

ELECTRONICS LINE 3000 LTD.

INTERIM CONSOLIDATED FINANCIAL STATEMENTS

AS OF SEPTEMBER 30, 2005

U. S. DOLLARS IN THOUSANDS

UNAUDITED

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CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands

	September 30,		December 31,
	2005	2004	2004
	Unaudited		Audited
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	6,443	5,429	6,658
Trade receivables	10,646	8,333	6,668
Income tax receivable	434	1,440	1,565
Prepaid expenses and other receivables	776	890	861
Inventories	7,542	6,343	6,789
<u>Total</u> current assets	25,841	22,435	22,541
NONCURRENT ASSETS:			
Property, plant and equipment:			
Cost	14,583	13,113	14,594
Less - accumulated depreciation	8,332	6,574	7,663
	6,251	6,539	6,931
Intangible assets, net	5,382	4,731	5,432
Deferred taxes	1,106	1,694	1,683
Security deposits	107	81	106
<u>Total</u> noncurrent assets	12,846	13,045	14,152
<u>Total</u> assets	38,687	35,480	36,693

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

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands

	<u>September 30,</u>		<u>December 31,</u>
	<u>2005</u>	<u>2004</u>	<u>2004</u>
	<u>Unaudited</u>		<u>Audited</u>
LIABILITIES AND EQUITY			
CURRENT LIABILITIES:			
Short-term credit from banks	18,008	20,829	21,236
Loan from shareholders	509	-	502
Trade payables	6,857	3,852	4,859
Accrued expenses	662	316	589
Income tax payable	40	170	79
Other current liabilities	2,783	1,514	1,953
<u>Total current liabilities</u>	<u>28,859</u>	<u>26,681</u>	<u>29,218</u>
LONG-TERM LIABILITIES:			
Accrued severance pay, net	472	449	446
Loan from shareholders	509	-	502
<u>Total long-term liabilities</u>	<u>981</u>	<u>449</u>	<u>948</u>
EQUITY:			
Share capital	9,901	9,359	9,359
Additional paid-in capital	1,937	1,317	1,317
Foreign currency translation reserve	1,871	1,197	1,871
Accumulated deficit	(4,862)	(3,523)	(6,020)
<u>Total equity</u>	<u>8,847</u>	<u>8,350</u>	<u>6,527</u>
<u>Total liabilities and equity</u>	<u>38,687</u>	<u>35,480</u>	<u>36,693</u>

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

November 17, 2005

Date of approval of the
financial statements

Bob Marbut
Chairman of the
Board of Directors

Amir Hayek
President and CEO

Amir Blumenfeld
CFO

CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Nine months ended September 30,		Three months ended September 30,		Year ended December 31,
	2005	2004	2005	2004	2004
	Unaudited				Audited
Revenues	32,899	27,023	12,072	9,356	34,760
Cost of revenues	20,333	17,487	7,190	6,599	23,431
Gross profit	12,566	9,536	4,882	2,757	11,329
Operating costs and expenses:					
Research and development	1,076	1,111	360	380	1,559
Selling and marketing	6,552	6,373	2,175	2,154	8,868
General and administrative	3,408	3,237	1,028	883	4,677
Total operating costs and expenses	11,036	10,721	3,563	3,417	15,104
Operating profit (loss)	1,530	(1,185)	1,319	(660)	(3,775)
Financial income (expenses), net	218	(1,055)	(364)	(254)	(795)
Other expenses, net	4	91	1	20	92
Profit (loss) before taxes on income	1,744	(2,331)	954	(934)	(4,662)
Taxes on income (income tax benefit)	586	(587)	351	(258)	(421)
Net profit (loss)	1,158	(1,744)	603	(676)	(4,241)
Net earnings (loss) per share (basic and diluted)	0.13	(0.25)	0.07	(0.08)	(0.58)

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

STATEMENTS OF CHANGES IN EQUITY

U.S. dollars in thousands

	Nine months ended September 30, 2005 (unaudited)					Total recognized income (expense)
	Share capital	Additional paid-in capital	Foreign currency translation reserve	Accumulated deficit	Total equity	
Balance at the beginning of the period (audited)	9,359	1,317	1,871	(6,020)	6,527	-
Issuance of shares, net of issuance costs	542	521	-	-	1,063	-
Cost of share-based payments	-	99	-	-	99	-
Net profit	-	-	-	1,158	1,158	1,158
Balance at the end of the period	<u>9,901</u>	<u>1,937</u>	<u>1,871</u>	<u>(4,862)</u>	<u>8,847</u>	<u>1,158</u>

