



Zone-IP Ltd.
and its subsidiaries

(Formerly Ki-Bi Mobile Technologies Ltd.)

**Consolidated
Financial Statements**

31 December 2007

Consolidated Financial Statements

AS OF 31 DECEMBER 2007

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Chairman's Statement

In the year ended 31 December 2007 the Company incurred a loss on continuing operations of \$2.75 million (2006: \$5.88 million) on turnover of \$8.26 million (2006: \$6.57 million). At that date, the Company had a cash portfolio of \$5.2 million.

The year ended 31 December 2007 was a turnaround year for the Company. Following the completion of the strategic review in the last quarter of 2006, I indicated in my Chairman's statement accompanying the 2006 results that the Company intended to launch new products in the first half of 2007. I am pleased to advise you that the first six months of the year saw the introduction of the next generation of endpoints and infrastructure servers: xPoint - a new top of the line room system featuring ISDN and 4CIF technologies, VCBpro - a new state-of-the-art HD Multipoint appliance with full audio and video transcoding and vPoint V8 - an HD desktop client.

In Q4 2007, Wainhouse Research, an independent market research firm that focuses on critical issues in rich media communications and conferencing, conducted an evaluation, sponsored by the Company, of Emblaze-VCON's xPoint appliance-based videoconferencing system. The evaluation included ease of use, video performance, audio performance, data collaboration support, interoperability and security/ encryption. Based on the rating determined by Wainhouse Research in the report, xPoint earned a good overall rating of 3.8 out of 5. Specific areas of strength include exceptional ease of use, strong video performance, especially at relatively low call speeds, and solid interoperability with the other systems in the test lab. Wainhouse Research found that the xPoint performed at least as well, if not better, than its peers and in many ways exceeded their expectations. The full report can be found on the Company's website.

The second half of the year saw an overall change both on the business and the operational side. The release of a brand new up-to-standard product line has enabled us to sign distribution agreements with leading audio and video resellers across the world and win new business. It has also enabled us to embark on new OEM discussions with leading video vendors. Business focus was shifted to better reflect the Company's core technology and vision of Video over PC-based systems for competitive pricing.

On the operational side, the Company has dramatically improved its execution capabilities as well as reducing the rate of returned units.

Current trading

The early months of the current year will see further new product launches and upgrades in our existing product line. Emblaze VCON intends to extend its range of products and service offering to customers and enhance the technology of existing products to Full HD.

Future prospects

The Directors expect that demand for video over the desktop will increase as enterprises worldwide move to replace and converge their legacy analog systems into more advanced IP based products. The growing demand for visual communication solutions will allow Emblaze VCON to enhance its market presence through the introduction of the xPoint and VCBpro products. Having a complete offering will enable us to create a strong lead with AV resellers and take part in lucrative bids. Emblaze VCON will also endeavor to strengthen its leading position in the desktop Video-over-IP with special focus on web-based collaborative solutions. We will also strive to enhance our relationships and partnerships with industry technology and service providers.

Dr Hans Wagner
Chairman

Board of Directors

Dr Hans Wagner, Chairman

Dr. Wagner (77) has been Chairman of the Company since its admission to AIM in May 2005. He has served as deputy chairman of M-Systems since November 2002. Since 2003 Dr. Wagner has been chairman of Bamboo Multicasting, an Israeli company in the area of Mobile Infrastructure-Media equipment and in April 2006 became chairman of Eyesquad GmbH, a German company in the area of optical improvement of cameras for mobile phones. Dr. Wagner was senior partner of Omega Partners Ltd., a telecommunications consultancy firm, of which he was a founder in 1977. Dr. Wagner also founded and serves as vice chairman of Ozone Ltd., a manufacturer of ozone generators founded in 1996, and was chairman and founder of Pelikon Ltd., a developer and manufacturer of electro-luminescent displays. From 1995 to 2000, Dr. Wagner served as a strategic adviser to the management of Ericsson Mobile. From 1984 to 1992, Dr. Wagner was a founder and served as chairman of Technophone, a mobile telephone manufacturer which was the worldwide number three in sales prior to its acquisition by Nokia in 1991. From 1973 to 1977, Dr. Wagner served as the assistant secretary general of the UNDP. From 1969 to 1973, Dr. Wagner served as the chief executive officer of SONAB AB, then Sweden's second largest communication equipment manufacturer. From 1963 to 1969, Dr. Wagner served as the chief operating officer of Incentive AB, then Sweden's largest technical conglomerate.

Tal Barnoach, Executive Vice Chairman

Mr. Barnoach (44) was appointed to the board of directors in January 2006 as a non-executive director. In September 2006, Mr. Barnoach was appointed by the Board of Directors as Executive Vice Chairman, with the intent that he devotes more time to certain executive assignments and responsibilities relating to the Company's operations. Mr. Barnoach is an expert in the areas of enterprise software and the Internet. Since 1994 Mr. Barnoach has served as chief executive officer & chairman of S.E.A Multimedia and led that company's IPO in London in 1996. In 1999, Mr. Barnoach was appointed chairman of Orca Interactive Ltd., a public company traded on AIM since October 2004. From 2000 and until 2003, Mr. Barnoach was the chairman of Icoognito and Dotomi. In 2002 he co-founded BelnSync, a company that developed a secure peer to peer synchronization solution and he is serving as the chief executive officer of that company. Mr. Barnoach holds a BA in economics from the University of Tel-Aviv.

Shimon Laor, Non-Executive Director

Mr. Laor (41) serves as Finance Director of the Company in a part-time capacity. He served as the Chief Financial Officer of Emblaze until August 2000. Since then he has served as a non-executive director on the Emblaze board and has been engaged in private business initiatives. Mr. Laor also serves as a non-executive director of Orca Interactive Ltd. and Visual Defence Inc., partly-owned subsidiaries of Emblaze. Prior to joining Emblaze in August 1995, he was an economist at the Head Office Foreign Currency Division of the First International Bank of Israel.

Guy Bernstein, Non-Executive Director

Mr. Bernstein (40) is the chief executive officer of Emblaze Ltd. since December 2006. Prior to this appointment, he served as Emblaze's chief financial officer of since April 2004. Prior to joining Emblaze Ltd., Mr. Bernstein served as chief financial and operations officer of Magic Software Enterprises (NASDAQ: MGIC) ("Magic"), a position he had held since 1999. At Magic, Mr. Bernstein's responsibilities included the overseeing of all finance operations, legal and M&A worldwide including budget planning, sales forecasting, board and SEC reporting and investor relations. Guy joined Magic from Kost, Forer Gabbay & Kasierer, a member of Ernst & Young Global, where he acted as senior manager from 1994 to 1997. Mr. Bernstein is a Certified Licensed Public Accountant and holds a BA in Accounting.

Naamit Salomon, Non-Executive Director (Resignation from the board on 1 March 2007)

Ms. Salomon was appointed to the board in July 2006 as a non-executive director and external director of the Company. She has been the VP Finance of Formula Systems Ltd. since August 1997. Ms. Salomon also serves as a director of Magic Software Enterprises Ltd., Sapiens International and BluePhoenix Solutions Ltd. From 1990 to August 1997, Ms. Salomon was a controller of two large, privately held companies in the Formula Group. Ms. Salomon holds a BA degree in economics and business administration from Ben-Gurion University and an LL.M. degree from the Bar-Ilan University.

Board of Directors

CONTINUED

David Leichner, Non-Executive Director (Resignation from the board on 29 May 2007)

Mr. Leichner (44) was appointed to the board in July 2006 as a non-executive director and external director of the Company. Mr. Leichner is chief marketing officer at Telrad Networks, a leading provider of products and solutions for the implementation of next generation networks. At Telrad, David is responsible for developing and executing the company's marketing and product strategy. Prior to Telrad, David was a vice-president of marketing at Unipier Ltd., a provider of service delivery solutions to the mobile telecoms industry. Mr. Leichner joined Unipier Ltd. from Magic Software Enterprises Ltd. (NASDAQ: MGC), where he was vice president of Worldwide Marketing from 1998 to 2004. Prior to Magic, Mr. Leichner held various international marketing management and technical positions at Emultek, Information Builders, Bezeq Communications, TRW Space and Defense Systems and Salomon Brothers. Mr. Leichner holds a BA in Computer Science and a MBA in International Business, from the City University of New York.

David Blass, Non-Executive Director (Appointment as of 10 May 2007)

Mr. David Blass (64) was appointed by the board of directors in May 2007. During the years 1993 through 1999, Mr. Blass was Managing Director of the Investment Company for Industrial Development in Israel Ltd., Chairman of the Board of Directors of two companies, a director of two public companies and a member of the investment committee of a venture capital firm. From 1999 until 2003, Mr. Blass was Deputy General Manager and Head of Banking and Credit Division at the Industrial Development Bank of Israel Ltd. Mr. Blass holds a BA in economics from the Bar-Ilan University and a Master of Business Administration (MBA) from the Tel Aviv University

Amira Paz, Non-Executive Director (Appointment as of 16 July 2007)

Ms. Paz (41) was appointed to the Board in July 2007. Ms. Paz served as a chief financial officer in three software companies since 1996: Tiltan Software Engineering, Enformia Software and Idit Technologies. Ms. Paz's responsibilities included overseeing of all the finance operations, budget planning, projects forecasting, board reporting and human resources and administration functions. Prior thereto, Ms. Paz served as a senior inspector with the Israeli Income Tax Authority. Ms. Paz is a Certified Licensed Public Accountant and holds a B.A. in Economics and Business Management from Ben Gurion University, an M.B.A. in Finance and Accounting from Tel Aviv University and an LL.M. from Bar Ilan University.

