MAGAL SECURITY SYSTEMS LTD
Form 20-F
June 30, 2008

SECURITIES AND EXCHANGE COMMISSION

Washington D.C. 20549

FORM 20-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934**

OR

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2007

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from _________ to _________

OR

o **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Date of event requiring this shell company report __________

Commission file number: 0-21388

MAGAL SECURITY SYSTEMS LTD.

(Exact name of Registrant as specified in its charter
and translation of Registrant s name into English)

Israel

(Jurisdiction of incorporation or organization)

P.O. Box 70, Industrial Zone, Yehud 56100, Israel
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Ordinary Shares, NIS 1.0 Par Value	**NASDAQ Global Market**
	Tel Aviv Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **None**

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

Ordinary Shares, par value NIS 1.0 per share . 10,396,548

(as of December 31, 2007)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes o No x

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes o No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer x Non-accelerated filer o

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP x International Financial Reporting Standards as issued by the International Accounting Standards Board o Other o

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 Item 18 x

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

This Annual Report on Form 20-F is incorporated by reference into the Registrant s Registration Statements on Form S-8, File Nos. 333-96929 and 333-127340.

INTRODUCTION

Magal Security Systems Ltd. develops, manufactures, markets and sells complex computerized security systems, including a line of perimeter security systems, a hardware and software all in one security solution which integrates closed circuit television, or CCTV, related applications such as outdoor and indoor video motion detection systems, security management and control systems, personal emergency location systems and a pipeline security system. Our predecessor commenced operations in 1969 as a department specializing in perimeter security systems within the electronics division of Israel Aircraft Industries Ltd., or IAI. Effective April 1984, we purchased from IAI substantially all of the assets, and assumed substantially all of the related liabilities, of that department. In March 1993, we completed an initial public offering of 1,380,000 ordinary shares, in February 1997, we completed a public offering of an additional 2,085,000 ordinary shares and in April 2005, we completed a public offering of an additional 1,700,000 ordinary shares. Our ordinary shares are traded on the NASDAQ Global Market and on the Tel Aviv Stock Exchange under the symbol MAGS.

Except for the historical information contained in this annual report, the statements contained in this annual report are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to our business, financial condition and results of operations. Actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including all the risks discussed in Item 3.D. Key Information Risk Factors and elsewhere in this annual report.

Statements which use the terms believe, do not believe, expect, plan, intend, estimate, anticipate and similar expressions are inte identify forward-looking statements. These statements reflect our current views with respect to future events and are based on assumptions and are subject to risks and uncertainties. Except as required by applicable law, including the securities laws of the U.S., we do not intend to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

We have trademark rights in the United States and other national jurisdictions arising out of our trademark registrations, applications, and/or use of the following trademarks and service marks: SENSTAR-STELLAR logo, the S logos, SENSTAR-STELLAR, SENSTAR-STELLAR (and design) SENSTAR, STELLAR, STELLAR SYSTEMS, STELLAR SYSTEMS (and design), PANTHER, GUIDAR, REPELS, SENNET, PERIMITRAX, INTELLI-FLEX, INTELLI-FIELD, X-FIELD, OMNITRAX, STARLED, STARNET, FRONTLINE, E-FIELD, H-FIELD, E-FLEX, ARMOURFLEX, SIMPL, CROSSFIRE, ECHOCHECK, FLASH, FLARE, SENTRAX, OMNITRAX, XFIELD, DTR, DreamBox, Magal logo and all other marks used to identify particular products and services associated with our businesses.

Any other trademarks and trade names appearing in this annual report are owned by their respective holders.

Our address on the Internet is www.magal-ssl.com. The information on our website is not incorporated by reference into this annual report.

Our consolidated financial statements appearing in this annual report are prepared in U.S. dollars and in accordance with U.S. generally accepted accounting principles, or U.S. GAAP. All references in this annual report to dollars or $ are to U.S. dollars and all references in this annual report to NIS are to New Israeli Shekels. The representative exchange rate between the NIS and the dollar as published by the Bank of Israel on June 24, 2008 was NIS 3.373 per $1.00.

As used in this annual report, the terms we, us and our mean Magal Security Systems Ltd. and its subsidiaries, unless otherwise indicated.

Statements made in this annual report concerning the contents of any contract, agreement or other document are summaries of such contracts, agreements or documents and are not complete descriptions of all of their terms. If we filed any of these documents as an exhibit to this annual report or to any registration statement or annual report that we previously filed, you may read the document itself for a complete description of its terms.

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PART I

ITEM 1. Identity of Directors, Senior Management and Advisers

Not applicable.

ITEM 2. Offer Statistics and Expected Timetable

Not applicable.

ITEM 3. Key Information

A. Selected Consolidated Financial Data.

We have derived the following selected consolidated financial data as of December 31, 2006 and 2007 and for each of the years ended December 31, 2005, 2006 and 2007 from our consolidated financial statements set forth elsewhere in this annual report that have been prepared in accordance with U.S. GAAP. We have derived the following selected consolidated financial data as of December 31, 2003, 2004 and 2005 and for each of the years ended December 31, 2003 and 2004 from our audited consolidated financial statements not included in this annual report.

	Year Ended December 31,				
	2003	**2004**	**2005**	**2006**	**2007**
	(in thousands except per share data)				
Consolidated Statement of Income Data:					
Revenues	$ 58,252	$ 58,408	$ 58,385	$ 63,600	$ 72,375
Cost of revenues	31,852	30,532	36,658	37,236	43,510
Gross profit	26,400	27,876	21,727	26,364	28,865
Operating expenses:					
Research and development, net	4,773	4,683	5,265	5,378	5,764
Selling and marketing, net	10,577	11,923	12,385	11,603	12,930
General and administrative	4,907	4,767	4,965	5,547	6,561
Special post employment benefit					904
Award granted by principal shareholders		1,172			
Total operating expenses	20,257	22,545	22,615	22,528	26,159
Operating income (loss)	6,143	5,331	(888)	3,836	2,706
Financial expenses, net	1,003	774	813	864	2,137
Income (loss) before income taxes	5,140	4,557	(1,701)	2,972	569
Income taxes (tax benefit)	910	1,574	(28)	943	373
Income (loss) from continuing operations	4,230	2,983	(1,673)	2,029	196
Income (loss) from discontinued operations, net	(1,826)	(1,930)	(1,538)	(1,219)	1,686
Net income (loss)	2,404	1,053	(3,211)	810	1,882
Basic net earnings (loss) per share from continuing operations	$ 0.53	$ 0.35	$ (0.17)	$ 0.20	$ 0.02
Basic net earnings (loss) per share from discontinued operations	(0.23)	(0.23)	(0.15)	(0.12)	0.16

Basic net earnings (loss) per share	$ 0.30	$ 0.12	$ (0.32)	$ 0.08	$ 0.18
Diluted net earnings (loss) per share from continuing operations	$ 0.53	$ 0.35	$ (0.17)	$ 0.20	$ 0.02
Diluted net earnings (loss) per share from discontinued operations	(0.23)	(0.23)	(0.15)	(0.12)	0.16
Diluted net earnings (loss) per share	$ 0.30	$ 0.12	$ (0.32)	$ 0.08	$ 0.18
Weighted average number of ordinary shares used in computing basic net earnings per share	7,948	8,581	9,883	10,384	10,395
Weighted average number of ordinary shares used in computing diluted net earnings per share	8,029	8,636	9,900	10,442	10,431
Cash dividend per share	$ 0.05	$	$	$	$

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Our board of directors declared share dividend distributions of 3.0% and 5.0% in May 2003 and July 2004, respectively. All per share data in the above table has been adjusted to reflect the share dividends.

Effective as of September 1, 2007, our consolidated financial statements include those of the recently acquired European integration company. In December 2007, we decided to dispose of our U.S. based video monitoring business operated by SIS systems, Inc. (formerly Smart Interactive Systems Inc.,) or Smart. Accordingly, the operating results, balance sheet and cash flows relating to the video monitoring operations were presented in our statements of income, balance sheets and cash flows as discontinued operations, and the comparative figures were reclassified for all periods presented.

	As of December 31,				
	2003	2004	2005	2006	2007
			(in thousands)		
Consolidated Balance Sheet Data:					
Cash and cash equivalents	$ 4,389	$ 11,964	$ 10,099	$ 4,908	$ 9,205
Short and long-term bank deposits, marketable securities structured notes and escrow deposit	12,051	5,994	18,853	22,053	26,972
Working capital	21,608	21,504	35,071	39,884	41,526
Total assets	71,443	77,976	101,842	103,681	126,157
Short-term bank credit (including current maturities of long-term loans)	16,438	17,467	21,715	17,821	20,737
Long-term bank loans	1,873	3,500	1,653	7,399	3,095
Total shareholders equity	38,984	43,548	56,950	58,150	65,578

B. Capitalization and Indebtedness.

Not applicable

C. Reasons for the Offer and Use of Proceeds.

Not applicable.

D. Risk Factors.

Our business, results of operations and financial condition could be seriously harmed due to any of the following risks, among others. If we do not successfully address the risks to which we are subject, our business, results of operations and financial condition may be materially and adversely affected and our share price may decline.

Risks Related to Our Business

We depend on large orders from a relatively small number of customers for a substantial portion of our revenues. As a result, our revenues and operating results may vary from quarter to quarter.

We receive large orders from a relatively small number of customers and our revenues and operating results are subject to substantial periodic variations. Individual orders from customers can represent a substantial portion of our revenues in any one period and significant orders by a customer during one period may not be followed by further orders from the same customer in subsequent periods. As a result, our revenues and operating results for a specific quarter may not be indicative of our future performance and quarter-to-quarter comparisons of our operating results may not be meaningful, making it difficult for investors to evaluate our future prospects based on the results of any quarter. In addition, we have a limited order backlog, which makes revenues in any quarter substantially dependent upon orders we deliver in that quarter.

Our revenues depend on government procurement procedures and practices. A substantial decrease in our customers budgets would adversely affect our results of operations.

Our products are primarily sold to governmental agencies, governmental authorities and government-owned companies, many of which have complex and time-consuming procurement procedures. A substantial period of time often elapses from the time we begin marketing a product until we actually sell that product to a particular customer. In addition, our sales to governmental agencies, authorities and companies are directly affected by these customers budgetary constraints and the priority given in their budgets to the procurement of our products. A decrease in governmental funding for our customers budgets would adversely affect our results of operations.

The loss of one or more of our key customers, in particular the Israeli Ministry of Defense, would result in a loss of a significant amount of our revenues.

A relatively few customers account for a large percentage of our revenues. For the years ended December 31, 2005, 2006 and 2007, revenues generated from sales to the Israeli Ministry of Defense, or MOD, accounted for 23.9%, 33.7% and 13.0%, respectively, of our revenues. The loss of the MOD as a customer without replacement by a customer or customers of similar volume would have a material adverse effect on our financial results.

The level of our contracts may be reduced in the future due to changes in governmental priorities and audits.

Governmental purchases of our systems, products and services may decline in the future as the governmental purchasing agencies may terminate, reduce or modify contracts or subcontracts if:

- Their requirements or budgetary constraints change;
- they cancel multi-year contracts and related orders if funds become unavailable;
- they shift spending priorities into other areas or for other products; and
- they adjust contract costs and fees on the basis of audits.

Any such event may have a material adverse affect on us.

If we do not receive MOD approvals necessary for us to export the products we produce in Israel, our revenues may decrease.

Under Israeli law, the export of products that we manufacture in Israel and the export of certain of our know-how are subject to approval by the MOD. We must obtain permits from the MOD to initiate sales proposals with regard to these exports, as well as for actual export transactions. We may not be able to receive all the required permits for which we may apply in the future. If we do not receive the required permits for which we apply, our revenues may decrease.

The market for our products is characterized by changing technology, requirements, standards and products, and we may be adversely affected if we do not respond promptly and effectively to these changes.

The market for our products is characterized by evolving technologies, changing industry standards, changing regulatory environments, frequent new product introductions and rapid changes in customer requirements. The introduction of products embodying new technologies and the emergence of new industry standards and practices can render existing products obsolete and unmarketable. Our future success will depend on our ability to enhance our existing products and to develop and introduce, on a timely and cost-effective basis, new products and product features that keep pace with technological developments and emerging industry standards and address the increasingly sophisticated needs of our customers. In the future:

- we may not be successful in developing and marketing new products or product features that respond to technological change or evolving industry standards;

- we may experience difficulties that could delay or prevent the successful development, introduction and marketing of these new products and features; or
- our new products and product features may not adequately meet the requirements of the marketplace and achieve market acceptance.

If we are unable to respond promptly and effectively to changing technology, we will be unable to compete effectively in the future.

We face risks associated with doing business in international markets.

A large portion of our sales is to markets outside of Israel (58.5% of our sales in 2006 and 78.4% of our sales in 2007) and a key component of our strategy is to continue to expand in such markets. Our international sales efforts are affected by costs associated with the shipping of our products and risks inherent in doing business in international markets, including:

- unexpected changes in regulatory requirements;
- currency fluctuations;
- export restrictions, tariffs and other trade barriers;
- unexpected difficulties in staffing and managing foreign operations;
- longer payment cycles;
- difficulties in collecting accounts receivable;
- political instability; and
- seasonal reductions in business activities.

One or more of such factors may have a material adverse effect on us.

We may be adversely affected by our long sales cycles.

We have in the past and expect in the future to experience long time periods between initial sales contacts and the execution of formal contracts for our products and completion of product installations. The cycle from first contact to revenue generation in our business involves, among other things, selling the concept of our technology and products, developing and implementing a pilot program to demonstrate the capabilities and accuracy of our products, negotiating prices and other contract terms, and, finally, installing and implementing our products on a full-scale basis. This cycle entails a substantial period of time, sometimes as much as one or more years, and the lack of revenues during this cycle and the expenses involved in bringing new sales to the point of revenue generation may put a substantial strain on our resources.

We may not be able to implement our growth strategy.

As part of our growth strategy, we seek to acquire or invest in complementary, including competitive, businesses, products and technologies. We currently have no commitments or agreements with respect to any acquisitions or investments and we may not be able to consummate any acquisition or investment. Even if we do acquire or invest in these businesses, products or technology, the process of integrating acquired assets into our operations may result in unforeseen operating difficulties and expenditures and may absorb significant management attention that would otherwise be available for the ongoing development of our business.

In addition, we have limited experience in making acquisitions and managing growth. We may not be able to realize the anticipated benefits of any acquisition. Moreover, future acquisitions by us could result in potentially dilutive issuances of our equity securities, the incurrence of debt and contingent liabilities and amortization expenses related to identifiable intangible assets, any of which could materially adversely affect our operating results and financial position. Acquisitions also involve other risks, including risks inherent in entering markets in which we have no or limited prior experience and the potential loss of key employees and the risk that we may experience difficulty or delays in obtaining necessary permits.

We may not be able to protect our proprietary technology and unauthorized use of our proprietary technology by third parties may impair our ability to compete effectively.

Our success and ability to compete depend in large part upon protecting our proprietary technology. We have approximately 46 patents and have patent applications pending. We also rely on a combination of trade secret and copyright law and confidentiality, non-disclosure and assignment-of-inventions agreements to protect our proprietary technology. It is our policy to protect our proprietary rights in our products and operations through contractual obligations, including confidentiality and non-disclosure agreements with certain employees, distributors and agents, suppliers and subcontractors. These measures may not be adequate to protect our technology from third-party infringement, and our competitors may independently develop technologies that are substantially equivalent or superior to ours. Additionally, our products may be sold in foreign countries that provide less protection to intellectual property than that provided under U.S. or Israeli laws.

We could become subject to litigation regarding intellectual property rights, which could seriously harm our business.

Third parties may in the future assert against us infringement claims or claims asserting that we have violated a patent or infringed upon a copyright, trademark or other proprietary right belonging to them. In addition, we purchase components for our turnkey products from independent suppliers. Certain of these components contain proprietary intellectual property of these independent suppliers. Third parties may in the future assert claims against our suppliers that such suppliers have violated a patent or infringed upon a copyright, trademark or other proprietary right belonging to them. If such infringement by our suppliers or us were found to exist, a party could seek an injunction preventing the use of their intellectual property. In addition, if an infringement by us were found to exist, we may attempt to acquire a license or right to use such technology or intellectual property. Any infringement claim, even if not meritorious, could result in the expenditure of significant financial and managerial resources.

We depend on limited sources for components, and if we are unable to obtain these components when needed, we will experience delays in manufacturing our products and our financial results may be adversely affected.

We acquire most of the components utilized in our products, including, but not limited to, our turnkey products and certain services from a limited number of suppliers and subcontractors. We may not be able to obtain such items from these suppliers and subcontractors on satisfactory terms in the future. Temporary disruptions of our manufacturing operations would result if we were required to obtain materials from alternative sources, which may have an adverse effect on our financial results.

Undetected defects in our products may increase our costs and impair the market acceptance of our products.

The development, enhancement and implementation of our complex systems entail substantial risks of product defects or failures. Despite testing by us and our customers, errors may be found in existing or new products, resulting in delay or loss of revenues, warranty expense, loss of market share or failure to achieve market acceptance, or otherwise adversely affecting our business, financial condition and results of operations. Moreover, the complexities involved in implementing our systems entail additional risks of performance failures. We may encounter substantial delays or other difficulties due to such complexities. Any such occurrence could have a material adverse effect upon our business, financial condition and results of operations. In addition, the potential harm to our reputation that may result from product defects or implementation errors could be damaging to us.

We depend on our senior management and key personnel, particularly Izhar Dekel, our president and chief executive officer, and his loss would negatively affect our business.

Our future success depends in large part on the continued services of our senior management and key personnel. In particular, we depend on the services of Mr. Dekel, our president and chief executive officer. We carry key person life insurance for Mr. Dekel. Any loss of the services of Izhar Dekel, other members of senior management or other key personnel would negatively affect our business.

Our failure to retain and attract personnel could harm our business, operations and product development efforts.

Our products require sophisticated research and development, marketing and sales and technical customer support. Our success depends on our ability to attract, train and retain qualified research and development, marketing and sales and technical customer support personnel. Competition for personnel in all of these areas is intense and we may not be able to hire sufficient personnel to achieve our goals or support the anticipated growth in our business. If we fail to attract and retain qualified personnel, our business, operations and product development efforts would suffer.

We may fail to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act of 2002, which could have an adverse effect on our financial results and the market price of our ordinary shares.

The Sarbanes-Oxley Act of 2002 imposes certain duties on us and our executives and directors. Our efforts to comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 governing internal controls and procedures for financial reporting, which started in connection with our Annual Report on Form 20-F for the year ended December 31, 2006, have resulted in increased general and administrative expense and a diversion of management time and attention, and we expect these efforts to require the continued commitment of significant resources. We may identify material weaknesses or significant deficiencies in our assessments of our internal controls over financial reporting. Failure to maintain effective internal controls over financial reporting could result in investigation or sanctions by regulatory authorities and could have a material adverse effect on our operating results, investor confidence in our reported financial information and the market price of our ordinary shares.

Risks Relating to Our Ordinary Shares

Volatility of the market price of our ordinary shares could adversely affect our shareholders and us.

The market price of our ordinary shares has been, and is likely to be, highly volatile and could be subject to wide fluctuations in response to numerous factors, including the following:

- political, economic and other developments in the State of Israel;
- terrorist attacks and other acts of war, and any response to them;
- actual or anticipated variations in our quarterly operating results or those of our competitors;
- announcements by us or our competitors of technological innovations or new and enhanced products;
- developments or disputes concerning proprietary rights;
- introduction and adoption of new industry standards;
- changes in financial estimates by securities analysts;
- market conditions or trends in our industry;
- changes in the market valuations of our competitors;
- announcements by us or our competitors of significant acquisitions;

- entry into strategic partnerships or joint ventures by us or our competitors; and
- additions or departures of key personnel.