	Nine months ended September 30, 2004 (unaudited)					Total recognized income (expense)
	Share capital	Additional paid-in capital	Foreign currency translation reserve	Accumulated deficit	Total equity	
Balance at the beginning of the period (audited)	6,172	1,317	1,319	(1,779)	7,029	-
Issuance of share capital against conversion of shareholders' loan	3,187	-	-	-	3,187	-
Loss	-	-	-	(1,744)	(1,744)	(1,744)
Currency translation differences	-	-	(122)	-	(122)	(122)
Balance at the end of the period	<u>9,359</u>	<u>1,317</u>	<u>1,197</u>	<u>(3,523)</u>	<u>8,350</u>	<u>(1,866)</u>

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

STATEMENTS OF CHANGES IN EQUITY

U.S. dollars in thousands

	Three months ended September 30, 2005 (unaudited)					
	Share capital	Additional paid-in capital	Foreign currency translation reserve	Accumulated deficit	Total equity	Total recognized income (expense)
Balance at the beginning of the period	9,359	1,317	1,871	(5,465)	7,082	-
Issuance of shares, net of issuance costs	542	521	-	-	1,063	-
Costs of share - based payments	-	99	-	-	99	-
Net profit	-	-	-	603	603	603
Balance at the end of the period	<u>9,901</u>	<u>1,937</u>	<u>1,871</u>	<u>(4,862)</u>	<u>8,847</u>	<u>603</u>
	Three months ended September 30, 2004 (unaudited)					
	Share capital	Additional paid-in capital	Foreign currency translation reserve	Accumulated deficit	Total equity	Total recognized income (expense)
Balance at the beginning of the period	9,359	1,317	1,076	(2,847)	8,905	-
Loss	-	-	-	(676)	(676)	(676)
Currency translation differences	-	-	121	-	121	121
Balance at the end of the period	<u>9,359</u>	<u>1,317</u>	<u>1,197</u>	<u>(3,523)</u>	<u>8,350</u>	<u>(555)</u>
	Year ended December 31, 2004 (audited)					
	Share capital	Additional paid-in capital	Foreign currency translation reserve	Accumulated deficit	Total equity	Total recognized income (expense)
Balance at the beginning of the year	6,172	1,317	1,319	(1,779)	7,029	-
Issuance of share capital against conversion of shareholders' loan	3,187	-	-	-	3,187	-
Loss	-	-	-	(4,241)	(4,241)	(4,241)
Currency translation differences	-	-	552	-	552	552
Balance at the end of the year	<u>9,359</u>	<u>1,317</u>	<u>1,871</u>	<u>(6,020)</u>	<u>6,527</u>	<u>(3,689)</u>

