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, 2004
Commission File No. 0-11456

ELRON ELECTRONIC INDUSTRIES LTD.

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

ISRAEL
(Jurisdiction of incorporation or organization)

3 Azrieli Center, 42nd Floor, Tel-Aviv, Israel 67023
(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act:
Not Applicable
(Title of Class)

Securities registered or to be registered pursuant to Section 12(g) of the Act:
Ordinary Shares, nominal value 0.003 New Israeli Shekels per share
(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:
Not Applicable
(Title of Class)

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: **29,414,424**

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 of 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: **Yes [x]** **No [ ]**

Indicate by check mark which financial statements the registrant has elected to follow:

Item 17 [ ] **Item 18** [x]

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Forward-Looking Statements

This Annual Report on Form 20-F includes certain “forward-looking” statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended. The use of the words “projects,” “expects,” “may,” “plans” or “intends,” or words of similar import, identifies a statement as “forward-looking.” There can be no assurance, however, that actual results will not differ materially from our expectations or projections. Factors that could cause actual results to differ from our expectations or projections include the risks and uncertainties relating to our business described in this Annual Report under Item 3 titled “Risk Factors” as well as those discussed elsewhere in this Annual Report and in our other filings with the Securities and Exchange Commission. Any forward-looking statements contained in this Annual Report speak only as of the date of this Annual Report, and we caution investors and potential investors not to place undue reliance on these statements. We undertake no obligation to update or revise any forward-looking statements. All subsequent written or oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the Risk Factors.

For the purpose of this Annual Report on Form 20-F, the terms “group companies” and “companies in our group” collectively refer to subsidiaries, affiliated and other companies in which we have direct or indirect holdings through our wholly-owned subsidiaries, Elbit Ltd., or Elbit, and DEP Technology Holdings Ltd., or DEP, including DEP’s subsidiary, RDC Rafael Development Corporation Ltd., or RDC. Our ownership interests in our group companies reflected in this Annual Report represent our beneficial ownership interests in these companies as of May 31, 2005 unless otherwise expressly indicated. We have also indicated our direct holding and our share in the holding of RDC in a group company where applicable. The references in this Annual Report to balance sheet items are as of December 31, 2004.

PART I

Item 1. Identity of Directors, Senior Management and Advisers

Not Applicable.

Item 2. Offer Statistics and Expected Timetable

Not Applicable.

Item 3. Key Information

A. Selected Financial Data

The following selected financial data for the years ended December 31, 2000, 2001, 2002, 2003 and 2004 are derived from our audited consolidated financial statements of which the financial statements as of December 31, 2003 and 2004, and for each of the years ended December 31, 2002, 2003 and 2004 appear later in this Form 20-F. The audited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States, or U.S. GAAP.

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands of U.S. Dollars, except per share data)