In addition, the stock market in general, and the market for Israeli companies and home defense companies in particular, has been highly volatile. Many of these factors are beyond our control and may materially adversely affect the market price of our ordinary shares, regardless of our performance.

Risks Relating to Our Location in Israel

Political, economic and military instability in Israel may disrupt our operations and negatively affect our business condition, harm our results of operations and adversely affect our share price.

We are incorporated under the laws of, and our principal executive offices and manufacturing and research and development facilities are located in, the State of Israel. As a result, political, economic and military conditions affecting Israel directly influence us. Any major hostilities involving Israel, a full or partial mobilization of the reserve forces of the Israeli army, the interruption or curtailment of trade between Israel and its present trading partners, or a significant downturn in the economic or financial condition of Israel could have a material adverse effect on our business, financial condition and results of operations.

Since the establishment of the State of Israel in 1948, Israel and its Arab neighbors have engaged in a number of armed conflicts. A state of hostility, varying from time to time in intensity and degree, has led to security and economic problems for Israel. Major hostilities between Israel and its neighbors may hinder Israel s international trade and lead to economic downturn. This, in turn, could have a material adverse effect on our operations and business. There has been an increase in unrest and terrorist activity in Israel, which began in September 2000 and which has continued with varying levels of severity through 2007. The future effect of this deterioration and violence on the Israeli economy and our operations is unclear. Recently, there was an escalation in violence among Israel, Hamas, the Palestinian Authority and other groups, as well as extensive hostilities along Israel s northern border with Lebanon in the summer of 2006, and extensive hostilities along Israel s border with the Gaza Strip since June 2007 when the Hamas effectively took control of the Gaza Strip, which have intensified since February 2008. Ongoing violence between Israel and the Palestinians as well as tension between Israel and the neighboring Syria and Lebanon may have a material adverse effect on our business, financial conditions and results of operations.

Furthermore, there are a number of countries, primarily in the Middle East, as well as Malaysia and Indonesia, that restrict business with Israel or Israeli companies, and we are precluded from marketing our products to these countries. Restrictive laws or policies directed towards Israel or Israeli businesses may have an adverse impact on our operations, our financial results or the expansion of our business.

Our results of operations may be negatively affected by the obligation of our personnel to perform military service.

Many of our executive officers and employees in Israel are obligated to perform annual reserve duty in the Israeli Defense Forces, or IDF, and are subject to being called for active duty under emergency circumstances at any time. If a military conflict or war arises, these individuals could be required to serve in the military for extended periods of time. Our operations could be disrupted by the absence for a significant period of one or more of our executive officers or key employees or a significant number of other employees due to military service. Any disruption in our operations could adversely affect our business.

We may be adversely affected by a change in the exchange rate of the NIS against the dollar.

Because exchange rates between the NIS, our functional currency, and the dollar fluctuate continuously, exchange rate fluctuations, particularly larger periodic devaluations, may have an impact on our profitability and period-to-period comparisons of our results. In 2006 and 2007, the NIS appreciated against the U.S. dollar by 8.2% and 9.0%, respectively, and the Euro appreciated against the U.S. dollar by 10.2% and 10.5%, respectively. A portion of our expenses, primarily labor expenses, is incurred in NIS and a part of our revenues are quoted in NIS. Additionally, certain assets, as well as a portion of our liabilities, are denominated in NIS. Our results may be adversely affected by the devaluation of the NIS in relation to the dollar (or if such devaluation is on lagging basis), if our revenues in NIS are higher than our expenses in NIS and/or the amount of our assets in NIS are higher than our liabilities in NIS. Alternatively, our results may be adversely affected by an appreciation of the NIS in relation to the dollar (or if such appreciation is on a lagging basis), if the amount of our expenses in NIS are higher than the amount of our revenues in NIS and/or the amount of our liabilities in NIS are higher than our assets in NIS.

We currently benefit from government programs and tax benefits that may be discontinued or reduced.

We currently receive grants and tax benefits under Israeli government programs, we must continue to meet specified conditions, including, but not limited to, making specified investments from our equity in fixed assets and paying royalties with respect to grants received. In addition, some of these programs restrict our ability to manufacture particular products or transfer particular technology outside of Israel. If we fail to comply with these conditions in the future, the benefits we receive could be canceled and we could be required to refund any payments previously received under these programs, including any accrued interest, or pay increased taxes or royalties. The Israeli government has reduced the benefits available under these programs in recent years and these programs and benefits may be discontinued or curtailed in the future. If the Israeli government ends these programs and benefits, our business, financial condition, results of operations and net income could be materially adversely affected.

Your rights and responsibilities as a shareholder will be governed by Israeli law and differ in some respects from the rights and responsibilities of shareholders under U.S. law.

We are incorporated under Israeli law. The rights and responsibilities of holders of our ordinary shares are governed by our memorandum of association, articles of association and by Israeli law. These rights and responsibilities differ in some respects from the rights and responsibilities of shareholders in typical U.S. corporations. In particular, shareholder of an Israeli company has a duty to act in good faith in exercising his or her rights and fulfilling his or her obligations toward the company and other shareholders and to refrain from abusing his power in the company, including, among other things, in voting at the general meeting of shareholders on certain matters. Israeli law provides that these duties are applicable in shareholder votes on, among other things, amendments to a company s articles of association, increases in a company s authorized share capital, mergers and interested party transactions requiring shareholder approval. In addition, a controlling shareholder of an Israeli company or a shareholder who knows that it possesses the power to determine the outcome of a shareholder vote or who has the power to appoint or prevent the appointment of a director or executive officer in the company has a duty of fairness toward the company. However, Israeli law does not define the substance of this duty of fairness. Because Israeli corporate law has undergone extensive revision in recent years, there is little case law available to assist in understanding the implications of these provisions that govern shareholder behavior.

It may be difficult to enforce a non-Israeli judgment against us, our officers and directors.

All of our executive officers and directors are nonresidents of the United States, and a substantial portion of our assets and the assets of these persons are located outside the United States. Therefore, it may be difficult for an investor, or any other person or entity, to enforce against us or any of those persons in an Israeli court a U.S. court judgment based on the civil liability provisions of the U.S. federal securities laws. It may also be difficult to effect service of process on these persons in the United States. Additionally, it may be difficult for an investor, or any other person or entity, to enforce civil liabilities under U.S. federal securities laws in original actions filed in Israel.

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

As a foreign private issuer whose shares are listed on The NASDAQ Global Market, we are permitted to follow certain home country corporate governance practices instead of certain requirements of the NASDAQ Marketplace Rules. A foreign private issuer that elects to follow a home country practice instead of such requirements must submit to NASDAQ in advance a written statement from an independent counsel in such issuer s home country certifying that the issuer s practices are not prohibited by the home country s laws. In addition, a foreign private issuer must disclose in its annual reports filed with the Securities and Exchange Commission or on its website each such requirement that it does not follow and describe the home country practice followed by the issuer instead of any such requirement. As a foreign private issuer listed on The NASDAQ Global Market, we may follow home country practice with regard to, among other things, composition of the board of directors, director nomination procedure, compensation of officers, and quorum at shareholders meetings. In addition, we may follow our home country law, instead of the NASDAQ Marketplace Rules, which require that we obtain shareholder approval for certain dilutive events, such as for the establishment or amendment of certain equity based compensation plans, 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.

ITEM 4. Information on the Company

A. History and Development of the Company.

We were incorporated under the laws of the State of Israel on March 27, 1984 under the name Magal Security Systems Ltd. We are a public limited liability company under the Israeli Companies Law, 5739-1999 and operate under this law and associated legislation. Our principal executive offices and primary manufacturing and research and development facilities are located near Tel Aviv, Israel, in the Yehud Industrial Zone. Our mailing address is P.O. Box 70, Industrial Zone, Yehud 56100, Israel and our telephone number is 972-3-539-1444. Our agent for service of process in the U.S. is Magal Senstar Inc., 43184 Osgood Road, Fremont, CA, 94539. Our address on the Internet is www.magal-ssl.com. The information on our website is not incorporated by reference into this annual report.

We develop, manufacture, market and sell complex computerized security systems, including a line of perimeter security systems, a hardware and software all in one security solution which integrates CCTV, related applications such as outdoor and indoor video motion detection systems, security management and control systems, personal emergency location systems and a pipeline security system.

On August 31, 2007, we entered into an agreement to purchase all of the shares of a European company engaged in the installation and integration of security systems, in consideration for 6.8 million Euros (approximately $9.3 million). Of such amount, three million Euros are being held in escrow and is payable subject to the fulfillment of certain conditions. Additional amounts will be paid over the next five years based on the European company s pre-tax income. The European company s financial statements have been consolidated, effective as of September 1, 2007, into our financial statements. This acquisition is in line with our strategic plan. The company is active in geographic areas where we have limited activity, and we expect it to contribute to our expansion in the integration field, particularly in countries with strong growth potential for our leading security solutions.

In December 2007 we sold our U.S. based video monitoring business that was operated by Smart, for $8.5 million. We recorded a gain of approximately $2.4 million on the sale in 2007. For a discussion of our capital expenditures and divestitures, see Item 5.B. Operating and Financial Review and Prospects Liquidity and Capital Resources.

B. Business Overview.

General

We develop, manufacture, market and sell complex computerized security systems. Our systems are used in more than 75 countries to protect sensitive facilities, including national borders, military bases, power plant installations, airports, postal facilities, prisons, industrial locations and municipalities from terrorism, theft and other threats. Our revenues are principally derived from:

- installation of comprehensive security systems for which revenues are generated from long-term fixed price contracts;
- sales of security products; and
- services and maintenance, which are performed either on a fixed-price basis or as time-and-materials based contracts.

Business and Marketing Strategy

Our primary objective is to become a leading provider of security systems worldwide. To achieve this objective, we have implemented a business strategy incorporating the following key elements:

Refine and Broaden Product Line. We have identified the security needs of our customers and intend to enhance our current products and develop new products to meet those needs. We intend to continue to focus on developing new products, expanding the capabilities of existing products and making custom enhancements for specific projects.

Enter New Markets and Strengthen Presence in Existing Markets. In 2008 we intend to continue to penetrate new geographic markets by various means, including the establishment of alliances with local distributors and international integrators of security systems. In September 2007, we acquired a European company which is engaged in the installation and integration of security systems, and is active in geographical areas where we had limited activity so far. We believe that this newly acquired company will help us enter into new geographical markets. We also intend to increase our marketing efforts in our existing markets and to acquire or invest in complementary, including competitive, businesses, products and technologies.

Leverage Existing Customer Base; Cross-Market Products. We believe that we have the capability to offer certain of our customers a comprehensive security package. As part of our product development process, we seek to maintain close relationships with our customers to identify market needs and to define appropriate product specifications. We intend to expand the depth and breadth of our existing customer relationships while initiating similar new relationships

Offer Comprehensive Turnkey Solutions. By broadening our product range to include both indoor and outdoor security systems and by developing our security management and control systems and Dreambox   all in one   CCTV security solution, we now offer comprehensive turnkey security solutions that provide a comprehensive security implementation process. This process entails:

- in-depth threat analysis;
- determination of the appropriate hardware and software solutions;
- training sessions for systems operators; and
- upon customer approval, integration of the required systems into our security management and control systems.

We believe that the market for turnkey security solutions presents a significant opportunity. In addition, we believe that we will be able to expend our activities in the market for turnkey security solution through the European company we acquired in 2007. We are emphasizing our ability to offer turnkey solutions in keeping with our objective of becoming a leading provider of comprehensive security solutions.

Products and Services

Perimeter Security Systems

Perimeter security systems enable customers to monitor, limit and control access by unauthorized personnel to specific regions or areas. High-end perimeter systems are sophisticated in nature and are used by correctional facilities, military installations, power companies and other high-security installations. We believe that we are a leading provider of security systems and maintenance in this industry.

Our line of perimeter security systems utilizes sophisticated sensor devices to detect and locate intruders and identify the nature of intrusions. Our perimeter security systems have been installed along thousands of kilometers of borders and facility boundaries throughout the world, including more than 600correctional institutions in the U.S. and correctional institutions in several other countries. In addition, we have installed several hundred miles of high security electronic perimeter systems along Israel s borders.

Our line of perimeter security systems consists of the following:

- taut wire perimeter intrusion detection systems;
- vibration detection systems;
- field disturbance sensors;
- video analytics and video motion detection systems; and
- the *MTC-1500E* and the *MSS-1500*.

Taut Wire Perimeter Intrusion Detection Systems

Our taut wire systems consist of wire strung at high tension between anchor posts. Sensor posts are located at the middle between anchor posts. These sensor posts contain one or more devices that detect changes in the tension being exerted on and by the taut wires. Any force applied against these wires, or released from them, as by cutting, unless within the parameters designed into the sensors themselves or programmed into the central control units, automatically triggers an alarm. We use taut wire perimeter systems as both an integral component of intruder detection systems and as a physical barrier to infiltration.

Our sealed sensors are not affected by radio frequency interference, climatic or atmospheric conditions, or electrical transients from power lines or passing vehicles. The sensors self-adjust to, or remain unaffected by, extreme temperature variations, minor soil movements and other similar environmental changes that might trigger false alarms in less sophisticated systems. Our taut wire perimeter systems are designed to discriminate automatically between fence tension changes typically caused by small animals or violent weather and forces more typically exerted by a human intruder.

Our taut wire perimeter systems offer customers a wide range of installation options. Sensor posts can be as far as 200 feet apart, with relatively inexpensive ordinary fence anchor posts between them. These systems may stand alone, be mounted on a variety of fence posts or added to an existing wall or other structure, or mounted on short posts, with or without outriggers.

Taut wire perimeter systems have been approved by various Israeli and U.S. security and military authorities. We have installed several hundred kilometers of these perimeter systems along Israel s borders to assist in preventing unauthorized entry and infiltration. Our taut wire perimeter systems are sold for approximately $50-$150 per meter.

Vibration Detection Systems

We offer various types of vibration detection systems. While less sensitive than taut wire installations, the adaptability of these systems to a wide range of pre-existing barrier structures makes these products viable alternatives for cost-conscious customers. Our vibration detection devices are most effective when installed on common metal fabric perimeter systems, such as chain link or welded mesh. In our BARRICADE 500 system, pairs of electro-mechanical sensors are attached to fence panels three meters apart on any of several common types of fence structures. Once attached to the fence, each sensor detects vibrations in the underlying structures. The sensor system s built-in electro-mechanical filtering combines with system input from a weather sensor to minimize the rate of false alarms from wind, hail or other sources of nuisance vibrations.

Intelli-FLEX, Intelli-FIBER and fence protection systems, or FPS, microprocessor-based triboelectric and electric cable fence sensors are vibration sensitive transducers. These systems detect any attempt to cut, climb or penetrate the fence and have microphonic properties. The microphonic feature permits audio to be used for low-cost alarm assessment, providing users with an additional tool for determining the nature of an attempted intrusion. Our vibration detection system is sold for between $9-$60 per meter.

Field Disturbance Sensors

We offer a number of types of field disturbance sensors that detect intrusions before the intruder touches the sensor. Our line of field disturbance sensors consists of the following:

- The Intelli-Field volumetric electronic field disturbance sensor can be installed outdoors on perimeter systems, buildings or as free-standing units. The Intelli-Field system is sold for approximately $95-$160 per meter. The Perimitrax buried volumetric field disturbance sensor can be buried in most types of soil and paved areas and uses leaky coax technology to detect attempted perimeter penetrations. The Perimitrax system is sold for approximately $70-$180 per meter.

- Omnitrax is a fifth generation, covert outdoor perimeter security intrusion detection sensor that generates an invisible radar detection field around buried sensor cables. An alarm is emitted and the exact location identified within one meter if an intruder disturbs the field. Targets are detected by their conductivity, size and movement and the digital processor is able to filter out common alarms caused by environmental conditions and small animals. The Omnitrax system is sold for approximately $57-$176 per meter.

- X-Field is a terrain following, volumetric sensor that creates an electrostatic field around a set of 4 or 8 parallel field and sense wires. These wires can be mounted on free-standing poles, existing fences, walls or rooftops and will sense changes, via the processor, in the electrostatic field when events such as intruders penetrating through the wires take place. The system s tall, narrow, well contained detection zone allows the sensor to be installed in almost any application and minimizes nuisance alarms caused by nearby moving objects. The X-Field system is sold for approximately $114-$190 per meter.

We have installed high-security taut wire electronic perimeter systems over several hundred kilometers of Israel s borders and have sold a number of our high-security perimeter systems to protect other locations in Israel, including Ben-Gurion International Airport, facilities of IAI and the Israel Electric Company, industrial plants, prisons, refineries, ports and military bases. Outside Israel, our high-security perimeter systems have been purchased to protect various sites, including military installations, airports, ports, refineries, conventional and nuclear power stations, oil tank farms, industrial facilities, storage areas and warehouses, royal palaces and presidential residences in various European countries, North America, South America, Africa and the Far East.

Currently, airport security activities concentrate almost exclusively on screening passengers and luggage within the airport terminal in connection with passenger check-in. We are aware of only a few airports in the world which currently have high-security perimeter protection systems to prevent infiltrators from reaching the airport s grounds from outside. Most of these airports utilize a system manufactured by us. In marketing our high-security perimeter systems, we target authorities responsible for airport security. To date, we have sold and installed perimeter systems at certain airports in Israel, Europe, the U.S. and the Far East. We are continuing to negotiate with authorities in several other countries to install our perimeter systems around airports.However, we cannot assure you that any revenues will result from these negotiations.

Our high-security perimeter systems offer prison authorities the opportunity to address an escape attempt in real-time, rather than at the next roll-call, which may be several hours after the escape. Our high-security perimeter systems have already been installed in prisons in Australia, Europe, Israel, North America, South America and the Far East.

The IDF has tested our perimeter security products along with those of several of our competitors and our system and two competitor s systems were the only systems to be approved for participation in the MOD s bid for perimeter security systems.

Video analytics and video motion detection systems

The DreamBox is a state-of-the-art embedded hardware and software product which integrates a number of CCTV related applications into one box. The system is designed to be economical, as well as compact to save space, by avoiding the use of a complicated cable installation and integration. It contains twelve different applications, including a digital video and audio recording, video and audio matrix switcher, outdoor and indoor video motion detection system, or VMD, security management system, or SMS, and a transmission system.

The DreamBox, is sold at a substantially lower price than the cost of the other product applications if sold separately, a factor which positions DreamBox as the leading security solution for all strategic facilities. Its target markets include governmental, institutional and other sensitive facilities, such as airports, train stations, seaports, prisons, casinos and hospitals, all of which require the use of high quality CCTV applications.

We refer to the DreamBox s target market as an add-on market for us, and believe that this product is substantially broadening our target markets. As an example, we entered the field of digital video recording, which is only one of many DreamBox applications.

MTC-1500E

The MTC-1500E is an integrated thermal/daylight camera, specially designed for strategic sites and secured areas such as borders, airports, seaports, pipelines, refineries, communication centers, prisons, special operations and municipal surveillance. The all-weather sealed unit provides high resolution multi-sensor monitoring, utilizing an electro-optical video system which combines a micro bolometric thermal camera for night vision and a CCD camera for daylight use. This solution is able to detect human targets from more then 1500 meters under variable lighting, temperature and weather conditions- day or night, from sub-zero to very high temperatures- in rain, dust, sand or fog.

MSS-1500

The MSS-1500 is a rapidly-deployable, flexible, high-definition, surveillance system for use by surveillance and security forces. It monitors situations and detect intrusions and suspicious movements through high-quality optical and thermal cameras having a continuous operating capability of over 4 hours. The MSS-1500 is a stand-alone system consisting of a remote observation unit, self-sufficient power supply and command center. The system may be set up and be fully deployed in just 4 minutes. It is a vital resource in special surveillance situations, including criminal investigation, crowd and riot control and border patrol.