Assaf Medina, Non-Executive Director (Appointment as of 16 July 2007)

Mr. Medina (40) was appointed to the Board in July 2007. Mr. Medina served as Chief Operating Officer of SkyVision Ltd. from 2005 to 2006. At SkyVision, Mr. Medina's responsibilities included managing service organizations and operational processes relying on RF and IP technologies. Between 2003 and 2005, Mr. Medina held the position of VP Operations at Babylon Ltd., where his responsibilities included managing the IT, QA, customer care and technical support. From 2000 until 2003, Mr. Medina held the position of VP Operations at Magic Software Enterprises Ltd. (NASDAQ: MAGI), where his responsibilities included managing the worldwide operations, customer services, product release, logistics, ISO9001 and IT. From 1995 to 2000, Mr. Medina held several management positions at Magic. Mr. Medina holds an Industrial and Management practical engineering degree.

Corporate Governance

The Financial Reporting Council published its new Combined Code in July 2003, which was implemented on 1 November 2003. It incorporated the major recommendations of the Higgs review and also of Sir Robert Smith's review of audit committees. It also repeated the requirements to comply with the Directors Remuneration Report Regulations and the Internal Control guidance of the Turnbull Report. The new Combined Code of July 2003 (the "Code") supersedes and replaces the Combined Code issued by the Hampel Committee in June 1998.

The Code's overall aim is to "enhance Board effectiveness and to improve investor confidence by raising standards of corporate governance."

Incorporated in Israel, Zone-IP Ltd. is listed on the AIM Market of the London Stock Exchange and the Board of directors of Zone-IP (the "Board") has therefore decided, as a matter of best corporate practice, that the Company should seek to comply with the main provisions of the Code, insofar as possible and appropriate given the Company's size, the constitution of the Board and taking into account the Corporate Governance Guidelines on AIM companies published by the Quoted Companies Alliance in July 2005.

The Board

During the year ended December 2007, the Board comprised the following:

Dr. Hans Wagner, the Non-Executive Chairman
Tal Barnoach, the Executive Vice Chairman
Shimon Laor, a Non-Executive director
Guy Bernstein, a Non-Executive Director
Naamit Salomon, a Non-Executive Director ¹
David Leichner, Non-Executive Director ²
David Blass, Non-Executive Director ³
Amira Paz, Non-Executive Director ⁴
Assaf Medina, Non-Executive Director ⁴

In March 2007, Ms. Naamit Salomon resigned from the Board due to conflict of interest with other directorships she holds.

In May 2007, Mr. David Leichner resigned from the Board due to conflict of interest with other responsibilities and services he agreed to take.

The Chairman, Dr. Hans Wagner, is acting as a non-executive Chairman and he does not receive any remuneration. On 01 May 2007, 22 June 2007 and 17 December 2007 Dr. Wagner purchased 2,716,395, 2,128,112 and 5,338,816 ordinary shares in the Company, respectively. Following these purchases, Dr. Wagner now holds 10,183,323 ordinary shares in the Company, equivalent to 19.92 per cent. of the issued voting share capital of Zone-IP and is therefore not considered under the Code to be independent.

Shimon Laor and Guy Bernstein are appointees of significant shareholders of the Company and they would therefore not be deemed to be independent.

Tal Barnoach, Executive Vice Chairman, purchased on 01 May 2007, 22 June 2007 and 17 December 2007; 905,465, 709,371 and 1,779,638 ordinary shares in the Company, respectively. Following these purchases, Mr. Barnoach now holds 3,394,474 ordinary shares in the Company, equivalent to 6.64 per cent. of the issued voting share capital of Zone-IP.

¹ Resignation as of 1 March 2007

² Resignation as of 29 May 2007

³ Appointment as of 10 May 2007

⁴ Appointment as of 16 July 2007

Corporate Governance

CONTINUED

The Chairman and Non-Executive Directors have service contracts with the Company. Details of their respective terms are set out in the Report on Directors' Remuneration.

The Board meets on a regular basis to discuss the overall direction and strategic plan of the Company. The Board also monitors the Company's budget, performance and achievements.

Prior to each Board meeting, each Director receives information on the performance and progress of the Company since the last Board meeting as well as background material related to the issues for discussion at the meeting itself.

There is in place a procedure under which the Directors, in furtherance of their duties, are able to take professional advice, if necessary, at the Company's expense.

The Israeli Companies Law requires the Company to appoint two "External Directors" who meet certain statutory criteria of independence. Under Israeli law the initial term of an External Director is three years and the term may be extended for an additional three-year period. Naamit Salomon and David Leichner were appointed as External Directors at the Extraordinary General Meeting held on 4 January 2006 until the conclusion of the Annual General Meeting to be held in 2009 but they both resigned during 2007 due to conflict with other responsibilities and/or directorships. On 16 July 2007, the Annual General Meeting of the Company appointed Ms. Amira Paz and Mr. Assaf Medina to assume the position of the External Directors for a three-year term.

Except for the External Directors, Directors are subject to re-election at every Annual General Meeting.

Board Committees

The Board has established Audit, Remuneration and Nomination Committees. The duties of these committees are set out clearly in formal terms of reference, which are available for inspection upon request.

Audit Committee

In May 2007, the Board appointed Mr. David Blass as a Director and member of the Audit Committee. Naamit Solomon and David Leichner both resigned during 2007 due to conflict with other responsibilities and/or directorships. Therefore, Ms. Amira Paz and Mr. Assaf Medina were appointed as the two other members of the Audit Committee commencing their appointment to the Board in July 2007.

Under its terms of reference, the Audit Committee is required to oversee the relationship with the Company's external auditors, to review the Company's preliminary results, interim results and financial statements and to monitor compliance with statutory and listing requirements for any exchange on which the Company's shares are quoted.

The Audit Committee also reviews the Company's internal control and risk management as well as the Company's cash investment policy.

The Company's Chairman and Chief Financial Officer may attend meetings at the Committee's request.

Remuneration Committee

Dr. Hans Wagner is the chairman of the Remuneration Committee. Naamit Solomon and David Leichner both resigned from the Board in May 2007 and therefore, Ms. Amira Paz and Mr. Assaf Medina were appointed as the two other members. Their appointment to the Board commenced in July 2007.

The Remuneration Committee approves the remuneration of all senior executives in the Company. It is also responsible for making recommendations to the Board on the Company's framework of executive remuneration and for determining on behalf of the Board the remuneration package for each executive director.

The remuneration of Non-Executive Directors is determined by the entire Board, but the Non-Executive Directors do not participate in Board discussions or vote on matters relating to their own fees.

Corporate Governance

CONTINUED

Nomination Committee

Mr Guy Bernstein is the chairman of the Nomination Committee. The other member is Ms. Amira Paz, who was appointed to the Board in July 2007.

The Nomination Committee leads the process for Board appointments and makes recommendations to the Board.

Relations with Shareholders

The Company welcomes dialogue with its shareholders and communicates with them through its interim and annual reports.

At the Annual General Meeting, shareholders can raise questions with the Directors. Separate resolutions are proposed on each substantially different issue so that each receives proper consideration. Resolutions include the approval of the annual report and accounts. Proxy votes are announced after each resolution has been dealt with by a show of hands. Notice of the Annual General Meeting and related documentation are sent to shareholders at least 35 days in advance.

Report on Directors' Remuneration

Policy on remuneration of Directors

The remuneration of the Non-Executive Directors is set by the Remuneration Committee and approved by the Board of Directors, subject to the approval of the Annual General Meeting.

The remuneration of Directors is set below:

Dr. Hans Wagner	None (only reimbursement of expenses)
Mr. Tal Barnoach	£24,000 gross per annum paid quarterly in arrears as of July 2007. Until July 2007, remuneration was set at £20,000 gross per annum
Mr. Shimon Laor	£20,000 gross per annum paid quarterly in arrears £10,000 for his role as a director and £10,000 for his role as part-time finance director
Mr. Guy Bernstein	None (only reimbursement of expenses)
Mr. Naamit Solomon	£20,000 gross per annum paid quarterly in arrears until March 2007
Mr. David Leichner	£20,000 gross per annum paid quarterly in arrears until May 2007
Mr. David Blass	\$US 12,000 gross per annum paid quarterly in arrears as of May 2007
Ms. Amira Paz	\$US 12,000 gross per annum paid quarterly in arrears as of July 2007
Mr. Assaf Medina	\$US 12,000 gross per annum paid quarterly in arrears as of July 2007

Share Options

Mr. Shimon Laor, Director and part-time CFO of the Company, has benefited from the Company's share option scheme. On 13 July 2006, Mr. Laor was granted with 250,000 options at an exercise price of 0.24p (the fair market value of the grant date), which vest in four equal installments on the first, second, third and fourth anniversary as of the grant date.

