you that the Israeli tax authorities will not adversely modify the tax benefits that we could have enjoyed prior to these events."

We currently have Approved Enterprise programs under the Capital Investments Law, which to our belief, entitle us to certain tax benefits. The tax benefit period for these programs has not yet commenced. We have elected the Alternative Benefits Program which provides for the waiver of grants in return for tax exemption. Accordingly, our income is tax exempt for a period of two years commencing with the year we first earn taxable income relating to each expansion program, and is subject to corporate taxes at the reduced rate of 10% to 25%, for an additional period of five to eight years, depending on the percentage of the company's ordinary shares held by foreign shareholders in each taxable year. The exact rate reduction is based on the percentage of foreign ownership in each tax year. See note 12 to our consolidated financial statements. A company that has elected to participate in the Alternative Benefits Program and that subsequently pays a dividend out of the income derived from the Approved Enterprise during the tax exemption period will be subject to corporate tax in respect of the gross amount distributed, including withholding tax thereon, at the rate that would have been applicable had the company not elected the Alternative Benefits Program, ranging from 10% to 25%. The dividend recipient is subject to withholding tax at the reduced rate of 15%, applicable to dividends from Approved Enterprises if the dividend is distributed within 12 years after the benefits period. The withholding tax rate will be 25% after such period as described below.

From time to time, the Israeli government has discussed reducing the benefits available to companies under the Capital Investments Law. The termination or substantial reduction of any of the benefits available under the Capital Investments Law could materially impact the cost of our future investments.

The benefits available to an Approved Enterprise are conditional upon the fulfillment of certain conditions stipulated in the Capital Investments Law and its regulations and the criteria set forth in the specific certificate of approval, as described above. In the event that these conditions are violated, in whole or in part, we might be required to refund the amount of tax benefits, together with linkage differences to the Israeli CPI and interest. We believe that our Approved Enterprise programs operate in compliance with all such conditions and criteria.

Amendments to the Law for the Encouragement of Capital Investments, 1959:

In December 2010, the "Knesset" (Israeli Parliament) passed the Law for Economic Policy for 2011 and 2012 (Amended Legislation), 2011, which prescribes, among other things, amendments in the Law for the Encouragement of Capital Investments, 1959 ("the Law"). The amendment became effective as of January 1, 2011. According to the amendment, the benefit tracks in the Law were modified and a flat tax rate applies to the Company's entire preferred income. The Company will be able to elect to apply the amendment (the waiver is irrevocable) and from then on we will be subject to the amended tax rates that are: 2011 and 2012 - 15% (in development area A - 10%), 2013 and 2014 - 12.5% (in development area A - 7%) and in 2015 and thereafter - 12% (in development area A - 6%).

Foreign investor’s Company (“FIC”) –

A company that has an approved enterprise program is eligible for further tax benefits if it qualifies as a foreign investors’ company. A foreign investors company is a company which more than 25% of its share capital and combined share and loan capital is owned by non-Israeli residents. A company that qualifies as a foreign investors’ company and has an approved enterprise program is eligible for tax benefits for a ten-year benefit period. As specified above, depending on the geographic location of the approved enterprise within Israel, income derived from the approved enterprise program may be entitled to the following:

- Exemption from tax on its undistributed income up to ten years.
- An additional period of reduced corporate tax liability at rates ranging between 10% and 25%, depending on the level of foreign (i.e., non-Israeli) ownership of our shares. Those tax rates and the related levels of foreign investment are as set forth in the following table:

Rate of Reduced Tax	Reduced Tax Period	Tax Exemption Period	Percent of Foreign Ownership
25	5 years	2 years	0-25%
25	8 years	2 years	25-48.99%
20	8 years	2 years	49-73.99%
15	8 years	2 years	74-89.99%
10	8 years	2 years	90-100%

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- The twelve years limitation period for reduced tax rate of 15% on dividend from the approved enterprise does not apply to Foreign Investor's Company.

Tax Benefits under the 2005 Amendment

On April 1, 2005, an amendment to the Investment Law went into effect (the "2005 Amendment"). As a result of the 2005 Amendment, a company is no longer obliged to acquire Approved Enterprise status in order to receive the tax benefits previously available under the Alternative Benefits provisions, and therefore generally there is no need to apply to the Investment Center for this purpose (Approved Enterprise status remains mandatory for companies seeking grants). Rather, the Company may claim the tax benefits offered by the Investments Law directly in its tax returns, provided that its facilities meet the criteria for tax benefits set out by the Amendment. A company is also granted a right to approach the Israeli Tax Authority for a pre-ruling regarding their eligibility for benefits under the Amendment. Among other things, the 2005 Amendment provides tax benefits to both local and foreign investors and simplifies the approval process. The period of tax benefits for a new Privileged Enterprise begins in the "Year of Commencement." This year is the later of (i) the year in which taxable income is first generated by a company, or (ii) a year selected by the company for commencement, on the condition that the company meets certain provisions provided by the Investment Law (Year of Election). The 2005 Amendment does not apply to investment programs approved prior to December 31, 2004. The new tax regime applies to new investment programs only. Therefore, our existing Approved Enterprises will not be subject to the provisions of the 2005 Amendment.

The Company's Tax Benefits Prior the Amendment –According to the provision of the law, we have elected the "alternative benefits" track provisions of the Investment Law, pursuant to which we have waived our right to grants and instead receive a tax benefit on undistributed income derived from the "Approved Enterprise" program. The tax benefits under the Investment Law may not be available with respect to income derived from products developed and manufactured outside of Israel or developed or manufactured in Israel but outside of the Approved Enterprises mentioned above and may be affected by the current location of our facilities in Israel. The relative portion of taxable income that should be allocated to each Approved Enterprise and expansion is subject to the fulfillment of covenants with the tax authorities.

Several of our facilities have been granted Approved Enterprise status:

(i) Nazareth Facilities: On December 31, 1997, our production facilities in Nazareth were granted Approved Enterprise status. Subject to compliance with applicable requirements, the income derived from the Nazareth Approved Enterprise is tax exempt for a period of 10 years from the commencement year.

(ii) Status Expansion of Nazareth and Migdal Ha-emek: In 2000, we received approval of our application for an expansion of our Approved Enterprise status with respect to our Nazareth facility. This expansion included, among other things, our Carmiel facility, which during 2004 was relocated to Migdal Ha-emek. The income derived from this Approved Enterprise is tax-exempt for a period of 10 years from the commencement year. The relative portion of taxable income that should be exempt for a 10-year period is subject to final covenants with the tax authorities.

(iii) Or Yehuda / Tel Aviv Facilities: In 1997, Floware submitted a request for Approved Enterprise status of its production facility in Or Yehuda. This request was approved. After the merger, Floware's enterprise was relocated into our facilities in Tel Aviv. The income derived from this Approved Enterprise is tax exempt for a period of two years and thereafter will be subject to a reduced tax rate between 10% and 25% for an additional period of five to eight years depends on the percentage of the non-Israeli holders of our share capital. The period of benefits will commence with the first year that we earn taxable income after the commencement year. The period of benefits for this plan has expired in 2011. Please note that the year limitation does not apply to the exemption period.

In order to maintain eligibility for the above programs and benefits, we must meet specified conditions stipulated by the Investment Law, regulations published there-under and the letters of approval for the specific investments in “Approved Enterprises.” In the event of failure to comply with these conditions, any benefits that were previously granted may be canceled, and we may be required to refund the amount of the benefits, in whole or in part, including interest and CPI adjustments.

If these retained tax-exempt profits are distributed they would be taxed at the corporate tax rate applicable to such profits as if we had not elected the alternative system of benefits, currently between 10% - 25% for an “Approved Enterprise.” As of December 31, 2011, our accumulated deficit does not include tax-exempt profits earned by our “Approved Enterprise.”

The Company's Tax Benefits under the Amendment –On April 1, 2005, an amendment to the Investment Law came into effect (the "Amendment”) and has significantly changed the provisions of the Investment Law. The Amendment limits the scope of enterprises that may be approved by the Investment Center. The Investment Center is a statutory body in Israel. The Law for Encouragement of Capital Investments, 1959 provides certain grants and/or tax benefits subject to certain criteria and limitations. These criteria set for the approval of a facility as a “Privileged Enterprise,” include a generally required provision that at least 25% of the Privileged Enterprise’s income must be derived from export. Additionally, the Amendment enacted major changes concerning the manner in which tax benefits are awarded under the Investment Law so that companies no longer require the Investment Center's approval in order to qualify for tax benefits. However, the Amendment provides that terms and benefits that were included in any certificate of approval which was already granted will remain subject to the provisions of the law as they were on the date of such approval.

Status Expansion of our Production Facilities: Under the Amendment, in 2005 and 2007, we submitted an expansion request for additional “Privileged Enterprise” approval regarding our production facilities. A portion of the income derived from this “Privileged Enterprise” will be tax-exempt for a period of 10 years from the commencement year.

Our Israeli company had no taxable income since inception nor any profit under our Approved or Privileged Enterprise plans.

Israeli Transfer Pricing Regulations –

On November 29, 2006, Income Tax Regulations (Determination of Market Terms), 2006, promulgated under Section 85A of the Tax Ordinance, came into effect (the “TP Regs”). Section 85A of the Tax Ordinance and the TP Regs generally requires that all cross-border transactions carried out between related parties be conducted on an arm’s length principle basis and will be taxed accordingly. The TP Regs had no material effect on the Company.

Measurement of Taxable Income –

Results for tax purposes are measured in real terms, in accordance with the changes in the Israeli Consumer Price Index, or changes in exchange rate of the NIS against the dollar, for a “foreign investors” company. Until taxable year 2002, we measured our results for tax purposes in accordance with changes in the Israeli consumer price index. Commencing with taxable year 2003, we have elected to measure our results for tax purposes on the basis of the changes in the exchange rate of NIS against the U.S. dollar.

Tax Benefits of Research and Development –

Israeli tax law permits, under certain conditions, a tax deduction in the year incurred for expenditures, including capital expenditures, in scientific research and development projects, if the expenditures are approved by the relevant government ministry, determined by the field of research, and if the research and development is for the promotion of the enterprise and is carried out by, or on behalf of, a company seeking such deduction. Expenditures not so approved are deductible over a three year period; however, expenditures made out of proceeds made available to us through government grants are not deductible.

Withholding and Capital Gains Taxes Applicable to Non-Israeli Shareholders –

Nonresidents of Israel are subject to income tax on income accrued or derived from sources in Israel. These sources of income include passive income such as dividends, royalties and interest, as well as non-passive income from services rendered in Israel. We are generally required to withhold income tax at the rate of 25% on all distributions of dividends, although, with respect to U.S. taxpayers, if the dividend recipient holds 10% or more of our voting stock for a certain period prior to the declaration and payment of the dividend, we are only required to withhold at a 12.5% rate. Notwithstanding the foregoing, with regard to dividends generated by an Approved Enterprise, we are required to withhold income tax at the rate of 15%.

Israeli law generally imposes a capital gains tax on the sale of publicly traded securities. Pursuant to changes made to the Israeli Income Tax Ordinance in January 2006, capital gains on the sale of our ordinary shares will be subject to Israeli capital gains tax, generally at a rate of 20% unless the holder holds 10% or more of our voting power during the 12 months preceding the sale, in which case it will be subject to a 25% capital gains tax. However, as of January 1, 2003, nonresidents of Israel are exempt from capital gains tax in relation to the sale of our ordinary shares for so long as (i) our ordinary shares are listed for trading on a stock exchange outside of Israel, (ii) the capital gains are not accrued or derived by the nonresident shareholder's permanent enterprise in Israel, (iii) the ordinary shares in relation to which the capital gains are accrued or derived were acquired by the nonresident shareholder after the initial listing of the ordinary shares on a stock exchange outside of Israel, and (iv) neither the shareholder nor the particular capital gain is otherwise subject to certain sections of the Israeli Income Tax Ordinance. As of January 1, 2003, nonresidents of Israel are also exempt from Israeli capital gains tax resulting from the sale of securities on the Tel Aviv Stock Exchange; provided that the capital gains are not accrued or derived by the nonresident shareholder's permanent enterprise in Israel.

In addition, under the income tax treaty between the United States and Israel, a U.S. resident holder of ordinary shares that are not listed for trading on a stock exchange outside of Israel will be exempt from Israeli capital gains tax on the sale, exchange or other disposition of such ordinary shares unless the holder owns, directly or indirectly, 10% or more of our voting power during the 12 months preceding such sale, exchange or other disposition.

A nonresident of Israel who receives interest, dividend or royalty income derived from or accrued in Israel, from which tax was withheld at the source, is generally exempt from the duty to file tax returns in Israel with respect to such income, provided such income was not derived from a business conducted in Israel by the taxpayer.

Israel presently has no estate or gift tax.

United States Federal Income Tax Considerations with Respect to the Acquisition, Ownership and Disposition of Our Ordinary Shares –

The following is a discussion of certain U.S. federal income tax consequences applicable to “U.S. Holders” (as defined below) who beneficially own our ordinary shares. The discussion is based on the Internal Revenue Code of 1986, as amended, or the Code, applicable U.S. Treasury Regulations promulgated thereunder, and existing administrative rulings and court decisions in effect as of the date of this Annual Report, all of which are subject to change at any time, possibly with retroactive effect. For purposes of this discussion, it is assumed that U.S. Holders of our ordinary shares hold such stock as a capital asset within the meaning of Section 1221 of the Code, that is, generally for investment. This discussion does not address all aspects of United States federal income taxation that may be relevant to a particular U.S. Holder of our ordinary shares in light of his or her circumstances or to a U.S. Holder of our ordinary shares subject to special treatment under United States federal income tax law, including, without limitation:

- banks, other financial institutions, real estate investment trusts, insurance companies or mutual funds;
- broker-dealers, including dealers in securities or currencies, or taxpayers that elect to apply a mark-to-market method of accounting;
- shareholders who hold our ordinary shares as part of a hedge, straddle, or other risk reduction, constructive sale or conversion transaction;
- tax-exempt entities;
- persons who have a functional currency other than the U.S. dollar;
- persons who have owned at any time or who own, directly, indirectly, constructively or by attribution, ten percent or more of the total voting power of our share capital;
- grantor trusts or S corporations;
- certain expatriates or former long-term residents of the United States; and
- shareholders who acquired our ordinary shares pursuant to the exercise of an employee stock option or right or otherwise as compensation.

In addition, not discussed is the application of: (i) foreign, state or local tax laws; (ii) United States federal and state estate and/or gift taxation; or (iii) the alternative minimum tax.

If a partnership (or any entity treated as a partnership for U.S. federal income tax purposes) holds ordinary shares, the tax treatment of the partnership and a partner in such partnership will generally depend on the activities of the partnership. Such a partner or partnership should consult its tax advisor as to its tax consequences.

As used in this section, the term “U.S. Holder” refers to any beneficial owner of our ordinary shares that is any of the following:

- an individual who is a citizen or resident of the United States for U.S. federal income tax purposes;
- a corporation (or other entity treated as a corporation for U.S. federal income tax purposes) created or organized in the United States or under the laws of the United States, any State or political subdivision thereof, or the District of Columbia;
- an estate the income of which is includible in gross income for U.S. federal income tax purposes regardless of its source;
- a trust (i) if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more United States persons have the authority to control all of such trust’s substantial decisions; or (ii) that has in effect a valid election under applicable U.S. Treasury Regulations to be treated as a U.S. person.

Certain aspects of U.S. federal income tax relevant to a holder of our ordinary shares that is not a U.S. Holder (a "Non-U.S. Holder") are also discussed below.

Each holder of our ordinary shares is advised to consult his or her own tax advisor with respect to the specific tax consequences to him or her of purchasing, holding or disposing of our ordinary shares, including the applicability and effect of federal, state, local and foreign income and other tax laws to his or her particular circumstances.