Security Management and Control Systems

The deployment of multiple security systems creates the need for a system that can manage and control these systems through a single database. In response to this need, we offer MagNet and Fortis, security management and control systems that integrate the management, control and display of various security systems, both outdoor, such as perimeter security systems, and indoor, such as fire detection, entry monitoring and alarm systems, into a single, real-time database, and support real-time decision making and wide area command and control. These systems were developed to improve the response to real-time security events by sharing video and geographical information between the control center and security personnel acting in the field. Since their introduction, we have sold our security management systems and provided turnkey projects to several customers, including large international companies and international airports.

MagNet Security Management System

MagNet, our security management system, integrates the management, control and display of various security systems into a single, real-time database. MagNet, which is based on computer communications and controlled by a unique server developed by us, converts real-time data received from field units, analyzes that data and transmits operational commands accordingly. It also generates alarms to indicate problems with any connected security system and provides explanations as to the causes of the alarms. MagNet displays video pictures of the alarm source, using an advanced video matrix with a user-friendly interface. The operational commands transmitted by MagNet are routed back to the field units or to operator workstations which then convert these commands to visual information and allow the system operator to respond and influence the system s operation.

MagNet integrates various detection technologies, including infrared and microwave, and enables multiple operators to simultaneously control the system. It can serve and manage multiple security systems, sensors, detectors and controllers, and is unaffected by the distance between the various system components under its control. MagNet can integrate and control both outdoor security systems and indoor security systems, and its open architecture enables operation with systems manufactured by other manufacturers as well as those manufactured by us. Data can be entered into the MagNet system from anywhere in the world through the Internet, provided appropriate authorization exists. In addition, MagNet s TCP/IP protocol and Ethernet boards, using the Windows NT operating system, allow the system to use a wide range of communications media, such as telephone lines, fiber optics and wireless communication. MagNet operates with, and can provide solutions for, various types of security configurations, as well as adaptations for additional and new security systems.

Fortis Integrated Command and Control System

Fortis, our fully integrated command and control system, supports real-time decision making and wide-area command and control. Fortis reduces the period of time from intruder detection to intruder engagement to a minimum. Fortis was developed to improve the response to real-time security events by sharing video and geographical information between the control center and security personnel acting in the field.

The system creates a unified and interactive intelligence picture - drawing data from all sensors, while displaying the movement of security personnel in the field and adding other relevant information, such as video from various sources, auxiliary services and weather conditions. This combined picture, which is continuously updated, is sent by the central command to all security personnel in the command chain, and serves as a unified basis for operational planning and allocation of tasks. Using advanced technology, Fortis provides the security officer with a graphical command tool, which updates the location details and video view of the alerting area, while simultaneously enabling a constant watch over security personnel movements, thus optimizing the operational response.

Fortis target markets include governmental, institutional and large sensitive facilities, such as borders, airports, hospitals, power plants and water sources, as well as large manufacturing facilities requiring real-time control and protection.

Pipeline Security Systems

As of end of 2007, there were an estimated three million miles of unprotected oil and gas pipelines worldwide. Although the need for securing these pipelines has been strongly recognized by the oil and gas industry for years, and in spite of increasing threats since the events of 9/11 and current instability in Iraq and elsewhere in the Middle East, there was no effective solution for securing buried pipes against damage caused by terror, sabotage, theft or other third party threats. We have identified the demand and have implemented a technology aimed at meeting this challenge. PipeGuard, our pipeline security system, provides a solution for securing buried assets and infrastructure, including oil and gas pipelines and buried communication lines such as fiber optic cables.

PipeGuard utilizes an innovative and unique technology to guard buried pipelines, regardless of pipeline length, with the ability to detect potential attack and alert authorities before potential harm or damage occurs. Its target market includes oil and gas companies, owners and operators of pipelines or communication cables and governmental agencies dealing with security and environment.

In addition, since 2006 we market and sell PipeGuard to banks, to protect them from underground intrusions. Following a long and thorough market study, we determined that one of the major physical threats that banks worldwide currently face, are robberies of valuables contained in safes located below ground by the digging of tunnels beneath the bank s building. PipeGuard has the ability to prevent underground intrusions into bank buildings and break-ins into bank s safes and other secure areas.

PipeGuard combines well proven sensors, geophones, with advanced edge of technology recognition algorithm capabilities based on the analysis of seismic signals, thus effectively filtering out false alarms. Using state of the art communications, only predefined signals are transmitted to the control station.

PipeGuard is suitable for all pipes or cables, from existing and operational pipelines, to new pipelines under construction. The system can easily be integrated into a full turnkey security solution, including perimeter protection, ground or air patrol and others. By answering the challenge of securing pipelines, we offer a total security solution for the oil and gas industry - from the oil field to the refineries.

Personal Emergency Location Systems

Our products deliver high reliability personal portable duress alarm systems to protect personnel in correctional facilities. These products identify individuals in distress and can pinpoint the location of the distress signal with an indoor-to-outdoor and floor-to-floor accuracy unmatched by any other product.

Flash Personal Emergency Alarm Systems, or Flash, and Flare Personal Emergency Locating Systems, or Flare, use radio frequency technology to provide a one touch emergency system that is so small it can be worn on a belt. The systems, sold mainly to correctional facilities, consist of transmitters that send distress signals to receivers mounted throughout the building. Receivers relay the signal to a central location indicating someone requires assistance and their location in the building. The systems employ automated testing procedures that help to reduce maintenance costs. The hardware and software was developed and researched in the U.S. and competes against infrared and ultrasonic technologies.

Our personal alarm system, or PAS, uses an ultrasonic based emergency notification and communication system. The system, sold mainly to correctional facilities, allows individuals moving throughout a facility to quickly indicate their exact location in a crisis situation through a transmitter that is carried by them.

Marketing, Sales and Distribution

We market products primarily to government agencies, government authorities and government-owned companies. However, the activities of certain of these government bodies are increasingly being privatized in jurisdictions throughout the world. We believe that our reputation as a vendor of high-security products in one of the world s most security-conscious countries often provides us and our sales representatives with direct access to senior government and corporate officials in charge of security matters elsewhere.

We also distribute perimeter intrusion detection systems to private corporations. We attempt to initiate contacts with potential customers at trade shows, where we demonstrate our products and distribute promotional materials. After initial discussions, we generally seek to provide potential customers with products on a trial basis or in a small-scale installation. We believe that this affords prospective purchasers an opportunity to assess our products over a sustained period of time under realistic conditions. We have sales offices in the United Kingdom, Germany, Mexico, the United States, China, Romania and Poland.

In 2006, our U.S. subsidiary opened a new marketing and sales office in Herndon, VA, adjacent to Washington Dulles Airport. This office serves the growing needs of local, state and federal Homeland Security requirements. This office focuses exclusively on providing a comprehensive security architecture for perimeter applications, which is comprised of command and control, physical security sensors, and intelligent video. The office hosts a solution center demonstrating several of our advanced sensor solutions for intrusion detection, pipeline infiltration, intelligent video surveillance, multi-sensor command and control, as well as integration of our leading perimeter sensors, with advanced intelligent video for real time decision support on the response to possible intrusions.

Perimeter Intrusion Detection Systems

We generally sell our perimeter intrusion detection systems to distributors for various geographic territories or for specific projects. These distributors then resell these products at prices negotiated with their respective customers. In some cases, however, we pay commissions on these third-party sales either to the distributor or to the sales representatives responsible for facilitating the transaction. In addition to marketing activities, some of our distributors also provide installation and maintenance services for our products. We currently have over 50distributors who resell these systems. We occasionally use agents to find suitable distributors and pay finders fees to these agents for their services.

Security Management and Control Systems, DreamBox and Turnkey Projects

Our marketing efforts for our Security Management and Control Systems, DreamBox and turnkey projects consists of direct contacts with potential customers. We offer the MagNet, Fortis and DreamBox products primarily as part of comprehensive turnkey project solutions or, at the customer s preference, as stand-alone products. We distribute our systems in the U.S. and Canada through our U.S. and Canadian subsidiaries**.**

Pipeline Security Systems

The target markets for our pipeline security systems include oil and gas companies, owners and operators of pipelines or communication cables and governmental agencies engaged with security and environment issues.

Personal Emergency Location Systems

We market our personal emergency location systems directly to potential customers, mainly correctional facilities in North America.

The following table shows the breakdown of our consolidated revenues for the calendar years 2005, 2006 and 2007 by operating segment:

	Year Ended December 31,		
	2005	**2006**	**2007**
		(In thousands)	
Perimeter products	$ 40,143	$ 47,186	$ 43,781
Turnkey projects	17,970	16,167	28,167
Other	272	247	427
Total	$ 58,385	$ 63,600	$ 72,375

Customers

The following table shows the geographical breakdown of our consolidated revenues for the calendar years 2005, 2006 and 2007:

	Year Ended December 31,		
	2005	2006	2007
		(In thousands)	
Israel	$ 19,309	$ 26,385	$ 15,663
North America	19,047	14,176	14,869
Europe	9,935	9,793	18,342
South and Latin America	3,165	7,456	6,818
Africa	700	321	10,879
Others	6,229	5,469	5,804
Total	$ 58,385	$ 63,600	$ 72,375

For the years ended December 31, 2005, 2006 and 2007, revenues generated from sales to the MOD and the IDF, accounted for 23.9%, 33.7% and 13%, respectively, of our revenues. We cannot assure you that the MOD, IDF, or any of our other major customers will maintain their volume of business with us or that, if such volume is reduced, other customers generating similar revenues will replace the lost business. The loss of one or more of these existing customers without replacement by a customer or customers of similar volume would have a material adverse effect on our financial results.

In January 2008 we received a series of orders totaling approximately $45 million for a turnkey project to protect critical infrastructure facilities. The turnkey project incorporates fence perimeter protection systems, access control systems and CCTV products. We expect to recognize income from these orders over the next two years.

Support and Maintenance

Our systems are installed by us or by the customer after appropriate training, depending on the size of the specific project and the location of the customer s facilities, as well as on the customer s prior experience with our systems. We generally provide our customers with training on the use and maintenance of our systems. This training is conducted either on-site or at our facilities. In addition, some of our local perimeter security systems customers have signed maintenance contracts with us. For systems installed outside of Israel, maintenance is provided by an independent third party, by distributors or by the end user. We also provide services, maintenance and support on an as needed basis.

We require distributors of our high-security perimeter systems to purchase a demonstration kit that includes full-scale models of our perimeter products, and to send technical personnel to Israel to participate in courses given by us that focus on the marketing, installation and servicing of our products.

Similarly, with regard to our subsidiaries products, customer personnel are trained in product installation and maintenance either at the subsidiaries facilities or at the customer s facility. Installation supervision and assistance are sometimes purchased along with the equipment. The life expectancy of a high-security perimeter system is approximately ten years. Consequently, many miles of perimeter systems need to be replaced each year.

During 2007, we derived approximately 6% of our total revenues from maintenance and services. We generally provide a 12 to 24 months warranty on most of our products.

Research and Development; Royalties

We place considerable emphasis on research and development to improve our existing products and technology and to develop new products and technology. We believe that our future success will depend upon our ability to enhance our existing products and technology and to introduce on a timely basis new commercially viable products and technology addressing the needs of our customers. We intend to continue to devote a significant portion of our personnel and financial resources to research and development. As part of our product development process, we seek to maintain close relationships with our customers to identify market needs and to define appropriate product specifications. Our development activities are a direct result of the input and guidance we receive from our marketing personnel during our annual meetings with such personnel. In addition, the heads of research and development for each of our development centers discussed below meet annually to identify market needs for new products.

Our research and development expenses during 2005, 2006 and 2007 were approximately $5.4 million, $5.5 million and $5.9 million respectively, which were offset by Canadian investment tax credits, of approximately $154,000, $162,000 and $160,000 and a $8,000 grant form the OCS in 2005. In addition to our own research and development activities, we also acquire know-how from external sources. We cannot assure you that any of our research and development projects will yield profitable results.

We have the following three development centers, each of which develops various products and technologies based on its area of expertise:

- Israel - we develop a wide range of products including our taut wire, mechanical vibration, video and high-end SMS systems and PipeGuard;
- in California - we develop our microphonic fence sensors as well as our microwave detection, personal alarm and small/medium and control systems; and
- Canada - we develop our leaky coax radar, triboelectric and fiber-optic fence sensors, electrostatic volumetric detection and medium to high-end control systems and personal emergency location systems.

Office of the Chief Scientist of the Israel Ministry of Industry, Trade and Labor

We have historically sought co-financing of our development projects from the office of the OCS. We are obligated to pay royalties to the OCS, amounting to 3% to 4.5% of revenues derived from sales of the products funded with these grants, up to an amount equal to 100% of the grants received, linked to the U.S. dollar. All grants received after January 1, 1999 also bear interest at the rate of LIBOR. The obligation to pay these royalties is contingent on actual sales of the products, and in the absence of such sales, no payment is required. We paid royalties amounting to $83,000, $79,000 and $143,000 in the years ended December 31, 2005, 2006 and 2007, respectively. As of December 31, 2007, our aggregate contingent obligation to the OCS amounted to $1.5 million.

The terms of these grants require that the manufacture of products developed with these grants be performed in Israel and prohibit transferring technology developed with grants without the prior consent of the Research Committee of the OCS. We cannot assure you that, if requested, the OCS will grant such consent. Each application to the OCS is reviewed separately, so we cannot assure you that the Israeli Government will continue to support our research and development.

Backlog

As of May 31, 2008, our backlog amounted to approximately $64.9 million of which approximately $45.6 million is expected to be delivered by the end of 2008, $18.7 million is expected to be delivered by the end of 2009 and $586,000 million is expected to be delivered thereafter.

Manufacturing and Supply

Our manufacturing operations consist of designing and developing our products, fabricating and assembling components and finished products, quality control and final testing. Substantially all of our manufacturing operations are currently performed at our plant in Yehud, Israel. See Property, Plants and Equipment below.

We acquire most of the components utilized in our products, including, but not limited to, our turnkey products, and certain services from a limited number of suppliers and subcontractors. We cannot assure you that we will continue to be able to obtain such items from these suppliers on satisfactory terms. Alternative sources of supply are available, and therefore, we are not dependent upon these suppliers and subcontractors. We also maintain an inventory of systems and spare parts in order to enable us to overcome potential temporary supply shortages until an alternate source of supply is available. Nevertheless, temporary disruptions of our manufacturing operations would result if we were required to obtain materials from alternative sources, which may have an adverse effect on our financial results.

Our Canadian manufacturing operations are located at our facility in Carp, Ontario, Canada and consist of design and development, assembly, final testing and quality control. We use local subcontractors for producing and mounting our printed circuit board assemblies.

Our U.S. manufacturing operations are located at our facility in Fremont, California and consist of development and design, assembly, quality control and final testing. We use local subcontractors for producing and mounting our printed circuit board assemblies.

Competition

The principal factors affecting competition in the market for security systems are a system s high probability for detection and low probability of false and nuisance alarms. We believe that a manufacturer s reputation for reliable equipment is a major competitive advantage, and that such a reputation will usually be based on the performance of the manufacturer s installed systems. Additional competitive factors include quality of customer support, maintenance and price. We believe that we are competitive with respect to these factors and that we have a good reputation in the markets in which we compete.

Several companies, including Elbit Systems Ltd., Elfar Ltd. and RB-Tec Ltd. in Israel, and Detektion Security Systems Inc., Herras, Remsdaq, Del-Norte Security, Geoquip Ltd., Southwest Microwave Inc., and Siemens AG outside of Israel, produce high-security detection systems.

There are a number of companies that have developed video motion detection systems, including Geutebruck GmbH, Xtralis, Siemens AG, Ioimage Ltd., ObjectVideo Inc., Nice Systems Ltd. and Bosch.

We believe that our principal competitors for Dreambox systems are Nice Systems Ltd., Verint Systems Inc., Indigo and DVTel Inc.

We believe that our principal competitors for security management and control systems and turnkey project offerings include, among others, Honeywell Inc., Lockheed Martin Corporation, Raytheon Company, Siemens AG, Dornier, Elbit Systems Ltd., Thales, 4D, EADS N.V. and Rafael Advanced Defense Systems Ltd.

We believe that our principal competitor for the Pipeguard system is an Australian company, Future Fibre Technologies Pty. Ltd.

We believe that our principal competitors for personal emergency location systems are Actall Corp. and Visonic Networks.

Some of our competitors and potential competitors have greater research, development, financial and personnel resources, including governmental support, or more extensive business experience than we do. We cannot assure you that we will be able to maintain the quality of our products relative to those of our competitors or continue to develop and market new products effectively.

Intellectual Property Rights

We have approximately 46 patents issued and patent applications pending in the U.S. and in several other countries and have obtained licenses to use proprietary technologies developed by third parties. We cannot assure you:

- that patents will be issued from any pending applications, or that the claims allowed under any patents will be sufficiently broad to protect our technology;

- that any patents issued or licensed to us will not be challenged, invalidated or circumvented; or
- as to the degree or adequacy of protection any patents or patent applications may or will afford.

In addition, we claim proprietary rights in various technologies, know-how, trade secrets and trademarks relating to our principal products and operations. We cannot assure you as to the degree of protection these claims may or will afford. It is our policy to protect our proprietary rights in our products and operations through contractual obligations, including confidentiality and non-disclosure agreements with certain employees and distributors. We cannot assure you as to the degree of protection these contractual measures may or will afford. Although we are not aware that we are infringing upon the intellectual property rights of others, we cannot assure you that an infringement claim will not be asserted against us in the future. We believe that our success is less dependent on the legal protection that our patents and other proprietary rights may or will afford than on the knowledge, ability, experience and technological expertise of our employees. We cannot provide any assurance that we will be able to protect our proprietary technology. The unauthorized use of our proprietary technology by third parties may impair our ability to compete effectively. We could become subject to litigation regarding intellectual property rights, which could seriously harm our business.

We have trademark rights associated with our use of Flash and Intelli-FLEX, and rights obtained by trademark registration for Flare, Perimitrax, Panther, Intelli-FIELD, Senstar, Senstar-Stellar and the Senstar-Stellar logo, Sentrax, Omnitrax, Xfield, DTR, DreamBox and the Magal logo.

In September 2006, we signed a non exclusive agreement with a third party for the right to use certain intangible assets such as know-how and patents for the production, sale and marketing of a perimeter security system based on fiber-optics that is primarily used to protect marine sites. The contract period is two years and we have the right to extend the contract for additional five years. The consideration for the license is approximately $548,000, payable in 24 monthly installments. In addition, we will pay royalties based on a formula as defined in the agreement.

Government Regulation of Certain Exports

Under Israeli law, the export of products that we manufacture in Israel and/or certain know-how is subject to approval by the MOD. We must obtain permits from the MOD to initiate sales proposals with regard to such exports, as well as for actual export transactions. We cannot assure you that we will receive all the required permits for which we may apply in the future.

C. Organizational Structure.

We, or one of our subsidiaries, own 100% of the outstanding capital stock of our subsidiaries in Canada, United States, Germany, the Netherlands, Mexico, United Kingdom, Switzerland, Cyprus, Romania and Poland.