	Year ended December 31				
	2000	2001	2002	2003	2004
Income:					
Net revenues	$ 27,018	$ 23,782	$ 15,179	$ 16,547	$ 16,330
Equity in losses of affiliated companies	(11,159)	(28,787)	(24,189)	(8,698)	(10,492)
Gain from disposal of businesses and affiliated companies and changes in holdings in affiliated companies, net	26,819	3,179	6,888	25,754	132,396
Other income (expenses), net	43,464	(4,888)	(743)	14,665	4,784
	86,142	(6,714)	(2,865)	48,268	143,018
Costs and Expenses:					
Cost of revenues	25,292	21,059	10,716	10,198	9,650
Research and development costs, net	2,553	3,801	3,418	3,787	3,637
Marketing and selling expenses, net	2,571	2,496	6,412	7,763	3,202
General and administrative expenses	9,629	9,390	9,658	13,923	13,285
Restructuring costs	—	1,192	1,747	—	225
Amortization of intangible assets	2,649	2,448	1,044	1,073	731
Impairment of goodwill	—	—	—	—	1,980
Impairment of intangible assets and property and equipment	—	—	—	—	7,097
Financial expenses (income), net	(2,984)	(1,708)	81	753	(643)
	39,710	38,678	33,076	37,497	39,164
Income (loss) before tax benefit (taxes on income)	46,432	(45,392)	(35,941)	10,771	103,854
Tax benefit (taxes on income)	(8,061)	2,985	2,862	(6,834)	(15,132)
Income (loss) after taxes on income	38,371	(42,407)	(33,079)	3,937	88,722
Minority interest in losses (income) of subsidiaries	—	438	2,823	(10,907)	(4,135)
Income (loss) from continuing operations	38,371	(41,969)	(30,256)	(6,970)	84,587
Loss from discontinued operations	(11,531)	(10,390)	(11,323)	(235)	(454)
Net Income (loss)	$ 26,840	$ (52,359)	$ (41,579)	$ (7,205)	$ 84,133
Income (loss) per share:					
Basic -					
Income (loss) from continuing operations	$ 1.81	$ (1.98)	$ (1.15)	$ (0.24)	$ 2.89
Loss from discontinued operations	(0.54)	(0.49)	(0.43)	(0.01)	(0.02)
Net income (loss)	$ 1.27	$ (2.47)	$ (1.58)	$ (0.25)	$ 2.87
Weighted average number of ordinary shares used in computing basic net income (loss) per share (thousands)	21,172	21,191	26,272	29,194	29,266
Diluted -					
Income (loss) from continuing operations	$ 1.79	$ (1.99)	$ (1.15)	$ (0.24)	$ 2.88
Loss from discontinued operations	(0.54)	(0.49)	(0.43)	(0.01)	(0.02)
Net income (loss)	$ 1.25	$ (2.48)	$ (1.58)	$ (0.25)	$ 2.86
Weighted average number of ordinary shares used in computing diluted net income (loss) per share thousands)	21,446	21,191	26,272	29,194	29,385
Dividend per share	$ 2.62	$ —	$ —	$ —	$ —

	2000	2001	2002	2003	2004
Balance Sheet Data		(U.S. Dollars in thousands)			
Cash, cash equivalents and short-term cash investments	$ 118,280	$ 90,668	$ 71,081	$ 121,064	$ 188,620
Long-term assets	197,183	190,379	255,518	290,333	281,183
Working capital	91,666	75,909	31,791	57,032	158,817
Short-term debt	16,458	16,617	32,999	56,007	5,053
Long-term debt	42,797	51,808	49,389	17,221	4,072
Shareholders' equity	273,720	233,915	259,441	296,130	389,080
Total assets	364,022	321,512	394,253	450,704	501,156

B. Capitalization and Indebtedness

Not Applicable.

C. Reasons for the Offer and Use of Proceeds

Not Applicable.

D. Risk Factors

Risks Affecting us and the Companies in our Group

Our financial results and financial condition are principally impacted by the results of, and the value of our holdings in, our group companies. For the year ended December 31, 2004, our share in the results of operations of our group companies and gain upon the sale of shares in our group companies accounted for substantially all of our income. In addition, as of December 31, 2004, our holdings in group companies represented approximately 54% of our total assets, including 27% attributed to our holding in Partner Communications Company Ltd., or Partner, (Nasdaq:PTNR), most of which holding we sold in April 2005. If our group companies experience difficulties in the future, or if there are adverse changes in their market price or fair value, our financial results and/or the value of our assets will be adversely affected, and we may need to write-down or write-off the carrying value of our holding. In particular, as of December 31, 2004, the carrying value of our holdings in Given Imaging Ltd., or Given Imaging, (Nasdaq:GIVN) represented approximately 14% of our total assets, and the carrying value of our holding in Oncura, Inc., or Oncura, through our subsidiary Galil Medical Ltd., or Galil Medical, represented approximately 6% of our total assets. Any adverse change in the results of operations or financial condition of Given Imaging, Oncura or our other group companies may have a substantial negative impact on results of operations or financial condition.