Distributions

Subject to the discussion below under the heading "Passive Foreign Investment Company Status," to the extent paid out of our current or accumulated earnings and profits, as determined under United States federal income tax principles, a distribution made with respect to our ordinary shares (including the amount of any non-U.S. withholding tax thereon) will be includible for U.S. federal income tax purposes in the income of a U.S. Holder as a taxable dividend. Dividends that are received by U.S. Holders that are individuals, estates or trusts will be taxed at the rate applicable to long-term capital gains (a maximum rate of 15%) for taxable years beginning on or before December 31, 2012, provided that such dividends meet the requirement of "qualified dividend income" as defined by the Code. Dividends that fail to meet such requirements, and dividends received by corporate U.S. Holders, are taxed at ordinary income rates. No dividend received by a U.S. Holder will be a qualified dividend (1) if the U.S. Holder held the ordinary share with respect to which the dividend was paid for less than 61 days during the 121-day period beginning on the date that is 60 days before the ex-dividend date with respect to such dividend, excluding for this purpose, under the rules of Code Section 246(c), any period during which the U.S. Holder has an option to sell, is under a contractual obligation to sell, has made and not closed a short sale of, is the grantor of a deep-in-the-money or otherwise nonqualified option to buy, or has otherwise diminished its risk of loss by holding other positions with respect to, such ordinary share (or substantially identical securities) or (2) to the extent that the U.S. Holder is under an obligation (pursuant to a short sale or otherwise) to make related payments with respect to positions in property substantially similar or related to the ordinary share with respect to which the dividend is paid. If we were to be a "passive foreign investment company" (as such term is defined in the Code), or PFIC, for any taxable year, dividends paid on our ordinary shares in such year or in the following taxable year would not be qualified dividends. In addition, a non-corporate U.S. Holder will be able to take a qualified dividend into account in determining its deductible investment interest (which is generally limited to its net investment income) only if it elects to do so; in such case the dividend will be taxed at ordinary income rates.

To the extent that a distribution exceeds our earnings and profits and provided that we were not a PFIC, such distribution will be treated as a non-taxable return of capital to the extent of the U.S. Holder's adjusted tax basis in our ordinary shares and thereafter as taxable capital gain. Dividends paid by us generally will not be eligible for the dividends received deduction allowed to corporations under the Code. Dividends paid in a currency other than the U.S. dollar will generally be includible in income of a U.S. Holder in a U.S. dollar amount based on the exchange rate on the date the distribution is included in income. A U.S. Holder who receives a foreign currency distribution and converts the foreign currency into U.S. dollars subsequent to receipt may have foreign exchange gain or loss, based on any appreciation or depreciation in the value of the foreign currency against the U.S. dollar, which will generally be U.S. source ordinary income or loss.

Subject to certain conditions and limitations set forth in the Code (including certain holding period requirements), U.S. Holders generally will be able to elect to claim a credit against their United States federal income tax liability for any non-U.S. withholding tax deducted from dividends received in respect of our ordinary shares. For purposes of calculating the foreign tax credit, dividends paid on our ordinary shares generally will be treated as income from sources outside the United States and foreign source "passive income" for U.S. foreign tax purposes. In lieu of claiming a tax credit, U.S. Holders that itemize deductions may instead claim a deduction for foreign taxes withheld, subject to certain limitations. The rules relating to the determination of the amount of non-U.S. income taxes that may be claimed as foreign tax credits are complex and U.S. Holders should consult their tax advisors to determine whether and to what extent a credit would be available.

Disposition of the Ordinary Shares

Subject to the discussion below under the heading "Passive Foreign Investment Company Status," upon the sale, exchange or other disposition of our ordinary shares, a U.S. Holder generally will recognize gain or loss for U.S. federal income tax purposes in an amount equal to the difference between the U.S. dollar value of the amount realized on the disposition of our ordinary shares and the U.S. Holder's adjusted tax basis in our ordinary shares, which is usually the U.S. dollar cost of the ordinary shares. Such gain or loss generally will be long-term capital gain or loss if our ordinary shares have been held for more than one year on the date of the disposition. Non-corporate U.S. Holders are currently subject to a reduced rate of taxation on long-term capital gains (15% for taxable years beginning on or before December 31, 2012). The deductibility of a capital loss recognized on the sale or exchange of ordinary shares is subject to limitations. Any gain or loss generally will be treated as United States source income or loss for United States foreign tax credit purposes.

Passive Foreign Investment Company Status

Generally a non-U.S. corporation is treated as a PFIC for U.S. federal income tax purposes if either:

- 75% or more of its gross income (including the pro rata share of gross income of any corporation (U.S. or foreign) of which such corporation is considered to own 25% or more of the ordinary shares by value) for the taxable year is passive income; or
- 50% or more of its gross assets (including its pro rata share of the assets of any corporation in which such corporation is considered to own 25% or more of the ordinary shares by value) during the taxable year computed on a quarterly average basis produce or are held for the production of passive income.

As a result of the combination of our substantial holdings of cash, cash equivalents and securities and the decline in the market price of our ordinary shares from its historical highs, there is a risk that we could be classified as a PFIC, for U.S. federal income tax purposes. Based upon our market capitalization during 2011, we do not believe that we were a PFIC for 2011. In addition, based upon an independent valuation of our assets as of the end of each quarter of 2001 and based upon our valuation of our assets for 2002 and 2003, we do not believe that we were a PFIC for 2001, 2002 or 2003 despite the relatively low market price of our ordinary shares during much of those taxable years. We cannot assure you, however, that the United States Internal Revenue Service ("IRS") or the courts would agree with our conclusion if they were to consider our situation. In addition, the tests for determining PFIC status are applied annually and it is difficult to make accurate predictions of our future income and assets and the future price of our ordinary shares, which are all relevant to the determination of whether we are classified as a PFIC. There is no assurance that we will not become a PFIC in 2012 or subsequent taxable years.

If we were deemed to be a PFIC for any taxable year during which a U.S. Holder held our shares and such holder failed to make either a "QEF election" or a "mark-to-market election" (as described below) for the first taxable year during which we were a PFIC and the U.S. Holder held our shares:

- gain recognized (including gain deemed recognized if our ordinary shares are used as security for a loan) by the U.S. Holder upon the disposition of, as well as income recognized upon receiving certain "excess distributions" in respect of, our ordinary shares would be taxable as ordinary income;
- the U.S. Holder would be required to allocate such excess distribution and/or disposition gain ratably over such holder's entire holding period for our ordinary shares; the U.S. Holder's income for the current taxable year would include (as ordinary income) amounts allocated to the current year (i.e., the year of the distribution or disposition) and to any period prior to the first day of the first taxable year for which we were a PFIC;
- the amount allocated to each year other than (i) the year of the distribution or disposition and (ii) any year prior to our becoming a PFIC, would be subject to tax at the highest individual or corporate marginal tax rate, as applicable, in effect for that year, and an interest charge would be imposed with respect to the resulting tax liability;
- U.S. Holders will generally be required to file an annual report with the IRS if we are a PFIC for taxable years beginning on or after March 18, 2010; and
- any U.S. Holder who acquired our ordinary shares upon the death of a U.S. Holder would not receive a step-up of the income tax basis to fair market value for such shares. Instead, such U.S. Holder would have a tax basis equal to the lesser of the decedent's basis, or the fair market value of the ordinary shares on the date of the decedent's death.

Although a determination as to a non-U.S. corporation's PFIC status is made annually, an initial determination that a non U.S. corporation is a PFIC for any taxable year generally will cause the above-described consequences to apply for all future taxable years to U.S. Holders who held shares in the corporation at any time during a taxable year when the corporation was a PFIC and who made neither a QEF election nor a mark-to-market election (as discussed below) with respect to such shares with their tax return for the year that included the last day of the corporation's first taxable year as a PFIC. This will generally be true even if the corporation ceases to be a PFIC in later years.

Generally, if a U.S. Holder makes a valid QEF election with respect to our ordinary shares, the U.S. Holder would be required, for each taxable year for which we are a PFIC, to include in income such holder's pro-rata share of our: (i) ordinary earnings as ordinary income and (ii) net capital gain as long-term capital gain, in each case computed under U.S. federal income tax principles, even if such earnings or gains have not been distributed, unless the shareholder makes an election to defer this tax liability and pays an interest charge.

The QEF election is made on a shareholder-by-shareholder basis. Thus, any U.S. Holder of our ordinary shares can make its own decision whether to make a QEF election. A QEF election applies to all of our ordinary shares held or subsequently acquired by an electing U.S. Holder and can be revoked only with the consent of the IRS. A shareholder makes a QEF election by attaching a completed IRS Form 8621, using the information provided in the PFIC annual information statement, to a timely filed U.S. federal income tax return. In order to permit our shareholders to make a QEF election, we must supply them with certain information. We will supply U.S. Holders with the information needed to report income and gain pursuant to the QEF election in the event that we are classified as a PFIC for any taxable year and will supply such additional information as the IRS may require in order to enable U.S. Holders to make the QEF election. It should be noted that U.S. Holders may not make a QEF election with respect to warrants or rights to acquire our ordinary shares. Under certain circumstances, a U.S. Holder that has not made a timely QEF election may obtain treatment similar to that afforded a shareholder who has made a timely QEF election. Such a U.S. Holder may make an election in a taxable year subsequent to the first taxable year during the U.S. Holder's holding period that we are classified as a PFIC to treat such holder's interest in our Company as subject to a deemed sale of its PFIC stock and recognize gain, but not loss, on such deemed sale in accordance with the general PFIC rules, including the interest charge provisions, described above and thereafter treating such interest in our Company as an interest in a QEF. In addition, under certain circumstances U.S. Holders may make a retroactive QEF election, but may be required to file a timely protective statement to preserve their ability to make a retroactive QEF election. U.S. Holders should consult their tax advisors regarding the advisability of filing a protective statement.

Alternatively, a U.S. Holder of shares in a PFIC can elect to mark “marketable stock” (e.g. stock that is “regularly traded” on the NASDAQ Global Select Market) to market annually recognizing as ordinary income or loss each year the shares are held, as well as on the disposition of the shares, in a taxable year that we are a PFIC, an amount equal to the difference between the shareholder’s adjusted tax basis in the PFIC stock and its fair market value. Under current law, U.S. Holders may not make a mark-to-market election with respect to warrants or rights to acquire our ordinary shares. Ordinary loss generally is recognized only to the extent of net mark-to-market gains previously included in income by the U.S. Holder under the election in prior taxable years. A mark-to-market election applies for so long as our ordinary shares are “marketable stock and is irrevocable without obtaining the consent of the IRS.

The PFIC rules described above are complex. U.S. Holders of our ordinary shares (or warrants or rights to acquire our ordinary shares) are urged to consult their tax advisors about the PFIC rules, including the advisability, procedure and timing of making a QEF or mark-to-market election, in connection with their holding of our ordinary shares.

Tax Consequences for Non-U.S. Holders of Our Ordinary Shares

Except as described in “Information Reporting and Backup Withholding” below, a Non-U.S. Holder of our ordinary shares will not be subject to U.S. federal income or withholding tax on the payment of dividends on, and the proceeds from the disposition of, our ordinary shares, unless in the case of U.S. federal income taxes:

- such item is effectively connected with the conduct by the Non-U.S. Holder of a trade or business in the United States and, in the case of a resident of a country which has a treaty with the United States, such item is attributable to a permanent establishment or, in the case of an individual, a fixed place of business, in the United States, or

- in the case of the disposition or our ordinary shares, the Non-U.S. Holder is an individual who holds our ordinary shares as a capital asset and is present in the United States for 183 days or more in the taxable year of the disposition, and certain other conditions are met.

Information Reporting and Backup Withholding

U.S. Holders (other than certain exempt recipients, such as corporations) generally are subject to information reporting requirements and backup withholding (currently at a rate of 28%) with respect to dividends paid in the U.S. on, and the proceeds from the disposition of, our ordinary shares, unless they:

- furnish a correct taxpayer identification number and certify that they are not subject to backup withholding on an IRS Form W-9; or
- provide proof that they are otherwise exempt from backup withholding.

Non-U.S. Holders generally are not subject to information reporting or backup withholding with respect to dividends paid on, or upon the disposition of, our ordinary shares, provided that such Non-U.S. Holder provides a tax payer identification number, certifies to its foreign status, or otherwise establishes an exemption.

Backup withholding is not an additional tax. The amount of any backup withholding is allowable as a credit against the U.S. or Non-U.S. Holder’s United States federal income tax liability, provided that such holder provides the requisite information to the IRS.

F.DIVIDENDS AND PAYING AGENTS

Not applicable.

G.STATEMENT BY EXPERTS

Not applicable.

H. DOCUMENTS ON DISPLAY

We are subject to the informational requirements of the Exchange Act applicable to foreign private issuers and fulfill the obligation with respect to such requirements by filing reports with the SEC. As a foreign private issuer, we are exempt from the rules under the Exchange Act prescribing the furnishing and content of proxy statements, and our officers, directors and principal shareholders are exempt from the reporting and "short-swing" profit recovery provisions contained in Section 16 of the Exchange Act. In addition, we are not required under the Exchange Act to file periodic reports and financial statements with the SEC as frequently or as promptly as U.S. companies whose securities are registered under the Exchange Act. However, we file with the SEC an annual report on Form 20-F containing consolidated financial statements audited by an independent accounting firm no later than four months after the close of each fiscal year. We also furnish reports on Form 6-K containing unaudited consolidated financial information after the end of each of the first three quarters. You may read and copy any document we file with the SEC at prescribed rates at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Copies of such material may be obtained by mail from the Public Reference Branch of the SEC at such address, at prescribed rates. Please call the SEC at l-800-SEC-0330 for further information on the public reference room. A copy of each report submitted in accordance with applicable U.S. law is also available for public review at our principal executive offices.

In addition, the SEC maintains an Internet website at http://www.sec.gov that contains reports, proxy statements, information statements and other material that are filed through the SEC's Electronic Data Gathering, Analysis and Retrieval (EDGAR) system. We began filing our reports through the EDGAR system in November 2002.

The Israeli Securities Authority maintains an Internet website at http://www.isa.gov.il that contains reports, proxy statements, information statements and other material that are filed through the electronic disclosure system (MAGNA). We began filing our reports through the MAGNA system in August 2003.

I.SUBSIDIARY INFORMATION

Not applicable.

ITEM 11.QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to both interest rate and foreign exchange risk.

Interest risk:

We are exposed to Interest risk associated with the SVB Long Term Loan obtained in 2011.

Our investment portfolio includes held to maturity marketable securities. These securities include investments issued by agencies of the U.S. government that have an implied guarantee by the U.S. government or were nationalized by U.S. government or are investments issued by highly rated corporations. As of December 31, 2011, the rating of the securities in our portfolio were at least A. The declines in interest rates in 2010 and 2011 have reduced and are expected to continue to reduce our interest income. In addition as a result of the loan obtain in 2011, as the loan is linked to the LIBOR for three month plus a fixed percentage, and the fact that the LIBOR for three month might fluctuate over time our interest expense on the loan might change.

The table below provides information regarding our investments in cash, cash equivalents and marketable securities (in thousands), as of December 31, 2011 and 2010:

	Amortized cost Maturity 2012	Fair value at Dec. 31, 2011
Corporate bonds	$1,644	$1,650
Cash and short term bank deposit	62,764	62,764
Total	$64,408	$64,414

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	Amortized cost		Total Amortized cost	Fair value at Dec. 31, 2010
	Maturity 2011	2012		
US Government agencies	$1,318	$-	$1,318	$1,322
Corporate bonds	14,816	2,564	17,380	17,517
Cash and short term bank deposit	64,647	-	64,647	64,647
Total	$80,781	$2,564	$83,345	$83,486

Foreign Currency Risk –

We are exposed to financial market risk associated with changes in foreign currency exchange rates. To mitigate these risks, we use derivative financial instruments. The majority of our revenues and expenses are generated in U.S. dollars. A portion of our expenses, however, is denominated in NIS. In order to protect ourselves against the volatility of future cash flows caused by changes in foreign exchange rates, we use currency forward contracts and currency options. We hedge the part of our forecasted expenses denominated in NIS. If our currency forward contracts and currency options meet the definition of a hedge, and are so designated, changes in the fair value of the contracts will be offset against changes in the fair value of the hedged assets or liabilities through earnings. For derivative instruments not designated as hedging instruments, the gain or loss is recognized in current earnings during the period of change. Our hedging program reduces, but does not eliminate, the impact of foreign currency rate movements, and as a result of the general economic slowdown along with the devaluation of the dollar, our results of operations may be adversely affected.