D. Property, Plants and Equipment.

Our principal facility in Israel is a two-story 2,533 square meter facility located on a 4,352 square meter parcel in the Yehud Industrial Zone. Approximately 600 square meters are devoted to administrative, marketing and management functions and approximately 700 square meters are used for engineering, system integration and customer service. We use the remaining 1,233 square meters for production management, production operations, including manufacturing, assembly, testing, warehousing, shipping and receiving. In accordance with Israeli law, this parcel of land is still registered in the name of the Israel Land Authority. We will be entitled to have title to the property recorded in our name when Israeli authorities subdivide the property into parcels. This procedure is a statutory requirement for transferring land ownership in Israel. In 2007, we leased a one-story 810 square meter facility located on a 1,820 square meter parcel in the Yehud Industrial Zone for $80,000 per year for use in production and operations. The products that we manufacture at our facilities in the Yehud Industrial Zone include our taut-wire intrusion detection systems, our vibration detection systems, our video-motion detection systems, MagNet, Fortis, DreamBox, PipeGuard, MTC- 1500, MSS-1500 and other perimeter systems.

We own a 33,000 square foot facility in Carp, Ontario, Canada. Approximately 7,000 square feet are devoted to administrative, marketing and management functions and approximately 8,000 square feet are used for engineering, system integration and customer service. We use the remaining 18,000 square feet for production operations, including cable manufacturing, assembly, testing, warehousing, shipping and receiving. In December 2004, we purchased an additional 182,516 square feet of vacant land adjacent to this property for future expansion. We also lease 358,560 square feet of land near this facility, for $2,500per year for use as an outdoor sensor test and demonstration site for our products. The products manufactured at this facility include the Perimitrax/Panther 2000 and Omnitrex buried cable intrusion detection systems, the Intelli-Field electro static detection system, the X-Field volumetric system the Intelli-FLEX microphonic fence detection system, Flash and Flare, and various perimeter monitoring and control systems.

We own a 20,000 square foot facility in Fremont, California. The products manufactured at this facility include Intelli-Wave, various sensors, the PAS personal alarm system and the MX control and monitoring center.

We lease 2,793 square feet of office space in Herndon, Virginia at a cost of $5,754 per month. The lease commenced on December 1, 2006 and will end on November 30, 2010. We utilize this space, which houses marketing demo rooms, as a sales office for our US subsidiary.

Smart leased 8,000 square feet of commercial space in College Point, New York at a cost of $10,997 per month. The lease will terminate on September 30, 2008.On April 15, 2008, Smart subleased the upper floor of the buildings for $5,000 per month. The sublease will end in September 30, 2008. During the sublease period, we are paying the landlord an additional $1,000 per month in addition to the sublease amount.

We also lease small offices in Germany, the United Kingdom, Mexico, Romania and Poland for our sales and marketing entities.

We believe that our facilities are suitable and adequate for our current operations and the foreseeable future.

ITEM 4A. Unresolved Staff Comments

Not applicable.

ITEM 5. Operating and Financial Review and Prospects

The following discussion of our results of operations and financial condition should be read in conjunction with our consolidated financial statements and the related notes thereto included elsewhere in this annual report. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those set forth in Item 3.D. Key Information Risk Factors.

Overview

We develop, manufacture, market and sell complex computerized security systems. Our systems are used in more than 75 countries to protect aircraft, national borders and sensitive facilities, including military bases, power plant installations, airports, postal facilities, prisons and industrial locations from terrorism, theft and other security threats. Our revenues are principally derived from:

- installation of comprehensive security systems for which revenues are generated from long-term fixed price contracts;

- sales of security products; and
- services and maintenance, which are performed either on a fixed-price basis or as time-and-materials based contracts.

Business Challenges/Areas of Focus

Our primary business challenges and areas of focus include:

- continuing the growth of revenues and profitability of our perimeter security system line of products;
- enhancing the introduction and recognition of our new products into the markets;
- penetrating into new markets and strengthening our presence in existing markets;
- succeeding in selling our comprehensive turnkey solutions; and

Seam -Line Perimeter System

The continued state of hostility between the State of Israel and the Palestinian Authority has caused the State of Israel to increase its efforts to protect its facilities and installations from unauthorized intrusions. In 2002, the Israeli Government announced the construction of a perimeter system to seal off parts of the West Bank to prevent Palestinian terrorists from entering Israel. In September 2002, we won 80% of the bids published by the MOD for the installation of intrusion detection systems along the seam-line between Israel and the West Bank. We received orders having a value of approximately $19 million to install intrusion detection systems along approximately 150 kilometers. As of December 31, 2004, this project was completed. In 2003, the Israeli Government resolved to extend the perimeter system and to continue construction along most of the remaining parts of the seam-line. However, following the UN resolution to refer the question of the legality of the seam-line perimeter systems to the International Court of Justice in Hague, an international opposition to the route selected by the Israeli government arose, causing the Israeli Government to change and shorten the route of the seam-line perimeter system. This opposition, as well as certain decisions of the Israeli Supreme Court, caused a halt in the building of the seam-line fence during 2004. In 2005 the Israeli Government approved a new seam-line fence route and the MOD renewed the work on the southern portion of the seam line. According to recent reports in the Israeli press, the majority of the remaining segments of the fence will be completed during 2008. Although we believe that we will record revenues from the seam line project in 2008, we cannot assure you that Israel will follow through with its decision to build the perimeter system along the seam-line, or if such perimeter system is constructed or rebuilt, that our products will be utilized.

Key Performance Indicators and Sources of Revenues

Our management believes that our revenues, sources of revenues and operating income are among the key performance indicators for our business. Our revenues from our principal lines of business for the three years ended December 31, 2005, 2006 and 2007 were as follows:

	Year Ended December 31,		
	2005	**2006**	**2007**
		(In thousands)	
Perimeter products	$ 40,143	$ 47,186	$ 43,781
Turnkey projects	17,970	16,167	28,167
Other	272	247	427
Total	$ 58,385	$ 63,600	$ 72,375

Our operating income from our principal lines of business for the three years ended December 31, 2005, 2006 and 2007 were as follows:

	Year Ended December 31,		
	2005	2006	2007
		(In thousands)	
Perimeter products	$ 4,334	$ 3,070	$ 2,421
Turnkey projects	(5,290)	935	506
Other	53	(138)	(193)
Eliminations	15	(31)	(28)
Total	$ (888)	$ 3,836	$ 2,706

Cost and Expenses

Cost of revenues. Our cost of revenues for perimeter products consists of component and material costs, direct labor costs, shipping expenses, overhead related to manufacturing and depreciation. Our cost of revenues for turnkey projects consists primarily of component and material costs, subcontractor costs, direct labor costs and overhead related to the turnkey projects. Our cost of revenues for other consists primarily of direct labor costs and material costs relating to our maintenance services.

Our gross margin is affected by the proportion of our revenues generated from perimeter products, turnkey projects and other. Our revenues from perimeter products, generally have higher gross margins than our other segments.

Research and development expenses, net. Research and development expenses, net consists primarily of expenses for on-going research and development activities and other related costs.

Selling and marketing expenses. Selling and marketing expenses consist primarily of commission payments, compensation and related expenses of our sales teams, attendance at trade shows and advertising expenses and related costs for facilities and equipment.

General and administrative expenses. Our general and administrative expenses consist primarily of salary and related costs associated with our executive and administrative functions, legal and accounting expenses, allowances for doubtful accounts and bad debts and other miscellaneous expenses. Staff costs include direct salary costs and related costs such as severance pay, social security and retirement fund contributions, vacation and other pay.

Depreciation and Amortization. The amount of depreciation and amortization attributable to our business segments for the years ended December 31, 2005, 2006 and 2007 are as follows:

	Year Ended December 31,		
	2005	2006	2007
		(In thousands)	
Perimeter products	$ 1,228	$ 1,070	$ 1,087
Turnkey projects	19	133	966
Other	4		2
Total	$ 1,251	$ 1,203	$ 2,055

Financial Expenses, Net. Financial expenses, net include exchange rate differences arising from changes in the value of monetary assets and monetary liabilities stated in currencies other than the functional currency of each entity, interest charged on loans from banks as well as interest income on our cash and cash equivalents and short term investments.

Tax expense. Tax expense consists of federal, state and local taxes on the income of our business. On July 25, 2005, the Knesset, the Israeli parliament, passed the Law for the Amendment of the Income Tax Ordinance (No. 147 and Temporary Order) - 2005, or the 2005 Amendment, which provides for a gradual reduction in the company tax rate in the following manner: in 2007, the tax rate was 29%, in 2008, the tax rate will be 27%, in 2009, the tax rate will be 26% and from 2010 onward the tax rate will be 25%. Furthermore, from 2010, upon reduction of our tax rate to 25%, real capital gains will be subject to tax of 25%.

Discussion of Critical Accounting Policies

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and the use of different assumptions would likely result in materially different results of operations. Critical accounting policies are those that are both most important to the portrayal of our financial position and results of operations, and require management s most difficult, subjective or complex judgments. Although not all of our significant accounting policies require management to make difficult, subjective or complex judgments or estimates, the following policies and estimates are those that we deem most critical:

Revenue Recognition

We generate our revenues mainly from (1) installation of comprehensive security systems for which revenues are generated from long-term fixed price contracts; (2) sales of security products; and (3) services and maintenance, which are performed either on a fixed-price basis or as time-and-materials based contracts.

Revenues from installation of comprehensive security systems are generated from fixed-price contracts according to which the time between the signing of the contract and the final customer acceptance is usually over one year. Such contracts require significant customization for each customer specific needs and, as such, revenues from these types of contracts are recognized using contract accounting on a percentage of completion method. Accounting for long-term contracts using the percentage-of-completion method stipulates that revenue and expense are recognized throughout the life of the contract, even though the project is not completed and the purchaser does not have possession of the project. Percentage of completion is calculated based on the Input Method.

Project costs include materials purchased to produce the system, related labor and overhead expenses and subcontractor s costs. The percentage to completion is measured by monitoring costs and efforts devoted using records of actual costs incurred to date in the project compared to the total estimated project requirement, which corresponds to the costs related to earned revenues. The amounts of revenues recognized are based on the total fees under the agreements and the percentage to completion achieved. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract. Until 2006, we did not experience any material cancellations for any of our projects.

Estimated gross profit or loss from long-term contracts may change due to changes in estimates resulting from differences between actual performance and original forecasts. Such changes in estimated gross profit are recorded in results of operations when they are reasonably determinable by management, on a cumulative catch-up basis.

We believes that the use of the percentage of completion method is appropriate as we has the ability to make reasonably dependable estimates of the extent of progress towards completion, contract revenues and contract costs. In addition, contracts executed include provisions that clearly specify the enforceable rights regarding services to be provided and received by the parties to the contracts, the consideration to be exchanged and the manner and the terms of settlement, including in cases of terminations for convenience. In all cases we expect to perform our contractual obligations and our customers are expected to satisfy their obligations under the contract.

Fees are payable upon completion of agreed upon milestones and subject to customer acceptance. Amounts of revenues recognized in advance of contractual billing, are recorded as unbilled accounts receivable. The period between most instances of advanced recognition of revenues and the customers billing generally ranges between one to six months. At December 31, 2007, we recorded $4.1 million of such unbilled receivables.

We sell security products to customers according to customers orders without installation work. The customers are not entitled to return the products. Revenues from security product sales are recognized when delivery has occurred, persuasive evidence of an agreement exists, the vendor s fee is fixed or determinable, no further obligation exists and collectibility is probable.

Services and maintenance are performed under either fixed-price based or time-and-materials based contracts. Under fixed-price contracts, we agree to perform certain work for a fixed price. Under time-and-materials contracts, we are reimbursed for labor hours at negotiated hourly billing rates and for materials. Related revenues from such service contracts are recognized as those services are performed or over the term of the related agreements provided that, an evidence of an arrangement has been obtained, fees are fixed and determinable and collectibility is reasonably assured.

Deferred revenue includes unearned amounts under installation services, service contracts and maintenance agreements.

Inventories

Inventories are stated at the lower of cost or market value. We periodically evaluate the quantities on hand relative to historical and projected sales volumes, current and historical selling prices and contractual obligations to maintain certain levels of parts. Based on these evaluations, inventory write-offs are provided to cover risks arising from slow-moving items, discontinued products, excess inventories, market prices lower than cost and adjusted revenue forecasts. Cost is determined as follows:

- Raw materials, parts and supplies - using the first-in, first-out method.
- Work-in-progress and finished products - on the basis of direct manufacturing costs with the addition of allocable indirect manufacturing costs.

During 2005, 2006 and 2007, we recorded inventory write-offs from continuing operations in the amounts of $420,000, $760,000 and $646,000, respectively. Such write-offs were included in cost of revenues.

Income taxes

We account for income taxes in accordance with Statement of Financial Accounting Standard No. 109 Accounting for Income Taxes. This statement 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. We provide a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value.

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves estimating our actual current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and we must establish a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. Increases in the valuation allowance result in additional expense to be reflected within the tax provision in the consolidated statement of income. At December 31, 2007, we had a deferred tax asset of $602,000. We have total estimated available carry forward tax losses of $7 million. As of December 31, 2007, we recorded a valuation allowance on carry forward tax losses of $4.4 million due to the uncertainty of their future realization. Our subsidiaries in the United States and the United Kingdom have estimated total available carry-forward tax losses of $5.3 million and $930,000, respectively that may be used as an offset against future taxable profit for 16-20 years and an indefinite period, respectively. As of December 31, 2007, we recorded a full valuation allowance of our subsidiaries tax assets due to the uncertainty of their future realization.

Utilization of U.S. net operating losses may be subject to a substantial annual limitation due to the change in ownership provisions of the Internal Revenue Code of 1986 and similar state provisions. The annual limitation may result in the expiration of net operating losses before utilization.

Goodwill

Goodwill represents the excess of the costs over the net fair value of the assets of the businesses acquired. Goodwill is tested for impairment at least annually or between annual tests in certain circumstances, and written down when impaired, rather than being amortized.

We test goodwill impairment on acquisition and at least annually thereafter or between annual tests in certain circumstances, we write down goodwill when impaired, Goodwill attributable to each of the reporting units is tested for impairment by comparing the fair value of each reporting unit with its carrying value. Fair value is determined using discounted cash flow.

Significant estimates used in these methodologies include estimates of future cash flows, future short-term and long-term growth rates and weighted average cost of capital for each of the reportable units. During 2005, 2006 and 2007, no impairment losses were identified. As of December 31, 2007, our goodwill amounted to $5.6 million of which $4.6 million and $1.0 million relate to our perimeter security systems segment and project segment, respectively.

Impairment of long lived assets

Our Group s long-lived assets and certain identifiable intangibles are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of a group of assets may not be recoverable. Recoverability of a group of assets to be held and used is measured by a comparison of the carrying amount of the group of assets to the future undiscounted cash flows expected to be generated by the group of assets. If such group of assets is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the group of assets exceeds their fair value. During 2005, 2006 and 2007, no impairment losses were identified.

Functional Currency and Financial Statements in U.S. Dollars

We have determined that our reporting currency is the dollar. We determined that as of October 1, 2006 our functional currency changed from the U.S. dollar to NIS. Translation adjustments resulting from translating our financial statements from the NIS to the dollar are reported as a separate component in shareholders equity. As of December 31, 2006 and 2007 our foreign currency translation totaled $297,000 and $2.6 million respectively.

Accordingly, we had accumulated foreign currency translation income of approximately $2.4 million and $5.8 million that was included as part of accumulated other comprehensive income within our balance sheets at December 31, 2006 and 2007, respectively. During 2005, 2006 and 2007, foreign currency translation adjustments, net of $87,000, ($72,000) and $3.5 million, respectively, were included under accumulated other comprehensive income. Had we determined that the functional currency of our subsidiaries (not including our U.S. subsidiaries) was the U.S. dollar, these gains would have increased our income for each of the years presented.

The first step in the translation process is to identify the functional currency for each entity included in the financial statements. The accounts of each entity are then re-measured in its functional currency. All transaction gains and losses from the re-measurement of monetary balance sheet items are reflected in the statement of operations as financial income or expenses, as appropriate.

After the re-measurement process is complete the financial statements are translated into the reporting currency, which is the dollar, using the current rate method. Equity accounts are translated using historical exchange rates. All other balance sheet accounts are translated using the exchange rates in effect at the balance sheet date. Statement of operations amounts have been translated using the average exchange rate for the year. The resulting translation adjustments are reported as a component of shareholders equity in accumulated other comprehensive income (loss).

Concentrations of credit risk

Financial instruments that are potentially subject to concentrations of credit risk consist principally of cash and cash equivalents, short and long-term bank deposits, marketable securities, unbilled accounts receivable, trade receivables, long-term trade receivables and long-term loans.

Of our cash and cash equivalents, marketable securities and short-term and long-term bank deposits at December 31, 2007, $19.9 million is invested in major Israeli and U.S. banks, approximately $16.3 million is invested in other banks, mainly with Deutsche Bank, RBC Royal Bank, Leutkircher Bank, Commerzbank and Natwest Bank. Cash and cash equivalents invested in the United States may be in excess of insured limits and are not insured in other jurisdictions. We believe that the financial institutions that hold our investments are financially sound and, accordingly, minimal credit risk exists with respect to these investments. Our marketable securities include investments in U.S. government debentures, foreign banks shares, mutual funds and money market funds. Our management believes that those securities are financially sound and that the portfolios are well-diversified, and accordingly, moderate credit risk exists with respect to these marketable securities. Moreover, our investment policy, limits the amount we may invest. During the recent turmoil in capital markets, we have tightened our control and monitoring over our marketable securities portfolio.

The short term and long term trade receivables and the unbilled accounts receivable of our company and our subsidiaries are derived from sales to large and solid organizations located mainly in Israel, the United States, Canada, Mexico and Europe. We perform ongoing credit evaluations of our customers and to date have not experienced any material losses. An allowance for doubtful accounts is determined with respect to those amounts that we have determined to be doubtful of collection and in accordance with an aging policy. In certain circumstances, we may require letters of credit, other collateral or additional guarantees. During the years ended December 31, 2005, 2006 and 2007, we recorded ($54,000), $138,000 and ($68,000) of expenses (income) related to doubtful accounts, respectively. As of December 31, 2007, the allowance for doubtful accounts amounted to $343,000. The loan granted to a third party is secured by a personal guarantee of the beneficial owner. We believe that the loan is well secured, and accordingly, minimal credit risk exists with respect to this loan.

We have no significant off-balance sheet concentration of credit risks, such as foreign exchange contracts or foreign hedging arrangements, except derivative instruments, which are detailed below.

Derivative instruments

We recognize our derivative instruments as either assets or liabilities in our statement of financial position at fair value. The accounting for changes in the fair value (i.e., gains or losses) 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.

To protect against the change in the forecasted foreign currency cash flows of certain sale arrangements resulting from changes in the exchange rate during 2003, 2005 and 2006, we entered into forward contracts, to hedge portions of our forecasted revenue and unbilled accounts receivable denominated in Euros and Polish Zlotys. We have designated the forward instruments as cash flow hedges for accounting purposes.

For derivative instruments designated as cash flow hedges (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 and reclassified into earnings in the same line item associated with the forecasted transaction in the same period or periods during which the hedged transaction affects earnings.

In 2005 a sales arrangement in Polish Zlotys that was to take place from 2005 to 2007 was canceled. Accordingly, changes in the fair value of the forward contracts were recorded as financial expenses in the years ended December 31, 2005, 2006 and 2007.

On October 1, 2006, we changed our functional currency from the dollar to NIS. From the date of change in functional currency, the hedge of the revenues in Euros is no longer effective. Changes in the fair value of the forward contracts from October 1, 2006 were charged to financial expenses. We recorded $110,000, $915,000 and $666,000 as financial expenses related to forward contracts transactions, in 2005, 2006 and 2007, respectively.

