



**ClickSoftware**

Making Service Click

who



does what



with what



when



where



for whom



*Leading Service Businesses to Excellence*

**annual report 2013**

## About ClickSoftware

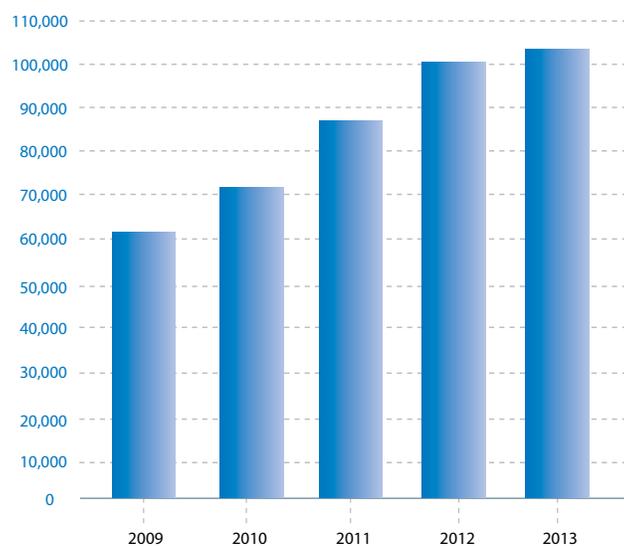
ClickSoftware (NasdaqGS: CKSW) is the leading provider of automated mobile workforce management and service optimization solutions for the enterprise, both for mobile and in-house resources. As pioneers of the "Service chain optimization" and "The real-time service enterprise" concepts, our solutions provide organizations with end-to-end visibility and control of the entire service management chain by optimizing forecasting, planning, shift and task scheduling, mobility and real-time management of resource and customer communication.

Available via the cloud or on-premise, our products incorporate best business practices and advanced decision-making algorithms to manage service operations more efficiently, in a scalable, integrated manner. Our solutions have become the backbone for many leading organizations worldwide by addressing the fundamental question of job fulfillment: Who does What, for Whom, With what, Where and When.

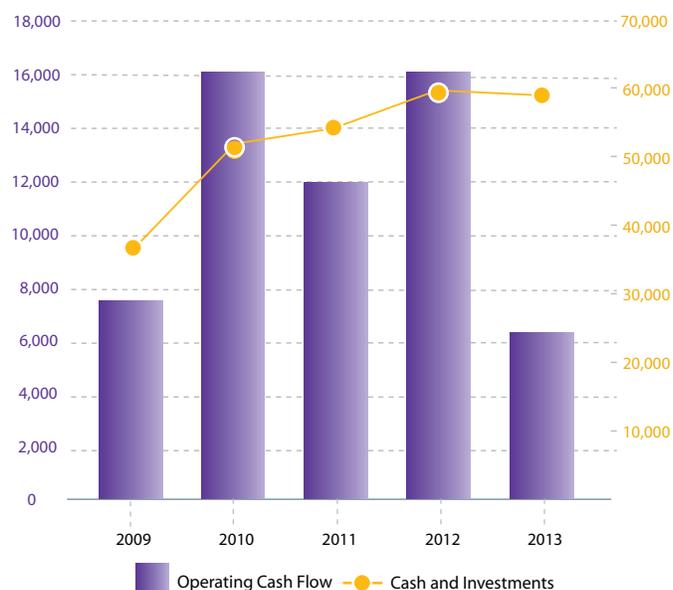
ClickSoftware is the premier choice for delivering superb business performance to service sector organizations of all sizes. The Company is headquartered in the United States and Israel, with offices across Europe, and Asia Pacific. For more information, please visit <http://www.clicksoftware.com>. Follow us on Twitter.

To download ClickSoftware's investor relations app, which offers access to SEC documents, press releases, videos, audiocasts and more, please visit Apple's App Store for your iPhone and iPad, or Google Play for your Android mobile device.

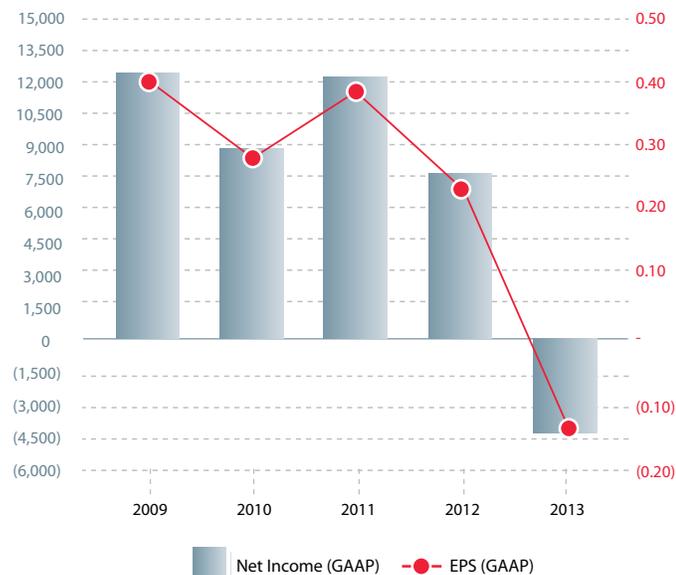
### Annual Revenues 2009–2013 (in thousands \$U.S.)



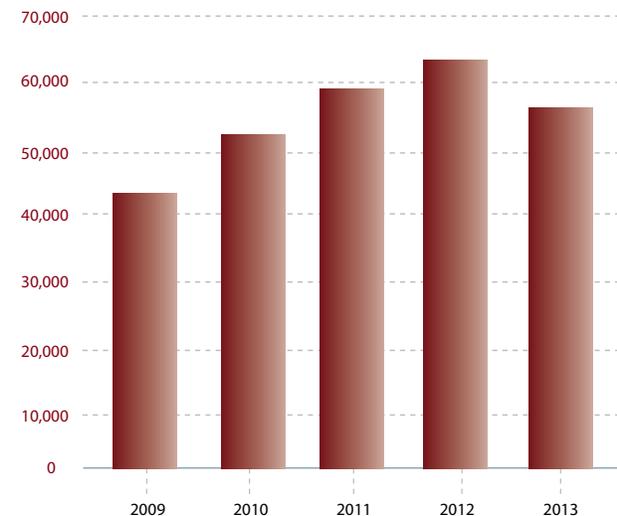
### Operating Cash Flow & Cash and Investments 2009–2013 (in thousands \$U.S.)



### Annual Net Income & EPS (GAAP) 2009–2013 (in thousands \$U.S., except per share amounts)



### Shareholders' Equity 2009–2013 (in thousands \$U.S.)



May 2014

## CEO Letter to Shareholders

Dear Fellow Shareholders,

2013 was a transformative year for ClickSoftware. Macro market trends within the software industry drove a growing interest for cloud-based solutions, including from large enterprises. Our ability to offer a best of breed solution both on premise and in the cloud is a key competitive advantage for ClickSoftware. This capacity enables us to expand our market share in tandem with the gradual shift toward cloud, and has generated a strong pipeline of new business opportunities for the year ahead.

During the first three quarters of the year, the shift to the cloud led to smaller initial deal sizes which impacted up-front license revenues and ultimately affected our quarterly financial results. However, the strong demand for our cloud-based SaaS (Software as a Service) products, which we witnessed toward the end of the year, exceeded even our own expectations. As a result, we posted record revenues in the fourth quarter and saw a remarkable improvement in our business. Even more encouraging was the significant improvement we saw in our win rate against the competition, which was quite convincing. In total, for the full year of 2013, we had 54 new customer wins, which is 59% above the 34 new customers that chose ClickSoftware in 2012. Out of these 54 new customers, 24, or 44%, were cloud customers, more than double the number of new cloud customer wins in 2012.

With the acquisition of Xora in early 2014, and the expansion of apps in our own ClickAppStore, we now have one of the richest portfolios of business apps in the cloud. The Xora acquisition will also extend ClickSoftware's market reach into the SMB (Small and Medium Businesses) market, and opens up distribution channels through leading wireless carriers.

As a strategy, we focus on what we do best: the business functionality layer of software to manage service companies, and accordingly we set the boundaries of our products. Simultaneously, we ensure that our products will work in harmony with platforms and infrastructure of the industry leading vendors. Take mobility for example: our apps are designed to run on IBM Mobile First [Worklight], Salesforce1 from Salesforce.com, and SUP from SAP, and we were one of the first vendors to offer apps on these platforms.

As new technologies were emerging right and left over recent years, I have been updating you on directions we are taking and where we are investing. Many of the initiatives we invested in are now converging in perfect synchronization with industry trends. HTML5, for example, gives us device agnostic capabilities which, in a world of BYOD and where almost every quarter new devices are appearing on the market, is a great asset and unique differentiator. Our mobile apps run on Android and Apple iOS and have recently been certified to run on Windows8 – the demand for which seems to be growing every day in business mobility. Furthermore, with our unique Responsive UI technology, our apps adapt themselves automatically to the size of the screen of the mobile device, with no user involvement.

We have also created ClickButler, our award winning technology for context-aware intelligent personal assistants for mobile devices. We started this initiative several years ago and it is now perfectly aligned with industry trends for mobile-based personal assistants. ClickButler is not just

one or a few limited apps. We enable ClickButlers, as a way of life, in every app we develop, essentially creating a virtual personal assistant that shadows the user like his or her twin persona, anticipates his or her needs and acts on them proactively. It never takes a vacation, nor goes to sleep. It is available 24/7 to minimize inefficient use of time on mobile devices and allows people to focus more time on delivering business results than on using their mobile devices. Numerous business scenarios show how this practical and powerful tool improves customer delight, and actually saves time and increases productivity.

ClickSoftware's innovative technology was recognized as being among the best of the best for service to utilities when we won a Bronze Stevie® Award in the 2013 App - Utilities & Services category. Additionally, ClickSoftware's ServiceOptimization Suite and ClickAppStore have been named winners in the 11th Annual Mobile Star Awards™ program. As this letter is going to print, we were informed that our Xora business unit won the North American Frost & Sullivan Award for Customer Value Leadership, and that our SHOUT app for business collaboration won 1st place in the Mobile App Throwdown competition at IBM's 2014 Impact event. We believe these awards are a testament to the high level of customer satisfaction and customer loyalty that our customers experience.

So the story of ClickSoftware is much bigger than it was. Today ClickSoftware has the largest and richest variety of products and apps to cover the end-to-end needs of service providers of all sizes - from 5 employees to 50,000. Apps can be purchased alone as point solutions for well-focused business needs, or in bundles for bigger needs or larger overall transformation projects. This gives us more flexibility in penetrating new customers.

ClickSoftware was and is today the premium choice for companies looking to **delight their customers and achieve operational excellence**. The velocity with which we are winning cloud customers clearly proves that ClickSoftware is executing very well the transition of large companies to cloud-based solutions.

To summarize, with the new cloud wins we have been reporting over past quarters and the installed base of Xora, we believe that we are now the #1 cloud company in our space, both in terms of size of the user-base in the cloud, and the spectrum of our state-of-the-art cloud solutions we offer for companies of all sizes.

I would like to thank our customers, partners, employees and shareholders for your ongoing support.

Respectfully,



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**Moshe BenBassat, Ph.D.**  
Founder and Chief Executive Officer

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2013

Commission file number: 000-30827

**ClickSoftware Technologies Ltd.**  
(Exact name of Registrant as specified in its charter)

**State of Israel**  
(Jurisdiction of incorporation or organization)

**Azorim Park, Oren Building**  
**94 Em Hamoshavot Road**  
**Petach Tikva 4970602 Israel**  
(Address of principal executive offices)

**Shmuel Arvatz**  
**Tel. +972-3-7659-400**  
**Fax +972-3-7659-401**

**Azorim Park, Oren Building**  
**94 Em Hamoshavot Road**  
**Petach Tikva 4970602 Israel**  
(Name, Telephone and/or Facsimile number and Address of Company Contact Person)

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

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
Ordinary Shares, par value of NIS 0.02	Nasdaq Global Select Market

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

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

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

32,494,575 Ordinary Shares, par value NIS 0.02 per share

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

Yes  No

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

Yes  No

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

Yes     No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes     No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Act).

Large Accelerated Filer     Accelerated Filer     Non-Accelerated Filer

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

U.S. GAAP

International Financial Reporting Standards as issued by the International Accounting Standards Board

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

Item 17                       Item 18

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

Yes     No

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## INTRODUCTION

Unless otherwise indicated, all references to the "Company," "we," "our" and "ClickSoftware" refer to ClickSoftware Technologies Ltd. and its subsidiaries. References to "U.S. dollars" and "\$" are to the lawful currency of the United States of America, and references to "NIS" are to new Israeli shekels. References to "Ordinary Shares" are to our Ordinary Shares, par value of NIS 0.02 per share.

We do not endorse or adopt any third-party research or forecast firms' statements or reports referred to in this annual report and assume no responsibility for the contents or opinions represented in such statements or reports, nor for the updating of any information contained therein.

This annual report on Form 20-F includes statistical, market and industry data and forecasts which we obtained from publicly available information and independent industry publications and reports that we believe to be reliable sources. These publicly available industry publications and reports generally state that they obtain their information from sources that they believe to be reliable, but they do not guarantee the accuracy or completeness of the information. Although we believe that these sources are reliable, we have not independently verified the information contained in such publications.

## SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This annual report contains express or implied "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and other U.S. Federal securities laws. These forward-looking statements include, but are not limited to, those statements regarding future results of operations, future changes in our expenses and investments, average deal size and number of new deals, the results and expected benefits of our acquisition of Xora, capitalization of cloud services momentum, trend information, sufficiency of our office space, visibility into future periods, expected growth, expected rates of growth, expansion into new territories, and expectations regarding future closing of contracts, receipt of orders, recognition of revenues, exploration of acquisitions, future tax rates, reduction of expenses, revenue trends, collection of accounts receivable and deferred revenues. In some cases, forward-looking statements are identified by terminology such as "may," "will," "could," "should," "expects," "plans," "anticipates," "believes," "intends," "estimates," "predicts," "potential," or "continue" or the negative of these terms or other comparable terminology. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results or performance to differ materially from those projected. Achievement of these results by ClickSoftware may be affected by many factors, including, but not limited to, risks and uncertainties regarding the general economic outlook, the length of or changes in ClickSoftware's sales cycle, ClickSoftware's ability to close sales to potential customers in a timely manner and maintain or strengthen relationships with strategic partners, the timing of revenue recognition, foreign currency exchange rate fluctuations, and ClickSoftware's ability to maintain or increase its sales pipeline. The forward-looking statements contained in this annual report are subject to risks and uncertainties, including those discussed under Item 3.D. – "Risk Factors" and in our other filings with the Securities and Exchange Commission, or the SEC. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Except as otherwise required by law, ClickSoftware is under no obligation to (and expressly disclaims any such obligation to) update or alter its forward-looking statements whether as a result of new information, future events, or otherwise.

## PART ONE

### ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

### ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

### ITEM 3. KEY INFORMATION

#### 3.A. Selected financial data

Our historical consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States and are presented in U.S. dollars. The selected historical consolidated financial information as of December 31, 2012 and 2013 and for each of the years ended December 31, 2011, 2012 and 2013 have been derived from, and should be read in conjunction with, the consolidated financial statements of ClickSoftware Technologies Ltd. and notes thereto appearing elsewhere in this annual report. The selected financial data as of December 31, 2009, 2010 and 2011 and for each of the years ended December 31, 2009 and 2010 have been derived from the audited financial statements of ClickSoftware Technologies Ltd. not included in this annual report.

The information presented below is qualified by the more detailed historical consolidated financial statements set forth in this annual report, and should be read in conjunction with those consolidated financial statements, the notes thereto and the discussion under Item 5 – "Operating and Financial Review and Prospects" - included elsewhere in this annual report.

#### **Consolidated Statement of Operations Data – Year Ended December 31** *(in thousands of U.S. dollars, except share and per share data)*

	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Revenues	\$ 103,181	\$ 100,046	\$ 87,087	\$ 71,019	\$ 61,123
Cost of revenues	44,307	38,871	31,696	26,913	20,831
Gross profit	58,874	61,175	55,391	44,106	40,292
Research and Development, net	15,970	13,146	9,019	7,920	6,499
Selling and Marketing	39,706	31,977	23,382	19,213	16,240
General and Administrative	9,121	8,779	7,386	6,747	6,423
Impairment of goodwill	-	-	939	-	-
Total operating expenses	64,797	53,902	40,726	33,880	29,162
Operating (loss) income	(5,923)	7,273	14,665	10,226	11,130
Other income	-	110	-	-	-
Financial income, net	839	274	7	189	380
Net (loss) income before taxes	(5,084)	7,657	14,672	10,415	11,510
Taxes on income (Tax benefit)	(924)	169	2,462	1,370	(1,004)
Net (loss) income	\$ (4,160)	\$ 7,488	\$ 12,210	\$ 9,045	\$ 12,514
Basic net (loss) earnings per share	\$ (0.13)	\$ 0.24	\$ 0.39	\$ 0.30	\$ 0.43
Diluted net (loss) earnings per share	\$ (0.13)	\$ 0.23	\$ 0.38	\$ 0.28	\$ 0.40
Dividend declared per share	\$ 0.21	\$ 0.24	\$ 0.32	-	-
Shares used in computing basic net (loss) earnings per share	32,048,030	31,545,435	31,014,373	30,415,679	29,400,973
Shares used in computing diluted net (loss) earnings per share	32,048,030	32,837,789	32,226,883	32,037,399	31,137,238

## Consolidated Balance Sheet Data – Year Ended December 31

(in thousands of U.S. dollars, except for share data)

	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Working capital	\$ 54,444	\$ 58,565	\$ 54,726	\$ 48,710	\$ 37,666
Total assets	97,568	94,469	90,632	79,827	66,449
Long-term liabilities	9,522	5,968	5,855	5,208	5,461
Shareholders' equity	\$ 56,919	\$ 62,918	\$ 59,104	\$ 54,088	\$ 42,658
Number of shares outstanding	32,494,575	31,654,942	31,368,888	30,634,227	30,244,330

### 3.B. Capitalization and indebtedness

Not applicable.

### 3.C. Reasons for the offer and use of proceeds

Not applicable.

### 3.D. Risk factors

In conducting our business, we face many risks that may interfere with our business objectives. Some of these risks could materially and adversely affect our business, financial condition and results of operations. In particular, we are subject to various risks resulting from changing economic, political, industry, business and financial conditions. The risks and uncertainties described below are not the only ones we face.

You should carefully consider the following factors and other information in this annual report before you decide to invest in our Ordinary Shares. If any of the negative events referred to below occur, our business, financial condition and results of operations could suffer. In any such case, the trading price of our Ordinary Shares could decline, and you may lose all or part of your investment.

#### Risks Related to Our Business

##### *We face competition, which could make it difficult for us to achieve our targets.*

Competition, particularly direct competition, continues to intensify as current competitors expand their product offerings and new companies attempt to enter the market. In addition, smaller competitors have been acquired by large organizations with broader product offerings, or been awarded venture funding, promoting competition on price and away from value. The industries where we are active have witnessed a substantial amount of merger and acquisition activity over the past few years and this trend of industry consolidation will likely continue, particularly as larger, better capitalized companies seek to acquire smaller, weaker rivals that have been adversely affected by the economic downturn.

Competitors vary in size and in the scope and breadth of the products and services they offer. Some of our current and potential competitors are among the largest and most well capitalized software companies in the world and have significant competitive advantages over us, including greater name recognition, longer operating histories, larger customer bases and significantly greater financial, technical, marketing, public relations, sales, distribution and other resources than us. Because the market for workforce management and optimization software is evolving, we expect additional competition from other established and emerging companies if this market continues to develop and expand. For example, we could face competition from our strategic partners or from other companies that may in future decide to enter and compete in our market. In particular, since our contracts with large resellers generally do not include non-competition provisions, it may be easier for these partners to compete with us in the future. SAP A.G. acquired Syclo in 2012, one of our competitors in the mobility space. SAP has its own offering which competes with our ClickSchedule product. Another of our partners, IBM, recently acquired Worklight Ltd., a potential mobility competitor. We may also face competition from Accenture LLP.

We offer mobility and shift-planning solutions for which competition may be more intense than our traditional offerings. Mobility is oriented more towards the mass market which is more commodity oriented than our traditional markets. Competition could result in price reductions, fewer customer orders, reduced gross margin

and loss of market share, any of which could cause our business, financial condition and results of operations to suffer. We may not be able to compete successfully with existing or future competitors. If we fail to compete successfully against current and future competitors, our business, financial condition and results of operations would be materially and adversely affected.

At the lower end of our potential customer base for field service management, there are a large number of vendors offering basic services such as dispatching tasks and gathering task execution data via mobile forms. Some customers may find such solutions appealing. Therefore, if we are unable to educate the market about the higher value of our solutions, or if we cannot deliver simple-to-implement solutions that address such basic needs, we may be at a disadvantage when selling to these customers.

***Our market may experience rapid changes in customer preferences or technology that could impact our revenues or require us to redesign our products, which would result in increased research and development expenses.***

The market for our products is competitive and rapidly changing. We have detected a pattern in the IT market towards smaller initial transactions relative to the approach we saw in prior years. This has led to a smaller initial transaction size with new customers, and will require us to scale up the number of our transactions in order to maintain our growth.

The pattern of smaller initial deal size coincides with the expected shift from traditional on-premises deployment of our products to the cloud-based software-as-a-service, or SaaS, model. This shift has occurred faster than we expected. Although this shift has long-term benefits in the form of a more stable future revenue stream for us, the tendency of customers to shift to the SaaS model in order to lower up-front investment does impact the Company's short term growth rate. SaaS, combined with general macro-economic concerns, has moderated buyers' tolerance for risk versus price, thereby encouraging a smaller initial deployment size than we have seen in the past.

Further, as customers become more acquainted with cloud-based SaaS, there is a greater expectation for low initial financial investment. In order to remain competitive and satisfy low initial customer outlay, it may require us to propose a low-cost implementation which could impact our consulting revenues.

Our market is also characterized by rapid technological change, dynamic customer needs and frequent introductions of new products and product enhancements. If we fail to anticipate or respond adequately to technology developments and customer requirements, or if our product development or introduction is delayed, our business will suffer. Client product requirements can change rapidly as a result of computer hardware and software innovations or changes in and the emergence, evolution and adoption of new industry standards. The actual or anticipated introduction of new products has resulted, and will continue to result, in some reformulation of our product offerings. Technology and industry standards can make existing products obsolete or unmarketable or result in delays in the purchase of such products. In the mobility sector, technological changes with regard to platforms and operating systems with which we integrate are typically rapid. As a result, the life cycles of our products are difficult to estimate. We must respond to developments rapidly and continue to make substantial product development investments. We have previously experienced delays in introducing new products and features, and we may experience delays in the future that could impair our revenue and operating results. Our business, financial condition and results of operations will be materially and adversely affected if we fail to respond to our rapidly changing market by enhancing our product functionality to meet our customers' needs.

***The market may not accept our products and services.***

Historically, all of our operating revenue has come from sales of, and services related to, our end-to-end optimization suite of products, or our Service Optimization Suite, which includes ClickSchedule, ClickAnalyze, ClickPlan, ClickMobile, ClickRoster, ClickForecast, ClickLocate and ClickContact. Our packaging includes three distinct entry points for a customer organization that has medium-to-large size or requirement complexity: a Field Service Suite, a Mobility Suite and a Roster Suite. We also offer our Service Optimization Suite and Mobility Suite under a cloud-based model. For customers with smaller sizes and requirement complexity, we offer our ClickExpress solution under a cloud-based model. We continually aim to improve and enhance our products and services to meet market requirements. Our growth depends on the market acceptance of these products and services, and in particular the pace at which the market adopts our cloud-based offerings. If our products and services do not achieve continued customer acceptance, our business, financial condition and results of operations would be materially and adversely affected.

***Failure to fully develop or maintain key alliance relationships could limit our ability to sell additional licenses, thereby decreasing our revenues and increasing our sales and marketing expenses.***

Our success in penetrating our target markets depends, in part, on our ability to develop and maintain relationships with key value-added resellers, agents, systems integrators and distribution partners. We have entered into agreements with third parties relating to the integration of our products with their product offerings, and distribution, reselling and consulting services. We derive revenues from these agreements, but may not be able to continue to do so in the future. Also, our marketing strategy includes selling through distributors, value-added resellers and agents, as well as direct selling by our own sales force. We may not be successful in extending the terms of our various agreements or establishing similar relationships with these partners if our current agreements expire or are terminated. If we fail to fully develop or maintain key alliance relationships, we could materially and adversely affect our business, financial condition or results of operations.

***Our quarterly operating results are subject to significant fluctuations.***

Our quarterly operating results are subject to significant fluctuations and are difficult to predict. Historically, a significant percentage of our quarterly revenues has been derived from orders placed towards the end of a given quarter. If sales forecasted from a specific customer or partner for a particular quarter are not realized in that quarter, we may not be able to generate revenues from alternate sources in time to compensate for the shortfall. Also, frequently our quarterly revenue performance depends upon a sale of significant size to a single customer. Due to the relatively large size of some orders, a lost or delayed sale could have a material adverse effect on our quarterly revenue.

The factors that may cause significant fluctuations in our quarterly operating results include, but are not limited to, the following:

- the volume, timing and recognition of customer orders;
- internal budget constraints and approval processes of our customers;
- the length and unpredictability of our sales cycle;
- the recognition of a portion of our revenues on a contract accounting basis;
- the recent pattern of smaller initial deal size coinciding with a shift from traditional on-premises deployment of our products to the cloud-based SaaS model;
- the indirect nature of some of our sales efforts through our channel and strategic partners;
- the mix of revenue generated by product licenses and professional services;
- new product introductions or enhancements by us or our competitors;
- price and product competition;
- changes to our pricing strategies and those of our competitors;
- inclusion of revenues following existing and future acquisitions of third parties;
- timing and amount of sales and marketing expenses;
- changes in the composition and success of our business and partner relationships;
- technical difficulties affecting the operation of our software;
- foreign currency exchange rate fluctuations;
- general economic conditions, including a prolonged economic recession; and
- difficulties in collecting accounts receivable.

Because of the numerous factors that may cause significant fluctuations in our quarterly operating results, we believe that period-to-period comparisons of our results of operations are not necessarily meaningful and that such comparisons should not be relied upon as an indication of future performance.

***We may not be able to achieve and maintain the same level of profitability as we achieved in the past.***

We recorded a profit for each of the fiscal years 2006 through 2012, and incurred a net loss in 2013. We may not generate sufficient revenues to achieve profitability in the future. To achieve profitability, we must increase our revenues while controlling our expenses. Although we implemented cost reduction measures for 2014, some of our expenses, such as administrative and management payroll and rent and utilities, are fixed in the short term, must be incurred in advance of when revenue is generated and cannot be quickly reduced if we experience revenue declines. Therefore, if our projected revenue does not meet our expectations, we are likely to experience

an even larger adverse impact on our results. As a result, we must generate and maintain growing revenues to achieve and maintain profitability, which we may not accomplish.

***Our sales cycle is variable, often long, dependent on factors outside our control and involves investment of significant resources on our part, but may never result in actual sales.***

The length of our sales cycle – the period between initial contact with a potential customer and the signing of a license and related agreements - has historically been lengthy and variable, typically lasting from three to nine months. We generally must educate our potential customers about the use and benefit of our products and services, which can require the investment of significant time and resources, causing us to incur most of our selling and marketing expenses in advance of a potential sale. In addition, a number of companies decide which products to buy through a request for proposal process. In those situations, we run the risk of investing significant resources in a proposal that results in a competitor obtaining the desired contract from the customer or in a decision by a customer not to proceed. Sales of licenses are subject to a number of risks outside our control, including budgeting, approval and competitive evaluation processes that typically accompany significant capital expenditures. Potential customers consider many factors in evaluating our products, and the length of time a customer devotes to evaluation, contract negotiation and budgeting processes varies significantly from company to company. In certain circumstances, we may invest significant resources in a sales process that does not result in actual sales.

***Our implementation cycle depends on factors outside our control.***

Depending on the nature and specific needs of a customer, the implementation of our products typically takes six to twelve months. During the implementation cycle, there are a number of factors beyond our control that may affect the implementation timeline, including a customer's budgetary constraints and internal acceptance reviews, the success and continued internal support of a customer's own development efforts, the nature, size and specific needs of a customer, the possibility that a customer cancels an order and the level and quality of service provided by third-party implementation and professional services partners. Long implementation cycles may delay the recognition of revenue as some of our customers engage us to perform system implementation services, which can defer revenue recognition for the related software license revenue. In addition, when we experience long implementation cycles, we may incur costs at a higher level than anticipated, which may reduce the anticipated profitability of a given implementation. We continue in our efforts to simplify the implementation process. However, because our implementation cycle depends on factors outside of our control, we may experience delays or other complications with our implementation timeline that may materially and adversely affect our business, financial condition and results of operations.

***Any future mergers with or acquisitions of companies, products or technologies and the resultant integration process may distract our management and disrupt our business.***

One of our business strategies is to consider strategic partnerships, alliances, mergers and/or acquisitions of complementary businesses, products and technologies. Mergers with or acquisitions of companies, products or technologies, such as our recent acquisition of Xora, Inc. (Xora) as described elsewhere in this annual report, involve a number of risks, including:

- the diversion of management time and resources;
- the difficulty of assimilating the operations and personnel of the merged or acquired companies;
- the possibility the business cultures will not be compatible;
- the difficulty of incorporating acquired technology and rights into our products and services;
- unanticipated expenses related to integration of the acquired companies;
- difficulties in implementing and maintaining uniform standards, controls and policies;
- the impairment of relationships with employees and customers as a result of any integration of new personnel;
- potential inability to retain, integrate and motivate key management, marketing, technical sales and customer support personnel;
- potential unknown liabilities associated with acquired businesses;
- expending significant cash;
- incurring substantial debt;

- dilution of current shareholders' percentage ownership (if equity securities are issued as consideration);
- assumption of contingent liabilities; and
- impairment of goodwill and other assets acquired.

Pursuant to our business strategy, we will continue to consider additional merger or acquisition transactions.

Any future merger and acquisition activity could distract our management and disrupt our business, thereby materially and adversely affecting our business, financial condition or results of operations.

***If we fail to expand our relationships with third parties that provide implementation and professional services to our customers, we may be unable to increase our revenues.***

In order for us to focus more effectively on our core business of developing and licensing software solutions, we must continue to establish relationships with third parties that provide implementation and professional services to our customers. Third-party implementation and professional services firms can be influential in the choice of optimization applications by new customers. These third parties are under no obligation to recommend or support our products; they could recommend or give higher priority to the products of other companies or to their own products. If we are unable to establish and maintain effective, long-term relationships with implementation and professional services providers, or if these providers do not meet the needs or expectations of our customers, we may be unable to increase our revenues, which would materially and adversely affect our business, financial condition and results of operations.

Even if we establish relationships with these third party implementation and professional services firms, we may be unable to attract sufficient focus and resources from them to meet all of our customers' needs as a result of the limited resources and capacities of many third-party providers. If sufficient resources are unavailable, we could be required to provide these services internally, which could limit our ability to meet other demands. We cannot control the level and quality of service provided by these partners.

***Our revenues still depend on a small number of products, and in particular ClickSchedule, and our results may be vulnerable to unexpected shifts in demand.***

While other offerings gained momentum (both in absolute terms and relative to overall revenue) ClickSchedule still accounted for the majority of our license revenues in each of years ended December 31 2013, 2012 and 2011 and we expect that this will be the case in the foreseeable future. Accordingly, any decline in the demand for ClickSchedule will have a material adverse effect on our license revenues. A decline in the demand for ClickSchedule may also reduce revenues derived from our other products.

***Failure to fully develop or maintain key supplier relationships could limit our ability to sell additional licenses, thereby decreasing our revenues and increasing our sales and marketing expenses.***

Our success in penetrating our target markets depends, in part, on our ability to develop and maintain key relationships with software vendors. For example, we depend on certain suppliers for the development, supply and support of third-party software components that are integrated into our products. We do not have long-term contracts with some of these suppliers, and they are not obligated to provide us with products or services for any specified period of time. If we fail to maintain these relationships, our ability to sell additional licenses could be limited. Furthermore, if any of our software vendors cease production, cease operations or fail to timely deliver orders, we could be required to provide these services internally, which could limit our ability to meet other demands and we may not be able to meet our delivery obligations to our customers, in which case we could lose revenues and harm our customer relationships. If we fail to fully develop or maintain key supplier relationships, we could materially and adversely affect our business, financial condition or results of operations.

***Our risk from exposure to foreign currency fluctuations is increasing, and we may not be able to fully mitigate the risk.***

We are exposed to movements in foreign currency exchange rates since we realize our revenues and expenses in several currencies and we translate foreign currencies into U.S. dollars for reporting purposes. Our primary exposures have related to operating expenses and sales, principally in Europe and Israel, which were not U.S. dollar-denominated. In 2013, the rate of growth of our costs increased in part due to exchange rate fluctuations and weakness in the U.S. dollar compared to NIS that significantly increased the cost of our Israel-based operations. We continue to expand our global operations, and revenue recognized in currencies other than U.S.

dollars may increase. In 2013, 65% of our expenses and 49% of our revenues were incurred in non-U.S. dollar currencies. We incur a portion of our expenses, principally with respect to salaries and related personnel expenses in Israel, in NIS. In 2013, 46% of our expenses were incurred in NIS. Currency fluctuations in the major currencies in which we operate could materially and adversely affect our business, financial condition and results of operations. In addition, we have balance sheet exposure related to foreign net assets. Although we engage in non-speculative hedging transactions from time to time to minimize the impact of changes in foreign currency exchange rates on earnings, we may not be able to fully mitigate these risks.

***Our cash may be subject to a risk of loss and we may be exposed to fluctuations in the market values of our portfolio investments and in interest rates.***

Our assets include a significant component of cash, as well as marketable securities. We adhere to an investment policy which requires investment in high-quality investment-grade securities provided, however, that up to \$10 million of our total cash and investments may be invested in equity of companies that have a policy to regularly distribute dividends or in Exchange Traded Funds, or ETFs, of a similar nature. We believe that our cash is held in institutions whose credit risk is minimal and that the value and liquidity of our marketable securities are accurately reflected in our consolidated financial statements as of December 31, 2013. However, nearly all of our cash and marketable securities are not insured by the Federal Deposit Insurance Corporation, or the FDIC, or similar governmental deposit insurance outside the United States. Therefore, our cash and any marketable securities that we now hold or may acquire in the future may be subject to risks, including the risk of loss or of reduced value or liquidity, particularly in light of the recent volatility and worldwide pressures in the financial and banking sectors. In the future, should we determine that there is a decline in value of any of our portfolio securities which is not temporary in nature, this would result in a loss being recognized in our consolidated statements of operations.

***We depend on key personnel, and the loss of any key personnel could affect our ability to compete and impair our ability to attract additional key personnel.***

Our future success depends on the continued service of our executive officers, including Moshe BenBassat, Shmuel Arvatz, Zvi Piritz and Stephen Timms, and other key sales and marketing, product development and professional services personnel. Competition for these employees can be intense, including in a number of our key markets and locations, such as Israel, India, the United States, the United Kingdom and Australia. More generally, we may be unable to attract and retain a sufficient number of highly qualified professional services personnel to meet our business needs.

Customers that license our software typically engage our professional services organization to assist with the installation and operation of our software applications. Our professional services organization also typically assists with the installation and implementation of our customers' software systems. Future growth in licenses of our software will depend, in part, on our ability to continue providing customers with these services. To the extent that we receive several large orders simultaneously or in close proximity to one another, we could place added strain on our existing personnel. The market for the qualified personnel we require is very competitive because of the limited number of people available with the necessary technical and sales skills and understanding of our products and technology. If we are unable to maintain and expand our professional services organization, our ability to support our service business would be limited.

The services of our key personnel would be difficult to replace and the loss of any of these employees could harm our business significantly. Although we have employment or consulting agreements with our executive officers that generally require 60 to 90 days notification prior to departure, our relationships with these officers and key employees are at will and can be terminated by either party without cause. The loss of any of our key personnel could harm our ability to execute our business strategy and remain competitive.

***Global economic conditions may adversely affect our business.***

Our operations and performance depend on worldwide economic conditions and their impact on levels of business spending, which have deteriorated significantly in many countries and regions and may remain depressed for the foreseeable future. This may adversely affect the budgeting and purchasing behavior of our customers and our partners' customers, which could adversely affect our product sales.

Continuing uncertainties in the macroeconomic conditions may adversely affect the ability of our customers, suppliers and channel partners (e.g., distributors and resellers) to obtain financing for significant purchases and operations and to perform their contractual obligations with us. While in 2013 there was a slow recovery in the

global economy, in 2011 and 2012 we encountered a slowdown in the EMEA region. As a result, we could encounter, among other adverse effects, a decrease in or cancellation of orders for our products and services, and an increase in additional reserves for uncollectible accounts receivable being required.

***If our relationships with our key customers are terminated, our revenues will decline and our business will be adversely affected.***

During 2013, our five largest customers together accounted for approximately 26% of our revenues. If for any reason, our relationship with a key customer is terminated, or if any of our key customers reduces purchases of our products, then our business, financial condition and results of operations could be materially and adversely affected. The impact of the termination or reduction in demand of a key customer would be intensified if we were unable to increase sales to other customers to offset this termination or reduction in demand. We expect that a significant portion of our future revenues will continue to be derived from a small number of customers.

***Our products could be susceptible to errors or defects or contain inaccurate data from third-party vendors.***

Complex software products, such as ours, often contain errors or defects, particularly when first introduced or when new versions or enhancements are released. In the past, some of our products have contained errors and defects that have delayed implementation or required us to expend additional resources to correct the problems. Testing of our products is particularly challenging because it is difficult to simulate the wide variety of customer environments into which our products are deployed. Despite internal testing, testing by current and potential customers and the history of use by our installed base of customers, our current and future products may contain defects or errors. We also commit to service level agreements in connection with our cloud-based offerings, and any excessive downtime may harm the perception of our offerings by our customers. With regard to our entire suite of products and services, defects or errors could result in adverse customer reaction and publicity, damage to our reputation, diversion of resources, increased service and maintenance costs, loss of market demand, loss of market share, loss of potential new customers, lost revenues, liability or a delay in market acceptance of these products, any of which could have a material adverse effect on our business, financial condition and results of operations.

We host our cloud-based offerings on Amazon Web Services, or AWS, and are dependent on the continued reliability of AWS. The performance of our products also depends, in part, upon the accuracy and continued availability of third-party data. We rely on third parties that provide information such as street and address locations and mapping functions that we incorporate into our products. If these parties do not provide accurate information, or if we are unable to maintain our relationships with them, our reputation and competitive position could suffer and we could be unable to develop or enhance our products as required.

***Security breaches could disrupt our information technology systems or expose us to liability and our reputation and business could suffer.***

A breach of our information technology systems and/or infrastructure by persons with or without authorized access could disrupt our operations. We could also experience business interruption, information theft and/or reputational damage from cyber-attacks, which may compromise our systems and lead to data breaches either internally or at our third party infrastructure providers. Although we have invested in measures to reduce these risks, these measures may not be successful in preventing compromise and/or disruption of our information technology systems and related data.

We retain sensitive data, including intellectual property, books of record and personally identifiable information, on our networks. Customers require us to adhere to various data protection regulations throughout the world. It is critical to our business strategy that our infrastructure and other infrastructure we use to host our solutions remain secure and are perceived by customers and partners to be secure. Despite our security measures, our infrastructure and third party infrastructure we use to host our solutions may be vulnerable to attacks by hackers or other disruptive problems. Our cloud-based offering may create additional vulnerabilities due to the inherent risks of doing business on the internet. Any such security breach may compromise information stored on our networks. Such an occurrence could negatively affect our reputation as a trusted provider of solutions and hosting such solutions by adversely affecting the market's perception of the security or reliability of our products or services.

***Our intellectual property could be used by third parties without our consent because protection of our intellectual property is limited.***

Our success and ability to compete substantially depend upon our internally developed technology, which we protect through a combination of trade secrets, copyrights, trademarks, patents and intellectual property law, together with non-disclosure and invention assignment agreements. These legal protections are limited. Unauthorized parties may attempt to copy or otherwise obtain and use our products or technology. Policing unauthorized use of our products and technology is difficult and costly, particularly in countries where the laws may not protect our proprietary rights as fully as in the United States. The steps we have taken may not prevent infringement or misappropriation of our intellectual property rights.