A majority of our revenues are generated in U.S. dollars. In addition, most of our costs are denominated and determined in U.S. dollars and NIS according to the salient economic factors indicated in ASC 830 “Foreign Currency Matters”. Our cash flow, sale price, sales market, expense, financing and inter-company transactions, and arrangement indicators, are predominantly denominated in U.S. dollars. In addition, the U.S. dollar is the primary currency of the economic environment in which we operate, and thus, the U.S. dollar is our functional and reporting currency. In our balance sheet, we re-measure into U.S. dollars all monetary accounts (principally cash and cash equivalents and liabilities) that are maintained in other currencies. For this re-measurement, we use the relevant foreign exchange rate at the balance sheet date. Any gain or loss that results from this re-measurement is reflected in the statement of operations as appropriate.

We measure and record non-monetary accounts in our balance sheet in U.S. dollars. For this measurement, we use the U.S. dollar value in effect at the date that the asset or liability was initially recorded in our balance sheet (the date of the transaction).

To hedge against the risk of overall changes in cash flows resulting from foreign currency trade payables and salary payments during the year, we have instituted a foreign currency cash flow hedging program. We hedge portions of our forecasted expenses denominated in NIS with currency forwards and option tools. These forward and option contracts are designated as cash flow hedges and are all effective.

As of December 31, 2011, we recorded accumulated other comprehensive net gain in the amount of approximately $2.7 million from our currency forward and option transactions with respect mainly to trade payables and payroll expenses. Such amount will be recorded into earnings during 2012.

See also “Item 5—Operating and Financial Review and Prospects—Operating Results Impact of Inflation and Currency Fluctuations”.

ITEM 12.DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

ITEM 14.MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

Not applicable.

ITEM 15.CONTROLS AND PROCEDURES

a. Disclosure Controls and Procedures

The Company's management, with the participation of its chief executive officer and chief financial officer, evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act) as of December 31, 2011. Based on this evaluation, the Company's chief executive officer and chief financial officer have concluded that, as of such date, the Company's disclosure controls and procedures were (i) designed to ensure that material information relating to the Company, including its consolidated subsidiaries, is made known to its management, including the Company's chief executive officer and chief financial officer, by others within those entities, as appropriate to allow timely decisions regarding required disclosure, particularly during the period in which this report was being prepared and (ii) effective, in that they provide reasonable assurance that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

b. Management's Annual Report on Internal Control Over Financial Reporting –

Our management, under the supervision of our Chief Executive Officer and Chief Financial Officer, is responsible for establishing and maintaining adequate internal control over our financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) of the Securities Exchange Act. The Company's internal control over financial reporting is designed to provide reasonable assurance to the Company's management and board of directors regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes policies and procedures that:

- pertain to the maintenance of our records that in reasonable detail accurately and fairly reflect our transactions and asset dispositions;
- provide reasonable assurance that our transactions are recorded as necessary to permit the preparation of our financial statements in accordance with generally accepted accounting principles;
- provide reasonable assurance that our receipts and expenditures are made only in accordance with authorizations of our management and board of directors (as appropriate); and
- provide reasonable assurance regarding the prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. In addition, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2011 based on the framework for Internal Control – Integrated Framework set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Management has excluded Wavion, which is included in the 2011 consolidated financial statements of Alvarion Ltd. and subsidiaries and constituted approximately $43.1 million and $27.9 million of total and net assets, respectively, as of December 31, 2011 and $4.3 million and $ 1.0 million of revenues and net income, respectively, for the year then ended because ownership was acquired by Alvarion during November 2011. Based on our assessment under that framework and the criteria established therein, our management concluded that the Company's internal control over financial reporting were effective as of December 31, 2011.

Our financial statements and internal control over financial reporting has been audited by Kost, Forer, Gabbay & Kasierer (A member of Ernst & Young Global), an independent registered public accounting firm.

c. Attestation Report of the Registered Public Accounting Firm

This Annual Report includes an attestation report of our registered public accounting firm regarding internal control over financial reporting on page F-3 of our audited consolidated financial statements set forth in "Item 18 – Financial Statements", and is incorporated herein by reference.

d. Changes in Internal Control over Financial Reporting

There were no changes in our internal controls over financial reporting identified with the evaluation thereof that occurred during the period covered by this Annual Report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting

ITEM 16. Reserved.

ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Our board of directors has determined that Professor Amit, a member of our audit committee, qualifies as an "audit committee financial expert" and is "independent," each as defined in the applicable SEC and NASDAQ regulations.

ITEM 16B.CODE OF ETHICS

In 2003, we adopted a Code of Ethics that applies to our Chief Executive Officer, Chief Financial Officer, all other senior officers and all of our employees. In March 2008 and July 2011, we updated the Code of Ethics. The updated Code of Ethics is included as an Exhibit hereto.

ITEM 16C.PRINCIPAL ACCOUNTANT FEES AND SERVICES –

The following is a summary of the fees billed to us for audit, audit-related, tax and other services provided by Kost, Forer, Gabbay & Kasierer for the years ended December 31, 2010 and December 31, 2011:

Fee Category	2010	2011
Audit Fees	$ 340,000	$ 280,000
Audit-Related Fees	$ -	$ -
Tax Fees	$ 74,914	$ 89,639
All other fees	$ -	$ -
Total Fees	$ 414,914	$ 369,639

Audit Fees: Consists of the aggregate fees billed and accrued for professional services rendered for the audit of our annual financial statements and services that are normally provided by Kost, Forer, Gabbay & Kasierer in connection with statutory and regulatory filings or engagements.

Audit Related Fees: Consists of the aggregate fees billed for assurance and related services that are reasonably related to the performance of the audit or review of our financial statements and are not reported under "Audit Fees." We did not have such services in 2011 or 2010.

Tax Fees: Consists of the aggregate fees billed for professional services rendered for tax compliance, tax advice and tax planning. These services include assistance regarding international and Israeli tax services.

All Other Fees: Consists of the aggregate fees billed for products and services other than the services reported above. We did not have such services in 2011 or 2010.

Our audit committee has adopted a policy for pre-approval of audit and non-audit services. Under the policy, proposed services either may be pre-approved without consideration of specific case-by-case services by the audit committee ("general pre-approval") or they may require the specific pre-approval of the audit committee ("specific pre-approval"). The audit committee employs a combination of these two approaches. Unless a type of service has received general pre-approval, it will require specific pre-approval by the audit committee if it is to be provided by the independent auditor. The term of any general pre-approval is 12 months from the date of pre-approval, unless the audit committee considers a different period and states otherwise. The audit committee reviews annually and pre-approves the services that may be provided by the independent auditor without obtaining specific pre-approval from the audit committee. The audit committee adds to or subtracts from the list of general pre-approved services from time to time, based on subsequent determinations. Pre-approval fee levels or budgeted amounts for all services to be provided by the independent auditor are to be established annually by the audit committee. Any proposed services exceeding these levels or amounts require specific pre-approval by the audit committee. All of the fees listed in the table above were approved by the audit committee.

ITEM 16D.EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES

Not applicable.

ITEM 16E.PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS

In October 2008, following the approval of our board of directors and the receipt of a court approval, we were authorized to use up to $30 million of our available cash to repurchase our shares. Through December 31, 2008, we repurchased under this repurchase program 1,449,999 ordinary shares at a weighted average price of approximately $3.44 per share for an aggregate price of approximately $5.0 million. During 2010 and 2011 we did not repurchase any additional ordinary shares under this repurchase program or otherwise.

Under our first repurchase program in 2002, our board of directors authorized a share repurchase of up to $9 million of our ordinary shares. Under this 2002 repurchase plan, we repurchased until December 31, 2003 3,796,773 ordinary shares at a weighted average price per share of approximately $2.07 for an aggregate of $7.9 million. Since such date, we have not utilized the remainder of this first repurchase program.

ITEM 16F.CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT

Not applicable.

ITEM 16G.CORPORATE GOVERNANCE

As a foreign private issuer whose shares are listed on the NASDAQ Global Select Market, we are permitted to follow certain home country corporate governance practices instead of certain requirements of the NASDAQ Listing Rules.

We do not comply with the NASDAQ requirement that we obtain shareholder approval for certain dilutive events, such as for the establishment or amendment of certain equity based compensation plans. Instead, we follow Israeli law and practice in accordance with which the establishment or amendment of certain equity based compensation plans is approved by our board of directors.

As a foreign private issuer listed on the NASDAQ Global Select Market, we may also follow home country practice with regard to other matters, including those set forth below:

- Nomination – NASDAQ rules require that director nominees be selected, or recommended for the board of directors, either by (a) a majority of independent directors or (b) a nominations committee comprised solely of independent directors. Under Israeli law and practice, directors are recommended by our board of directors for election by our shareholders.
- Compensation – NASDAQ rules regarding compensation of executive officers require that the compensation of the chief executive officer and all other executive officers be determined, or recommended to the board of directors for determination, either by (i) a majority of the independent directors or (ii) a compensation committee comprised solely of independent directors. Under the Israeli Companies Law, the compensation arrangements for officers who are not directors require the approval of the audit committee and the board of directors. The audit committee approval may be substituted by the approval of the compensation committee, provided the compensation committee complies with the audit committee requirements prescribed by the Israeli Companies Law. If the compensation arrangement is an immaterial amendment to an existing compensation arrangement of an officer who is not a director, the approval of the audit committee is sufficient. Arrangements regarding the compensation of directors require the approval of the audit committee, the board and the shareholders, in that order.
- Shareholder Approval for Dilutive Events – NASDAQ rules require that we obtain shareholder approval for certain dilutive events, such as for the establishment or amendment of certain equity based compensation plans and arrangements, an issuance that will result in a change of control of the company, certain transactions other than a public offering involving issuances of a 20% or more interest in the company and certain acquisitions of the stock or assets of another company. Under Israeli law and practice, in general, the approval of the board of directors is required for the establishment or amendment of equity based compensation plans and arrangements, unless the arrangement is for the benefit of a director, or a controlling shareholder, in which case audit committee and shareholder approval are also required. Similarly, the approval of the board of directors is generally sufficient for a private placement unless the private placement involves a director, a controlling shareholder or is deemed a “significant private placement,” in which case shareholder approval, and, in some cases, audit committee approval, would also be required. The Israeli Companies Law defines a “significant private placement” as a private placement (i) resulting in a party becoming a controlling shareholder, or (ii) involving the issuance of a 20% or more voting rights in the company, which (A) results in a 5% or more shareholder increasing its interest in the company or an offeree becoming a 5% or more shareholder, and (B) involves consideration that is not solely cash or public traded securities, or is not on fair market terms.

For a discussion of the requirements of Israeli law in this regard, see Item 6.C. "Directors, Senior Management and Employees –Board Practices," and Item 10.B. "Additional Information – Memorandum and Articles of Association."

ITEM 16H.MINE SAFETY DISCLOSURE

Not applicable

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PART III

ITEM 17.FINANCIAL STATEMENTS

We have responded to Item 18 in lieu of this item.

ITEM 18. FINANCIAL STATEMENTS

The financial statements required by this item are at the end of this Annual Report, beginning on page F-1.

ITEM 19.EXHIBITS

The exhibits filed with or incorporated into this Annual Report are listed on the index of exhibits below.

Exhibit No.	Description
1.1	Memorandum of Association (English translation accompanied by Hebrew original) (1)
1.2	Articles of Association(2)
1.3	Certificate of Name Change (English translation accompanied by Hebrew original) (3)
2.1	Form of Ordinary Share Certificate (4)
4.1	Lease Agreement, dated April 16, 2000, between the Registrant and Bet Dror Ltd. And Ziviel Investments Ltd. (English summary accompanied by Hebrew original) (1)
4.2	Form of Indemnity Agreement for Directors and Executive Officers*
4.3	Addendum, dated September 2000, to Lease Agreement between the Registrant and Bet Dror Ltd. and Ziviel Investments Ltd. (English summary accompanied by Hebrew original) (5)
4.4	Sublease Agreement, dated July 5, 2001, between Floware Wireless Systems Ltd. and Ceragon Networks Ltd. (English summary accompanied by Hebrew original) (5)
4.5	Addendum, dated October 5th, 2010, to Lease Agreement between the Registrant and Bet Dror Ltd. and Ziviel Investments Ltd. (English summary translation accompanied by Hebrew original) *
8.1	Subsidiaries of Alvarion Ltd.*
10.1	Loan and Security Agreement, dated June 21, 2011, between Alvarion and Silicon Valley Bank (the "Long Term Loan Agreement with SVB")*
10.2	First Modification, dated November 17, 2011 to the Long Term Loan Agreement with SVB*
10.3	Second Modification, dated January 31, 2012 to the Long Term Loan Agreement with SVB*
10.4	Third modification, dated April 5 2012, to the Long Term Loan Agreement with SVB*
10.5	Fourth Modification , dated April 25 2012 to the Long Term Loan Agreement with SVB*
10.6	Agreement and Plan of Merger, dated November 2, 2011, among Alvarion Inc., Alvarion Acquisition Inc. and Wavion Inc. *
11	Amended Code of Ethics*
12.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 *
12.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
13.1	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 *
13.2	Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 *
15.1	Consent of Kost, Forer, Gabay & Kasierer*

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* Filed herewith

(1) Incorporated herein by reference to the Registration Statement on Form F-1 (File No. 333-11572).

(2) Incorporated by reference to the Annual Report on Form 20-F for the fiscal year ended December 31, 2008.

(3) Incorporated by reference to the Registration Statement on Form S-8 (File No. 333-13786).

(4) Incorporated by reference to the Registration Statement on Form S-8 (File No. 333-14142).

(5) Incorporated by reference to the Annual Report on Form 20-F for the fiscal year ended December 31, 2001.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this Annual Report on its behalf.

ALVARION LTD.

By: /s/ Eran Gorev
Eran Gorev
Chief Executive Officer
Date: April 30, 2012

ALVARION LTD. AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2011

IN U.S. DOLLARS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

ALVARION LTD.

We have audited the accompanying consolidated balance sheets of Alvarion Ltd. ("the Company") and subsidiaries as of December 31, 2010 and 2011, and the related consolidated statements of operations, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2011. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits 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. 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, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and subsidiaries as of December 31, 2010 and 2011, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2011, in conformity with U.S. generally accepted accounting principles.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's and its subsidiaries' internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 30, 2012 expressed an unqualified opinion thereon.

Tel-Aviv, Israel
April 30, 2012

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

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

ALVARION LTD.

We have audited Alvarion Ltd. ("the Company") and subsidiaries' internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("the COSO criteria"). The Company and its subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

As indicated in the accompanying Management's Annual Report on Internal Control Over Financial Reporting management's assessment of and conclusion on the effectiveness of internal control over financial reporting did not include the internal controls of Wavion, Inc. ("Wavion"), which is included in the 2011 consolidated financial statements of Alvarion Ltd. and subsidiaries and constituted approximately $43,068 thousands and $27,883 thousands of total and net assets, respectively, as of December 31, 2011 and $4,316 thousands and $ 1,013 thousands of revenues and net income, respectively, for the year then ended. Our audit of internal control over financial reporting of Alvarion Ltd. and subsidiaries also did not include an evaluation of the internal control over financial reporting of Wavion Inc.

In our opinion, the Company and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2011, based on the COSO criteria.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company and subsidiaries as of December 31, 2010 and 2011, and the related consolidated statements of operations, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2011 and our report dated April 30, 2012 expressed an unqualified opinion thereon.