Fair value of financial instruments

The following methods and assumptions were used by us and our subsidiaries in estimating the fair value of our financial instruments:

- the carrying amounts of cash and cash equivalents, marketable securities, short-term bank deposits, trade receivables, unbilled accounts receivable, short-term bank credit and trade payables approximate their fair value due to the short-term maturity of such instruments.
- the carrying amount of our long-term trade receivables and long-term bank deposits approximate their fair value. The fair value was estimated using discounted cash flows analyses, based on our investment rates for similar types of investment arrangements.
- the carrying amounts of our long-term bank debt are estimated by discounting the future cash flows using current interest rates for loans of similar terms and maturities. As of December 31, 2006, the fair value of our long-term borrowings was approximately $8.2 million, compared to the carrying amount of approximately $8.2 million. As of December 31, 2007, the fair value of our long-term borrowings was approximately $7.5 million, compared to the carrying amount of $7.4 million.

A. *Operating Results.*

Due to the nature of our customers and products, our revenues are often generated from a relatively small number of large orders. Consequently, individual orders from individual customers can represent a substantial portion of our revenues in any one period and significant orders by any customer during one period may not be followed by further orders from the same customer in subsequent periods. Our revenues and operating results may, therefore, vary substantially from period to period. Consequently, we do not believe that our revenues and operating results should necessarily be judged on a quarter-to-quarter comparative basis.

The following table presents, for the periods indicated, certain financial data expressed as a percentage of revenues:

	Year Ended December 31,				
	2003	**2004**	**2005**	**2006**	**2007**
Revenues	100%	100%	100%	100%	100%
Cost of revenues	55	52	63	59	60
Gross profit	45	48	37	41	40
Operating expenses:					
Research and development, net	8	8	9	8	8
Selling and marketing, net	18	21	21	18	18
General and administrative	8	8	9	9	9
Special post employment benefit Award granted by principal shareholders		2			1
Operating income (loss)	11	9	(2)	6	4
Financial expenses, net	(2)	(1)	(1)	(1)	(3)
Income (loss) before income taxes	9	8	(3)	5	1
Income taxes (tax benefit)	2	3		2	1

Income (loss) from continuing operations	7	5	(3)	3	0
Income (loss) from discontinued operations, net	(3)	(3)	(2)	(2)	3
Net income (loss)	4%	2%	(5)%	1%	3%

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Years ended December 31, 2006 and 2007

Revenues. Revenues increased by 13.8% from $63.6 million in the year ended December 31, 2006 to $72.4 million in the year ended December 31, 2007. Revenues from sales of perimeter systems decreased from $47.2 million in 2006 to $43.8 million in 2007, a decrease of 7.2% mainly as a result in decrease in orders from the Israeli MOD, which was partly offset by orders from clients outside of Israel.Revenues from security turnkey projects increased by 74.2% from $16.2 million in 2006 to $28.2 million in 2007, primarily due to a $5.7 million project performed for the Israeli government and the acquisition of a European integration company. Other revenues, mainly from services for screening pallets and newly developed products, increased by 72.9% from $247,000 in the year ended December 31, 2006 to $427,000 in the year ended December 31, 2007.

Based on our backlog of approximately $64.9 million as of May 30, 2008, our revenues in the first quarter of 2008 and our assessment of the market, we anticipate that our revenues will increase in 2008 compared to our revenues in 2007.

Cost of revenues. Cost of revenues increased from $37.2 million in the year ended December 31, 2006 to $43.5 million in the year ended December 31, 2007. Cost of revenues as a percentage of revenues increased from 58.5% in 2006 to 60.1% in 2007, primarily as a result of the increase in the turnkey projects segment of our business which has a lower profit margin. In addition, we recorded a loss provision for one of the projects performed for the Israeli government. In our perimeter segment, our cost of sales was adversely affected by an increase in production costs. We anticipate that our cost of revenues as a percentage of revenues will remain at the same level in 2008 as in 2007.

Gross profit. Gross profit increased from $26.4 million in the year ended December 31, 2006 to $28.9 million for the year ended December 31, 2007, primarily as a result of the **increase in revenues.**

Research and development expenses, net. Research and development expenses, net increased from $5.4million for the year ended December 31, 2006, to $5.8 million for the year ended December 31, 2007, an increase of 7.2%. Research and development expenses, net amounted to 8.5% of revenues in 2006, compared to 8.0% in 2007. Investment tax credits with respect to our Canadian subsidiary totaled $162,000 in 2006 and $160,000 in 2007. We expect that our net research and development expenditures as a percentage of revenues will remain at the same level in 2008 as in 2007.

Selling and marketing expenses, net. Selling and marketing expenses, increased from $11.6 million for the year ended December 31, 2006 to $12.9 million for the year ended December 31, 2007, an increase of 11.4%. The increase in selling and marketing expenses in 2007 was primarily due to the amortization of customer related assets attributable to the acquisition of the European integration company. Selling and marketing expenses amounted to 18.2% and 17.9% of revenues in each of 2006 and 2007, respectively. We expect that our selling and marketing expenses as a percentage of revenues will remain at the same level in 2008 as in 2007.

General and administrative expenses. General and administrative expenses increased from $5.5 million for the year ended December 31, 2006 to $6.6 million for the year ended December 31, 2007, an increase of 18.3%. The increase in general and administrative expenses was due to expenses associated with our compliance with the requirements of the Sarbanes-Oxley Act, increase in salaries and legal expenses. General and administrative expenses amounted to 8.7% of revenues in 2006 compared to 9.1% in 2007.We expect that our general and administrative expenses will remain at the same level in 2008 as in 2007.

Special post employment benefit. In the year ended December 31, 2007 we recorded a special post employment expense of $904,000, 1.2% of our total revenues, related to benefits payable to our retired chairman.

Operating income (loss). Our operating income declined from $3.8 million for the year ended December 31, 2006 to $2.7 million for the year ended December 31, 2007. The operating income of our three business segments for the years ended December 31, 2006 and 2007 are as follows:

	Year Ended December 31,	
	2006	2007
	(In thousands)	
Perimeter products	$ 3,070	$ 2,421
Turnkey projects	935	506
Other	(138)	(193)
Eliminations	(31)	(28)
Total	$ 3,836	$ 2,706

The operating income of our perimeter products segment decreased from $3.1 million in the year ended December 31, 2006 to $2.4 million in the year ended December 31, 2007, primarily as a result of the increase in production costs and the devaluation of the U.S. dollar against the NIS and the Canadian dollar. The operating results for our turnkey projects segment declined from an operating income of $935,000 in the year ended December 31, 2006 to operating income of $506,000 in the year ended December 31, 2007, primarily as a result of a loss incurred in one of our major projects and the amortization of the customer related assets attributable to the acquisition of the European integration company. The operating loss from our other operations increased from $138,000 in the year ended December 31, 2006 to $193,000 in the year ended December 31, 2007.

Financial expenses, net. Financial expenses, net increased from $864,000 for the year ended December 31, 2006 to $2.1 million for the year ended December 31, 2007, an increase of 147.3%. Our financial expenses increased by $1.3 million, mainly due to the devaluation of the U.S. dollar against the NIS and the Canadian dollar, which caused an increase of foreign exchange losses, net of $1.1 million. In addition, interest on short term bank credits increased by $648,000 due to the higher level of short term loans incurred in 2007, which was offset in part by a decease in forward contracts loss of $249,000.

Income taxes. We recorded an income tax expenses of $943,000 for the year ended December 31, 2006 compared to a $373,000 for the year ended December 31, 2007, primarily as a result of the decrease in our income before taxes. The effective tax rate increased to 65.6% for 2007 compared to 31.7% in 2006 due to the fact that we recorded a valuation allowance on losses of $765,000, due to the low likelihood that our deferred tax assets will be recovered from future taxable income.

Years ended December 31, 2005 and 2006

Revenues. Revenues increased by 8.9% from $58.4 million in the year ended December 31, 2005 to $63.6 million in the year ended December 31, 2006. Revenues from sales of perimeter systems increased from $40.1 million in 2005 to $47.2million in 2006, an increase of 17.5%, mainly due to a $10.1 million order from the Israeli MOD to protect the Northern border of Israel, which was partly offset by a $2.2 million decrease in orders from the Israeli MOD to protect the seam-line.Revenues from security turnkey projects decreased by 10% from $18.0 million in 2005 to $16.2 million in 2006, primarily due to a $4.7 million decrease in revenues from a project in Romania that for which we provided less services in 2006 and a $3.3 million decrease in revenues from projects in Canada. These declines were offset by a $5.0 million increase in revenues from projects in Mexico and by a $1.2 million increase in revenues from an Eastern European customer. Other revenues, primarily from the maintenance of pallet screening machines decreased by 9.2% from $272,000 in the year ended December 31, 2005 to $247,000 in the year ended December 31, 2006.

Cost of revenues. Cost of revenues increased from $36.7 million in the year ended December 31, 2005 to $37.2 million in the year ended December 31, 2006. Cost of revenues as a percentage of revenues declined from 62.8% in 2005 to 58.5% in 2006 primarily as a result of the expenses we incurred in 2005 in connection with a project in Eastern Europe that was cancelled. Due to the uncertainty in preventing the forfeiture of a performance bank guarantee, we included a provision of $1.4 million in respect of this guarantee in our financial statements for the year ended December 31, 2005. On April 28, 2006, we commenced arbitration proceedings against the customer and on July 11, 2006, the customer made a demand for the payment of the full amount of a $1.4 million performance. Under the terms of a settlement reached in the District Court in Haifa, we paid the customer approximately $700,000 of the disputed amount and the balance will be paid only if we are found liable for damages exceeding the amount previously paid by us. Based on the opinion of our legal counsel, we believe that it is probable that the ongoing arbitration in this matter will result in a favorable decision for us, resulting in the dismissal of all claims raised by the customer. In view of the above and due to the uncertainty of our preventing the forfeiture of the bank performance guarantee, we included a $1.4 million provision in respect of this guarantee in our financial statements for the year ended December 31, 2005. Based on the settlement, we cancelled the balance of the provision made in our financial statements in 2006.

Gross profit. Gross profit increased from $21.7 million in the year ended December 31, 2005 to $26.4 million for the year ended December 31, 2006, primarily as a result of the expenses we incurred in 2005 in connection with the cancellation of the project in Eastern Europe.

Research and development expenses, net. Research and development expenses, net for the year ended December 31, 2006 increased to $5.4 million from $5.3million for the year ended December 31, 2005, an increase of 2.1%, Research and development expenses, net amounted to 9.0% of revenues in 2005, compared to 8.5% in 2006. Investment tax credits with respect to our Canadian subsidiary totaled $154,000 in 2005 and $162,000 in 2006.

Selling and marketing expenses, net. Selling and marketing expenses, decreased from $12.4 million for the year ended December 31, 2005 to $11.6 million for the year ended December 31, 2006, a decrease of 6.3%. The decrease in selling and marketing expenses in 2006 was primarily due to a decrease in commissions paid in connection with our turnkey projects. Selling and marketing expenses amounted to 21.2% and 18.2% of revenues in 2005 and 2006, respectively.

General and administrative expenses. General and administrative expenses increased from $5.0 million for the year ended December 31, 2005 to $5.5 million for the year ended December 31, 2006, an increase of 11.7%. The increase in general and administrative expenses was due to a $138,000 increase in expenses related to doubtful accounts and due to expenses associated with our compliance with the requirements of the Sarbanes-Oxley Act. General and administrative expenses amounted to 8.5% of revenues in 2005 compared to 8.7 % in 2006.

Operating income (loss). Our operating results improved from an operating loss of $888,000 for the year ended December 31, 2005 to operating income of $3.8 million for the year ended December 31, 2006. The operating income (loss) of our business segments for the years ended December 31, 2005 and 2006 are as follows:

	Year Ended December 31,	
	2005	**2006**
	(In thousands)	
Perimeter products	$ 4,334	$ 3,070
Projects	(5,290)	935
Other	53	(138)
Eliminations	15	(31)
Total	$ (888)	$ 3,836

The operating income of our perimeter products segment declined from $4.3 million in the year ended December 31, 2005 to $3.1 million in the year ended December 31, 2006, principally as a result of a change in the product mix of perimeter products sold. The operating results for our projects segment rebounded from an operating loss of $5.3 million in the year ended December 31, 2005 to operating income of $935,000 in the year ended December 31, 2006, primarily as a result of the impact of expenses we incurred in 2005 in connection with the cancellation of an Eastern European project. The operating results of our other segment went from operating income of $53,000 in the year ended December 31, 2005 to an operating loss of $138,000 in the year ended December 31, 2006, primarily as a result of the decrease in revenues in 2006 and the higher cost of revenues, primarily materials.

Financial expenses, net. Financial expenses, net increased from $813,000 for the year ended December 31, 2005 to $864,000 for the year ended December 31, 2006, an increase of 6.3%. Our financial expenses increased by $963,000 mainly due to a forward contract loss, which was offset by a $912,000 increase in financial income, mainly due to increased interest income and foreign exchange gains. We determined that as of October 1, 2006 our functional currency changed from the U.S. dollar to NIS. The U.S. dollar remains our reporting currency. This change resulted in our incurring additional financial expenses in the fourth quarter of 2006.

Income taxes (tax benefit). We recorded a tax benefit of $28,000 for the year ended December 31, 2005, primarily as a result of the loss incurred in 2005, compared to income tax expenses of $943,000 for the year ended December 31, 2006.

Quarterly Results of Operations

The following tables set forth certain unaudited quarterly financial information for the two years ended December 31, 2007 The data has been prepared on a basis consistent with our audited consolidated financial statements included elsewhere in this annual report and include all necessary adjustments, consisting only of normal recurring adjustments that we consider necessary for a fair presentation. The operating results for any quarter are not necessarily indicative of results for any future periods.

	Three months ended							
	2006				2007			
	Mar. 31,	Jun. 30,	Sept. 30,	Dec. 31,	Mar. 31,	Jun. 30,	Sept. 30,	Dec. 31,
	(In thousands)							
Consolidated Statement of Income Data:								
Revenues	$ 12,712	$ 13,965	$ 15,288	$ 21,635	$ 14,113	$ 14,091	$ 21,016	$ 23,155
Cost of revenues	7,064	7,931	8,593	13,648	7,732	7,650	13,291	14,837
Gross profit	5,648	6,034	6,695	7,987	6,381	6,441	7,725	8,318
Operating expenses:								
Research and development, net	1,200	1,450	1,152	1,576	1,454	1,148	1,283	1,879
Selling and marketing, net	2,383	2,608	2,751	3,861	2,709	3,028	3,794	3,399
General and administrative	1,147	1,253	1,474	1,673	1,316	1,407	1,505	2,333
Special post employment benefit							960	(56)
Total operating expenses	4,730	5,311	5,377	7,110	5,479	5,583	7,542	7,555
Operating income (loss)	918	723	1,318	877	902	858	183	763
Financial expenses, net	(157)	(229)	(262)	(216)	(303)	(141)	(983)	(710)
Income (loss) before income taxes	761	494	1,056	661	599	717	(800)	53
Income taxes (tax benefit)	153	118	345	327	148	280	749	(804)

Income (loss) from continuing operations	608	376	711	334	451	437	(1,549)	857
Loss from discontinued operations, net	(459)	(107)	(88)	(565)	(153)	(95)	(88)	2,022
Net income (loss)	149	269	623	(231)	298	342	(1,637)	2,879

	Three months ended							
	2006				2007			
	Mar. 31,	Jun. 30,	Sept. 30,	Dec. 31,	Mar. 31,	Jun. 30,	Sept. 30,	Dec. 31,
	(As a percentage of total revenues)							
Consolidated Statement of Income Data, expressed as a percentage of revenues:								
Revenues	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Cost of revenues	55.6	56.8	56.2	63.1	54.8	54.3	63.2	64.1
Gross profit	44.4	43.2	43.8	36.9	45.2	45.7	36.8	35.9
Operating expenses:								
Research and development, net	9.4	10.4	7.5	7.3	10.3	8.1	6.1	8.1
Selling and marketing, net	18.7	18.7	18.0	17.9	19.2	21.5	18.0	14.7
General and administrative	9.0	9.0	9.7	7.7	9.3	10.0	7.2	10.0
Special post employment benefit							4.6	(0.2)
Total operating expenses	37.1	38.1	35.2	32.9	38.8	39.6	35.9	32.6
Operating income (loss)	7.3	5.1	8.6	4.0	6.4	6.1	0.9	3.3
Financial expenses, net	(1.2)	(1.6)	(1.7)	(1.0)	2.2	1	4.7	3.1
Income (loss) before income taxes	6.1	3.5	6.9	3.0	4.2	5.1	(3.8)	0.2
Income taxes (tax benefit)	1.2	0.8	2.3	1.5	1	2	3.6	(3.5)
Income (loss) from continuing operations	4.9	2.7	4.6	1.5	3.2	3.1	(7.4)	3.7
Loss from discontinued operations, net	(3.6)	(0.8)	(0.5)	(2.6)	(1.1)	(0.7)	(0.4)	8.7
Net income (loss)	1.3%	1.9%	4.1%	(1.1)%	2.1%	2.4%	(7.8)%	12.4%

Seasonality

Our operating results are characterized by a seasonal pattern, with a higher volume of revenues towards the end of the year and lower revenues in the first part of the year. This pattern, which is expected to continue, is mainly due to two factors:

- our customers are mainly budget-oriented organizations with lengthy decision processes which tend to mature late in the year; and
- due to weather and other conditions, payments are often postponed from the first quarter to subsequent quarters.

See also Item 3.D. Key Information Risk Factors. Our revenues are dependent on government procurement procedures and practices, and because we receive large product orders from a relatively small number of customers, our revenues and operating results are subject to substantial periodic variations.

Impact of Inflation and Devaluation on Results of Operations, Liabilities and Assets

Exchange rate fluctuations between the NIS and the dollar, particularly larger periodic devaluations, may have an impact on our profitability and period-to-period comparison of our results. In 2005, the rate of devaluation of the NIS against the dollar was 6.8%, while in 2003, 2004, 2006 and 2007 the NIS appreciated in value in relation to the dollar by 7.6%, 1.6%, 8.2% and 9% respectively. A portion of our expenses, primarily labor expenses, is incurred in NIS and a part of our revenues are quoted in NIS. Additionally, certain assets, as well as a portion of our liabilities, are denominated in NIS. Our results may be adversely affected by the devaluation of the NIS in relation to the dollar (or if such devaluation is on lagging basis), if our revenues in NIS are higher than our expenses in NIS and/or the amount of our assets in NIS are higher than our liabilities in NIS. Alternatively, our results may be adversely affected by an appreciation of the NIS in relation to the dollar (or if such appreciation is on a lagging basis), if the amount of our expenses in NIS are higher than the amount of our revenues in NIS and/or the amount of our liabilities in NIS are higher than our assets in NIS.

The following table presents information about the rate of devaluation of the NIS against the dollar:

Year ended December 31,	Israeli inflation rate %	NIS devaluation rate %	Israeli inflation adjusted for devaluation %
2003	(1.9)	(7.6)	5.7
2004	1.2	(1.6)	2.8
2005	2.4	6.8	(4.4)
2006	(0.1)	(8.2)	8.1
2007	3.4	(9.0)	12.4

Because exchange rates between the NIS and the dollar fluctuate continuously, exchange rate fluctuations, particularly larger periodic devaluations, may have an impact on our profitability and period-to-period comparisons of our results. We are also subject to exchange rate fluctuations related to our activities in Canada. During the year ended December 31, 2005, foreign currency fluctuations had an adverse impact on our results of operations, and our foreign exchange losses, net were $145,000. During the year ended December 31, 2006, our foreign exchange gains, net were $276,000. During the year ended December 31, 2007, our foreign exchange losses, net were $792,000. We cannot assure you that in the future our results of operations may not be materially adversely affected by currency fluctuations.