Mr. Tal Barnoach, Executive Vice Chairman, was granted on 24 July 2007 with options to purchase an aggregate of 1,278,006 ordinary shares of the Company, representing 2.5 per cent of the current outstanding share capital of the Company. The exercise price of the options was set at US\$0.147 per share (which was higher than the fair market value of the Company's shares at the time of the entering into such agreement, subject to all necessary approvals, in January 2007). The options vest over four years, with 25 per cent. of the options vesting on 31 December 2007 and 12.5 per cent. of the options vesting semi-annually thereafter.

Service Contracts

Non-Executive Directors have service contracts with the Company. With the exception of the two Outside Directors who are appointed for terms of three years at a time as required by Israeli law, each Non-Executive Director is subject to re-election at each Annual General Meeting. None of the Directors is involved in any discussions with the Board or any committee of the Board relating to their own remuneration, nor do they participate in any vote on their remuneration by the Board or any committee of the Board.

The fees paid to Non-Executive Directors are determined with reference to available information on the fees paid in other companies of broadly similar size and market cap. Non-Executive Directors are entitled to reimbursement of reasonable out-of-pocket expenses.

Independent Auditors' Report

To the Shareholders of ZONE IP LTD.
(Formerly: Ki-Bi Mobile Technologies Ltd.)



We have audited the accompanying financial statements of ZONE IP LTD. (formerly: Ki-Bi Mobile Technologies Ltd.) ("the Company") and its subsidiaries ("the Group"), which comprise the consolidated balance sheets as at 31 December 2007 and 2006, and the consolidated income statements, consolidated statements of changes in equity and consolidated statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as of 31 December 2007 and 2006, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KOST FORER GABBAY & KASIERER

A Member of Ernst & Young Global

Tel-Aviv, Israel

June 12, 2008

Consolidated Balance Sheets

		31 December	
	Note	2007 (US\$'000)	2006(US\$'000)
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	3	1,968	1,613
Restricted cash		1,257	237
Short-term available-for-sale marketable securities	4	150	3,974
Trade receivables	5	2,383	1,660
Other accounts receivable and prepaid expenses	6	529	387
Inventories	7	2,730	1,407
Total current assets		9,017	9,278
NON-CURRENT ASSETS:			
Long-term available-for-sale marketable securities	4	1,869	1,505
Property and equipment	8	397	501
Intangible assets	9	650	894
Total non-current assets		2,916	2,900
Total assets		11,933	12,178

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

Consolidated Balance Sheets

		31 December	
	Note	2007 (US\$'000)	2006 (US\$'000)
LIABILITIES AND EQUITY			
CURRENT LIABILITIES:			
Short-term bank credit	10	2,330	515
Trade payables		3,042	1,549
Employees and payroll accruals		515	628
Related party	18	53	513
Government grants	12	767	577
Deferred revenues		203	471
Accrued expenses and other liabilities	11	429	389
Total current liabilities		7,339	4,642
NON-CURRENT LIABILITIES:			
Government grants	12	593	847
Employees benefits liability	13	232	149
Total non-current liabilities		825	996
Liabilities attributed to discontinued operations	1c	111	250
Total liabilities		8,275	5,888
EQUITY:			
Ordinary shares		109	109
Share premium		13,203	12,989
Net unrealized losses reserve		(139)	(10)
Foreign currency translation reserve		4	(2)
Accumulated deficit		(9,519)	(6,796)
Total equity		3,658	6,290
Total liabilities and equity		11,933	12,178

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

Consolidated Statements of Operations

	For the year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
CONTINUING OPERATIONS:		
Revenues	8,265	6,577
Cost of revenues	(3,294)	(3,344)
Gross profit	4,971	3,233
Operating expenses:		
Research and development	3,019	3,018
Selling and marketing	2,682	3,816
General and administrative	1,840	1,714
Total operating expenses	7,541	8,548
Operating loss	(2,570)	(5,315)
Finance income	594	175
Finance costs	(832)	(212)
Loss for the period from continuing operations	(2,808)	(5,352)
DISCONTINUED OPERATION:		
Income /(Loss) for the period from a discontinued operation	85	(531)
Net loss for the year	(2,723)	(5,883)
Loss per share:		
Basic and diluted loss per share from continuing operations	(0.05)	(0.13)
Basic and diluted loss per share from a discontinued operation	(0.00)	(0.02)
Basic and diluted loss per share	(0.05)	(0.15)
Weighted average number of shares used in computing basic and diluted loss per share	51,120,253	40,083,881

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

Consolidated Statements of Changes in Equity

	Share premium (US\$'000)	Share premium (US\$'000)	Net unrealized loss reserve (US\$'000)	Foreign currency translation adjustments reserve (US\$'000)	Accumulated deficit (US\$'000)	Total equity (US\$'000)	Total recognized income (expenses) (US\$'000)
Balance as of 1 January 2006	66	3,539	-	(2)	(913)	2,690	
Reverse acquisition of net assets of Zone IP, net of issuance expenses	43	9,450	-	-	-	9,493	-
Net loss on available-for-sale financial assets	-	-	(10)	-	-	(10)	(10)
Net loss	-	-	-	-	(5,883)	(5,883)	(5,883)
							<u>(5,893)</u>
Balance as of 31 December 2006	109	12,989	(10)	(2)	(6,796)	6,290	-
Foreign currency translation	-	-	-	6	-	6	6
Net loss on available-for-sale financial assets	-	-	(129)	-	-	(129)	(129)
Share-based payment	-	214	-	-	-	214	-
Net loss	-	-	-	-	(2,723)	(2,723)	(2,723)
							<u>(2,846)</u>
Balance as of 31 December 2007	109	13,203	(139)	4	(9,519)	3,658	

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

Consolidated Statements of Cash Flows

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	(2,723)	(5,883)
Adjustments to reconcile the net loss to net cash used in operating activities:		
(Income) / Loss from discontinued operations	(85)	531
Depreciation and amortization	522	547
Share-based payment	214	-
Increase in employee benefits liability	83	149
Amortization of premium and discount of marketable securities	41	-
(Increase) / Decrease in short and long-term Government grants payables	(64)	63
Working capital adjustments:		
(Increase) / Decrease in trade receivables	(722)	453
(Increase) / Decrease in other accounts receivable and prepaid expenses	(141)	153
Increase in inventories	(1,437)	(221)
Increase in trade payables	1,459	155
Decrease in employees and payroll accruals	(112)	(402)
(Decrease) / Increase in deferred revenues	(268)	330
Increase in accrued expenses and other liabilities	41	241
Net cash flows used in continuing operating activities	(3,192)	(3,884)
Net cash flows used in discontinued operating activities (3)	(54)	(772)
Net cash used in operating activities	(3,246)	(4,656)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(26)	(232)
Restricted cash	(1,020)	(237)
Investment in marketable securities	(2,680)	(3,083)
Proceeds from sale of marketable securities	5,970	6,650
Net cash provided by investing activities	2,244	3,098
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase in short-term bank credit	1,815	148
Increase in cash upon reverse acquisition	-	585
(Decrease) / Increase in related party	(460)	182
Net cash provided by financing activities	1,355	915
Increase / (Decrease) in cash and cash equivalents	353	(643)
Net foreign exchange difference	2	-
Cash and cash equivalents at beginning of year	1,613	2,256
Cash and cash equivalents at end of period	1,968	1,613

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

Consolidated Statements of Cash Flows

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
(1) SUPPLEMENTAL DISCLOSURE OF CASH FLOW ACTIVITIES:		
Interest received	302	479
Interest paid	72	49
Tax paid	15	13
(2) NON-CASH ACTIVITIES:		
Transfer from inventories to property and equipment	114	81
Property acquired through suppliers' credit	34	-
(3) NET CASH FLOWS USED IN DISCONTINUED OPERATING ACTIVITIES:		
Profit / (Loss) from a discontinued operation	85	(531)
Less decrease in accrued expenses associated with the discontinued operation	(139)	(241)
	(54)	(772)

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

Notes to the Financial Statements

FOR THE YEAR ENDED 31 DECEMBER 2007

I. GENERAL

- a. Zone IP Ltd. ("the Company") was incorporated on 29 August 2002 in Israel. In July 2006, the Company changed its name from Ki-Bi Mobile Technologies Ltd. ("Ki-Bi") to Zone-IP Ltd. The Company's ordinary shares are traded on the AIM Market of the London Stock Exchange ("AIM").
- b. The consolidated financial statements of the Company and its subsidiaries ("the Group") for the year ended 31 December 2007 were authorized for issue in accordance with a resolution of the Company's board of directors dated June 11, 2008.
- c. At the end of May 2006, the Company signed an agreement with Emblaze Vcon Ltd ("EVC") and its shareholders under which the Company agreed to acquire 100 per cent of EVC's shares in exchange for the issuance of shares that will represent 60 per cent of the outstanding shares of the Company immediately following the consummation of the agreement with EVC's shareholders.