Tel-Aviv, Israel	KOST FORER GABBAY & KASIERER
April 30 , 2012	A Member of Ernst & Young Global

ALVARION LTD. AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands

	December 31,	
	2010	2011
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 61,297	$ 57,787
Short-term bank deposits	3,350	4,977
Marketable securities (Note 3)	16,134	1,644
Trade receivables, net (Note 2t)	49,931	48,294
Other accounts receivable and prepaid expenses (Note 4)	10,807	7,658
Inventories (Note 5)	56,078	36,215
Total current assets	197,597	156,575
LONG TERM MARKETABLE SECURITIES (Note 3)	2,564	-
LONG TERM TRADE RECEIVABLES	-	6,986
LONG TERM PREPAID EXPENSES	-	171
PROPERTY AND EQUIPMENT, NET (Note 7)	14,603	9,774
INTANGIBLE ASSETS, NET (Note 8)	-	20,245
GOODWILL (Note 1g)	-	13,087
Total assets	$ 214,764	$ 206,838

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

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ALVARION LTD. AND ITS SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

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

	December 31, 2010	December 31, 2011
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Current maturity on long-term loan (note 10)	$ -	$ 12,813
Trade payables	51,242	36,243
Other accounts payable and accrued expenses (Note 9)	36,377	45,441
Total current liabilities	87,619	94,497
LONG-TERM LIABILITIES:		
Long term accrued expenses	-	547
Severance pay and long term employee liabilities	2,712	1,173
Other long-term liabilities	2,346	7,280
Long-term loan (note 10)	-	17,187
Total long term liabilities	5,058	26,187
COMMITMENTS AND CONTINGENT LIABILITIES (Note 11)		
SHAREHOLDERS' EQUITY:		
Share capital (Note 12) -		
Ordinary shares of NIS 0.01 par value -		
Authorized: 120,080,000 shares at December 31, 2010 and 2011;		
Issued: 67,507,508 and 67,625,573 shares at December 31, 2010 and 2011, respectively;		
Outstanding: 62,260,736 and 62,378,801shares at December 31, 2010 and 2011, respectively	166	166
Additional paid-in capital	431,368	434,530
Treasury shares at cost: 5,246,772 shares at December 31, 2010 and 2011	(12,872)	(12,872)
Other accumulated comprehensive income (loss)	2,599	(2,674)
Accumulated deficit	(299,174)	(332,996)
Total shareholders' equity	122,087	86,154
Total liabilities and shareholders' equity	$ 214,764	$ 206,838

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

ALVARION LTD. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Year ended December 31, 2009	2010	2011
Sales (Note 14)			
Products	$ 218,137	$ 180,447	$ 163,744
Services	27,102	25,368	26,293
Total Sales	245,239	205,815	190,037
Cost of Sales			
Products	113,576	101,955	95,129
Services	14,885	26,623	23,726
Write-off of excess inventory and provision for inventory purchase commitments (Note 2g)	3,993	4,897	2,580
Inventory write-off related to bankruptcy of a customer (Note 15a)	-	-	7,144
Gross profit	112,785	72,340	61,458
Operating costs and expenses:			
Research and development, net (Note 15b)	50,790	38,717	27,964
Selling and marketing	52,022	43,376	37,576
General and administrative	15,087	19,920	13,877
Amortization of intangible assets	132	130	186
Impairment of investment (Note 2y)	1,554	-	-
Acquisition related expenses (Note 1b)	-	-	2,622
Impairment of goodwill and intangible assets (Note 2j)	-	57,110	-
Restructuring and other charges (Note 2z)	2,787	3,573	12,040
Total operating costs and expenses	122,372	162,826	94,265
Operating loss	(9,587)	(90,486)	(32,807)
Other (loss) income (Note 1f and Note 6)	731	(7,000)	-
Financial income (expense), net (Note 15c)	1,668	(99)	(1,015)
Loss before income taxes	(7,188)	(97,585)	(33,822)
Taxes on income (Note 13e)	-	894	-
Net loss	$ (7,188)	$ (98,479)	$ (33,822)
Net loss per share (Note 15d):			
Basic and diluted	$ (0.12)	$ (1.58)	$ (0.54)

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

ALVARION LTD. AND ITS SUBSIDIARIES

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share data

	Ordinary shares		Additional paid-in capital	Treasury shares	Other accumulated comprehensive income (loss)	Accumulated deficit	Total comprehensive income (loss)	Total shareholders' equity
	Number	Amount						
Balance at January 1, 2009	61,929,895	$165	$423,303	$(12,872)	$ (1,183)	$ (193,507)		$ 215,906
Exercise of employee stock options	214,539	1	371	-	-	-		372
Stock-based compensation expenses related to ASC 718		-	4,246	-	-	-		4,246
Unrealized gains on foreign currency cash flow hedges		-	-	-	3,308	-	$ 3,308	3,308
Net loss		-	-	-	-	(7,188)	(7,188)	(7,188)
Total comprehensive loss							$ (3,880)	
Balance at December 31, 2009	62,144,434	166	427,920	(12,872)	2,125	(200,695)		216,644
Exercise of employee stock options	116,302	-	114	-	-	-		114
Stock-based compensation expenses related to ASC 718	-	-	3,334	-	-	-		3,334
Unrealized gains on foreign currency cash flow hedges	-	-	-	-	474	-	$ 474	474
Net loss	-	-	-	-	-	(98,479)	(98,479)	(98,479)
Total comprehensive loss							$ (98,005)	
Balance at December 31, 2010	62,260,736	166	431,368	(12,872)	2,599	(299,174)		122,087
Exercise of employee stock options	118,065	-	9	-	-	-		9
Stock-based compensation expenses related to ASC 718	-	-	3,153	-	-	-		3,153
Unrealized losses on foreign currency cash flow hedges	-	-	-	-	(5,273)	-	$ (5,273)	(5,273)
Net loss	-	-	-	-	-	(33,822)	(33,822)	(33,822)
Total comprehensive loss							$ (39,095)	
	62,378,801	$166	$434,530	$(12,872)	$ (2,674)	$ (332,996)		$ 86,154

Balance at December 31,
2011

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

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ALVARION LTD. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2009	2010	2011
Cash flows from operating activities:			
Net loss	$(7,188)	$(98,479)	$(33,822)
Adjustments required to reconcile net loss to net cash used in operating activities:			
Depreciation	7,231	6,662	5,433
Capital loss on disposal of property and equipment	267	363	3,908
Other income from LGC transaction	(716)	-	-
Stock-based compensation expenses related to ASC 718	4,246	3,334	3,153
Accrued interest, amortization of premium and accretion of discounts on held-to-maturity marketable securities and bank deposits	589	786	108
Amortization of other intangible assets	132	130	1,764
Impairment of goodwill and other intangible assets	-	57,110	-
Impairment of investment in affiliate	1,554	-	-
Impairment of short term investment	-	7,000	-
Decrease (increase) in trade receivables, net	(5,676)	15,559	5,397
Decrease (increase) in other accounts receivable and prepaid expenses	2,487	(3,526)	2,323
Decrease (increase) in inventories	17,693	(20,096)	21,299
Increase in long term prepaid expenses	-	-	(171)
Increase in long-term trade receivables	-	-	(6,986)
Increase (decrease) in trade payables	(21,452)	15,661	(18,552)
Increase (decrease) in other accounts payable and accrued expenses	(13,218)	(5,392)	164
Increase in long term accrued expenses	-	-	547
Increase (decrease) in other long-term liabilities, net	26	91	(864)
Decrease in severance pay net and long-term employee liabilities	(1,477)	(1,642)	(1,742)
Net cash used in operating activities	(15,502)	(22,439)	(18,041)
Cash flows from investing activities:			
Purchase of property and equipment	(7,196)	(5,025)	(3,344)
Proceeds from property and equipment	43	7	149
Investment in short term investment	-	(7,000)	-
Proceeds from bank deposits	15,112	8,056	3,350
Investment in bank deposits	(8,020)	(3,345)	(4,916)
Investment in held-to-maturity marketable securities	(9,281)	(2,424)	-
Proceeds from maturity of held-to-maturity marketable securities	29,161	24,273	16,885
Proceeds related to the LGC transaction	716	-	-
Acquisition of Wavion (a)	-	-	(24,618)
Net cash provided by (used in) investing activities	20,535	14,542	(12,494)

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

ALVARION LTD. AND ITS SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2009	2010	2011
Cash flows from financing activities:			
Proceeds from exercise of employee stock options	372	114	9
Receipt of long term loan	-	-	30,000
Repayment of Long term loan	-	-	(2,984)
Net cash provided by financing activities	372	114	27,025
Increase (decrease) in cash and cash equivalents	5,405	(7,783)	(3,510)
Cash and cash equivalents at the beginning of the year	63,675	69,080	61,297
Cash and cash equivalents at the end of the year	$69,080	$61,297	$57,787
Supplemental disclosure of cash flows activities:			
Cash paid during the year for taxes	$461	$572	$500
(a) Payment for the acquisition of Wavion:			
Estimated fair value of assets acquired and liabilities assumed at the acquisition date:			
Working capital deficit (excluding cash and cash equivalents)	$-	$-	$102
Property and equipment	-	-	1,317
Accrued severance pay	-	-	(203)
Other intangible assets	-	-	22,009
Goodwill	-	-	13,087
Less - accrued OCS commitment	-	-	(5,992)
Long-term loan	-	-	(2,984)
	-	-	27,336
Less - accrued earn out payment	-	-	(2,718)
	$-	$-	$24,618

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

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

NOTE 1:- GENERAL

a. Alvarion Ltd. together with its worldwide subsidiaries ("the Company") is a provider of wireless broadband systems. The Company supplies top-tier carriers, Internet Service Providers ("ISPs") and private networks in vertical markets with solutions based on WiMAX, Wi-Fi and other wireless broadband technologies.

As for geographic markets and major customers, see Note 14.

b. Acquisition of Wavion:

On November 23, 2011, the Company completed the acquisition of all of the outstanding shares of Wavion Inc. and its subsidiary (together “Wavion”), a technology leader in outdoor WiFi applications for metro and rural areas with deployments in more than 75 countries. Wavion offers end-to-end solutions including access, backhaul, CPEs, management and service provisioning tools, and was acquired for for an aggregate consideration of $ 28,433. The total purchase price of Wavion was composed of the following:

Cash	$ 25,715
Earn out *)	2,718
Total purchase price	$ 28,433

*) The agreement stipulated for an Earn out based on performance milestones for up to an amount of $3,750. The performance milestone was for the period from acquisition date through December 31, 2011. The actual calculated Earn out amounted to $2,718 based on Wavion's result for the stipulated period and has been paid subsequent to the balance sheet date.

The acquired business provides a significant new market opportunity. The cash consideration was financed by a loan that we received from Silicon Valley Bank (“SVB”) (see Note 10) . The Company believes that the acquisition of Wavion will enable the Company to expand our solutions and to become a multi-technology wireless broadband solution powerhouse.

Certain shareholders are entitled to $ 785 if they will complete a retention period as Wavion's employees. This amount was placed in escrow as an assurance for employees' undertaking to continue their employment with the Company. If an employee does not complete full term of retention, the amount in escrow related to him will be released to the Company. This amount will be recorded as compensation and not as part of the purchase price of Wavion. As of December 31, 2011 there is a short term and long term prepaid balance of $ 565 and $ 171 relating to this amount, which will be recorded as compensation expense on a straight line basis over the retention period.

The acquisition was accounted for by the acquisition method. The results of operations were included in the consolidated financial statements of the Company commencing November 23, 2011. The consideration for the acquisition was attributed to acquired net assets and assumed liabilities on the basis of their fair value, based on a valuation performed by an outsourced advisor which included a number of factors.

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

NOTE 1:- GENERAL (Cont.)

Identifiable intangible assets acquired included Customer relationships and Backlog which were valued using the income approach, and Technology which was valued using the income approach, specifically the “Relief From Royalty method”.

The Company also assumed a liability related to Wavion's Officer Chief Scientist ("OCS") royalty bearing grant obligation. The liability was valued based on 100% of the outstanding obligation discounted based on a Market Participant interest rate.

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

Cash	$1,097
Trade receivables	3,760
Other receivables and prepaid expenses	942
Current deferred tax assets	1,334
Inventories	1,436
Property and equipment	1,317
Long-term deferred tax assets	6,480
Other intangible assets	22,009
Goodwill	13,087
Total assets acquired	51,462
Trade payables	(3,553)
Accrued expenses and other liabilities	(3,532)
Other long-term liabilities	(4,943)
Severance pay	(203)
Long-term loan	(2,984)
Long-term deferred tax liabilities	(7,814)
Total liabilities assumed	(23,029)
Net assets acquired	$28,433

The excess of cost of acquisition over the fair value of net tangible and identifiable intangible assets on acquisition amounted to $13,087, and was allocated to goodwill, which is due to primarily the expected synergies.

As part of the acquisition the Company incurred certain acquisition related expenses in an aggregate amount of $1,122. These expenses, as well as other transaction related expenses, have been recorded as Acquisition related expenses in the statement of operation.

Below are certain unaudited pro forma combined statements of income data for the years ended December 31, 2010 and 2011, as if the acquisition had occurred January 1, 2010, after giving effect to purchase accounting adjustments, including amortization of identifiable intangible assets. This pro forma financial information is not necessarily indicative of the combined results that would have been attained had the acquisition taken place at the beginning of 2010, nor is it necessarily indicative of future results. The amounts of revenue and earnings of Wavion since the acquisition date included in the consolidated statement for the the year ended December 31, 2011 was $ 4,316 and $1,013, respectively.

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

NOTE 1:- GENERAL (Cont.)

	Year ended December 31,	
	2010 Unaudited	2011 Unaudited
Total revenues	$ 215,413	$ 208,456
Net loss	106,409	42,738
Net loss per share basic and diluted	$ 1.71	$ 0.69

c. Acquisition of Clariton:

At the beginning of 2011, the Company acquired the intellectual property of Clariton Ltd., ("Clariton") for indoor wireless solution called Clariton's Distributed Antenna System (DAS) for no consideration. The Company also assumed Clariton's related OCS royalty bearing grant obligation, Clariton Networks.

d. Alvarion Ltd. has wholly-owned active subsidiaries in the United States, France, Romania, Brazil, Singapore, Mexico, Poland, Uruguay, Spain, South-Africa, Italy, Argentina, India, Chile, Taiwan, Indonesia, Canda, Japan and the Philippines primarily engaged in marketing, pre-sales, sales and developing activities.

e. Certain of the raw materials, components, and subassemblies included in the products manufactured by the Company's subcontractors, are obtained from and manufactured by a limited group of suppliers and manufaturers. Disruptions, shortages, termination of certain of these sources of supply, or termination of manufacturing subcontractors agreements could occur and could negatively affect the Company's financial condition and results of operations.

f. Discontinued operations of the Cellular Mobile Unit ("CMU"):

In September 2007, the Company converted convertible notes into LGC Wireless Inc. ("LGC") Common shares as part of an agreement to sell substantially all of the Company's assets and certain liabilities related to the Company's CMU, representing the majority of former interWAVE Communications International Ltd ("interWAVE") business. On November 30, 2007, ADC Telecommunication Inc. ("ADC"), a U.S. publicly traded company, completed its acquisition of LGC. As of December 31, 2008, the Company received approximately $ 16,100, out of which approximately $ 8,900 was received during 2008, in respect of the Common shares of LGC while an additional $ 1,000 was secured in escrow. During the year ended December 31, 2009 the Company received approximately $ 700 and the residual $ 300 represented all indemnification obligations, costs and expenses. The amount received of approximately $700 was recorded as additional proceeds in 2009 as "other income".

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

NOTE 1:- GENERAL (Cont.)

g. Goodwill impairment:

In accordance with ASC 350 "Intangibles - Goodwill and Others", the Company tests for goodwill impairment on an annual basis for its single reporting unit. The continuing global economic downturn during 2010 had negatively affected the Company and significantly reduced the Company's market capitalization. As a result of its impairment test, the Company determined that there would be no implied value attributable to its reporting unit's goodwill and fully impaired the recorded amount.

The Goodwill as of December 31, 2011 resulted from Wavion's acquisition. See also Note 2j.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements are prepared in accordance with U.S generally accepted accounting principles ("U.S. GAAP").

a. Use of estimates:

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates, judgments and assumptions. The Company's management believes that the estimates, judgments and assumptions used are reasonable based upon information available at the time they are made. These estimates, judgments and assumptions can 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

b. Financial statements in U.S. dollars ("dollars"):

A majority of the Company's revenues are generated in dollars. In addition, most of the Company's costs are denominated and determined in dollars. The Company's management believes that the dollar is the currency in the primary economic environment in which the Company operates. Thus, the functional and reporting currency of the Company is the dollar.