Our performance significantly depends on the results of operations of our group companies. Our results of operations are directly impacted by the results of operations of our group companies. To the extent any of these companies have poor financial results or encounter difficulties in their operations, our financial results will be negatively impacted. Many of these companies have not yet generated significant revenues, have incurred losses and have invested heavily in research, development and marketing of their products. We anticipate that the majority of these companies will continue to record losses in the future.

Our results may be affected by volatility in the securities markets. Securities markets in general are volatile, and in particular, with respect to high-technology companies, including companies that have a significant presence in Israel. Although the volatility of these companies' securities has often been unrelated to their operating performance, these companies may experience difficulties in raising additional financing required to effectively operate and grow their businesses. These difficulties and the volatility of the securities markets in general may also affect our and our group companies' ability to realize investments, such as by selling holdings in these companies.

Our financial results are directly impacted by our ability to conclude profitable "exit" transactions. Our financial results are directly impacted by our ability to conclude profitable "exit" transactions regarding certain of the companies in our group. If worldwide market conditions in the technology industry do not permit us to conclude these types of transactions, our results will be adversely affected.

We may face difficulties in our ability to dispose of our shares in publicly traded companies in our group. Due to the limitations of U.S. securities laws, material non-public information to which we may become exposed due to our representation on the boards of directors of companies in our group, and contractual and legal limits on the tradability of the shares, we may face difficulties in our ability to dispose of our shares in publicly traded companies in our group at a time and in a manner we deem suitable.

Our market value significantly depends on the market values of publicly-traded companies in our group. Our market value is directly impacted by the market values of Given Imaging, Partner and NetVision Ltd., or NetVision, each of whose shares are traded in the public markets. To the extent that the share prices of any of these companies decline, our market value will be negatively impacted. In particular, we are affected by the price of shares of Given Imaging, of which we beneficially own approximately 37% of the outstanding shares representing all shares owned by us, RDC and DIC (which we may be deemed to beneficially own as a result of the voting agreement between DIC and us), or approximately 20%, representing our direct holding and our share in the holding of RDC. If any of these companies experience difficulties in the future and their share prices decline, our market value could be adversely affected.

The market price of our ordinary shares is subject to fluctuations. The market value of our ordinary shares has fluctuated over time. The following factors may significantly impact the market price of our ordinary shares:

- the market price of our group companies which are publicly traded, in particular, Given Imaging;
- our group companies, their competitors or other third parties announcing technological innovations, new products or earnings or losses;
- periodic variations in results of operations of our group companies;
- factors that generally affect the market for stocks of medical device, telecommunications, semiconductor and advanced materials companies;
- political, economic or other developments affecting Israel;
- global economic and other external factors; and

- quarter-to-quarter fluctuations in our financial results.

Many of our group companies may face difficulties in obtaining future financing on favorable terms or at all. Many of our group companies have extensive research and development and marketing costs and limited revenues, if any. In order to succeed, these companies may require additional capital to fund these costs. If these companies have difficulties in obtaining financing from their current shareholders, which may also include additional investments by us in these companies, or from new financing sources, their continued operations may be at risk. This would adversely affect our financial performance and results of operations.

Bank of Israel regulations limit our and our group companies' ability to borrow from Israeli banks. Bank of Israel regulations stipulate lending limits of Israeli banks to companies and individuals considered to be in an affiliated group, which limits the amount available to such affiliated group to borrow from such banks. We and our group companies are part of the IDB affiliated group of companies, which is one of the largest group of affiliated companies in Israel. The IDB group includes many Israeli companies, which require, or which hold ownership interests in companies which require, extensive credit facilities from Israeli banks for the operation of their businesses. These regulations may result in difficulties for us and our group companies to obtain bank financing , if required

The downturn experienced by the technology markets in which our group companies operate may re-occur. Our group companies are affected by the demand for the technologies and technology products they develop and produce. The technology sector generally has previously experienced a prolonged and severe downturn, reflected in a steep decline in technology spending resulting in revenue declines for our more mature companies and difficulties in raising financing for our early stage companies. Although this downturn shows signs of reversal, there is no assurance the technology sector will continue to grow. If the downturn re-occurs, our and our group companies' operations will be adversely affected.