Our end-user licenses are designed to prohibit unauthorized use, copying or disclosure of our software and technology in the United States, Israel and other countries. However, these provisions may be unenforceable under the laws of some jurisdictions. Unauthorized third parties may be able to copy portions of our products, reverse engineer or obtain and use information and technology that we regard as proprietary. In addition, some of our licensed users may allow additional unauthorized users to use our software, and if we do not detect such use, we could lose potential license fees. In addition, as we deepen our ties with our channel and strategic partners, the number of people who are exposed to and interact with our software and other intellectual property increases. Despite our best efforts to protect our intellectual property, our channel or strategic partners, or their employees or customers, may copy portions of our products or otherwise obtain and use information and technology that we regard as proprietary. Our channel or strategic partners might also improperly incorporate portions of our technology into their own products or otherwise exceed the authorized scope of their licenses to our technology. If we are unable to successfully detect infringement and/or to enforce our intellectual property rights, our competitiveness may be adversely affected.

***Our technology and other intellectual property may be subject to infringement claims.***

Substantial litigation regarding technology rights and other intellectual property rights exists in the software industry both in terms of infringement and ownership issues. We expect that software products may be increasingly subject to third-party infringement or ownership claims as the number of competitors in our industry segment grows and the functionality of products in different industry segments overlaps. A successful claim of patent, copyright or trademark infringement or conflicting ownership rights against us could require us to make changes in our business.

Third parties may make a claim of infringement or conflicting ownership rights against us with respect to our products and technology. Any claims, with or without merit, could:

- be expensive and time-consuming to defend;
- divert management's attention and resources;
- cause product shipment and installation delays; or
- require us to enter into royalty or licensing agreements to obtain the right to use a necessary product or component, which may not be available on commercially reasonable terms, if at all.

We also generally indemnify our customers against claims that our products infringe the intellectual property rights of others. We have only conducted a partial search for existing patents and other intellectual property registrations, and our products may infringe issued patents. In addition, because most patent applications are not publicly disclosed until sometime after the application is filed, applications may have been filed that relate to our products. If a successful claim was made against us and we failed to commercially develop or license a substitute technology, our business, financial condition and results of operations could be materially and adversely affected.

***Our business is susceptible to numerous risks associated with international operations.***

We derive a substantial portion of our revenues from international sales and we maintain significant portions of our operations outside the United States. We expect international revenues to continue to account for a significant percentage of total revenues and we believe we must continue to expand our international sales and professional services activities to be successful. Our facilities are located in North America, Israel, the European continent, the United Kingdom, Australia, India and South Africa, and our executive officers and other key employees are dispersed throughout the world. This geographic dispersion requires significant management

resources that may place us at a disadvantage compared to our locally-based competitors. In addition, our international operations are generally subject to a number of risks, including but not limited to:

- foreign currency exchange rate fluctuations;
- longer sales cycles;
- multiple, conflicting and changing governmental laws and regulations;
- difficulties in staffing and managing foreign operations;
- licenses, tariffs and other trade barriers;
- loss of proprietary information due to piracy, misappropriation or weaker laws regarding intellectual property protection;
- difficulties in communication and monitoring compliance with our internal corporate controls and policy;
- difficulties in complying with a variety of foreign laws and legal standards;
- potentially adverse tax consequences;
- differing labor standards;
- expenses associated with customizing products for foreign countries;
- protectionist laws and business practices that favor local competition;
- difficulties in collecting accounts receivable; and
- political and economic instability.

Also, as we continue to expand into new geographic territories such as Latin America and Russia/Commonwealth of Independent States, adequate controls must be applied to our operations in these new territories in order to ensure compliance with all applicable laws and regulations.

One or more of these risks could harm our future international sales. Our business, financial condition and results of operations could be materially and adversely affected if we fail to manage the risk of doing business internationally.

***The large amount of intangible assets and goodwill recorded on our balance sheet may continue to lead to significant impairment charges in the future.***

We regularly review our long-lived assets, including identifiable intangible assets and goodwill, for impairment. Goodwill and acquired indefinite life intangible assets are subject to impairment review on an annual basis and whenever potential impairment indicators are present. Other long-lived assets are reviewed when there is an indication that impairment may have occurred. The amount of goodwill and identifiable intangible assets on our consolidated balance sheet is expected to increase significantly following the purchase of Xora as described in section 4.B below to about \$15 million and may increase further following future acquisitions. For example, in 2013, we recorded identifiable intangible assets impairment charges of \$0.2 million. Changes in market conditions or other changes in the future outlook of value may lead to further impairment charges in the future. In addition, we may from time to time sell assets that we determine are not critical to our strategy or execution. Future events or decisions may lead to asset impairments and/or related charges. Certain non-cash impairments may result from a change in our strategic goals, business direction or other factors relating to the overall business environment. Any significant impairment charges could have a material adverse effect on our results of operations.

**Investment Risks**

***If our tax structure is challenged or determined to be inappropriate, our tax liabilities could increase.***

We have created an intercompany tax structure based on accepted tax standards and in consultation with our tax advisors. We have potential tax exposures resulting from the varying application of statutes, regulations and interpretations, including exposures with respect to marketing, sales and distribution functions. Tax authorities in various jurisdictions may disagree with and challenge the amount of profits taxed in such jurisdictions, which may increase our tax liabilities and could have a material adverse effect on the results of our operations.

***Our Chief Executive Officer owns a significant percentage of our Ordinary Shares and therefore could significantly influence the outcome of actions.***

As of March 25, 2014, our Chief Executive Officer, Dr. Moshe BenBassat, beneficially owned approximately 6.9% of our outstanding Ordinary Shares in the form of Ordinary Shares and options for the purchase our Ordinary Shares. Dr. BenBassat's wife, Idit BenBassat, owns approximately 5.4% of our outstanding Ordinary Shares (of which Dr. BenBassat disclaims beneficial ownership and voting control). Due to the wide dispersion of our share capital, Dr. BenBassat may be able to influence certain matters requiring approval by our shareholders, including the election of directors, or a change of control of our Company. The influence of our Chief Executive Officer could adversely affect our stock price.

***If we are characterized as a passive foreign investment company, our U.S. shareholders will be subject to adverse tax consequences.***

If, for any taxable year, either, (1) 75% or more of our gross income is passive income or (2) 50% or more of our assets, averaged over the year and generally determined based upon value, including cash (even if held as working capital), produce or are held to produce passive income, we may be characterized as a "passive foreign investment company", or PFIC for United States federal income tax purposes. As a result of our cash position and the value of our assets, we may be deemed to be a PFIC for U.S. federal income tax purposes.

If we are characterized as a PFIC, our shareholders who are residents of the United States will be subject to adverse U.S. tax consequences. Our treatment as a PFIC could result in a reduction in the after-tax return to shareholders resident in the United States and may cause a reduction in the value of our shares. If we were to be treated as a PFIC, our shareholders will be required, absent certain elections, to pay an interest charge together with tax calculated at the then prevailing highest tax rates on ordinary income on certain "excess distributions" including any gain on the sale of Ordinary Shares. The consequences of holding shares in a PFIC are described below under "Additional Information – United States Federal Income Tax Consequences – Passive Foreign Investment Companies." Prospective investors should consult with their own tax advisors with respect to the tax consequences applicable to them of investing in our Ordinary Shares.

***We may raise additional equity from time to time, which could cause dilution for our existing shareholders or a decline in our share price.***

We may raise equity capital through the issuance of additional Ordinary Shares, subject to market and other conditions. The future issuances of Ordinary Shares could cause the market price of our Ordinary Shares to decline and could cause our existing shareholders to experience significant dilution.

### **Risks Relating to Our Location in Israel**

***We are incorporated in Israel and have important facilities and resources located in Israel, which could be negatively affected due to military or political tensions.***

We are incorporated under the laws of the State of Israel and our research and development facilities, as well as significant executive offices, are located in Israel. Although substantially all of our sales are to customers located outside of Israel, we are directly influenced by the political, economic and military conditions in Israel. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors and a state of hostility, varying in degree and intensity, has led to security and economic problems for Israel. Historically, Arab states have boycotted any direct trade with Israel and, to varying degrees, have imposed a secondary boycott on any company carrying on trade with, or doing business in, Israel. Although Israel has entered into agreements with Egypt, Jordan and Palestinian representatives, there have been continued and increasing difficulties in the relationship with the Palestinians and no prediction can be made as to whether a resolution of past problems will be achieved or as to the nature of any such resolution. Recent political uprisings and civil resistance demonstrations in various countries in the Middle East, including Egypt and Syria, are affecting the political stability of those countries. It is not clear how this instability, or the 'Arab Spring' in general, will develop and how it will affect the political and security situation in the Middle East. This instability may lead to deterioration of the political relationships that exist between Israel and these countries, and have raised concerns regarding security in the region and the potential for armed conflict. In addition, it is widely believed that Iran, which has previously threatened to attack Israel, has been stepping up its efforts to achieve nuclear capability. Iran is also believed to have a strong influence among extremist groups in the region, such as Hamas in Gaza and Hezbollah in Lebanon. The tension between Israel and Iran and/or these groups may escalate in the future and turn violent, which could affect the Israeli economy generally and us in particular. Any

armed conflicts, terrorist activities or political instability in the region could adversely affect business conditions and could harm our results of operations.

For example, any major escalation in hostilities in the region could result in a portion of our employees being called up to perform military duty for an extended period of time. Certain of our employees in our office in Israel are currently obligated to perform up to 36-45 days of annual reserve duty in the Israel Defense Forces and are subject to being called for active military duty at any time. The loss or extended absence of any of our key personnel due to these requirements could harm our business.

To date, these matters have not had a material and adverse effect on our business, financial condition or results of operations, but they may do so in the future.

We have taken measures to put in place a business continuity plan addressing foreseen scenarios. However these scenarios do not include the whole range of possibilities and combinations of circumstances.

***The tax benefits available to us require us to meet several conditions, and may be terminated or reduced in the future, which would increase our taxes.***

For the year ended December 31, 2013, we incurred a pre-tax loss and recorded a tax benefit due to increase in deferred tax benefits. We have benefited or currently benefit from a variety of government programs and tax benefits that generally carry conditions that we must meet in order to be eligible to obtain any benefit. Going forward we expect our effective tax rates to increase compared to effective tax rates in 2012 due to the utilization of tax losses carry forwards mostly in Israel as well as our move to a less favorable tax bracket in Israel.

If we fail to meet the conditions upon which certain favorable tax treatment is based, we would not be able to claim future tax benefits and could be required to refund tax benefits already received. Additionally, some of these programs and the related tax benefits are available to us for a limited number of years, and these benefits expire from time to time.

Any of the following could have a material effect on our overall effective tax rate:

- some programs may be discontinued;
- we may be unable to meet the requirements for continuing to qualify for some programs;
- these programs and tax benefits may be unavailable at their current levels;
- upon expiration of a particular benefit, we may not be eligible to participate in a new program or qualify for a new tax benefit that would offset the loss of the expiring tax benefit; or
- we may be required to refund previously recognized tax benefits if we are found to be in violation of the stipulated conditions.

Additional details are provided in "Item 5 – Operating and Financial Review and Prospects" under the caption "Taxes on income", in "Item 10 – Additional Information" under the caption "Israeli taxation, foreign exchange regulation and investment programs" and in Note 14 to our consolidated financial statements.

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

We are incorporated under the laws of the State of Israel. The rights and responsibilities of holders of our Ordinary Shares are governed by our memorandum of association, articles of association and by Israeli law. These rights and responsibilities may differ in some respects from the rights and responsibilities of shareholders in U.S. corporations. In particular, a shareholder of an Israeli company has a duty to act in good faith in exercising his or her rights and fulfilling his or her obligations toward the company and other shareholders and to refrain from abusing his or her power in the company, including, among other things, in voting at the general meeting of shareholders on certain matters. Israeli law provides that these duties are applicable in shareholder votes at the general meeting with respect to, among other things, amendments to a company's articles of association, increases in a company's authorized share capital, mergers and acquisitions and transactions involving interests of officers, directors or other interested parties which require the shareholders' general meeting's approval. In addition, a controlling shareholder of an Israeli company or a shareholder who knows that he or she possesses the power to determine the outcome of a vote at a meeting of our shareholders, or who has, by virtue of the company's articles of association, the power to appoint or prevent the appointment of an office holder in the company, or any other power with respect to the company, has a duty of fairness toward the

company. The Israeli Companies Law, or the Companies Law, does not establish criteria for determining whether or not a shareholder has acted in good faith. Moreover, the Companies Law is relatively new and there is little case law available on the duty of a non-controlling shareholder to act in good faith.

***It may be difficult to effect service of process and enforce judgments against directors, officers and experts in Israel.***

We are incorporated and maintain significant operations in Israel. Some of our executive officers and directors and the Israeli accountants named in this annual report reside outside the United States and a significant portion of our assets and the assets of these persons are located outside the United States. Therefore, it may be difficult for an investor, or any other person or entity, to affect service of process on us or any of those persons or to enforce a U.S. court judgment based upon the civil liability provisions of the U.S. federal securities laws, against us or any of those persons, in an Israeli court. Additionally, it may be difficult for an investor or any other person or entity to enforce civil liabilities under U.S. federal securities laws in original actions instituted in Israel.

***We are subject to anti-takeover provisions that could delay or prevent our acquisition by another entity.***

Provisions of Israeli corporate and tax law and of our articles of association may have the effect of delaying, preventing or making more difficult any merger or acquisition of us. In addition, any merger or acquisition of us will require the prior consent of the office of the chief scientist, or the Chief Scientist, if intellectual property is removed from Israel, as well as the Investment Center of the Israeli Ministry of Industry, Trade and Employment, or the Investment Center. Israeli law regulates mergers, votes required to approve a merger, acquisition of shares through tender offers and transactions involving significant shareholders. In addition, our articles of association provide for a staggered board of directors. Any of these provisions may make it more difficult to acquire us. Accordingly, our acquisition by another entity could be delayed or prevented even if it would be beneficial to our shareholders.

***The government programs in which we have participated and the tax benefits we receive require us to satisfy prescribed conditions and may be delayed, terminated or reduced in the future.***

Until 2010, we accepted grants from the Chief Scientist that helped us finance a portion of our research and development expenditures in Israel. In 2010 2% of our research and development expenses were financed with royalty-exempt grants from the Chief Scientist. Since 2010 we have not requested any further grants from the Chief Scientist. Although we do not rely on financing provided by the Chief Scientist and we have fully repaid our royalty commitments to the Chief Scientist, we must continue to satisfy the conditions of the grants. For example, if we fail to comply with the representations and covenants we made to the Chief Scientist concerning our research and development activities in Israel, we could be required to refund the amount of the benefits we have received, adjusted for interest, inflation and penalties.

In addition, we are subject to other restrictions with respect to products developed with grants from the Chief Scientist. Any know-how from the research developed with the grants from the Chief Scientist may not be transferred to third parties without prior approval of the Chief Scientist, and approval is contingent on the recipient agreeing to abide by the provisions of the Encouragement of Industrial Research and Development, 1984, or the Research Law, and related regulations. Also, our ability to manufacture products and transfer know how outside Israel without the approval of the Chief Scientist is restricted under Israeli law and we are required to pay increased royalties to the Chief Scientist of up to 300% of the original grant amount with respect to any products manufactured outside Israel. Since we conduct all of our manufacturing activities in Israel and intend to continue doing so, we do not expect any increase in the amount of royalties we are required to pay to the Chief Scientist.

## **ITEM 4. INFORMATION ON THE COMPANY**

### **4.A. History and development**

Our corporate name is ClickSoftware Technologies Ltd. for both legal and commercial purposes. We were incorporated as a company under the laws of the State of Israel in 1979 and are subject to the Companies Law. From inception until 1996, we operated as a consulting company in the area of optimization and intelligent decision support systems. Thereafter, we transformed our business model to provide workforce management and optimization products and solutions. We have been listed for trading on the Nasdaq stock market since 2000. Our principal executive offices are located at Azorim Park, Oren Building, 94 Em Hamoshavot Road, Petach Tikva 4970602, Israel, and the telephone number at that location is +972-3-765-9400. Our website is located at <http://www.clicksoftware.com>, which is not a part of this annual report. Our wholly owned U.S. subsidiary, ClickSoftware, Inc., has been appointed our agent in the United States and is located at 35 Corporate Drive, Suite 400, Burlington, Massachusetts.

Our capital expenditures for 2013, 2012, and 2011 amounted to \$3.5 million, \$2.5 million, and \$2.0 million, respectively. These expenditures were primarily for hardware and software and leasehold improvements. Our current capital expenditures are primarily for leasehold improvements and hardware and software, and we expect to finance these expenditures primarily from cash on hand.

### **4.B. Business overview**

#### **Who We Are**

We are a leading provider of software products and solutions for workforce management and optimization both for mobile and in-house resources. We derive revenues from the licensing of our software products installed on-premises or via subscriptions to our software when delivered as cloud-based SaaS; and the provision of consulting and support services. Our products for resource optimization are aimed at the service sector, where the primary resources are people (e.g., service technicians), unlike the manufacturing sector, where the primary resources are machines and raw materials. Another key differentiator from manufacturing is that a customer receiving service is typically part of the service process, having to stay home for the service, while in manufacturing the customer is not required to be present during the actual production process. Thus time utilization is critical for both the service resource and the customer, with the service provider seeking to avoid the well-known scenario of a customer waiting at home for the service resource to arrive, while also maximizing the utilization of its workforce.

#### **Our Focus**

We continue our focus on three major growth engines: cloud services, mobility and territorial expansion.

##### **(1) Cloud Services**

We continue to upgrade our infrastructure to support our cloud-based offerings. We have a separate division fully dedicated to selling cloud-based solutions of all our products, including our cloud-based ClickExpress product for the SMB market and its built-in mobility component. With this offering, we now have one of the best solutions for the field service mid-market where cloud-based solutions are gaining popularity. In 2013, we had significant achievements in this area, including the addition of several notable customers for our cloud-based solutions. We intend to capitalize on this momentum in 2014 and beyond.

##### **(2) Mobility**

We believe that market penetration via mobility is a key to our growth. Customers now tend to first address workforce management improvement through mobility solutions, as opposed to optimization solutions. This is expected to significantly expand our addressable market. We will leverage our leadership position in deploying large scale enterprise mobility solutions at some of the most demanding organizations in the world as well as our ClickAppStore for business mobility solutions. We are already working to broaden awareness of our patent-pending ClickButler technology, a context-aware intelligent inference engine that increases productivity of mobile workers. Once a customer uses ClickSoftware's mobility products, it dramatically increases the potential that we can upsell our schedule optimization and decision-making products. In addition, mobility solutions will assist us in selling our cloud-based offerings by enabling us to generate new business via small "apps" that are hosted in the cloud.

### **(3) Territorial Expansion**

We have now established operations in Brazil and Russia. Our local presence supports acceleration of sales in these territories and increases brand awareness. This initiative capitalizes on early successes in these emerging markets and our global leadership position in the utilities, telecommunication, and oil & gas industries, all of which are experiencing rapid growth in these markets. We continue to focus on expansion in markets in Latin America, Asia, and other emerging markets.

### **Our Mission**

In today's highly competitive environment, our mission is to enable service organizations to execute on their service commitments at the right time and place effectively and efficiently. We achieve that goal by leveraging optimization and mobility technologies, as well as best practices, for real time on-going management of customers' commitments and the organization's resources. By so doing we improve the experience of our customers' customers, maximize productivity and service revenues and minimize the cost of service delivery. The end result is higher customer acquisition and retention as well as improved financial performance.

Our products and solutions incorporate best business practices, key business functions of service operations, and sophisticated decision-making algorithms that enable our customers to manage their service operations more efficiently in a scalable, integrated manner. Our products for daily management are mission critical applications that manage incoming jobs from the moment a job is opened until it is successfully closed, including generating the appointment time for a customer, assigning the job to the appropriate technician, designing the optimal route for the technician to minimize travel, and monitoring progress. Mobility solutions on smartphones, tablets and laptops are also part of our offering aimed at on-going real time optimization of customer response and at increasing the productivity of technicians, supervisors, managers and executives. Our solutions have become the backbone of service operations management in many large scale leading organizations worldwide by addressing the fundamental question of job fulfillment: Who does What, for Whom, With what, Where and When (W-6).

Our enterprise mobility initiative continues to serve as a major growth engine for our company and generates value for our customers in several ways. First, at the group level of matching jobs and resources, it addresses the dynamic decision-making required during the day of service. Second, once a given resource receives its sequence of jobs for the day, our mobile software enhances his/her productivity. With the proliferation of new tablets and smartphones for consumer usage, businesses are looking for ways to leverage these new devices and technologies in their businesses. We view the mobile device as the field office of the technician, and accordingly offer functionality to facilitate his/her daily activities and to promote paperless operations. The market for enterprise mobility is expanding with the explosive growth in consumer-related mobile applications, or apps. With years of experience in developing and deploying business mobility solutions, we believe that we have the right platform at the right time to take full advantage of these opportunities. In 2012, our Mobility solutions and ClickAppStore won four categories in the eleventh annual Mobile Star Awards™ program, including Dr. Moshe BenBassat, our CEO, winning the enterprise mobile software visionary category. In 2013, we received, together with our customer Portugal Telecom, the Global Telecoms Business Innovation Award for innovating through automated scheduling and mobility. In 2014, we received Frost & Sullivan's Innovation Award for developing a context-aware, artificial intelligence-based software assistant for mobile field workers.

The enterprise mobility initiative is based on our ClickAppStore which includes numerous ready-to-use mobile business apps, as well as a unique integrated development environment (IDE) in which IT professionals can assemble business apps into end-user solutions using primarily no-coding 'drag and drop' visual wizards. As more companies move to build their own application stores for smartphones and tablets, we believe that we have one of the best platforms for enabling IT professionals to develop their own application store with minimal time to market per app, and with considerably lower technical skills requirements.

In 2013, we achieved recognition for our enterprise mobility from analysts and partners. For example, Gartner, a leading information technology research and advisory company, included us in its Magic Quadrant for Mobile Application Development Platforms (MADP). Gartner assessed 22 vendors based on their ability to execute and completeness of vision (source: Gartner Magic Quadrant for Mobile Application Development Platforms, by

Ian Finley, Van L. Baker, Ken Parmelee, David Mitchell Smith, Ray Valdes, Gordon Van Huizen, published 7 August 2013).<sup>1</sup>

We also partner with software vendors that supply other parts of the mobility software technology infrastructure, including SAP and IBM.

By offering scaled down versions of our products, or specially developed versions for medium and small businesses, or SMB, we now address the needs of service sector companies of all sizes - from companies with 50,000 employees to companies with five employees. Recognizing that many large service companies today outsource or utilize external contractors, we offer capabilities in our products to support such operations under a variety of arrangements between our client and its contractors.

While other service management applications, such as Customer Relationship Management, Enterprise Asset Management, or Outage Management Systems, produce work orders to be executed, our products for Workforce Management and Service Optimization focus on the fulfillment/delivery of these work orders in a cost-effective manner. In a way our software is the flip side of those other service management applications. All of these combined may also be categorized as an Asset Performance Optimization offering.

### **Internal and External Interoperability**

Our products operate on the same software architecture with extensive interoperability within our own products, as well as with external products. In 2009, we released Version 8 of our products which is based on Service Oriented Architecture (SOA), an architecture which, we believe, is the standard in the software industry. This architecture enables interoperability via web services and greatly facilitates integration with the outside world. The ease with which our products can be integrated with leading CRM, Enterprise Resource Planning, or ERP, and EAM solutions, often with standard interface adaptors, enables our customers to efficiently deploy our solutions. We continue to develop our products and currently offer Version 8.10 to our customers.

In our ClickPlatform we have also adopted an extensive approach towards interoperability. Our Mobility Platform is infrastructure-agnostic and can integrate with various state-of-the-art vendors such as Microsoft (RDA), SAP (Sybase/SUP), IBM (Worklight) and pure HTML5\WebService. We further provide an innovative set of visual configuration tools and a flexible object model for building mobile business applications and storing them in our shared ClickAppStore. Our ClickStudio, using drag-&-drop functions, allows the creation of modules and workflows components based on ClickApps, with the ability to connect them together into one or more business applications.

### **Methodically Expanding the Industry Verticals We Address**

Over the years we have been methodically expanding, and continue to expand, the industry verticals we address. Historically our focus was on mobile workforce for field service operations, including utility (electricity, gas and water) companies, telecommunication, computer and office equipment, medical equipment, and the like. A typical scenario would be optimal resource and time slot allocation for a stream of incoming service calls to install, repair or service customer or infra-structure/network equipment. Over the years, this group expanded to include insurance agents, home health care and oil and gas companies. With the introduction of enhanced shift scheduling (rostering) products, we expanded to cover industry verticals that operate a shift-based workforce - 24x7 or more than one shift. These verticals include both field service operations such as public transportation, airport security and in-house service operations such as prison contact centers, retail stores, and more. A typical scenario involves the assignment of people to shifts in such a way that estimated customer demand for service is optimally covered, employee desires are respected, and cost is minimized.

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## **Value to Our Customers**

We sell end-to-end solutions to support decision-making and execution needs across the service enterprise covering long, mid, and short term needs, including intense real time processes to address the dynamic aspects during the day of service. We sell to service operations that need to (1) optimize the delivery of their service commitments, and (2) grow the cost of service at slower pace than their revenue growth. We create value by considerably increasing compliance with service commitments, resource productivity and overall visibility and control.

We offer value to customers at several levels which can be generally categorized into two main categories. The first category is group productivity (W-6). The second category is personal productivity – maximizing the resource's individual productivity and job quality.

Before optimization and mobility solutions are introduced to a service organization, W-6 decisions are made manually by schedulers/dispatchers, and communication with the field during the day is non-existent or limited to voice communication. Our products are designed to markedly improve the customer experience in today's intense and demanding service world. Our goal is to eliminate the so called "service guy syndrome" – a situation we are all too familiar with of waiting at home endlessly for the service technician to arrive. In addition to improving customer service, which by itself has substantial impact on business success and market share, our products enable our clients to improve productivity by reducing travel time, reducing overtime, increasing on-site efficiency and minimizing overall time waste. The value delivered by our products is quantifiable and can be measured by business metrics that directly impact the financial results of our clients. These metrics include, for instance, impact on revenues derived from improvements in productivity as measured by an increase in the number of jobs delivered, or impact on operating profit. With our products, our clients can scale up their revenues and profits faster than the scale up needed in their cost of operation in order to achieve their business growth.

## **Markets and Product Offerings**

### **Task-based versus Shift-based Service Operations**

Service operations can also be classified into field service operations - operations where the service is delivered at the customer location - and in-house operations - where the customer comes to the service provider to receive service, or receives the service by phone, e.g. hospitals, retail, or airports. In field service operations, the basic time units in daily management are job duration at customer sites and travel time from customer to customer, or task-based scheduling. On the other hand, in many in-house service operations the basic time units for daily management are shifts, e.g. 7AM to 3PM, 3PM to 11PM, etc., and the challenge for these operations is shift-based scheduling. Many service operations requires both shift scheduling as well as intra-shift task-based scheduling, such as position switching of airport security agents within a shift, or agents in contact centers within a given shift, or accompanying prisoners to the court house. One of our unique differentiators is the ability to address within one set of integrated products a wide range of field service and in-house service scenarios - from operations with relatively low changes during the day to companies with high rates of dynamic changes requiring real time workforce optimization. We believe that this unique differentiator increases our win rate for new clients in certain industries. By adding shift optimization solutions to our offerings we increased considerably the size of our addressable market by expanding into in-house service operations, or other shift-based operations such as public safety forces and transportation.

### **Service Chain Optimization: From Daily Management to Tactical and Strategic Decision Making**

The optimization and decision-making support which our products offer do not start on the day of service. By the time we reach the day of service, the workforce's size and skill mix have already been determined down to the names of the individuals and the shift each one of them will be staffing on that day. This capacity is the result of a sequence of decisions, some of which may have been made as long as a year or more in advance. In the period just before the day of service individuals are assigned to shifts for the coming weeks in a way that their quantity and skill mix can cover the estimated demand for each hour of the day/week. In the months prior to staffing the shifts for a given week, we need to first ensure that an adequate group of people mix by skill and sites will be available for selection from the personnel available for the shifts, e.g., approving vacation requests, training assignments and delegation to sub-contractors. Hiring options at this stage are fairly limited. This stage is for "master" planning, also known as tactical resource planning.

Several months prior to the day of service, capacity planning takes place. This phase involves determining the size and the skill mix in each territory as a function of the company's strategic plan and forecasted demand for customer service. For example, a company may plan to introduce a new product line or expand in a given territory. At this stage, sufficient time is available for hiring and training new employees or relocating or re-training existing employees. For each of these decision-making stages, a key input is demand forecasting by job type and territories with the time accuracy required for that stage.

This concept of continuous optimization over the decision making time horizon is known as "service chain optimization," a process pioneered by us in the 1990's and for which we have been issued a U.S. patent (see "Intellectual Property" below).

Our products cover the needs of companies across the entire service decision making chain. This holistic approach – which is a key differentiator of our offering - streamlines operations across all levels and functions in the organization from executives to forecasters and planners all the way to regional service managers, dispatchers and individual resources, e.g. technicians. We leverage recent technology developments in devices (e.g., tablets, smartphones) as well as delivery models (e.g., on-premise, hosted). By incorporating these into our offerings, we provide the latest and most advanced work force management solutions to our clients, and the best possible customer experience to their customers. We continue to grow a knowledge base and approach to service optimization and time-related needs. Our scalability, algorithmic intelligence and power, broadly applicable service platform (ClickPlatform), and integration of all aspects of the service model allow us to address nearly every service problem, in any environment, for any size and type of organization.

### **Mobility Technology Enabling the Real Time Service Enterprise**

A service operation is ultimately measured by its performance at the day of service. A typical day in a field service operation starts with the morning schedule that contains the assignments for all the known work orders of the day. As the day develops, emergencies may arise, cancellations may occur, jobs may take longer or shorter than expected, and traffic problems may cause unexpected delays. These contingencies present significant challenges and an effective workforce management solution must minimize the disruptions to the existing work orders while accommodating the new emergency orders that must be delivered on the same day. By integrating real-time updates from the technician's mobile devices and/or GPS-based location reporting devices with our decision-making algorithms, our solutions offer comprehensive coverage to address these challenges and help ensure that the work-plan is continually optimized.

The wide acceptance of mobile devices, including smartphones and tablets offer unique opportunities to continually optimize service delivery execution. We believe that handheld data communication devices and GPS location reports can be used far beyond their traditional role of data transmission to and from the field. These tools can be used for real-time decision-making in order to increase productivity and customer responsiveness. For instance, our products and solutions enable a concept known as "drip feed" management by which, initially, every technician receives only the first two tasks of the day. Upon completing the first task, the technician confirms task completion and a new task is assigned. This technique contributes to improved priority management, travel minimization and customer responsiveness. Similarly, with a GPS reporting system, the dispatcher need not ask technicians where they are located since he or she knows at all times where every technician is located, generating additional efficiencies by improved customer-technician assignments. We also provide applications via mobile devices that support specific business process flows that enables the technician to manage business process including connectivity to back office systems like ERP and CRM.

Our solutions constantly monitor the incoming list of new tasks at all levels of frequency in full synchronization with the delivery status of the existing tasks and the availability of technicians and spare parts in order to maximize productivity and output while complying with promised delivery dates and other business rules.

### **Mobility Technology Enabling Higher Personal Productivity**

The early mobile devices were quite limited in terms of screen size, graphics, typing, and overall user-interface, and not much could be done with them beyond job-dispatch and job-delivery exchange. With the introduction of smartphones and tablets, greater opportunities exist to support the individual user. Once several jobs have been assigned to a resource, our mobility apps further improve the resource's productivity by offering timely help in navigation, asset information, timesheets, job reporting, upselling and more. The mobile device transforms into the mobile office of the resource, virtually eliminating paperwork, minimizing errors, and

increasing productivity even further. All these benefits are compounded on top of the business gain derived from the group productivity.

### **ClickAppStore and Enterprise Mobility**

With the proliferation of smartphones and tablets for consumer use, business people are naturally looking for ways to use them for business needs. According to VDC Research estimates, there were approximately 300 million smartphone users and 25 million tablet users in the enterprise market in 2012, – and by 2014, the research firm projects the mobile workforce will grow to 1.2 billion workers.

The current enterprise mobility market is one of “apps in the cloud”. The trend is away from buying enterprise software as large monolithic do-everything solutions. Instead, enterprises are buying business apps, with each app serving specific goals and enabling the organization to achieve rapid selection, deployment and ROI. Our mobility strategy and solutions, as described below, are built to support this trend via a rich selection of apps in the ClickAppStore. One potential weakness of the replacement of enterprise software with separate apps is that typical apps are standalone, forcing users to repeatedly jump between apps and re-enter data. However, with ClickApps, once an organization chooses apps from the ClickAppStore, these apps automatically combine to create an environment with shared data and workflows.

**Types of mobile users and advantages:** Two main types of mobile business users can be distinguished: an office worker who is occasionally in the field, and a mobile worker who spends most of his/her working time in the field. Examples of the mobile worker are: utility and telecommunication engineers - for both consumer work as well as infrastructure work, oil and gas employees, technicians for office, high tech or medical equipment, insurance claim adjusters, home healthcare providers, field door to door sales agents, pharmaceutical agents, and the like. While the advantages of mobile devices for the occasional user are moderate, they offer tremendous benefits for the field mobile worker in terms of productivity gains and customer satisfaction. The mobile field user's attention, e.g., cable technician, or insurance agent, is focused on the mobile device for only short time slots as most of their time should be devoted to interacting with people, servicing equipment, driving, or other tasks involved in getting the job done. Thus it is critical to have streamlined user interfaces that require minimal typing and easily handle all back-office communication. Without these prerequisites, users will resort back to paper-work and voice communication despite all their limitations, e.g., time consumption and errors.

**Uniqueness of business mobile apps:** The main difference between consumer mobile apps and business mobile apps is in the type of need they answer for the user of the mobile device. Consumer mobile apps are designed for the single user, typically are not interoperable and do not easily connect to enterprise back-end organizational systems. They are not geared for the tight security requirements of business systems. Additionally, business people often need to use multiple apps to carry out their business role, where the output of one app serves as the input for another app, and apps are assumed to be aware of common data (as opposed to having the user copy and paste data from one app to another). The need for streamlined workflow is critical for the business mobile apps. The benefits of these apps, specifically those designed for the enterprise, are that they work together and provide an end-to-end connection between the mobile device and the back-office enterprise IT systems. In addition to simplifying everyday processes and improving productivity, business apps provide the potential to significantly increase customer satisfaction by introducing processes that automate response or notifications to the customer.

The **ClickAppStore** is a virtual store implemented through an application website that contains a wide variety of business-oriented “ClickApps”. The ClickApps address a range of common business scenarios/processes for different industries, including upselling, employee collaboration, timesheet management, employee safety and travel navigation.

Using an integrated development environment called “ClickStudio,” discrete apps can be combined to form composite apps for complete end to end work flows and solutions. A significant portion of this process is accomplished via “drag & drop” operations with minimal coding and without having to upgrade the existing underlying infrastructure. Our ClickAppStore uses our ClickPlatform to keep track and maintain context across multiple mobile apps, in order to make these workflows seamless and friendly.

We intend to embed the ClickButler technology serving as the user’s ultimate personal assistant in just about every ClickApp where it may be useful. Contemporary mobile solutions require too much swiping and typing which consume precious time and reduce user-acceptance and usage. ClickButler technology leads to significant efficiencies and improvement in compliance with company policies derived from prompts and reminders,

minimal typing, health and safety aids, and more. The ClickButler concept is designed to improve the built-in “intelligence” of our mobile and non-mobile apps by anticipating what the user needs and acting on it proactively, and within the right context. Our notion of a “Context Board” and its related actions expands the definition of “state,” “context” and “action” to just about any parameter in the ‘Business Universe’ under consideration - such as customer contract, technician skill, spare-part availability or job urgency. Unlike the consumer world where location-awareness, time-awareness, and weather-awareness cover the vast majority of the behaviors seen today, ClickButlers’ generalized engine for context- aware computing, systematizes the creation of butler behavior, including tools to configure them at a group and individual level. (Certain butler behaviors are derived from company practices and policies and thus are common to all users, e.g. service technicians).

### **Suites, Products and Services**

Our solutions are designed to deliver improvements in:

- workforce productivity;
- responsiveness to customers;
- customer service experience;
- profitability of the service operation; and
- reduction in missed customer commitments.

Once we sell our products we are frequently contracted for services to help with their deployment. To ensure success and minimize cost to our customers, each of our services engagements follows a structured implementation methodology which has proven successful in hundreds of customer implementations. This methodology includes the following phases: planning, requirements gathering, design, delivery, training, testing, go-live and transition to worldwide support organization. Each phase requires the cooperation of and contributions from the customer in order to ensure a successful delivery. Unlike more traditional methodologies, when we start working with a new client, we do not start with a blank slate, ask the users what they want, write down the answers, and return months later with an implemented version, only to learn that certain points were missing or misunderstood. To deliver what the users really need, we have developed a set of "starter kits" and automatic adaptation processes that together deliver ready-to-go "close-enough" solutions. We work with the users on real-life scenarios on a working solution, and the users only need to point out what they like and what they want to change, leading to a much faster and more reliable process of delivering a usable solution. We call this methodology "WISIK", or "When I See (it) I'll Know (it)". Users are much better at adapting on a working system than they are at designing a system from scratch.

### **Suites**

Our solutions are offered individually or packaged into four main suites which together comprise our Service Optimization Suite:

**Field Service Daily Suite** covers automatic decision making and optimization support to manage field service operations: commencing from appointment booking and scheduling during the period around the day of service, followed by real time scheduling and optimization during the day of service and culminating with reports and business metrics analytics after the day of service.

**Roster (Shift Planning) Suite** covers shift planning needs for both the manager as well as the employee to optimize the balance between staffing levels needed for serving customers and managing labor costs, and employee preferences. This suite is offered in several configurations for different industry verticals ranging from police forces to contact centers, and more.

**Mobility Suite** covers the needs of the mobile individual and back-office staff for field data communication, such as sending jobs from the back office to the person's hand-held device, and the person's ability to accept/decline the job, report on progress and job completion, as well as up-selling by a repair technician, capturing customers' signatures, or sending the person's own time sheet to the back office. Geography support, such as travel guidance and information about underground equipment are also covered. Together with the Field Service Daily Suite, the Mobility Suite offers a complete solution for the real time service enterprise, another concept which we have pioneered.

**Forecasting and Planning Suite** covers tactical short term resource planning, such as vacation requests and training needs, as well as longer term capacity planning that addresses the question: what should be the size and skill mix of the field force in each of the territories. To perform these planning questions we also offer forecasting capabilities by which our customer predicts the volume and type of service calls that will arrive at each territory unit for a given time horizon.

## **Products**

**ClickSchedule** optimizes service scheduling and routing to improve workforce productivity by balancing customer, service and asset resources, and organizational preferences, including contractual commitments, priority, drive time, skills, and service and asset resources availability. Configuration capabilities, a high degree of scalability and use of standard service oriented architecture compliant web services interface coupled with graphic mapping tools are designed to ease and improve integration with other enterprise systems and deployment according to organizational business policies and processes. ClickSchedule is our main software platform and accounted for the majority of our license revenues in each of 2013, 2012 and 2011.

**ClickMobile** provides a highly flexible and scalable enterprise mobile workforce solution which can be configured with mobile business applications from the ClickAppStore. It is designed to support mobile field service users working in any kind of environment, offline and online, with rich features and full accessibility to back-office systems. ClickMobile is widely used across entire organizations by large enterprises with thousands of resources, using the system in mission critical environments.

**ClickAnalyze** provides reporting, monitoring and service business analytics for workforce performance measurement and strategic decision support. ClickAnalyze enables analysis of key performance indicators, including resource productivity, operational costs, and responsiveness to customers. Integrated within the Service Optimization Suite, ClickAnalyze provides executive level summaries, as well as operational detailed reporting and analysis by territory, job type, time frame and other criteria.

**ClickLocate (LBS)** captures the location information of a field service engineer and/or his or her vehicle obtained via GPS or other technology and integrates it with ClickSchedule for use in optimized scheduling. LBS then enables service organizations to improve their service operations by allowing them to make decisions and take actions based on location information, including near real-time engineer locations. In effect, LBS enables service managers to "see" the current location of the entire mobile workforce at one time.