Accordingly, monetary accounts maintained in currencies other than the dollar are remeasured into dollars in accordance with Accounting Standards Codification ("ASC") 830, "Foreign Currency Matters". All transaction gains and losses from the remeasurement of monetary balance sheet items are reflected in the statement of operations as appropriate.

c. Principles of consolidation:

The consolidated financial statements include the accounts of Alvarion Ltd. and its wholly-owned subsidiaries. Intercompany transactions and balances, including profits from intercompany sales not yet realized outside the Company, have been eliminated in consolidation.

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

d. Cash equivalents:

Cash equivalents are short-term highly liquid investments that are readily convertible to cash, with maturities of three months or less at the date acquired.

e. Short-term bank deposits:

Bank deposits with maturities of more than three months and up to one year were included in short-term bank deposits. As of December 31, 2010 and 2011, most of the bank deposits are in U.S. dollars and bore interest at a weighted average interest rate of 0.81% and 2.48%, respectively. The deposits are presented at their cost, including accrued interest.

f. Held-to-maturity securities:

The Company accounts for investments in debt securities in accordance with ASC 320 "Investments - Debt and Equity Securities".

Management determines the appropriate classification of its investments in debt securities at the time of purchase and reevaluates such determinations at each balance sheet date. Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity, and are stated at amortized cost. The amortized cost of held-to-maturity securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization, impairment of value judged to be other than temporary, and interest are included in financial income, net.

For the years ended December 31, 2009, 2010 and 2011, all securities covered by ASC 320 were designated by the Company's management as held-to-maturity.

The Company recognizes an impairment charge when a decline in the fair value of its investments below the amortized cost basis is judged to be other-than-temporary. The Company periodically assesses whether its investments with unrealized losses are other than temporarily impaired.

Under the impairment model, an other-than-temporary impairment loss is recognized in earnings when the Company does not expect to recover the entire amortized cost basis of the security (that is, a credit loss exists). The amount of impairment to be recognized in earnings is limited to the amount related to credit losses, while impairment related to other factors is recognized in other comprehensive income.

For the years ended December 31, 2009, 2010 and 2011, no other-than-temporary impairment losses have been identified.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

g. Inventories:

The Company manages its inventory according to the FIFO method.

Inventories are stated at the lower of cost or market value. Cost is determined as follows:

Raw materials and components - using the "weighted moving average cost" method.

Work in progress and finished products are based on the cost of raw materials and components used and the cost of production including labor and overhead calculated on a periodic basis.

Inventory write-offs have been provided to cover risks arising from dead and slow moving items, technological obsolescence and excess inventories according to revenue forecasts.

During 2009, 2010 and 2011, the Company recorded inventory write-off for inventory and for inventory purchase commitments, for inventory no longer required in a total amount of $ 3,993, $ 4,897 and $ 2,580, respectively.

In 2009, 2010 and 2011, approximately $ 578, $ 388 and $ 375, respectively, of inventory previously written-off was used as product components in the Company's ordinary production course and was sold as finished goods to end users. The sales of these related manufactured products were reflected in the Company's revenues without an additional charge to the cost of sales in the period in which the inventory was utilized.

h. Property and equipment, net:

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

	%
Office furniture and equipment	6 - 15
Computers and electronic equipment	14 - 33
Motor vehicles	15
Leasehold improvements	Over the shorter of the related lease period or the life of the asset

i. Impairment of long-lived assets:

The Company's property and equipment and certain identifiable intangible assets are reviewed for impairment in accordance with ASC 360, "Property, Plant, and Equipment", whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Intangible assets that are not considered to have an indefinite useful life have been amortized using the straight-line basis over their estimated useful lives (Customer relationship 6 years and Technology 4-12 years). Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the future undiscounted cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets (or asset group) exceeds the fair value of the assets (or asset group). For the year ended December 31, 2009, no impairment losses were recorded. As of December 31, 2010, all of the Company's intangible assets have been amortized or written off. In November 2011 due to the completion of Wavion acquisition, the Company recorded intangible assets in an amount of $22,009. Since the acquisition date, no indications for impairment have been noted.

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

j. Goodwill:

The Company reviews goodwill for impairment annually and whenever events or changes in circumstances indicate its carrying value may not be recoverable in accordance with ASC 350 "Intangibles - Goodwill and Others".

Goodwill impairment testing is a two-step process. The first step involves comparing the fair value of a company's reporting units to their carrying amount. If the fair value of the reporting unit is determined to be greater than its carrying amount, there is no impairment. If the reporting unit's carrying amount is determined to be greater than the fair value, the second step must be completed to measure the amount of impairment, if any. Step two calculates the implied fair value of goodwill by deducting the fair value of all tangible and intangible assets, excluding goodwill, of the reporting unit from the fair value of the reporting unit as determined in step one. The implied fair value of the goodwill in this step is compared to the carrying value of goodwill. If the implied fair value of the goodwill is less than the carrying value of the goodwill, an impairment loss equivalent to the difference is recorded.

For purposes of testing goodwill in accordance with ASC 350 for the year ended December 31, 2010, the Company operated in one operating segment, and this segment comprises of a single reporting unit. During 2010, the global economic downturn had negatively affected the Company's results of operations with a significant reduction in the Company's market capitalization. In calculating the fair value of the reporting unit, the Company used Discounted Cash Flow (DCF) approach. The Company further applied a market approach, using multiples of earnings, to corroborate the results achieved in the estimated discounted cash flows model. As a result of performing step two, the Company's implied fair value of the reporting unit goodwill has decreased to zero.

For the year ended December 31, 2009 no impairment losses were recorded; In 2010, the Company recorded impairment of the outstanding Goodwill balance in the amount of $ 57,106.

The acquisition of Wavion in November 2011 has been incorporated into the single reportable segment of the Company. Nevertheless, Wavion’s full integration into the activity of the Company has not yet been completed. As part of Wavion acquisition, the Company recorded goodwill in amount of $13,087. Since the transaction occurred in November 2011, there are no indicators of impairment at December 31, 2011 and no outstanding Goodwill balances remained prior to the acquition, no annual impairment test has been completed and no impairment has been recorded in 2011.

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

k. Income taxes:

The Company accounts for income taxes in accordance with ASC 740, "Income Taxes". This guidance prescribes the use of the liability method whereby deferred tax asset and liability account balances are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company provides a valuation allowance, if necessary, to reduce deferred tax assets to the amount that is more likely than not to be realized. The operating expenses for the year ended December 31, 2009 includes $ 783 income tax expenses respectively. These expenses were not presented in income tax due to immateriality.

The Company implements a two-step approach to recognize and measure uncertain tax positions. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% (cumulative basis) likely to be realized upon ultimate settlement.

The Company recognizes interest, if any, related to unrecognized tax benefits in financial expenses. The Company recognizes penalties, if any, related to unrecognized tax benefits for the year ended December 31, 2009 in general and administrative expenses and for the years ended December 31, 2010 and 2011 in taxes on income.

l. Accounting for stock-based compensation:

The Company accounts for stock-based compensation in accordance with ASC 718 Compensation - Stock Compensation. ASC 718 requires companies to estimate the fair value of equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company's consolidated statements of operations.

During 2008, the Company granted 963,000 options at par value and Restricted Shares Unit to Management and Senior Executives, the vesting of which is subject to the Company achieving certain performance related ratios, 33% of each grant's vesting being accrued respectively on February 28, 2010, February 28, 2011 and February 28, 2012. The Company accounts for these grants in accordance with ASC 718 and estimates the fair value of equity based payment awards only when the achieving the performance criteria is probable. As of December 31, 2011, the performance related ratios for the first and second installments have not achieved, and the corresponding part (66%) of the grant has been cancelled. Further, the Company estimates that it is less than probable that the last installments' performance related ratio criteria will be achieved and has not recorded any expenses related to this equity based award. Subsequent to balances sheet date, the February 2012 performance criteria has not been met and an additional corresponding (33%) of the grant has been cancelled.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company recognizes compensation expenses for the value of its awards granted based on the straight line method over the requisite service period of each of the awards, net of estimated forfeitures. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Estimated forfeitures are based on actual historical pre-vesting forfeitures.

The Company estimates the fair value of stock options granted under ASC 718 using the Black-Scholes-Merton option-pricing model that uses the weighted-average assumptions noted in the following table. The Company values restricted stock units and options granted at par value based on the market value of the underlying shares at the date of grant.

Expected volatility is based on historical volatility that is representative of future volatility over the expected term of the options. In 2009, 2010 and 2011, the expected term of options granted is estimated based on historical experience and represents the period of time that options granted are expected to be outstanding. The risk free interest rate is based on the yield of U.S. treasury bonds with equivalent terms. The dividend yield is based on the Company's historical and future expectation of dividends payouts. Historically, the Company has not paid cash dividends and has no foreseeable plans to pay cash dividends in the future.

	Year ended December 31,		
	2009	2010	2011
Volatility	56.1%	56.5%	59.4%
Risk-free interest rate	2.5%	1.45%	1.40%
Dividend yield	0%	0%	0%
Expected term	4.7 years	4.47 years	4.21 years
Average Forfeiture rate	8%	13%	19%

The Company's annual compensation cost for the years ended December 31, 2009, 2010 and 2011 totaled $ 4,246, $ 3,334 and $ 3,153, respectively.

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The total equity-based compensation expense related to all of the Company's equity-based awards, recognized for the years ended December 31, 2009, 2010 and 2011, was comprised as follows:

	Year ended December 31,		
	2009	2010	2011
Cost of goods sold	$ 331	$ 434	$ 295
Research and development	1,553	780	495
Sales and marketing	1,204	733	775
General and administrative	1,158	1,387	1,588
Equity-based compensation expenses	$ 4,246	$ 3,334	$ 3,153

m. Revenue recognition:

The Company generates revenues from sales of products, which include hardware and software, professional services and maintenance. Professional services include mainly installation, project management, consulting and training. The Company sells its products directly through its sales force and indirectly through a global network of distributors, system integrators and strategic partners, all of whom are considered end-users.

Revenues from maintenance and professional services are recognized ratably over the contractual period or as services are performed, respectively.

Revenues from products are recognized in accordance with ASC 605-10-S99-1 ("Revenue Recognition") and with ASC 605-25 "Multiple-Element Arrangements" as amended by ASU 2009-13, when the following criteria are met: persuasive evidence of an arrangement exists, delivery has occurred, the seller's price to the buyer is fixed or determinable, no further obligation exists and collection is probable.

The Company generally does not grant a right of return. However, the Company has granted to certain distributors limited rights of return on unsold products. Product revenues on shipments to these distributors are recognized based on their history of actual returns provided that all other revenue recognition criteria are met.

Starting January 1, 2011 the Company adopted the guidance of ASU 2009-13 "Multiple-Deliverable Revenue Arrangements", (amendments to FASB ASC Topic 605, Revenue Recognition) ("ASU 2009-13") and ASU 2009-14, "Certain Revenue Arrangements That Include Software Elements", (amendments to FASB ASC Topic 985, Software) ("ASU 2009-14"). ASU 2009-13 requires entities to allocate revenue in an arrangement using estimated selling prices of all deliverables in an arrangement based on a selling price hierarchy. The amendment eliminates the residual method of revenue allocation and requires revenue to be allocated using the relative selling price method. ASU 2009-14 removes tangible products from the scope of software revenue guidance and provides guidance in determining whether software deliverables in an arrangement that includes a tangible product are covered by the scope of the software revenue guidance. Company's management determined that the software is incidental to the product as a whole and therefore ASC 985-605 and ASU 2009-14 should not apply.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company prospectively applied these provisions to all revenue arrangements entered into or materially modified after January 1, 2011. This guidance does not generally change the units of accounting for the Company’s revenue transactions. Most products and services qualify as separate units of accounting and the revenue is recognized when the applicable revenue recognition criteria are met. The Company’s arrangements generally do not include any provisions for cancellation, termination, or refunds that would significantly impact recognized revenue. While certain of the Company’s bundled products are now accounted for following the ASU 2009-13 amendments to ASC 605, the impact of the adoption of these standards was immaterial in 2011 and is expected to remain so in periods after adoption.

The Company's revenue recognition policies provide that, when a sales arrangement contains multiple elements, the Company allocates revenue to each element based on a selling price hierarchy. The selling price for a deliverable is based on its vendor specific objective evidence ("VSOE"), if available, third party evidence ("TPE") if VSOE is not available, or estimated selling price ("ESP") if neither VSOE nor TPE is available. The Company establishes VSOE of selling price using the price charged for a deliverable when sold separately and, when they have not yet sold the deliverable separately, using the price established by management having the relevant authority. When VSOE cannot be established, the Company establishes selling price of each element based on TPE. TPE is determined based on competitor prices for similar deliverables when sold separately. The best estimate of selling price is established considering several external and internal factors including, but not limited to, historical sales, pricing practices and geographies in which the Company offers its products. The determination of ESP is judgmental.

For arrangements which include multiple elements, the Company considers the sale of equipment, professional services and maintenance to be three separate units of accounting in the arrangement in accordance with ASC 605-25, Since all three elements have value to the customer on a standalone basis.

Equipment includes the software as the software is deemed incidental to the product as a whole. The Equipment element price was obtained by using management’s best estimate based on the historical prices sold by the Company. The historical prices have been allocated based on product and region, due to variances between the regions in which the products have been sold.

Professional Services prices were based on TPE for which the Company has accumulated the prices from its suppliers throughout the year.

Maintenance price has been established using VSOE of the selling price of maintenance services, based on the price charged when sold separately at renewal.

In transactions where a customer's contractual terms include a provision for customer acceptance, revenues are recognized either when such acceptance has been obtained or the acceptance provision has lapsed.

Advances from customers include advances and payments received from customers, for which revenue has not yet been recognized.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

n. Warranty costs:

The Company provides a 14 to 21 month warranty period for all of its products lines. The specific terms and conditions of a warranty vary depending upon the product sold and customer it is sold to. The Company estimates the costs that may be incurred under its warranty and records a liability in the amount of such costs at the time a product is delivered. Factors that affect the Company's warranty liability include the number of units, historical rates of warranty claims and cost per claim. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

Changes in the Company's warranty allowance during the period are as follows:

	Year ended December 31,		
	2009	2010	2011
Balance at the beginning of the year	$ 3,186	$ 1,880	$ 1,605
Warranties issued during the year	1,552	1,447	500
Settlements/adjustments made during the year	(2,858)	(1,722)	(1,457)
Balance at the end of the year	$ 1,880	$ 1,605	$ 648

o. Research and development:

Research and development costs, net of participation funding received and grants, are charged to the statement of operations as incurred. See also Note 15b.

p. Participations and grants:

Grants and participations received for funding approved research and development projects are recognized at the time the Company is entitled to such grants, on the basis of the costs incurred and included as a deduction from research and development costs.

q. Severance pay and long term employee liabilities:

The Company's agreements with the majority of its employees in Israel are under section 14 of the Severance Pay Law -1963. The Company's contributions for severance pay shall be instead of its severance liability. Upon contribution of the full amount from the employee's monthly salary, no additional calculations shall be conducted between the parties regarding the matter of severance pay and no additional payments shall be made by the Company to the employee. Further, the related obligation and amounts deposited on behalf of such obligation are not stated on the balance sheet, as the Company is legally released from obligation to employees once the deposit amounts have been paid.

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Additional payments have been paid to Company's employees at the time of termination by the Company. The estimation of those payments is appropriately recorded as a liability at each of the balance sheet date.

Severance pay expenses for the years ended December 31, 2009, 2010 and 2011 were $ 3,059, $ 3,059 and $ 2,218, respectively.

r. Advertising expenses:

Advertising expenses are carried to the statement of operations as incurred. Advertising expenses for the years ended December 31, 2009, 2010 and 2011 were $ 1,923, $ 1,652 and $ 1,094, respectively.

s. Basic and diluted net loss per share:

Basic net loss per share is computed based on the weighted average number of Ordinary shares outstanding during each year. The diluted net earnings per share are computed based on the weighted average number of Ordinary shares outstanding during each year plus dilutive potential equivalent Ordinary shares considered outstanding during the year, in accordance with ASC 260, "Earnings Per Share". For the years ended December 31, 2009, 2010 and 2011, all outstanding options to purchase shares were excluded from the calculation of diluted loss per share because their effect on the loss per share is anti-dilutive.

t. Concentration of credit risk:

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, short-term bank deposits, marketable securities, trade receivables and foreign currency derivative contracts.