The consummation of the agreement was approved by the shareholders at the Annual General Meeting ("AGM") of the Company that took place on 12 July 2006. The number of shares issued to the shareholders of EVC was 30,672,152. Due to the size of EVC in relation to the size of the Company, the acquisition constituted a reverse takeover - See Note 2c.

EVC was incorporated in August 2005 in Israel. Shortly after its incorporation EVC purchased a substantial portion of the assets, liabilities and employees of Vcon Telecommunications Ltd., for a consideration of US\$1,600. The acquisition was accounted for under the purchase method.

EVC and its wholly-owned subsidiary in the U.S. design, develop, manufacture and sell high-performance, multi-function conferencing systems designed for a variety of networks, including those based on the Internet protocol. EVC's systems facilitate interactive communication between remote users through videoconferencing, video streaming, audio conferencing and data collaboration. These systems are primarily targeted at business, distance learning, telemedicine and government.

EVC distributes its products worldwide, primarily through distributors and value-added resellers, as well as original equipment manufacturers. In addition, the Company maintains regional sales and support offices.

d. **Discontinued operations - Electronic content cards ("Cards"):**

Prior to the reverse takeover as described in the previous section, the Board of Directors of Ki-Bi had decided in April 2006 to cease the operations of its Cards business, including the termination of substantially all of its employees. In September 2006, the Company signed an agreement with Spiral Solutions Ltd. according to which the Company's remaining Cards assets, including inventory, property and equipment and intellectual property were sold in consideration for US\$373 which approximated the carrying value of these assets.

The operating expenses of the Cards business from the date of reverse takeover are presented as discontinued operations in the statement of operations.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES

a. Statement of compliance

These consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS").

b. Basis of preparation:

These consolidated financial statements have been prepared on a historical cost basis except for available-for-sale marketable securities which have been measured at fair value.

The consolidated financial statements are presented in U.S. Dollars and all values are rounded to the nearest thousand (US\$'000) except when otherwise indicated.

c. Basis of consolidation:

As a result of the issuance of the Ordinary shares by the Company in July 2006, as described in note 1 (b); the shareholders of EVC obtained control of the Company. Accordingly, the transaction was accounted for as a reverse acquisition in accordance with IFRS 3, "Business Combinations". For financial reporting purposes, EVC (the legal subsidiary) is the acquirer and the Company (the legal parent) is the acquiree.

The consolidated financial statements prepared following the reverse acquisition are issued under the name of the Company, but they are a continuance of the financial statements of EVC. Because such consolidated financial statements represent a continuation of the financial statements of EVC:

- (i) The assets and liabilities of EVC have been recognized and measured in these consolidated financial statements at their pre-combination carrying amounts.
- (ii) The retained earnings and other equity balances recognized in these consolidated financial statements are the retained earnings and other equity balances of EVC immediately before the business combination.
- (iii) The amount recognized as issued equity instruments in these consolidated financial statements has been determined by adding to the issued equity of EVC immediately before the business combination the cost of the combination determined as described in the following paragraph. However, the equity structure appearing in these consolidated financial statements (the number and type of equity instruments issued) reflects the equity structure of the Company, including the equity instruments issued by the Company to effect the combination.

These consolidated financial statements prepared following the reverse acquisition reflect the carrying values of the assets and liabilities of EVC (the acquirer for accounting purposes) and the fair values of the net assets of the Company (the acquiree for accounting purposes) in the amount of US\$10,238. As substantially all of the net assets of the Company were comprised of cash and cash equivalents and marketable securities, the fair value of the Company's assets was equivalent to their carrying value.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

The direct transaction costs incurred in connection with the issuance of the Ordinary shares by the Company in the amount of US\$745 has been recorded as a reduction in additional paid-in share capital.

The revenues and loss of the Group for the year ended 31 December 2006, had the reverse acquisition occurred on 1 January 2006, would have been US\$6,577 and US\$8,517, respectively.

d. Significant accounting judgments, estimates and assumptions:

The preparation of financial statements in accordance with IFRS requires estimates and assumptions by the Company's management. In the process of applying the entity's accounting policies, management makes various judgments, apart from those involving estimations, that can significantly affect the amounts recognized in the financial statements. The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Judgments

In the process of applying the Group's accounting policies, management has made the following judgment, apart from those involving estimations, which has the most significant effect on the amounts recognised in the financial statements:

Operating Leases

The Group leases facilities from third parties. The Company has determined, based on an evaluation of the terms and conditions of the agreement that the significant risks and rewards of ownership of these facilities were not transferred to the Group and so accounts for the arrangements as operating leases.

Operating lease payments are recognised as an expense in profit or loss on a straight line basis over the lease term.

Estimates And Assumptions

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

- Impairment of non-financial assets - the Group assesses whether there are any indicators of impairment for all non-financial assets at each reporting date. Non-financial assets are tested for impairment when there are indicators that the carrying amount may not be recoverable. When value in use calculations are undertaken, management must estimate the expected future cash flows from the assets or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

- Impairment of available-for-sale financial assets - the Group classifies certain assets as available-for-sale and recognizes movements in their fair value in equity. When the fair value declines, management makes assumptions about the decline in value to determine whether it is an impairment that should be recognized in profit or loss. At 2007 and 2006 no impairment losses have been recognized for available-for-sale sets.
- Share-based payment - the Group measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value requires determining the most appropriate valuation model for a grant of equity instruments, which is dependent on the terms and conditions of the grant. This also requires determining the most appropriate inputs to the valuation model including the expected life of the option, volatility and dividend yield and making assumptions about them. The assumptions and models used are disclosed in Note 15.
- Employees benefits liability - the measurement of the liability in respect of the defined benefit pension plans is determined using actuarial valuations. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Due to the long term nature of these plans, such estimates are subject to significant uncertainty. Further details are given in Note 13.

e. Changes in accounting policy and disclosures:

The accounting policies adopted are consistent with those of the previous financial year except as follows:

The Group has adopted the following new and amended IFRS and IFRIC interpretations during the year. Adoption of these revised standards and interpretations did not have any effect on the financial performance or position of the Group. They did however give rise to additional disclosures, including in some cases, revisions to accounting policies.

IFRS 7 Financial Instruments: Disclosures

IAS 1 Amendment - Presentation of Financial Statements

The principal effects of these changes are as follows:

IFRS 7 - Financial Instruments: Disclosures

This standard requires disclosures that enable users of the financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments. The new disclosures are included throughout the financial statements. While there has been no effect on the financial position or results, comparative information has been revised where needed.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

IAS 1 - Presentation of Financial Statements

This amendment requires the Group to make new disclosures to enable users of the financial statements to evaluate the Group's objectives, policies and processes for managing capital.

f. Functional currency and translation:

The majority of the Company's sales are made outside of Israel, mainly in U.S. Dollars. A substantial portion of the Company's costs, mainly selling, marketing and service costs are incurred in U.S. Dollars. Accordingly, the U.S. Dollar is the functional and presentation currency of the Company.

Transactions in non-dollar currencies are recorded based on the exchange rate on the date of the transaction. Monetary assets and liabilities in non-dollar currencies are retranslated at the functional currency rate of exchange at the balance sheet date. Exchange rate differences are recorded in the statement of operations.

Non-monetary items that are measured at historical cost in non-dollar currencies are translated at the historical exchange rate on the date of the transaction.

The financial statements of certain subsidiaries, whose functional currency is not the U.S. Dollar, have been translated into U.S. Dollars. Assets and liabilities of these subsidiaries have been translated using the exchange rates in effect at the balance sheet date. Statement of income amounts have been translated using an average exchange rate. The resulting translation adjustments are reported as a separate component of equity. At the time of disposal of these subsidiaries, the deferred cumulative amount recognized in equity relating to those subsidiaries will be recognized in the statement of income.

Following are data about the representative exchange rate of the US Dollar in relation to the New Israeli Shekel ("NIS"), Euro and the GBP:

As of	Exchange rate	Exchange rate	Exchange rate
	of US\$ 1	of US\$ 1	of US\$ 1
	NIS	Euro	GBP
31 December 2007	3.85	0.68	0.50
31 December 2006	4.22	0.76	0.51
Change during the year ended	per cent.	per cent.	per cent.
31 December 2007	(9.0)	(10.5)	(2.1)
31 December 2006	(8.2)	(10.2)	(12.1)

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

g. Share-based payment transactions:

Employees and Directors of the Company and other service providers receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments (equity settled transactions).

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date on which they are granted. The fair value is determined by an external valuator using an appropriate pricing model, further details of which are given in Note 15.

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the vesting date). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. The income statement charge or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period.

No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense if the terms had not been modified. An additional expense is recognized for any modification, which increases the total fair value of the share based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

h. Principles of consolidation:

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries as at 31 December each year after the elimination of all intercompany balances, transactions, income and expenses and profits and losses resulting from intra-group transactions.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Company and its subsidiaries obtains control, and continue to be consolidated until that such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the parent company, using consistent accounting policies.

All intra-group balances, income and expenses and unrealized gains and losses resulting from intra-group transactions are eliminated in full.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

i. **Scope of consolidation:**

The following wholly owned subsidiaries are consolidated as of 31 December 2007:

Emblaze Vcon Ltd.