We compete with other entities for acquisition and investment opportunities. As part of our overall strategy, we pursue acquisitions of, and investments in, Israeli companies and Israel-related technology companies. The success of a number of Israeli companies, particularly information technology, communication and medical device companies, has prompted potential investors to seek investment opportunities in Israel allowing many Israeli high-technology companies to gain direct access to Israeli and foreign public securities markets. We compete for acquisition and investment opportunities with other established and well-capitalized entities. There can be no assurance that we will be able to locate acquisition or investment opportunities upon favorable terms. Our failure to consummate further acquisitions or investments in the future may hinder our ability to grow and could harm our business, financial condition and results of operations.

There is no assurance that our subsidiary, RDC, will identify existing technology, or that Rafael Armaments Development Authority Ltd,. or Rafael, will develop new technologies that can be commercially exploited in non-military markets. Our wholly-owned subsidiary, DEP holds approximately 50.1% of the outstanding shares and voting rights of RDC established by DEP together with Rafael Armaments Development Authority Ltd., or Rafael. RDC has first rights to exploit commercially, technologies of Rafael for the development of products for use in non-military markets, which rights are dependent primarily upon RDC’s or Rafael’s identification of existing technologies for commercial uses, or the development by Rafael of new technologies, Rafael's willingness to transfer the necessary human resources to develop and exploit commercially its technology in non-military markets, and RDC reaching agreement on the terms of any commercial exploitation. If Rafael or RDC do not identify existing technology, or Rafael does not develop new technology, that can be commercially exploited in non-military markets, or if Rafael does not transfer the necessary human resources to develop and exploit commercially this technology in non-military markets, or if RDC does not reach agreement on the terms of any commercial exploitation, then we will not realize the full potential value of the agreement with Rafael, which could harm our ability to continue to grow and develop RDC which, in turn, could harm our business, financial condition and results of operations.

Most of our group companies are dependent upon proprietary technology which may be infringed upon or may infringe upon the proprietary technology of others. Most of our group companies greatly depend on their proprietary technology for their success. Like other technology companies, most of these companies rely on a combination of patent, trade secret, copyright and trademark laws, together with non-disclosure agreements, confidentiality clauses in their agreements, including employment agreements, and technical measures to establish and protect proprietary rights in their products. These companies may not be able to enforce their proprietary rights under the laws of certain jurisdictions. Our group companies may not successfully protect their technology because:

- some foreign countries may not protect their proprietary rights as fully as do the laws of the United States;
- enforcing their rights may be time consuming and costly, diverting management's attention and company resources;
- measures such as entering into non-disclosure agreements afford only limited protection;
- unauthorized parties may attempt to copy aspects of their products and develop similar software or to obtain and use information that they regard as proprietary; and
- competitors may independently develop products that are substantially equivalent or superior to their products or circumvent intellectual property rights.

In addition, others may assert infringement claims against our group companies. The cost of responding to infringement claims could be significant, regardless of whether the claims are valid.

Many of our group companies experience intense competition. Many of our group companies experience competition from companies with significantly greater financial, technical, marketing and public relations resources, who have easier market access, better operational infrastructure, longer operating histories, larger installed client bases, greater name recognition, more established relationships and alliances in their industries and offer a broader range of products and services. As a result, these competitors may be able to respond more quickly to new or emerging technologies or changes in clients' requirements, benefit from greater purchasing economies, offer more aggressive product and services pricing or devote greater resources to the promotion of their products and services. If our group companies are unable to successfully compete, their businesses, financial condition and results of operations could be seriously harmed, which would in turn negatively affect our financial condition and results of operations.