The majority of the Company's cash and cash equivalents and short-term bank deposits are invested in U.S. dollar deposits with major U.S., European and Israeli banks, and the foreign currency derivative contracts are with the same banks. Deposits in the U.S. may be in excess of insured limits and are not insured in other jurisdictions. Generally cash and cash equivalents and short term deposits may be redeemed on demand and therefore low credit risk exists with respect to these investments.

The Company's marketable securities include investments in debentures of U.S. corporations and U.S. government agencies.

Since the turmoil in capital markets the Company tightened its control and monitoring over its marketable securities portfolio in order to minimize potential risks. Such measures included among others: Company's investment policy is approved by the Investment Committee, limits on the amount the Company may invest in any one type of investment or issuer and the grade of the security, thereby reducing credit risk concentrations.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The trade receivables of the Company are derived from sales to customers located primarily in North and South America, Asia Pacific, Africa and Europe and represent amounts with maturity dates of less than one year. Customers balances with maturity dates exceeding one year, are disclosed as Long Term Trade Receivables. Under certain circumstances, the Company and its subsidiaries may require letters of credit, other collateral, additional guarantees or advance payments. The Company obtains credit insurance where applicable. The Company and its subsidiaries perform ongoing credit evaluations of their customers and establish an allowance for doubtful accounts based upon a specific review of their accounts.

Allowance for doubtful accounts amounted to $ 5,052 and $ 5,525 as of December 31, 2010 and 2011, respectively. Balance as of December 31, 2011, includes allowance for doubtful accounts from Wavion acquisition in amount of $294. The Company charges off receivables when they are deemed uncollectible. Actual collection experience may not meet expectations and there may be an effect in the Company's ability to collect customers' debts in a timely manner or at all and this may result in increased bad debt expense.

Total doubtful debts expenses during 2009, 2010 and 2011 amounted to $ 904, $ 4,604 and $ 1,994, respectively. The 2010 expense is mainly a result of a single customer for which the Company deemed the balance as uncollectable. Total write offs amounted $ 0, $ 690 and $ 1,815 in 2009, 2010 and 2011, respectively.

u. Fair value of financial instruments:

Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value:

Level 1 - Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 - Includes other inputs that are directly or indirectly observable in the marketplace.

Level 3 - Unobservable inputs which are supported by little or no market activity.

The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

In accordance with ASC 820 "Fair Value Measurements and Disclosures", the Company measures its foreign currency derivative contracts at fair value using a market approach valuation technique based on marketplace observable inputs foreign exchange rates, as follows:

	December 31, 2011 Fair value measurements using input type			
	Level 1	Level 2	Level 3	Total
Assets:				
Foreign currency option	$ -	$ 16	$ -	$ 16
Foreign currency forwards	-	86	-	86
Total financial assets	$ -	$ 102	$ -	$ 102
Liabilities:				
Foreign currency option	$ -	$ 1,033	$ -	$ 1,033
Foreign currency forwards	-	1,657	-	1,657
Total financial liabilities	$ -	$ 2,690	$ -	$ 2,690

	December 31, 2010 Fair value measurements using input type			
	Level 1	Level 2	Level 3	Total
Assets:				
Foreign currency option	$ -	$ 524	$ -	$ 524
Foreign currency forwards	-	2,176	-	2,176
Total financial assets	$ -	$ 2,700	$ -	$ 2,700
Liabilities:				
Foreign currency option	$ -	$ 41	$ -	$ 41
Foreign currency forwards	-	133	-	133
Total financial liabilities	$ -	$ 174	$ -	$ 174

The carrying amounts of cash and cash equivalents, short-term bank deposits, trade receivables, trade payables and loan approximate their fair values, due to the short-term maturities of these instruments.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

v. Derivative instruments:

The Company accounts for derivatives and hedging based on ASC 815 "Derivatives and Hedging". ASC 815 requires a company to recognize all derivative instruments on the balance sheet at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship. For those derivative instruments that are designated and qualify as hedging instruments, a company must designate the hedging instrument, based upon the exposure being hedged, as a fair value hedge, cash flow hedge or a hedge of a net investment in a foreign operation.

The Company has instituted a foreign currency cash flow hedging policy in order to hedge against the risk of overall changes in future cash flows for a period of approximately 1 year resulting from foreign currency trade payables and salary payments during the year. The Company hedges portions of its forecasted expenses denominated in NIS and Romanian New Lei ("RON") with currency forwards contracts and put and call options. These forward and option contracts are designated as cash flow hedges. The Company does not have a master netting policy and as such each arrangement is accounted for separately.

For derivative instruments that are designated and qualify as a cash flow hedge (i.e., hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income (loss) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item, if any, is recognized in current earnings during the period of change. For derivative instruments not designated as hedging instruments, the gain or loss is recognized in current earnings during the period of change.

During 2010-2011 the Company performed organizational changes and headcount reductions, and as a result the payroll and trade payables payments have decreased. There was an ineffective portion of the hedging in an amount of $96 and $ 3, respectively which has been recognized in statement of operations in the financial income (expense) net, as ineffective hedge portion. The Company does not enter into derivative transactions for trading purposes.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

As of December 31, 2011, the Company recorded accumulated other comprehensive loss in the net amount of $ 2,674 (as further detailed in the following tables) from its currency forward and put and call options transactions with respect to trade payables and payroll expenses expected to be incurred during 2012 and 2013. Such amount will be reclassified into earnings within the next 13 months.

The notional principal of foreign exchange contracts to purchase NIS with U.S. dollars was $39,700 and $ 81,158 at December 31, 2010 and 2011, respectively. The notional principal of foreign exchange contracts to purchase RON with U.S. dollars was $ 3,750 and $ 5,750 at December 31, 2010 and 2011, respectively.

The fair value of the Company's outstanding derivative instruments qualified as hedging instruments at December 31, 2010 and 2011 is summarized below:

	Balance sheet location	December 31, 2010	December 31, 2011
Assets			
Foreign exchange option contracts	Other accounts receivable and prepaid expenses	$ 523	$ 16
Foreign exchange forward contracts		2,116	-
		$ 2,639	$ 16
Liabilities			
Foreign exchange option contracts	Other accounts payable and accrued expenses	$ (40)	$ (1,033)
Foreign exchange forward contracts		-	(1,657)
		$ (40)	$ (2,690)
Derivatives assets (liabilities), net		$ 2,599	$ (2,674)

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The effect of derivative instruments in cash flow hedging relationships on income (loss) and other comprehensive income (loss) for the years ended December 31, 2009, 2010 and 2011 is summarized below:

	Increase (decrease) in gains recognized in other comprehensive income (loss) on derivative (effective portion) Year ended December 31,		
	2009	2010	2011
Derivative in cash flow hedging relationship			
Foreign exchange option contracts	$ 3,781	$ 662	$ (1,177)
Foreign exchange forward contracts	2,124	2,428	(1,229)
	$ 5,905	$ 3,090	$ (2,406)

The following is the change in the other comprehensive income (loss) of unrealized gains on foreign currency cash flow hedge during 2011:

	Other comprehensive income (loss)
Other comprehensive income from unrealized gains on foreign currency cash flow hedge as of January 1, 2011	$ 2,599
Reclassification to earnings of realized gains on foreign currency cash flow hedge	(2,867)
Unrealized net losses on foreign currency cash flow hedge	(2,406)
Other comprehensive loss from losses on foreign currency cash flow hedge as of December 31, 2011	$ (2,674)

		Gains (losses) reclassified from other comprehensive income (loss) into income (expenses) (effective portion) Year ended December 31,		
	Location	2009	2010	2011
Derivative in cash flow hedging relationship				
Foreign exchange option contracts	Cost of sales and operating expenses	$ (2,390)	$ 175	$ 273
Foreign exchange forward contracts	Cost of sales and operating expenses	(207)	2,441	2,591
		$ (2,597)	$ 2,616	$ 2,864

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company entered into forward contracts to hedge the fair value of assets and liabilities denominated in Euros. As of December 31, 2010, the Company had outstanding forward contracts that did not meet the definition of hedge accounting, in the notional amount of $ 5,938, the fair value of which is presented in other accounts payable and accrued expenses, and in the notional amount of $ 1,395 the fair value of which is presented in other accounts receivable and prepaid expenses. These contracts were for a period of up to twelve months. As of December 31,2011, the Company had outstanding forward contracts that did not meet the definition of hedge accounting, in the notional amount of $1,142, the fair value of which is presented in other accounts receivable and prepaid expenses. The Company measured the fair value of the contracts in accordance with ASC 820 at level 2. The net gains (losses) recognized in statement of operations in the financial income (expenses) net during 2009, 2010 and 2011 were $ (128), $ 528 and $ (307), respectively.

w. Comprehensive income:

The Company accounts for comprehensive income in accordance with ASC 220 "Comprehensive Income". This Statement establishes standards for the reporting and display of comprehensive income and its components in a full set of general purpose financial statements. Comprehensive income generally represents all changes in shareholders' equity during the period except those resulting from investments by, or distributions to, shareholders. The Company determined that its items of comprehensive income relate to gains and losses on hedging derivative instruments.

x. Treasury stock:

The Company repurchases its Ordinary shares from time to time in the open market and holds such shares as treasury stock. The Company presents the cost to repurchase treasury stock as a reduction of shareholders' equity.

y. Investment in affiliate:

The Company accounts for its investment in an affiliate in which the Company holds less than 20%, using the cost method of accounting since the Company does not have the ability to exercise significant influence over operating and financial policies of this investee.

The Company's investment is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the investment may not be recoverable. Following the Company's decision not to continue funding the affiliate, the Company's holding was diluted into an immaterial amount during 2009, and the Company recorded an impairment of the entire investment in the amount of $ 1,554 in the year end December 31, 2009.

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

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

z. Restructuring and other charges:

During 2009 and 2010, the Company implemented separate restructuring plans, their main purposes were to close and minimize several internal activities, reorganize its units, and reduce headcount of approximately 90 and 160 employees, respectively. During 2011 the Company implemented an additional plan for cost reduction and organizational changes to certain of the Company's units of operations and reduced by 194 the Company's headcount. The Company recorded in 2009, 2010 and 2011 charges of $ 2,787, $ 3,573 and $ 12,040, respectively. In addition to the charges to short and long term accrued amounts below, these charges included $ 282, $ 343 and $ 650, respectively, related to write-offs of leasehold improvements due to abandonment of rental premises as a result of the above mentioned plans. The 2011 plan also included costs amounting to approximately $ 3,000 due to fixed assets disposals, $ 154 due to reverse of grants receivable and $ 359 prepaid service R&D. The Company has accounted for the restructuring and cost reduction plans in accordance with ASC 420 "Exit or Disposal Cost Obligations".

As of December 31, 2011, the short term components of the restructuring and cost reduction plan accrual are as follows:

	Employee termination benefits	Repayments of grants	Lease abandonment	Other	Total
Balance as of January 1, 2010	$ 1,190	$ 923	$ 340	$ 42	$ 2,495
Charges	1,868	-	1,175	186	3,229
Cash outlays	(2,777)	-	(917)	(175)	(3,869)
Balance as of December 31, 2010	281	923	598	53	1,855
Charges (Reverse)	2,954	(923)	3,158	1,526	6,715
Cash outlays	(1,785)	-	(1,881)	(427)	(4,093)
Balance as of December 31, 2011	$ 1,450	$ -	$ 1,875	$ 1,152	$ 4,477

As of December 31, 2011, the long term components of the cost reduction plan amounted to $ 547 and are presented as Long term accrued expenses. These costs are due to lease abandonment and are expected to be paid during 2013.

The restructuring and other charges do not include the impact related to stock based compensation (for stock based compensation see Note 12c).

aa. Transfers of financial assets:

ASC 860 "Transfers and Servicing", establishes a standard for determining when a transfer of financial assets should be accounted for as a sale. The Company's arrangements are such that the underlying conditions are met for the transfer of financial assets to qualify for accounting as a sale, excluding transactions presented below as a secured borrowing. The transfers of financial assets are typically performed by the factoring of receivables to three Israeli financial institutions.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

During the years ended December 31, 2009, 2010 and 2011, the Company sold trade receivables to Israeli financial institutions in a total amount of $ 44,991, $ 43,046 and $ 52,303, respectively. Control and risk of those trade receivables were fully transferred in accordance with ASC 860. As of December 31, 2010 and 2011, the Company had a transaction that did not meet the guidance of ASC 860 and is presented as a secured borrowing as part of other accounts payable and accrued expenses in the amount of $ 1,770 and $ 987, respectively.

The agreements, pursuant to which the Company sells its trade receivables, are structured such that the Company (i) transfers the proprietary rights in the receivable from the Company to the financial institution; (ii) legally isolates the receivable from the Company's other assets, and presumptively puts the receivable beyond the lawful reach of the Company and its creditors, even in bankruptcy or other receivership; (iii) confers on the financial institution the right to pledge or exchange the receivable; and (iv) eliminates the Company's effective control over the receivable, in the sense that the Company is not entitled and shall not be obligated to repurchase the receivable other than in case of failure by the Company to fulfill its commercial obligation.

The aggregate amounts of financing expense related to the sales of trade receivables for the years ended December 31, 2009, 2010 and 2011 were $ 661, $ 578 and $ 818, respectively.

ab. Business Combination:

According to ASC 805 "Business Combination", the Company recognizes assets acquired, liabilities assumed and any non-controlling interest at the acquisition date measured at their fair values as of that date. ASC 805 also requires the fair value of acquired in-process research and development to be recorded as intangibles with indefinite lives, contingent consideration to be recorded on the acquisition date, and restructuring and acquisition-related deal costs to be expensed as incurred. According to ASC 805, the Company is required to allocate the purchase price of acquired companies to the tangible and intangible assets acquired, and liabilities assumed based on their estimated fair values. In allocating the purchase price of acquired companies to the tangible and intangible assets acquired and liabilities assumed, the Company developed the required assumptions underlying the valuation work. Critical estimates in valuing certain of the intangible assets include but are not limited to: future expected cash flows from customer contracts, customer lists and distribution agreements,. Management’s estimates of fair value are based upon assumptions believed to be reasonable, utilizing a market participant approach, but which are inherently uncertain and unpredictable. Assumptions may be incomplete or inaccurate, and unanticipated events and circumstances may occur.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

ac. Impact of recently issued Accounting Standards:

In May 2011, the Financial Accounting Standards Board, or FASB issued ASU 2011-04 Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs, codified in ASC 820 "Fair Value Measurement". The guidance requires an entity to use a consistent definition of fair value to ensure that the fair value measurement and disclosure requirements are similar between U.S. GAAP and International Financial Reporting Standards. The guidance changes certain fair value measurement principles and enhances the disclosure requirements particularly for Level 3 fair value measurements, and will become effective for the Company beginning January 1, 2012. The Company does not expect the adoption of this new guidance to have a material impact on its financial statements.

In June 2011, the FASB issued ASU 2011-05 Presentation of Comprehensive Income, codified in ASC 220 "Comprehensive Income". The guidance requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The guidance also eliminates the option to present the components of other comprehensive income as part of the statement of equity. In December 2011, the FASB issued ASU 2011-12, deferring indefinitely the effective date for some of the amendments outlined in ASU 2011-05, but the remainder of its provisions will become effective for the Company beginning January 1,2012. The Company is still evaluating whether to present other comprehensive income in a single continuous statement of comprehensive income or in two separate but consecutive statements.

In September 2011, the FASB issued ASU 2011-08, Testing Goodwill for Impairment, codified in ASC 350 "Intangibles – Goodwill and Other". The revised accounting standard update intends to simplify how an entity tests goodwill for impairment. The amendment will allow an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity no longer will be required to calculate the fair value of a reporting unit unless the entity determines, based on a qualitative assessment, that it is more likely than not that its fair value is less than its carrying amount. This accounting standard update will be effective for the Company beginning January 1, 2012. The Company does not expect the adoption of this new guidance to have a material impact on its financial statements.