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Nine months ended September 30,		Three months ended September 30,		Year ended December 31,
	2005	2004	2005	2004	2004
	Unaudited				Audited
<u>Cash flows from operating activities:</u>					
Net profit (loss) before taxes on income	1,744	(2,331)	954	(934)	(4,662)
Adjustments for:					
Depreciation and amortization	1,490	1,302	478	426	1,763
Loss on sale of property, plant and equipment	34	1	-	-	-
Increase (decrease) in accrued severance pay	26	29	31	(14)	(16)
Cost of share-based payments	99	-	99	-	-
Financial expenses (income), net	(218)	1,055	364	254	795
Operating cash flows before working capital changes	3,175	56	1,926	(268)	(2,120)
Decrease (increase) in trade receivables	(3,978)	239	(1,684)	410	2,568
Decrease in prepaid expenses and other receivables	85	18	81	43	130
Decrease (increase) in inventories	(753)	224	(873)	1,118	437
Decrease (increase) in long-term receivables	(1)	24	(1)	1	10
Increase (decrease) in trade payables	1,998	(504)	659	(1,016)	32
Increase (decrease) in accrued expenses	73	(164)	(10)	(15)	52
Increase in other current liabilities	830	123	837	584	377
	(1,746)	(40)	(991)	1,125	3,606
Cash provided by operations	1,429	16	935	857	1,486
Interest received	53	42	21	16	43
Interest paid	(850)	(556)	(296)	(317)	(714)
Income taxes received	1,198	3	-	3	-
Income taxes paid	(115)	(421)	(67)	-	(498)
Net cash provided by (used in) operating activities	1,715	(916)	593	559	317
<u>Cash flows from investing activities:</u>					
Acquisition of intangible assets	(656)	(740)	(237)	(254)	(1,009)
Acquisition of property, plant and equipment	(229)	(458)	(80)	(80)	(559)
Proceeds from sale of equipment	91	32	-	-	43
Net cash used in investing activities	(794)	(1,166)	(317)	(334)	(1,525)
<u>Cash flows from financing activities:</u>					
Proceeds from issuance of shares net of issuance costs	1,063	-	1,063	-	-
Receipt of loans from shareholders	-	-	-	-	954
Increase (decrease) in short-term bank credit, net	(2,199)	2,940	(623)	753	1,715
Net cash provided by (used in) financing activities	(1,136)	2,940	440	753	2,669
<u>Effect of exchange rate changes on cash and cash equivalents</u>					
	-	(109)	-	68	517
Increase (decrease) in cash and cash equivalents	(215)	749	716	1,046	1,978
Cash and cash equivalents at beginning of period	6,658	4,680	5,727	4,383	4,680
Cash and cash equivalents at end of period	6,443	5,429	6,443	5,429	6,658
<u>Significant non-cash transactions:</u>					
Issuance of shares in consideration for loan from shareholders	-	3,187	-	-	3,187

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

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1:- GENERAL

- a. These financial statements have been prepared in a condensed format as of September 30, 2005 and for the nine and three months then ended. These financial statements should be read in conjunction with the Company's audited annual consolidated financial statements and accompanying notes as of December 31, 2004 ("the annual financial statements").
- b. Due to losses the Company incurred in 2003 and 2004, the management of the Company has implemented several cost saving measures that include a reduction in the number of employees (approximately 25). In light of the steps that were taken, the additional equity financing from the private placement in July 2005 (see Note 8a) and the generation of net profit of \$ 1,158 thousand for the nine months ended September 30, 2005, the management of the Company believes that it will have sufficient financing in the future to fund its operations and meet its obligations.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

- a. The interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) in the context of interim financial reporting standards. The significant accounting policies and methods of computations applied in the preparation of the interim financial statements are the same as those applied in the annual financial statements.
- b. Functional and presentation currency:

Until December 31, 2004, the functional currency of the Company and of its subsidiaries ("the Group") was the Euro. In the beginning of 2005, the Group reevaluated the factors used in determining its functional currency, including the currency in which the Group's sales and its costs are denominated and settled. Based on this reevaluation, the Group concluded that the U.S. dollar presently reflects the primary economic environment in which the Group operates, and therefore, the U.S. dollar is the Group's functional currency. In accordance with IAS 21, "The Effects of Change in Foreign Exchange Rates", the change in functional currency from the Euro to the U.S. dollar is accounted for prospectively. Accordingly, assets and liabilities in the balance sheet at December 31, 2004, were translated from the Euro to U.S. dollar at the exchange rate in effect as of December 31, 2004.

Due to the change in the functional currency, the Group has selected the US dollar as the presentation currency for all reported periods. Accordingly, the financial statements of the Group for comparative periods in which the functional currency was the Euro have been translated from the Euro to the presentation currency in accordance with the principles set forth in IAS 21, as follows:

Assets and liabilities are translated into U.S. dollars at the closing rate at the date of each balance sheet. Issued capital, additional paid-in capital and other reserves are translated into U.S. dollars using the exchange rate on the date of the transaction. Income and expenses are translated at average monthly exchange rates. Translation differences resulting from the translation are recognized as a separate component of equity ("foreign currency translation reserve").