Our group companies may experience delays in product development. Companies in our group involved in technology product development may experience delays in development which may result in loss of, or delay in, market acceptance. Delays and difficulties associated with new product introductions or product enhancements could negatively impact the business, financial condition, prospects and results of operations of these companies and, as a result, our financial results.

Israeli government programs in which certain of our group companies participate, may be terminated or reduced in the future. In addition, the terms of such programs restrict the ability of our group companies to manufacture products and/or transfer technologies outside of Israel. Certain of our group companies participate in programs of the Israeli Chief Scientist's Office and the Israel Investment Center, for which they receive grants and tax related and other benefits. The benefits available under these programs depend on our group companies meeting specified conditions. If our group companies fail to comply with these conditions, they may be required to pay additional taxes and penalties and be denied future benefits. We cannot assure you that these benefits will be available in the future at their current levels or at all.

In June 2005, certain amendments to these restrictions came into effect permitting, subject to the consent of the Israeli Chief Scientist in most circumstances:

(i) the transfer of manufacturing activities to third parties outside Israel in exchange for the import of manufacturing activities to Israel,
(ii) the transfer of technologies to third parties outside Israel in exchange for a portion of the consideration from the sale of such technologies, knowhow from such third parties or cooperation with such third parties in research and development, to the satisfaction of the Israeli Chief Scientist, and
(iii) the sale, merger or any similar transaction in a company subject to the payment to the Israeli Chief Scientist of a portion of the consideration paid.

The above mentioned restrictions may limit the ability of our group companies to conclude transactions with international companies, including "exit" transactions.

We and our group companies may have difficulty retaining key employees. Our success and the success of our group companies depend, in large part, on a limited number of key management, scientific and technical personnel. In addition, future success will depend upon, in part, attracting and retaining highly qualified personnel. There can be no assurance that we or our group companies will be able to either retain present personnel or acquire additional qualified personnel as and when needed. The loss of the services of our key personnel or those of our group companies and the failure to attract highly qualified personnel may have a negative impact on our business.

Many of our group companies depend on international operations. Many of our group companies depend on sales to customers outside Israel. We expect that international sales will continue to account for a significant portion of these companies' revenues for the foreseeable future. As a result, changes in international, political, economic or geographic events could result in significant shortfalls in orders or revenues. These shortfalls could cause the business, financial condition and results of operations of these companies to be harmed. Some of the risks of doing business internationally include:

- unexpected changes in regulatory requirements;
- the inability of our group companies, their subsidiaries and subcontractors to obtain export licenses;
- imposition of tariffs and other barriers and restrictions;
- burdens of complying with a variety of foreign laws;
- political and economic instability;
- changes in diplomatic and trade relationships; and
- acts of terror.

Some of these factors, such as the ability to obtain export licenses and changes in diplomatic relations, may be affected by Israel's overall political situation. See "Conditions in Israel may affect our operations and the operations of our group companies." In addition, the economic and political stability of the countries of the major customers and suppliers of our group companies may also impact their business.

Conditions in Israel may affect our operations and the operations of our group companies. We and most of our group companies conduct our principal operations in Israel, and therefore are directly affected by the political, economic, and military conditions affecting Israel and the Middle East. In particular, we could be adversely affected by:

- any major hostilities involving Israel;
- a full or partial mobilization of the reserve forces of the Israeli army;
- the interruption or curtailment of trade between Israel and its present trading partners;
- a significant increase in inflation;
- a significant downturn in the economic or financial condition of Israel;
- a significant downgrading of Israel's international credit rating; and
- labor disputes and strike actions.

Since September 2000, there has been a significant increase in violence, civil unrest and hostility, including armed clashes, between the State of Israel and the Palestinians, and acts of terror have been committed inside Israel and against Israeli targets in the West Bank and Gaza including armed hostilities between Israel, the Palestinian Authority and other groups in the West Bank and Gaza Strip. Any further escalation in these hostilities or any future armed conflict, political instability or violence in the region could have a negative effect on our and our group companies' business condition, harm our and our group companies' results of operations and adversely affect our share price or the share prices of our group companies that are publicly traded.