**ClickContact** is a customer interaction management solution that enables self-service appointment booking, order updating, automatic customer notifications and customer satisfaction surveying. From scheduling the initial appointment through enabling a post-service follow-up survey, ClickContact provides enhanced customer interaction management throughout the service lifecycle.

**ClickRoster** provides interactive and automated workforce shift planning based on forecasted workload by quantities and skill requirements, rules and regulations, working contracts, engineer skills, calendar and preferences.

**ClickPlan** provides interactive and automated workforce planning for staffing and deployment of the field workforce based on forecasted workload. ClickPlan is designed to enable service organizations to resolve workforce shortages and surpluses weeks and months in advance. Comparing available resources to forecasted workloads, ClickPlan helps determine the best strategy to ensure the right people are in the right place at the right time.

**ClickForecast** provides field service workload forecasting to enable companies to project workforce capacity. ClickForecast can combine historical service workload with future business events to create a forecast for each territory, job type, or business unit. ClickForecast enables service managers, marketing, and sales to collaboratively determine the demand levels of customers, and to create multiple forecast scenarios, each with different business assumptions.

## **ClickSoftware Cloud Services**

**ClickSoftware Cloud Services** enable the customer to utilize our full product offering in the cloud, thus gaining low total cost of ownership, shorter deployment period, minimal up-front investment, scalability and single sign-on from any location.

**ClickCloud** offers medium and large market enterprise customers an alternative to our classic on-premises deployment of the Service Optimization Suite. ClickCloud also enables a hybrid IT model, which is a solution comprised of a mix of Cloud and on-premises deployment. Using ClickCloud customers can choose to control their maintenance and upgrade schedule, as well as the add-ons that they use to enhance their individual solution.

**ClickExpress** offers SMB customers the ability to be up and running within a relatively short period of time, with the latest version of our products. ClickExpress provides the key capabilities required by a service organization including work order management, automated scheduling, mobile dispatching and reporting from the field using our advanced device agnostic mobility solution and a full range of analytics and reporting tools.

**ClickWorkforce** is an end-to-end mobile workforce management solution hosted on the cloud that provides optimized scheduling and mobility, fully integrated within salesforce.com.

### **Acquisition of Xora, Inc.**

On March 4, 2014 we closed the acquisition of Xora, a cloud-based market leader in mobile workforce management, by merger. Under the terms of the merger agreement, the consideration for the transaction was approximately \$15 million in cash, including working capital and cash adjustments.

Xora provides SaaS solutions for companies whose success depends on the productivity and efficiency of ‘always mobile’ workers. Xora delivers its solutions to more than 130,000 users and is one of North America’s largest providers of mobile workforce management solutions. The company was recognized by Frost & Sullivan in 2012 with the Market Share Leadership Award for its intuitive StreetSmart application that helps companies, across a wide variety of industries, to more effectively manage the activities and performance of their employees in the field. Among Xora’s distribution channels are leading US carriers such as Verizon, AT&T and Sprint.

We believe that our merger with Xora creates a company with breadth and depth for a much bigger market under one roof that will strengthen our leadership position by offering customers a broader range of cloud-based mobile workforce management apps.

By combining ClickSoftware’s sophisticated, highly configurable offerings for the large and higher end of the mid-size enterprise market with Xora’s suite of configurable, ready-to-use solutions for the lower end of the mid-size and small business market, we achieve the strategic objective to offer a complete portfolio of best-in-class mobile apps for all business roles, in all size companies, in all industry verticals. Xora’s extensive and long term experience selling packaged apps through the wireless carriers like AT&T, Verizon and Sprint, considerably expands our distribution channels.

The Xora product line includes:

**Xora StreetSmart:** a suite of mobile workforce management applications for field employees.

**Xora InVehicle:** management tools for fleets of all sizes and vehicle types.

**Verizon Field Force Manager:** developed by Xora specifically for Verizon phones and tablets.

**Enterprise Mobile Resource Manager:** available through Sprint; includes a hard-mounted tracking device and portable navigator.

### **Principal Markets**

Traditionally, we have focused on the large enterprise market. We have over 250 enterprise customers and dozens of smaller customers. Our workforce management and optimization solutions are utilized by leading organizations in a number of service industry segments, including: utilities and energy, telecommunications, oil and gas, retail, insurance, high-technology, computer and office equipment, industrial equipment, medical equipment, building automation, public security, home services and transportation.

In addition to expanding to new industry verticals we continue to invest in Russia/Commonwealth of Independent States and Latin America.

We sell our products to a broad base of customers representing a variety of industries with unique needs. During 2013, our five largest customers together accounted for approximately 26% of our revenues. See Item 3.D – Risk factors "If our relationships with our key customers are terminated, our revenues will decline and our business will be adversely affected."

With the introduction of additional products and services as described above we expanded our addressable market in a significant way as well as addressing new markets, as follows:

- (a) The Mobility Suite enables us to attract customers who prefer to start with mobility needs as opposed to optimization. See "ClickMobile and Mobility Suite" above.
- (b) ClickSoftware cloud Services enable us to attract customers who prefer cloud-based solutions as opposed to the more traditional on-premise software solutions. See "ClickSoftware Cloud Services" above.
- (c) The Xora product line enables us to address smaller customers, and customers with simpler requirements, with quick deployment, and adds telecommunications carriers as channels selling our products.

The above offerings join our traditional workforce management and optimization products for our markets. We remain focused on the service sector, and intend to capitalize on the positive synergies between our offerings to create force multipliers. For example, most enterprise field operations require a mobility solution. Thus a client for the Field Service Daily Suite is also a candidate for the Mobility Suite and vice versa. Many enterprise field operations employ small contractors that can use the SMB or cloud solutions, and via integration of the two a win-win situation is created to streamline the interaction between a service provider and its contractors. Finally, many in-house service operations that face intra-day scheduling challenges can also use our classic scheduling products.

### **Sales and Marketing Channels**

We market and sell our products through our direct sales force located in North America, Europe and the Asia Pacific region, as well as through reseller agreements with partners. Recently we have increased our focus on markets in Latin America and Russia/Commonwealth of Independent States. We continue to create and strengthen partner relations. Our multidisciplinary sales teams consist of direct sales executives and sales executives who work with our resellers, sales support consultants and internal sales staff. The internal sales staff is responsible for generating leads and screening prospective customers. Sales support engineers assist the sales executives in the technical aspects of the sales process, including preparing demonstrations and technical proposals. Our sales executives are responsible for completing the sales process and managing the post-sale customer relationship, which consists of ongoing relationship management and the sale of additional licenses and products. Our management also takes an active role in our sales efforts. The knowledge gained by our sales, alliances and marketing force is also communicated to our product marketing group, which guides our development team. This enables our organization to align the functionality of our products with customer and partner needs.

We typically focus our direct sales and marketing efforts on the customer's executive officers, including the vice president of customer service, the chief information officer, the chief financial officer and other senior executives responsible for improving customer service at our customers' organization. To effectively promote product awareness, we engage in marketing activities in a wide variety of areas, including public relations and analyst relations, email campaigns, web seminars with our customers and industry analysts, newsletters and advertising creation and placement, direct mailings and trade shows.

In 2008, we entered into a global reseller agreement with SAP AG, pursuant to which SAP resells certain of our products. We also provide second-level support to SAP in connection with our products. Our products are included on SAP's global pricelist in specified bundles, and sold under the standard SAP end-user license agreement and global support commitments. We believe that our alliance with SAP increases our presence in our existing markets and assists with introducing our products into new markets. In 2011, we entered into a global solution partner agreement with Infor Global Solutions Limited, or Infor.

In 2013, we also engaged partner channels for our cloud-based offerings. We launched ClickWorkforce, a mobile workforce management application suite, on salesforce.com's AppExchange. We also partnered with NetSuite, the industry's leading provider of cloud-based financials/ERP software suites, to build the ClickSoftware SuiteApp, built using NetSuite's SuiteCloud Computing Platform.

Our corporate development organization supports joint sales and marketing activities with our business partners. Our business relationships with large ERP, CRM, Human Capital Management, or HCM, and EAM enterprise

software vendors enable us to use our partners' market presence and sales channels to create significant additional revenue opportunities. Our strategy is based on entering into reseller relationships with the leading enterprise software vendors. This strategy is further enhanced through our offering of adaptors that enable rapid integration and implementation of our products into other major ERP, HCM, CRM and EAM systems such as SAP ERP and CRM, and Infor EAM and ERP.

We also market our products through the systems integrator community, or SIs, including companies such as Accenture, IBM, Infosys and Cap Gemini. These relationships complement our enterprise software reseller agreements and extend our presence and brand name in new and existing markets. These SIs provide various levels of resources to integrate, customize and implement our solutions. Depending on the strength of the relationship, we have co-invested via our partner enablement program in jointly developing industry-specific solutions, training and certifying the partner's professional services teams, developing co-marketing programs, and incorporating our products into their marketing/referral strategies.

### **Implementation Methodology and Implementation Partners**

We also invested in the development of a methodology and a set of tools to support implementation processes which have evolved in a way that streamlines the deployment phase and shortens "time to value." This methodology and the tool set are used by both our internal project teams as well as by certified implementation partners. We also provide best-practice consulting on improving and transforming the service process.

### **Agile Development Methodology**

Since 2010, our research and development department has implemented the "Agile" development methodology known as "scrum" framework. The Agile methodology allows us to be more flexible and dynamic and to deliver new features on short notice. Our customers can influence our product road map "on the fly" so that we can adjust our development plans on a monthly or even weekly basis. The Agile methodology brings our research and development efficiency to a new level of accuracy in meeting the demands of our customers. The Agile methodology is based on sophisticated electronic tools that support the procedures and processes of the scrum framework and provide monitoring and control mechanisms.

### **Competition**

The market for our products is competitive and rapidly changing. Competition may increase in the future as the workforce management and optimization market gains size and increased business focus, current competitors expand their product offerings, and new companies enter the market. See Item 3D – Risk factors – "We face competition, which could make it difficult to compete successfully."

In 2013, Gartner included us in Gartner's Magic Quadrant for Field Service Management. We were positioned within the "Leaders" quadrant (source: Gartner Magic Quadrant for Field Service Management, William McNeill, Michael Maoz, Gordon Van Huizen, published 9 October 2013).

Gartner also included ClickSoftware in the Gartner Magic Quadrant for Mobile Application Development Platforms, by Ian Finley, Van L. Baker, Ken Parmelee, David Mitchell Smith, Ray Valdes, Gordon Van Huizen, published 7 August 2013.

The principal competitive factors in the workforce management and optimization industry are:

- the technological capabilities and performance of the solution;
- installed base, domain expertise and experience with large-scale implementations;
- the acceptance and adaptability of the workforce management and optimization solution to the solution offerings of large SIs and CRM/ERP vendors, and the ability to form marketing alliances with the foregoing; and
- pricing.

We believe our solutions compare favorably with our competitors' solutions based on these competitive factors. Other key competitive factors include a broad base of users, strategic alliances, key reference customers, interoperability, integration of complementary products and services, technological leadership, product performance, price, customer support, name recognition, relationships with partners and distribution channels, the ability to respond quickly to emerging opportunities and our financial strength.

Our current and potential competitors include:

- software application vendors that offer workforce management solutions with certain optimization modules as part of their overall offerings, either on premises or via a hosted/cloud service including, but not limited to, Oracle, ServicePower Technologies plc., Ventyx (part of ABB Ltd.), TOA Technologies, Astea and ServiceMax;
- systems integrators and internal information technology departments that may elect to develop a solution in-house;
- software vendors developing solutions that compete with our shift management solutions, such as Quintiq, Kronos, Verint and Allocate Software; and
- mobile field service vendors such as Syclo (an SAP company) and Antenna Software, recently acquired by Pegasystems, Inc.

### ***Intellectual Property***

We believe that the improvement in our existing products and technologies and the development of new products are important in establishing and maintaining a competitive advantage.

We have been issued three patents. One of these patents was issued in the United States and describes a method and system for assigning human resources to provide services. We own a similar patent in Israel. A third United States patent relates to workforce collaboration on real-time problem resolution and automatic reuse of the discussion for solving similar problems in the future. Our patents will expire during 2020-2022. We also have six patent applications pending in the United States and two patent applications pending in Israel. As we continue to develop new applications of our products, we will consider submitting additional patent applications. Patents may not issue from any of these pending applications and, even if patents do issue, the claims allowed may not be sufficiently broad to protect our technology. In addition, patents issued to us may be challenged, invalidated or circumvented, and the rights granted thereunder may not adequately protect us.

We own several trademark registrations for various marks in the U.S., the European Community, the UK and Israel.

Our success and ability to compete substantially depend on our internally developed technology, which we protect through a combination of trade secrets, copyrights, trademarks, patents and intellectual property law, together with non-disclosure and invention assignment agreements. These legal protections provide only limited protection. See Item 3.D – Risk factors – "Our intellectual property could be used by third parties without our consent because protection of our intellectual property is limited" and this Item 4.B – Business Overview - "Competition". Although we rely on a combination of means by which to protect our intellectual property, we believe that factors such as the technological and creative skills of our personnel, new product developments, frequent product enhancements and reliable product maintenance are more essential to establishing and maintaining a technology leadership position than intellectual property protection.

We generally enter into non-disclosure agreements with our customers, business partners, employees and consultants and generally control access to and distribution of our software, documentation and other proprietary information. Also, our end-user licenses are designed to prohibit unauthorized use, copying and disclosure of our software and technology in the United States, Israel and other countries.

Substantial litigation regarding technology rights exists in the software industry, and we expect that software products may be increasingly subject to third-party infringement and ownership claims as the number of competitors in our industry segment grows and the functionality of products in different industry segments overlap. See Item 3.D – Risk factors – "Our technology and other intellectual property may be subject to infringement claims".

### ***Regulation***

We do not operate in a market governed by specific regulations but our business is affected by certain government regulations. For example, our ability to manufacture products outside Israel without the approval of the Chief Scientist is restricted under law and we are required to pay increased royalties to the Chief Scientist of up to 300% with respect to any products manufactured outside Israel. See Item 3.D – Risk factors – "The government programs in which we have participated and the tax benefits we receive require us to satisfy

prescribed conditions and may be delayed, terminated or reduced in the future." Also, any merger or acquisition of us will require the prior consent of the Chief Scientist, as well as authorization from the Investment Center.

#### **4.C. Organizational structure**

Our directly and indirectly held principal operating, wholly-owned subsidiaries and their countries of incorporation are:

- ClickSoftware, Inc. (United States)
- ClickSoftware Central Europe GmbH (Germany)
- ClickSoftware Europe Limited (United Kingdom)
- ClickSoftware Belgium N.V. (Belgium)
- ClickSoftware Australia Pty. Ltd. (Australia)
- ClickSoftware India Private Limited (India)
- ClickSoftware Singapore Pte. Ltd. (Singapore)
- ClickSoftware Technologies (Pty) Ltd. (South Africa)
- ClickSoftware Brasil Soluções em Gestão de Forças de Trabalho Ltda. (Brazil)
- ClickSoftware Limited Liability Company (Russia)
- Xora, Inc. (United States)
- Gearworks, Inc. (United States)
- Xora Software Systems Private Limited (India)
- Xora Australia Pty Ltd. (Australia)

#### **4.D. Property, plants and equipment**

We have a lease for approximately 58,000 square feet of office space located in Petach Tikva, Israel. This lease expires in January 2015 and includes an option allowing us to extend the lease term to January 2017. This office space is used for management, marketing, sales, research and development and implementation activities.

Our subsidiaries lease offices in several locations and typically engage in sales and marketing, implementation and support, and administration activities.

Our U.S. subsidiary operates from a leased facility of approximately 25,000 square feet of office space located in Burlington, Massachusetts. This lease expires in May 2017.

Our U.K. subsidiary operates from a leased facility of approximately 11,500 square feet located in Burnham, near London. This lease expires in March 2023 and includes an early termination right allowing us to terminate the lease term in March 2018.

Our Australian subsidiary operates from a leased facility of approximately 10,000 square feet located in Melbourne. This lease expires in December 2017 and includes an option allowing us to extend the lease term to December 2022.

Our Indian subsidiary operates from a leased facility of approximately 22,000 square feet located in Gurgaon near New-Delhi. This lease expires in December 2015 and includes an option allowing us to extend the lease term to December 2021.

We also lease additional smaller offices in various sites in the Americas, Europe and Asia.

Our recently acquired subsidiary, Xora operates from three locations:

A leased facility of approximately 17,000 square feet of office space located in Mountain View, California. This lease expires in December 2014.

A leased facility of approximately 5,000 square feet of office space located in Eagan, Montana. This lease expires in January 2015.

A leased facility of approximately 10,000 square feet of office space located in Bangalore, India. This lease expires in April 2017.

We consider that our current office space is sufficient to meet our anticipated needs for the foreseeable future and is suitable for the conduct of our business.

#### **ITEM 4A. UNRESOLVED STAFF COMMENTS**

None.

#### **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

##### **Overview**

We derive revenues from the licensing of our software products and the provision of consulting and support services. We recognize revenues in accordance with the Accounting Standards Codification Topic, or ASC, 985-605, "Software Revenue Recognition", as amended, or ASC 985-605 (see Note 2 of the notes to our consolidated financial statements included later in this annual report).

Service revenues are comprised of revenues from consulting, training, and post-contract customer support. Consulting services are billed at an agreed-upon rate, plus incurred expenses. Customers licensing our products generally enter into consulting agreements with us. Post-contract customer support arrangements provide technical support and the right to software updates. Post-contract customer support revenues are charged as a percentage of license fees depending on the level of support coverage requested by the customer. Our support contracts typically renew automatically for successive 12-month periods, unless the customer informs us of its desire not to renew.

In 2013, 2012 and 2011, we also derived an immaterial amount of revenues from cloud-based SaaS.

##### **Highlights**

Our revenues grew by 3% in 2013 compared to 2012, representing growth in services revenues offset by a decrease in licenses revenues. Our growth in services revenues was in both professional services revenues and post-contract support revenues and was primarily attributable to the increase in the number of new customers as well as strong repeat business. The decrease in our license revenues was mainly due to a lower average deal size per customer.

Net loss for 2013 was \$4.2 million compared to net income of \$7.5 million in 2012. We generated \$6.4 million in positive cash-flow from operations in 2013.

As of December 31, 2013, our cash and cash-equivalents, and short and long-term investments decreased to \$58.0 million from \$59.4 million as of December 31, 2012 after distribution of cash dividends aggregating \$6.7 million.

##### **Critical Accounting Policies**

In preparing our consolidated financial statements, we are required to make estimates, judgments and assumptions that affect the reported amounts of revenues and expenses, assets and liabilities and contingent assets and liabilities at the date of the financial statements.

On an ongoing basis, we evaluate our estimates, judgments and assumptions, including those related to revenue recognition, allowances for doubtful accounts, stock-based compensation and goodwill and other intangible assets. We base our estimates, judgments and assumptions on historical experience and forecasts, and on various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. We believe that the following critical accounting policies affect our more significant estimates, judgments and assumptions used in the preparation of our consolidated financial statements.

##### **Revenue Recognition**

Revenue results are difficult to predict, and any shortfall in revenues or delay in recognizing revenues could cause our operating results to vary significantly from quarter to quarter and could result in future operating

losses. In addition, the timing of our revenue recognition influences the timing of certain expenses, such as commissions and royalties. We follow very specific and detailed guidelines in measuring revenues; however, certain judgments affect the application of our revenue recognition policy.

Our revenues are principally derived from licensing the rights to use our software and sales of professional services, including consulting, implementation and training. We recognize revenues in accordance with ASC 985-605 ("Software Revenue Recognition"). Revenues from software license fees are recognized when persuasive evidence of an arrangement exists, either by written agreement or a purchase order signed by the customer, the software product has been delivered, the license fees are fixed and determinable, and collection of the license fees is considered probable.

License fees from software arrangements that involve multiple elements, such as consulting, training and post-contract customer support, are allocated to each element based on the residual method. Under the residual method, consideration is allocated to undelivered elements based upon the vendor specific objective evidence for fair value (VSOE) of those elements, with the residual of the arrangement fee allocated to and recognized as software license revenue. We measure the VSOE for each element according to the price charged when the element is sold separately. For post-contract customer support, we determine the VSOE based on the renewal rates agreed to in the contracts. For other services, such as consulting and training, we determine the VSOE based on the fixed hourly/daily rate charged in stand-alone service transactions.

Arrangements that include professional services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. When services are considered essential, revenue under the arrangement is recognized using contract accounting. When services are not considered essential, revenue allocable to the services is recognized as the services are performed.

Revenue from software licenses that require significant customization, integration and implementation are recognized based on ASC 605-35 ("Construction-Type and Production-Type Contracts") using contract accounting on the percentage-of-completion method, based on the relationship of actual working hours incurred to total working hours estimated to be incurred over the duration of the contract. In recognizing revenues based on the percentage-of-completion method, we estimate time to completion with revisions to estimates reflected in the period in which changes become known. If we do not accurately estimate the resources required or the scope of work to be performed, or do not manage our services properly within the planned periods of time or satisfy our obligations under the contracts, then future services margins may be significantly and negatively affected or losses on existing contracts may need to be recognized. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract.

Service revenues are comprised of revenues from consulting, training, and post-contract customer support. Revenues from consulting services are recognized on a time and material basis, or in a fixed price contract, on a percentage of completion basis. Revenues from training are recognized as the services are provided. Post-contract customer support arrangements provide for technical support and the right to unspecified updates on an if-and-when-available basis. Revenues from these arrangements are recognized ratably over the term of the arrangement, usually one year.

We classify revenue as either software license revenue or services revenue for statement of operations presentation. We allocate revenue to each of these categories based on the VSOE for elements in each revenue arrangement and based on the application of the residual method for arrangements in which we have established the VSOE for all undelivered elements.

Where we are unable to establish the VSOE for some of the undelivered elements, we take a systematic approach, whereby we first allocate revenue to any undelivered elements for which the VSOE has been established, and then allocate revenue to any undelivered elements for which the VSOE has not been established based on management's best estimate of the fair value of those undelivered elements. We then apply a residual method to determine the license fee. Management's best estimate of fair value of undelivered elements for which the VSOE has not been established is based upon the VSOE of similar offerings and other objective criteria.

We also enter into software arrangements with resellers whereby revenues are recognized upon sale through to the end user by the reseller.

Our standard payment terms are between 30 and 120 days. Our policy is not to grant extended payment terms to our customers over 120 days.

We generally do not grant a right-of-return to our customers. We generally provide a warranty period of about three months at no extra charge. As of December 31, 2013 and 2012, the provision for warranty cost was immaterial.

#### **Allowance for Doubtful Accounts**

We maintain an allowance for doubtful accounts using estimates that we make based on factors we believe appropriate, such as the composition of the accounts receivable aging, historical bad debts, changes in payment patterns, customer creditworthiness and current economic trends. If we used different assumptions, or if the financial condition of customers were to deteriorate, resulting in an impairment of their ability to make payments, additional provisions for doubtful accounts would be required and would increase our bad debt expense.

In judging the probability that we will be able to collect software license fees, we continuously monitor collection and payments from our customers and maintain a provision for estimated credit losses based on our historical experience generally, as well as our experience with specific customers. In connection with customers with whom we have no previous experience, we typically utilize public financial information or independent resources to evaluate the creditworthiness of these customers. We perform on-going credit evaluations of our customers.

#### **Recent Accounting Pronouncements**

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-02, *Comprehensive Income: Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, which requires companies to disclose significant amounts that have been reclassified out of accumulated other comprehensive income. Amounts that are required to be reclassified in their entirety to net income must be disclosed either on the face of the income statement or in the notes to the financial statements. Amounts that are not required to be reclassified in their entirety to net income in the same reporting period must be disclosed by a cross reference to other disclosures that provide additional information regarding such amounts. ASU No. 2013-02 is effective for fiscal years and interim periods beginning after December 15, 2012. The adoption of ASU No. 2013-02 has not had a material impact on our financial position or results of operations.

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*, which provides explicit guidance on the financial statement presentation of an unrecognized tax benefit. ASU No. 2013-11 requires unrecognized tax benefits to be presented as a reduction to a deferred tax asset, except that, if a net operating loss carryforward, a similar tax loss or a tax credit carryforward is not available at the reporting date to settle any additional income taxes that would result from the disallowance of a tax position, then the unrecognized tax benefit should be presented as a liability. ASU No. 2013-11 has become effective for fiscal years and interim periods beginning after December 15, 2013. The adoption of ASU No. 2013-11 has not had a material impact on our financial position or results of operations.

## 5.A. Results of operations

Our operating results for each of the three years ended December 31, 2013, 2012 and 2011 expressed as a percentage of revenues are as follows:

	<b>YEAR ENDED DECEMBER 31,</b>		
	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Revenues:			
Software license	28%	35%	36%
Services	72	65	64
Total revenues	<u>100</u>	<u>100</u>	<u>100</u>
Cost of revenues:			
Software license	4	4	3
Services	39	35	33
Total cost of revenues	<u>43</u>	<u>39</u>	<u>36</u>
Gross profit	<u>57</u>	<u>61</u>	<u>64</u>
Operating expenses:			
Research and development	15	13	10
Selling and marketing	39	32	27
General and administrative	9	9	9
Impairment of goodwill	-	-	1
Total operating expenses	<u>63</u>	<u>54</u>	<u>47</u>
Operating (loss) income	(6)	7	17
Other income	-	0	-
Financial income, net	1	0	0
Net (loss) income before taxes	<u>(5)</u>	<u>7</u>	<u>17</u>
Taxes on income (Tax benefit)	(1)	0	3
Net (loss) income	<u>(4%)</u>	<u>7%</u>	<u>14%</u>

Our operating results for each of the three years ended December 31, 2013, 2012 and 2011 are as follows:

	<b>YEAR ENDED DECEMBER 31,</b>		
	<i>(In thousands)</i>		
	<u><b>2013</b></u>	<u><b>2012</b></u>	<u><b>2011</b></u>
<b>Revenues:</b>			
Software license	\$ 28,679	\$ 34,541	\$ 31,542
Services	74,502	65,505	55,545
Total revenues	<u>103,181</u>	<u>100,046</u>	<u>87,087</u>
<b>Cost of revenues:</b>			
Software license	4,413	3,686	2,519
Services	39,894	35,185	29,177
Total cost of revenues	<u>44,307</u>	<u>38,871</u>	<u>31,696</u>
Gross profit	<u>58,874</u>	<u>61,175</u>	<u>55,391</u>
<b>Operating expenses:</b>			
Research and development	15,970	13,146	9,019
Selling and marketing	39,706	31,977	23,382
General and administrative	9,121	8,779	7,386
Impairment of goodwill	-	-	939
Total operating expenses	<u>64,797</u>	<u>53,902</u>	<u>40,726</u>
Operating (loss) income	(5,923)	7,273	14,665
Other income	-	110	-
Financial income, net	839	274	7
Net (loss) income before taxes	<u>(5,084)</u>	<u>7,657</u>	<u>14,672</u>
Taxes on income (Tax benefit)	(924)	169	2,462
Net (loss) income	<u>\$ (4,160)</u>	<u>\$ 7,488</u>	<u>\$ 12,210</u>

**Comparison of results for years ended December 31, 2013, 2012 and 2011:**

**Revenues**

	<u><b>Revenue Breakdown</b></u>				
	<u><b>2013</b></u>	<u><b>% Change</b></u>	<u><b>2012</b></u>	<u><b>% Change</b></u>	<u><b>2011</b></u>
	<i>(In thousands)</i>				
<b>Revenues:</b>					
Software license	\$ 28,679	(17%)	\$ 34,541	10%	\$ 31,542
Percentage of total revenues	28%		35%		36%
Services	74,502	14%	65,505	18%	55,545
Percentage of total revenues	<u>72%</u>		<u>65%</u>		<u>64%</u>
Total Revenues	<u>\$103,181</u>	3%	<u>\$100,046</u>	15%	<u>\$ 87,087</u>

Revenues increased 3% to \$103.2 million in 2013, compared with \$100.0 million in 2012 and \$87.1 million in 2011. The change in revenues in 2013 was attributable to an increased demand for professional services and post-contract services offset by a decrease in revenues from software licenses primarily due to an emerging customer preference towards smaller initial transaction size and smaller cloud transactions. The revenues we derived from cloud transactions were immaterial. The growth in revenues in 2012 was attributable to an increased demand for professional services and post-contract services and an increase in the volume of licenses sold via our partners and directly, mostly from the telecommunications and retail industries. In addition, the strengthening of the U.S. dollar against other currencies decreased our revenue growth from about 17% to about 15%.

### Revenues by Territory

	<u>2013</u>	<u>%</u>	<u>2012</u>	<u>%</u>	<u>2011</u>	<u>%</u>
	<u>Revenues</u>		<u>Revenues</u>		<u>Revenues</u>	
	<i>(In thousands)</i>					
Revenues:						
Americas	\$ 50,573	49%	\$ 60,123	60%	\$ 40,070	46%
EMEA	42,548	41%	32,888	33%	39,455	45%
Israel	245	0%	456	0%	847	1%
Asia Pacific	9,815	10%	6,579	7%	6,715	8%
Total Revenues	<u>\$103,181</u>	100%	<u>\$100,046</u>	100%	<u>\$ 87,087</u>	100%

In 2013, 49% of our revenues were generated in the Americas (with 35% in the United States, 12% in Canada and 2% in Latin America), 41% in EMEA (including 18% in the United Kingdom, 6% in Germany and 4% in Netherlands), 10% in Asia Pacific (including 6% in Australia) and less than 1% in Israel. Revenues in the Americas decreased by \$9.6 million, or 16%, compared to 2012. Revenues in EMEA grew by \$9.7 million, or 29%, compared to 2012. Revenues in Asia Pacific increased by \$3.2 million, or 49%, compared to 2012. The emerging customer preference towards smaller initial transaction size and smaller cloud transactions impacted the Americas more than other territories due to the faster adoption of cloud transactions in the Americas. In the longer term we anticipate continued growth in the Americas as we increase our investment to drive top line revenues.

In 2012, 60% of our revenues were generated in the Americas (with 42% in the United States, 11% in Canada and 7% in Latin America), 33% in EMEA (including 15% in the United Kingdom, 3% in Germany and 3% in Sweden), 7% in Asia Pacific (including 4% in Australia) and less than 1% in Israel. Revenues in the Americas grew by \$20.0 million, or 50%, compared to 2011. Revenues in EMEA decreased by \$6.6 million, or 17%, compared to 2011. Revenues in Asia Pacific decreased by \$0.1 million, or 2%, compared to 2011.

In 2012, due to the macro-economic slowdown in Europe, we focused more of our sales effort on growth opportunities in the Americas. As a result, sales in the Americas reached a record level. The growth in the Americas more than offset the weakness we saw in some of our European markets which were still being impacted by challenging economic conditions.

In 2011, 46% of our revenues were generated in the Americas (with 39% in the United States and 7% in Canada), 45% in EMEA (including 21% in the United Kingdom, 6% in The Netherlands and 5% in Sweden), 8% in Asia Pacific (including 5% in Australia) and 1% in Israel. Revenues in the Americas grew by \$11.4 million, or 40%, compared to 2010. Revenues in Asia Pacific grew by \$2.3 million, or 52%, compared to 2010. The increases in revenues in all regions were attributable mainly to increased demand for our products from the telecommunications industry, large implementation projects and demand for post-contract services. The higher growth in the Americas was due to better macroeconomic conditions and our ability to attract large customers mostly in the telecommunications industry. This relatively slower growth in EMEA was due to overall weak macroeconomic conditions and a slowdown in revenues from our customers in the utility sector.

#### **Software Licenses**

Software license revenues were \$28.7 million, or 28% of revenues, in 2013, compared with \$34.5 million, or 35% of revenues, in 2012, and \$31.5 million, or 36% of revenues, in 2011. The decrease in software license revenues from 2012 to 2013 of \$5.9 million, or 17%, was primarily due to towards smaller initial transaction size and smaller cloud transactions. Despite this trend, we did see an overall increase in the number of new customers. The increase in software license revenues from 2011 to 2012 of \$3.0 million, or 10%, was primarily due to an increase in the volume of licenses sold to new customers directly and via our partners in the Americas.

#### **Services**

Service revenues were \$74.5 million or 72% of revenues in 2013, compared with \$65.5 million, or 65% of revenues in 2012, and \$55.5 million, or 64% of revenues in 2011. The increase in service revenues from 2012 to 2013 was due to both increased demand for our professional services and post-contract services. The increase in professional services was due to new customer implementations as well as strong repeat business. The

increase in service revenues from 2011 to 2012 was due to increased demand for our professional services and post-contract services.

### **Cost of Revenues**

Cost of revenues consists of cost of software license revenues and cost of services. Cost of software license revenues consists of expenses related to costs of software purchased or licensed for resale and of costs related to hosting (including salaries and subcontractors). Cost of services consists of expenses related to salaries and expenses of our professional services organizations, costs related to third-party consultants, and equipment costs.

Cost of revenues was \$44.3 million, or 43% of revenues, in 2013, compared with \$38.9 million, or 39% of revenues, in 2012 and \$31.7 million, or 36% of revenues, in 2011. The increase in the cost of revenues from 2012 to 2013 was primarily due to higher costs associated with meeting increased demand for our services and software and increased investment in cloud infrastructure. In 2013, the cost of licenses increased while license revenues decreased resulting in lower profitability compared to 2012. The cost of services increased at the same pace as the increase in service revenues, as explained below in "Cost of Services," resulting in the same profitability from services for both 2013 and 2012. The increase in the cost of revenues from 2011 to 2012 was primarily due to higher costs associated with meeting increased demand for our services and software. In 2012, the cost of licenses increased at a higher pace than the increase in license revenues resulting in lower profitability compared to 2011, the cost of services increased at a higher pace than the increase in service revenues, as explained below in "Cost of Services," resulting in lower profitability from services for 2012 as compared to 2011.

### **Cost of Software Licenses**

Cost of software license revenues was \$4.4 million, or 4% of revenues, in 2013, compared with \$3.7 million, or 4% of revenues, in 2012 and \$2.5 million, or 3% of revenues, in 2011. The increase in cost of software license revenues from 2012 to 2013 was primarily due to an increase of \$0.9 million in hosting costs (including payroll costs) associated with our cloud services partially offset by a decrease of \$0.2 million in costs of third party licenses. The increase in cost of software license revenues from 2011 to 2012 was primarily due to an increase of \$1.0 million in hosting costs (including payroll costs) and an increase of \$0.2 million in costs of third party licenses.

### **Cost of Services**

Cost of service revenues was \$39.9 million, or 39% of revenues, in 2013, compared with \$35.2 million, or 35% of revenues, in 2012 and \$29.2 million, or 33% of revenues, in 2011.

The increase in the cost of services revenues from 2012 to 2013 of \$4.7 million, or 13%, was primarily due to higher expenses associated with the provision of our services as described below. In 2013, services revenues grew roughly at the same pace as cost of services resulting in steady profitability. Compared with our costs relating to providing services in 2012, in 2013 there was an increase in our related payroll expenses of \$4.2 million, a decrease in subcontractors' costs of \$1.3 million and an increase of \$1.8 million in other costs, mainly overhead. In addition, the overall impact of the weakening U.S. dollar against certain currencies in 2013 spread over the various expense items above increased our costs by about \$0.4 million.

The increase in the cost of services revenues from 2011 to 2012 of \$6.0 million, or 21%, was primarily due to higher expenses associated with the provision of our services as described below. In 2012, services revenues grew at a slower pace than cost of services resulting in a decline in profitability. This decline in profitability relates to our professional services activities that generated lower margins due to newly launched versions of our products that required us to increase our implementation efforts and thus reduced our efficiency. Compared with our costs relating to providing services in 2011, in 2012 there was an increase in our related payroll expenses of \$4.0 million, an increase in subcontractors' costs of \$0.5 million and an increase of \$1.5 million in other costs, mainly overhead. In addition, the overall impact of the strengthening U.S. dollar against certain currencies in 2012 spread over the various expense items above decreased our costs by about \$1.4 million.

### **Gross Profit**

Gross profit was \$58.9 million, or 57% of revenues, in 2013 compared with \$61.2 million, or 61% of revenues, in 2012, and \$55.4 million, or 64% of revenues, in 2011. The decrease in gross profit from 2012 to 2013 of \$2.3 million, or 4%, was due to the shift to higher service revenues and an absolute decrease in license revenue which reduced gross profit. The increase in gross profit from 2011 to 2012 of \$5.8 million, or 10%, was due to an

increase in gross profit both from services activities and license revenues. The decrease in gross margin from 2012 to 2013 was mainly due to change in revenue mix towards higher service revenues (which generates lower gross margins and lower license revenues. The decrease in gross margin from 2011 to 2012 was mainly due to a decrease in margins generated by professional services and licenses activities as explained in cost of services and cost of licenses sections above.

### **Operating Expenses**

Operating expenses are categorized into research and development expenses, selling and marketing expenses and general and administrative expenses. Total operating expenses were \$64.8 million, or 63% of revenues, in 2013, compared with \$53.9 million, or 54% of revenues, in 2012 and \$40.7 million, or 47% of revenues, in 2011.

The increase in operating expenses from 2012 to 2013 of \$10.9 million, or 20%, was primarily due to an increase in research and development expenses and selling and marketing expenses. The increases in selling and marketing expenses and research and development expenses resulted from our efforts to accelerate our growth, maintain our competitive advantage in the market and capture additional market share. Due to measures we have implemented to reduce our cost base in 2014, we do not anticipate any increase in operating expenses, other than those costs which we will assume due to the acquisition of Xora. The increase in operating expenses from 2011 to 2012 of \$13.2 million, or 32%, was primarily due to an increase in research and development expenses and selling and marketing expenses. The increases in research and development expenses and selling and marketing expenses result from our efforts to maintain our competitive advantage in the market, capture additional market share and place ourselves in a better position to accelerate the growth of our future revenues.

### **Research and Development Expenses**

Research and development expenses consist primarily of personnel costs for product development, net of grants received from the Chief Scientist. In return for some of these grants, we are obligated to pay the Israeli government royalties as described below which are included in cost of revenues. In 2008, we completed repayment of our royalty commitments to the Chief Scientist, but remain subject to continued compliance with the conditions of the grants we received. Grants which we received in 2009 through 2010 are not subject to royalty payments. See Item 3.D – Risk factors – "The government programs in which we have participated and the tax benefits we receive require us to satisfy prescribed conditions and may be delayed, terminated or reduced in the future." Software research and development costs incurred prior to the establishment of technology feasibility are included in research and development expenses as incurred. Software development costs incurred subsequent to the establishment of technological feasibility through the period of general market availability of the products are capitalized, if material, after consideration of various factors, including net realizable value. To date, software development costs that are eligible for capitalization have not been material and have been expensed.

Research and development expenses were \$16.0 million, or 15% of revenues, in 2013, compared with \$13.1 million, or 13% of revenues, in 2012 and \$9.0 million, or 10% of revenues, in 2011. The increase in research and development expenses from 2012 to 2013 was primarily due to an increase of \$1.3 million in payroll expenses, an increase of \$1.0 million in subcontractor's costs and an increase in other costs, mainly overhead of \$0.6 million. The increased efforts in research and development (which continued from the previous year) were aimed at improving our product and cloud platforms, our mobility offering, including our ClickAppStore as well as our Rostering. In addition, the overall impact of the weakening of the U.S. dollar against the NIS in 2013 spread over the various expense items above increased our research and development costs by about \$0.4 million. The increase in research and development expenses from 2011 to 2012 was primarily due to an increase of \$2.7 million in payroll expenses, an increase of \$0.6 million in subcontractor's costs and an increase in other costs, mainly overhead of \$0.8 million. The increased efforts in research and development were aimed at improving our product and cloud platforms, our mobility offering, including our ClickAppStore as well as our Rostering offering. In addition, the overall impact of the strengthening of the U.S. dollar against the NIS in 2012 spread over the various expense items above decreased our research and development costs by about \$0.9 million.

### **Selling and Marketing Expenses**

Selling and marketing expenses consist primarily of personnel and related costs for marketing and sales functions, including related travel, direct advertising costs, expenditures on trade shows, market research and promotional printing.