Emblaze Vcon Inc. (U.S.)

Emblaze Vcon GmbH (Germany)

Ki-Bi Ltd. U.K.

j. **Cash and cash equivalents:**

Cash and cash equivalents in the balance sheet comprise cash at banks and on hand short term deposits with an original maturity of three months or less.

For the purpose of the consolidated cash flow statements, cash and cash equivalents consist of cash and cash equivalents as defined above.

k. **Restricted cash:**

Restricted cash is due to a bank guarantee.

l. **Securities available-for-sale:**

Securities available-for-sale are measured at fair value. After initial measurement, available for sale financial assets are measured at fair value with unrealised gains or losses being recognized directly in equity in the net unrealised loss reserve. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognized in the statement of operations.

m. **Fair value:**

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument which is substantially the same, discounted cash flow analysis or other valuation models.

n. **Trade receivables:**

Trade receivables are recognized and carried at original invoice amounts less an allowance for any uncollectible amounts. An estimate for doubtful debts is made when collection of the full amount is no longer probable. Bad debts are written-off when identified.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

o. Inventories:

Inventories are valued at the lower of cost or net realizable value.

Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

Cost incurred in bringing each product to its present location and condition are accounted for as follows:

- Raw materials - at weighted average cost.
- Finished goods - includes average cost of direct materials and labour and a proportion of manufacturing overheads based on a normal level of activity but excluding borrowing costs.

p. Property and equipment:

Property and equipment is stated at cost less accumulated depreciation and accumulated impairment losses. Such cost includes the cost of replacing part of the property and equipment when the cost is incurred, if the recognition criteria are met. Likewise, when a major inspection is performed, its cost is recognized in the carrying amount of the property and equipment as a replacement if the recognition criteria are satisfied. All other repair and maintenance costs are recognized in profit or loss as incurred.

No impairment losses were recorded during 2007 and 2006.

Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, at the following annual rates:

	<u>Per cent.</u>
Computers and peripheral equipment	33
Office furniture and other equipment	6 - 15
Leasehold improvements	The shorter of the term of the lease or the useful life of the asset

The asset's residual values, useful lives and methods of depreciation are reviewed, and adjusted if appropriate, at each financial year end.

The Group periodically assesses the recoverability of the carrying amount of property and equipment and provides for any possible impairment loss based upon the difference between the carrying amount and recoverable amount of such assets in accordance with IAS 36, "Impairment of Assets". No impairment losses have been identified in the periods presented.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

q. Intangible assets:

Intangible assets acquired separately are measured on initial recognition at cost.

Cost of intangible assets acquired in a business combination, are recorded at fair value at the date of acquisition. Following initial recognition, the intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

The useful lives of the acquired intangible assets are assessed to be finite. Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in profit or loss in the expense category consistent with the function of the intangible asset.

The estimated benefit period of the acquired intangible assets is seven years for core technology and four years for other developed technology.

The Group assesses at each reporting date whether there is an indication that an intangible asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. As of 31 December 2007 and 2006, no impairment losses have been identified.

r. Government grants:

Royalty-bearing grants from the Government of Israel through the Office of the Chief Scientist for funding approved research and development projects are recognized where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. Grants are recorded as a deduction of research and development costs when there is reasonable assurance that the grants will not be repaid based on estimate future sales. Such grants are recorded as a liability when repayment is probable to the extent of the Group's estimate of sales from products developed with these projects.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

s. Revenue recognition:

The Company generates revenues from sale of a bundled hardware and software solution that is delivered together and maintenance, consulting and training services. The Company sells its products primarily through distributors and resellers which are all considered end-users. Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenues from sales of goods are recognized when the significant risks and rewards of ownership of the goods have passed to the buyer, usually up on delivery of the goods. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and other sales taxes or duty.

Deferred revenues include amounts received from customers for which revenues have not been recognized.

Revenues from services are recognised when the service is provided. Maintenance revenues are comprised of revenues from support arrangements that include technical support and the right to unspecified upgrades on an if-and-when-available basis. Revenues from these services are deferred and recognized on a straight-line basis, over the life of the related agreement, which is typically one year.

t. Research and development costs:

Research costs are expensed as incurred. Development costs in respect of individual projects are capitalized only if future recoverability is reasonably assured and various other criteria as set forth in IAS 38 Intangible Assets have been met. Since these criteria have not been satisfied, development costs are expensed.

u. Income taxes:

The Company accounts for income taxes under the liability method of accounting. Under the liability method, deferred taxes are determined based on the differences between the financial reporting and tax basis of assets and liabilities at enacted tax rates that will be in effect in the year in which the differences are expected to reverse. Deferred tax assets in respect of carryforward losses and other temporary deductible differences are recognised to the extent that it is probable that they will be utilized.

v. Basic and diluted net loss per share:

Basic net loss per share has been computed using a weighted average number of ordinary shares outstanding during the period. Diluted net loss per share is computed based on the weighted average number of shares outstanding during each period, plus the dilutive potential shares considered outstanding during the period, in accordance with IAS 33, Earnings per Share (Except when such potential shares are anti-diluted).

For the purpose of calculating the weighted average number of shares outstanding during the year 2006, in which the reverse acquisition occurred:

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

1. the number of shares outstanding from the beginning of 2006 is deemed to be the number of shares issued by the Company to the shareholders of EVC; and
2. the number of shares outstanding from the acquisition date to the end of 2006 is the actual number of shares of the Company outstanding during that period.

w. **Employee benefits:**

The Company operates a defined benefit plan for severance pay pursuant to the Israel's Severance Pay Law. Under the Severance Pay Law, Israeli resident employees are entitled to receive severance pay upon involuntary termination of employment, or upon retirement, which is calculated based on the most recent monthly salary at the time of termination, multiplied by the number of years of employment.

The Company funds its liability for severance pay by monthly payments to pension funds and insurance companies ("plan assets"). The plan assets include profits accumulated up to the balance sheet date. The plan assets may be withdrawn only in accordance with Israel's Severance Pay Law or labor agreements.

The cost for providing severance pay is determined using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognized immediately in the period in which they occur. The severance pay liability recognized in the balance sheet represents the present value of the defined benefit obligation reduced by the fair value of plan assets.

x. **IFRSs and IFRIC interpretations not yet effective:**

The following are IFRSs and IFRIC interpretations that have been issued recently:

1. **IAS 1 (Revised) Presentation of Financial Statements:**

IAS 1 (Revised) requires entities to present a separate statement of comprehensive income disclosing, other than the net income as stated in the income statement, all the items carried in the reported period directly to equity that do not derive from transactions with the shareholders in their capacity as shareholders (other comprehensive income) such as foreign currency translation adjustments of foreign operations, reclassification of fair value to available-for-sale financial assets, adjustments to revaluation reserve of fixed assets and such, while properly allocated between the Company and the minority interests. Alternatively, the items of other comprehensive income may be disclosed along with the items of the income statement in one single statement entitled statement of comprehensive income. Only the items carried to equity deriving from transactions with the shareholders in their capacity as shareholders (such as capital issuances, dividend distribution etc.) will be disclosed in the statement of changes in equity as will the summary line carried forward from the statement of comprehensive income, while properly allocated between the Company and the minority interests. IAS 1 (Revised) is effective for annual financial statements for periods commencing on 1 January 2009 with early adoption permitted. The effect of the adoption of IAS 1 (Revised) will require the Company to disclose the above items in the financial statements.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

2. IFRIC 12 *Service Concession Arrangements*:

IFRIC Interpretation 12 was issued in November 2006 and becomes effective for annual periods beginning on or after 1 January 2008. This Interpretation applies to service concession operators and explains how to account for the obligations undertaken and rights received in service concession arrangements. No member of the Group is an operator and hence this Interpretation will have no impact on the Group.

3. IFRIC 13 *Customer Loyalty Programs*:

IFRIC Interpretation 13 was issued in June 2007 and becomes effective for annual periods beginning on or after 1 July 2008. This Interpretation requires customer loyalty award credits to be accounted for as a separate component of the sales transaction in which they are granted and therefore part of the fair value of the consideration received is allocated to the award credits and deferred over the period that the award credits are fulfilled. The Company expects that this interpretation will have no impact on its financial statements as no such programs currently exist.

4. IFRS 2 (Revised) "Share-based Payment"

The amendment to IFRS 2 Share-based Payments was published in January 2008 and becomes effective for financial years beginning on or after 1 January 2009. The standard restricts the definition of "vesting condition" to a condition that includes an explicit or implicit requirement to provide services. Any other conditions are nonvesting conditions, which have to be taken into account to determine the fair value of the equity instruments granted. In the case that the award does not vest as the result of a failure to meet a non-vesting condition that is within the control of either the entity or the counterparty, this must be accounted for as a cancellation.

The Group has not entered into share-based payment schemes with non-vesting conditions attached and, therefore, does not expect significant implications on its accounting for share-based payments.

The Company estimates that the revised standard is not expected to have a material effect on its financial position, operating results and cash flows.