To protect against the change in the forecasted foreign currency cash flows of certain sale arrangements resulting from changes in the exchange rate, during 2003, 2005 and 2006 we entered into forward contracts in order to hedge portions of our forecasted revenue and unbilled accounts receivable denominated in Euros and Polish Zlotys. We have designated the forward instruments as cash flow hedges for accounting purposes.

For derivative instruments designated as cash flow hedges (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 and reclassified into earnings in the same line item associated with the forecasted transaction in the same period or periods during which the hedged transaction affects earning.

In 2005 a sales arrangement in Polish Zlotys that was to take place from 2005 to 2007 was canceled. Accordingly, changes in the fair value of the forward contracts were recorded as financial expenses in the years ended December 31, 2005, 2006 and 2007.

On October 1, 2006, we changed our functional currency from the dollar to NIS. From the date of change in functional currency, the hedge of the revenues in Euros is no longer effective. Changes in the fair value of the forward contracts from October 1, 2006 were charged to financial expenses.

We recorded $110,000, $915,000 and $666,000 in financial expenses related to forward contracts transactions in 2005, 2006 and 2007, respectively.

Effective Corporate Tax Rate

Israeli companies are generally subject to income tax on their worldwide taxable income. The applicable rate for 2007 was 29%, which was reduced to 27% in 2008, and will be further reduced to 26% in 2009 and 25% in 2010 and thereafter. However, certain of our manufacturing facilities have been granted approved enterprise status under the Law for the Encouragement of Capital Investments, 1959, as amended, commonly referred to as the Investment Law, and, consequently, are eligible, subject to compliance with specified requirements, for tax benefits beginning when such facilities first generate taxable income. The tax benefits under the Investment Law are not available with respect to income derived from products manufactured outside of Israel. We have derived, and expect to continue to derive, a substantial portion of our income from our approved enterprise facilities. Subject to certain restrictions, we are entitled to a tax exemption in respect of income derived from our approved facilities for a period of two years, commencing in the first year in which such income is earned, and will be entitled to a reduced tax rate of 10% to 25% for an additional five to eight years if we qualify as a foreign investors company. If we do not qualify as a foreign investors company, we will instead be entitled to a reduced rate of 25% for an additional five years, rather than eight years. A foreign investors company is defined in the Investment Law as a company in which more than 25% of its shareholders are non-Israeli residents. Pursuant to the Investment Law, a foreign investors company may enjoy benefits for a period of up to ten years, (the actual length of the benefits period is graduated based on the percentage of foreign ownership).

Our effective corporate tax rate may substantially exceed the Israeli tax rate. Our U.S. subsidiaries will generally be subject to applicable federal, state, local and foreign taxation, and we may also be subject to taxation in the other foreign jurisdictions in which 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, which will apply to us.

As of December 31, 2007, we had a deferred tax asset of $602,000. We have total estimated available carry forward tax losses of $7 million. As of December 31, 2007, we recorded a valuation allowance on carry forward tax losses of $4.4 million due to the uncertainty of their future realization.

As of December 31, 2007, our subsidiaries in the United States and the United Kingdom had estimated total available carry forward tax losses of $5.3 million and $0.9 million, respectively, to offset against future taxable income for 16 to 20 years and an indefinite period, respectively. A full valuation allowance was recorded due to the uncertainty of the tax assets future realization. Utilization of U.S. net operating losses may be subject to a substantial annual limitation due to the change in ownership provisions of the Internal Revenue Code of 1986 and similar state tax law provisions. The annual limitation may result in the expiration of net operating losses before utilization.

On December 2007 we entered into a tax assessment agreement with the Israeli Tax Authority, with respect to the years 2001 to 2004. According to the agreement we paid $402,000. Since one of our approved enterprises has not receive final approval as of yet, the tax assessment agreement determined that if we will not get such approval within two years we will pay an additional amount of $467,000 to the tax authority.

Recently Issued Accounting Standards

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS 157) which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 applies to other accounting pronouncements that require or permit fair value measurements and, accordingly, does not require any new fair value measurements. SFAS 157 is effective for fiscal years beginning after November 15, 2007 for financial assets and liabilities, as well as for any other assets and liabilities that are carried at fair value on a recurring basis, and should be applied prospectively. The adoption of the provisions of SFAS 157 related to financial assets and liabilities and other assets and liabilities that are carried at fair value on a recurring basis is not anticipated to materially impact our consolidated financial position and results of operations. Subsequently, the FASB provided for a one-year deferral of the provisions of SFAS 157 for non-financial assets and liabilities that are recognized or disclosed at fair value in the consolidated financial statements on a non-recurring basis. We are currently evaluating the impact of adopting the provisions of SFAS 157 for non-financial assets and liabilities that are recognized or disclosed on a non-recurring basis.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). Under this Standard, we may elect to report financial instruments and certain other items at fair value on a contract-by-contract basis with changes in value reported in earnings. This election is irrevocable. SFAS 159 provides an opportunity to mitigate volatility in reported earnings that is caused by measuring hedged assets and liabilities that were previously required to use a different accounting method than the related hedging contracts when the complex provisions of SFAS 133 hedge accounting are not met. SFAS 159 is effective for years beginning after November 15, 2007. As we did not elect the fair value option in the date of adoption, we do not expect the adoption of SFAS 159 will have a material impact on our consolidated financial.

In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (Revised 2007) (SFAS 141R), Business Combinations. SFAS 141R will change the accounting for business combinations. Under SFAS 141R, an acquiring entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. SFAS 141R will change the accounting treatment and disclosure for certain specific items in a business combination. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. SFAS 141R will have an impact on our accounting for future business combinations once adopted and not on prior acquisitions.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements (SFAS 160). SFAS 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent s ownership interest and the valuation of retained noncontrolling equity investments when a subsidiary is deconsolidated. SFAS 160 also establishes reporting requirements that provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the noncontrolling owners. This standard is effective for fiscal years beginning after December 15, 2008and should be applied prospectively. However, the presentation and disclosure requirements of the statement shall be applied retrospectively for all periods presented. The adoption of the provisions of Statement No. 160 is not anticipated to materially impact our consolidated financial position and results of operations.

In December 2007, the SEC staff issued Staff Accounting Bulletin (SAB) 110, Share-Based Payment, which amends SAB 107, Share-Based Payment, to permit public companies, under certain circumstances, to use the simplified method in SAB 107 for employee option grants after December 31, 2007. Use of the simplified method after December 2007 is permitted only for companies whose historical data about their employees exercise behavior does not provide a reasonable basis for estimating the expected term of the options. Based on the significant restrictions on employee trading during the restatement periods, we have not experienced regular employee exercise behavior since the implementation of SFAS No. 123R on January 20, 2006. We do not expects to continue to use the simplified method as allowed under SAB 110.

B. Liquidity and Capital Resources

General

Our ongoing liquidity requirements arise primarily from our need to service debt and provide working capital. From our inception until our initial public offering in March 1993, we financed our activities mainly through cash flow from operations and bank loans. In March 1993, we received proceeds of $9.8 million from an initial public offering of 1,380,000 ordinary shares. In February 1997, we raised $9.4 million from a follow-on offering of 2,085,000 ordinary shares and in April 2005, we raised an additional $14.9 million from a follow-on offering of 1,700,000 ordinary shares. The proceeds from these offerings together with cash flow from operations and our credit facilities are our main sources of working capital.

Our working capital increased from $39.9 million at December 31, 2006 to $41.5 million at December 31, 2007. Cash and cash equivalents amounted to $4.9 million at December 31, 2006 compared to $9.2 million at December 31, 2007. Short-term and long-term bank deposits, marketable securities and escrow deposits amounted to $22.1 million at December 31, 2006 compared to $26.9million at December 31, 2007. Our cash and cash equivalents, short and long-term bank deposits and marketable securities are held mainly in U.S. dollars and Euros.

We expect to fund our short-term liquidity needs, including our obligations under our credit facilities, other contractual agreements and any other working capital requirements, from cash and cash equivalents, operating cash flow and our credit facilities. We believe that our current cash and cash equivalents, including bank deposits, marketable securities and our expected cash flow from operations in 2008 will be sufficient to meet our cash requirements through 2008.

Cash Flows

The following table summarizes our cash flows for the periods presented:

	Year ended December 31,		
	2005	2006	2007
		(in thousands)	
Net cash provided by (used in) continuing operations	$ (2,915)	$ (2,019)	10,420
Net cash provided by (used in) discontinued operations	(1,224)	643	(519)
Net cash provided by (used in) operating activities	(4,139)	(1,376)	9,901
Net cash provided by (used in) investing activities	(15,248)	(5,248)	(464)
Net cash provided by financing activities	17,269	1,688	(5,477)
Effect of exchange rate changes on cash and cash equivalents	253	(255)	337
Increase (decrease) in cash and cash equivalents	(1,865)	(5,191)	4,297
Cash and cash equivalents at the beginning of the year	11,964	10,099	4,908
Cash and cash equivalents at the end of the year	$ 10,099	$ 4,908	$ 9,205

Net cash used in operating activities was approximately $4.1 million and $1.4 million in the years ended December 31, 2005 and 2006, respectively, compared to $9.9 million in the year ended December 31, 2007.

Net cash used in operating activities in the year ended December 31, 2005, was primarily attributable to a net loss of $3.2 million, an increase in trade receivables of $8.7 million an increase in deferred income taxes of $1 million, an increase in unbilled accounts receivable of $2.8 million and an increase in other accounts receivable and prepaid expenses of $580,000 which was offset in part by an increase in customer advances of $4.0 million for turnkey projects, a $3.2 million increase in trade payables, an increase in other accounts payable and accrued expenses of $2 million, depreciation and amortization of $1.3 million and a $1.7 million decrease in inventories for our perimeter security systems segment.

Net cash used in operating activities in the year ended December 31, 2006, was primarily attributable to an increase in trade receivables of $4.4 million, an increase in inventories of $2.7 million, a return of $2.8 million of customer advances and a decrease in trade payables of $666,000, which was offset in part by net income of $810,000, depreciation and amortization of $1.2 million, a decrease in unbilled accounts receivable of $3.5 million, an increase in other accounts payable and accrued expenses of $717,000 and a $437,000 decrease in other accounts receivable and prepaid expenses.

Net cash provided by operating activities in the year ended December 31, 2007, was primarily attributable to an increase in customer advances of $10.4 million, an increase of $4.3 million and $1.8 million in trade receivables and unbilled accounts receivable, respectively, an increase of $1.8 million in accrued interest on marketable securities and short and long term bank deposits and depreciation and amortization of $2.1 million, which was offset in part by decrease in trade payables of $6.3 million, a decrease in other accounts payable and accrued expenses of $1.8 million, an increase in long term trade receivable of $1.8 million and a gain from discontinued operation of $1.7 million.

Net cash used in investing activities was approximately $15.2 million and $5.2 million for the years ended December 31, 2005 and 2006, respectively, compared to $464,000 in the year ended December 31, 2007. In the year ended December 31, 2005,we purchased $16.7 million of short-term deposits and $750,000 of property and equipment, which purchases were offset by proceeds of $3.0 million from the redemption of structured notes and $1.2 million from the sale of long-term deposits. In the year ended December 31, 2006, we purchased $906,000 of property and equipment, $8.2 million of marketable securities, invested $622,000 in a long term loan and purchased know how and patents for $148,000 with the proceeds from the sale of marketable securities of $5.2 million. In the year ended December 31, 2007 we acquired a European integration company for $4 million and purchased $10.8 million of marketable securities, $4.4 million of escrow deposit and $890,000 of property and equipment purchases which were offset by proceeds of $8.5 million from the sale of the assets and business of a subsidiary, proceeds of $5.6 million from the sale of marketable securities and $5.7 million from the sale of short term bank deposits.

In the year ended December 31, 2005, net cash provided by financing activities of $17.3 million was primarily attributable to the receipt of net proceeds of $14.9 million from the issuance of ordinary shares, $2.4 million from short-term bank credit to finance the operations of our video monitoring segment and $1.8 million from proceeds of long-term loans that we used to refinance the loan we incurred to finance the purchase of a building in Fremont CA, which was offset in part by the repayment of $1.8 million of long-term bank loans. In the year ended December 31, 2006, net cash provided by financing activities of $1.7 million was primarily attributable to $3.2 million from proceeds of long-term loans that we incurred to finance the costs incurred in connection with the cancellation of a project in Eastern Europe and our receipt of $163,000 from the exercise of employee stock options, which was offset in part by $1.4 million from short-term bank credits to finance the operations of our video monitoring segment and the repayment of $306,000 of long-term bank loans. In the year ended December 31, 2007, net cash used in financing activities of $5.5 million was primarily due to the repayment of $4.7 million of short term bank credits and repayment of $796,000 of long term bank loans which was offset in part by receipt of $43,000 from the exercise of employee stock options.

We had capital expenditures of approximately $750,000, $906,000 and $890,000 in 2005, 2006 and 2007, respectively. These capital expenditures were principally for computers, other machinery and equipment and for expanding our facilities. We estimate that our capital expenditures for 2008 will total approximately $1.6 million, substantially all of which will relate to our perimeter security and project segments. We expect to finance these expenditures primarily from our cash and cash equivalents, operating cash flow and our credit facilities. However, the actual amount of our capital expenditures will depend on a variety of factors, including general economic conditions, changes in the demand for our products.

Credit Lines and Other Debt

We currently have credit lines with Bank Leumi Le-Israel B.M., or BLL, Union Bank of Israel Ltd., or Union Bank, Mizrahi Tefahot Bank B.M., or MTB, and Bank Hapoalim B.M. totaling $54.4 million in the aggregate. There are no restrictions as to our use of any of these credit lines. We agreed not to pledge any of our assets without the consent of these banks. In addition, in connection with two of these credit lines, a fixed charge was placed on our physical plant in Israel by each of BLL and Union Bank, each of which ranks pari-passu with the other.

As of December 31, 2007 we are not under any obligation to maintain financial ratios or other terms in respect of our credit lines. Our loans under these credit lines are denominated in dollars and NIS.

In addition, our subsidiaries currently have credit lines with Bank Leumi USA, Royal Bank of Canada and Deutsche Bank, totaling $9.2 million in the aggregate.

Our Canadian subsidiary, which is primarily engaged in sale of perimeter products and turnkey projects, has undertaken to maintain general covenants and the following financial ratios and terms in respect of its outstanding credit lines:

- A quick ratio of not less than 1.25;
- A ratio of total liabilities to tangible net worth of not greater than 0.75; and
- Tangible net worth of at least $9.0 million.

As of December 31, 2007, our Canadian subsidiary was in compliance with these ratios and terms.

As of December 31, 2007, we had approximately $26 million available under our credit lines. In addition, our subsidiaries had approximately $2.8 million available under their credit lines.

As of December 31, 2007, our outstanding balances under our credit lines consisted of:

- Short-term NIS-denominated loans of approximately $8.2 million, bearing an average interest at a rate of 5.58%;
- Short-term dollar-denominated loans of approximately $8.1 million, bearing an average interest at a rate of 5.82%;
- Long-term dollar-denominated loans of approximately $2.4 million, bearing an average interest at a rate of 5.50%; and
- Several bank performance and advance payment guarantees totaling approximately $9.8 million, at an annual cost of 0.5%-1.0%.

As of December 31, 2007, our subsidiaries had an aggregate of $145,000 in short term bank credit and $5 million in long-term loans primarily relating to our perimeter security segment as follows:

- $2.5 million, bearing interest at a fixed annual rate of 6.06%. This loan is due in July 2008;
- $500,000, bearing interest at an annual rate of 6.19% and collateralized by the assets of our US subsidiary, Magal Senstar Inc., or MSI. This loan is due in July 2008;
- $500,000, bearing interest at an annual rate of 5.8% and collateralized by MSI s assets. This loan is due in July 2008;
- $518,000 bearing interest at a fixed rate of 5.45%. The loan is payable in 20 quarterly installments of $47,200, commencing February 2006. We have guaranteed the full amount of this loan; and
- $980,000, bearing interest at a fixed rate of 5.45%. The loan is due in one installment in November 2010. We have guaranteed the full amount of this loan.

In connection with the related loans listed immediately above, Bank Leumi USA placed a $3 million fixed charge on our deposits with that bank.

The two $500,000 promissory notes issued to Bank Leumi USA both contain covenants that require us to maintain $1 million in deposits at all times, otherwise the interest rate on the notes become the bank s rate plus 0.25% until the minimum deposit is maintained.

C. Research and Development, Patents and Licenses.

Government Grants

We participate in programs sponsored by the Israeli Government for the support of research and development activities. In the year ended December 31, 2005, we obtained $8,000, of royalty-bearing grants from the OCS for certain of our research and development projects for perimeter security products. We did not obtain any grants form the OCS for the years ended December 31, 2006 and 2007. We are obligated to pay royalties to the OCS amounting to 3%-4.5% of revenues derived from sales of the products funded with these grants, up to 100% of the grants received, linked to the U.S. dollar. All grants received after January 1, 1999 will also bear interest at the rate of LIBOR. The obligation to pay these royalties is contingent on actual sales of the products, and in the absence of such sales no payment is required.

Royalties paid to the OCS amounted to $83,000, $79,000 and $143,000 in the years ended December 31, 2005, 2006 and 2007, respectively. These royalties related to sales of perimeter security products and management security system.

As of December 31, 2007, we had a contingent obligation to pay royalties of approximately $1.5, million to the OCS upon the successful sale of perimeter security products developed using research and development programs sponsored by the OCS.

The Israeli Government, through the Fund for the Encouragement of Marketing Activities, or the Fund, awarded us grants for overseas marketing expenses. We are obligated to pay royalties to this fund at the rate of 3% of the increase in export sales, up to the amount of the grants we received. To date, we have received $253,000 in grants from the Fund and, during the years ended December 31, 2005, 2006 and 2007, we did not pay any royalties. As of December 31, 2007, we had a remaining contingent obligation to the Fund of $82,000.

Investment Tax Credit

Our Canadian and U.S subsidiaries are eligible for investment tax credits on their research and development activities and on certain current and capital expenditures. During the years ended December 31, 2005, 2006 and 2007, our Canadian subsidiary recognized $154,000, $162,000 and $160,000, respectively, of investment tax credits as a reduction of research and development expenses. In addition, our Canadian and U.S subsidiaries have available investment tax credits of approximately $738,000to reduce future federal income taxes payable. These credits will expire in 2014 through 2027. See also Item 4.B. Information on the Company Business Overview Research and Development; Royalties.

D. Trend Information.

We cannot assure you that the MOD, IDF or any of our other major customers will maintain their volume of business with us or that, if such volume is reduced, other customers of similar volume will replace the lost business. The loss of one or more of these existing customers without replacement by a customer or customers of similar volume would have a material adverse effect on our financial results.

For additional discussion of the information required by this item see Operating and Financial Review and Prospects Operating Results and Operating and Financial Review and Prospects Liquidity and Financial Resources above.

E. Off-Balance Sheet Arrangements.

At December 31, 2007, we have guaranteed the advance payments and the performance of our work to certain of our customers (usually government entities). Such guarantees are required by contract for our performance during the installation and operational period of projects throughout Israel and the rest of the world. The guarantees for installation typically expire soon after certain milestones are met and guarantees for operations typically expire proportionally over the contract period. The maximum potential amount of future payments we could be required to make under our guarantees at December 31, 2007 and March 31, 2008 were $9.8 million and $8.9 million, respectively. We have not recorded any liability for such amounts, as we expect that our performance will be acceptable and to date, no performance bank guarantees have been exercised against us except with respect to our dispute relating to the project in Eastern Europe. See Item 8.A - Consolidated Statements and Other Financial Information-Legal Proceedings.

F. Tabular Disclosure of Contractual Obligations.

The following table summarizes our minimum contractual obligations and commercial commitments as of December 31, 2007 and the effect we expect them to have on our liquidity and cash flow in future periods.