Selling and marketing expenses were \$39.7 million, or 39% of revenues, in 2013, compared with \$32.0 million, or 32% of revenues, in 2012 and \$23.4 million, or 27% of revenues, in 2011. We increased our selling and marketing expenses in order to accelerate our revenue growth in the coming years. Specifically, we increased sales capacity in the Americas and EMEA to support our expansion into new territories as we established offices in Brazil and Russia. The increase in the selling and marketing expenses from 2012 to 2013 of \$7.7 million, or 24%, was due to an increase of \$3.9 million in payroll expenses and an increase in soft marketing of \$3.8 million. In addition the overall impact of the weakening U.S. dollar against certain currencies in 2013 spread over the various expense items above increased our selling and marketing costs by about \$0.7 million. The increase in the selling and marketing expenses from 2011 to 2012 of \$8.6 million, or 37%, was due to an increase of \$6.2 million in payroll expenses and an increase in our other (mainly overhead and marketing) selling and marketing activities of \$2.4 million. In addition the overall impact of the strengthening U.S. dollar against certain currencies in 2012 spread over the various expense items above decreased our selling and marketing costs by about \$1.0 million.

### **General and Administrative Expenses**

General and administrative expenses consist primarily of personnel and related costs for corporate functions, including information services, finance, legal, accounting, human resources, facilities, provision for doubtful accounts and costs related to our status as a public company.

General and administrative expenses were \$9.1 million, or 9% of revenues, in 2013, compared with \$8.8 million, or 9% of revenues, in 2012 and \$7.4 million, or 9% of revenues, in 2011. The increase of \$0.3 million in general and administrative expenses from 2012 to 2013 was mostly due to an increase of \$0.1 million in payroll expenses and an increase in other costs, mainly professional fees of \$0.2 million. The increase of \$1.4 million in general and administrative expenses from 2011 to 2012 was mostly due to an increase of \$0.6 million in payroll expenses and an increase in other costs, mainly professional fees and stock-based compensation costs of \$0.8 million. In addition, the overall impact of the strengthening U.S. dollar against certain currencies in 2012 spread over the various expense items above decreased our general and administrative costs by about \$0.4 million.

### **Impairment of goodwill and other intangible assets**

We perform our annual impairment tests in the fourth quarter. For impairment testing we identified two separate reporting units: ClickSoftware and ST (acquired from AST Technologies in 2009). For ClickSoftware the fair value was significantly higher than the carrying amount. In the fourth quarter of 2013 we determined that ST technology will no longer be used by the Company. Thus we reassessed the remaining core technology of ST at a value of zero. As a result, \$0.2 million of intangible assets impairment charges was recorded as of December 31, 2013.

### **Financial Income, Net**

Financial income includes interest income, gains and dividends earned on our cash and investments, including marketable securities as well as the effects of foreign currency fluctuations offset by interest expense.

Financial income net of interest expenses was \$0.8 million, or 1% of revenues, in 2013, compared with \$0.3 million, or 0% of revenues, in 2012 and \$0.0 million, or 0% of revenues, in 2011. The increase in financial income from 2012 to 2013 was attributable to increases mostly in dividend income received from our holdings in dividend yielding securities and lower foreign currency exchange rate fluctuations. The increase in financial income from 2011 to 2012 was attributable to lower foreign currency exchange rate fluctuations.

### **Income Taxes**

Income taxes expenses consist of deferred taxes and current taxes.

Income tax benefit were \$0.9 million, or 1% of revenues, in 2013, compared with income tax expenses of \$0.2 million, or 0% of revenues, in 2012 and \$2.5 million, or 3% of revenues, in 2011. The tax benefit change in income taxes from 2012 to 2013 was mainly due to the pre-tax loss incurred during 2013 which resulted in changes in deferred taxes and lower taxable income. The reduction in income taxes from 2011 to 2012 was mainly due to changes in deferred taxes and lower pre-tax income. Deferred taxes assets increased from 2011 to 2012 due to temporary differences in the research and development costs in Israel and higher than expected utilization of loss carry forwards, partially offset by a deferred tax provision as described below. See Note 14 to

our consolidated financial statements for further information. We expect higher tax rates in 2014 due to partial utilization of tax loss carry forwards in Israel as well as our move to a less favorable tax bracket.

Our future consolidated tax expense is expected to reflect various statutory tax rates in the United States, Israel, United Kingdom, Germany, Australia, India, Brazil, South Africa and Russia. Future tax rates may also increase due to tax withholdings by various tax authorities, which are not expected to be utilized in the foreseeable future.

As of December 31, 2013, net operating loss carry forwards in Israel amounted to approximately \$4.8 million. Additional tax loss carry forwards of approximately \$18.6 million at the federal level and approximately \$5.9 million at the state level remain attributable to our U.S. subsidiary. Other U.S. tax loss carry forwards in other jurisdictions are immaterial. The U.S. net operating loss carry forwards will expire gradually from 2014 through 2024. Utilization of U.S. net operating losses would be subject to substantial annual limitations due to the "change in ownership" provisions of the Internal Revenue Code of 1986 and similar state law provisions. The annual limitations would result in the expiration of part of net operating losses before utilization.

In November 2012, a law was enacted in Israel to incentivize companies to pay taxes on those Approved Enterprises earnings as if distributed, and effectively release the earnings from any further tax liabilities at the parent company level. The law, although not mandatory, offers lower tax rates on those earnings, accumulated through the year ended December 31, 2011, elected to be "released" which as applicable to us will be approximately 6%. During 2013, we elected to use the incentive available under the law, releasing 2011 tax-exempt earnings of \$12.2 million for future dividend distributions, by paying tax of \$0.7 million. We distributed during 2013 a dividend in the amount of \$6.7 million. Part of this dividend was under the release of 2011 tax-exempt earnings, and therefore, although paid from Approved Enterprises earnings, such distribution did not result in additional Israeli tax liability. Deferred tax provision was included in our financial statements for the year ended December 31, 2012.

#### **Net Income (loss)**

Net loss for 2013 was \$4.2 million, or \$0.13 per fully diluted share, or 4% of revenues, compared with net income of \$7.5 million, or \$0.23 per fully diluted share, or 7% of revenues, in 2012 and net income of \$12.2 million, or \$0.38 per fully diluted share, or 14% of revenues, in 2011. Net income in 2013 was lower relative to 2012 due to increased operating and cost of revenues expenses. Net income in 2012 was lower relative to 2011 due to increased operating and cost of revenues expenses.

#### **Foreign Currency Fluctuations**

Our reporting and functional currency is the U.S. dollar. A significant portion of our expenses related to our Israeli operations are incurred in NIS, and a portion of our revenues and expenses are incurred in British pounds, Euros, Australian dollars and Indian Rupees. The results of our operations are subject to fluctuations in these exchange rates. In 2013, 65% of our expenses and 49% of our revenues were incurred in non-U.S. dollar currencies. We engage in non-speculative forward contracts related to foreign currencies in order to minimize the impact of changes in foreign currency exchange rates on our earnings. In 2013, the net effect of the change in value of the U.S. dollar against other currencies was a minor increase in revenues by \$50,000, an increase in costs of revenues by \$0.4 million and an increase in operating expenses by \$1.0 million. See Item 3.D – Risk factors "Our risk exposure to foreign currency fluctuations is increasing, and we may not be able to fully mitigate the risk."

#### **5.B. Liquidity and capital resources**

Our cash and investments decreased by \$1.4 million, or 2%, to \$58.0 million as of December 31, 2013, compared with \$59.4 million as of December 31, 2012, which was an increase of \$4.4 million, or 8%, compared with \$55.0 million as of December 31, 2011. Our primary sources of cash and investments during 2013 were cash flows of \$6.4 million generated from operations and \$2.0 million from exercises of employee stock options. During 2013, we distributed cash dividends aggregating \$6.7 million. Our primary sources of cash and investments during 2012 were cash flows of \$16.2 million generated from operations and \$0.7 million from exercises of employee stock options. During 2012, we distributed cash dividends aggregating \$10.1 million.

As of December 31, 2013, we had cash and cash equivalents of \$25.3 million, short-term deposits of \$9.0 million, marketable securities of \$22.6 and long-term deposits of \$1.1 million. As of December 31, 2013, \$1.1 million in long-term deposits had been deposited with banks to secure letters of credit totaling \$1.1 million, which are described below. Our cash, short-term deposits and long-term deposits are deposited primarily in low-

risk and predominantly U.S. dollar denominated investments and bank deposits. The bank deposits are typically held in the form of certificates of deposit for a period of more than three months and up to 12 months and bear fixed income interest. As of December 31, 2013, these bank deposits had an average interest rate per annum of 2.1%. Our marketable securities are invested in government and corporate bonds and had an average annual yield of 1.5%. We adhere to an investment policy which requires investment in high-quality investment-grade securities provided, however, that up to \$10 million of our total cash and investments may be invested in equities of companies that have a policy to regularly distribute dividends or in ETFs of a similar nature. As of December 31, 2013, out of \$22.6 million invested in marketable securities, approximately \$7.4 million was invested in dividend yielding equity securities.

Nearly all of our cash and investments are not insured by the FDIC or other similar governmental insurance limits. See Item 3.D – Risk Factors "Our cash may be subject to risk of loss and we may be exposed to fluctuations in the market value of our portfolio investments and in interest rates."

<b>Cash and Investments</b>					
<b>December 31,</b>					
	<b><u>2013</u></b>	<b><u>% Change</u></b>	<b><u>2012</u></b>	<b><u>% Change</u></b>	<b><u>2011</u></b>
	<i>(In thousands)</i>				
Cash and cash equivalents	\$ 25,346		\$ 12,793		\$ 14,683
Short-term deposits	9,001		30,310		28,243
Marketable securities	22,586		15,635		10,945
Long-term deposits	1,072		621		1,093
Total cash and investments	<u>\$ 58,005</u>	(2%)	<u>\$ 59,359</u>	8%	<u>\$ 54,964</u>

For the year ended December 31, 2013, net cash provided by operations was \$6.4 million, comprising net loss of \$4.2 million, an increase in trade receivables of \$0.7 million, an increase in deferred taxes of \$2.3 million, an increase in other receivables of \$0.8 million, an increase in accounts payable of \$1.2 million, and an increase in deferred revenues of \$7.5 million, which was partially offset by non-cash charges of \$5.7 million.

The decrease in cash provided from operations in 2013 compared to 2012 was mostly due to higher expense levels and moderate growth rate which impacted our profitability and cash generation.

For the year ended December 31, 2012, net cash provided by operations was \$16.2 million, comprising net income of \$7.5 million, a decrease in trade receivables of \$1.6 million, an increase in deferred taxes of \$0.5 million, an increase in other receivables of \$0.1 million, an increase in accounts payable of \$2.9 million, and a decrease in deferred revenues of \$0.8 million, which was partially offset by non-cash charges of \$5.7 million.

The increase in cash provided from operations in 2012 compared to 2011 was mostly due to from timing of booking and invoicing more evenly spread during the year which resulted in strong collections during 2012.

For the year ended December 31, 2011, net cash provided by operations was \$11.9 million, comprising net income of \$12.2 million, an increase in trade receivables of \$9.1 million, a decrease in deferred taxes of \$1.3 million, an increase in other receivables of \$0.4 million, an increase in accounts payable of \$1.0 million, and an increase in deferred revenues of \$1.6 million, which was partially offset by non-cash charges of \$5.3 million.

Net cash provided by investment activities was \$10.8 million in 2013, consisting of \$20.9 million used in investments in deposits, \$15.7 million invested in marketable securities, \$9.2 million provided by the sale of marketable securities and \$3.5 million used for purchases of equipment and systems, including computer equipment and fixtures and furniture and for leasehold improvements.

Net cash used in investment activities was \$8.6 million in 2012, consisting of \$1.6 million used in investments in deposits, \$7.5 million invested in marketable securities and \$2.5 million used for purchases of equipment and systems, including computer equipment and fixtures and furniture and for leasehold improvements, partially offset by \$2.9 million provided by proceeds from sales of marketable securities.

Net cash used in investment activities was \$17.0 million in 2011, consisting of \$12.0 million used in investments in deposits, \$8.3 million invested in marketable securities and \$2.0 million used for purchases of equipment and

systems, including computer equipment and fixtures and furniture and for leasehold improvements, partially offset by \$5.3 million provided by proceeds from sales of marketable securities.

Net cash used in financing activities was \$4.7 million in 2013, consisting of \$6.7 million used for cash dividends, which was partially offset by exercise of employee stock options of \$2.0 million. Net cash used in financing activities was \$9.5 million in 2012, consisting of \$10.1 million used for cash dividends, which was partially offset by exercise of employee stock options of \$0.7 million. Net cash used in financing activities was \$6.0 million in 2011, consisting of \$7.5 million used for cash dividends, which was partially offset by exercise of employee stock options of \$1.5 million. There are no restrictions on the flow of funds between us and any of our subsidiaries.

As of December 31, 2013, we had outstanding trade receivables of approximately \$22.5 million, which represented approximately 22% of revenue in 2013. As of December 31, 2012, we had outstanding trade receivables of approximately \$21.8 million, which represented approximately 22% of revenue in 2012. As of December 31, 2011, we had outstanding trade receivables of approximately \$23.4 million, which represented approximately 27% of revenue in 2011. Our standard payment terms are typically between 30 and 120 days and our policy is not to grant extended payment terms to our customers over 120 days. Days sales outstanding, or DSO, calculated based on revenues for the most recent quarter and accounts receivable at the balance sheet date, decreased to 66 DSO as of December 31, 2013, compared with 69 DSO as of December 31, 2012, and 88 DSO as of December 31, 2011, due to timing of booking towards the end of the quarter and specific customer milestones. DSO was relatively high in 2011 compared to 2012 and 2013 due to relatively strong bookings towards the end of 2011.

Our capital requirements depend on numerous factors, including market demand and acceptance of our products, the resources we devote to developing, marketing, selling and supporting our products, the timing and extent of establishing additional international operations, investments in computers, office equipment and office fixtures and our acquisition activities. We intend to continue investing significant resources in our selling and marketing, research and development operations in the future and expect to continue investing in computers, office equipment and office fixtures. We also intend to continue exploring acquisition opportunities.

On March 4, 2014 we closed the acquisition of Xora in consideration for the payment of approximately \$15 million in cash from our cash resources.

We believe that we have sufficient cash to fund our operations for at least the next 12 months.

### **5.C. Research and development**

We have invested significant time and resources in creating a structured process for undertaking all product development projects. These include documenting product requirements, specifying product features and workflow, developing software, performing quality assurance and creating documentation and packaging. Our research and development center in Israel is ISO 9001 compliant and continuously updates its software development procedures to maintain an ongoing improvement process and high quality products.

Our future research and development strategies will concentrate on strengthening our product offerings in decision support and optimization, mobility, forecasting, capacity and shift planning and monitoring; continuing to enhance the technology and scalability of our products; continuing to improve our mobile and location-based capabilities; and continuing the development of offerings for specific vertical industries.

We invested \$16.0 million in 2013, \$13.1 million in 2012 and \$9.0 million in 2011 in research and development activities.

### **5.D. Trend information**

We operate in the rapidly evolving market for workforce management and optimization for the service sector including field and in-house resources. Workforce management spending remained strong in 2013. Despite the current uncertainties in the global economy, we have continued to experience strong demand for our products and services. This is supported by analyst findings. For example, "Gartner research puts the revenue for packaged field service dispatch and workforce management software applications, including maintenance and service revenue, at approximately \$1.2 billion in 2012, with a compound annual growth rate of 12.7%" (source:

Gartner Magic Quadrant for Field Service Management, William McNeill, Michael Maoz, Gordon Van Huizen, published 9 October 2013).

We believe that the market for field service management is largely untapped. Frost & Sullivan, using a similar definition of “Mobile Workforce Management”, identified ClickSoftware as one of the vendors with the largest market share in this space, and estimates the compound annual growth rate for this market from 2013 to 2017 at 40.5%, leading to market size of about \$3 billion by 2018 (Source: Mobile Workforce management Market: Prepackaged Mobile Field-Based Worker Applications in North America, Frost & Sullivan report NC4B-65, December 2013). The acquisition of Xora is intended to enable us to quickly expand our access to this growing market and extend our market leading position, including leveraging their distribution channels via carriers.

Our strategy is to continue to increase marketing efforts through our channel and strategic partners to target these potential customers, side by side with our direct sales force. Companies in the mid-market are also seeking solutions to improve productivity, and we address this need with some of our offerings including ClickExpress and ClickCloud.

Since 2009 we have invested significantly in our mobility offering. We believe there is a global trend of moving enterprise software to mobile devices to enable service people to manage applications through their mobile devices. Overall, there is a growing focus on mobility, outpacing even social media. This focus is prominent in corporate strategies. According to IDC, “driven by major technology trends in consumer and enterprise markets, the Enterprise MADP software market is in a period of rapid growth.” In 2012, IDC believed the total market reached a size of \$938.5 million. By 2017, the market will experience a 38.7 percent CAGR to reach \$4.8 billion.” (Source: “Worldwide Mobile Enterprise Application Development Platform 2013–2017 Forecast and 2012 Vendor Shares”, IDC Doc #244418, by Stacy K. Crook and John Jackson, published November 2013). As noted above, Gartner placed ClickSoftware in their MADP Magic Quadrant for 2013.

As part of our strategic plan, we expect increased sales from new territories. We continue to believe that developing countries such as Russia and those in Latin America are investing in solutions which provide improved quality of service and efficiency, reduce cost and increase regulatory compliance.

We have detected a pattern in the IT area towards smaller initial transactions relative to the approach we saw in prior years. In particular, there is a tendency of customers to shift to the SaaS model in order to lower up-front investment. This has led to a smaller initial transaction size with new customers, and will require us to scale up the volume of our transactions in order to maintain our growth.

In 2013, the ratio of our license revenues to service revenues decreased. We expect license and services revenues to grow in 2014. We expect to continue to grow our revenues in 2014 despite the continued uncertainty in the economic conditions. In 2013, our results in EMEA and APAC grew whereas Americas declined, but we expect revenue from all regions to grow in 2014.

We believe that companies focused on cost control are likely to demand products and services, such as our workforce management and optimization solutions, that aim to maximize efficiency and decrease customers' operating expenses. As of December 31, 2013, we had a backlog of approximately \$42.7 million, compared to \$33.2 million at the end of 2012.

The economic uncertainties may affect the competitive environment in our industry. For example, larger, better capitalized companies may seek to acquire smaller, weaker rivals that have been adversely affected by the economic downturn.

In 2013, approximately 49% of our revenues and 65% of our expenses were denominated in non-U.S. dollar currencies. Any changes in the value of the U.S. dollar against these currencies affect our reported earnings in U.S. dollars. In 2013, the net effect of the change in value of the U.S. dollar against other currencies was a minor increase in revenues by \$50,000, an increase in costs of revenues by \$0.4 million and an increase in operating expenses by \$1.0 million. At the start of 2014, the U.S. dollar has strengthened against each of the NIS, Euro and British Pound. The net effect on our financial results was immaterial.

#### **5.E. Off-balance sheet arrangements**

Except for the arrangements with the Chief Scientist discussed in Item 5.A above, we do not have any off-balance sheet arrangements.

## 5.F. Tabular disclosure of contractual obligations

We have various commitments primarily related to guarantees, letters of credit and capital lease obligations. The following table provides details regarding our contractual cash obligations and other commercial commitments as of December 31, 2013:

Contractual Obligations *	Payments due by Period (in thousands)				Total
	2014	2015	2016-2018 (aggregate amount)	2019-2021 (aggregate amount)	
Office Lease Obligations	\$ 3,783	\$ 2,127	\$ 2,982	\$ 281	\$ 9,173
Net Severance Pay Obligation	-	-	-	2,788	2,788
Total	\$ 3,783	\$ 2,127	\$ 2,982	\$ 3,069	\$ 11,961

\* Does not include Xora commitments as of March 25, 2014 of \$0.7 million office lease obligations and capital lease obligations of \$0.2 million.

Commercial Commitments	Total Amounts Committed (in thousands)	Amount of Commitment Expiration Per Period (in thousands)
		2014-2017
Guarantees/Letters of Credit*	\$ 1,070	\$ 1,070

\* We have entered into standby letter of credit agreements with banks and financial institutions primarily relating to the guarantee of rental agreements. As of December 31, 2013, contingent liabilities on outstanding letter of credit agreements aggregated \$1.1 million. We expect to renew most of these letters of credit. The letters of credit are secured by \$1.1 million in deposits to cover potential payments under the guarantees.

## ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

### 6.A. Directors and senior management

#### Senior Management

The members of our executive management are as follows:

<u>Name</u>	<u>Age</u>	<u>Position</u>
Dr. Moshe BenBassat	66	Chief Executive Officer
Shmuel Arvat	51	Executive Vice President and Chief Financial Officer
Zvi Piritz	49	President EMEA and APAC
Stephen Timms	43	President Americas

**DR. MOSHE BENBASSAT** co-founded ClickSoftware in 1979 and has served as our Chief Executive Officer since our inception. Dr. BenBassat also served as our Chairman from inception until 2013. From 1987 to 1999, Dr. BenBassat served as a Professor of Information Systems at the Faculty of Management at Tel-Aviv University. Dr. BenBassat has also held academic positions at the University of Southern California and the University of California in Los Angeles. Dr. BenBassat holds B.S., M.S. and Ph.D. degrees in Mathematics and Statistics from Tel-Aviv University. Dr. BenBassat pioneered the field of 'service chain optimization', a term he coined in the 1990s and is considered to be one of the world's leading experts in the field.

**SHMUEL ARVATZ** has served as our Executive Vice President and Chief Financial Officer since 2002. Prior to joining ClickSoftware, Mr. Arvatz served as the Chief Financial Officer at Shrem, Fudim, Kelner Technologies Ltd., at that time a leading investment house in Israel. From 1999 to 2001, Mr. Arvatz served as Executive Vice President and Chief Financial Officer of Tecnomatix Technologies Ltd., a provider of software e-manufacturing solutions. From 1990 to 1999, Mr. Arvatz served as Vice President and Chief Financial Officer at ADC Israel Ltd. (previously Teledata Communications Ltd.), a telecommunications equipment provider. Mr. Arvatz holds a Bachelor of Arts degree in Accounting and Economics from Bar-Ilan University in Tel Aviv, Israel and is a Certified Public Accountant in Israel.

**ZVI PIRITZ** has served as our Executive Vice President World Wide Sales and Marketing from 2011 to 2014 and as our President of EMEA and APAC since 2014. Previously, Mr. Piritz served as our Senior Vice President World Wide Sales and managed our sales organization worldwide. He has been with the Company since 1999 serving in various executive management roles. Prior to joining us, Mr. Piritz held various positions with international software companies, leading both the operational and the sales and marketing teams. Mr. Piritz holds a B.A. degree in Economics from Tel Aviv University, Israel and an M.B.A. degree in Marketing & International Accounting from Fordham University, New York, USA.

**STEPHEN TIMMS** has served as our Senior Vice President of Sales in Americas from 2010 to 2014 and as our President of Americas since 2014. Prior to moving to the United States, from 2005 to 2009, Mr. Timms held various positions in our sales organization, serving as our Vice President of Sales in EMEA and as the Director of Sales in West Region, EMEA. Before joining us, Mr. Timms served as Director for UK Business and as International Sales Executive at IDVelocity, a software company in the manufacturing and service industry. Prior to that he held several positions that included sales roles with leading software vendors, and very deep technical roles which required delivering training to post-graduate students. Mr. Timms graduated Harvard Business School Executive Education – General Manager Program, in 2013.

Our executive officers serve at the discretion of our board of directors. The employment of each of our executive officers is at will and may be terminated at any time, with or without cause, subject to contractual notice provisions.

## Directors

Our articles of association provide for a minimum of two members and a maximum of eleven members on our board of directors. Except for External Directors (as defined in the Companies Law), all directors are classified into three classes, as nearly equal in number as possible, based on the amount of time they have held office, with the members of each class to hold office until their successors have been duly elected and qualified. At each annual meeting, the class of directors whose term expires at that meeting shall be elected to hold office for a term expiring at the annual meeting to be held in the third year following their election and until their successors have been duly elected and qualified.

We have a classified board of directors as set forth below:

<u>Name of Director and Class</u>	<u>Age</u>	<u>Term Expires</u>	<u>Independent Director (1)</u>	<u>Member of Audit Committee</u>	<u>Member of Compensation Committee</u>	<u>Member of Corporate Governance and Nominating Committee</u>
Israel Borovich, Class II (Chairman)	72	2014	X			
Gil Weiser, Class II	72	2014	X	X		
Moshe BenBassat, Class III	66	2015				
Shlomo Nass, Class III (2)	53	2015	X	X		X
Nira Dror, External Director (3)	59	2015	X	X	X	X
Shai Beilis, External Director	65	2015	X	X	X	X
Menahem Shalgi, External Director	63	2016	X	X	X	

(1) as defined under Rule 5605(a)(2) to the Nasdaq Listing Rules, or the Nasdaq Rules.

(2) "Audit Committee Financial Expert" under SEC rules and requisite experience under Nasdaq Rules with respect to membership on the Audit Committee. See Item 16A below.

(3) "Financial Expert" as required by the Companies Law with respect to membership on the Audit Committee.

**DR. ISRAEL BOROVICH** rejoined the board of directors in 2011, having previously served as a director of the Company from 1997 (and as an External Director according to the Companies Law from 2001) until March 2009. In 2013, Dr. Borovich was appointed Chairman of our Board of Directors. Dr. Borovich serves as the Dean of the School of Business and Economics at the Academic College of Tel Aviv-Jaffa. From 2005 to 2011, Dr. Borovich served as a member of the Board of Directors of El Al Israel Airlines Ltd. and as its Chairman from 2005 until 2008. From 1993 until 2006, he served as President and Chief Executive Officer of Knafaim Holdings Ltd., from 2006 to 2010, he served as its Vice Chairman, and from 1994 until now, he serves as a director on its Board of Directors. From 1999 until 2006, Dr. Borovich served as Chairman of Granit Hacarmel Investments Ltd. From 2006 until 2010, Dr. Borovich served on the Board of Trustees of the Polytechnic Institute of New York University in New York. From 2006 to 2008, he served as Chairman of the Board of Governors of Afeka Tel Aviv Academic College of Engineering. From 2008 until 2011, he served as Chairman of Alut Society for Autistic Children. From 2008 until 2012, he served as Chairman of the Board of Trustees of Wingate Institute. From 2010 until 2012, he served as member on the advisory board of All Cargo Logistics Services, and from 2011 until 2012 as Chairman of the Board of Galil Cargo. Currently, Dr. Borovich serves as Chairman of the Board of Ayalon Highways Co. Ltd. (since 1998), director of the Interdisciplinary Center Herzliya (since 1994), and director of Kenes International (since 2010). Dr. Borovich has also served as the Dean of the School of Management & Economics at the Academic College of Tel Aviv-Yaffo since 2012. He previously served as a Professor on the Faculty of Management of Tel Aviv University where he is currently a Professor Emeritus. Dr. Borovich holds B.Sc. and M.Sc. degrees in Industrial Engineering and a Ph.D. degree in Operations Research from the Polytechnic Institute in New York City.

**GIL WEISER** has served as a director of the Company since 2003. Mr. Weiser has been active in the high tech industry for the past 30 years. He is currently Chairman of the Board of BG Negev Technologies and a member of the board of Attunity Ltd. Mr. Weiser served as CEO of Orsus Solutions Ltd., Hewlett-Packard Israel, Fibronics Corporation and Digital Corporation Israel. He has also served as director of numerous companies including the Tel Aviv Stock Exchange. Mr. Weiser served as Chairman of the Executive Committee of Haifa University from 1994 to 2006. He holds a B.Sc. degree from the Technion Institute and an M.Sc. degree from the University of Minnesota in Minneapolis.

**DR. SHLOMO NASS** has served as a director of the Company since 2009. Dr. Nass currently serves as Senior Partner at Dr. Shlomo Nass & Co., an Israeli law firm that he founded in December 2002, specializing in real estate, liquidations, receiverships and corporate rehabilitation, arbitration, corporate and commercial law. Since 2011, he has served as a director of City-Group Financial Products Israel Ltd. of the City Bank Group. Since 2008 he has served as a director of The Blue Shore Development Company (Tel Aviv-Herzliya) Ltd., and as a director of Aviv Alron Ltd. (former Yuli Capital Markets Ltd.). Since 1991, he has served as Vice Chairman of the public advisory committee on trade levies. From 2009 until 2013, Dr. Nass served as a director, as a member of the investment committee and as a member of the auditing committee of Partner Communications Company Ltd. From 2011 until 2013, he served as a director and a member of the auditing committee of Tempo Beer Industries Ltd. From 2006 until 2011, he served on the Board of Directors of NMC United Entertainment Ltd. From 2003 until 2010, he served as Chairman of the financial statement and auditing committee of Formula Systems (1985) Ltd. From 2003 until 2009, he served as Chairman of the financial statement committee and as a member of the Board of Directors of IBC-Industrial Buildings Corporation Ltd. From 2005 until 2008, he served as the Chairman of the Board of Directors of Ayalon Insurance Co. Ltd. and Ayalon Financial Solutions Ltd. Dr. Nass also serves as Chairman of the Board of Directors of the following companies: since 2013 of S.A.L Mishkenot Haretz, since 2011 of Hevruta Marketing Ltd. and Hevruta Consumering Ltd., since 2010 of Kada Buildings, since 2008 of Chaniman Entrepreneurship Ltd., since 2005 of M.D.K Touch Ltd. and since 2004 of Shir-Lak Ltd. Dr. Nass received his Ph.D. and LL.B. in Law and B.Sc., Economics and Accounting from Bar-Ilan University, and completed a Mediators Course of the Ministry of Justice. He is a member of the Israeli Bar Association and is a Certified Public Accountant in Israel. Dr. Nass is also a Certified Information System Auditor, C.I.S.A (USA). Dr. Nass is a lecturer on Corporate Law at IDC – Interdisciplinary Center Herzliya, and Bar-Ilan University. He is also a lecturer in the Directors’ Training seminar at “Lahav” Executive Education at the Recanati Faculty of Management in Tel-Aviv University. In his military service, Dr. Nass served as an officer in the Israeli Defense Forces, or IDF, the Information Systems Auditing Team for the Paymaster General Administration.

**NIRA DROR** has served as a director of the Company since 2009. Ms. Dror is the owner and the General Manager of Nira Dror Ltd., a company which she founded in 2006 that provides consulting and representation services for companies in the aviation and tourism industries. From 2003 to 2005, Ms. Dror served as Deputy General Manager and as General Manager of North America at El Al. From 1999 to 2003, she served as General

Manager of Eastern Europe and East Mediterranean at British Airways, and from 1989 to 1999, as General Manager for Israel. From 1986 to 1989, Ms. Dror served as the General Manager of Histour Ltd., a tourism company, and from 1979 to 1985, she served as the chief economist for Teus Azorei Pituach Ltd. Ms. Dror currently serves on the board of directors and as chairperson of the audit committee of Shemen Oil and Gas Resources Limited. Ms. Dror currently serves on the board of directors and as a member of the audit committee of the following companies: Shlomo Insurance Company, S. Shlomo Holding Ltd., Sharonim Ltd., and Dikla Insurance Company Ltd. She served on the board of directors and as a member of the audit committee of Tzur Shamir Holdings Ltd. from 2006 to 2013, and as chairperson of the audit committee of Bank Hapoalim Ltd. from 2006 to 2012. She was a member of the board of directors of H&O Ltd. from 2005 to 2008, and of Chamei Yoav Tourism from 2005 to 2008. Ms. Dror was also a member of the executive committee of the panel of airlines in Israel from 1990 to 1999. Ms. Dror holds a B.A. in Economics and Business Administration and an M.B.A. from Tel Aviv University.

**SHAI BEILIS** has served as a director of the Company since 2009. Mr. Beilis is currently Chairman of the Board of Keebali Media Ltd. and BotanoCap Ltd. and a member of the board of directors of Earnix Ltd. Mr. Beilis founded Formula Ventures (within the Formula Group) in 1998 and has been the Chairman of the Board since its inception. Formula Ventures Ltd. was the advisor and General Partner of two venture capital funds: Formula Ventures I and Formula Ventures II. Mr. Beilis joined the Formula Group in 1994 as chief executive officer of Argotec. Mr. Beilis was CEO of Clal Computers and Technology Ltd. from 1993 to 1995, an Israeli IT holding company traded in the Tel-Aviv Stock Exchange. From 1987 to 1993 Mr. Beilis was Vice President at Digital Equipment Corporation Israel. From 1978 to 1986, he was Chief Executive Officer of Yael Software and Services. From 2002 to 2006 Mr. Beilis was the Chairman of Formula Vertex UK Ltd., which was the advisor for the European Technology Venture Portfolio of UBS Capital. Mr. Beilis has served as director or chairman of over sixty Israeli high tech companies (including the following Nasdaq listed companies: Wiztec Solutions Ltd. (1996 to 1999), BluePhoenix Solutions Ltd. (1995 to 2008), RadView Software Ltd. (1998 to 2010), and Formula Systems (1985) Ltd. (1997 to 2005)). Mr. Beilis holds an M.Sc. in Computer Science from the Weizmann Institute of Science in Rehovot, Israel, and a B.Sc., cum laude, in Mathematics and Economics from the Hebrew University in Jerusalem, Israel.

**MENACHEM SHALGI** has served as a director of the Company since 2010. Mr. Shalgi served at Amdocs Ltd. as Vice President of Business Development and M&A from 1998 to 2003, and as Vice President and Executive Account Manager from 1993 to 1998, and at various other positions from 1985 to 1993. Mr. Shalgi has served as an external director of Mind CTI since April 2005 and serves as the chairman of AfterDox Ltd., an investment house in Israel, since June 2007. Mr. Shalgi served as a director of Pilat Media PLC in the UK from 2006 until mid-2009. Mr. Shalgi holds a B.A. in Economics and Statistics from Tel-Aviv University and an M.Sc. in Computer Sciences from the Weizmann Institute of Science.

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

There are no arrangements or understandings with major shareholders, customers, suppliers or others pursuant to which any of our executive management or our directors were selected.

## **6.B. Compensation**

The aggregate amount of compensation paid or accrued to all of our directors and executive officers as a group of 9 persons with respect to 2013 was \$1.8 million in salaries, consulting fees, directors' fees, and bonuses, compared to \$1.8 million in 2012, and \$0.2 million in amounts set aside or accrued to provide pension, retirement or similar benefits but does not include expenses (including business travel, professional and business association dues) compared to \$0.4 million in 2012. In addition, we granted an aggregate of 458,000 options to purchase Ordinary Shares to our officers (including the option granted Dr. Moshe BenBassat, described below) at an average exercise price of \$7.80 per share. At our July 28, 2013 Annual Shareholders Meeting, or 2013 ASM, our shareholders approved the grant of options to Dr. Moshe BenBassat (or a consulting company through which he provides services to us). Consequently, the Company granted Dr. BenBassat options to purchase 90,000 Ordinary Shares at an exercise price of \$8.41, the closing sale price of our Ordinary Shares on the trading day immediately preceding the 2013 ASM.

In 2012, we granted an aggregate of 250,000 options to purchase Ordinary Shares to our officers (including the option granted Dr. Moshe BenBassat, described below) at an average exercise price of \$10.03 per share. At our June 28, 2012 Annual Shareholders Meeting, or 2012 ASM, our shareholders approved the grant of options to

Dr. Moshe BenBassat (or a consulting company through which he provides services to us). Consequently, the Company granted Dr. Moshe BenBassat options to purchase 100,000 Ordinary Shares at an exercise price of \$8.22, the closing sale price of our Ordinary Shares on the trading day immediately preceding the 2012 ASM.

In 2011 we granted an aggregate of 130,000 options to our officers (including the option granted Dr. Moshe BenBassat, described below) at an average exercise price of \$9.66 per share. Our July 21, 2011 Annual Shareholders Meeting, or 2011 ASM, approved the grant of options to Dr. Moshe BenBassat (or a consulting company through which he provides services to us) to purchase 100,000 Ordinary Shares at an exercise price of \$9.71, the closing sale price of our Ordinary Shares on the trading day immediately preceding the 2011 ASM.

Options granted to our officers in 2012 and 2013 expire seven years after the date of the grant and vest as follows: 25% on the first anniversary date of grant and 1/48 at the end of each month thereafter.

In addition, we granted an aggregate of 48,000 RSUs in each of 2011, 2012 and 2013 to our non-employee directors in accordance with a plan for equity compensation of our non-employee directors. The exercise price of the RSUs equals the par value of our Ordinary Shares, which is NIS 0.02. This plan provides that (i) each non-employee director who is appointed as our director in 2011 or thereafter is automatically granted 8,000 RSUs, or the First Grant, upon the date such individual first becomes a director; and (ii) each non-employee director is automatically granted 8,000 RSUs, or the Subsequent Grant, following each annual meeting of our shareholders, beginning in 2011, if on such date he or she shall have served on our Board for at least the preceding six months. The terms of each RSU are as follows: (i) the term of the RSU shall be seven years; (ii) the exercise price per share shall be equal to the par value of each share underlying the RSU; (iii) the First Grant shall vest on the first anniversary of the date of grant, provided that the grantee continues to serve as a director on such date; and (iv) each Subsequent Grant shall vest in twelve equal monthly installments after the date of grant, provided that the grantee continues to serve as a director on the applicable vesting date.

In addition to equity compensation, each non-employee director receives an annual cash compensation package of \$22,000 plus VAT, if applicable, and reimbursement of expenses incurred by such director in connection with participation in meetings of the board of directors or committees thereof.

Our executive officers participate in a bonus plan in which they may receive bonuses based on achieving Company goals on revenues and operating profit, and based on achieving personal performance-related goals. The goals for our Chief Executive Officer are determined on an annual basis by the Compensation Committee, and the goals for our other executive officers are determined by the Chief Executive Officer.

In December 2012, an amendment to the Companies Law, or Amendment 20, became effective, requiring companies to appoint a compensation committee. Our existing compensation committee as detailed in Item 6.C. "Board Practices. Compensation Committee" below meets this requirement.

Amendment 20 also required that companies adopt a compensation policy by September 11, 2013, which will set forth company policy, or the Compensation Policy, regarding the terms of office and employment of office holders, including compensation, equity awards, severance and other benefits, exemption from liability, insurance and indemnification, referred to as the Terms of Office and Employment. The term "office holder," is defined in the Companies Law as a general manager, chief executive officer, chief business manager, deputy general manager, vice general manager, any other person assuming the responsibilities of any of the foregoing positions without regard to such person's title, a director and a manager directly subordinate to the chief executive officer.

The Compensation Policy must be approved by the board of directors, after considering the recommendations of the compensation committee. The Compensation Policy must also be approved by a majority of the company's shareholders, provided that (i) such majority includes at least a majority of the shareholders who are not controlling shareholders and who do not have a personal interest in the matter, present and voting (abstentions are disregarded), or (ii) the non-controlling shareholders and shareholders who do not have a personal interest in the matter who were present and voted against the policy hold two percent or less of the voting power of the company (the "Compensation Majority"). The Compensation Policy must be approved by the board of directors and the shareholders every three years. In the event that the Compensation Policy is not approved by the shareholders, the Compensation Committee and the board of directors may nonetheless approve the policy, if the Compensation Committee and the board of directors determine, based on specified reasons and following further discussion of the matter, that the Compensation Policy is in the best interests of the company. Our Compensation Policy for Executive Officers and Directors (the "Compensation Policy") was approved by

our shareholders on July 8, 2013, following the recommendation of the Compensation Committee and approval by our Board of Directors.

Under Amendment 20, the Terms of Office and Employment of office holders require the approval of the Compensation Committee and the board of directors. The Terms of Office and Employment of directors and the chief executive officer must also be approved by shareholders.

Changes to existing Terms of Office and Employment of office holders (other than directors) can be made with the approval of the Compensation Committee only, if the committee determines that the change is not substantially different from the existing terms.

Pursuant to Amendment 20, any arrangement between a company and an office holder (other than a director or the chief executive officer) as to his or her terms of office and employment must be in line with the Compensation Policy and requires the approval of the Compensation Committee and the board of directors. However, under certain circumstances, the Compensation Committee and the board of directors may approve an arrangement that deviates from the Compensation Policy, provided that such arrangement is approved by the company's shareholders by the Compensation Majority. The board of directors and the compensation committee may, under special circumstances and for specified reasons, approve such an arrangement even if the shareholders did not approve it, following a re-discussion of the matter in which, among other things, the shareholders' objection was examined.

### ***Directors***

Pursuant to Amendment 20, any arrangement between a company and a director as to his or her terms of office and employment must be in line with the Compensation Policy and requires the approval of the compensation committee, the board of directors and the shareholders by a simple majority.