5. IFRS 3 (Revised), "Business Combinations" and IAS 27 (Revised), "Consolidated and Separate Financial Statements":

The revised standards were issued in January 2008 and become effective for financial years beginning on or after 1 July 2009. IFRS 3R introduces a number of changes in the accounting for business combinations that will impact the amount of goodwill recognized, the reported results in the period that an acquisition occurs, and future reported results. IAS 27R requires that a change in the ownership interest of a subsidiary is accounted for as an equity transaction. Therefore, such a change will have no impact on a goodwill, nor will it give rise to a gain or loss.

Notes to the Financial Statements

CONTINUED

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Furthermore, the amended standard changes the accounting for losses incurred by the subsidiary as well as the loss of control of a subsidiary.

The changes introduced by IFRS 3R and IAS 27R must be applied prospectively and will affect future acquisitions and transactions with minority interests.

6. IFRS 8 *Operating Segments*:

This standard requires disclosure of information about the Group's operating segments and replaced the requirement to determine primary (business) and secondary (geographical) reporting segments of the Group.

IFRS 8 is effective for annual financial statements for periods commencing on 1 January 2009 with early adoption permitted.

7. IAS 23 "Borrowing Costs"

A revised IAS 23 Borrowing Costs was issued in March 2007, and becomes effective for financial years beginning on or after 1 January 2009. The standard has been revised to require capitalisation of borrowing costs when such costs relate to a qualifying asset. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. In accordance with the transitional requirements in the Standard, the Group will adopt this as a prospective change. Accordingly, borrowing costs will be capitalised on qualifying assets with a commencement date after 1 January 2009. No changes will be made for borrowing costs incurred to this date that have been expensed.

8. Amendments to IAS 32 and IAS 1 Puttable Financial Instruments

Amendments to IAS 32 and IAS 1 were issued in February 2008 and become effective for annual period beginning on or after 1 January 2009. The amendment to IAS 32 requires certain puttable financial instruments and obligations arising on liquidation to be classified as equity if certain criteria are met. The amendment to IAS 1 requires disclosure of certain information relating to puttable instruments classified as equity. The Group does not expect these amendments to impact the financial statements of the Group.

9. IFRIC 14 IAS 19 - The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction

IFRIC Interpretation 14 was issued in July 2007 and becomes effective for annual periods beginning on or after 1 January 2008. This Interpretation provides guidance on how to assess the limit on the amount of surplus in a defined benefit scheme that can be recognised as an asset under IAS 19 Employee Benefits. The Group expects that this Interpretation will have no impact on the financial position or performance of the Group as all defined benefit schemes are currently in deficit.

Notes to the Financial Statements

CONTINUED

3. CASH AND CASH EQUIVALENTS

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
In U.S. Dollar	1,828	1,466
In Euro	110	81
In other currencies	30	66
	1,968	1,613

4. AVAILABLE-FOR-SALE MARKETABLE SECURITIES

Short-Term Available-for-Sale Marketable securities as of 31 December 2007 and 2006 were all with contractual maturities of less than one year as follows:

	31 December 2007			
	Effective interest rate (per cent.)	Amortized cost (US\$'000)	Unrealized losses (US\$'000)	Market value (US\$'000)
Corporate debentures	3.88	150	-	150
		150	-	150

	31 December 2006			
	Effective interest rate (per cent.)	Amortized cost (US\$'000)	Unrealized gains (losses) (US\$'000)	Market value (US\$'000)
Corporate debentures	5.25	2,553	(8)	2,545
U.S. Government and agency debt	4.66	949	(2)	947
Mutual funds	5.25	482	-	482
		3,984	(10)	3,974

Long-Term Available-for-Sale Marketable securities as of 31 December 2007 and 2006 were all with contractual maturities of more than one year as follows:

	31 December 2007			
	Effective interest rate (per cent.)	Amortized cost (US\$'000)	Unrealized gains (losses) (US\$'000)	Market value (US\$'000)
Mature after one year and less than five years:				
Corporate debentures	5.54	1,407	(144)	1,263
Foreign government bonds denominated in U.S. Dollar	5.45	601	5	606
		2,008	(139)	1,869

Notes to the Financial Statements

CONTINUED

4. AVAILABLE-FOR-SALE MARKETABLE SECURITIES (Continued)

	31 December 2006			
	Effective interest rate (per cent.)	Amortized cost (US\$'000)	Unrealized losses (US\$'000)	Market value (US\$'000)
Mature after one year and less than five years:				
Corporate debentures	5.60	504	(2)	502
Foreign bonds denominated in U.S. Dollar	5.39	1,001	2	1,003
		1,505	-	1,505

The fair value of the quoted financial assets is determined by reference to published price quotations in an active market.

There were no impairment provisions on available-for-sale financial assets in 2007 or 2006.

5. TRADE RECEIVABLES

Trade receivables are non-interest bearing and are generally on 60 days' terms.

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
Trade receivables	2,514	1,839
Allowance for doubtful accounts	(131)	(179)
	2,383	1,660

	Allowance for doubtful accounts (US\$'000)
Balance as of 1 January 2006	-
Provision, net of recoveries	179
Balance as of 31 December 2006	179
Provision, net of recoveries	64
Write-off	(112)
Balance as of 31 December 2007	131

Notes to the Financial Statements

CONTINUED

5. TRADE RECEIVABLES (Continued)

As at 31 December, the ageing analysis of trade receivables is as follows:

	Total	Neither past due nor impaired	Past due but not impaired				
			< 30 days	30 - 60 days	60 - 90 day	90 - 120 day	>120 days
2007	2,383	2,076	70	-	10	37	190
2006	1,660	605	285	438	-	215	117

6. OTHER ACCOUNTS RECEIVABLE AND PREPAID EXPENSES

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
VAT and customs authorities	326	107
Prepaid expenses and other	193	258
Advances to vendors	10	22
	<u>529</u>	<u>387</u>

7. INVENTORIES

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
Raw materials	1,182	600
Finished goods	1,548	807
Total inventories	<u>2,730</u>	<u>1,407</u>

Notes to the Financial Statements

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8. PROPERTY AND EQUIPMENT

	Computers and peripheral equipment (US\$'000)	Office furniture and other equipment (US\$'000)	Leasehold improvements (US\$'000)	Total (US\$'000)
Cost:				
At 1 January 2006	590	18	15	623
Additions	146	7	160	313
At 31 December 2006	736	25	175	936
Additions	158	16	-	174
At 31 December 2007	894	41	175	1,110
Accumulated depreciation:				
At 1 January 2006	131	1	-	132
Depreciation charge for the year	272	1	30	303
At 31 December 2006	403	2	30	435
Depreciation charge for the year	230	13	35	278
At 31 December 2007	633	15	65	713
Net book value:				
At 31 December 2007	261	26	110	397
At 31 December 2006	333	23	145	501
At 1 January 2006	459	17	15	491

Notes to the Financial Statements

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9. INTANGIBLE ASSETS

	Core technology (US\$'000)	Developed technology (US\$'000)	Total (US\$'000)
Cost:			
At 1 January 2006	577	648	1,225
At 31 December 2006	577	648	1,225
At 31 December 2007	577	648	1,225
Amortization and impairment:			
At 1 January 2006	43	44	87
Amortization	82	162	244
Balance at 31 December 2006	125	206	331
Amortization	82	162	244
At 31 December 2007	207	368	575
Net book value:			
At 31 December 2007	370	279	650
At 31 December 2006	452	442	894
At 1 January 2006	534	604	1,138

Amortization expense is recorded in cost of sales.

10. SHORT-TERM BANK CREDIT

Short-term bank credit includes bank overdrafts which bear interest at an annual rate of 7 per cent. and which are secured by restricted cash.

11. ACCRUED EXPENSES AND OTHER LIABILITIES

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
Royalties payable to third parties *	362	245
Other liabilities and accrued expenses	67	144
	429	389

* EVC is committed to pay royalties to various software suppliers based on proceeds from the sale of products developed pursuant to the agreements, which are limited in time and territory.

Notes to the Financial Statements

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12. LIABILITY FOR GOVERNMENT GRANTS

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
Total liability	1,234	1,361
Accrued interest	126	63
Less:- current portion	(767)	(577)
Non current portion	593	847
See also note 14b		

13. EMPLOYEE BENEFITS LIABILITY

a. The Group has a defined benefit plan for severance pay pursuant to the Israeli Severance Pay Law. The following tables summarize the components of net benefit expense recognized in the statement of operations and the amounts recognized in the balance sheet in accordance with IAS 19 provisions.

b. **Expenses in respect of employee benefits, net (recognized in cost of sales):**

	Year ended 31 December 2007 (US\$'000)
Current service cost	175
Interest cost on benefit obligation	34
Expected return on the plan assets	(21)
Net actuarial loss recognized in the year	48
Net benefit expense	236

c. **Benefit assets / (liabilities):**

Defined benefit obligation	(597)
Fair value of plan assets	365
Total liability, net	232

d. **Changes in the present value of the defined benefit obligation are as follows:**

Defined benefit obligation as of 1 January 2007	429
Interest cost	34
Current service cost	175
Benefits paid	(58)
Actuarial losses on obligation	17
Defined benefit obligation as of 31 December 2007	597

Notes to the Financial Statements

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13. EMPLOYEE BENEFITS LIABILITY (Continued)

e. The plan assets:

1. The plan assets include primarily stocks and bonds held in a long-term employee benefit fund as well as in managers' insurance policies.
2. Changes in the fair value of plan assets are as follows:

	31 December 2007 (US\$'000)
Fair value of plan assets as of 1 January 2007	280
Expected return	21
Contributions by employer	153
Benefit paid	(58)
Actuarial losses	(31)
Fair value of plan assets as of 31 December 2007	<u>365</u>

f. The principal assumptions used in determining the defined benefit obligation are shown below:

	31 December 2007 (per cent.)
Discount rate	<u>6.35</u>
Expected rate of return on plan assets	<u>6.35</u>
Future salary increases	<u>7.5</u>

14. COMMITMENTS AND CONTINGENT LIABILITIES

a. Operating lease commitments:

The Group leases office space under non-cancellable operating lease agreements for periods through 2010. Future minimum commitments under these leases are as follows:

	31 December 2007 (US\$'000)
2008	201
2009	114
2010	63
	<u>378</u>

Notes to the Financial Statements

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14. COMMITMENTS AND CONTINGENT LIABILITIES (Continued)

Rent expenses for lease of facilities for the years ended 31 December 2007 and 2006 are US\$250 and US\$252, respectively.