Contractual Obligations	Payments due by Period (in thousands)				
	Total	less than 1 year	1-2 years	3-5 years	more than 5 years
Long-term bank debt obligations	$ 7,398	$ 4,303	$ 813	$ 1,802	$ 480
Operating lease obligations	1,619	693	562	301	63
Purchase obligations	184	184			
Other long-term liabilities reflected on our balance sheet under U.S. GAAP	3,873			3,873	
Total	$ 13,074	$ 5,180	$ 1,375	$ 5,976	$ 543

ITEM 6. Directors, Senior Management and Employees

A. Directors and Senior Management.

Set forth below are the name, age, principal position and a biographical description of each of our directors and executive officers:

Name	Age	Position
Jacob Perry	64	Chairman of the Board
Izhar Dekel	56	President, Chief Executive Officer and Director
Lian Goldstein	33	Vice President Finance, Chief Financial Officer and Secretary
Yehezkel Farber	67	Vice President Operations
Zvi Dank	58	Vice President Research and Development
Asaf Even-Ezra	42	Executive Vice President Sales & Marketing
Dany Pizen	56	Vice President East European and CIS Marketing
Raffi Netzer	45	Vice President Africa and Latin America Marketing
Yehonatan Ben- Hamozeg	49	Vice President Integrated Systems Development
Jacob Even-Ezra	77	Director
Nathan Kirsh	76	Director
Zeev Livne	63	Director
Jacob Nuss	60	Director
Shaul Kobrinsky	56	Outside Director
Anat Winner	49	Outside Director

Messrs. Perry, Even-Ezra, Dekel, Kirsh, Nuss, and Livne will serve as directors until our 2008 Annual General Meeting of Shareholders. Mr. Kobrinsky and Mrs. Winner will serve as outside directors pursuant to the provisions of the Israeli Companies Law for three-year terms until our 2010 annual general meeting of shareholders.

Jacob Even-Ezra and Asaf Even-Ezra are father and son. Izhar Dekel is Jacob Even-Ezra s son-in-law and Asaf Even-Ezra s brother-in-law. Other than these relationships, there are no other family relationships among our directors and senior executives.

Jacob Perry has served as chairman of our board since January 2008, as deputy chairman of the board since 2006, and as a director since December 2002,. From 1995 to December 2002, Mr. Perry was President and CEO of Cellcom Israel Ltd., Israel s largest cellular phone operator. Mr. Perry served 29 years with the Israeli General Security Service, and served as its chief from 1988 until 1995. Mr. Perry has also served as a coordinator to the Israeli Prime Minister on the subject of prisoners of war and missing persons. He was a board member of El-Al Israel Airlines and a member of the management of many public organizations. Mr. Perry is also a chairman of the board of directors of various companies, including Mizrahi Tefahot Bank, Pinpoint Advanced Corp., Inc., a blank check company traded in the U.S. and Keren Mor, a real estate fund. Mr. Perry serves as a director of Tamarind Technologies and New Kopel Israel s largest vehicle and car service group. Mr. Perry holds an A.M.P. from Harvard Business School and a B.A. in Oriental Studies and History of the Jewish People from Tel-Aviv University.

Izhar Dekel has served as our chief executive officer since 2006, as our president since 1990, and as a director since 1993. Mr. Dekel served as our finance manager from 1984 to 1990. Mr. Dekel holds an M.B.A. and a B.A. in Economics and International Relations from the Hebrew University of Jerusalem.

Lian Goldstein has served as our chief financial officer and secretary since January 2008. Before joining us, from 2002 to 2007, Ms. Goldstein served as chief financial officer of Johnson & Johnson Medical Israel Ltd. Prior to that, from 1999 to 2002, Ms. Goldstein served as a senior audit manager with Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global. Ms. Goldstein holds an M.B.A. and a B.A. in Accounting and Business from the Israel College of Management, and has been a Certified Public Accountant (Israel) since 2000.

Yehezkel Farber has served as our vice president - operations since 1986. Mr. Farber previously served as the manager of the customer systems department of IAI.

Zvi Dank has served as our vice president - research and development since 1984. Before joining us, Mr. Dank worked as an electronic engineer in the electronics division of IAI. Mr. Dank holds a B.Sc. in Electrical Engineering from the Israel Institute of Technology, or the Technion.

Asaf Even-Ezra has served as our executive vice-president for sales and marketing since July 2007. Mr. Even-Ezra joined us in 1995 and served as our vice president - Israel and West European marketing since 1998. Mr. Even-Ezra also heads our video motion detection division and is in charge of Israel and West European marketing. Mr. Even-Ezra holds an M.B.A. and a B.A. in Business from the New York Institute of Technology.

Dany Pizen has served as our vice president - East European and CIS marketing since 1995. Before joining us, Mr. Pizen served as vice president of business development of Eldor Electronics Ltd., before which he served for 20 years in the IDF and retired as a Lieutenant Colonel. Mr. Pizen holds a B.A. in Social Science from Bar Ilan University.

Rafi Nezer has served as our vice president - Africa and Latin America marketing since 2004. Before joining us and since 1999, Mr. Nezer acted as director of marketing for Rada Electronic Industries Ltd. Mr. Nezer holds an M.B.A. in Business Administration from INSEAD and an L.L.B. from the Tel Aviv University.

Yehonatan Ben- Hamozeg has served as our vice president Integrated Systems Development since 2002. Before joining us, Mr. Ben Hamozeg served in the IDF for 24 years and retired as a Colonel. Mr. Ben Hamozeg holds an M.B.A. in Business Management and a B.A. in Economics and Statistics from Haifa University.

Jacob Even-Ezra has served as a director since 1984. From 1984 until December 2007, Mr. Even-Ezra served as the chairman of our board. From 1984 until 2006, he also served as our chief executive officer, and from 1987 until 1990 he served as our president as well. He is currently a member of the Executive Council and the Management Committee of Tel-Aviv University. From 1985 to 1988, Mr. Even-Ezra was also chairman of the Israel Export Institute. Mr. Even-Ezra holds a B.Sc. in Electrical Engineering from the Technion.

Nathan Kirsh has served as a director since 1984. Mr. Kirsh is an independent investor. Mr. Kirsh serves as one of the trustees of the Eurona Foundation, the beneficial owner of 100% of the ordinary shares of our company that are held by Mira Mag Inc. Mr. Kirsh holds a B.S. in Commerce from the University of Witwatersrand, Johannesburg.

Zeev Livne has served as a director since July 2004. Mr. Livne has served as the chairman of Livne Strategic Consultants LTD.since 2001.Mr. Livne served 39 years with the IDF until 2001. During his long military career with the IDF, Mr. Livne served as the Defense Attaché to the U.S. and Canada from 1997 to 2001, Military Secretary to the Prime Minister of Israel from 1996 to 1997 and Ground Force Commander from 1994 to 1996. From 1992 to 1994 Mr. Livne established the IDF Home Front Command and served as its first Commander. Mr. Livne serves on the board of directors of PAZKAR, a private Israeli company. Mr. Livne holds a B.A. in History from the Tel Aviv University, and an M.A. in Geography from the University of Haifa.

Jacob Nuss has served as a director since 1993. Mr. Nuss currently serves as the vice president - internal auditing of IAI, and served as IAI s deputy vice president - internal auditing from 1999 to 2003. From 1993 to 1999, Mr. Nuss served as the director of finance of IAI s electronics group. From 1991 to 1993, Mr. Nuss served as assistant to the chairman of the board of IAI. Mr. Nuss has served in various financial management capacities at IAI since 1975. Mr. Nuss holds an M.B.A. in Business from the Tel Aviv University and a B.A. in Economics and Business Management from Bar Ilan University. Mr. Nuss holds a certificate in internal auditing.

Shaul Kobrinsky has served as an outside director since July 2004. Mr. Kobrinsky has served as the President and Chief Executive Officer of Urdan Industries Ltd., an investment and holding company since 1997. Since 2003, Mr. Kobrinsky has served as senior managing director of Alagem Capital Group a Beverly Hills based investment group. From 1989 to 1997, Mr. Kobrinsky served as chief executive officer of Cargal Ltd., an Israeli company that manufactures corrugates. Previously, and since 1984, Mr. Kobrinsky served as deputy managing director of Clal Industries Ltd., a holding and investment company. Mr. Kobrinsky serves as an outside director and a member of the audit committee of Scope Metal Trading Ltd. Mr.Kobrinsky holds a B.A. in Economics from Tel Aviv University. Mr. Kobrinsky is a member of the anti-trust court of the State of Israel.

Anat Winner has served as an outside director since July 2004. Mrs. Winner has been a business advisor since 2003. Mrs. Winner served from October 2001 to May 2003 as Chief Executive Officer and Chief Financial Officer of Israel News Ltd. From 1999 to October 2001, Mrs. Winner served as Chief Financial Officer of DBS Satellite Services (1998) Ltd. (YES), an Israeli company that is engaged in setting up and operating DBS television systems. From 1998 to 2000 Mrs. Winner served as an outside Director and chairman of the audit committee of Memsar Ltd. Previously, from 1995 to 1998, Mrs. Winner served as chief financial officer of Eurocom Cellular Communications Ltd., an Israeli company that is engaged in importing and marketing cellular phones. From 1989 to 1995, Mrs. Winner served in various finance positions, including Chief Financial Officer of the Seed company (1939) Ltd. From 1984 to 1989 Mrs. Winner served as a senior audit manager with Ronel Stetner & Co., Certified Public Accountants in Israel. Mrs. Winner also serves as a director of Internet Gold-Golden Lines Ltd and 012 Smile.Communications Ltd. Mrs. Winner holds a B.A. degree in Accounting and Economics from Haifa University and has been a Certified Public Accountant (Israel) since 1987.

Ofer Katz, our vice president - aviation security, retired in April 2008.

B. Compensation.

During the fiscal year ended December 31, 2007, we paid aggregate compensation to all of our executive officers and directors as a group (consisting then of 16 persons) of approximately $1.8 million. In addition, we have provided automobiles to our executive officers at our expense. We have two key-man life insurance policies for Izhar Dekel and are the beneficiary of one of these policies and certain of Mr. Dekel s family members are the beneficiaries of the other policy. We bear the cost of both of these insurance policies.

During the year ended December 31, 2007 and until March 6, 2008, our outside directors and our independent directors (directors who are not employees of our company or officers or employees of any entity that beneficially owns 5% or more of our ordinary shares), received an annual fee of $5,600 and an additional fee of $300 for each board or committee meeting that they attend. Effective as of March 6, 2008 our audit committee and board of directors approved an increase of the annual fees payable to our outside and independent directors, to NIS 59,100 (approximately $17,382) and an additional fee of NIS 2,000 (approximately $588) for each board or committee meeting that they attend. The outside directors compensation was approved without shareholder approval in accordance with the Companies Regulations (Rules for Compensation and Expenses of Outside Director) 5760-2000, promulgated under the Israeli Companies Law. The independent directors compensation was approved without shareholder approval in accordance with the Companies Regulations (Relief from Related Party Transactions) 5760-2000, promulgated under the Israeli Companies Law. In the event that within 14 days from the date of the disclosure of the resolution of the audit committee and the board of directors to increase the independent directors compensation, shareholders holding at least 1% of our voting rights will so request, this resolution will be subject to the approval of the general meeting of the shareholders of our company.

We follow Israeli law and practice, instead of the NASDAQ Marketplace requirements, regarding the compensation of our chief executive office and other executive officers. Under the Israeli Companies Law, arrangements as to compensation of office holders who are not directors require approval by the board of directors, provided that they are not deemed extraordinary transactions. Any compensation arrangement with an office holder who is not a director that is deemed an extraordinary transaction, the exemption of such office holder from liability, the insurance of such office holder and the indemnification of such office holder, or an undertaking to indemnify such office holder, require both board of directors and audit committee approval. The compensation, exemption, indemnification and insurance of office holders who are directors must be approved by our audit committee, board of directors and shareholders, unless an exemption applies. If the office holder is a controlling shareholder or a relative of a controlling shareholder, any extraordinary transaction, compensation, exemption, indemnification and insurance of the office holder must be approved by our audit committee, board of directors and shareholders, supported by the vote of at least one-third of the shares of the non-controlling shareholders voting on the matter, or provided that the total number of shares held by non-controlling shareholders that voted against the proposal did not exceed one percent of all of the voting rights in the company. See below in this Item 6.C.   Directors, Senior Management and Employees - Board Practices - NASDAQ Exemptions for Foreign Private Issuers.

As of December 31, 2007, our directors and executive officers as a group, consisting of 16 persons, held options to purchase an aggregate of 256,800 ordinary shares, having exercise prices ranging from $7.66 to $13.00. Generally, the options vest over a two years period. The options will expire between 2009 to 2012 or earlier upon termination of employment as an executive officer or service as a director of our company. All of such options were granted under our 2003 Stock Option Plan. See this Item 6E.   Directors, Senior Management and Employees - Share Ownership - Stock Option Plans.

We entered into a retirement agreement with Mr. Jacob Even-Ezra who retired from his position as the chairman of our Board of Directors as of on January 1, 2008, based on the terms that were approved by our shareholders in August 2007. Pursuant to the retirement agreement, Mr. Even- Ezra has undertaken not to compete with our company for a period of three years following his retirement. In consideration we agreed to pay Mr. Even-Ezra $360,000. In addition, and as gratitude for his long and outstanding efforts in furthering our business and interests, we agreed to provide him with certain benefits and services, the value thereof are presently estimated to be $50,000 per year, for the rest of his life. As of December 31, 2007, the actuarial value of these perquisites is estimated by approximately $544,000.

We entered into an employment agreement with Izhar Dekel, effective January 1993. This agreement contain certain non-competition and confidentiality provisions. In addition, this agreement establishes a base salary and a package of benefits with an aggregate value of approximately 20% of the base salary, as well as a car and a possible bonus. In December 2000, our board of directors extended the term of Mr. Dekel s employment until such time as it is terminated by us or by Mr. Dekel pursuant to the terms of the agreement. Under the Israeli Companies Law, the terms of employment of Mr. Dekel, who is also a member of our board of directors requires shareholders approval. Our shareholders approved Mr. Dekel s terms in July 2004 and August 2007.

Mr. Jacob Perry served as deputy chairman of our board of directors since September 6, 2006. Our audit committee, board of directors and shareholders approved the payment to Mr. Perry, in addition to the directors fees, of an additional compensation for his services as deputy chairman, in the amount of NIS 25,000 per month (approximately $7,500), payable as of the date of his appointment as deputy chairman. Since January 1, 2008, Mr. Perry has served as the chairman of our board of directors. Our audit committee and board of directors approved, subject to our shareholder approval, to enter into an agreement with Mr. Perry pursuant to which Mr. Perry will be entitled to receive a monthly payment of NIS 50,000, (approximately $15,000), customary social benefits and an annual bonus based on our performance. In addition Mr. Perry will be entitled to receive, subject to our shareholders approval, options to purchase 300,000 ordinary shares of our company. Such options will vest over four year period.

C. Board Practices

Introduction

According to the Israeli Companies Law and our Articles of Association, the management of our business is vested in our board of directors. The board of directors may exercise all powers and may take all actions that are not specifically granted to our shareholders. Our executive officers are responsible for our day-to-day management. The executive officers have individual responsibilities established by our chief executive officer and board of directors. Executive officers are appointed by and serve at the discretion of the board of directors, subject to any applicable agreements.

Election of Directors

Our articles of association provide for a board of directors of not less than three and not more than eleven members as may be determined from time to time at our annual general meeting. Our board of directors is currently composed of eight directors.

Our directors (except the outside directors as detailed below), are elected by our shareholders at our annual general meeting and hold office until the next annual general meeting. All the members of our board of directors (except the outside directors as detailed below), may be reelected upon completion of their term of office. Our annual general meetings are held at least once every calendar year, but not more than fifteen months after the last preceding annual general meeting. In the intervals between our annual general meetings, the board of directors may appoint new directors to fill vacancies. All of our current directors, including the outside directors, were elected by our shareholders at our annual general meeting of shareholders of August 2007. Our outside directors will hold office until our 2010 annual general meeting of shareholders.

Under the Israeli Companies Law, our board of directors is required to determine the minimum number of directors who must have accounting and financial expertise, as such term is defined in regulations promulgated under the Israeli Companies Law. Our board of directors has determined that our board of directors will include at least one director who has accounting and financial expertise, within the meaning of the regulations promulgated under the Israeli Companies Law. Our board of directors has further determined that Ms. Anat Winner has the requisite accounting and financial expertise.

We do not follow the requirements of the NASDAQ Marketplace Rules with regard to the nomination process of directors, and instead, we follow Israeli law and practice, in accordance with which our directors are recommended by our board of directors for election by our shareholders. See below in this Item 6.C. Directors, Senior Management and Employees - Board Practices - NASDAQ Exemptions for Foreign Private Issuers.

Outside and Independent Directors

Outside Directors. The Israeli Companies Law requires Israeli companies with shares that have been offered to the public in or outside of Israel to appoint at least two outside directors. Outside directors must be Israeli residents who are qualified to be appointed as directors, unless the company s shares have been offered to the public outside of Israel or have been listed on a stock exchange outside of Israel. The Israeli Companies Law provides that a person may not be appointed as an outside director if the person, or the person s relative, partner, employer or an entity under that person s control, has or had during the two years preceding the date of appointment any affiliation with the company, or any entity controlling, controlled by or under common control with the company. The term relative means a spouse, sibling, parent, grandparent, child or child of spouse or spouse of any of the above. The term affiliation includes an employment relationship, a business or professional relationship maintained on a regular basis, control and service as an office holder, excluding service as an outside director of a company that is offering its shares to the public for the first time.

In addition, no person may serve as an outside director if the person s position or other activities create, or may create, a conflict of interest with the person s responsibilities as director or may otherwise interfere with the person s ability to serve as director. If, at the time an outside director is appointed, all current members of the board of directors are of the same gender, then that outside director must be of the other gender. A director of one company may not be appointed as an outside director of another company if a director of the other company is acting as an outside director of the first company at such time.

At least one of the elected outside directors must have accounting and financial expertise and any other outside director must have accounting and financial expertise or professional qualification, as such terms are defined by regulations promulgated under the Israeli Companies Law. However, Israeli companies listed on certain stock exchanges outside Israel, including The NASDAQ Global Market, are not required to appoint an outside director with accounting and financial expertise if a director with accounting and financial expertise who qualifies as an independent director for purposes of audit committee membership under the laws of the foreign country in which the stock exchange is located serves on its board of directors. All of the outside directors of such a company must have professional qualification.

The outside directors are elected by shareholders at a general meeting. The shareholders voting in favor of their election must include at least one-third of the shares of the non-controlling shareholders of the company who voted on the matter. This minority approval requirement need not be met if the total shareholdings of those non-controlling shareholders who vote against their election represent 1% or less of all of the voting rights in the company.

In general, outside directors serve for a three-year term and may be reelected to one additional three-year term. However, Israeli companies listed on certain stock exchanges outside Israel, including The NASDAQ Global Market, may appoint an outside director for additional terms of not more than three years 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 outside director for an additional term is in the best interest of the company. Outside directors can be removed from office only by the same special percentage of shareholders that can elect them, or by a court, and then only if the outside directors cease to meet the statutory qualifications with respect to their appointment or if they violate their duty of loyalty to the company.

Any committee of the board of directors that is authorized to exercise powers vested in the board of directors must include at least one outside director and the audit committee must include all the outside directors. All outside directors are members of the audit committee of our company. An outside director is entitled to compensation as provided in regulations adopted under the Israeli Companies Law and is otherwise prohibited from receiving any other compensation, directly or indirectly, in connection with such service.