Our and our group companies' operations could be disrupted as a result of the obligation of key personnel in Israel to perform military service. All non-exempt male adult permanent residents of Israel under a specified age, as a general rule, are obligated to perform military reserve duty and may be called to active duty under emergency circumstances. Our operations and those of our group companies could be disrupted by the absence for a significant period of one or more of our or our group companies' officers or employees. While we and our group companies have operated effectively despite these conditions in the past, we cannot assess what impact these conditions may have in the future, particularly if emergency circumstances arise.

The results of operations of our group companies may be harmed by foreign currency exchange rate fluctuations. To the extent that our group companies are based in Israel and have international operations, or operate only in Israel but conduct their business in different currencies, their revenues, expenses, assets and liabilities, are not necessarily in the same currency and therefore they are exposed to foreign exchange rate fluctuations. These fluctuations may negatively affect their results of operations. Some of our group companies may attempt to hedge their foreign currency exposure from time to time; however, we cannot assure you that they will be successful.

Our group companies may not be able to enforce covenants not to compete. Some of our group companies currently have non-competition agreements with substantial numbers of their employees who are involved in research and development. In many cases, these employees are located primarily in Israel. These agreements prohibit the company's employees, if they cease working for the company, from directly competing with the company or working for its 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 any of our group companies cannot demonstrate that harm would be caused to it, the company may be unable to prevent its competitors from benefiting from the expertise of its former employees.

Product liability claims could adversely affect the business results of our group companies operating in the medical device industry. Product liability is an inherent risk for our group companies operating in the medical device industry. A product liability claim, regardless of its merit or eventual outcome, could result in substantial costs to a group company and a substantial diversion of management attention. A product liability claim or any product recalls could also harm a group company's reputation and result in a decline in revenues. Substantial damages awards have been made in some jurisdictions against medical device companies based upon claims for injuries allegedly caused by the use of their products. There can be no assurance that a future product liability claim or series of claims brought against our group companies would not have an adverse effect on their business or the results of operations, or that product liability insurance would be adequate.

Product regulation may adversely affect the ability of our medical device group companies to bring new products to market or to continue to supply existing products to the market. Our medical device group companies are subject to strict government controls on the development, manufacture, labeling, distribution and marketing of products. They must obtain and maintain regulatory approval for their products from regulatory agencies before products may be sold in a particular jurisdiction. Each regulatory authority may impose its own requirements and delay or refuse to grant approval, even though a product has been approved in another country. Regulatory delays, the inability to successfully complete clinical trials, claims and concerns about safety and efficacy, new discoveries, patents and products of competitors and related patent disputes and claims about adverse side effects are only a few of the factors that could adversely affect the realization of product registration. Noncompliance with applicable regulatory requirements can result in enforcement action which may include recalling products, ceasing product marketing, paying significant fines and penalties, and similar regulatory actions which could limit product sales, delay or halt product shipment, delay new product clearance or approval, and adversely affect such group companies' results of operations.

Because the medical device industry is litigious, our medical device group companies are susceptible to intellectual property suits that could cause our group companies to incur substantial costs or pay substantial damages or prohibit them from selling their products. There is a substantial amount of litigation over patent and other intellectual property rights in the medical device industry. Whether a product infringes a patent involves complex legal and factual issues, the determination of which is often uncertain. Infringement and other intellectual property claims, with or without merit, can be expensive and time-consuming to litigate and can divert management's attention from the company's core business.

If our medical device group companies are unable to obtain reimbursement coverage from third-party healthcare payors for procedures using their products, or if reimbursement is insufficient to cover the costs of purchasing their products, demand for their products may be adversely affected. If physicians, hospitals and other healthcare providers are unable to obtain sufficient coverage and reimbursement from third-party payors for products produced by our medial device group companies, or if reimbursement is insufficient to cover the costs of purchasing our medical device group companies' products or does not adequately compensate physicians and health care providers compared to alternative procedures, our medical device group companies may be unable to generate sufficient sales to support their businesses. In addition, our medical device group companies could be adversely affected by changes in reimbursement policies of governmental or private healthcare payors to the extent any such changes affect reimbursement amounts or methods for procedures in which their products are used.