The Company leases motor vehicles under a cancellable lease agreement. The Company has an option to cancel the lease agreement, which may result in penalties in the maximum amount of US\$36. Expenses for the lease of motor vehicles for the years ended 31 December 2007 and 2006 were US\$321 and US\$363, respectively.

b. Royalty commitments:

Some of the core technologies of the Company were financed by the Government of Israel through the Office of the Chief Scientist of the Ministry of Industry, Trade and Labor ("OCS") and by the BIRD-Fund by participations in a portion of research and development expenditures incurred by VCON.

The Company is obligated, due to the acquisition of VCON's assets and liabilities, to pay royalties amounting to three to five per cent. of the sales of the products and other related revenues generated from such financed technologies, up to the amount of grants received from the OCS, plus interest at LIBOR.

As of 31 December 2007, the Company recorded a liability for grants received by VCON in the amount of US\$1,487. With respect to these grants, the Company has an outstanding contingent obligation to pay royalties in the amount of US\$4,181 in respect of projects for which there is a reasonable assurance that part or all of the grants received will not be repaid. The Company will revise its recorded liability related to this contingent obligation if facts and circumstances arise that will cause the Company to change its estimates of future sales.

See also Note 12 with regards to the liability for government grant.

c. Guarantees:

Zone-IP Limited guaranteed 23.6 per cent. of the bank overdraft to a maximum amount of US\$550 as of 31 December 2007 (2006 - US\$237).

15. EQUITY

a. As of 31 December 2007 and 2006 the Company's Ordinary shares of NIS 0.01 par value consist of 70,000,000 authorized shares. As of 31 December 2007 and 2006 the Company's Ordinary shares consist of 51,120,253 issued and outstanding shares.

b. Share-based payments:

The share-based payment plans are described below. There have been no cancellations or modifications to any of the plans during 2007 or 2006.

Notes to the Financial Statements

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15. EQUITY (Continued)

1. The Company

In 2004, the Company implemented the 2004 Stock Option Plan ("the Zone IP Plan"). Under the plan, 900,000 options to purchase Ordinary shares were reserved for issuance. These options which may be granted to consultants, directors and employees will generally vest over a period of up to four years from the date of grant, and if not exercised, the options expire on the tenth anniversary of the date of grant. The exercise price of these options may be less than 100 per cent. of the fair value of the share at the date of grant. Any options which are cancelled or forfeited before expiration become available for future grants. In July 2006, the Company's shareholders resolved to increase the reserve of shares reserved for issuance under the Plan. The fair value of the options is estimated at the grant date, using a Black and Scholes pricing model in 2006 and a binomial model in 2007, taking into account the terms and conditions upon which the instruments were granted.

The contractual life of each option granted is 10 years. There are no cash settlement alternatives.

The total amount of options available for future grants as of 31 December 2007, amounted to 3,418,994.

The following table illustrates the number (No.) and weighted average exercise prices (WAEP) of, and movements in, share options during the six month period from the date of the reverse acquisition see Note 1a to 31 December 2006 and during the year 2007:

	2007		2006	
	Amount	WAEP (US\$'000)	Amount	WAEP (US\$'000)
Outstanding at 1 July	-	-	349,902	0.36
Outstanding at 1 January	450,001	0.29	-	-
Granted during the year	1,278,006	0.49	250,000	0.44
Forfeited during the year	(155,001)	0.13	(149,901)	0.70
Outstanding at 31 December	1,573,006	0.49	450,001	0.29
Exercisable at 31 December	382,002	0.49	155,001	0.13

- (i) The weighted average fair value of the options granted in 2007 and 2006 was US\$0.16 and US\$0.33, respectively.
- (ii) The weighted average remaining contractual life of the share options outstanding as at 31 December 2007 is 9.28 years (2006: 6 years).

Notes to the Financial Statements

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15. EQUITY (Continued)

The following table lists the inputs to the model used for the period ended 31 December 2007 and 2006:

	2007	2006
Dividend yield	0 per cent.	0 per cent.
Expected volatility	69.1 per cent.	72 per cent.
Risk free interest rate	4.7 per cent.	5.6 per cent.
Early exercise multiple	3	-
Expected life of option (years)	10	8
Weighted average share price	US\$ 0.49	US\$ 0.44
Weighted average exercise price	US\$ 0.49	US\$ 0.13
Model used	Binomial	Black and Scholes

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome.

The total expense in respect of share-based payments in 2007 was US\$130 (2006: US\$0).

2. EVC

In December 2005, EVC approved the 2005 Global Option Plan ("the Option Plan"). Under the Option Plan, options may be granted to the Company's employees and consultants to purchase Ordinary shares of the Company. The options generally vest in equal portions, mainly over a period of four years commencing on the date of grant.

The options granted under the Option Plan expire 10 years from the date of grant or upon termination of the option holder's employment (the employee has 90 days to exercise his vested options upon employment termination). Any options which are cancelled or forfeited before expiration become available for future grants. The fair value of the options is estimated at the grant date, using a binomial pricing model, taking into account the terms and conditions upon which the instruments were granted.

There are no cash settlement alternatives.

The Company has made an election that options granted pursuant to Section 102(b) of the Income Tax Ordinance (New Version) 1961 (the "Ordinance"), to option holders who are Israeli residents be granted pursuant to the capital gains route.

The total number of Ordinary shares available for future grants as of 31 December 2007, amounted to 711,465.

Notes to the Financial Statements

CONTINUED

15. EQUITY (Continued)

The following table illustrates the number (No.) and weighted average exercise prices (WAEP) of, and movements in, share options during the year 2007:

	2007	
	No.	WAEP (US\$'000)
Outstanding at 1 January	-	-
Granted during the year	646,000	1
Forfeited during the year	6,500	1
Outstanding at 31 December	639,500	1
Exercisable at 31 December	85,000	1

The following table lists the inputs to the model used for the period ended 31 December 2007:

	2007
Dividend yield	0 per cent.
Expected volatility	74 per cent.
Risk free interest rate	4.9 per cent.
Early exercise multiple	5
Weighted average share price	US\$ 0.34
Weighted average exercise price	US\$ 1
Model used	Binomial

The expected life of the options is based on historical data and is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumption that the historical volatility is indicative of future trends, which may also not necessarily be the actual outcome.

The total equity-based compensation expense related to all of the Company's equity-based awards, recognized for the years ended 31 December 2007, was comprised as follows:

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
Cost of revenues	1	* -
Research and development	33	-
Selling and marketing	40	-
General and administrative	140	-
Total stock-based compensation expenses	214	-

* The total expense in respect of share-based payments in 2006 was immaterial.

The weighted average remaining contractual life for the share options outstanding as at 31 December 2007 is 9.3 years.

Notes to the Financial Statements

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16. INCOME TAXES

a. Israeli taxation:

1. Corporate tax rate:

On 25 July 2005, the Israeli Parliament approved an amendment to the Income Tax Ordinance (No. 147) 2005, which prescribes, among others, a gradual decrease in the corporate tax rate in Israel to the following tax rates: in 2006 - 31 per cent., in 2007 - 29 per cent., in 2008 - 27 per cent., in 2009 - 26 per cent., 2010 and thereafter - 25 per cent.

2. EVC submitted an application to assign the programs of VCON under the Law for the Encouragement of Capital Investments, 1959 ("the Law") to EVC and thus enjoy the tax benefits (primarily reduced tax rates) of an "Approved Enterprise" as defined by the Law. The application was approved by the Israel Investment Center (a department of the Ministry of Industry, Trade and Labor).

The Company's production facilities in Israel have been granted "Approved Enterprise" status, for six investment programs approved under the Law. According to the provisions of the Law, the Company has elected the "alternative benefits" track, the waiver of grants in return for a tax exemption and, accordingly, the Company's income from the "Approved Enterprise" is tax exempt for a period of two years commencing with the year it first earns taxable income and afterwards is entitled to a reduced tax rate of 10 per cent to 25 per cent for an additional period of five to eight years (depending on the level of foreign investment in the Company).