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NOTE 3:- MARKETABLE SECURITIES

The following is a summary of held-to-maturity marketable securities:

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair market value
December 31, 2011:				
Maturing within one year:				
Corporate bonds	$ 1,644	$ 6	$ -	$ 1,650
	$ 1,644	$ 6	$ -	$ 1,650
December 31, 2010:				
Maturing within one year:				
U.S. Government agencies	$ 1,318	$ 4	$ -	$ 1,322
Corporate bonds	14,816	120	(1)	14,935
	16,134	124	(1)	16,257
Maturing over one year:				
Corporate bonds	2,564	18	-	2,582
	2,564	18	-	2,582
	$ 18,698	$ 142	$ (1)	$ 18,839

During 2011, a security with maturity date in 2012 and a callable feature was called by its issuer. This security was classified as held to maturity since at the acquisition there was no significant premium related to it, The net carrying amount of this security on the date of sale amounted to $ 808. The realized gain amounted to $ 1.

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NOTE 4:- OTHER ACCOUNTS RECEIVABLE AND PREPAID EXPENSES

	December 31, 2010	December 31, 2011
Government authorities	$ 3,648	$ 2,625
Deposits	717	672
Derivatives	2,700	102
Prepaid expenses	1,390	1,351
Advances to suppliers and others	2,352	2,908
	$ 10,807	$ 7,658

NOTE 5:- INVENTORIES

See also Note 2g.

	December 31, 2010	December 31, 2011
Raw materials and components	$ 12,746	$ 19,727
Work in progress	8,317	6,190
Finished products *)	35,015	10,298
	$ 56,078	$ 36,215

*) Includes inventory held by customers in the amount of $ 15,082 and $ 654 as of Decemeber 31, 2010 and 2011, respectively.

NOTE 6: - OTHER LOSS RELATED TO SHORT TERM INVESTMENT

On February 11, 2010, the Company and one of its customers (the "Customer") entered into a Note Purchase Agreement (the "Note Purchase Agreement"). Pursuant to the Note Purchase Agreement, the Company purchased from the Customer subordinated convertible promissory notes in the aggregate original principal amount of up to $ 7,000 (the "Notes") in 2010.

The outstanding principal balance of the Notes together with interest accrued and unpaid to date shall be due and payable at any time on or after such date that is the earliest of (a) August 11, 2011, (b) an Event of Default (as defined in the Notes), (c) at the Company's election, upon the consummation of an Acquisition Event or an Equity Financing (as defined in the Notes).

The Company's investment in the Note was reviewed for impairment whenever events or changes in circumstances indicated that the carrying amount of the investment may not be recoverable. The Company does not expect to collect, therefore following the Company's review for impairment of the Note, the Company recorded an impairment of the entire investment in the amount of $ 7,000 in the year ended December 31, 2010. The Company has not collected any portion of the Note in 2011.

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 7: - PROPERTY AND EQUIPMENT

	December 31,	
	2010	2011
Cost:		
Office furniture and equipment	$ 5,218	$ 4,869
Computers and electronic equipment	52,598	48,974
Motor vehicles	100	79
Leasehold improvements	4,574	3,729
	62,490	57,651
Accumulated depreciation:		
Office furniture and equipment	2,480	2,527
Computers and manufacturing equipment	42,497	42,672
Motor vehicles	20	24
Leasehold improvements	2,890	2,654
	47,887	47,877
Depreciated cost	$ 14,603	$ 9,774

Depreciation expenses for the years ended December 31, 2009, 2010 and 2011 amounted to $ 7,231, $ 6,662 and $ 5,433, respectively.

During 2011, the Company recorded disposals and sales of property and equipment in the amount of $ 9,500 and accumulated depreciation in the amount of $ 5,443, out of which the amount of $ 8,516 and related accumulated depreciation in the amount of $ 4,842 was associated with the Company's restructuring activities.

NOTE 8:- INTANGIBLE ASSETS, NET

	December 31,	
	2010	2011
Cost:		
Current technology	$ 17,871	$ 18,557
Customer relations	500	1,874
Backlog	-	1,578
	18,371	22,009
Accumulated amortization:		
Current technology	17,871	160
Customer relations	500	26
Backlog	-	1,578
	18,371	1,764
Amortized cost	$ -	$ 20,245

ALVARION LTD. AND ITS SUBSIDIARIES

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NOTE 8:- INTANGIBLE ASSETS, NET (Cont.)

Amortization expenses for the years ended December 31, 2009, 2010 and 2011 amounted $ 132, $ 130 (including an impairment of the remaining other intangible assets, in amount of $ 4) and $ 1,764, respectively. Intangibles and the related accumulated amortization of $18,371 at December 31, 2010 were written off in 2011.

See also Note 1b regarding Wavion acquisition

Estimated amortization expenses for the years ended:

Year ended December 31,		Amortization expenses
2012	$	2,235
2013		2,235
2014		2,235
2015		2,188
2016		1,671
Thereafter		9,681
	$	20,245

NOTE 9:- OTHER ACCOUNTS PAYABLE AND ACCRUED EXPENSES

	December 31,			
		2010		2011
Service providers, consultants and accrued expenses	$	9,768	$	11,139
Employees and payroll accruals		11,061		14,013
Advances from customers		4,519		2,246
Provision for agent commissions		3,777		2,695
Secured borrowings *)		1,770		987
Restructuring and other charges **)		1,855		4,477
Warranty provision		1,605		648
Royalties		1,214		2,355
Derivatives		174		2,690
Advances from grants		570		1,413
Earn out provision		-		2,718
Others		64		60
	$	36,377	$	45,441

*) See Note 2aa.
**) See also Note 2z .

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

NOTE 10:- LONG TERM LOAN

a. On June 21, 2011, the Company entered into a Loan & Security Agreement (the "Agreement"), with Silicon Valley Bank ("SVB"), whereby SVB provided a $ 30,000 credit line for the financing the acquisition of Wavion. The Company fully utilized the credit line on November 18, 2011.

As part of the transaction, the Company pledged all of its assets under a floating charge, and created a fixed charge on its Intellectual Property (“IP”) rights and receivables (. The Agreement with SVB contains various provisions related to compliance with financial covenants, restrictive covenants, including negative pledges, and other commitments , typically contained in facility agreements of this type. The credit line consist of Facility A ($25,000) and Facility B ($5,000).

Facility A will be repaid in thirty six (36) equal monthly installments starting March 1st, 2012. Interest rate applicable to Facility A is LIBOR for three months plus 4.75%, payable monthly starting December 1, 2011. Facility B will be repaid in one (1) installment after thirty six (36) months following first repayment of Facility A of the credit line. Interest rate applicable to Facility B is LIBOR for three months plus 4.50%, payable monthly starting December 1, 2011.

The Agreement was amended on January 31, 2012 with effective date as of December 31, 2011 to reflect certain changes to the Agreement (for example, changing the financial covenants). As of December 31, 2011, the Company was in full compliance with the covenants of the amended Agreement.

As of April 1, 2012 the Company was in breach of certain financial covenants set forth in the Long Term Loan but on April 25, 2012, it reached a general agreement with SVB for the grant of a temporary forbearance of the breached covenants and a modification of the terms of the Long Term Loan, which terms include (i) an increase of the interest rate applicable to Facility A and Facility B to LIBOR for three months plus 5.85% and (ii) the early repayment of $5,000 and $2,222 as of April 30, 2012 and July 1, 2012, respectively, of principal on the Long Term Loan.

b. As of December 31, 2011, the aggregate annual maturities according to the loan agreement are as follows:

Year ended December 31,		Repayment amount
2012 (current maturities)	$	12,813
2013		5,625
2014		5,625
2015		5,937
Total	$	30,000

c. In respect of the loan provided, the Company is required to meet certain financial covenants which includes non-gaap adjusted profit/loss, quick asset ratio and account receivable levels.

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

NOTE 11:- COMMITMENTS AND CONTINGENT LIABILITIES

a. Premises occupied by the Company are leased under various lease agreements. The lease agreements for these premises will expire in 2012-2015.

The Company has leased various motor vehicles and computers under operating lease agreements. These leases expire in fiscal year 2014.

Future minimum rental payments under such leases as of December 31, 2011 are as follows:

	Rental of premises	Lease of computers	Lease of motor vehicles
2012	$ 3,657	$ 143	$ 1,133
2013	1,463	43	638
2014	130	6	235
2015	28	-	-
	$ 5,278	$ 192	$ 2,006

Rental of premises expenses for the years ended December 31, 2009, 2010 and 2011, were $ 6,809, $ 6,442 and $ 5,363, respectively. Motor vehicle leasing expenses for the years ended December 31, 2009, 2010 and 2011, were $ 3,633, $ 2,961 and $ 1,896, respectively. Computer leasing expenses for the years ended December 31, 2009, 2010 and 2011, were $ 542, $ 497 and $ 226, respectively.

b. Litigation:

On November 21, 2001, a purported Class Action lawsuit ("the Action") was filed against interWAVE (a company merged into the Company in 2003), certain of its former officers and directors, and certain of the underwriters for interWAVE's initial public offering ("the IPO"). On April 19, 2002, the plaintiffs filed an amended complaint. The amended complaint alleged that the prospectus from interWAVE's IPO failed to disclose certain alleged improper actions by various underwriters for the offering, in violation of the Securities Act of 1933, as amended and the Securities Exchange Act of 1934, as amended ("the Exchange Act"). Similar complaints have been filed concerning more than 300 other IPOs; all of these cases have been coordinated as In re Initial Public Offering Securities Litigation, 21 MC 92. On October 8, 2002, the Court entered an Order of Dismissal as to all of the individual defendants in the IPO litigation, without prejudice. In 2007, a settlement that had been pending with the Court since 2004, was terminated by stipulation. After a ruling by the Second Circuit Court of Appeals in six "focus" cases in the coordinated proceedings (interWAVE is not one of the six test cases) made it unlikely that the settlement would receive final Court approval, plaintiffs filed amended master allegations and amended complaints in the six test cases. In 2008, the Court largely denied the defendants' motion to dismiss the amended complaints.

NOTE 11:- COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

This action has been resolved through a global settlement of the coordinated litigation. Under the settlement, the insurers pay the full amount of the settlement share allocated to the Company, and the Company bears no financial liability. InterWAVE, as well as the officer and director defendants who were previously dismissed from the Action pursuant to tolling agreements, receive complete dismissals from the case. On October 5, 2009, the Court entered an order granting final approval of the settlement. Although certain objectors filed appeals, by early 2012 all of those appeals had been withdrawn or dismissed and the settlement is now final.

c. Guarantees:

As of December 31, 2011, the Company:

Had outstanding bank guarantees in the total amount of approximately $ 4,647, in favor of customers, lessors and Government authorities.

d. Royalties:

The Company's research and development efforts have been partially financed through grants from the Office of the Chief Scientist ("OCS") of the Israeli Government. The Company entered an arrangement during 2003 with the OCS in Israel's Ministry of Industry and Trade where it participates in new OCS programs under which the Company is eligible to receive grants for research and development projects without any royalty repayment obligations, excluding OCS programs grants resulting from the acquisition of InnoWave, Clariton Networks and Wavion which were not included in this arrangement.

The Company did not receive grants-bearing royalties from the OCS during the years 2006 until 2011. Through the 2011 acquisition of Wavion (see Note 1b), the Company assumed Wavion's royalty bearing grant, and the royalties assumed has been recognized as a liability as part of the acquisition. In return for the OCS's participation for some of the grants applications (from InnoWave, Clariton Networks and Wavion), the Company is committed to pay royalties to the Israeli Government at the rate of 3.5% of sales of products in which the Israeli Government has participated in financing the research and development, up to the amounts granted. The grants received bear annual interest at LIBOR as of the date of approval. The grants are presented in the consolidated statements of operations as an offset to related research and development expenses.

Repayment of the grants is not required in the event that there are no sales of products developed within the framework of such funded programs. Royalties payable to the OCS are recorded as they become due and are classified as cost of sales. Royalty expenses relating to OCS grants included in cost of sales for the years ended December 31, 2009, 2010 and 2011, amounted to $ 159, $ 67 and $ 186, respectively. The maximum amount of the contingent liability related to royalty bearing grants payable to the Israeli Government was approximately $ 23,651 as of December 31, 2011.

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

NOTE 11:- COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

e. Liens:

Pursuant to its Loan and Security Agreement with SVB (see note 10), the Company pledged all of its assets under a floating charge and created a fixed charge on its IP rights and receivables.

NOTE 12:- SHAREHOLDERS' EQUITY

a. The Company's shares are listed for trading on the NASDAQ National Market and on the Tel-Aviv Stock Exchange.

b. Shareholders' rights:

The Ordinary shares confer upon the holders rights to receive notice to participate and vote in general meetings of the Company, to receive dividends, if and when declared and to receive, upon liquidation, a pro rata share of any remaining assets.

c. Share options:

The Company has six stock option plans under which 34,886,495 Ordinary shares were reserved for issuance.

In 2006, the Company adopted the 2006 shares options plan ("the 2006 Plan"). Under the 2006 Plan, the Company may grant restricted share units ("RSU"), restricted shares, options and other equity awards to employees, directors, consultants, advisers and service providers of the Company and its subsidiaries.

Pursuant to the 2006 Plan, 1,500,000 Ordinary shares were initially reserved for issuance upon the exercise of awards granted under the 2006 Plan. The number of Ordinary shares available for issuance under the 2006 Plan shall be reset annually on April 1 of each year to equal 4% of the total outstanding shares as of such reset date. The Company also grants its options under 2002 Plan. Options that are cancelled or forfeited become available for future grants. RSUs vest over a three year period of employment and may be subject to performance criteria. RSUs that are cancelled or forfeited become available for future grants.

During 2009, 2010 and 2011, the Company did not grant any performance based options. The Company did not record compensation expenses for 963,000 performance based options that were granted during 2008 since as of December 31, 2011, the Company did not reach the performance targets and the plan was canceled. During 2011, 174,000 performance based options were forfeited.

NOTE 12:- SHAREHOLDERS' EQUITY (Cont.)

Under the terms of the Company's plans, options generally vest ratably over a period of up to four years, commencing on the date of grant. The options expire no later than 6 years from the date of grant (under the old plans the options expired after 10 years), and are non-transferable, except under the laws of succession. Each option may be exercised to purchase one Ordinary share for an exercise price that is generally equal to the fair market value of the underlying share on the date of grant. Part of the options under the 2006 plan were granted at par value.

As of December 31, 2011, 9,212,839 Ordinary shares of the Company are still available for future grants under the various option plans.

A summary of option activity under the Company's stock option plans as of December 31, 2011 and changes during year than ended are as follows:

	Year ended December 31, 2011			
	Amount of options	Weighted average remaining contractual term (in years)	Weighted average exercise price	Aggregate intrinsic value
Options outstanding at beginning of year	11,178,511	3.68	$ 5.55	$ 4,938
Changes during the year:				
Granted	1,771,573		$ 1.49	
Exercised	(118,065)		$ 0.08	
Forfeited or cancelled	(3,518,691)		$ 5.60	
Options outstanding at end of year	9,313,328	2.95	$ 4.83	$ 1,447
Options vested or expected to vest	8,233,146	2.66	$ 5.26	$ 1,214
Options exercisable at end of year	6,164,768	2.00	$ 6.51	$ 459

The weighted-average grant-date fair value of options granted during the years ended December 31, 2009, 2010 and 2011 was $ 4.95, $ 2.44 and $ 0.92, respectively. The weighted-average fair value of the options vested during the year ended December 31, 2011 was $ 2.81. The total intrinsic value for the options exercised for the years ended December 31, 2009, 2010 and 2011 was, $ 436, $ 169 and $ 107, respectively.

As of December 31, 2011, there was approximately $ 4,003 of total unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the Company's stock option plans. That cost is expected to be recognized over the next 3 years.

NOTE 12:- SHAREHOLDERS' EQUITY (Cont.)