Our telecommunications group companies operate in a highly regulated telecommunications market which limits their flexibility to manage their businesses. The telecommunications market is subject to government regulation regarding licensing, competition, frequency allocation and costs and arrangements pertaining to interconnection and leased lines. The business and operations of our group companies which operate in this market, primarily Partner and NetVision, could be adversely affected by changes in laws, regulations or government policy affecting its business activities. These could include decisions by the regulator increasing the rate of royalties to be paid to the State of Israel, enlarging the types of revenues which the royalties apply to, setting policies and imposing new regulations governing electronic trade and mobile commerce, or further reducing call or Short Message Service, or SMS, termination tariffs, as well as the amendment or revocation of their licenses.

Certain of our telecommunications group companies can only operate their businesses for as long as they have a license from the Ministry of Communications. Partner and NetVision conduct their respective operations pursuant to their respective licenses granted to each of them by the Ministry of Communications. These licenses are subject to revocation in accordance with their terms, and the terms of the licenses are subject to change by the Ministry of Communications (including by imposing additional requirements).

The semiconductor industry in which certain of our group companies operate is cyclical in nature and is characterized by ongoing changes. The semiconductor industry has historically been a highly cyclical industry. Companies in the semiconductor industry have expanded aggressively during periods of increased demand. This expansion has frequently resulted in overcapacity and excess inventories during periods of downturn, thereby adversely impacting upon the results of operations of our group companies operating in the semiconductor field.

In addition, the semiconductor industry is characterized by rapid ongoing changes, including: (1) changes in customers' capacity requirements and capital spending, which depend in part on customers' inventory levels relative to demand for their products; (2) the importance of driving down cost of ownership of systems; (3) more complex technology requirements; (4) the increasing significance of consumer electronics as a driver for chip demand and the related focus on lower prices; (5) varying levels of business information technology spending; (6) the growing types and varieties of integrated circuits and applications; (7) an increasing number of applications across multiple substrate sizes in the semiconductor industry, resulting in divergent interests among semiconductor manufacturers; (8) a rising percentage of business from customers in Asia and emergence of customers and competitors in new geographical regions; (9) customer demands for shorter lead times for the manufacture and installation of semiconductor manufacturing equipment; and (10) higher capital requirements for new semiconductor fabrication plants. If our semiconductor companies do not successfully manage the risks resulting from the ongoing changes occurring in the semiconductor industry, their businesses, financial condition and results of operation could be materially and adversely affected.

Specific Risks Affecting Elron

We may be deemed to be an investment company under the Investment Company Act of 1940. Generally, a company must register under the Investment Company Act of 1940, or the 1940 Act, and comply with significant restrictions on operations and transactions with affiliates if its investment securities exceed 40% of the company's total assets, or if it holds itself out as being primarily engaged in the business of investing, owning or holding securities. The 1940 Act provides for various exemptions from the obligation to register thereunder, and in 1980 we received an order from the Securities and Exchange Commission, or SEC, declaring that we are not an investment company under the 1940 Act. If certain of our investments were to adversely affect our status under the 1940 Act, we might need to dispose of or acquire other investments to avoid the requirement to register as an investment company on terms that may not be favourable to us. In addition, if we were deemed to be an investment company and therefore required to register as such under the 1940 Act, we would be unable to continue operating as we currently do, as a result of which our market value would be severely harmed.

If we are characterized as a passive foreign investment company for U.S. federal income tax purposes, our U.S. shareholders may suffer adverse tax consequences. Generally, if for any taxable year 75% or more of our gross income is passive income, or at least 50% of our assets are held for the production of, or produce, passive income, we may be characterized as a passive foreign investment company for U.S. federal income tax purposes.