Under certain circumstances and conditions, the compensation committee and the board of directors may approve an arrangement that deviates from the Compensation Policy, provided that such arrangement is approved by the company's shareholders by the Compensation Majority.

Under the Companies Law and regulations promulgated pursuant thereto, the compensation payable to external directors and independent directors is subject to certain further limitations.

### ***Chief Executive Officer***

Pursuant to Amendment 20, any arrangement between a company and its chief executive officer as to his or her terms of office and employment must be in line with the Compensation Policy and requires the approval of the compensation committee, the board of directors and the company's shareholders by the Compensation Majority.

Under certain circumstances and conditions, the compensation committee and the board of directors may approve an arrangement that deviates from the Compensation Policy provided it is approved by the shareholders by the Compensation Majority. In addition, under certain circumstances, a company may be exempt from receiving the shareholders' approval with respect to the terms of office and employment of a candidate for chief executive officer if such candidate meets certain independence criteria and the compensation committee has determined for specified reasons that shareholder approval would prevent the engagement, provided that the terms are in line with the Compensation Policy.

Under the Companies Law and related regulations, the compensation payable to statutory independent directors and independent directors is subject to certain further limitations. See Item 6.C. "Board Practices. External and Independent Directors" below.

## **6.C. Board practices**

We are subject to the provisions of the Companies Law, which requires, in part, that Israeli companies whose shares have been offered to the public in or outside of Israel appoint at least two External Directors (as such term is defined in the Companies Law) to serve on their board of directors. In the event that the board does not nominate a candidate to be appointed to a specific class of directors at any annual meeting of shareholders, then instead of electing directors to succeed the directors whose term in office expires at the date of such annual meeting, the shareholders may elect one or more additional External Directors in addition to the minimum number of External Directors required by the Companies Law.

There are no service contracts between us or any of our subsidiaries, on the one hand, and our directors in their capacity as directors, on the other hand, providing for benefits upon termination of service, except for the termination provisions included in the consulting agreement of our chief executive officer who is also a director. The benefits upon termination provided for in such consulting agreements relate solely to the termination of Mr. BenBassat from his position as a consultant, and not from his position as a director or chairman of the board.

In addition to the insurance coverage, we have agreed to indemnify our directors and officers in an amount not to exceed \$20 million, for all persons and all events to be indemnified, for certain events and occurrences while the director or officer is, or was serving, at our request in such capacity. The indemnification agreements entered into with the directors and officers are substantially in the form of the Amended Form of Indemnification Agreement previously filed as an exhibit to this annual report. As permitted under the Companies Law, the indemnification agreements provide protection against personal liability. We have director and officer insurance coverage that may limit our exposure and may enable us to recover a portion of any future amounts paid.

### ***External and Independent Directors***

Under the Companies law, publicly held Israeli companies, such as us, are required to appoint at least two External Directors, each of whom must also serve on the audit committee. All other board committees exercising powers delegated by the board of directors must include at least one External Director.

The initial three-year term of service of External Directors can be extended, at the election of the Company subject to certain conditions, by two additional three-year terms. External Directors will be elected by a majority vote at a shareholders' meeting, provided that either the majority of shares voted at the meeting, including at least one-half of the shares held by non-controlling shareholders voted at the meeting, vote in favor; or the total number of shares held by non-controlling shareholders voted against does not exceed two percent of the aggregate voting rights in the company.

Furthermore, External Directors may be re-elected for additional terms by means of one of the following mechanisms: (i) the board of directors proposed the nominee and his appointment was approved by the shareholders in the manner required to appoint external directors for their initial term, or (ii) a shareholder holding 1% or more of the voting rights proposed the nominee, and the nominee is approved by a majority of the votes cast by the shareholders of the company, excluding the votes of controlling shareholders and those who have a personal interest in the matter as a result of their relations with the controlling shareholders, provided that, the aggregate votes cast by shareholders who are not controlling shareholders and do not have a personal interest in the matter as a result of their relations with the controlling shareholders in favor of the nominee constitute more than 2% of the voting rights in the Company.

The external director who has been nominated in such fashion by the shareholders must not be a linked or competing shareholder, and not have or not had, on or within the two years preceding the date of such person's appointment to serve another term as external director, any affiliation with a linked or competing shareholder. The term "linked or competing shareholder" means the shareholder(s) who nominated the external director for reappointment or a shareholder of the company holding more than 5% of the company's issued share capital or its voting rights, provided that at the time of the reappointment, such shareholder(s) of the company, the controlling shareholder of such shareholder(s) of the company, or a company under such shareholder(s) of the company's control, has a business relationship with the company or is a competitor of the company.

The term of office of external directors of Israeli companies traded on certain foreign stock exchanges, including the Nasdaq Capital Market, may be further extended, indefinitely, in increments of additional three-year terms, in each case provided that, in addition to reelection in such manner described above, (i) the audit committee and subsequently the board of directors of the Company confirm that, in light of the external director's expertise and special contribution to the work of the board of directors and its committees, the reelection for such additional period is beneficial to the Company, and (ii) prior to the approval of the reelection of the external director, the Company's shareholders have been informed of the term previously served by such nominee and of the reasons why the board of directors and audit committee recommended the extension of such nominee's term

External directors can be removed from office only by the court or by the same special majority of shareholders that can elect them, and then only if the external directors cease to meet the statutory qualifications with respect to their appointment or if they violate their fiduciary duty to the company. The court may additionally remove external directors from office if they were convicted of certain offenses by a non-Israeli court or are permanently unable to fulfill their position.

Each of Mr. Beilis, Ms. Dror and Mr. Shalgi serves as an external director.

Under the Companies Law, public companies are required to elect at least two external directors who must meet specified standards of independence. External directors may not have had during the two years preceding their appointment, directly or indirectly through a relative, partner, employer or controlled entity, any affiliation with (i) the company, (ii) those of its shareholders who are controlling shareholders at the time of appointment and/or their relatives, or (iii) any entity controlled by the company or by its controlling shareholders.

The term "affiliation" includes an employment relationship, a business or professional relationship maintained on a regular basis, control and services as an office holder. The term "controlling shareholder" is defined as a shareholder who has the ability to direct the activities of a company, other than if this power derives solely from the shareholder's position on the board of directors or any other position with the company. The definition also includes shareholders that hold 25% or more of the voting rights if no other shareholder holds more than 50% of the voting rights in the company.

In addition, an individual may not be appointed as an External Director in a company that does not have a controlling shareholder, in the event that he has affiliation, at the time of his appointment, to the chairman, chief executive officer, a 5% shareholder or the chief financial officer. An individual may not be appointed as an External Director if his relative, partner, employer, supervisor, or an entity he controls, has other than negligible business or professional relations with any of the persons with which the External Director himself may not be affiliated.

No person can serve as an external director if the person's other positions or business creates or may create conflicts of interest with the person's responsibilities as an external director. Until the lapse of two years from termination of office, a company may not engage an external director as an employee or otherwise. If, at the time an external director is to be appointed, all current members of the board of directors, who are not controlling shareholders of the company or their relatives, are of the same gender, then at least one external director appointed must be of the other gender.

If delegated any authority of the board of directors, any committee of the board of directors must include at least one external director. An external director is entitled to compensation as provided in regulations adopted under the Companies Law and is otherwise prohibited from receiving any other compensation, directly or indirectly, in connection with such service.

The Companies Law requires external directors to submit to the company, prior to the date of the notice of the general meeting convened to elect the external directors, a declaration stating their compliance with the requirements imposed by the Companies Law for the office of external director.

Israeli law further requires that at least one External Director has either financial and accounting expertise, or professional competence, as determined by the Company's board of directors. At least one of the external directors is required to qualify as a financial and accounting expert, as determined by the board of directors. Under relevant regulations, a director having financial and accounting expertise is a person who, due to his or her education, experience and talents, is highly skilled in respect of, and understands, business and accounting matters and financial reports, in a manner that enables him or her to have an in-depth understanding of the Company's financial information and to stimulate discussion in respect of the manner in which the financial data is presented. Under relevant regulations, a director having professional competence is a person who meets any of the following criteria: (i) has an academic degree in either economics, business administration, accounting, law or public administration; (ii) has a different academic degree or has completed higher education in an area relevant to the company's business or in an area relevant to his or her position; or (iii) has at least five years' experience in at least two of the following: (a) a senior position in the business management of a corporation with a substantial scope of business (b) a senior public position or a senior position in public service, or (c) a senior position in the main field of the Company's business.

Ms. Dror was determined by our board of directors to be a financial and accounting expert and Mr. Beilis was determined to have professional competence, each as determined by Israeli law.

#### ***Audit Committee***

Our audit committee consists of Dr. Nass, Ms. Dror, Mr. Beilis, Mr. Weiser and Mr. Shalgi, each of whom is "independent," as such term is currently defined in Rule 5605(a)(2) to the Nasdaq Rules. Our board of directors

has determined that Dr. Nass also qualifies as an "audit committee financial expert" within the meaning of SEC rules and has the requisite experience under Nasdaq Rules. The audit committee provides assistance to the board of directors in fulfilling its legal and fiduciary obligations with respect to matters involving the accounting, auditing, financial reporting and internal control functions of our Company and our subsidiaries as well as complying with the legal requirements under Israeli law and the regulation promulgated under the Sarbanes-Oxley Act of 2002. The purposes of the audit committee include:

- overseeing the accounting and financial reporting processes of our Company and audits of its financial statements;
- assessing the scope of work of the independent registered public accounting firm and recommending to our shareholders to appoint and approve the compensation of the independent registered public accounting firm engaged to audit our financial statements;
- overseeing and monitoring (i) the integrity of our financial statements, (ii) our compliance with legal and regulatory requirements as they relate to financial statements or accounting matters, (iii) the independent registered public accounting firm's qualifications, independence and performance, and (iv) our internal accounting and financial controls;
- provide our board of directors with the results of its monitoring and recommendations derived therefrom;
- provide to our board of directors such additional information and materials as it may deem necessary to make it aware of significant financial matters that require its attention;
- monitor deficiencies in the management of the Company, inter alia, in consultation with the independent registered public accounting firm and internal auditor, and advise our board of directors on how to correct the deficiencies;
- decide whether to approve engagements or transactions that require Audit Committee approval under the Companies Law, relating generally to certain related party transactions, approval of the terms of employment of officers and determining whether certain related party actions and transactions are "material" or "extraordinary" in connection with their approval procedures;
- meet and receive reports from both the internal auditors and independent registered public accounting firm dealing with matters that arise in connection with their audits;
- assessing the our internal audit system and the performance of our internal auditor;
- determining whistle blower procedures (including in respect of the protections afforded to whistle blowers); and
- conduct any investigation appropriate to fulfilling its responsibilities, and have direct access to the independent registered public accounting firm as well as anyone in our Company.

Under the Companies Law, publicly traded companies must establish an audit committee. The audit committee must consist of at least three members, and must include all of the company's external directors. The majority of the members of the audit committee, as well as the majority of members present at audit committee meetings, will be required to be "independent directors" (as defined in the Companies Law) and the chairman of the audit committee will be required to be an External Director. In addition, under the amendment, the following will be disqualified from serving as members of the audit committee: the chairman of the board, the controlling shareholder and his relatives, any director employed by the company or by its controlling shareholder or by an entity controlled by the controlling shareholder, a director who regularly provides services to the company or to its controlling shareholder or to an entity controlled by the controlling shareholder, and any director who derives most of his or her income from the controlling shareholder. Any persons disqualified from serving as a member of the audit committee may not be present at the audit committee meetings, unless the chairman of the audit committee has determined that such person is required to be present at the meeting or if such person qualifies under one of the exemptions specified in the Companies Law.

An audit committee may not approve an action or a transaction with an officer or director, a transaction in which an officer or director has a personal interest, a transaction with a controlling shareholder and certain other transactions specified in the Companies Law, unless at the time of approval two external directors are serving as members of the audit committee and at least one of the external directors was present at the meeting in which an approval was granted.

Our audit committee convenes at least once per quarter to review our quarterly financial results and to address other matters within the committee's responsibilities. Our audit committee duties are governed by a written charter.

### ***Compensation Committee***

Under the Companies Law, publicly traded companies must establish a compensation committee, which must consist of at least three directors. Under the Companies Law, the compensation committee must include all of the statutory independent directors, one of which must serve as the chairman of the committee, and the committee must include only additional members that satisfy the criteria for remuneration applicable to the statutory independent directors. Our compensation committee consists of Mr. Beilis, Ms. Dror and Mr. Shalgi, each of whom is "independent," as such term is defined in Rule 5605(a)(2) to the Nasdaq Rules and our compensation committee meets the requirements of the Companies Law.

Under the Companies Law, the compensation committee is responsible for: (i) making recommendations to the board of directors with respect to the approval of the Compensation Policy and any extensions thereto; (ii) periodically reviewing the implementation of the Compensation Policy and providing the board of directors with recommendations with respect to any amendments or updates thereto; (iii) reviewing and resolving whether or not to approve arrangements with respect to the Terms of Office and Employment of office holders; and (iv) determining whether or not to exempt a transaction with a candidate for chief executive officer from shareholder approval.

Our compensation committee meets at least twice a year and its duties are governed by a written charter.

### ***Corporate Governance and Nominating Committee***

Our corporate governance and nominating committee consists of Dr. Nass, Ms. Dror and Mr. Beilis, each of whom is "independent," as such term is defined in Rule 5605(a)(2) to the Nasdaq Rules. Our corporate governance and nominating committee meets at least once a year. Functions of the corporate governance and nominating committee include:

- to monitor the composition of our board of directors and, when appropriate, seek, screen and recommend for nomination qualified candidates for election to our board of directors at the Company's annual meeting of shareholders;
- to seek qualified candidates to fill vacancies on our board of directors;
- to evaluate candidates identified on its own initiative as well as candidates referred to it by other members of the board of directors, by our management, by shareholders who submit names to our secretary for referral to the corporate governance and nominating committee, or by other external sources; and
- to evaluate the structure and practices of our board of directors and, when appropriate, recommend new policies.

Our corporate governance and nominating committee duties are governed by a written charter. In addition, a code of recommended corporate governance practices has been attached to a recent amendment to the Companies Law which we intend to refer to if applicable and not inconsistent with our written charter.

## **6.D. Employees**

At December 31, 2013, we had 602 full time employees. Of these employees, 269 were based in Israel, 145 in Americas, 100 in Asia Pacific and 88 in EMEA.

The following is a detailed breakdown of persons employed by main category of activity, as at December 31, 2013:

<u>Department</u>	<b>YEAR ENDED DECEMBER 31,</b>		
	<u>2013</u>	<u>2012</u>	<u>2011</u>
Services	288	245	199
Research and Development	94	88	66
Sales and Marketing	146	112	85
General and Administrative	74	64	55
<b>Total</b>	<b>602</b>	<b>509</b>	<b>405</b>

In addition to the number of full-time employees listed above, as at December 31, 2013 we had 79 full-time contractors in Israel (compared to 52 full-time contractors as at December 31, 2012) who work at an offsite location, focusing mainly on quality assurance for our professional services and research and development organizations.

We believe that our relations with our employees are good. Neither our employees nor we are party to any collective bargaining agreements, except for provisions of such agreements that are applicable to the industry by virtue of extension orders issued under applicable Israeli laws.

Israeli law and certain provisions of the nationwide collective bargaining agreements between the Histadrut (General Federation of Labor in Israel) and the Manufacturer's Association of Israel apply to our Israeli employees. These provisions principally concern the maximum length of the work day and the work week, minimum wages, paid annual vacation, contributions to a pension fund, insurance for work-related accidents, procedures for dismissing employees, determination of severance pay and other conditions of employment. We provide our employees with benefits and working conditions above the required minimums. Furthermore, pursuant to such provisions, the wages of most of our employees are subject to cost of living adjustments, based on changes in the Israeli CPI. The amounts and frequency of such adjustments are modified from time to time. Israeli law generally requires the payment of severance upon the retirement or death of an employee or upon termination of employment by the employer or, in certain circumstances, by the employee. We currently fund our ongoing severance obligations for our Israeli employees by making monthly payments for insurance policies and severance funds. Outside of Israel we accrue severance pay obligations when required under the applicable laws in such jurisdictions. Severance pay obligations made to Israeli employees are significant compared to employees of our subsidiaries outside of Israel. Severance payment expenses, net of changes in the value the insurance policies and severance funds, amounted to \$1,932,000 in 2013, \$1,632,000 in 2012, and \$1,383,000 in 2011. The increase in 2013, 2012 and 2011 was largely attributable to appreciation in the value of the insurance policies and severance funds as well as to an increase in the number of employees. We obtain and maintain for all of our Israeli employees' pension funds or manager's insurance as required by applicable Israeli law.

We typically maintain non-competition agreements with our employees which prohibit them, if they cease working for us, from directly competing with us or working for our competitors. Israeli courts have required employers seeking to enforce non-compete undertakings of a former employee to demonstrate that the competitive activities of the former employee will harm one of a limited number of material interests of the employer which have been recognized by the courts, such as the secrecy of a Company's confidential commercial information or its intellectual property. If we cannot demonstrate that material harm would be caused to us, we will be unable to enforce these non-competition agreements and our competitors may be able to benefit from the expertise of our former employees.

Effective as of the closing of the acquisition of Xora on March 4, 2014, we added about 130 employees.

#### **6.E. Share ownership**

As of March 25, 2014, each of our executive officers and directors beneficially owned less than 1% of our Ordinary Shares, with the exception of Dr. Moshe BenBassat, who beneficially owned 2,264,079 Ordinary Shares (or 6.9% of our outstanding Ordinary Shares), which includes 640,500 options for the purchase of our Ordinary Shares.

The following table summarizes information about the options to purchase our Ordinary Shares owned by Dr. Moshe BenBassat that were outstanding as of March 25, 2014:

RANGE OF EXERCISE PRICE \$	NUMBER OUTSTANDING AT MARCH 25, 2014	NUMBER EXERCISABLE AT MARCH 25, 2014 <sup>(1)</sup>	EXPIRATION DATE
1.92-2.81	228,000	228,000	2014-2015
4.43	70,000	70,000	2014
5.91	100,000	95,834	2017
8.12	130,000	130,000	2016
8.22	100,000	45,833	2019
8.41	90,000	-	2020
9.71	100,000	70,833	2018
	818,000	640,500	

<sup>(1)</sup> Includes options for Ordinary Shares held that are exercisable within 60 days of the date stated above.

### **Share Incentive Plans**

We have established a number of employee option plans containing terms and conditions for the vesting and exercising of options granted to employees for the purchase of our Ordinary Shares.

Our umbrella stock option plan, as amended, or the Plan, was adopted in 2000 and defines our stock option pool available for grants worldwide. Employees outside of the United States typically receive options under a local stock option plan from the worldwide pool defined by the Plan. Pursuant to the Plan's evergreen mechanism, or Evergreen Mechanism, the number of Ordinary Shares made available thereunder automatically increases on the first day of the Company's fiscal year to equal the lesser of: (i) 5% of the outstanding Ordinary Shares on such date, (ii) 1,250,000 Ordinary Shares or (iii) an amount determined by the Company's board of directors. In accordance with the Evergreen Mechanism, the board of directors increased the number of Ordinary Shares reserved under the Plan by 7,097,269 Ordinary Shares in the aggregate. As of March 25, 2014, 2,319,139 options were available under the Plan.

The purposes of the Plan are to enable us to attract and retain qualified persons as employees, officers, directors, consultants, advisors and service providers and to motivate such persons by providing them with an equity participation in our company. The Plan will expire in 2017, unless terminated earlier by the board of directors.

The Plan was amended at our 2010 ASM to include the right to grant RSUs. Currently, RSUs have been granted only to independent directors. For more information about grants of RSUs to our directors, please see Item 6.B. "Compensation".

The Plan is administered by our board of directors or a committee of our board of directors, which has broad discretion, subject to certain limitations, to determine the persons entitled to receive options. Options generally have a term of between seven and ten years. Earlier termination may occur if an individual's employment with us is terminated or if certain corporate changes or transactions occur. Our board of directors determines the grant and the exercise price at the time the options are granted.

Under the Plan, the terms and conditions under which options are granted and the number of shares subject thereto are determined by our board of directors or a committee of our board of directors. The board of directors or such committee also has discretion to determine the nature of the consideration to be paid upon the exercise of an option under the Plan. Such consideration generally consists of cash, but may include a recourse promissory note.

The Ordinary Shares acquired upon exercise of an option are subject to certain restrictions on transfer, sale or hypothecation. Options are exercisable and restrictions on disposition of shares lapse pursuant to the terms of the individual agreements under which the options were granted or the shares were issued.

The exercise price per share is usually granted at the approximate fair market value of the shares on the date of grant, as determined by the closing price of our Ordinary Shares as reported by Nasdaq on the date immediately prior to the date of grant.

Each share incentive agreement specifies the date and period over which the option becomes exercisable. Options granted by us generally vest over a period of four years.

Vesting is conditional upon the employee remaining continuously employed by us, or in the case of a director, remaining a director.

In 2001, we adopted the 2000 Approved U.K. Share Scheme for our employees located in the United Kingdom and in 2003, we adopted the 2003 Israeli Share Option Plan for our employees located in Israel, both of which were adopted under the Plan.

## ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

### 7.A. Major shareholders

The following table sets forth, as of the date indicated below, the total number of Ordinary Shares beneficially owned by (i) all shareholders known to us to own more than 5% of our outstanding Ordinary Shares, and (ii) all of our directors and executive officers as a group. Unless otherwise set forth below, the information below reflects holdings as of March 25, 2014.

<u>Name and Address</u>	<u>Ordinary Shares Beneficially Owned</u>	
	<u>Number</u>	<u>Percent</u> <sup>(1)</sup>
Dr. Moshe BenBassat <sup>(2)</sup>	2,264,079	6.9%
Idit BenBassat <sup>(3)</sup>	1,775,694	5.4%
G. Nicholas Farwell <sup>(4)</sup>	2,149,920	6.5%
FMR LLC <sup>(5)</sup>	2,937,476	8.9%
Soros Fund Management LLC <sup>(6)</sup>	3,130,000	9.5%
Officers and directors as a group <sup>(7)</sup> (11 persons)	2,875,882	8.7%

(1) The percentages shown are based on 32,922,650 shares issued and outstanding as of March 25, 2014.

(2) Includes (i) 428,001 options to purchase the Company's ordinary shares, exercisable within 60 days of March 25, 2014 held by Dr. BenBassat; (ii) 1,623,579 shares held by Dr. BenBassat and (iii) 212,499 options to purchase the Company's Ordinary Shares exercisable within 60 days of March 25, 2014 held by Plataine Technologies Ltd., an Israeli corporation controlled by Idit BenBassat and Dr. BenBassat (the "Plataine Options"). The Plataine Options were granted by the Company in connection with services provided to the Company by Dr. BenBassat through Plataine Technologies Ltd. The Plataine Options are reported as beneficially owned in their entirety by both Idit BenBassat, on the amendment to Schedule 13G she filed on February 13, 2014, and by Dr. BenBassat, herein, because of their shared control of Plataine Technologies Ltd.; however, they constitute only a single set of options.

(3) Based on Amendment No. 3 to Schedule 13G filed with the SEC on February 13, 2014 by Idit BenBassat, and which reflects holdings as of December 31, 2013. Includes 1,581,944 shares held by Idit BenBassat and 193,750 options to purchase the Company's Ordinary Shares exercisable within 60 days of December 31, 2013 held by Plataine Technologies Ltd., an Israeli corporation controlled by Idit BenBassat and Dr. Moshe BenBassat. The Plataine Options were granted by the Company in connection with services provided through Plataine by Dr. Moshe BenBassat to the Company. The Plataine Options are reported as beneficially owned in their entirety by both Dr. Moshe BenBassat and Idit BenBassat on the amendments to Schedule 13G that each filed because of their shared control of Plataine Technologies Ltd., but constitute only a single set of options.

(4) Based solely on information provided by G. Nicholas Farwell to us on February 13, 2013.

(5) Based solely on Amendment No. 4 to Schedule 13G filed with the SEC on February 14, 2014 by FMR LLC and certain of its affiliates, which reflect holdings as of December 31, 2013. Edward C. Johnson 3d, together with family members, is reported as being deemed to control FMR LLC.

(6) Based solely on Amendment No. 1 to Schedule 13G filed with the SEC on February 14, 2013 by Soros Fund Management LLC and its affiliates George Soros and Robert Soros, and which reflect holdings as of December 31, 2012.

(7) Includes 888,148 Ordinary Shares for which options and RSUs exercisable within 60 days of the date stated above, but does not include 545,379 Ordinary Shares for which options and RSUs granted to officers and directors which are not currently, and will not within 60 days be, exercisable.

Changes in the percentage of ownership of major shareholders during the past three years were as follows:

	<u>Year Ended December 31,</u> <u>2010</u>		<u>Year Ended December 31,</u> <u>2013</u>	
		%		%
Total shares	30,634,227		32,494,575	
Dr. Moshe BenBassat	2,218,302	6.9%	2,445,329	7.5%
Idit BenBassat	1,680,887	5.5%	1,775,694	5.5%
FMR LLC	2,936,098	9.6%	2,937,476	9.0%
Soros Fund Management LLC	(*)	-%	3,130,000	9.6%
G. Nicholas Farwell	2,134,105	7.0%	2,149,920	6.6%

(\*) *Not known to us.*

Our major shareholders do not have different voting rights from each other or other shareholders.

According to our transfer agent, as of December 31, 2013, there were 20 holders of record of our Ordinary Shares in the United States, representing approximately 93% of our outstanding shares. The number of record holders in the United States is not representative of the number of beneficial holders nor is it representative of where such beneficial holders reside since many of our Ordinary Shares are held by brokers or other nominees. None of the Company's preferred Shares are issued or outstanding.

To our knowledge, we are not directly or indirectly owned or controlled by another corporation, any foreign government or any other natural or legal person severally or jointly.

#### **7.B. Related party transactions**

Since January 1, 2013, we have engaged in no material commercial transactions with related parties, nor are there any outstanding loans to related parties concerning this period of time, except for service agreements with our Chief Executive Officer Dr. Moshe BenBassat (See Item 10.C "Material contracts not in the ordinary course of business") and compensation to our directors and officers (See Item 6.B "Compensation").

#### **7.C. Interests of experts and counsel**

Not applicable.

### **ITEM 8. FINANCIAL INFORMATION**

#### **8.A. Consolidated statements and other financial information**

See Item 18 – Financial Statements.

##### ***Export Sales***

Export sales from Israel in 2013 were \$103 million, or 99.8% of revenues, compared with \$99.6 million, or 99.5% of revenues, in 2012, and \$86.2 million, or 99.0% of revenues, in 2011.

##### ***Legal Proceedings***

From time to time, we are involved in various routine legal proceedings incidental to the ordinary course of our business. We do not believe that the outcome of these legal proceedings have had in the recent past, or will have (with respect to any pending proceedings), significant effects on our financial position or profitability.

##### ***Dividends***

We do not have a formal dividend policy governing the amounts and payment of dividends. Until 2011, we retained all earnings for use in our business. During 2011, we declared a cash dividend to our shareholders in the amount of \$10 million (\$0.32 per share). During 2011, we distributed a cash dividend of \$7.5 million (\$0.24

per share). During 2012, we declared a cash dividend to our shareholders in the amount of \$7.5 million (\$0.24 per share) and distributed a cash dividend of \$10 million (\$0.32 per share). During 2013, we declared a cash dividend to our shareholders in the amount of \$6.7 million (\$0.21 per share) and distributed a cash dividend of \$6.7 million (\$0.21 per share). Payment of future dividends is at the discretion of our board of directors.

## 8.B. Significant changes

Except as disclosed elsewhere in this annual report, there have been no other significant changes since December 31, 2013.

## ITEM 9. THE OFFER AND LISTING

### 9.A. Offer and listing details

Our Ordinary Shares are listed for trading on the Nasdaq Global Select Market. The following table sets forth for the periods listed the high and low market prices of our Ordinary Shares on the Nasdaq Global Select Market (since July 1, 2009) or Nasdaq Capital Market (prior to July 1, 2009).

	<u>High</u>	<u>Low</u>
<b>Annual Information</b>	(\$)	(\$)
2009	8.43	1.88
2010	8.07	4.82
2011	10.70	7.24
2012	12.98	6.88
2013	9.06	5.84
 <b>Quarterly Information</b>		
First quarter 2012	12.98	9.48
Second quarter 2012	12.96	8.02
Third quarter 2012	8.74	7.09
Fourth quarter 2012	8.72	6.88
First quarter 2013	9.06	7.91
Second quarter 2013	8.37	7.01
Third quarter 2013	8.41	5.84
Fourth quarter 2013	7.57	5.88
 <b>Monthly Information</b>		
September 2013	6.85	5.84
October 2013	7.47	5.88
November 2013	7.36	7.02
December 2013	7.57	7.09
January 2014	9.40	7.27
February 2014	10.29	8.50
March 2014 (through March 24)	10.68	9.88

### 9.B. Plan of distribution

Not applicable.

### 9.C. Market for Ordinary Shares

Our Ordinary Shares have been quoted on the Nasdaq Global Select Market since July 1, 2009 under the symbol CKSW. From August 29, 2002 to July 1, 2009, our Ordinary Shares were traded on the Nasdaq Capital Market

under the same symbol (except between November 6, 2002 and March 6, 2003, when our symbol was CKSWE). Prior to that, beginning on June 22, 2000, our Ordinary Shares were quoted on the Nasdaq National Market under the same symbol, CKSW.

**9.D. Selling shareholders**

Not applicable.

**9.E. Dilution**

Not applicable.

**9.F. Expenses of the issue**

Not applicable.

**ITEM 10. ADDITIONAL INFORMATION**

**10.A. Share capital**

Not applicable.

**10.B. Memorandum and articles of association**

*Securities Register*

We are registered with the Israeli Registrar of Companies. Our registration number is 510829971. Section 2 of our articles of association provides that we may engage in any type of lawful business as may be determined by our board of directors from time to time.

*Board of Directors*

The Companies Law requires that certain transactions, actions and arrangements be approved as provided for in a company's articles of association and in certain circumstances by the audit committee (or with respect to terms of office and employment, the compensation committee), by the board of directors itself and by the shareholders. The vote required by the audit committee and the board of directors for approval of such matters, in each case, is a majority of the disinterested directors participating in a duly convened meeting.

The Companies Law requires that an office holder in the company or a controlling shareholder in a public company promptly disclose any personal interest that he or she may have (either directly or by way of any corporation in which he or she is, directly or indirectly, a 5% or greater shareholder, director or general manager or in which he or she has the right to appoint at least one director or the general manager) and all related material information known to him or her, in connection with any existing or proposed transaction by the company, no later than the first meeting of the board of directors to discuss such existing or proposed transaction. For these purposes, a shareholder that holds 25% or more of the voting rights in a company is considered a controlling shareholder if no other shareholder holds more than 50% of the voting rights. In addition, if the transaction is an extraordinary transaction (that is, a transaction other than in the ordinary course of business, otherwise than on market terms, or is likely to have a material impact on the company's profitability, assets or liabilities), the office holder in the company or a controlling shareholder in a public company also must disclose any personal interest held by his or her spouse, siblings, parents, grandparents, descendants, spouse's descendants and the spouses of any of the foregoing. Under the Companies Law, extraordinary transactions with a controlling shareholder or in which a controlling shareholder has a personal interest, and agreements relating to employment and compensation of a controlling shareholder, require shareholders' approval that shall either include at least one-half of the shares held by disinterested shareholders participating in the vote, or, alternatively, the total shareholdings of disinterested shareholders voting against the transaction must not represent more than two percent of the voting rights; agreements relating to engagement or provision of services for a period exceeding three years, must generally be approved once every three years.

Once the office holder in the company complies with the above disclosure requirement, a company may approve the transaction in accordance with the provisions of its articles of association. If the transaction is with a third

party in which the office holder in the company has a personal interest, the approval must confirm that the transaction is not adverse to the company's interest. Furthermore, if the transaction is an extraordinary transaction, then, in addition to any approval stipulated by the articles of association, it also must be approved by the company's audit committee (or with respect to terms of office and employment, the compensation committee) and then by the board of directors, and, under certain circumstances, by the shareholders.

Our articles of association provide that, all actions done bona fide at any meeting of the board of directors or by a committee thereof or by any person(s) acting as director(s) will, notwithstanding that it may afterwards be discovered that there was some defect in the appointment of the participants in such meeting or any of them or any person(s) acting as aforesaid, or that they or any of them were disqualified, be as valid as if there were no such defect or disqualification.

- Our articles of association provide that a director who has a personal interest in an extraordinary transaction which is brought for discussion before our board of directors or our audit committee shall neither vote in nor attend discussions concerning the approval of such transaction. If the director did vote or attend as aforesaid, the approval given to the aforesaid activity or arrangement will be invalid.
- Our articles of association provide that, subject to the Companies Law, our board of directors may delegate its authority, in whole or in part, to such committees of the board of directors as it deems appropriate, and it may from time to time revoke such delegation. To the extent permitted by the Companies Law, our board of directors may from time to time confer upon and delegate to a President, Chief Executive Officer, Chief Operating Officer or other executive officer then holding office, such authorities and duties of the board of directors as it deems fit, and they may delegate such authorities and duties for such period and for such purposes and subject to such conditions and restrictions which they consider in our best interests, without waiving the authorities of the board of directors with respect thereto.
- Arrangements regarding compensation of directors require the approval of the compensation committee, audit committee, our board of directors and the shareholders.

#### ***Rights, Preferences and Restrictions of Shares***

- General. Our share capital is NIS 2,100,000, divided into: (i) 100,000,000 Ordinary Shares, and (ii) 5,000,000 Special Preferred Shares of NIS 0.02 par value each. Our Ordinary Shares do not have preemptive rights.
- The Ordinary Shares do not have cumulative voting rights in the election of directors. As a result, the holders of Ordinary Shares that represent more than 50% of the voting power have the power to elect all the Directors.
- Dividend and liquidation rights. Our board of directors may declare a dividend to be paid to the holders of our Ordinary Shares according to their rights and interests in our profits and may fix the record date for eligibility and the time for payment. The directors may from time to time pay to the shareholders on account of the next forthcoming dividend such interim dividends as, in their judgment, our position justifies. All dividends unclaimed for one year after having been declared may be invested or otherwise used by the directors for our benefit until claimed. No unpaid dividend or interest shall bear interest as against us. Our board of directors may determine that a dividend may be paid, wholly or partially, by the distribution of certain of our assets or by a distribution of paid up shares, debentures or debenture stock or any of our securities or of any other companies or in any one or more of such ways in the manner and to the extent permitted by the Companies Law.
- Transfer of shares; record dates. Fully paid up Ordinary Shares may be freely transferred pursuant to our articles of association unless such transfer is restricted or prohibited by another instrument or securities laws. Each shareholder who would be entitled to attend and vote at a General Meeting of shareholders is entitled to receive notice of any such meeting. For purposes of determining the shareholders entitled to notice and to vote at such meeting, the board of directors will fix a record date.
- Voting; annual general and extraordinary meetings. Subject to any rights or restrictions for the time being attached to any class or classes of shares, each shareholder shall have one vote for each share of which he or she is the holder, whether on a show of hands or on a poll. Our articles of association do not permit cumulative voting and it is not mandated by Israeli law. Votes may be given either personally or by proxy. A proxy need not be a shareholder. If any shareholder is without legal capacity, he may vote by means of a trustee or a legal custodian, who may vote either personally or by proxy. If two or

more persons are jointly entitled to a share then, in voting upon any question, the vote of the senior person who tenders a vote, whether in person or by proxy, shall be accepted to the exclusion of the votes of the other registered holders of the share and, for this purpose seniority shall be determined by the order in which the names stand in the shareholder register.

- No business shall be transacted at any General Meeting unless a quorum is present when the meeting proceeds to business. The quorum at any Meeting shall be two shareholders present in person or by proxy, holding or representing at least 33% of our total voting rights. A meeting adjourned for lack of quorum is adjourned to the same day in the next week at the same time and place, or any time and hour as the board of directors shall designate and state in a notice to the shareholders entitled to vote at the original meeting, and if, at such adjourned meeting, a quorum is not present within half an hour from the time appointed for holding the meeting any two shareholders present in person or by proxy shall constitute a quorum. Notwithstanding the aforesaid, if a General Meeting is convened at the demand of shareholders as permitted by of the Companies Law, then a quorum at such adjourned meeting shall be one or more shareholders holding in the aggregate at least 5% of our issued share capital and at least 1% of our voting rights, or one or more shareholders who hold in the aggregate at least 5% of our voting rights. Rule 5620(c) to Nasdaq Rules requires that an issuer listed on the Nasdaq Global Select Market should have a quorum requirement that in no case be less than 33 1/3% of the outstanding shares of the company's common voting stock. However, as mentioned above, our articles of association, consistent with the Companies Law, provide for a lower general quorum requirement of 33% of our outstanding shares and an even lower quorum in the event that the required quorum is not present within half an hour from the time appointed for holding an adjourned meeting, or, in the case the meeting that was adjourned was convened by the shareholders, if the required quorum is not present at the time appointed for holding such adjourned meeting.
- Unless a longer period for notice is prescribed by the Companies Law, at least 10 days and not more than 60 days' notice of any general meeting shall be given, specifying the place, the day and the hour of the meeting and, in the case of special business, the nature of such business, shall be given in the manner hereinafter mentioned, to such shareholders as are under the provisions of our articles of association, entitled to receive notices from us. Only shareholders of record as reflected on our share register at the close of business on the date fixed by the board of directors as the record date determining the then shareholders who will be entitled to vote, shall be entitled to notice of, and to vote, in person or by proxy, at a general meeting and any postponement or adjournment thereof.
- General Meetings are held at least once in every calendar year at such time (within a period of 15 months after the holding of the last preceding General Meeting), and at such time and place as may be determined by the board of directors. At a General Meeting, decisions shall be adopted only on matters that were specified on the agenda. The board of directors is obligated to call extraordinary general meeting of the shareholders upon a written request in accordance with the Companies Law. The Companies Law provides that an extraordinary general meeting of shareholder may be called by the board of directors or by a request of two directors or 25% of the directors in office, or by shareholders holding at least 5% of the issued share capital of the company and at least 1% of the voting rights, or of shareholders holding at least 5% of the voting rights of the company.
- Except as otherwise provided in the articles of association, any resolution at a General Meeting shall be deemed adopted if approved by the holders of a majority of our voting rights represented at the meeting in person or by proxy and voting thereon. In the case of an equality of votes, the chairman of the meeting shall not be entitled to a further or casting vote.
- Discrimination against shareholders. According to our articles of association, there are no discriminating provisions against any existing or prospective holders of our shares as a result of a shareholder holding a substantial number of shares.

### ***Modification of Class Rights***

If, at any time, the share capital is divided into different classes of shares, the rights attached to any class (unless otherwise provided by the terms of issuance of the shares of that class) may be varied with the consent in writing of the holders of all the issued shares of that class, or with the sanction of a majority vote at a meeting of the shareholders passed at a separate meeting of the holders of the shares of the class. The provisions of our articles of association relating to general meetings shall apply, mutatis mutandis, to every such separate general meeting. Any holder of shares of the class present in person or by proxy may demand a secret poll.

Unless otherwise provided by the conditions of issuance, the enlargement of an existing class of shares, or the issuance of additional shares thereof, shall not be deemed to modify or abrogate the rights attached to the previously issued shares of such class or of any other class. These conditions provide for the minimum shareholder approvals permitted by the Companies Law.

### ***Restrictions on Shareholders Rights to Own Securities***

Our articles of association and the laws of the State of Israel do not restrict in any way the ownership or voting or our shares by non-residents of Israel, except with respect to subjects of countries which are in a state of war with Israel.

### ***Acquisitions under Israeli Law***

#### **Full tender offer**

A person wishing to acquire shares of an Israeli public company and who would as a result hold over 90% of the target company's issued and outstanding share capital is required by the Companies Law to make a tender offer to all of the company's shareholders for the purchase of all of the issued and outstanding shares of the company.

A person wishing to acquire shares of an Israeli public company and who would as a result hold over 90% of the issued and outstanding share capital of a certain class of shares is required to make a tender offer to all of the shareholders who hold shares of the same class for the purchase of all of the issued and outstanding shares of the same class.

If the shareholders who do not respond to or accept the offer hold less than 5% of the issued and outstanding share capital of the company or of the applicable class of the shares, and more than half of the shareholders who do not have a personal interest in the offer accept the offer, all of the shares that the acquirer offered to purchase will be transferred to the acquirer by operation of law. However, a tender offer will be accepted if the shareholders who do not accept it hold less than 2% of the issued and outstanding share capital of the company or of the applicable class of the shares.