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS**NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)**

- c. Following are data regarding the Israeli CPI and the exchange rate of the U.S. dollar and the Euro:

<u>As of</u>	<u>Israeli CPI</u> <u>Points *)</u>	<u>Exchange rate</u> <u>of U.S. \$ 1</u> <u>NIS</u>	<u>Exchange rate</u> <u>of € 1</u> <u>NIS</u>
September 30, 2005	184.2	4.598	5.528
September 30, 2004	180.7	4.482	5.525
December 31, 2004	180.7	4.308	5.877
<u>Change during the period</u>	<u>%</u>	<u>%</u>	<u>%</u>
September 2005 (nine months)	1.9	6.7	(5.9)
September 2005 (three months)	1.4	0.5	0.0
September 2004 (nine months)	1.2	2.4	(0.2)
September 2004 (three months)	(0.2)	(0.3)	1.1
December 2004 (12 months)	1.2	(1.6)	6.2

*) The index on an average basis of 1993 = 100.

NOTE 3:- FINANCIAL COVENANTS

- a. On September 27, 2005, the Company recorded a floating charge (a non-specific lien on all assets of the Company on which there is no previous specific lien) on the Company's assets in favor of three of the Group's banks. Due to the recording of the floating charge, one of the Group's banks (Bank A) canceled its request for compliance with any financial covenants. As of September 30, 2005, the Company's balance of short-term credit from Bank A is \$ 6,663 thousand.
- b. On September 29, 2005, the Company approved new financial covenants in respect of credit from Bank B. As of September 30, 2005, the Company's balance of short-term credit from Bank B is \$ 4,630 thousand. The Company and Bank B reached an understanding as to certain customary financial covenants that the Company will have to fulfill, including the ratio of shareholders' equity to total assets, certain profitability level, cash balances and other balance sheet ratios. As of September 30, 2005, the Company is meeting the covenants that it is obligated to fulfill according to the new financial covenants agreed to on September 29, 2005.

NOTE 4:- TRANSACTIONS WITH A CONTROLLING SHAREHOLDER

Since March 1, 2003, Mr. Bob Marbut, who is the Chairman of the Board of Directors and an indirect controlling shareholder of the Company, has been acting as CEO and president of a subsidiary in the United States ("STG"). The employment contract was for a period of one year, but is automatically renewable for additional one year periods, unless one of the parties makes prior notice of cancellation. In consideration for his services, Mr. Marbut is entitled to an annual salary of \$ 350 thousand.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4:- TRANSACTIONS WITH A CONTROLLING SHAREHOLDER (Cont.)

Mr. Marbut has decided to waive his salary for 2005, and, accordingly, no salary expense for Mr. Marbut is included in the financial statements for the nine months ended September 30, 2005.

NOTE 5:- STOCK OPTION PLAN

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

On August 8, 2005, the Company's Board of Directors granted 102,500 options (including 15,000 options to the former Managing Director). The options granted expire 10 years after the date of grant and vest over a period ending in December 2008. The exercise price of the options granted is € 2.297 (\$ 2.844 on date of grant). The exercise price of the options was based on the average market price of the Company's shares for a period of 30 days prior to the grant. The options were granted under section 102 of the Israeli Income Tax Ordinance.

The weighted average fair value of options granted by the Company in August 2005 is € 1.64 (\$ 2), which was estimated using the Black-Scholes option pricing model, based on the following data and assumptions:

Share price - € 2.77 (\$ 3.43); exercise price - € 2.297 (\$ 2.84); expected volatility - 94%; risk-free interest rate - 2%; expected dividends - 0% and expected average life of options - 2.5 years.

Compensation costs in respect of these options, in accordance with IFRS 2, "Share-Based Payment", were recorded commencing in the third quarter of 2005.

On November 10, 2005, the Company's Board of Directors resolved to grant 22,500 options to the new President and CEO (who was appointed on November 1, 2005). The options granted expire 10 years after the date of grant and vest over a period ending in November 2009. The exercise price of the options granted is € 4.043 (\$ 4.757 on date of grant).

The weighted average fair value of options granted by the Company in November 2005 is € 1.48 (\$ 1.74), which was estimated using the Black-Scholes option pricing model. Compensation costs in respect of these options, in accordance with IFRS 2, "Share-Based Payment", are to be recorded commencing in the fourth quarter of 2005.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6:- CONTINGENT LIABILITIES

- a. Potential claim against EL-USA

On September 21, 2005, the wholly-owned US subsidiary ("EL-USA") received a letter from the attorneys of Kodicom Australia PTY. Limited ("Kodicom"), regarding a contract dispute and alleged breach of a certain Distribution Agreement entered into between Kodicom and EL-USA on April 11, 2002 (the "Agreement"). EL-USA's counsel has already responded to Kodicom's letter stating that EL-USA did not breach the Agreement and in fact, has several counter-claims against Kodicom concerning its performance pursuant to the Agreement. EL-USA's legal counsel has assessed that it is unlikely that Kodicom will actually file a lawsuit in connection with this claim.