The options outstanding as of December 31, 2011, have been separated into ranges of exercise prices, as follows:

Exercise price (range)	Options outstanding as of December 31, 2011	Weighted average remaining contractual life (years)	Weighted average exercise price	Options exercisable as of December 31, 2011	Remaining contractual life (years for exercisable options)	Weighted average exercise price
$ 0-0.003	1,579,466	4.13	0.003	506,345	3.15	0.003
$ 0.84-1.17	320,500	6.27	0.94	-	-	-
$ 1.49-2.19	2,017,323	3.32	1.99	1,044,174	1.42	2.04
$ 2.57-3.74	1,332,018	2.67	3.13	855,060	2.18	3.16
$ 3.88-5.80	939,900	3.66	4.53	655,900	3.38	4.80
$ 6.39-9.58	1,407,781	1.58	8.02	1,386,949	1.56	8.03
$ 10.24-15.404	1,716,340	1.75	12.22	1,716,340	1.75	12.22
	9,313,328			6,164,768		

A summary of the status of the Company's restricted shares units and options granted at par-value as of December 31, 2011, and changes during the year ended December 31, 2011, are presented below:

Unvested restricted share units and options at par value	Number of restricted share units and options at par value	Weighted average grant date fair value
Non vested at January 1, 2011	1,667,470	$ 4.01
Granted	250,000	$ 0.99
Vested	(607,231)	$ 4.28
Forfeited	(237,118)	$ 5.40
Non vested at December 31, 2011	1,073,121	$ 2.81

The total fair value of shares vested during the years ended December 31, 2009, 2010 and 2011 was $257, $358 and $932 respectively.

d. Dividends:

In the event that cash dividends are declared in the future, such dividends will be paid in NIS. The Company's Board of Directors has determined that tax exempt income if any, will not be distributed as dividends.

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 13:- TAXES ON INCOME

a. Commencing taxable year 2003, the Company has elected to measure its taxable income and file its tax return under the Israeli Income Tax Regulations (Principles Regarding the Management of Books of Account of Foreign Invested Companies and Certain Partnerships and the Determination of Their Taxable Income), 1986. Accordingly, results for tax purposes are measured in terms of earnings in U.S. dollars.

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

Alvarion Ltd. has been granted status as an "Approved Enterprise" under the Law for the Encouragement of Capital Investments, 1959 ("the Investment Law").

According to the provision of the Investment Law, Alvarion Ltd. has elected the "alternative benefits" track provisions of the Investment Law, pursuant to which Alvarion Ltd. has waived its right to grants and instead receives a tax benefit on undistributed income derived from the "Approved Enterprise" program. The entitlement to tax benefits depends upon compliance with the Investment Law regulations.

In 1997, Alvarion Ltd.'s production facility in Nazareth was granted a status of "Approved Enterprise". During 2000, Alvarion Ltd.'s expansion request for its second "Approved Enterprise" regarding its production facilities in Migdal Haemek was approved. In connection with its merger with Floware Ltd. ("Floware") in 2001, Floware Ltd. was granted "Approved Enterprise" status for its 1997 plan regarding the production facility in Or-Yehuda.

The period of benefits for all plans will commence with the first year in which the Company earns taxable income after the commencement year. The duration of tax benefits is subject to limits of the earlier of 12 years from the commencement of production, or 14 years from receiving the approval. The period of benefits for all plans has not yet commenced. The limitation mentioned does not apply to the exemption periods and plans.

Alvarion Ltd.'s entitlement to the above benefits is conditional upon its fulfilling the conditions stipulated by the Investment Law, regulations published thereunder and the letters of approval for the specific investments in "Approved Enterprises". In the event of failure to comply with these conditions, any benefits which were previously granted may be canceled and the Company may be required to refund the amount of the benefits, in whole or in part, including interest and CPI adjustments.

If these retained tax-exempt profits are distributed they would be taxed at the corporate tax rate applicable to such profits as if the Company had not elected the alternative benefit track. As of December 31, 2011, the accumulated deficit of the Company does not include tax-exempt profits earned by the Company's "Approved Enterprise".

NOTE 13:- TAXES ON INCOME (Cont.)

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

On April 1, 2005, an amendment to the Investment Law came into effect (the "Amendment") and significantly changed the provisions of the Investment Law. Generally, the Company's investment programs that obtained approval for Approved Enterprise status prior to enactment of the Amendment will continue to be subject to the old provisions of the Investment Law.

The Amendment enacted major changes in the manner in which tax benefits are awarded under the Investment Law so that companies are no longer required to get the Investment Center's prior approval to qualify for tax benefits. Such an enterprise is a "Privileged Enterprise", rather than the previous terminology of Approved Enterprise. The period of tax benefits for a new Privileged Enterprise commences in the "Year of Commencement", which is the later of: (1) the year of election, or (2) the year in which taxable income is first generated by the company after the election year.

The Amendment limits the scope of enterprises which may be approved by the Investment Center by setting criteria for the approval of a facility as a Privileged Enterprise, such as the provision generally requiring that at least 25% of the Privileged Enterprise's income will be derived from export.

Under the Amendment, in 2005 and 2007, the Company announced 2004 and 2006 (respectively) as the "Election Year" and submitted an expansion request for additional "Privileged Enterprise" status regarding its production facilities. A portion of the taxable income derived from this "Privileged Enterprise" will be tax-exempt for a period of 10 years. The 10 years period of benefits will commence with the first year in which the Company earns taxable income after the election year.

The Company has no taxable income since inception and does not have any profits under the Approved/Privileged Enterprise.

In December 2010, the "Knesset" (Israeli Parliament) passed the Law for Economic Policy for 2011 and 2012 (Amended Legislation), 2011, which prescribes, among others, amendments in the Law for the Encouragement of Capital Investments, 1959 ("the Law"). The amendment was enacted in 2011 and became effective as of January 1, 2011. According to the amendment, the benefit tracks in the Law were modified and a flat tax rate applies to the Company's entire preferred income. The Company will be able to elect to apply (the waiver is irrevocable) the amendment and from then on it will be subject to the amended tax rates that are: 2011 and 2012 - 15% (in development area A - 10%), 2013 and 2014 - 12.5% (in development area A - 7%) and in 2015 and thereafter - 12% (in development area A - 6%).

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 13:- TAXES ON INCOME (Cont.)

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

The Company is an "industrial company" under the above law and, as such, is entitled to certain tax benefits, mainly accelerated depreciation of machinery and equipment. For tax purposes only, the Company may also be entitled to deduct over a three-year period expenses incurred in connection with a public share offering and to amortize know-how over an eight-year period.

d. Loss before income tax expense:

	Year ended December 31,		
	2009	2010	2011
Domestic	$ (11,557)	$ (65,207)	$ (21,464)
Foreign	4,369	(32,378)	(12,358)
	$ (7,188)	$ (97,585)	$ (33,822)

e. Taxes on income are comprised of the following:

	Year ended December 31,	
	2010	2011
Current	$ 894	$ -
Deferred	-	-
	$ 894	$ -
Domestic	$ 125	$ 144
Foreign	769	(144)
	$ 894	$ -

Income tax expenses for 2009 are not presented due to immateriality.

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NOTE 13:- TAXES ON INCOME (Cont.)

f. Reconciliation of the theoretical tax expenses:

Reconciliation between the theoretical tax expenses, assuming all income is taxed at the statutory rate applicable and the actual income tax as reported in the statements of income, is as follows:

	Year ended December 31, 2010			Year ended December 31, 2011	
Loss before taxes	$	97,585		$	33,822	
Statutory tax rate in Israel		25 %			24 %
Tax benefit		(24,396)			(8,117)
Permanent differences		17,921			801
Loss for which a valuation allowance was provided		6,794			7,734
Tax expenses adjustment due to past years		45			124
Withholdings and other taxes		125			193
Differences in tax rate		404			163
Uncertain tax position and other differences		-			(898)
Tax expense	$	894		$	-

Income tax expenses for 2009 are not presented due to immateriality.

The main reconciling items between the statutory tax rate of the Company and the effective tax rate are the permanent differences and the non-recognition of tax benefits resulting from the Company's accumulated net operating losses carryforward due to the uncertainty of the realization of such tax benefits.

g. Carryforward losses:

As of December 31, 2011, Alvarion Ltd. and Wavion Ltd. had an available tax loss carry forward amounting to approximately $ 205,900 and $38,500, respectively, which may be carried forward, in order to offset taxable income in the future, for an indefinite period.

As of December 31, 2011, the U.S. subsidiaries had approximately $ 42,330 in federal net operating loss carryforward for income tax purposes, which can be carried forward and offset against taxable income for 20 years and will expire between 2012 and 2031. The state tax losses carryforwards of the U.S. subsidiaries are approximately $14,370 and this balance will expire between 2012 through 2021.

The state and U.S. federal loss carry forwards per the income tax returns filed included uncertain tax positions taken in prior years. Due to application of uncertain tax positions, they are larger than the net operating loss deferred tax asset recognized for financial statement purposes.

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 13:- TAXES ON INCOME (Cont.)

Utilization of U.S. net operating losses may be subject to substantial annual limitations due to the "change in ownership" provisions ("annual limitations") of the Internal Revenue Code of 1986 and similar state provisions. The annual limitation may result in the expiration of net operating losses before utilization.

h. Tax rates applicable to the income of the Company:

Taxable income of Israeli company is subject to tax at the rate of 26% in 2009, 25% in 2010 and 24% in 2011. In December 5, 2011, the Knesset (Israel's Parliament) passed a law for changing the tax burden (the Law), which cancels, among others, the gradual reduction in the corporate tax rates in Israel. In addition, the corporate tax in Israel will be increased to 25% starting in 2012. Accordingly, the real capital gains tax rate will increase to 25%. There was no effect on the Company as a result of the above mentioned changes.

i. Deferred taxes:

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

	December 31, 2010	December 31, 2011
Tax assets in respect of:		
Allowance for doubtful accounts	$ 1,319	$ 1,604
Accrued severance pay and accrued vacation pay	1,053	862
Reaserch and development expenses	4,457	4,270
Other deductions for tax purposes	2,452	1,712
Net loss carry forward	43,119	76,181
Total deferred tax assets	52,400	84,629
Deferred tax liabilities:		
Acquired intangibles	-	(7,743)
Deferred tax assets, net before valuation allowance	52,400	76,886
Valuation allowance	(52,400)	(76,886)
Deferred tax assets	$ -	$ -

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 13:- TAXES ON INCOME (Cont.)

j. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	December 31,	
	2010	2011
Opening balance	$ 3,223	$ 3,363
Additions for (settlement of) prior year tax positions	92	(878)
Additions for current year tax position	48	52
Closing balance	$ 3,363	$ 2,537

During the years ended December 31, 2009, 2010 and 2011, the Company recorded $ 26, $ 92 and $ 100, respectively for interest and penalties expenses related to uncertain tax positions. The liability for unrecognized tax benefits included accrued interest and penalties of $ 810 and $ 910 at December 31, 2010 and 2011, respectively.

As of December 31, 2011, the entire amount of unrecognized tax benefit could affect the Company's income tax provision and the effective tax rate.

k. The Company and its subsidiaries file income tax returns in Israel, USA and other foreign jurisdictions. With respect to Alvarion Ltd., the Israeli Tax Authorities had never examined the Company's tax returns, nevertheless the tax returns until 2006 tax year (including 2006 tax returns) are deemed to be approved. With respect to the Israeli subsidiary the tax returns until 2005 (including 2005 tax returns) are deemed to be approved. The statute of limitations relating to the U.S. Federal income tax return is closed for all tax years up to and including 2007.

NOTE 14:- INFORMATION ABOUT GEOGRAPHIC AREAS AND MAJOR CUSTOMERS

a. The Company operates in one reportable segment (see Note 1 for a brief description of the Company's business) and follows the requirements of ASC 280 "Segment Reporting".

b. Information on sales by geographic distribution:

The total revenues are attributed to geographic areas based on the location of the Company's end customers.

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 14:- INFORMATION ABOUT GEOGRAPHIC AREAS AND MAJOR CUSTOMERS (Cont.)

The following table presents total revenues for the years ended December 31, 2009, 2010 and 2011:

	Total revenues Year ended December 31,		
	2009	2010	2011
Israel	$ 697	$ 718	$ 736
United States	22,478	45,638	34,426
Canada	764	1,879	12,514
Europe (without, Italy, France, Spain and Denmark)	24,398	20,415	18,963
France	17,252	11,049	5,503
Italy	19,281	17,333	14,791
Spain	9,734	14,186	6,605
Denmark	35,483	7,115	5,608
Latin America (without Argentina)	29,313	21,980	26,388
Argentina	16,056	4,895	2,008
Africa (without Nigeria)	41,726	26,191	23,046
Nigeria	167	12,902	5,449
Asia (without India)	25,288	19,528	19,449
India	2,602	1,986	14,551
	$ 245,239	$ 205,815	$ 190,037

The following table presents total long-lived assets as of December 31, 2010 and 2011:

	Total long-lived assets December 31,	
	2010	2011
Israel	$ 10,185	$ 6,536
Romania	3,058	2,545
Other	1,360	693
	$ 14,603	$ 9,774

The total long-lived assets are attributed to geographic areas based on the location of the assets.

c. The following is a summary of the percentages of net sales from major customers:

	% of consolidated revenue Year ended December 31,		
	2009	2010	2011
Customer A	15 %	*) -	*) -

*) Less than 10% of the Company's consolidated revenues

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 15:- SELECTED STATEMENTS OF OPERATIONS DATA

a. One of the Company's customers ("ORC") has declared bankruptcy in 2011. As part of the bankruptcy, the Company recorded charges in the form of an inventory write-off which represents approximately $3,900 of Alvarion equipment which had been shipped to ORC but the related revenues had not been recognized, and this inventory can not be retrieved by the Company. In addition an approximate $3,300 of third-party equipment ordered by ORC, which had yet to be delivered by the Company to ORC as of the time of the bankruptcy filing, and equipment used for ORC by the Company, and the Company has no other line of business to sell or use the equipment in.

b. Research and development, net:

	Year ended December 31,		
	2009	2010	2011
Research and development costs	$ 54,674	$ 41,744	$ 32,404
Less - grants and participation	3,884	3,027	4,440
	$ 50,790	$ 38,717	$ 27,964

c. Financial income, net:

	Year ended December 31,		
	2009	2010	2011
Financial income:			
Interest on held-to-maturity marketable securities, amortization of premium and accretion of discounts on held-to-maturity marketable securities, interest on bank deposits and other interest	$ 2,583	$ 1,311	$ 778
Income related to ineffective derivative and derivative not designated as effective hedge	-	1,221	709
Foreign currency transaction differences, net	355	-	-
	2,938	2,532	1,487
Financial expenses:			
Interest and bank expenses including expense related to sale of trade receivables	(1,142)	(1,087)	(1,209)
Expenses related to ineffective derivative and derivative not designated as effective hedge	(128)	(597)	(1,016)
Foreign currency transaction differences, net	-	(947)	(277)
	(1,270)	(2,631)	(2,502)
	$ 1,668	$ (99)	$ (1,015)

ALVARION LTD. AND ITS SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

NOTE 15:- SELECTED STATEMENTS OF OPERATIONS DATA (Cont.)

d. Net loss per share:

The following table sets forth the computation of basic and diluted net loss per share:

	Year ended December 31, 2009	2010	2011
Numerator:			
Numerator for basic and diluted net loss per share	(7,188)	(98,479)	(33.822)
Denominator:			
Denominator for basic net loss per share - weighted average number of Ordinary shares	62,023,075	62,198,615	62,301,866
Effect of dilutive securities:			
Employee stock options	*) -	*) -	*) -
Denominator for diluted net loss per share - adjusted weighted average number of shares	62,023,075	62,198,615	62,301,866
Net loss per share Basic and Diluted	$ (0.12)	$ (1.58)	$ (0.54)

*) Antidilutive.

NOTE 16:- SUBSEQUENT EVENT

On April 5, 2012, the Company issued lower first quarter 2012 projected results, and as a result, indicated that it is in default on a financial covenant under its loan, however, on April 25, 2012, the Company reached an agreement with SVB, amending the loan agreement, following which the Company now complies with the amended loan covenants.