Upon a successful completion of such a full tender offer, any shareholder that was an offeree in such tender offer, whether such shareholder accepted the tender offer or not, may, within six months from the date of acceptance of the tender offer, petition the Israeli court to determine whether the tender offer was for less than fair value and that the fair value should be paid as determined by the court. However, under certain conditions, the offeror may determine in the terms of the tender offer that an offeree who accepted the offer will not be entitled to petition the Israeli court as described above.

If the shareholders who did not respond or accept the tender offer hold at least 5% of the issued and outstanding share capital of the company or of the applicable class, the acquirer may not acquire shares of the company that will increase its holdings to more than 90% of the company's issued and outstanding share capital or of the applicable class from shareholders who accepted the tender offer.

#### **Special tender offer**

The Companies Law provides that an acquisition of shares of an Israeli public company must be made by means of a special tender offer if as a result of the acquisition the purchaser would become a holder of at least 25% of the voting rights in the company. This rule does not apply if there is already another holder of at least 25% of the voting rights in the company.

Similarly, the Companies Law provides that an acquisition of shares in a public company must be made by means of a special tender offer if as a result of the acquisition the purchaser would become a holder of more than 45% of the voting rights in the company, if there is no other shareholder of the company who holds more than 45% of the voting rights in the company.

These requirements do not apply if the acquisition (i) occurs in the context of a private offering, on the condition that the shareholders meeting approved the acquisition as a private offering whose purpose is to give the acquirer at least 25% of the voting rights in the company if there is no person who holds at least 25% of the voting rights in the company, or as a private offering whose purpose is to give the acquirer 45% of the voting rights in the company, if there is no person who holds 45% of the voting rights in the company; (ii) was from a shareholder

holding at least 25% of the voting rights in the company and resulted in the acquirer becoming a holder of at least 25% of the voting rights in the company; or (iii) was from a holder of more than 45% of the voting rights in the company and resulted in the acquirer becoming a holder of more than 45% of the voting rights in the company.

The special tender offer may be consummated only if (i) at least 5% of the voting power attached to the company's outstanding shares will be acquired by the offeror and (ii) the special tender offer is accepted by a majority of the votes of those offerees who gave notice of their position in respect of the offer; in counting the votes of offerees, the votes of a holder of control in the offeror, a person who has personal interest in acceptance of the special tender offer, a holder of at least 25% of the voting rights in the company, or any person acting on their or on the offeror's behalf, including their relatives or companies under their control, are not taken into account.

In the event that a special tender offer is made, a company's board of directors is required to express its opinion on the advisability of the offer or shall abstain from expressing any opinion if it is unable to do so, provided that it gives the reasons for its abstention.

An office holder in a target company who, in his or her capacity as an office holder, performs an action the purpose of which is to cause the failure of an existing or foreseeable special tender offer or is to impair the chances of its acceptance, is liable to the potential purchaser and shareholders for damages resulting from his acts, unless such office holder acted in good faith and had reasonable grounds to believe he or she was acting for the benefit of the company. However, office holders of the target company may negotiate with the potential purchaser in order to improve the terms of the special tender offer, and may further negotiate with third parties in order to obtain a competing offer.

If a special tender offer was accepted by a majority of the shareholders who announced their stand on such offer, then shareholders who did not respond to the special offer or had objected to the special tender offer may accept the offer within four days of the last day set for the acceptance of the offer.

In the event that a special tender offer is accepted, then the purchaser or any person or entity controlling it and any corporation controlled by them shall refrain from making a subsequent tender offer for the purchase of shares of the target company and may not execute a merger with the target company for a period of one year from the date of the offer, unless the purchaser or such person or entity undertook to effect such an offer or merger in the initial special tender offer.

## **Merger**

The Companies Law permits merger transactions if approved by each party's board of directors and, unless certain requirements described under the Companies Law are met, a majority of each party's shareholders, by a majority of each party's shares that are voted on the proposed merger at a shareholders' meeting.

The board of directors of a merging company is required pursuant to the Companies Law to discuss and determine whether in its opinion there exists a reasonable concern that as a result of a proposed merger, the surviving company will not be able to satisfy its obligations towards its creditors, taking into account the financial condition of the merging companies. If the board of directors has determined that such a concern exists, it may not approve a proposed merger. Following the approval of the board of directors of each of the merging companies, the boards of directors must jointly prepare a merger proposal for submission to the Israeli Registrar of Companies.

For purposes of the shareholder vote, unless a court rules otherwise, the merger will not be deemed approved if a majority of the shares voting at the shareholders meeting (excluding abstentions) that are held by parties other than the other party to the merger, any person who holds 25% or more of the means of control of the other party to the merger or any one on their behalf including their relatives or corporations controlled by any of them, vote against the merger.

If the transaction would have been approved but for the separate approval of each class of shares or the exclusion of the votes of certain shareholders as provided above, a court may still rule that the company has approved the merger upon the request of holders of at least 25% of the voting rights of a company, if the court holds that the merger is fair and reasonable, taking into account the appraisal of the merging companies' value and the consideration offered to the shareholders.

Under the Companies Law, each merging company must send a copy of the proposed merger plan to its secured creditors. Unsecured creditors are entitled to receive notice of the merger, as provided by the regulations promulgated under the Companies Law. Upon the request of a creditor of either party to the proposed merger, the court may delay or prevent the merger if it concludes that there exists a reasonable concern that, as a result of the merger, the surviving company will be unable to satisfy the obligations of the target company. The court may also give instructions in order to secure the rights of creditors.

In addition, a merger may not be completed unless at least 50 days have passed from the date that a proposal for approval of the merger was filed with the Israeli Registrar of Companies and 30 days from the date that shareholder approval of both merging companies was obtained.

#### ***Potential Issues that Could Delay a Merger***

Our articles of association provides for a staggered board of directors, which could delay, defer or prevent a change of control. In addition, certain provisions of Israeli corporate and tax law may have the effect of delaying, preventing or making more difficult any merger or acquisition of us. For example, any merger or acquisition of us will require the prior consent of the Chief Scientist, as well as the Investment Center. See Item 3.D – Risk factors "We are subject to anti-takeover provisions that could delay or prevent our acquisition by another entity."

#### ***Requirement of Disclosure of Shareholder Ownership***

There are no provisions of our memorandum of association or articles of association governing the ownership threshold above which shareholder ownership must be disclosed. We are subject, however, to U.S. securities rules that require beneficial owners of more than 5% of our Ordinary Shares to make certain filings with the SEC.

#### ***Changes in Capital***

Our memorandum of association and articles of association do not impose any conditions governing changes in capital that are more stringent than required by the Companies Law.

#### **10.C. Material contracts**

On February 17, 2014, we entered into an Agreement and Plan of Merger, or the Merger Agreement, with Ajax Acquisition Corporation, a Delaware corporation and a wholly-owned subsidiary of the Company, or Sub, Xora, a Delaware corporation, Ned Carlson as Stockholder Representative, and other stockholders listed in the Merger Agreement.

On March 4, 2014, in accordance with the Merger Agreement, Sub was merged with and into Xora, the separate corporate existence of Sub ceased, and Xora continued as the surviving corporation and a wholly-owned subsidiary of the Company. Under the terms of the Merger Agreement, the consideration for the transaction was approximately \$15 million in cash, including working capital and cash adjustments.

The Merger Agreement includes customary representations, warranties and covenants by the parties, which survived the closing and, in general, expire on March 4, 2016. Under the Merger Agreement, certain stockholders of Xora agreed to indemnify the Company for damages arising out of breaches or inaccuracies of Xora's or Xora stockholders' representations, warranties and covenants subject to certain limitations, including, in general, that Xora stockholders shall not be liable for any losses until the aggregate amount of losses exceeds \$100,000, or the Threshold, and once such Threshold has been reached, the Xora stockholders shall be liable for their pro rata portion of such losses, including the Threshold. Notwithstanding the foregoing, the Threshold will not apply to any losses arising from fraud or willful breach of the Merger Agreement, Xora's breach of the representations and warranties regarding organization, company capital structure, authority or tax matters, and certain other losses as specified in the Merger Agreement. The indemnification obligation of the Xora stockholders is capped at 15% of the purchase price, excluding working capital and cash adjustments, or the Cap. The amount of the Cap is subject to an escrow. The Cap is subject to certain exceptions similar to those applicable to the Threshold, but in no event shall a stockholder be liable for more than its pro rata portion of any particular loss or an amount in excess of the consideration it is eligible to receive under the Merger Agreement.

#### **10.D. Exchange controls**

There are currently no Israeli currency control restrictions on payments of dividends or other distributions with respect to our Ordinary Shares or the proceeds from the sale of shares, except for the obligation of Israeli residents to file reports with the Bank of Israel regarding certain transactions. However, legislation remains in effect pursuant to which currency controls can be imposed by administrative action at any time.

Non-residents of Israel who purchase our securities with non-Israeli currency will be able to repatriate dividends (if any), liquidation distributions and the proceeds of any sale of such securities, into non-Israeli currencies at the rate of exchange prevailing at the time of repatriation, provided that any applicable Israeli taxes have been paid (or withheld) on such amounts.

Neither our articles of association nor the laws of the State of Israel restrict in any way the ownership or voting of Ordinary Shares by non-residents of Israel, except with respect to citizens of countries that are in a state of war with Israel.

#### **10.E. Taxation**

The following is a summary of the current tax structure, which is applicable to companies in Israel, with special reference to its effect on us. The following also contains a discussion of material Israeli and U.S. tax consequences to persons purchasing our Ordinary Shares and government programs from which we and some of our group companies benefit. To the extent that the discussion is based on new tax legislation, which has yet to be subject to judicial or administrative interpretation, there can be no assurance that the views expressed in the discussion will accord with any such interpretation in the future. The discussion is not intended and should not be construed as legal or professional tax advice and is not exhaustive of all possible tax considerations. An Israeli company that is subject to Israeli taxes on the income of its non-Israeli subsidiaries will receive a credit for income taxes paid/withheld or that will be paid/withheld by the subsidiary in its country of residence, according to the terms and conditions determined in the Israeli Tax Ordinance.

The following summary is included herein as general information only and is not intended as a substitute for careful tax planning. Accordingly, each investor should consult his or her own tax advisor as to the particular tax consequences to such investor of the purchase, ownership or sale of an ordinary share, including the effect of applicable state, local, foreign or other tax laws and possible changes in tax laws.

#### **Israeli Taxation Considerations**

##### **General Corporate Tax Structure**

Income not eligible for "Approved enterprise" benefits was taxed in 2013 at a regular corporate tax rate of 25% (25% in 2012 and 24% in 2011). The tax rate was scheduled to be gradually reduced to 18% in 2016 and beyond. This scheduled gradual reduction in corporate tax rates was repealed. Instead, the corporate tax rate was increased to 25% in 2012 and 2013, and to 26.5% in 2014 and thereafter. However, the effective rate of tax payable by a company which derives income from an "Approved Enterprise" may be considerably lower – see discussion below. Due to budgetary constraints, from time to time the Israeli Government has considered delaying the Israeli company tax rate decreases but no decisions have yet been taken in this regard.

##### **Law for the Encouragement of Capital Investments, 1959**

**General.** Certain of our production and development facilities have been granted approved enterprise status pursuant to the Law for the Encouragement of Capital Investments, 1959 (the "Investment Law"). Pursuant to the Investment Law, an Industrial Company is a company resident in Israel, if at least 90% of the income of which, in a given tax year, determined in Israeli currency (exclusive of income from some government loans, capital gains, interest and dividends), is derived from an Industrial Enterprise owned by it. An "Industrial Enterprise" is defined as an enterprise whose major activity in a given tax year is industrial production activity. The Investment Law provides that a capital investment in eligible facilities may, upon application to the Investment Center of the Ministry of Industry and Trade of the State of Israel, or the Investment Center, be designated as an Approved Enterprise. Each certificate of approval for an Approved Enterprise relates to a specific investment program delineated both by its financial scope, including its capital sources, and by its physical characteristics, e.g., the equipment to be purchased and utilized pursuant to the program. The tax benefits derived from any such certificate of approval relate only to taxable income attributable to the specific Approved Enterprise. Subject to certain provisions concerning income and subject to the Alternative Benefits

(see below), any distributed dividends are deemed attributable to the entire enterprise, and the effective tax rate and the effective withholding tax rates represent the weighted combination of the various applicable tax rates.

**Tax Benefits.** Taxable income of a company derived from an Approved Enterprise is subject to company tax at the rate of up to 25%, instead of the tax rates under the "General Corporate Tax Structure" above, for a certain period of time. The benefit period is a period of seven years commencing in the year in which the Approved Enterprise first generates taxable income. The benefits may be shorter as it is limited to 12 years from the commencement of production of the Approved Enterprise or 14 years from the date of approval, whichever is earlier. Under certain circumstances (as further detailed below), the benefit period may extend to a maximum of ten years or fifteen years (see the 2005 Amendment below) from the commencement of the benefit period. A company which operates under more than one approval or that has capital investments which are only partly approved (such a company being designated as a Mixed Enterprise), may have an effective company tax rate that is the result of a weighted combination of the various applicable rates.

A company owning an approved enterprise which was approved after April 1, 1986 may elect to forego the entitlement to grants or state guarantees and apply for an alternative package of tax benefits. These benefits provide that undistributed income from the approved enterprise is fully tax exempt from corporate tax for a defined period, which ranges between two and ten years from the first year of taxable income, subject to the limitations described above, depending principally upon the geographic location within Israel and the type of the approved enterprise. Upon expiration of such period, the approved enterprise is eligible for a beneficial tax rate (25% or lower in the case of an FIC, as described below), for the remainder of the otherwise applicable period of benefits, as described above.

Should the percentage of share capital of the companies having Approved Enterprises held by foreign shareholders exceed 25%, future Approved Enterprises of such companies would qualify for reduced tax rates for an additional three years, after the seven years mentioned above. The company tax rate applicable to income earned from Approved Enterprise programs (currently, for programs on which an application for an approved enterprise status was submitted before December 31, 2004) in the benefit period by a company meeting these qualifications is as follows:

<b><u>% of Foreign Ownership</u></b>	<b><u>Tax Rate</u></b>
Over 25% but less than 49%	25%
49% or more but less than 74%	20%
74% or more but less than 90%	15%
90% or more	10%

Entitlement to these tax benefits for enterprises to which Investment Center granted an Approved Enterprise status prior to December 31, 2004 (see the 2005 Amendment below) is subject to the final ratification of the Investment Center, and is conditioned upon fulfillment of all terms of the approved program. However, there can be no assurance that we will obtain approval for additional Approved Enterprises, or that the provisions of the Investment Law will not change with respect to future approvals, or that the above-mentioned shareholding portion will be reached for each subsequent year. In the event of our failure to comply with these conditions, the tax and other benefits could be canceled, in whole or in part, and we might be required to refund the amount of the canceled benefits, together with the addition of CPI linkage difference and interest. We believe that our Approved Enterprise substantially complies with all such conditions at present, but there can be no assurance that it will continue to do so. The undistributed income derived from each of our approved enterprise programs is tax-exempt for a two year period beginning with the first year in which it generates otherwise taxable income and is subject to a reduced tax rate for the remainder of the benefit period.

A company that pays a dividend out of income derived from the Approved Enterprise(s) during the tax exemption period will be subject to deferred company tax in respect of the amount distributed (including the recipient's tax thereon) at the rate which would have been applicable had such company not elected the Alternative Package. This rate is generally 10% to 25%, depending on the extent to which non-Israeli shareholders hold such company's shares.

The dividend recipient is taxed at the reduced rate applicable to dividends from Approved Enterprises (generally 15% as compared to 25% for individuals or an exemption for companies), if the dividend is distributed during the tax benefit period or within 12 years after this period. However, the limitation does not apply if the company

qualifies as a foreign investors' company. This tax must be withheld by such company at source, regardless of whether the dividend is converted into foreign currency.

Subject to certain provisions concerning income subject to Mixed Enterprises, all dividends are considered to be attributable to the entire enterprise and the effective tax rate on the dividend is the result of a weighted combination of the various applicable tax rates. However, such company is not obliged to distribute exempt retained profits under the Alternative Package, and such company may generally decide from which year's profits to declare dividends.

Each application to the Investment Center is reviewed separately, and a decision as to whether or not to approve such application is based, among other things, on the then prevailing criteria set forth in the Investment Law, on the specific objectives of the applicant company set forth in such application and on certain financial criteria of the applicant company. Accordingly, there can be no assurance that any such application by any of our group companies will be approved. In addition, the benefits available to an Approved Enterprise are conditional upon the fulfillment of certain conditions stipulated in the Investment Law and its regulations and the criteria set forth in the certificate of approval, as described above. In the event that these conditions are violated, in whole or in part, a company with an Approved Enterprise would be required to refund the amount of tax benefits, with the addition of the Israeli consumer price index linkage differences and interest.

A company which qualifies as a foreign investment company, or FIC, is a company, like us, in which more than 25% of the share capital (in terms of shares, rights to profit, voting rights and appointment of directors) and of the combined share and loan capital is owned, directly or indirectly, by non-residents of Israel and is therefore entitled to further tax benefits relating to its approved enterprises. Such a company will be eligible for an extension of the period of tax benefits for its approved enterprises (up to ten years) and further tax benefits, should the level of foreign ownership in it increase above 49%.

Notwithstanding the foregoing, proceeds received from the sale of our products may be deemed to be royalties under the domestic law of the country of residence of the purchaser/licensee or under an applicable tax treaty and as such subject to withholding tax in such country.

Where withholding tax is paid by our company to the country of residence of the purchaser/licensee, such tax would generally be creditable by our company for Israeli income tax purposes, pursuant to any relevant income tax treaty and under Israeli law against income derived from the same source. However, where we do not have taxable income for Israeli tax purposes because of the application of a tax exemption available to an Approved Enterprise or because of losses for tax purposes, we would have no Israeli tax liability against which to credit the foreign tax withheld and paid by us. Furthermore, under Israeli law, if certain conditions are not met we may not carry forward such unused credit to utilize in future tax years.

From time to time, the Government of Israel has discussed reducing the benefits available to companies under the Investment Law and currently such proposal is pending. The termination or substantial reduction of any of the benefits available under the Investment Law could have a material adverse effect on future investments by our company in Israel.

The law also provides that an approved enterprise is entitled to accelerated depreciation on property and equipment included in an approved investment program, generally ranging from 200% for equipment, to 400% for buildings, of ordinary depreciation rates during the first five tax years of the operation of these assets with a ceiling of 20% per year for depreciation on buildings.

Notwithstanding the foregoing, on March 29, 2005, the Israeli Parliament passed an amendment to the Investment Law, or the 2005 Amendment, which revamps the Israeli tax incentives for future industrial and hotel investments. A tax "holiday" package can now be elected for up to 15 years for a "Privileged Enterprise" as defined in the 2005 Amendment, if certain conditions are met, without needing to obtain approval. The extent of the tax benefits available depends upon the level of foreign investment.

The 2005 Amendment became effective on April 1, 2005. Taxpayers may, under certain conditions, claim Privileged Enterprise status for new and expanded enterprises with respect to 2004 or subsequent years, unless the Investment Center granted such taxpayer Approved Enterprise status prior to December 31, 2004.

Subject to certain conditions, various alternative tax-only benefit packages can now be elected with respect to investments in a "Privileged Enterprise", without prior approval. Companies in industry or tourism in Israel may elect between:

- Tax "holiday" package – for a "Privileged Enterprise": a tax exemption applies to undistributed profits for 2 to 10 years depending on geographical location of the "Privileged Enterprise" and the level of foreign ownership. Company tax rates of between 10% and 25% apply to distributed exempt profits or profits derived subsequent to the exempt period. The total period of tax benefits is 7 to 15 years, or
- Grant / Reduced tax package – for an "Approved Enterprise": Fixed asset grants of between 20% and 32% for enterprises in a development area and reduced company tax rates between 0% and 25% for a period of 7 to 15 years.

Dividend withholding tax also applies at a rate of 4% or 15% depending on the package selected and the residency of the shareholder.

Recently, new legislation amending the Investment Law was adopted. Under this new legislation, a uniform corporate tax rate will apply to all qualifying income of certain Industrial Companies (requirement of a minimum export of 25% of the company's total turnover), as opposed to the current law's incentives, which are limited to income from Approved Enterprises during their benefits period. Under the new law, the uniform tax rate will be 10% in areas in Israel designated as Development Zone A and 15% elsewhere in Israel during 2011-2012, 7% and 12.5%, respectively in 2013. From 2014 9% and 16%, respectively thereafter. The profits of these Industrial Companies will be freely distributable as dividends, subject to a 15% (20% from 2014) withholding tax (or lower, under an applicable tax treaty).

Under the transition provisions of the new legislation, we may decide to irrevocably implement the new law while waiving benefits provided under the current law or to remain subject to the current law. We chose not to adopt the new law. Changing from the current law to the new law is permitted at any time. We do not expect the new law to have material ramifications on the tax payable in respect of our Israeli operations.

The Company decided to implement the new law from 2013.

#### **Grants under the Law for the Encouragement of Industrial Research and Development, 1984**

Israeli tax laws have allowed, under certain conditions, a tax deduction for expenditures (including capital expenditures) in scientific research and development projects, if the expenditures are approved or funded by the Government of Israel and the research and development is for the promotion of the enterprise and is carried out by or on behalf of the company seeking such deduction. Expenditures not approved as above or funded are deductible in equal portions over a three-year period.

Under the Research Law, research and development programs that meet specified criteria and are approved by a committee of the Chief Scientist, are eligible for grants of up to 50% of the program's expenses. Under the provisions of Israeli law in effect until 1996, royalties of 2%-3% of the revenues derived in connection with products developed according to, or as a result of, a research and development program funded by the Chief Scientist had to be paid to the State of Israel. Pursuant to an amendment effected in 1996 effective with respect to Chief Scientist programs funded in or after 1994, royalties at the rate of 3% during the first three years, 4% over the following three years and 5% in or after the seventh year of the revenues derived in connection with products developed according to such programs are payable to the State of Israel. The maximum aggregate royalties will not exceed 100% (or, for funding prior to 1994, 100%-150%) of the dollar-linked value of the total grants received. Pursuant to an amendment effected in 2000, effective with respect to Chief Scientist programs funded in or after 2000, the royalty rates described above were updated to 3% during the first three years and 3.5% in or after the fourth year, of the revenues derived in connection with products developed under such programs. Pursuant to an amendment effected on January 1, 1999, effective with respect to Chief Scientist programs approved in or after 1999, funds received from the Chief Scientist shall bear annual interest at a rate equal to LIBOR for twelve months.

Generally, the Research Law requires that the manufacturing of any product developed through research and development funded by the Government of Israel shall be in Israel. It also provides that know-how from the research and development that is used to produce the product may not be transferred to third parties without the approval of a research committee of the Chief Scientist. Such approval is not required for the export of any products resulting from such research and development.

However, under the Regulations, in the event that any portion of the manufacturing is not performed in Israel, if approved by the Chief Scientist, we would be required to pay an increased royalty at the rates of 120%, 150% or 300% of the grant if the manufacturing portion that is performed outside of Israel is less than 50%, between 50% and 90% and more than 90%, respectively.

In 2002, the Research Law was amended to, among other things, enable companies applying for grants from the Chief Scientist to seek prior approval for conducting manufacturing activities outside of Israel without being subject to increased royalties. However, this amendment will not apply to any of our existing grants. In addition, the amendment provides that one of the factors to be taken into consideration by the Chief Scientist in deciding whether to approve a grant application is the percentage of the manufacturing of the relevant product that will be conducted outside of Israel. Accordingly, should we seek additional grants from the Chief Scientist in connection with which we also seek prior approval for manufacturing products outside of Israel, we may not receive such grant or may receive a grant in an amount that is less than the amount we sought.

### **Law for the Encouragement of Industry (Taxes), 1969**

Pursuant to the Law for the Encouragement of Industry (Taxes), 1969, a company qualifies as an "Industrial Company" if it is a resident of Israel and at least 90% of its gross income in any tax year (exclusive of income from certain defense loans, capital gains, interest and dividends) is derived from an "industrial enterprise" it owns. An "industrial enterprise" is defined as an enterprise whose major activity, in a given tax year, is industrial manufacturing.

We believe that we currently qualify as an Industrial Company. Accordingly, we are entitled to certain tax benefits, including a deduction of 12.5% per annum on the purchase of patents or certain other intangible property rights (other than goodwill) used for the development or promotion of the industrial enterprise over a period of eight years beginning with the year in which such rights were first used.

The tax laws and regulations dealing with the adjustment of taxable income for local inflation provide that an industrial enterprise is eligible for special rates of depreciation deductions. These rates vary in the case of plant and machinery according to the number of shifts in which the equipment is being operated and range from 20% to 40% on a straight-line basis, or 30% to 50% on a declining balance basis (instead of the regular rates which are applied on a straight-line basis).

Moreover, industrial enterprises which are Approved Enterprises can choose between (a) the special rates referred to above and (b) accelerated regular rates of depreciation applied on a straight-line basis with respect to property and equipment, generally ranging from 200% (with respect to equipment) to 400% (with respect to buildings) of the ordinary depreciation rates during the first five years of service of these assets, provided that the depreciation on a building may not exceed 20% per annum. In no event may the total depreciation exceed 100% of the cost of the asset.

In addition, Industrial Companies may (i) elect to file consolidated tax returns with additional related Israeli Industrial Companies and (ii) deduct expenses related to public offerings in equal amounts over a period of three years.

Eligibility for benefits under the Encouragement of Industry Law is not contingent upon the approval of any governmental authority. No assurance can be given that we will continue to qualify as an Industrial Company, or will avail ourselves of any benefits under this law in the future or that Industrial Companies will continue to enjoy such tax benefits in the future.

### **Taxation under Inflationary Conditions**

The Income Tax Law (Inflationary Adjustments), 5745-1985, generally referred to as the "Inflationary Adjustments Law," was designed to deal with taxation issues caused by rapid inflation. Under the Inflationary Adjustments Law, taxable results of Israeli companies up to and including the year 2007 were measured on a real basis, taking into account the rate of change in the Israeli Consumer Price Index. The Inflationary Adjustments Law was repealed commencing from tax year 2008.

Pursuant to an amendment to the Investments Law which became effective on November 12, 2012, a company that elects by November 11, 2013 to pay a corporate tax rate as set forth in that amendment (rather than the regular corporate tax rate applicable to Approved Enterprise income) with respect to undistributed exempt income accumulated by the company up until December 31, 2011, will be entitled to distribute a dividend from

such income without being required to pay additional corporate tax with respect to such dividend. A company that has so elected must make certain qualified investments in Israel over the five-year period commencing in 2013. A company that has elected to apply the amendment cannot change its election. We elected to take advantage of the amendment in 2013 and were required to pay about \$0.7 million as a one-time payment.

## **Taxation of our Shareholders**

### **Capital Gain**

Capital gain tax is imposed on the disposal of capital assets by an Israeli resident, and on the disposal of such assets by a non- Israel resident if those assets are either (i) located in Israel; (ii) are shares or a right to a share in an Israeli resident corporation (iii) represent, directly or indirectly, rights to assets located in Israel. The Israeli Tax Ordinance distinguishes between "Real Gain" and the "Inflationary Surplus". Real Gain is the excess of the total capital gain over Inflationary Surplus computed generally on the basis of the increase in the Israeli CPI between the date of purchase and the date of disposal.

The capital gain accrued by individuals on the sale of an asset purchased on or after January 1, 2003 will be taxed at the rate of 25%. However, if the individual shareholder is a "Controlling Shareholder" (*i.e.*, a person who holds, directly or indirectly, alone or together with other, 10% or more of one of the Israeli resident company's means of control at the time of distribution or at any time during the preceding 12 months period) such gain will be taxed at the rate of 30%. In addition, capital gain derived by an individual claiming deduction of financing expenses in respect of such gain will be taxed at the rate of 25%. The real capital gain derived by a corporation will be generally subject to tax at the rate of 25%. However, the real capital gain derived from sale of securities, as defined in Section 6 of the Inflationary Adjustment Law, by a corporation, which was subject upon December 31, 2005 to the provisions of Section 6 of the Inflationary Adjustment Law, will be taxed at the corporate tax rate (24% in 2011 and 25% in 2012 and thereafter). The capital gain accrued at the sale of an asset purchased prior to January 1, 2003 will be subject to tax at a blended rate. The marginal tax rate for individuals (up to 45% in 2011, up to 48% in 2012 and up to 50% in 2013 and thereafter) and the regular corporate tax rate for corporations (24% in 2011 and 25% in 2012 and thereafter) will be applied to the gain amount which bears the same ratio to the total gain realized as the ratio which the holding period commencing at the acquisition date and terminating on January 1, 2003 bears to the total holding period. The remainder of the gain realized will be subject to capital gains tax at the rates applicable to an asset purchased after January 1, 2003 (see aforementioned).

Individual and corporate shareholder dealing in securities in Israel are taxed at the tax rates applicable to business income (at a tax rate in 2011 of 24% and 25% in 2012 and thereafter for a corporation and a marginal tax rate of up to 45% in 2011, up to 48% in 2012 and up to 50% in 2013 and thereafter for individuals). Notwithstanding the foregoing, if the shareholder is a non-Israeli resident, then such taxation is subject to the provision of any applicable double tax treaty. Moreover, capital gain derived from the sale of the shares by a non-Israeli shareholder may be exempt under the Israeli income tax ordinance from Israeli taxation provided the following cumulative conditions are met: (i) the shares were purchased upon or after the registration of the shares at the stock exchange, (ii) the seller doesn't have a permanent establishment in Israel to which the derived capital gain is attributed, and (iii) if the seller is a corporation, less than 25% of its means of control are held by Israeli resident shareholders. In addition, the sale of the shares may be exempt from Israeli capital gain tax under an applicable tax treaty. Thus, the U.S.-Israel Double Tax Treaty exempts U.S. resident from Israeli capital gain tax in connection with such sale, provided (i) the U.S. resident owned, directly or indirectly, less than 10% of an Israeli resident company's voting power at any time within the 12 – month period preceding such sale; (ii) the seller, being an individual, is present in Israel for a period or periods of less than 183 days at the taxable year; and (iii) the capital gain from the sale was not derived through a permanent establishment of the U.S. resident in Israel.

Either the seller, the Israeli stockbroker or financial institution through which the sold securities are held, are obliged, subject to the above mentioned exemptions, to withhold tax upon the sale of securities from the real capital gain at the rate of 25% in respect of a corporation and 20% in respect of an individual in 2011.

Generally, within 30 days of a transaction, a detailed return, including a computation of the tax due, should be submitted to the Israeli Tax Authority, and an advanced payment amounting to the tax liability arising from the capital gain is payable. At the sale of traded securities, the aforementioned detailed return may not be submitted and the advanced payment should not be paid if all tax due was withheld at source according to applicable

provisions of the Israeli income tax ordinance and regulations promulgated thereunder. Capital gain is also reportable on the annual income tax return.

## **Dividends**

A distribution of dividend from income attributed to an "Approved Enterprise" will be subject to tax in Israel at the rate of 15%, subject to a reduced rate under any applicable double tax treaty. A distribution of dividend from income, which is not attributed to an "Approved Enterprise" to an Israeli resident individual, will generally be subject to income tax at a rate of 25%. However, a 30% tax rate will apply if the dividend recipient is a "Controlling Shareholder" (i.e., a person who holds, directly or indirectly, alone or together with other, 10% or more of one of the Israeli resident company's means of control at the time of distribution or at any time during the preceding 12 months period). If the recipient of the dividend is an Israeli resident corporation, such dividend will be exempt from income tax provided the income from which such dividend is distributed was derived or accrued within Israel.

Under the Israeli income tax ordinance, a non-Israeli resident (either individual or corporation) is generally subject to an Israeli income tax on the receipt of dividends at the rate of 25% (30% if the dividends recipient is a Controlling Shareholder at the time of distribution or at any time during the preceding 12-month period); those rates are subject to a reduced tax rate under an applicable double tax treaty. Thus, under the Double Tax Treaty concluded between the State of Israel and the U.S. the following rates will apply in respect of dividends distributed by an Israeli resident company to a U.S. resident: (i) if the U.S. resident is a corporation which holds during that portion of the taxable year which precedes the date of payment of the dividend and during the whole of its prior taxable year (if any), at least 10% of the outstanding shares of the voting stock of the Israeli resident paying corporation and not more than 25% of the gross income of the Israeli resident paying corporation for such prior taxable year (if any) consists of certain type of interest or dividends – the tax rate is 12.5%, (ii) if both the conditions mentioned in section (i) above are met and the dividend is paid from an Israeli resident company's income which was entitled to a reduced tax rate applicable to an "approved enterprise" under the Israeli Law for the Encouragement of Capital Investments of 1959– the tax rate is 15%, and (iii) in all other cases, the tax rate is 25%. The aforementioned rates under the Israel U.S. Double Tax Treaty will not apply if the dividend income was derived through a permanent establishment of the U.S. resident in Israel.

An Israeli resident company whose shares are listed on a stock exchange is obligated to withhold tax, upon the distribution of a dividend attributed to an Approved Enterprise's income, from the amount distributed, at the following rates: (i) Israeli resident corporation – 15%, (ii) Israeli resident individual – 15%, and (iii) non-Israeli resident – 15%, subject to a reduced tax rate under an applicable double tax treaty.

## **Estate and Gift Tax**

Israel law presently does not impose estate or gift tax.

## **United States Federal Income Tax Consequences**

THE FOLLOWING SUMMARY IS INCLUDED HEREIN FOR GENERAL INFORMATION AND IS NOT INTENDED TO BE, AND SHOULD NOT BE CONSIDERED TO BE, LEGAL OR TAX ADVICE. EACH U.S. HOLDER SHOULD CONSULT WITH HIS OR HER OWN TAX ADVISOR AS TO THE PARTICULAR U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE PURCHASE, OWNERSHIP AND SALE OF ORDINARY SHARES, INCLUDING THE EFFECTS OF APPLICABLE STATE, LOCAL, FOREIGN OR OTHER TAX LAWS AND POSSIBLE CHANGES IN THE TAX LAWS.

## **U.S. Federal Income Taxation**

Subject to the limitations described in the next paragraph, the following discussion summarizes the material U.S. federal income tax consequences to a "U.S. Holder" arising from the purchase, ownership and sale of the Ordinary Shares. For this purpose, a "U.S. Holder" is a holder of Ordinary Shares that is: (1) an individual citizen or resident of the United States, including an alien individual who is a lawful permanent resident of the United States or meets the substantial presence residency test under U.S. federal income tax laws; (2) a corporation (or other entity treated as a corporation for U.S. federal income tax purposes) or a partnership (other than a partnership that is not treated as a U.S. person under any applicable U.S. Treasury Regulations) created or organized in or under the laws of the United States or the District of Columbia or any political subdivision thereof; (3) an estate, the income of which is subject to U.S. federal income tax regardless of source; (4) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and

one or more U.S. persons have authority to control all substantial decisions of the trust; (5) a trust that has a valid election in effect to be treated as a U.S. person to the extent provided in U.S. Treasury regulations; or (6) any person otherwise subject to U.S. federal income tax on a net income basis in respect of the Ordinary Shares, if such status as a U.S. Holder is not overridden pursuant to the provisions of an applicable tax treaty.

This summary is for general information purposes only and does not purport to be a comprehensive description of all of the U.S. federal income tax considerations that may be relevant to a decision to purchase or hold our Ordinary Shares. This summary generally considers only U.S. Holders that will own our Ordinary Shares as capital assets. Except to the limited extent discussed below, this summary does not consider the U.S. federal tax consequences to a person that is not a U.S. Holder, nor does it describe the rules applicable to determine a taxpayer's status as a U.S. Holder. This summary is based on the provisions of the Internal Revenue Code of 1986, as amended, or the Code, final, temporary and proposed U.S. Treasury Regulations promulgated thereunder, administrative and judicial interpretations thereof, and the U.S./Israel Income Tax Treaty, all as in effect as of the date hereof and all of which are subject to change, possibly on a retroactive basis, and all of which are open to differing interpretations. The Company will not seek a ruling from the U.S. Internal Revenue Service, or the IRS, with regard to the U.S. federal income tax treatment of an investment in our Ordinary Shares by U.S. Holders and, therefore, can provide no assurances that the IRS will agree with the conclusions set forth below.

This discussion does not address all of the aspects of U.S. federal income taxation that may be relevant to a particular shareholder based on such shareholder's particular circumstances and in particular does not discuss any estate, gift, generation-skipping, transfer, state, local or foreign tax considerations. In addition, this discussion does not address the U.S. federal income tax treatment of a U.S. Holder who is: (1) a bank, life insurance company, regulated investment company, or other financial institution or "financial services entity"; (2) a broker or dealer in securities or foreign currency; (3) a person who acquired our Ordinary Shares in connection with employment or other performance of services; (4) a U.S. Holder that is subject to the U.S. alternative minimum tax; (5) a U.S. Holder that holds our Ordinary Shares as a hedge or as part of a hedging, straddle, conversion or constructive sale transaction or other risk-reduction transaction for U.S. federal income tax purposes; (6) a tax-exempt entity; (7) real estate investment trusts; (8) a U.S. Holder that expatriates out of the United States or a former long-term resident of the United States; or (9) a person having a functional currency other than the U.S. dollar. This discussion does not address the U.S. federal income tax treatment of a U.S. Holder that owns, directly or constructively, at any time, Ordinary Shares representing 10% or more of our voting power. Additionally, the U.S. federal income tax treatment of persons who hold Ordinary Shares through a partnership or other pass-through entity are not considered.

You are encouraged to consult your own tax advisor with respect to the specific U.S. federal and state income tax consequences to you of purchasing, holding or disposing of our Ordinary Shares, including the effects of applicable state, local, foreign or other tax laws and possible changes in the tax laws.

### **Distributions on Ordinary Shares**

Subject to the discussion under the heading "Passive Foreign Investment Companies" below, a U.S. Holder will be required to include in gross income as ordinary income the amount of any distribution paid on Ordinary Shares (including the amount of any Israeli tax withheld on the date of the distribution), to the extent that such distribution does not exceed our current and accumulated earnings and profits, as determined for U.S. federal income tax purposes. The amount of a distribution which exceeds our earnings and profits will be treated first as a non-taxable return of capital, reducing the U.S. Holder's tax basis for the Ordinary Shares to the extent thereof, and then capital gain. Corporate holders generally will not be allowed a deduction for dividends received. For noncorporate U.S. Holders, to the extent that their total adjusted income does not exceed applicable thresholds, the maximum federal income tax rate for "qualified dividend income" and long-term capital gains is generally 15%. For those noncorporate U.S. Holders whose total adjusted income exceeds such income thresholds, the maximum federal income tax rate for "qualified dividend income" and long-term capital gains is generally 20%. For this purpose, "qualified dividend income" means, *inter alia*, dividends received from a "qualified foreign corporation." A "qualified foreign corporation" is a corporation that is entitled to the benefits of a comprehensive tax treaty with the United States which includes an exchange of information program. The IRS has stated that the Israel/U.S. Tax Treaty satisfies this requirement and we believe we are eligible for the benefits of that treaty.

In addition, our dividends will be qualified dividend income if our Ordinary Shares are readily tradable on Nasdaq or another established securities market in the United States. Dividends will not qualify for the

preferential rate if we are treated, in the year the dividend is paid or in the prior year, as a passive foreign investment company, or PFIC. A U.S. Holder will not be entitled to the preferential rate: (1) if the U.S. Holder has not held our Ordinary Shares or ADRs for at least 61 days of the 121 day period beginning on the date which is 60 days before the ex-dividend date, or (2) to the extent the U.S. Holder is under an obligation to make related payments on substantially similar property. Any days during which the U.S. Holder has diminished its risk of loss on our Ordinary Shares are not counted towards meeting the 61-day holding period. Finally, U.S. Holders who elect to treat the dividend income as "investment income" pursuant to Code section 163(d)(4) will not be eligible for the preferential rate of taxation.

The amount of a distribution with respect to our Ordinary Shares will be measured by the amount of the fair market value of any property distributed, and for U.S. federal income tax purposes, the amount of any Israeli taxes withheld therefrom. (See discussion above under "Israeli Taxation Considerations - Taxation of Our Shareholders – Dividends.") Cash distributions paid by us in NIS will be included in the income of U.S. Holders at a U.S. dollar amount based upon the spot rate of exchange in effect on the date the dividend is includible in the income of the U.S. Holder, and U.S. Holders will have a tax basis in such NIS for U.S. federal income tax purposes equal to such U.S. dollar value. If the U.S. Holder subsequently converts the NIS, any subsequent gain or loss in respect of such NIS arising from exchange rate fluctuations will be U.S. source ordinary exchange gain or loss.