- b. Claims related to Metis:

As described in Note 25c to the consolidated financial statements as of December 31, 2004, on May 2, 2004 the Company entered into a Consultation Agreement with the former parent company ("Metis"- formerly "E.L."). In a letter to the Company dated March 6, 2005, Metis demanded that the Company pay the Consulting Fees pursuant to the terms of the Consulting Agreement.

In a response letter dated March 13, 2005, the Company rejected Metis' monetary demands and has not paid any Consulting Fees since July 1, 2004 to Metis. The Company has made a provision in its financial statements of \$ 1,125 thousand, which represents the entire unpaid amount.

The Company has serious concerns as to the validity and thus, the enforceability of the Consulting Agreement. At the Company's demand, the dispute was referred to arbitration on September 21, 2005, and an arbitrator has already been appointed by mutual agreement of the parties. Metis served the Company with its statement of claim on October 19, 2005. The Company is in the process of preparing its statement of defense and intends to vigorously defend its position.

NOTE 7:- GEOGRAPHICAL SEGMENTS

- a. General information:

The Company and the Group companies operate in two major geographical segments: the U.S. and Europe.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 7:- GEOGRAPHICAL SEGMENTS (Cont.)

b. Information about geographical segments:

	<u>U.S.</u>	<u>Europe</u>	<u>Other countries</u>	<u>Adjustments</u>	<u>Total - consolidated</u>
	<u>U.S. dollars in thousands</u>				
Nine months ended September 30, 2005 (unaudited)					
Segment revenues	8,466	24,042	3,340	(2,949)	32,899
Segment results	239	4,900	489	*) (4,098)	1,530
Nine months ended September 30, 2004 (unaudited)					
Segment revenues	8,120	19,007	3,229	(3,333)	27,023
Segment results	1,043	2,317	(42)	*) (4,503)	(1,185)
Three months ended September 30, 2005 (unaudited)					
Segment revenues	3,114	8,990	1,143	(1,175)	12,072
Segment results	187	2,033	239	*) (1,140)	1,319
Three months ended September 30, 2004 (unaudited)					
Segment revenues	3,309	6,133	1,265	(1,351)	9,356
Segment results	592	289	(122)	*) (1,419)	(660)
Year ended December 31, 2004 (audited)					
Segment revenues	10,900	24,178	4,363	(4,681)	34,760
Segment results	(391)	1,518	(367)	*) (4,535)	(3,775)

*) Including expenses not allocated to segments.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8:- OTHER INFORMATION

- a. On July 10, 2005, the Company's Board of Directors resolved to approve a private placement of 500,000 Ordinary shares to a third party intermediary in consideration of € 2 per share. The intermediary is to transfer the shares shortly after the issuance to several buyers, who subsequent to the transfer will each hold less than 5% of the Company's outstanding share capital.

On July 11, 2005, the 500,000 shares were issued to the intermediary.

- b. On September 5, 2005, the wholly-owned France subsidiary ("Sectec") signed an agreement, effective October 1, 2005, with a French company providing for the transfer of its business activities and operations (distribution of electronic security products), including certain assets for the consideration of € 200 thousand (\$ 250 thousand).

Within the framework of this agreement, the purchaser takes upon itself all of the liabilities and the commitments of Sectec.

The Company expects to record a gain of approximately € 150 thousand (\$ 188 thousand) upon the consummation of the sale.

Together with the agreement to transfer the business of Sectec, the Company entered into a distribution agreement with the acquirer.

- c. On July 25, 2005, the Knesset (Israeli Parliament) passed the Law for the Amendment of the Income Tax Ordinance (No. 147), 2005, which prescribes, among others, a gradual decrease in the corporate tax rate in Israel to the following tax rates: in 2006 - 31%, in 2007 - 29%, in 2008 - 27%, in 2009 - 26% and in 2010 and thereafter - 25%.

The effect of the aforementioned amendment on the interim financial statements is immaterial.