Independent Directors. In general, NASDAQ Marketplace Rules require that the board of directors of a NASDAQ-listed company have a majority of independent directors 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 Securities and Exchange Commission. However, foreign private issuers, such as our company, may follow certain home country corporate governance practices instead of certain requirements of the NASDAQ Marketplace Rules. On June 27, 2006, we provided NASDAQ with a notice of non-compliance with respect to the requirement to maintain a majority of independent directors, as defined under NASDAQ Marketplace Rules. Instead, we follow Israeli law and practice which requires that we appoint at least two outside directors, within the meaning of the Israeli Companies Law, to our board of directors. (See below in this Item 6C. Directors, Senior Management and Employees - Board Practices - NASDAQ Marketplace Rules and Home Country Practices.) In addition, in accordance with the rules of the Securities and Exchange Commission and NASDAQ, we have the mandated three independent directors, as defined by the rules of the Securities and Exchange Commission and NASDAQ, on our audit committee.

Our board of directors has determined that Ms. Winner and Mr. Kobrinsky qualify both as independent directors under the requirements of the Securities and Exchange Commission and NASDAQ and as outside directors under the requirements of the Israeli Companies Law. Our board of directors has further determined that Messrs. Nuss and Livne qualify as independent directors under the requirements of the Securities and Exchange Commission and NASDAQ.

Audit Committee

Our audit committee, which was established in accordance with Section 114 of the Israeli Companies Law and Section 3(a)(58)(A) of the Securities Exchange Act of 1934, assists our board of directors in overseeing the accounting and financial reporting processes of our company and audits of our financial statements, including the integrity of our financial statements, compliance with legal and regulatory requirements, our independent public accountants qualifications and independence, the performance of our internal audit function and independent public accountants, finding any defects in the business management of our company for which purpose the audit committee may consult with our independent auditors and internal auditor, proposing to the board of directors ways to correct such defects, and such other duties as may be directed by our board of directors.

The responsibilities of the audit committee also include approving related-party transactions as required by law. Under Israeli law an audit committee may not approve an action or a transaction with a controlling shareholder, or with an office holder, unless at the time of approval two outside directors are serving as members of the audit committee and at least one of the outside directors was present at the meeting in which an approval was granted.

Our audit committee consists of three board members who satisfy the respective independence requirements of the Securities and Exchange Commission, NASDAQ and Israeli Law for audit committee members. Our audit committee is currently composed of Ms. Anat Winner and Messrs. Shaul Kobrinsky and Jacob Nuss. Our board of directors has determined that Ms. Winner has financial expertise within the meaning of the Israeli Companies Law. The audit committee meets at least once each quarter. Our audit committee charter is available on our website at www.magal-ssl.com.

Our Board has appointed an investment committee composed of Mr. Jacob Even-Ezra, Mr. Kobrinsky, and Ms. Winner, and authorized it to receive resolutions in connection with the investment of our cash, including hedging transactions.

Internal Auditor

Under the Israeli Companies Law, the board of directors of a public company must appoint an internal auditor nominated by the audit committee. The role of the internal auditor is to examine whether the company s actions comply with the law, integrity and orderly business procedure. Under the Israeli Companies Law, the internal auditor may not be an interested party, an office holder, or an affiliate, or a relative of an interested party, office holder or affiliate, nor may the internal auditor be the company s independent accountant or its representative. Mr. Daniel Spira, CPA (Isr.) is our internal auditor.

Directors Service Contracts

We have entered into employment agreements with Mr. Izhar Dekel, our president and chief executive officer and Mr. Jacob Perry, the chairman of our board of directors. In addition we have entered into a retirement agreement with Mr. Jacob Even- Ezra regarding his retirement from his position of the chairman of our board of directors. See Item 6B. Directors, Senior Management and Employees - Compensation.

Other than as described in Item 6B, there are no arrangements or understandings between us and any of our subsidiaries, on the one hand, and any of our directors, on the other hand, providing for benefits upon termination of their employment or service as directors of our company or any of our subsidiaries.

Approval of Related Party Transactions Under Israeli Law

The Israeli Companies Law regulates the approval procedures for transactions of a company with its controlling shareholders or transactions in which an office holders or the controlling shareholders or their relative have personal interest. For this purpose, a controlling shareholder is defined as a shareholder that holds either solely or with others at least 25% of the issued share capital of the company unless another shareholder holds more than 50% of the issued share capital. The holdings of two or more shareholders, each having personal interest in the approval of the same transaction will be aggregated for this purpose.

Fiduciary Duties of Office Holders

The Israeli Companies Law codifies the fiduciary duties that office holders, including directors and executive officers, owe to a company. An office holder is defined in the Israeli Companies Law as a director, general manager, chief business manager, deputy general manager, vice general manager, other manager directly subordinate to the general manager or any other person assuming the responsibilities of any of the foregoing positions without regard to such person s title. 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 at a level of care that a reasonable office holder in the same position would employ under the same circumstances. This includes the duty to utilize reasonable means to obtain (i) information regarding the appropriateness of a given action brought for his approval or performed by him by virtue of his position and (ii) all other information of importance pertaining to the foregoing actions. The duty of loyalty includes (i) avoiding any conflict of interest between the office holder s position in the company and any other position he holds or his personal affairs, (ii) avoiding any competition with the company s business, (iii) avoiding exploiting any business opportunity of the company in order to receive personal gain for the office holder or others, and (iv) disclosing to the company any information or documents relating to the company s affairs that the office holder has received due to his position as an office holder.

Disclosure of Personal Interests of an Office Holder

The Israeli Companies Law requires that an office holder promptly, and no later than the first board meeting at which such transaction is considered, disclose any personal interest that he or she may have and all related material information known to him or her and any documents in their position, in connection with any existing or proposed transaction by us. In addition, if the transaction is an extraordinary transaction, that is, a transaction other than in the ordinary course of business, other than on market terms, or likely to have a material impact on the company s profitability, assets or liabilities, the office holder must also disclose any personal interest held by the office holder s spouse, siblings, parents, grandparents, descendants, spouse s descendants and the spouses of any of the foregoing, or by any corporation in which the office holder or a relative is a 5% or greater shareholder, director or general manager or in which he or she has the right to appoint at least one director or the general manager.

Approval of Transactions with Office Holders

Under the Israeli Companies Law, all arrangements as to compensation of office holders who are not directors require approval by the board of directors, and exculpation, insurance and indemnification of, or an undertaking to, indemnify an office holder who is not a director requires both board of directors and audit committee approval. The compensation of office holders who are directors must be approved by our audit committee, board of directors and shareholders.

Some transactions, actions and arrangements involving an office holder (or a third party in which an office holder has an interest) must be approved by the board of directors or as otherwise provided for in a company s articles of association, however, a transaction that is adverse to the company s interest may not be approved. In some cases, such a transaction must be approved by the audit committee and by the board of directors itself, and under certain circumstances shareholder approval may be required. A director who has a personal interest in a transaction that is considered at a meeting of the board of directors or the audit committee may not be present during the board of directors or audit committee discussions and may not vote on the transaction, unless the transaction is not an extraordinary transaction or the majority of the members of the board or the audit committee have a personal interest, as the case may be. In the event the majority of the members of the board of directors or the audit committee have a personal interest, then the approval of the general meeting of shareholders is also required.

Disclosure of Personal Interests of a Controlling Shareholder; Approval of Transactions with Controlling Shareholders

The disclosure requirements which apply to an office holder also apply to a controlling shareholder with respect to his or her personal interest in any existing or proposed transaction by us. The Israeli Companies Law provides that an extraordinary transaction with a controlling shareholder or an extraordinary transaction with another person in whom the controlling shareholder has a personal interest or a transaction with a controlling shareholder or his relative regarding terms of service and employment, must be approved by the audit committee, the board of directors and shareholders. The shareholder approval for such a transaction must include at least one-third of the shareholders who have no personal interest in the transaction who voted on the matter (not including abstentions). The transaction can be approved by shareholders without this one-third approval if the total shareholdings of those shareholders who have no personal interest and voted against the transaction do not represent more than one percent of the voting rights in the company.

Under the Companies Regulations (Relief from Related Party Transactions), 5760-2000, promulgated under the Israeli Companies Law, as amended, certain extraordinary transactions between a public company and its controlling shareholder(s) do not require shareholder approval. In addition, under such regulations, directors compensation and employment arrangements in a public company do not require the approval of the shareholders if both the audit committee and the board of directors agree that such arrangements are solely for the benefit of the company. Also, employment and compensation arrangements for an office holder that is a controlling shareholder of a public company do not require shareholder approval if certain criteria are met. The foregoing exemptions from shareholder approval will not apply if one or more shareholders holding at least 1% of the issued and outstanding share capital of the company or of the company s voting rights, objects to the use of these exemptions provided that such objection is submitted to the company in writing not later than fourteen days from the date of the filing of a report regarding the adoption of such resolution by the company pursuant to the requirements of the Israeli Securities Law, 5328-1968. If such objection is duly and timely submitted, then the transaction or compensation arrangement of the directors will require shareholders approval as detailed above.

In addition, a private placement of securities that will (i) cause a person to become a controlling shareholder, as defined above, or (ii) increase the relative holdings of a shareholder that holds 5% or more of the company s outstanding share capital, or (iii) will cause any person to become, as a result of the issuance, a holder of more than 5% of the company s outstanding share capital in a private placement in which 20% or more of the company s outstanding share capital prior to the placement are offered, the payment for which (in whole or in part) is not in cash or not under market terms, requires approval by the board of directors and the shareholders of the company.

The Israeli Companies Law provides that an acquisition of shares in a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 25% or greater shareholder of the company. This rule does not apply if there is already another 25% or greater shareholder of the company. Similarly, the Israeli Companies Law provides that an acquisition of shares in a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would hold greater than a 45% interest in the company, unless there is another shareholder holding more than a 45% interest in the company. These requirements do not apply if, in general, (i) the acquisition was made in a private placement that received shareholder approval, (ii) was from a 25% or greater shareholder of the company which resulted in the acquirer becoming a 25% or greater shareholder of the company, if there is not already a 25% or greater shareholder of the company, or (iii) was from a shareholder holding a 45% interest in the company which resulted in the acquirer becoming a holder of a 45% interest in the company if there is not already a 45% or greater shareholder of the company.

If, as a result of an acquisition of shares, the acquirer will hold more than 90% of a public company s outstanding shares or a class of shares, the acquisition must be made by means of a tender offer for all of the outstanding shares or a class of shares. If less than 5% of the outstanding shares are not tendered in the tender offer, all the shares that the acquirer offered to purchase will be transferred to the acquirer. The Israeli Companies Law provides for appraisal rights if any shareholder files a request in court within three months following the consummation of a full tender offer. If more than 5% of the outstanding shares are not tendered in the tender offer, then the acquirer may not acquire shares in the tender offer that will cause his shareholding to exceed 90% of the outstanding shares.

Indemnification of Directors and Officers and Limitations of Liability

Exculpation of Office Holders. The Israeli Companies Law provides that an Israeli company cannot exculpate an office holder from liability with respect to a breach of his or her duty of loyalty. If permitted by its articles of association, a company may exculpate in advance an office holder from his or her liability to the company, in whole or in part, with respect to a breach of his or her duty of care. However, a company may not exculpate in advance a director from his or her liability to the company with respect to a breach of his duty of care in the event of distributions.

Office Holders Insurance. Israeli law provides that a company may, if permitted by its articles of association, enter into a contract to insure its office holders for liabilities incurred by the office holder with a respect to an act performed in his or her capacity as an office holder, as a result of: (i) a breach of the office holder s duty of care to the company or another person; (ii) a breach of the office holder s duty of loyalty to the company, provided that the office holder acted in good faith and had reasonable cause to assume that the act would not prejudice the company s interests; and (iii) a financial liability imposed upon the office holder in favor of another person.

Indemnification of Office Holders. Under Israeli law a company may, if permitted by its articles of association, indemnify an office holder for acts performed by the office holder in such capacity for (a) monetary liability imposed upon the office holder in favor of another person by any court judgment, including a settlement or an arbitration award approved by a court; (b) reasonable litigation expenses, including attorney s fees, actually incurred by the office holder as a result of an investigation or proceeding instituted against him by a competent authority, provided that such investigation or proceeding concluded without the filing of an indictment against the office holder or the imposition of any monetary liability in lieu of criminal proceedings, or concluded without the filing of an indictment against the office holder and a monetary liability was imposed on him or her in lieu of criminal proceedings with respect to a criminal offense that does not require proof of criminal intent; and (c) reasonable litigation expenses, including attorneys fees, actually incurred by the office holder or imposed upon the office holder by a court: (i) in an action, suit or proceeding brought against the office holder by or on behalf of the company or another person, (ii) in connection with a criminal action in which the office holder was acquitted, or (iii) in connection with a criminal action in which the office holder was convicted of a criminal offence that does not require proof of criminal intent.

Israeli law provides that a company s articles of association may permit the company to (a) indemnify an office holder retroactively, following a determination to this effect made by the company after the occurrence of the event in respect of which the office holder will be indemnified; and (b) undertake in advance to indemnify an office holder, except that with respect to a monetary liability imposed on the office holder by any judgment, settlement or court-approved arbitration award, the undertaking must be limited to types of occurrences, which, in the opinion of the company s board of directors, are, at the time of the undertaking, foreseeable due to the company s activities and to an amount or standard that the board of directors has determined is reasonable under the circumstances.

Limitations on Exculpation, Insurance and Indemnification. These provisions are specifically limited in their scope by Israeli law, which provides that neither a provision of the articles of association permitting the company to enter into a contract to insure the liability of an office holder, nor a provision in the articles of association or a resolution of the board of directors permitting the indemnification of an office holder, nor a provision in the articles of association exculpating an office holder from duty to the company shall be valid, where such insurance, indemnification or exculpation relates to any of the following: (1) a breach by the office holder of his duty of loyalty unless, with respect to insurance coverage or indemnification, the office holder acted in good faith and had a reasonable basis to believe that the act would not prejudice the company; (2) a breach by the office holder of his duty of care if such breach was committed intentionally or recklessly, unless the breach was committed only negligently; (3) any act or omission done with the intent to unlawfully yield a personal benefit; or (4) any fine or forfeiture imposed on the office holder. Pursuant to the Israeli Companies Law, exculpation of, procurement of insurance coverage for, and an undertaking to indemnify or indemnification of, our office holders must be approved by our audit committee and our board of directors and, if the office holder is a director, also by our shareholders.

Our Articles of Association allow us to insure, indemnify and exempt our office holders, subject to the provisions of the Israeli Companies Law. We maintain a directors and officers liability insurance policy with a per claim and aggregate coverage limit of $5 million, including legal costs incurred in Israel. In addition, our audit committee, board of directors and shareholders resolved to indemnify our office holders, pursuant to a standard indemnification agreement that provides for indemnification of an office holder in an amount up to $5 million. We have not to date provided letters of indemnification to our officers or directors.

NASDAQ Exemptions and Home Country Practices

Under NASDAQ Marketplace Rule 4350, or Rule 4350, foreign private issuers, such as our company, are permitted to follow certain home country corporate governance practices instead of certain provisions of Rule 4350. A foreign private issuer that elects to follow a home country practice instead of any of such provisions of Rule 4350, must submit to NASDAQ, in advance, a written statement from an independent counsel in such issuer s home country certifying that the issuer s practices are not prohibited by the home country s laws.

On July 7, 2005 and June 26, 2006, we provided NASDAQ with notices of non-compliance with Rule 4350. We informed NASDAQ that we do not comply with the following requirements of Rule 4350, and instead follow Israeli law and practice in respect of such requirements:

- the requirement regarding the process of nominating directors. Instead, we follow Israeli law and practice in accordance with which our directors are recommended by our board of directors for election by our shareholders. See above in this Item 6.C. Directors, Senior Management and Employees - Board Practices - Election of Directors.
- the requirement regarding the compensation of our chief executive officer and all other executive officers. Instead, we follow Israeli law and practice in accordance with which our board of directors must approve all compensation arrangements for our chief executive officer and all compensation arrangements for officers are subject to the chief executive officer s approval. See above in this Item 6.C. Directors, Senior Management and Employees - Compensation.
- the requirement that our independent directors have regularly scheduled meetings at which only independent directors are present. Under Israeli law independent directors are not required to hold executive sessions.
- the requirement that we distribute to shareholders, and file with NASDAQ, copies of an annual report containing audited financial statements of our company and its subsidiaries within a reasonable period of time prior to our annual meeting of shareholders. Under Israeli law, as a company that is publicly traded both in Israel and outside of Israel, we are not required to distribute such annual reports to our shareholders. Our annual report on Form 20-F and audited financial statements are available on our website (www.magal-ssl.com), and we will send it to shareholders upon written request.

- the requirement to maintain a majority of independent directors, as defined under the NASDAQ Marketplace Rules. Instead, we follow Israeli law and practice which requires that we appoint at least two outside directors, within the meaning of the Israeli Companies Law, to our Board of Directors. In addition, we have the mandated three independent directors that meet the independent standards contained in the rules of the Securities and Exchange Commission and NASDAQ on our audit committee. See above in this Item 6C. Directors, Senior Management and Employees - Board Practices - Independent and Outside Directors.

D. Employees

As of December 31, 2007, we employed 303 full-time employees, of whom 38 were employed in general management and administration, 42 in marketing, 22 in production management, 149 in production, installation and maintenance, and 52 in engineering and research and development. Of our 303 full-time employees, 143 were employed in Israel, 34 were employed in the U.S., 81 were employed in Canada and 45 were employed in various other countries.

As of December 31, 2006, we employed 294 full time employees, of whom 34 were employed in general management and administration, 43in marketing, 23 in production management, 143 in production, installation and maintenance, and 51 in engineering and research and development. Of our 294 full time employees, 135 were employed in Israel, 49 were employed in the U.S., 78 were employed in Canada and 32 were employed in various other countries.

As of December 31, 2005, we employed 309 full time employees, of whom 34 were employed in general management and administration, 47 in marketing, 20 in production management, 155 in production, installation and maintenance, and 53 in engineering and research and development. Of our 309 full time employees, 129 were employed in Israel, 56 were employed in the U.S., 89 were employed in Canada and 35 were employed in various other countries.

We are subject to various Israeli labor laws, collective bargaining agreements entered into from time to time between the Manufacturers Association and the Histadrut, as well as collective bargaining arrangements. These laws, agreements and arrangements cover a wide range of areas, including minimum employment standards, such as working hours, minimum wages, vacation, severance pay and pension plans, and special issues, such as equal pay for equal work, equal opportunity in employment and employment of youth and army veterans. Certain of our employees are parties to individual employment agreements. We generally provide our employees with benefits and working conditions beyond the required minimums. Each of our subsidiaries provides a benefits package and working conditions which are competitive with other firms in their area of operations.

Israeli law generally requires severance pay upon the retirement or death of an employee or termination of employment without due cause. Furthermore, Israeli employees and employers are required to pay predetermined sums to the National Insurance Institute, which is similar to the U.S. Social Security Administration, which amounts also include payments for national health insurance.

E. Share Ownership.

The following table sets forth certain information regarding the ownership of our ordinary shares by our directors and executive officers as of June 23, 2008.

Name	Number of Ordinary Shares Owned(1)	Percentage of Outstanding Ordinary Shares(2)
Jacob Perry		
Izhar Dekel (3)(4)	154,427	1.47%
Lian Goldstein		
Yehezkel Farber	*	*
Zvi Dank	*	*
Asaf Even-Ezra (5)(6)	124,926	1.19%
Dany Pizen	*	*
Raffi Netzer	*	*
Yehonatan Ben- Hamozeg	*	*
Nathan Kirsh (7)	2,277,728	21.91%
Jacob Even-Ezra (4)(5)(8)	432,242	4.03%
Jacob Nuss		
Zeev Livne		