Distributions paid by us will generally be foreign source income for U.S. foreign tax credit purposes. Subject to the limitations set forth in the Code, U.S. Holders may elect to claim a foreign tax credit against their U.S. income tax liability for Israeli income tax withheld from distributions received in respect of the Ordinary Shares. In general, these rules limit the amount allowable as a foreign tax credit in any year to the amount of regular U.S. tax for the year attributable to foreign source taxable income. This limitation on the use of foreign tax credits generally will not apply to an electing individual U.S. Holder whose creditable foreign taxes during the year do not exceed \$300, or \$600 for joint filers, if such individual's gross income for the taxable year from non-U.S. sources consists solely of certain passive income. A U.S. Holder will be denied a foreign tax credit with respect to Israeli income tax withheld from dividends received with respect to the Ordinary Shares if such U.S. Holder has not held the Ordinary Shares for at least 16 days out of the 31-day period beginning on the date that is 15 days before the ex-dividend date or to the extent that such U.S. Holder is under an obligation to make certain related payments with respect to substantially similar or related property. Any day during which a U.S. Holder has substantially diminished his or her risk of loss with respect to the Ordinary Shares will not count toward meeting the 16-day holding period. A U.S. Holder will also be denied a foreign tax credit if the U.S. Holder holds the Ordinary Shares in an arrangement in which the U.S. Holder's reasonably expected economic profit is insubstantial compared to the foreign taxes expected to be paid or accrued. The rules relating to the determination of the U.S. foreign tax credit are complex, and U.S. Holders should consult with their own tax advisors to determine whether, and to what extent, they are entitled to such credit. U.S. Holders that do not elect to claim a foreign tax credit may instead claim a deduction for Israeli income taxes withheld, provided such U.S. Holders itemize their deductions.

### **Disposition of Shares**

Except as provided under the PFIC rules described below, upon the sale, exchange or other disposition of our Ordinary Shares, a U.S. Holder will recognize capital gain or loss in an amount equal to the difference between such U.S. Holder's tax basis in the sold Ordinary Shares and the amount realized on the disposition of such Ordinary Shares (or its U.S. dollar equivalent determined by reference to the spot rate of exchange on the date of disposition, if the amount realized is denominated in a foreign currency). The gain or loss realized on the sale or exchange or other disposition of Ordinary Shares will be long-term capital gain or loss if the U.S. Holder has a holding period of more than one year at the time of the disposition.

In general, gain realized by a U.S. Holder on a sale, exchange or other disposition of Ordinary Shares will generally be treated as U.S. source income for U.S. foreign tax credit purposes. A loss realized by a U.S. Holder on the sale, exchange or other disposition of Ordinary Shares is generally allocated to U.S. source income. However, U.S. Treasury Regulations require such loss to be allocated to foreign source income to the extent specified dividends were received by the taxpayer within the 24-month period preceding the date on which the taxpayer recognized the loss. The deductibility of a loss realized on the sale, exchange or other disposition of Ordinary Shares is subject to limitations.

## Tax on Net Investment Income

Above certain income thresholds, U.S. Holders who are individuals, estates or trusts will generally be required to pay a new 3.8% tax on their net investment income (including dividends on and gains from the sale or other disposition of our Ordinary Shares), or in the case of estates and trusts on their net investment income that is not distributed. In each case, the 3.8% Medicare tax applies only to the extent the U.S. Holder's total adjusted income exceeds applicable thresholds.

## Passive Foreign Investment Companies

Special U.S. federal income tax laws apply to a U.S. Holder who owns shares of a corporation that was (at any time during the U.S. Holder's holding period) a PFIC. We would be treated as a PFIC for U.S. federal income tax purposes for any tax year if, in such tax year, either:

- 75% or more of our gross income (including our pro rata share of gross income for any company, U.S. or foreign, in which we are considered to own 25% or more of the shares by value), in a taxable year is passive (the "Income Test"); or
- At least 50% of our assets, averaged over the year and generally determined based upon value (including our pro rata share of the assets of any company in which we are considered to own 25% or more of the shares by value), in a taxable year are held for the production of, or produce, passive income (the "Asset Test").

For this purpose, passive income generally consists of dividends, interest, rents, royalties, annuities and income from certain commodities transactions and from notional principal contracts. Cash is treated as generating passive income.

If we are or become a PFIC, each U.S. Holder who has not elected to treat us as a qualified electing fund by making a "QEF election", or who has not elected to mark the shares to market (as discussed below), would, upon receipt of certain distributions by us and upon disposition of our Ordinary Shares at a gain, be liable to pay U.S. federal income tax at the then prevailing highest tax rates on ordinary income plus interest on such tax, as if the distribution or gain had been recognized ratably over the taxpayer's holding period for the Ordinary Shares. In addition, when shares of a PFIC are acquired by reason of death from a decedent that was a U.S. Holder, the tax basis of such shares would not receive a step-up to fair market value as of the date of the decedent's death, but instead would be equal to the decedent's basis if lower, unless all gain were recognized by the decedent. Indirect investments in a PFIC may also be subject to special U.S. federal income tax rules.

The PFIC rules would not apply to a U.S. Holder who makes a QEF election for all taxable years that such U.S. Holder has held the Ordinary Shares while we are a PFIC, provided that we comply with specified reporting requirements. Instead, each U.S. Holder who has made such a QEF election is required for each taxable year that we are a PFIC to include in income such U.S. Holder's *pro rata* share of our ordinary earnings as ordinary income and such U.S. Holder's *pro rata* share of our net capital gains as long-term capital gain, regardless of whether we make any distributions of such earnings or gain. In general, a QEF election is effective only if we make available certain required information. The QEF election is made on a shareholder-by-shareholder basis and generally may be revoked only with the consent of the IRS. U.S. Holders should consult with their own tax advisors regarding eligibility, manner and advisability of making a QEF election if we are treated as a PFIC.

A U.S. Holder of PFIC shares which are traded on qualifying public markets, including the Nasdaq, can elect to mark the shares to market annually, recognizing as ordinary income or loss each year an amount equal to the difference as of the close of the taxable year between the fair market value of the PFIC shares and the U.S. Holder's adjusted tax basis in the PFIC shares. Losses are allowed only to the extent of net mark-to-market gain previously included income by the U.S. Holder under the election for prior taxable years.

In light of the complexity of PFIC rules, we cannot assure you that we have not been or are not a PFIC or will avoid becoming a PFIC in the future. U.S. Holders who hold Ordinary Shares during a period when we are a PFIC will be subject to the foregoing rules, even if we cease to be a PFIC, subject to specified exceptions for U.S. Holders who made a QEF or mark-to-market election. U.S. Holders are strongly urged to consult their tax advisors about the PFIC rules, including tax return filing requirements and the eligibility, manner, and consequences to them of making a QEF or mark-to-market election with respect to our Ordinary Shares in the event we that qualify as a PFIC.

## **Information Reporting and Withholding**

A U.S. Holder may be subject to backup withholding (at a rate of 28%) with respect to cash dividends and proceeds from a disposition of Ordinary Shares. In general, back-up withholding will apply only if a U.S. Holder fails to comply with specified identification procedures. Backup withholding will not apply with respect to payments made to designated exempt recipients, such as corporations and tax-exempt organizations. Backup withholding is not an additional tax and may be claimed as a credit against the U.S. federal income tax liability of a U.S. Holder, provided that the required information is timely furnished to the IRS.

Under the Hiring Incentives to Restore Employment Act of 2010 (the "HIRE Act"), some payments made to "foreign financial institutions" in respect of accounts of U.S. stockholders at such financial institutions may be subject to withholding at a rate of 30%. U.S. Treasury Regulations provide that such withholding will only apply to distributions paid on or after July 1, 2014, and to other "withholdable payments" (including payments of gross proceeds from a sale or other disposition of our Ordinary Shares) made on or after January 1, 2017. U.S. Holders should consult their tax advisors regarding the effect, if any, of the HIRE Act on their ownership and disposition of our Ordinary Shares. See "Non-U.S. Holders of Ordinary Shares."

### **Non-U.S. Holders of Ordinary Shares**

Except as provided below, an individual, corporation, estate or trust that is not a U.S. Holder generally will not be subject to U.S. federal income or withholding tax on the payment of dividends on, and the proceeds from the disposition of, our Ordinary Shares.

A non-U.S. Holder may be subject to U.S. federal income or withholding tax on a dividend paid on our Ordinary Shares or the proceeds from the disposition of our Ordinary Shares if: (1) such item is effectively connected with the conduct by the non-U.S. Holder of a trade or business in the United States or, in the case of a non-U.S. Holder that is a resident of a country which has an income tax treaty with the United States, such item is attributable to a permanent establishment or, in the case of gain realized by an individual non-U.S. Holder, a fixed place of business in the United States; (2) in the case of a disposition of our Ordinary Shares, the individual non-U.S. Holder is present in the United States for 183 days or more in the taxable year of the sale and other specified conditions are met; (3) the non-U.S. Holder is subject to U.S. federal income tax pursuant to the provisions of the U.S. tax law applicable to U.S. expatriates.

In general, non-U.S. Holders will not be subject to backup withholding with respect to the payment of dividends on our Ordinary Shares if payment is made through a paying agent, or office of a foreign broker outside the United States. However, if payment is made in the United States or by a U.S. related person, non-U.S. Holders may be subject to backup withholding, unless the non-U.S. Holder provides on an applicable Form W-8 (or a substantially similar form) a taxpayer identification number, certifies to its foreign status, or otherwise establishes an exemption. A U.S. related person for these purposes is a person with one or more current relationships with the United States.

The amount of any backup withholding from a payment to a non-U.S. Holder will be allowed as a credit against such holder's U.S. federal income tax liability and may entitle such holder to a refund, provided that the required information is timely furnished to the IRS.

The HIRE Act may impose withholding taxes on some types of payments made to "foreign financial institutions" and some other non-U.S. entities. Under the HIRE Act, the failure to comply with additional certification, information reporting and other specified requirements could result in withholding tax being imposed on payments of dividends and sales proceeds to U.S. Holders that own Ordinary Shares through foreign accounts or foreign intermediaries and specified non-U.S. Holders. The HIRE Act imposes a 30% withholding tax on dividends on, and gross proceeds from the sale or other disposition of, Ordinary Shares paid from the United States to a foreign financial institution or to a foreign nonfinancial entity, unless (1) the foreign financial institution undertakes specified diligence and reporting obligations or (2) the foreign nonfinancial entity either certifies it does not have any substantial U.S. owners or furnishes identifying information regarding each substantial U.S. owner. In addition, if the payee is a foreign financial institution, it generally must enter into an agreement with the U.S. Treasury that requires, among other things, that it undertake to identify accounts held by specified U.S. persons or U.S.-owned foreign entities, annually report certain information about such accounts, and withhold 30% on payments to other specified account holders. U.S. Treasury Regulations provide that such withholding will only apply to distributions paid on or after July 1, 2014, and to other "withholdable payments" (including payments of gross proceeds from a sale or other disposition of our Ordinary Shares) made on or after January 1, 2017. You should consult your tax advisor regarding the HIRE Act.

#### **10.F. Dividends and paying agents**

Not applicable.

#### **10.G. Statement by experts**

Not applicable.

#### **10.H. Documents on display**

We are subject to certain of the information reporting requirements of the Securities Exchange Act of 1934, or the Exchange Act. As a foreign private issuer, we are exempt from the rules and regulations under the Exchange Act prescribing the furnishing and content of proxy statements, and our officers, directors and principal shareholders are exempt from the reporting and "short-swing" profit recovery provisions contained in Section 16 of the Exchange Act, with respect to their purchase and sale of our shares. In addition, we are not required to file reports and financial statements with the SEC as frequently or as promptly as U.S. companies whose securities are registered under the Exchange Act. However, we are required to file with the SEC, within four months after the end of each fiscal year, an annual report on Form 20-F containing financial statements audited by an independent accounting firm. We publish unaudited interim financial information after the end of each quarter. We furnish this quarterly financial information to the SEC under cover of a Form 6-K.

You may read and copy any document we file with the SEC at its public reference facilities at 100 F Street, NE, Washington, D.C. 20549. You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, NE, Washington, D.C. 20549. The SEC also maintains a website that contains reports, proxy and information statements and other information regarding registrants that file electronically with the SEC. The address of this website is <http://www.sec.gov>. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference facilities.

#### **10.I. Subsidiary information**

Not applicable.

### **ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

In the ordinary course of our operations, we are exposed to certain market risks, primarily changes in foreign currency exchange rates and interest rates.

**Foreign Currency Exchange Rate Risk.** We develop products in Israel and sell them primarily in the Americas, EMEA, and the Asia Pacific region. As a result, our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. In 2013, 51% of our revenues and 35% of our expenses were denominated in U.S. dollars. Since our financial results are reported in U.S. dollars, fluctuations in the rates of exchange between the U.S. dollar and non-U.S. dollar currencies may have a material adverse effect on our business, financial condition and results of operations. We believe that our exposure to currency exchange rate risk is somewhat reduced due to the number of different countries and currencies in which we conduct business, including the main currencies of NIS, British pounds and Euros. For example, a ten percent increase or decrease from 2013 exchange rates could have a net effect of about \$1.8 million on our operating income. In 2013, the net effect of the change in value of the U.S. dollar against other currencies was a minor increase in revenues by \$50,000, an increase in costs of revenues by \$0.4 million and an increase in operating expenses by \$1.0 million.

In addition, we have balance sheet exposure arising from assets and liabilities denominated in currencies other than U.S. dollars, mainly in Euros, British pounds, NIS and Australian dollars. Any change of the conversion rates between the U.S. dollar and these currencies may create financial gain or loss. We enter from time to time into forward contracts related to foreign currencies in order to protect against monetary balances denominated in foreign currencies, and certain forecasted transactions. We do not participate in any speculative investments. At December 31, 2013, we had short forward exchange contracts to sell up to Euro 5.7 million for a total amount of \$7.9 million, British Pounds 4.7 million for a total amount of \$7.8 million and Australian Dollar 2.8 million for a total amount of \$2.4 million.

**Interest Rate Risk.** As of December 31, 2013, we had cash, cash equivalents and short-term investments of \$56.9 million, which consist mainly of cash, short-term bank deposits with major banks, government and corporate bonds. Of this, a total of \$12.1 million is denominated in non-U.S. dollar currencies. Nearly all of these cash and investments are not insured by the FDIC or similar governmental deposit insurance outside the United States. We believe a substantial decrease in market interest rates or market value would have an immaterial impact on our business, financial condition and results of operations. Our policy is that up to \$10 million of our total cash and investments may be invested in equity of companies that have a policy to regularly distribute dividends or in ETFs of a similar nature. As of December 31, 2013, \$7.4 million of our cash, cash equivalents and investments were invested in equity securities of such companies.

The following table provides information about our investment portfolio, cash, and investments as of December 31, 2013 and presents principal cash flows and related weighted averages interest rates by expected maturity dates.

<b>YEAR OF MATURITY</b>	<b>2014</b>
	<i>(in thousands of dollars)</i>
<b><u>A) Cash, cash equivalents and investments portfolio:</u></b>	
Cash and cash equivalents	\$ 25,346
Average interest rate	0.1%
Government and corporate bonds	\$ 15,203
Average interest (yield) rate	1.5%
Bank deposits	\$ 9,001
Average interest rate	2.1%
Equity securities	<u>\$ 7,383</u>
Total cash, cash equivalents and investments portfolio	<u>\$ 56,933</u>
<b><u>B) Long-term debts:</u></b>	
None	

## **ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES**

The Company does not have any outstanding American Depositary Shares or American Depositary Receipts.

## **PART TWO**

### **ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES**

None.

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

None.

### **ITEM 15. CONTROLS AND PROCEDURES**

#### **(a) Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31, 2013, or the Evaluation Date. Based on such evaluation, those officers have concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be included in periodic filings under the Exchange Act and that such information is accumulated and communicated to management, including our principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosure.

#### **(b) Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Exchange Act. Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based principally on the framework and criteria established in Internal Control - Integrated Framework (1992) issued by the Committee of Sponsoring Organizations of the Treadway Commission as of the end of the period covered by this report. Based on that evaluation, our management has concluded that our internal control over financial reporting was effective as of December 31, 2013 at providing reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

#### **(c) Attestation Report of the Registered Public Accounting Firm**

Brightman Almagor Zohar & Co., a member firm of Deloitte Touche Tohmatsu, the independent registered public accounting firm that audited our 2013 consolidated financial statements included in this annual report, has issued an attestation report on our internal control over financial reporting. The report appears elsewhere herein.

#### **(d) Changes in Internal Control over Financial Reporting**

During the year ended December 31, 2013, there were no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **ITEM 16A. Audit Committee Financial Expert**

Our board of directors has determined that Dr. Shlomo Nass, a member of our audit committee, is an audit committee financial expert, as defined under the Exchange Act Rules, and is independent in accordance with applicable Exchange Act Rules and Nasdaq Rules.

**ITEM 16B. Code of Ethics**

We have adopted a written code of ethics that applies to our officers and employees, including our principal executive officer, principal financial officer, principal controller and persons performing similar functions as well as our directors. Our Code of Business Conduct and Ethics is posted on our website at [www.clicksoftware.com](http://www.clicksoftware.com).

**ITEM 16C. Principal Accountant Fees and Services**

Brightman Almagor Zohar & Co., a member of Deloitte Touche Tohmatsu, has served as our principal independent registered public accounting firm for each of the three years ended December 31, 2013, 2012 and 2011.

The following table provides information regarding fees paid by us to Brightman Almagor Zohar & Co and/or other member firms of Deloitte Touche Tohmatsu for all services, including audit services, for the years ended December 31, 2013 and 2012:

	<b>Year Ended</b>	
	<b>December 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Audit fees <sup>(1)</sup>	\$ 177,000	\$ 171,000
Audit-related fees	-	-
Tax fees <sup>(2)</sup>	48,000	55,000
All other fees <sup>(3)</sup>	-	14,000
	<u>          </u>	<u>          </u>
Total	<u>\$ 225,000</u>	<u>\$ 240,000</u>

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(1) *Includes professional services rendered in connection with the audit of our annual financial statements and internal control over financial reporting and the review of our interim financial statements.*

(2) *Includes professional fees related to tax returns, transfer pricing and consulting on state and sales tax in the United States.*

(3) *Includes fees for services related to due diligence on the purchase of intangible assets.*

***Pre-Approval of Auditors' Compensation***

Our audit committee is responsible for pre-approving audit and non-audit services provided to us by our independent registered public accounting firm. 100% of the non-audit services provided to us by the independent auditors in 2013 and 2012 were either pre-approved by the full audit committee, or by the Chairman of the Audit Committee, who was delegated by the audit committee to approve the non-audit services provided by our independent auditors for amounts up to \$20,000 per instance (subject to later ratification by the audit committee). All approvals by the Chairman of the Audit Committee were duly ratified.

**ITEM 16D. Exemptions from the Listing Standards for Audit Committees**

Not applicable.

**ITEM 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers**

Not applicable.

**ITEM 16F. Change in Registrant's Certifying Accountant**

Not applicable.

**ITEM 16G. Corporate Governance**

Under Rule 5615(a)(3) to the Nasdaq Rules, foreign private issuers, such as us, are permitted to follow certain home country corporate governance practices instead of certain provisions of the Nasdaq Rules. A foreign private issuer that elects to follow a home country practice instead of any of such provisions must submit to Nasdaq, in advance, a written statement from an independent counsel in such issuer's home country certifying that the issuer's practices are not prohibited by the home country's laws. We have provided Nasdaq with a notice of non-compliance with respect to certain Nasdaq Rules. Below is a summary of the significant ways in which our corporate governance practices differ from the corporate governance requirements of Nasdaq Rules applicable to domestic U.S. listed companies.

As described in Item 10.B. "Memorandum and articles of association," Rule 5620(c) to Nasdaq Rules requires that an issuer listed on the Nasdaq Global Select Market has a quorum requirement that in no case be less than 33 1/3% of the outstanding shares of the such issuer's common voting stock. However, our articles of association, consistent with the Companies Law, provide for a lower general quorum requirement of 33% of our outstanding shares and even lower in the event that the required quorum is not present within half an hour from the time appointed for holding an adjourned meeting, or, in the case the meeting that was adjourned was convened by the shareholders, if the required quorum is not present at the time appointed for holding such adjourned meeting. Our quorum requirements for an adjourned meeting do not comply with the Nasdaq requirements and we instead follow our home country practice.

We have chosen to follow our home country practice in lieu of the requirements of Rule 5250(d)(1), relating to an issuer's furnishing of its annual report to shareholders and we post our annual report on Form 20-F on our website ([www.clicksoftware.com](http://www.clicksoftware.com)) as soon as practicable following the filing of the annual report on Form 20-F with the SEC.

**ITEM 16H. Mine Safety Disclosure**

Not applicable.

### **PART THREE**

#### **ITEM 17. FINANCIAL STATEMENTS**

Not applicable.

#### **ITEM 18. FINANCIAL STATEMENTS**

The following consolidated financial statements, and the related notes thereto, and the Reports of Independent Public Accountants are filed as a part of this annual report.

Reports of Independent Registered Public Accounting Firm.....	82
Consolidated Balance Sheets .....	84
Consolidated Statements of Operations .....	85
Consolidated Statements of Changes in Shareholders' Equity .....	86
Consolidated Statements of Cash Flows .....	87
Notes to Consolidated Financial Statements .....	88

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**To the Shareholders of  
ClickSoftware Technologies Ltd.  
Petach Tikva, Israel**

We have audited the accompanying consolidated balance sheets of ClickSoftware Technologies Ltd. and subsidiaries (the "Company") as of December 31, 2013 and 2012, and the related consolidated statements of operations, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2013. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2013 and 2012, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2013, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2013, based on the criteria established in *Internal Control — Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 7, 2014 expressed an unqualified opinion on the Company's internal control over financial reporting.

**/s/ Brightman Almagor Zohar & Co.  
Certified Public Accountants  
A member firm of Deloitte Touche Tohmatsu**

Tel Aviv, Israel  
April 7, 2014

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**To the Shareholders of  
ClickSoftware Technologies Ltd.  
Petach Tikva, Israel**

We have audited the internal control over financial reporting of ClickSoftware Technologies Ltd. and subsidiaries (the "Company") as of December 31 2013, based on criteria established in *Internal Control — Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying *Management's Report on Internal Control over Financial Reporting*. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on the criteria established in *Internal Control — Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements as of and for the year ended December 31, 2013 of the Company and our report dated April 7, 2014 expressed an unqualified opinion on those financial statements.

**/s/ Brightman Almagor Zohar & Co.  
Certified Public Accountants  
A member firm of Deloitte Touche Tohmatsu**

Tel Aviv, Israel  
April 7, 2014

**CLICKSOFTWARE TECHNOLOGIES LTD.**  
**CONSOLIDATED BALANCE SHEETS**  
*(in thousands, except share data)*

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents	\$ 25,346	\$ 12,793
Deposits (Note 3)	9,001	30,310
Marketable securities (Note 3)	22,586	15,635
Trade receivables, net of allowance for doubtful accounts of \$500 and \$738 as of December 31, 2013 and 2012, respectively (Note 4)	22,490	21,792
Deferred taxes (Note 14)	1,740	220
Other receivables and prepaid expenses (Note 5)	4,408	3,398
<b>Total Current Assets</b>	<b><u>85,571</u></b>	<b><u>84,148</u></b>
<b>Long-Term Assets:</b>		
Deposits (Note 6 & Note 11A)	1,072	621
Other receivables and prepaid expenses (Note 5)	218	275
Severance Pay funds (Note 7)	2,052	1,965
Deferred taxes (Note 14)	2,060	1,230
Identifiable Intangible assets, Net (Note 8)	-	452
Goodwill (Note 8)	1,572	1,572
Property and Equipment, Net (Note 9)	5,023	4,206
<b>Total Long-Term Assets</b>	<b><u>11,997</u></b>	<b><u>10,321</u></b>
<b>TOTAL ASSETS</b>	<b><u>\$ 97,568</u></b>	<b><u>\$ 94,469</u></b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current Liabilities:</b>		
Accounts payable and accrued expenses (Note 10)	\$ 17,707	\$ 16,536
Deferred revenues	13,420	9,047
<b>Total Current Liabilities</b>	<b><u>31,127</u></b>	<b><u>25,583</u></b>
<b>Long-Term Liabilities:</b>		
Accrued severance pay (Note 7)	4,840	4,465
Deferred tax liability (Note 14)	40	-
Deferred revenues	4,642	1,503
<b>Total Long-Term Liabilities</b>	<b><u>9,522</u></b>	<b><u>5,968</u></b>
<b>Total Liabilities</b>	<b><u>40,649</u></b>	<b><u>31,551</u></b>
<b>Commitments and Contingencies (Note 11)</b>		
<b>Shareholders' Equity (Note 12):</b>		
<i>Special preferred shares NIS 0.02 par value:</i>		
Authorized – 5,000,000 as of December 31, 2013 and 2012;		
No issued and outstanding shares as of December 31, 2013 and 2012;		
<i>Ordinary shares of NIS 0.02 par value:</i>		
Authorized - 100,000,000 as of December 31, 2013 and 2012;		
Issued – 32,533,575 shares as of December 31, 2013 and 31,693,942 as of December 31, 2012;		
Outstanding – 32,494,575 shares as of December 31, 2013 and 31,654,942 shares as of December 31, 2012;		
Additional paid-in capital	137	132
Accumulated other comprehensive income	92,301	87,566
Accumulated deficit	703	559
	<u>(36,179)</u>	<u>(25,296)</u>
	56,962	62,961
Treasury shares, at cost: 39,000 shares	(43)	(43)
<b>Total Shareholders' Equity</b>	<b><u>56,919</u></b>	<b><u>62,918</u></b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b><u>\$ 97,568</u></b>	<b><u>\$ 94,469</u></b>

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

**CLICKSOFTWARE TECHNOLOGIES LTD.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
*(in thousands, except share and per share amounts)*

	<b>YEAR ENDED DECEMBER 31,</b>		
	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Revenues (Note 13):			
Software license	\$ 28,679	\$ 34,541	\$ 31,542
Services	74,502	65,505	55,545
Total revenues	<u>103,181</u>	<u>100,046</u>	<u>87,087</u>
Cost of revenues:			
Software license	4,413	3,686	2,519
Services	39,894	35,185	29,177
Total cost of revenues	<u>44,307</u>	<u>38,871</u>	<u>31,696</u>
Gross profit	<u>58,874</u>	<u>61,175</u>	<u>55,391</u>
Operating expenses:			
Research and development	15,970	13,146	9,019
Selling and marketing	39,706	31,977	23,382
General and administrative	9,121	8,779	7,386
Impairment of goodwill	-	-	939
Total operating expenses	<u>64,797</u>	<u>53,902</u>	<u>40,726</u>
Operating (loss) income	<u>(5,923)</u>	<u>7,273</u>	<u>14,665</u>
Other income	-	110	-
Financial income, net	839	274	7
Net (loss) income before taxes	<u>(5,084)</u>	<u>7,657</u>	<u>14,672</u>
Taxes on income (Tax benefit) (Note 14)	(924)	169	2,462
Net (loss) income	<u>\$ (4,160)</u>	<u>\$ 7,488</u>	<u>\$ 12,210</u>
Other comprehensive income, net of tax:			
Gain in respect of marketable securities	411	37	45
Gain /(Loss) in respect of derivatives instruments designated for cash flow hedge	(267)	689	(440)
Comprehensive (loss) income	<u>\$ (4,016)</u>	<u>\$ 8,214</u>	<u>\$ 11,815</u>
Basic net (loss) earnings per share	<u>\$ (0.13)</u>	<u>\$ 0.24</u>	<u>\$ 0.39</u>
Diluted net (loss) earnings per share	<u>\$ (0.13)</u>	<u>\$ 0.23</u>	<u>\$ 0.38</u>
Shares used in computing basic net (loss) earnings per share	<u>32,048,030</u>	<u>31,545,435</u>	<u>31,014,373</u>
Shares used in computing diluted net (loss) earnings per share	<u>32,048,030</u>	<u>32,837,789</u>	<u>32,226,883</u>

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

**CLICKSOFTWARE TECHNOLOGIES LTD.**  
**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**  
*(in thousands, except share data)*

	Number of Ordinary Shares	Share Capital	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Treasury Shares	Total
Balance as of December 31, 2010	30,634,227	\$ 126	\$ 81,170	\$ (27,393)	\$ 228	\$ (43)	\$ 54,088
Employee options exercised	734,661	5	1,482	-	-	-	1,487
Stock-based compensation expense related to employees and consultants	-	-	1,731	-	-	-	1,731
Accumulated other comprehensive income	-	-	-	-	(395)	-	(395)
Dividend	-	-	-	(10,017)	-	-	(10,017)
Net income	-	-	-	12,210	-	-	12,210
Balance as of December 31, 2011	31,368,888	\$ 131	\$ 84,383	\$ (25,200)	\$ (167)	\$ (43)	\$ 59,104
Employee options exercised	286,054	1	649	-	-	-	650
Stock-based compensation expense related to employees and consultants	-	-	2,534	-	-	-	2,534
Accumulated other comprehensive income	-	-	-	-	726	-	726
Dividend	-	-	-	(7,584)	-	-	(7,584)
Net income	-	-	-	7,488	-	-	7,488
Balance as of December 31, 2012	31,654,942	\$ 132	\$ 87,566	\$ (25,296)	\$ 559	\$ (43)	\$ 62,918
Employee options exercised	839,633	5	1,991	-	-	-	1,996
Stock-based compensation expense related to employees and consultants	-	-	2,744	-	-	-	2,744
Accumulated other comprehensive income	-	-	-	-	144	-	144
Dividend	-	-	-	(6,723)	-	-	(6,723)
Net loss	-	-	-	(4,160)	-	-	(4,160)
Balance as of December 31, 2013	32,494,575	\$ 137	\$ 92,301	\$ (36,179)	\$ 703	\$ (43)	\$ 56,919

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

**CLICKSOFTWARE TECHNOLOGIES LTD.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

*(in thousands)*

	<b>YEAR ENDED DECEMBER 31,</b>		
	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net (loss) income	\$ (4,160)	\$ 7,488	\$ 12,210
Adjustments to reconcile net income to net cash provided by operating activities:			
Income and expense items not involving cash flows:			
Depreciation	2,593	2,144	1,519
Stock-based compensation	2,744	2,534	1,731
Amortization of acquired intangible assets	278	714	782
Impairment of goodwill	-	-	939
Impairment of acquired intangible assets	174	-	55
Severance pay, net	288	399	373
Gain on marketable securities	(429)	(146)	(94)
Other	92	13	11
Changes in operating assets and liabilities:			
Trade receivables	(698)	1,586	(9,123)
Deferred taxes	(2,310)	(540)	1,310
Other receivables	(809)	(104)	(443)
Accounts payable and accrued expenses	1,171	2,928	1,034
Deferred revenues	7,512	(807)	1,623
Net cash provided by operating activities	6,446	16,209	11,927
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Purchases of equipment	(3,502)	(2,490)	(2,018)
Decrease (Increase) in deposits, net	20,858	(1,595)	(11,969)
Investments in marketable securities	(15,686)	(7,459)	(8,298)
Proceeds from sales of marketable securities	9,164	2,915	5,286
Net cash provided by (used in) investing activities	10,834	(8,629)	(16,999)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Dividend paid	(6,723)	(10,120)	(7,481)
Employee options exercised	1,996	650	1,487
Net cash used in financing activities	(4,727)	(9,470)	(5,994)
Increase (decrease) in cash and cash equivalents	12,553	(1,890)	(11,066)
Cash and cash equivalents at beginning of year	12,793	14,683	25,749
Cash and cash equivalents at end of year	\$ 25,346	\$ 12,793	\$ 14,683
Supplemental cash flow information:			
Cash paid for taxes	\$ 2,052	\$ 692	\$ 713
Cash paid for interest	\$ -	\$ 1	\$ 4

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

## CLICKSOFTWARE TECHNOLOGIES LTD.

### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

*(dollars in thousands, except share amounts)*

#### NOTE 1 – GENERAL

ClickSoftware Technologies Ltd. (the "Company" or "ClickSoftware") was incorporated in Israel and is a leading provider of software products and solutions for workforce management and optimization. The Company's products and solutions incorporate best business practices, key business functions of service operations, and sophisticated decision-making algorithms that enable its customers to more efficiently manage their service operations in a scalable, integrated manner.

The Company's solutions are grouped into four main suites which together comprise its Service Optimization Suite:

- **Field Service Daily Suite** covers automatic decision making and optimization support to manage field service operations.
- **Roster (Shift Planning) Suite** covers shift planning needs for both the manager as well as the employee to optimize the balance between staffing levels needed for serving customers and managing labor costs, and employee preferences.
- **ClickMobile and Mobility Suite** covers the needs of the mobile individual and back-office staff for field data communication.
- **Forecasting and Planning Suite** covers tactical short term resource planning.

The Company's Service Optimization Suite is designed to increase service revenue and customer responsiveness while reducing costs. The Company's Service Optimization Suite includes strategic and tactical workforce planning, optimized service scheduling, intelligent problem resolution, mobile workforce management, shift planning and business analytics, connecting various organizational levels and all functions, from executive strategy to operational execution. The following comprise the individual products of the above suites: ClickSchedule, ClickAnalyze, ClickMobile, ClickLocate, ClickContact, ClickRoster, ClickPlan and ClickForecast. The Company provides a cloud-based offering of its Service Optimization Suite via ClickSoftware Cloud Services, which aims at the large market enterprise customers and ClickExpress, which aims at the small and mid-size company markets.

#### NOTE 2 -- SIGNIFICANT ACCOUNTING POLICIES

##### **Basis of presentation**

The financial statements have been prepared in conformity with accounting principles generally accepted in the United States.

##### **Principles of consolidation**

The consolidated financial statements include the financial statements of the Company and its wholly owned subsidiaries in the United States (ClickSoftware, Inc. a wholly owned subsidiary of ClickSoftware Europe Limited), in the United Kingdom (ClickSoftware Europe Limited), in Germany (ClickSoftware Central Europe, GmbH), in Belgium (ClickSoftware Belgium, N.V.), in Australia (ClickSoftware Australia Pty. Ltd., a wholly owned subsidiary of ClickSoftware, Inc.), in Japan (ClickSoftware Japan KK), in India (ClickSoftware India Private Limited), in South Africa (ClickSoftware Technologies (Pty) Ltd), in Brazil (ClickSoftware Brazil Soluções em Gestão de Forças de Trabalho Ltda) and in Russia (ClickSoftware Limited Liability Company). The subsidiaries are primarily engaged in the sale and marketing of the Company's products in the Americas, EMEA (Europe, Middle East and Africa but not including Israel) and the rest of the world. All significant intercompany balances and transactions have been eliminated.

##### **Financial statements in U.S. dollars**

The reporting currency of the Company is the U.S. dollar ("dollar"). The dollar is the functional currency of the Company and its subsidiaries. Transactions and balances originally denominated in dollars are presented at their

original amounts. Non-dollar transactions and balances are remeasured into dollars in accordance with the principles set forth in ASC 830 ("Foreign Currency Matters"). All exchange gains and losses from translation of monetary balance sheet items resulting from transactions in non-dollar currencies are recorded in the statement of operations as they arise.

### **Use of estimates**

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

### **Cash and cash equivalents**

Cash equivalents include short-term, highly liquid investments that are readily convertible to cash, with original maturities of three months or less.

### **Concentration of credit risk**

Financial instruments, which potentially subject the Company to credit risk, consist principally of cash instruments and accounts receivable. The Company maintains cash and cash equivalents and investments with major financial institutions in the United States, Europe and Israel. Nearly all of the cash and investments are not insured by the FDIC or other similar governmental insurance limits. The accounts receivable are derived from sales to a large number of customers, mainly large industrial corporations and their suppliers located mainly in Europe, the United States and Brazil. The Company generally does not require collateral. The Company performs ongoing credit evaluations of its customers and maintains an allowance for doubtful accounts which management believes adequately covers all anticipated losses in respect of trade receivables.

### **Short term bank deposits**

Bank deposits with maturities of more than three months but less than one year are included in short-term deposits.

### **Marketable securities**

Securities classified as available-for-sale are reported at fair value with unrealized gains and losses, net of related tax, recorded as a separate component of other comprehensive income in equity until realized. Unrealized losses that are considered to be other-than-temporary are charged to statement of operations as an impairment charge and are included in the consolidated statement of operations under financial expenses. Realized gains and losses on sales of the securities, as well as premium or discount amortization, are included in the consolidated statement of operations as financial income or expenses.

Fair values for marketable securities were determined using the quoted prices in active market for identical asset (level 1).

### **Property and equipment**

Property and equipment is stated at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, ranging from 3 to 16 years. Leasehold improvements are amortized using the straight-line method, over the shorter of the lease term or the useful lives of the improvements.

The Company complies with provisions of ASC 360 ("Property, Plant and Equipment"). ASC 360 requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to undiscounted future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less cost to sell.

### **Identifiable Intangible Assets**

Intangible assets representing primarily core technology and in process research and development ("IPR&D"), customer lists and relationships and non-competition arrangements (arising from business combinations) are

recorded at cost less accumulated amortization as outlined in Note 8. Intangible assets are amortized over their estimated useful lives on a straight-line basis ranging from 3 to 6 years. As of December 31, 2013 the balance is fully amortized or impaired.

### **Goodwill**

Goodwill represents the excess purchase price paid by the Company over the fair value of identifiable intangible assets as a result of purchasing a business. Goodwill is not amortized but instead is tested for impairment annually or more frequently if events or changes in circumstances indicate that it may be impaired. Goodwill impairment testing is a two-step process and may be preceded by a qualitative impairment assessment. Qualitative impairment assessment should be made to changes in circumstances and events indicating whether some of the intangible assets were impaired. When determined, on the basis of qualitative factors, that the fair value of the reporting unit is more likely than not less than the carrying amount, the two-step impairment test would be required. The first step involves comparing the fair value of a company's reporting units to their carrying amount. If the fair value of the reporting unit is determined to be greater than its carrying amount, there is no impairment. If the reporting unit's carrying amount is determined to be greater than the fair value, the second step must be completed to measure the amount of impairment, if any. Step two calculates the implied fair value of goodwill by deducting the fair value of all tangible and intangible assets, excluding goodwill, of the reporting unit from the fair value of the reporting unit as determined in step one. The implied fair value of the goodwill in this step is compared to the carrying value of goodwill. If the implied fair value of the goodwill is less than the carrying value of the goodwill, an impairment loss equivalent to the difference is recorded.

### **Software research and development costs**

Software research and development costs incurred prior to the establishment of technological feasibility are included in research and development expenses. The Company defines establishment of technological feasibility as the completion of a working model. Software development costs incurred subsequent to the establishment of technological feasibility through the period of general market availability of the products are capitalized, if material, after consideration of various factors, including net realizable value. To date, software development costs that are eligible for capitalization have not been material and have been expensed.

### **Revenue recognition**

The Company recognizes revenues in accordance with the ASC 985-605 ("Software Revenue Recognition").

In accordance with ASC 985-605, revenues from software license fees are recognized when persuasive evidence of an arrangement exists, the software product covered by written agreement or a purchase order signed by the customer has been delivered, the license fees are fixed and determinable, collection of the license fees is considered probable and vendor-specific objective evidence (VSOE) of the fair value of undelivered elements exists.

License fees from software arrangements that involve multiple elements, such as consulting, training and post-contract customer support, are allocated to each element of the arrangement based on the residual method. Under the residual method, consideration is allocated to undelivered elements based upon the VSOE of those elements, with the residual of the arrangement fee allocated to and recognized as software license revenue. The Company measures the VSOE for each element according to the price charged when the element is sold separately. For post-contract customer support, the Company determines the VSOE based on the renewal price charged. For other services, such as consulting and training, the Company determines the VSOE based on the fixed hourly/daily rate charged in stand-alone service transactions.

Arrangements that include professional services are evaluated to determine whether those services are essential to the functionality of other elements of the arrangement. When services are considered essential, revenue under the arrangement is recognized using contract accounting. When services are not considered essential, revenue allocable to the services is recognized as the services are performed.