The entitlement to the above benefits is conditional upon the fulfillment of the conditions stipulated by the above Law, regulations published there under and the letters of approval for the specific investments in "Approved Enterprises". In the event of failure to comply with these conditions, the benefits may be cancelled and the Company may be required to refund the amount of the benefits, in whole or in part, including interest.

The period of tax benefits, detailed above, is subject to limits of the earlier of 12 years from the commencement of production, or 14 years from the approval date. These limitation do not apply to the tax exempt period of the first two years.

Income from sources other than the "Approved Enterprise" during the benefit period will be subject to tax at the regular corporate tax rate.

Notes to the Financial Statements

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16. INCOME TAXES (Continued)

3. On 1 April 2005, an amendment to the Investment Law came into effect ("the Amendment") and has significantly changed the provisions of the Investment Law. The Amendment limits the scope of enterprises which may be approved by the Investment Center by setting criteria for the approval of a facility as an Approved Enterprise, such as provisions generally requiring that at least 25 per cent. of the Approved Enterprise's income will be derived from export. Additionally, the Amendment enacted major changes in the manner in which tax benefits are awarded under the Investment Law so that companies no longer require Investment Center approval in order to qualify for tax benefits.
4. However, the Investment Law provides that terms and benefits included in any letter of approval already granted will remain subject to the provisions of the law as they were on the date of such approval. Therefore the Israeli subsidiary's existing Approved Enterprise will generally not be subject to the provisions of the Amendment.

EVC is an "industrial company" under the Law for the Encouragement of Industry (Taxation), 1969 and as such is entitled to certain tax benefits, including a reduction in the purchase price for patents or certain other intangible property rights at the rate of 12.5 per cent. per year beginning with the first year the Company used such intangible property rights and the deduction of public offering expenses over three years.

b. Carryforward tax losses:

As of 31 December 2007, the Company has carryforward tax losses of approximately US\$11,000 (2006: approximately US\$10,000) that can be carried forward indefinitely.

As of 31 December 2007, EVC has carryforward tax losses of approximately US\$5,300 (2006: approximately US\$3,500) that can be carried forward indefinitely.

As of 31 December 2007, the U.S. subsidiary had U.S. federal carryforward tax losses of approximately US\$4,887 (2006: US\$4,980) that can be carried forward and offset against taxable income for 15-20 years and expire between 2020-2025.

Management currently believes that since the Company and its subsidiaries have no history of ongoing profits it is not probable that the deferred tax asset in respect of the loss carryforwards and other temporary differences, in the amount of US\$2,013 (2006 - US\$2,365), mainly due to research and development differences, will be realized.

c. Tax assessments:

To date, the Company and its Israeli subsidiary have not received any final tax assessments.

Notes to the Financial Statements

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17. SUPPLEMENTARY INFORMATION TO THE STATEMENTS OF OPERATIONS

a. The following is a summary of revenues based on customer location:

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
United States	1,834	1,496
Europe	2,673	3,094
Southeast Asia	2,556	1,767
Other	1,202	220
	<u>8,265</u>	<u>6,577</u>

b. Salaries and employee benefits expense:

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
1.		
Cost of revenues	189	219
Research and development	2,532	2,280
Selling and marketing	927	1,187
General and administrative	366	470
	<u>4,014</u>	<u>4,156</u>
2.		
Wages and salaries	3,641	3,855
Social security costs	136	144
Severance pay costs	154	157
Share-based payments	83	-
	<u>4,014</u>	<u>4,156</u>

c. Depreciation and amortization:

Cost of revenues	244	286
Selling and marketing	15	8
General and administrative	263	253
	<u>522</u>	<u>547</u>

Notes to the Financial Statements

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17. SUPPLEMENTARY INFORMATION TO THE STATEMENTS OF INCOME DATA (Continued)

d. Financial expenses, net:

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
Financial income:		
Interest from bank deposits and marketable debt securities	594	175
Financial expenses:		
Exchange rate differences and other	(371)	(87)
Interest and other bank charges	(461)	(125)
	(832)	(212)
	(238)	(37)

18. RELATED PARTY DISCLOSURES

a. Compensation of key management personnel of the group:

	31 December	
	2007 (US\$'000)	2006 (US\$'000)
Short-term employee benefits	308	686
Severance pay	18	40
Share-based payments	61	-
Total compensation paid to key management personnel	387	726

Directors' interests in an employee stock option plan:

Stock options held by executive members of the Board of Directors to purchase ordinary shares have the following expiry dates and exercise prices:

Issue date	Expiry date	Exercise price	2007	2006
			Number	Number
2006	2016	US\$ 0.44	250,000	250,000
2007	2017	US\$ 0.49	1,278,006	-

No share options have been granted to the non-executive members of the Board of Directors under this scheme.

Notes to the Financial Statements

CONTINUED

18. RELATED PARTY DISCLOSURE (Continued)

b. Entities with significant influence over the Group:

Emblaze Ltd. owns 64.88 per cent. of the ordinary shares in Zone IP Ltd.

Transactions

	Year ended 31 December	
	2007 (US\$'000)	2006 (US\$'000)
Rent and utilities expenses	80	64

c. Balances

Amount owed to Emblaze at 31 December 2007 and 2006 was US\$53 and US\$513, respectively.

19. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

- a. The Group's principal financial liabilities comprise of bank credit, trade payables and other payables. The main purpose of the bank credit is to support the Group's ongoing operations. The Group has various financial assets such as trade receivables and cash and short-term deposits, which arise directly from its operations.

The main risks arising from the Group's financial instruments are fair value interest rate risk, foreign currency risk and credit risk. The Board of Directors reviews and agrees policies for managing each of these risks which are summarized below.

- Interest rate risk - the Company's investments consist primarily of cash, cash equivalents and securities available-for-sale. Securities available-for-sale are interest bearing. The primary objective of the Company's investment activities is to preserve principal while maximizing the income received from the investments without significantly increasing risk and loss. The investments are exposed to market risk due to fluctuation in interest rates, which may affect the interest income and the fair market value of the investments. The Company manages this exposure by performing ongoing evaluations of the investments.

At 31 December 2006 and 2007, if U.S. Dollar denominated interest rate had been one per cent. higher/lower with all other variables held constant, pre-tax profit for the years then ended would have been US\$22 and US\$12, respectively, lower/higher, mainly as a result of the impact of the interest rate on Group's investment portfolio.

Notes to the Financial Statements

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19. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

At December 31, 2006 and 2007, if U.S. Dollar denominated interest rate had been one per cent. higher/lower with all other variables held constant, equity for the years then ended would have been US\$7 and US\$15, respectively, lower/higher, mainly as a result of the impact of the interest rate on Group's investment portfolio.

- Foreign currency risk

As a result of significant investment operations in the United States, Europe and Southeast Asia the Group's balance sheet can be affected significantly by movements in the U.S. Dollar/Euro exchange rates.

The Company's foreign currency exposures impacted by the market risk associated with exchange rate fluctuations of the U.S. Dollar, the Company's functional and reporting currency, mainly against the Euro, the GBP and the NIS. In 2007, the Company derived its revenues principally in U.S. Dollars and to a significantly lesser extent in Euros and in GBP. Although the majority of the Company's expenses were denominated in U.S. Dollars, a portion of it was denominated in NIS and to a significantly lesser extent in euros. The Israeli shekel-denominated expenses consist principally of facilities-related and salaries and benefit-related expenses of Israeli operations. The Company anticipated that a large portion of the expenses will continue to be denominated in NIS. Consequently the depreciation of the U.S. Dollar against the Israeli shekel has a negative impact on our profit margins. Although the majority of the receivables are denominated in U.S. Dollars, a portion of the receivables are denominated in shekels which mitigate the effect of foreign currency fluctuations.

The following table demonstrates the sensitivity to a reasonably possible change in the U.S. Dollar exchange rate, with all other variables held constant, of the Group's Loss (due to changes in the fair value of monetary assets and liabilities).

	Increase/ decrease in US Dollar rate (per cent.)	Effect on profit before tax
2007		
NIS	5	(33)
Euro	5	15
GBP	5	17
2006		
NIS	5	(39)
Euro	5	53
GBP	5	12

Notes to the Financial Statements

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19. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

- **Credit risk**

The Group trades only with recognised, creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an ongoing

basis with the result that the Group's exposure to bad debts is not significant. For transactions that do not occur in the country of the relevant operating unit, the Group does not offer credit terms without the approval of the Head of Credit Control. There are no significant concentrations of credit risk within the Group.

With respect to credit risk arising from the other financial assets of the Group, which comprise cash and cash equivalents and available-for-sale financial investments the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

The Company's cash, cash equivalents are invested in highly rated financial institutions, and approximate their fair value due to the short-term maturities of these instruments is also the carrying value of trade and other receivables and current liabilities approximate their fair value.

b. **Capital management**

The primary objective of the Group's capital management is to ensure its ongoing activities as a going concern while maximizing the return on capital to shareholders. Accordingly, management will consider whether to issue additional shares or increase the amount of debt in the future based on the economic conditions and the results of its operations.

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