Revenue from software licenses that require significant customization, integration and implementation are recognized based on ASC 605-35 ("Construction-Type and Production-Type Contracts") using contract accounting on the percentage-of-completion method, based on the relationship of actual working hours incurred to total working hours estimated to be incurred over the duration of the contract. In recognizing revenues based on the percentage-of-completion method, the Company estimates time to completion with revisions to estimates reflected in the period in which changes become known. Provisions for estimated losses on uncompleted

contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract.

Service revenues are comprised of revenues from consulting, training, and post-contract customer support. Revenues from consulting services are recognized on a time and material basis, or in a fixed price contract, on a percentage of completion basis. Revenues from training are recognized as the services are provided. Post-contract customer support arrangements provide for technical support and the right to unspecified updates on an if-and-when-available basis. Revenues from these arrangements are recognized ratably over the term of the arrangement, usually one year.

The Company classifies revenue as either software license revenue or services revenue for statement of operations presentation. The Company allocates revenue to each of these categories based on the VSOE for elements in each revenue arrangement and based on the application of the residual method for arrangements in which the Company has established the VSOE for all undelivered elements. Where the Company is unable to establish the VSOE for all undelivered elements, the Company takes a systematic approach, whereby the Company first allocates revenue to any undelivered elements for which the VSOE has been established, and then allocates revenue to any undelivered elements for which the VSOE has not been established based on management's best estimate of the fair value of those undelivered elements. The Company then applies a residual method to determine the license fee. Management's best estimate of fair value of undelivered elements for which the VSOE has not been established is based upon the VSOE of similar offerings and other objective criteria.

### **Basic and diluted net income per share**

Basic and diluted net income per share are presented in conformity with ASC 260 ("Earnings per Share") for all years presented. Basic net income per share have been computed using the weighted-average number of ordinary shares outstanding during the year, net of treasury shares (see Note 12). In computing diluted earnings (loss) per share, the potential dilutive effect of outstanding equity awards is taken into account using the treasury stock method.

Outstanding share options and shares issued and reserved for outstanding share options have been excluded from the calculation of basic and diluted net income per share to the extent such securities are anti-dilutive. The total number of options to purchase shares, excluded from the calculations of diluted net income per share, were 3,600,186, 1,242,416 and 497,000 for the years ended December 31, 2013, 2012 and 2011, respectively.

### **Fair value of financial instruments**

The financial instruments of the Company consist mainly of cash and cash equivalents, short-term and long-term investments, current accounts receivable, marketable securities and accounts payable. In view of their nature, the fair value of the financial instruments included in working capital of the Company (other than marketable securities) is usually identical or close to their carrying amounts.

### **Stock-based compensation**

ASC 718 ("Compensation – Stock Compensation") requires that compensation cost relating to share-based payment awards made to employees and directors be recognized in the financial statements. The main awards issued under Company stock-based compensation plans, which are described in Note 12D, "Employee, Directors, and Consultant Option Plans", include stock options and RSUs. The cost for such awards is measured at the grant date based on the calculated fair value of the award. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods (generally the vesting period of the equity award) reduced by estimated forfeitures in the Company Consolidated Statement of Operations.

### **Income taxes**

The Company accounts for income taxes, in accordance with the provisions of ASC 740 ("Income Taxes,") under the liability method of accounting. Under the liability method, deferred taxes are determined based on the differences between the financial statement and tax basis of assets and liabilities at enacted tax rates in effect in the year in which the differences are expected to reverse. Valuation allowances are established, when necessary, to reduce deferred tax assets to amounts expected to be realized.

Deferred tax liabilities and assets are classified as current or non-current based on the classification of the related asset or liability for financial reporting or, if not related to an asset or liability for financial reporting, according to the expected reversal dates of the specific temporary differences.

For uncertain tax positions, the Company follows a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon ultimate resolution. The Company's policy is to include interest and penalties related to unrecognized tax benefits within income tax expense.

### Recent accounting pronouncements

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-02, *Comprehensive Income: Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, which requires companies to disclose significant amounts that have been reclassified out of accumulated other comprehensive income. Amounts that are required to be reclassified in their entirety to net income must be disclosed either on the face of the income statement or in the notes to the financial statements. Amounts that are not required to be reclassified in their entirety to net income in the same reporting period must be disclosed by a cross reference to other disclosures that provide additional information regarding such amounts. ASU No. 2013-02 is effective for fiscal years and interim periods beginning after December 15, 2012. The adoption of ASU No. 2013-02 has not had a material impact on the Company's financial position or results of operations.

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*, which provides explicit guidance on the financial statement presentation of an unrecognized tax benefit. ASU No. 2013-11 requires unrecognized tax benefits to be presented as a reduction to a deferred tax asset, except that, if a net operating loss carryforward, a similar tax loss or a tax credit carryforward is not available at the reporting date to settle any additional income taxes that would result from the disallowance of a tax position, then the unrecognized tax benefit should be presented as a liability. ASU No. 2013-11 has become effective for fiscal years and interim periods beginning after December 15, 2013. The adoption of ASU No. 2013-11 has not had a material impact on the Company's financial position or results of operations.

### NOTE 3 -- SHORT-TERM DEPOSITS AND MARKETABLE SECURITIES

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Bank deposits <sup>(1)</sup>	\$ 9,001	\$ 30,310
Marketable securities - government and corporate bonds <sup>(2)</sup>	15,203	10,600
Marketable securities - equities <sup>(3)</sup>	7,383	5,035
	<u>\$ 31,587</u>	<u>\$ 45,945</u>

(1) The bank deposits bear interest at an average annual rate of 2.1% and 1.3% for 2013 and 2012, respectively.

(2) The Bonds provide a yield at an average annual rate of 1.5% and 1.55% for 2013 and 2012, respectively.

(3) Unrealized net gains are immaterial.

**NOTE 4 -- TRADE RECEIVABLES AND ALLOWANCE FOR DOUBTFUL ACCOUNTS****A. Trade receivables**

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Accounts receivables billed	\$ 20,190	\$ 18,847
Accounts receivables unbilled	2,800	3,683
Allowance for doubtful accounts	(500)	(738)
Trade receivables, net	<u>\$ 22,490</u>	<u>\$ 21,792</u>

**B. Allowance for doubtful accounts**

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Balance at beginning of year	\$ 738	\$ 701
Change of allowance	(97)	37
Write-off	(141)	-
Balance at year end	<u>\$ 500</u>	<u>\$ 738</u>

**NOTE 5 -- OTHER RECEIVABLES AND PREPAID EXPENSES**

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Prepaid expenses	\$ 1,675	\$ 1,890
Government receivables	1,533	616
Employees	467	198
Other	951	969
	<u>\$ 4,626</u>	<u>\$ 3,673</u>
Other receivables and prepaid expenses – Short term	\$ 4,408	\$ 3,398
Other receivables and prepaid expenses – Long term	218	275
	<u>\$ 4,626</u>	<u>\$ 3,673</u>

**NOTE 6 -- LONG-TERM DEPOSITS**

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Bank deposits (see also Note 11A)	\$ 1,072	\$ 621
	<u>\$ 1,072</u>	<u>\$ 621</u>

The bank deposits bear interest at an average annual rate of 2.1% and 1.3% for 2013 and 2012, respectively.

## NOTE 7 -- ACCRUED SEVERANCE PAY, NET

Under Israeli law and labor agreements, the Company is required to make severance payments to its dismissed employees and employees leaving its employment in certain other circumstances. The Company's severance pay obligation to its employees, which is calculated on the basis of the salary of each employee for the last month of the reported period multiplied by the years of such employee's employment, is reflected by the accrual presented in the balance sheet and is partially funded by deposits with insurance companies and provident funds. Outside of Israel the Company accrues severance pay obligations when required under the applicable laws in such jurisdictions. Severance pay obligations made to Israeli employees are considered significant compared to all other subsidiaries.

Severance pay expenses amounted to \$1,932, \$1,632 and \$1,383 for the years ended December 31, 2013, 2012 and 2011, respectively.

## NOTE 8 – GOODWILL AND OTHER INTANGIBLE ASSETS, NET

### A. Goodwill:

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Balance as of January 1	\$ 1,572	\$ 1,572
Changes during year:		
Impairment	-	-
Balance as of December 31	<u>\$ 1,572</u>	<u>\$ 1,572</u>

### B. Identifiable intangible assets, Net:

	<b><u>Useful life</u></b>	<b>DECEMBER 31,</b>	
		<b><u>2013</u></b>	<b><u>2012</u></b>
<b>Original amount</b>			
Core technology	3-6 years	\$ 1,507	\$ 1,507
In process research & development	4 years	472	472
Customer relationship, net of impairment (see C below)	3-6 years	1,007	1,007
Non-compete	4 years	127	127
		<u>\$ 3,113</u>	<u>\$ 3,113</u>
<b>Accumulated amortization</b>		3,113	2,661
<b>Identifiable intangible assets, Net</b>		<u>\$ -</u>	<u>\$ 452</u>

### C. Goodwill and Other Intangible Assets impairment testing

The company performs annual impairment tests in the fourth quarter. For impairment testing the company identified two separate reporting units: ClickSoftware and Service Tycoon (ST) (acquired from AST Technologies in 2009). For ClickSoftware the fair value was significantly higher than the carrying amount. For ClickSoftware reporting unit no events or changes in circumstances indicating intangible assets impairment were detected during 2013. In the fourth quarter of 2013 as a result of the Company's analysis, the company determined that ST technology will no longer be used by the Company. Thus the company reassessed the remaining core technology of ST at a value of zero. As a result a \$174 of intangible assets impairment charges was recorded as of December 31, 2013.

**NOTE 9 -- PROPERTY AND EQUIPMENT, NET**

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
<b>Cost</b>		
Computers and office equipment	\$ 10,928	\$ 8,645
Leasehold improvements	2,992	2,502
	<u>\$13,920</u>	<u>\$11,147</u>
<b>Accumulated depreciation</b>	8,897	6,941
<b>Property and equipment, net</b>	<u>\$ 5,023</u>	<u>\$ 4,206</u>

**NOTE 10 -- ACCOUNTS PAYABLE AND ACCRUED EXPENSES**

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Suppliers	\$ 4,720	\$ 5,392
Employee and related costs	9,235	8,598
Government commitment	3,752	2,546
	<u>\$17,707</u>	<u>\$16,536</u>

**NOTE 11 -- COMMITMENTS AND CONTINGENCIES**

- A. The Company has entered into standby letters of credit agreements with banks and financial institutions relating to the guarantee of future performance on certain contracts. As of December 31, 2013, contingent liabilities on outstanding letter of credit agreements which expire after December 31, 2014 were approximately \$1.1 million in the aggregate. The letters of credit are secured by \$1.1 million in deposits to cover any potential payments under the guarantees.
- B. The Company operates from leased facilities in Israel, the United States, United Kingdom, Germany, India and Australia. The leases for these facilities expire in the years 2014 through 2021. Minimum future rental payments, as of December 31, 2013 are as follows:

2014	\$ 3,783
2015	2,127
2016	1,615
2017-2021	1,648
	<u>\$ 9,173</u>

Rent expense amounted to \$3,527, \$2,442 and \$2,244 for the years ended December 31, 2013, 2012 and 2011, respectively. The Company has a lease for approximately 58,000 square feet of office space in Petach Tikva, Israel. The Company has a lease for office space in Burlington, Massachusetts for approximately 25,000 square feet. The Company has a lease for office space in Burnham, United Kingdom for approximately 11,500 square feet. The Company has a lease for office space in Melbourne, Australia for approximately 10,000 square feet. The Company has a lease for office space in Gurgaon, India for approximately 22,000 square feet.

- C. From time to time, the Company is involved in various routine legal proceedings incidental to the ordinary course of the Company's business. The Company does not believe that the outcome of these pending legal proceeding will have a material adverse effect on the Company's business or consolidated financial condition.

## **NOTE 12 -- SHAREHOLDERS' EQUITY**

### **A. Public Company**

The Company's shares are publicly traded on the Nasdaq Global Select Market.

### **B. Share Capital**

Share capital is comprised of issued and outstanding Ordinary Shares of NIS 0.02 par value.

### **C. Employee Stock Purchase Plan**

None.

### **D. Employee, Directors, and Consultant Option Plans**

The Company adopted its umbrella option plan in 2000 (the "Plan"). Pursuant to the Plan the number of Ordinary Shares made available under it automatically increases on the first day of the Company's fiscal year to equal the lesser of: (i) 5% of the outstanding Ordinary Shares on such date, (ii) 1,250,000 Ordinary Shares, and (iii) an amount determined by the Company's board of directors.

Under the Plan and its sub-plans, the Company granted options to purchase 1,241,000, 794,000 and 554,000 Ordinary Shares at an average exercise price of \$7.25, \$10.38 and \$8.71 for the years ended December 31, 2013, 2012 and 2011, respectively.

During the year ended December 31, 2010, the Company amended the Plan to include the right to grant Restricted Share Units with respect to Ordinary Shares of the Company ("RSUs") with an exercise price per share equal to the par value of each share underlying the RSU. In the year ended December 31, 2010, the board of directors and shareholders at the 2010 Annual Shareholders Meeting ("2010 ASM") approved the grants of an aggregate of 48,000 RSUs to independent directors and a grant of an option to the Company CEO to purchase 100,000 ordinary shares. This RSU grant was in accordance with the resolutions adopted by the shareholders at the 2010 ASM which provided that: (i) each independent director (defined for the purpose hereof as External Directors according to the Companies Law and all other directors other than our employees or our consultants or of any subsidiary), who is appointed as our director, at or after the 2010 ASM, is automatically granted 8,000 RSUs, upon the date such individual first becomes a director; and (ii) each independent director is automatically granted 8,000 RSUs, following each annual meeting of our shareholders, beginning with the Company's 2011 annual shareholders meeting, if on such date he or she shall have served on our Board for at least the preceding six months.

In accordance with the 2010 ASM resolutions, in the year ended December 31, 2013, the Company granted an aggregate of 48,000 RSUs to independent directors.

In accordance with the 2010 ASM resolutions, in the year ended December 31, 2012, the Company granted an aggregate of 48,000 RSUs to independent directors.

In accordance with the 2010 ASM resolutions, in the year ended December 31, 2011, the Company granted an aggregate of 48,000 RSUs to independent directors.

In the years ended December 31, 2013, 2012 and 2011, the board of directors and shareholders at the annual meetings approved a total grant of an option to the Company chairman to purchase 290,000 ordinary shares.

During the years 2003-2012 the board of directors decided to increase the reserve for grants under the Plan, by 7,097,269 options (and RSUs).

A summary of the status of the Company's stock option plans as of December 31, 2013, 2012 and 2011 and changes during the years then ended is as follows:

	OPTIONS AND RSUs AVAILABLE FOR GRANT	OUTSTANDING OPTIONS AND RSUs	WEIGHTED -AVERAGE EXERCISE PRICE PER SHARE (\$)	WEIGHTED -AVERAGE FAIR VALUE OF OPTION
Outstanding at December 31, 2010	2,528,737	3,248,120	3.31	
Increase in option pool, net	800,000	-	-	
Granted	(554,000)	554,000	8.71	\$5.17
Forfeited	45,650	(45,650)	6.14	
Exercised	-	(734,661)	2.07	
Outstanding at December 31, 2011	2,820,387	3,021,809	4.56	
Increase in option pool, net	516,691	-	-	
Granted	(794,000)	794,000	10.38	\$5.20
Forfeited	89,331	(89,331)	10.04	
Exercised	-	(286,054)	2.21	
Outstanding at December 31, 2012	2,632,409	3,440,424	5.96	
Increase in option pool, net	800,000	-	-	
Granted	(1,241,000)	1,241,000	7.25	\$3.64
Forfeited	241,605	(241,605)	8.52	
Exercised	-	(839,633)	2.38	
Outstanding at December 31, 2013	2,433,014	3,600,186	6.95	

The following table summarizes information about options outstanding and exercisable as of December 31, 2013:

RANGE OF EXERCISE PRICE \$	OPTIONS AND RSUs OUTSTANDING				OPTIONS AND RSUs EXERCISABLE		
	NUMBER OUTSTANDING AT DECEMBER 31, 2013	WEIGHTED- AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED- AVERAGE EXERCISE PRICE	NUMBER OUTSTANDING AT DECEMBER 31, 2013	WEIGHTED- AVERAGE REMAINING CONTRACTUAL LIFE	WEIGHTED- AVERAGE EXERCISE PRICE	
0.01	28,002*	6.4	\$0.01	-	-	-	
1.59 - 2.00	466,624	0.9	\$1.94	466,624	0.9	\$1.94	
2.42 - 4.43	345,770	1.6	\$3.19	345,770	1.6	\$3.19	
5.16 - 6.77	222,690	2.9	\$5.65	206,232	2.8	\$5.63	
7.06 - 7.48	1,252,601	5.9	\$7.23	278,664	3.4	\$7.07	
8.12 - 8.41	498,500	4.9	\$8.25	191,750	3.3	\$8.15	
9.48 - 9.71	454,333	4.3	\$9.54	288,750	4.3	\$9.54	
11.24 - 12.98	331,666	4.5	\$12.76	168,541	3.9	\$12.55	
	<u>3,600,186</u>			<u>1,946,330</u>			

\*RSUs

As of December 31, 2013, the aggregate intrinsic value for the options exercisable was \$4.5 million with a weighted-average remaining contractual life of 2.6 years. Additionally, there were 1.6 million options expected to vest with a weighted-average exercise price of \$8.1 and an aggregate intrinsic value of \$0.4 million with a weighted-average remaining contractual life of 6 years.

The weighted average fair value of options exercisable as of the years ended December 31, 2013, 2012 and 2011 was \$3.3, \$2.6 and \$2.32 respectively.

The aggregate intrinsic value for the options exercised during 2013, 2012 and 2011 was \$3.9 million, \$1.9 million and \$4.6 million respectively.

## E. Stock-based compensation expenses

The following table summarizes the effects of stock-based compensation resulting from the application of ASC 718 included in the Statements of Operations for the years ended December 31, 2013, 2012 and 2011:

	YEAR ENDED DECEMBER 31,		
	<u>2013</u>	<u>2012</u>	<u>2011</u>
Cost of revenues	\$ 357	\$ 312	\$ 202
Research and development expenses	292	254	168
Selling and marketing expenses	750	611	389
General and administrative expenses	1,345	1,357	972
Total	<u>\$ 2,744</u>	<u>\$ 2,534</u>	<u>\$ 1,731</u>

The unrecognized stock-based compensation cost calculated under the fair value method for shares incentives expected to vest (unvested shares net of expected forfeitures) as of December 31, 2013 was approximately \$6.1 million and is expected to be recognized over a weighted-average period of 2.2 years.

Under ASC 718, the fair market value of each option grant is estimated on the date of grant using the "Black-Scholes option pricing" method with the following weighted-average assumptions: (1) expected life of 4.8 years (2012 – 4.8, 2011 – 4.7); (2) dividend yield of 1.9% (2012 – 3.2%, 2011 – 3.4%); (3) expected volatility of 55% (2012 – 57%, 2011 – 61%); and (4) risk-free interest rate of 1.9% (2012 – 1.4%, 2011 – 2.5%).

## F. Dividend

During 2011, the Company declared a cash dividend to its shareholders in the amount of \$10 million (\$0.32 per share). During 2011 the Company distributed a cash dividend of \$7.5 million (\$0.24 per share).

During 2012, the Company declared a cash dividend to its shareholders in the amount of \$7.5 million (\$0.24 per share) and distributed a cash dividend of \$10 million (\$0.32 per share).

During 2013, the Company declared a cash dividend to its shareholders in the amount of \$6.7 million (\$0.21 per share) and distributed a cash dividend of \$6.7 million (\$0.21 per share).

## NOTE 13 -- SEGMENT REPORTING

The Company operates in one segment: the design, development, and marketing of software solutions.

The Company's revenues by geographic area are as follows:

Revenue	YEAR ENDED DECEMBER 31,		
	<u>2013</u>	<u>2012</u>	<u>2011</u>
Americas	\$ 50,573	\$ 60,123	\$ 40,070
EMEA	42,548	32,888	39,455
Israel	245	456	847
Asia Pacific	9,815	6,579	6,715
	<u>\$103,181</u>	<u>\$100,046</u>	<u>\$ 87,087</u>

Major customers - as percentage of total sales:

	<u>2013</u>	<u>2012</u>	<u>2011</u>
	%	%	%
Customer A	12	11	12
Customer B	(*)	(*)	10

(\*) Less than 10%

Long-lived assets by geographical areas are as follows:

	<b>YEAR ENDED DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
<b>Property and Equipment, Net</b>		
Americas	\$ 795	\$ 662
EMEA	634	421
Asia Pacific	1,145	411
Israel	2,449	2,712
	<u>\$ 5,023</u>	<u>\$ 4,206</u>

#### **NOTE 14 – TAXES ON INCOME (TAX BENEFIT)**

##### **A. Company**

Part of the Company's investment in equipment has received approvals ("Approved Enterprise" status) in accordance with the Law for the Encouragement of Capital Investments, 1959 (the "Investment Law"). The Company has chosen to receive its benefits through the "Alternative Benefits" track, and, as such, is eligible for various benefits. These benefits include accelerated depreciation of fixed assets used in the investment program, as well as a full tax exemption on undistributed income in relation to income derived from the first plan for a period of 2 years and for the second and third plans for a period of 4 years. Thereafter tax rate of 25% will be applicable for an additional period of up to 5 years for the first plan and 3 years for the second and third plans, commencing with the date on which taxable income is first earned but not later than certain dates. In the case of foreign investment of more than 25%, the tax benefits are extended to 10 years, and in the case of foreign investment ranging from 49% to 100% the tax rate is reduced on a sliding scale to 10%. The benefits are subject to the fulfillment of the conditions of the letter of approval. The first, second and third plans benefit periods have already expired.

On April 1, 2005, an amendment to the Investment Law came into effect ("the Amendment") that 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 a Privileged Enterprise, such as provisions generally requiring that at least 25% of the Privileged 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. However, the Investment Law provides that terms and benefits included in any certificate 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 companies with Approved Enterprise status will generally not be subject to the provisions of the Amendment. As a result of the amendment, tax-exempt income generated under the provisions of the new law, will subject the Company to taxes upon distribution or liquidation. Plans four, five and six are under Privileged Enterprise.

The benefit periods for plans one, two and three have expired.

In 2006, the Company received approval under the Amendment to its Fourth plan as a Privileged Enterprise. The commencement year was 2004. 2011 is the first year the Company generated income subject to the provisions of the new law. The expected expiration year is 2015.

In 2007, the Company received approval under the Amendment to its Fifth plan as a Privileged Enterprise. The commencement year was 2006. 2011 is the first year the Company generated income subject to the provision of the new law. The expected expiration year is 2017.

In 2008, the Company received approval under the Amendment to its sixth plan as a Privileged Enterprise. The commencement year was 2008. 2011 is the first year the Company generated income subject to the provision of the new law. The expected expiration year is 2019.

The entitlement to the above benefits is conditional upon the Company fulfilling the conditions stipulated by the above law, regulations published thereunder and the instruments of approval for the specific investments in

"Approved Enterprises". In the event of failure to comply with these conditions, the benefits may be canceled and the Company may be required to refund the amount of the benefits, in whole or in part, including interest.

Income not eligible for "Approved Enterprise" benefits mentioned above is taxed in 2013 at a regular rate of 25%.

In the event of distribution by the Company of a cash dividend out of retained earnings that were tax exempt due to its Approved Enterprise status, the Company would have to pay corporate tax of 10% - 25% on the income from which the dividend was distributed based on the extent to which non-Israeli shareholders hold Company's shares. A 15% withholding tax may be deductible from dividends distributed to the recipients. From 2011 the Company has earnings attributable to Approved Enterprise programs.

During the years 2011 and 2012, the Company distributed dividends in the aggregate amount of \$17.5 million. Such distributions were paid from the parent company earnings which were not derived from Approved Enterprises earnings, and as such did not result in additional Israeli tax liabilities for the Company.

In November 2012, a law was enacted in Israel to incentivize companies to pay taxes on those Approved Enterprises earnings as if distributed, and effectively release the earnings from any further tax liabilities at the parent company level. The law, although not mandatory, offers lower tax rates on those earnings, accumulated through the year ended December 31, 2011, elected to be "released" which as applicable to the Company will be approximately 6%. During 2013, the Company elected to use the incentive available under the law, releasing 2011 tax-exempt earnings of \$12.2 million for future dividend distributions, by paying tax of \$0.7 million. The Company distributed during 2013 a dividend in the amount of \$6.7 million. Part of this dividend was under the release of 2011 tax-exempt earnings, and therefore, although paid from Approved Enterprises earnings, such distribution did not result in additional Israeli tax liability. Deferred tax provision was included in the Company financial statements for the year ended December 31, 2012.

Except for 2011 Approved Enterprise profits as explained above, the Company has not provided deferred taxes on future distributions of tax-exempt earnings, as management and the board of directors have not yet determined to pay any dividend in the future from those earnings. Accordingly, such earnings have been considered to be permanently reinvested.

In 2011, new legislation amending to the Investment Law was adopted (the "2011 Amendment"). Under the 2011 Amendment, a uniform corporate tax rate will apply to all qualifying income of certain Industrial Companies (requirement of a minimum export of 25% of the company's total turnover), as opposed to the current law's incentives, which are limited to income from Approved Enterprises during their benefits period. Under the 2011 Amendment, the uniform tax rate will be 10% in areas in Israel designated as Development Zone A and 15% elsewhere in Israel during 2011-2012, in 2013 7% and 12.5%, respectively and from 2014, 9% and 16%, respectively. The profits of these Industrial Companies will be freely distributable as dividends, subject to a 15% (20% from 2014) withholding tax (or lower, under an applicable tax treaty).

Under the transition provisions of the 2011 Amendment, the Company may decide to irrevocably implement the provisions of the 2011 Amendment while waiving benefits provided under the current law or to remain subject to the current law.

Changing from the current law to the 2011 Amendment is permitted at any time. The Company does not expect the 2011 Amendment to have material ramifications on the tax payable in respect of its Israeli operations. The Company chose to adopt the 2011 Amendment during 2013 and a request for approval is pending with the tax authorities.

## **B. Tax assessments**

Final tax assessments in Israel have been received up to and including the 2011 tax year.

### C. Deferred taxes

Deferred tax assets, net consist of the following significant items:

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Net operating loss carry forwards of non-Israeli subsidiaries	\$ 7,249	\$ 7,360
Net operating loss carry forwards In Israel*	768	-
R&D cost temporary differences	991	984
Other timing differences	2,016	1,628
Deferred liability due to future dividend from 2012		
Approved Enterprise	-	(735)
Deferred tax assets before valuation allowance	<u>11,024</u>	<u>9,237</u>
Valuation allowance	<u>(7,264)</u>	<u>(7,787)</u>
Deferred tax assets, net of allowance	<u>\$ 3,760</u>	<u>\$ 1,450</u>

\* Based on 16% tax rate for 2014

Presentation in balance sheets:

	<b>DECEMBER 31,</b>	
	<b><u>2013</u></b>	<b><u>2012</u></b>
Current deferred tax asset, net	\$ 1,740	\$ 220
Non-current deferred tax asset, net	2,060	1,230
Non-current deferred tax liability, net	<u>(40)</u>	<u>-</u>
	<u>\$ 3,760</u>	<u>\$ 1,450</u>

Under ASC 740 ("Income Taxes"), deferred tax assets, net are to be recognized for the anticipated tax benefits associated with net operating loss carry-forwards and deductible temporary differences; unless it is more-likely-than-not that some or all of the deferred tax assets will not be realized. The adjustment is made by a valuation allowance. Since in previous years the realization of the net operating loss carry-forwards and deductible temporary differences was less likely than not, a valuation allowance has been established for the full amount of the tax benefits. For 2008, based on historical taxable income from continuing operations and projections for future taxable income, the Company determined that it is more likely than not that some of its deferred tax assets are expected to be realized, and reversed part of the valuation allowance. The reversal of the valuation allowance and other adjustments to the deferred tax assets resulted in the recognition of tax Benefit of \$2,310 and \$540 in 2013 and 2012, respectively.

As of December 31, 2013, net operating loss carry forwards in Israel amounted to approximately \$4.8 million and in U.S. \$18.6 million attributable to the federal tax and approximately \$5.9 million attributable to state tax. The tax loss carry-forwards in the U.S. expire from 2014 through 2024. Utilization of U.S. net operating losses would be subject to substantial annual limitations due to the "change in ownership" provisions of the Internal Revenue Code of 1986 and similar state law provisions. The annual limitations would result in the expiration of part of net operating losses before utilization. There are no material other tax loss carry-forwards in other companies in the group.

Deferred tax has not been provided on the following items:

(1) Taxes that would apply in the event of disposal of investments in subsidiaries, as it is generally the Company's intention to hold these investments, not to realize them.

(2) As for the year ended December 31, 2013, the amount of earnings subject to additional taxes for which deferred taxes were not provided was \$16.1 million and the potential tax liability was in the amount of \$2.4 million. The Company may avoid the tax liability if distribution is not made or is made from resources other than earnings from Approved Enterprises with those earnings permanently reinvested. The Company has not provided deferred taxes, as management and the board of directors have not yet determined to pay any dividend

from these earnings in the future. Accordingly, such earnings have been considered to be permanently reinvested.

(3) Dividends distributable from the income of foreign subsidiaries in the Group, as the Company does not expect these subsidiaries to distribute dividends from currently accumulated profits with tax costs in the foreseeable future. If these dividends were to be paid, the Company would have to pay additional taxes of about \$0.2 million on the distribution, and the amount would be recorded as an income tax expense in the period the dividend is declared.

#### D. Israel and International components of income profit before taxes

	<b>YEAR ENDED DECEMBER 31,</b>		
	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Israel	\$ (10,274)	\$ 4,482	\$13,330
International	5,190	3,175	1,342
	<u>\$ (5,084)</u>	<u>\$ 7,657</u>	<u>\$14,672</u>

#### E. Income taxes included in the statement of operations

	<b>YEAR ENDED DECEMBER 31,</b>		
	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Current taxes	\$ 642	\$ 709	\$1,152
Tax payment for previous years retained earnings (*)	744	-	-
Deferred taxes	(2,310)	(540)	1,310
	<u>\$ (924)</u>	<u>\$ 169</u>	<u>\$2,462</u>

(\*) See Note 14.A above

#### F. Tax reconciliation

The following is a reconciliation of the theoretical tax expense, assuming that all income is taxed at the ordinary statutory average corporate tax rate in Israel and other jurisdictions and the actual tax expense in the statement of operations, is as follows:

	<b>YEAR ENDED DECEMBER 31,</b>		
	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Net (loss) income before taxes	\$ (5,084)	\$ 7,657	\$ 14,672
Average Statutory tax rates	<u>22%</u>	<u>28%</u>	<u>27%</u>
Theoretical tax	<u>(1,118)</u>	<u>2,144</u>	<u>3,961</u>
Change in taxes resulting from effect of “privileged enterprise” status	2,569	(1,120)	(3,266)
Non-deductible expenses	577	1,235	(641)
Change in valuation allowance and deferred taxes	(2,887)	(1,775)	1,951
Other	<u>(65)</u>	<u>(315)</u>	<u>457</u>
	<u>194</u>	<u>(1,975)</u>	<u>(1,499)</u>
Actual tax (benefit) expense	<u>\$ (924)</u>	<u>\$ 169</u>	<u>\$ 2,462</u>

#### G. Uncertain tax positions

As of December 31, 2013, the Company maintains 3 uncertain tax positions accruals in the amounts of \$383, \$256 and \$117.

As of December 31, 2012, the Company maintained 4 uncertain tax positions accruals in the amounts of \$367, \$555, \$178 and \$19.

The Company believes that it has adequately provided for any reasonably foreseeable outcomes related to tax audits and settlement. The final tax outcome of its tax audits could be different from that which is reflected in the Company's income tax provisions and accruals. Such differences could have a material effect on the Company's income tax provision and net income in the period in which such determination is made.

#### **NOTE 15 – SUBSEQUENT EVENTS**

On March 4, 2014 the Company closed the acquisition of Xora, Inc., a cloud-based market leader in mobile workforce management, by merger. Under the terms of the merger agreement, the consideration for the transaction is approximately \$15 million in cash, including working capital and cash adjustments.

**ITEM 19. EXHIBITS**

**EXHIBIT INDEX**

<b>EXHIBIT NUMBER</b>	<b>DESCRIPTION OF DOCUMENT</b>
1.1 <sup>(1)</sup>	Memorandum of Association reflecting amendments integrated into the text as amended and restated as of July 15, 2010 (English translation from the official, original version in Hebrew)
1.2 <sup>(1)</sup>	Articles of Association of ClickSoftware Technologies Ltd., amended and restated as of July 15, 2010
4.1 <sup>(2)</sup>	Fourth Amended and Restated Registration Rights Agreement, dated December 15, 1999
4.2 <sup>(3)</sup>	2000 Share Incentive Plan, as amended and restated as of July 15, 2010
4.3 <sup>(2)</sup>	2000 Employee Share Purchase Plan
4.4 <sup>(4)</sup>	Employment Agreement between ClickSoftware Technologies Ltd. and Shmuel Arvatz effective October 20, 2002
4.5 <sup>(5)</sup>	Amended Form of Indemnification Agreement
4.6 <sup>(3)</sup>	Management and Consulting Agreements for Moshe BenBassat effective as of January 1, 2010
4.7 <sup>(3)</sup>	2003 Israeli Share Incentive Plan, as amended and restated as of July 15, 2010
4.8 <sup>(6)</sup>	Form of 2000 Unapproved U.K. Share Scheme, as amended
4.9 <sup>(7)</sup>	Form of 2000 U.K. Share Scheme, as amended
4.10	Agreement and Plan of Merger by and among Xora, Inc., Ajax Acquisition Corporation, Clicksoftware, Inc., Ned Carlson, as stockholder representative, and the signing stockholders party thereto, dated February 17, 2014
4.11 <sup>(5)</sup>	Summary of Material Terms of the Lease Agreement (originally in Hebrew) effective as of May 30, 2007 by and between ClickSoftware Technologies Ltd. and Azorim M.L.L. Industries Ltd. related to premises in Petach Tikva, Israel
8.1	Subsidiaries of the Registrant
12.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934
12.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934
13.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350
13.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350
15.1	Consent of Brightman Almagor Zohar & Co., a member of Deloitte Touche Tohmatsu
101	The following materials from our Annual Report on Form 20-F for the year ended December 31, 2013 formatted in XBRL (eXtensible Business Reporting Language) are filed herewith: (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Changes in Shareholders' Equity, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to Consolidated Financial Statements, tagged as blocks of text and in detail.

<sup>(1)</sup> Incorporated by reference to the Registrant's Annual Report on Form 20-F filed with the SEC on March 30, 2011.

<sup>(2)</sup> Incorporated by reference to the Registrant's Registration Statement on Form S-1 (file no. 333-30274), as amended, filed with the SEC on February 14, 2000.

<sup>(3)</sup> Incorporated by reference to the Registrant's Proxy Statement for its 2010 Annual Shareholders Meeting filed with the SEC on Form 6-K on June 2, 2010.

<sup>(4)</sup> Incorporated by reference to the Registrant's Annual Report on Form 10-K filed with the SEC on March 24, 2003.

<sup>(5)</sup> Incorporated by reference to the Registrant's Annual Report on Form 20-F filed with the SEC on April 16, 2008.

<sup>(6)</sup> Incorporated by reference to the Registrant's Annual Report on Form 10-K filed with the SEC on March 22, 2004.

<sup>(7)</sup> Incorporated by reference to the Registrant's Annual Report on Form 20-F filed with the SEC on April 11, 2007.

## SIGNATURES

ClickSoftware Technologies Ltd. hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

CLICKSOFTWARE TECHNOLOGIES LTD.

By: /s/ Shmuel Arvatz

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Shmuel Arvatz  
Chief Financial Officer

Date: April 8, 2014

## Board of Directors

### **Dr. Israel Borovich**

*Chairman of the Board and  
Former Chairman of the Board  
EL-AL Israel Airlines Ltd.*

### **Dr. Moshe BenBassat**

*Chief Executive Officer  
ClickSoftware Technologies Ltd.*

### **Mr. Shai Beilis**

*Founder & Chairman of the Board  
Formula Ventures Ltd.*

### **Ms. Nira Dror**

*General Manager  
Nira Dror Ltd.*

### **Dr. Shlomo Nass**

*Senior Partner  
Dr. Shlomo Nass & Co.*

### **Mr. Menahem Shalgi**

*Formerly VP of Business  
Development and M&A  
Amdocs Ltd.*

### **Mr. Gil Weiser**

*Formerly CEO of  
Hewlett-Packard Israel*

#### Safe Harbor

The enclosed letter from our Chairman and Chief Executive Officer contains express or implied forward-looking statements within the Private Securities Litigation Reform Act of 1995 and other U.S Federal securities laws. These forward-looking statements include, but are not limited to, those statements regarding ClickSoftware's growth, leadership position in our market for cloud solutions, market reach in the small and medium business market, expansion of distribution channels, product development plans, future financial performance, future competitive position and the performance of its products. For example, when ClickSoftware discusses anticipated benefits from products it introduced or its future expansion into new markets, ClickSoftware is using forward-looking statements. Such "forward-looking statements" involve known and unknown risks, uncertainties and other factors that may cause actual results or performance to differ materially from those projected. Achievement of these results by ClickSoftware may be affected by many factors, including, but not limited to, risks and uncertainties regarding the length of or changes in ClickSoftware's sales cycle, ClickSoftware's ability to close sales to potential customers in a timely manner and maintain or strengthen relationships with strategic partners, market acceptance of ClickSoftware's products, economic conditions that may affect information technology spending and otherwise affect demand for ClickSoftware's products, the impact of competitive pricing and competitive products, risks relating to product development, the timing of revenue recognition, foreign currency exchange rate fluctuations, and ClickSoftware's ability to maintain or increase its sales pipeline. The forward-looking statements contained in the enclosed letter are subject to other risks and uncertainties, including those discussed in the "Risk Factors" section and elsewhere in ClickSoftware's annual report on Form 20-F for the year ended December 31, 2013 and in subsequent filings with the Securities and Exchange Commission. Except as otherwise required by law, ClickSoftware is under no obligation to (and expressly disclaims any such obligation to) update or alter its forward-looking statements whether as a result of new information, future events or otherwise.

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## Executive Officers

### **Dr. Moshe BenBassat**

*Chief Executive Officer*

### **Mr. Shmuel Arvatz**

*Executive VP and  
Chief Financial Officer*

### **Mr. Zvi Piritz**

*President of EMEA & APAC*

### **Mr. Stephen Timms**

*President of Americas*

## Corporate Headquarters

### **US Office:**

*35 Corporate Drive, Suite 400  
Burlington, MA 01803  
(888) 438-3308  
(781) 272-5903*

### **Israel Office:**

*Azorim Park  
94 Em-Hamoshavot Road  
Petach Tikva 49527  
+972-3-765-9400*

## Investor Information

### **Corporate Counsel, USA**

*Sullivan & Worcester LLP  
New York, NY*

### **Corporate Counsel, Israel**

*Amit, Pollak, Matalon & Co.  
Tel-Aviv, Israel*

### **Independent Registered Public Accounting Firm**

*Deloitte Touche Tohmatsu  
("Brightman Almagor Zohar")  
Tel-Aviv, Israel*

### **Transfer Agent**

*American Stock Transfer  
& Trust Company  
6201 15th Avenue,  
Brooklyn, NY 11219  
(718) 921-8275*

### **Investor Relations**

*Noa Schuman  
Director of Investor Relations  
ClickSoftware Technologies Ltd.  
Israel  
+972-3-765-9467*

*Rob Fink*

*KCSA Strategic Communications  
New York, NY  
(212) 896-1206*

### **Stock Listing**

*Listed on the Nasdaq Global Select  
under the symbol "CKSW"*

### **Annual Meeting of Shareholders**

*Thursday, June 19, 2014,  
at 4:00 p.m. local time (9:00 a.m.  
ET) in our offices in Israel*

### **Company Information on the Web**

*Corporate, financial and shareholder  
information, including news  
releases, financial filings and stock  
quotes are available on the  
ClickSoftware website at:  
[www.clicksoftware.com](http://www.clicksoftware.com)*



To download ClickSoftware's IR App which offers access to stock data, SEC documents, press releases, videos, audiocasts and more, scan this QR Code or search for it on Apple's AppStore or Google Play

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