If we are characterized as a passive foreign investment company, or PFIC, our U.S. shareholders may suffer adverse tax consequences, including having gains realized on the sale of our shares taxed at ordinary income rates, rather than the capital gain rate. In addition, both gains upon disposition and amounts received as distributions could be subject to an additional interest charge by the Internal Revenue Service. A determination that we are a passive foreign investment company could also have an adverse effect on the price and marketability of our shares.

Concurrently with the announcement of the sale of our shares in Elbit Systems Ltd. in July 2004 (See Item 5, "Sale of Our Holdings in Elbit Systems"), we announced that, as a result of the transaction, we may be characterized as a passive foreign investment company for U.S. federal income tax purposes for 2004. At the time we filed our Form 6-K with the SEC regarding this matter, however, we believed, and our tax advisors concurred, that for 2004 we could potentially rely on the "change of business" exception to PFIC status provided under Section 1298(b)(3) of the U.S. Internal Revenue Code of 1986, as amended. Pursuant to this exception, in order to avoid PFIC status in 2004, among other requirements, we cannot be a PFIC in 2005 or 2006 (which cannot be determined at this time) or in any year prior to 2004 (which we believe was not the case). The tests for determining PFIC status are impacted by among other factors, changes in our holdings and in the value of our group companies, which are difficult to predict. Moreover, the sale of our shares in Partner in 2005 (See Item 5, "Sale of Partner Shares"), generated significant passive income. As a result, we believe that it is reasonably possible that we will be treated as a PFIC in 2005 and, as a result, in 2004 as well. The ultimate determination of our PFIC status for 2005 will depend on the composition of our gross income and assets for the entire year, the values of those assets, which are difficult to predict at this time and the appropriate value of our ownership interest in our group companies. Therefore, it is unclear whether the "change of business" exception would ultimately be satisfied for 2004. We cannot assure you that the Internal Revenue Service will not challenge our reliance on the "change of business" exception or our assumptions used in determining our percentage of passive assets and income. If there were such challenges, we could be classified as a passive foreign investment company for 2004, even if we are not a PFIC in 2005 or 2006. Furthermore, there can be no assurance that we will not become a passive foreign investment company in the future. (See "Item 10. Additional Information – Taxation – Federal Income Tax Considerations - Tax Consequences if we are a Passive Foreign Investment Company".)

U.S. holders of our shares are urged to consult their tax advisors regarding the application of the passive foreign investment company rules.

One of our shareholders beneficially owns a substantial amount of our ordinary shares and may therefore influence our affairs. As of June 28, 2005, Discount Investment Corporation Ltd., or DIC, beneficially owned an aggregate of approximately 47.5% of our ordinary shares and has the ability, in effect, to elect the members of our board of directors and to significantly influence our business. A majority of the members of our board of directors are officers or directors of DIC or its parent company, IDB Development Corporation Ltd., or IDBD, or its parent company, IDB Holding Corporation Ltd., or IDBH.

It may be difficult to serve process or to enforce a U.S. judgment against us, our directors and our officers. Since all of our directors and officers reside outside the United States, it may be difficult to effect service of process on us, our directors or officers within the United States. Furthermore, because most of our assets are located outside the United States, it may not be possible to enforce any judgment obtained in the United States against us or the aforementioned individuals in the United States. There is doubt as to the enforceability of civil liabilities under the U.S. Securities Act of 1933 and U.S. Securities Exchange Act of 1934 in original actions instituted in Israel.

Risks Affecting Our Holdings in Given Imaging

The following risk factor sections have been condensed for the purposes of this Annual Report. The risks associated with Given Imaging are more fully described in documents filed by Given Imaging with the SEC.

Given Imaging's quarterly financial performance is likely to vary in the future. Based on Given Imaging's experience to date, it believes that many of its customers delay purchasing systems until the end of the fiscal quarter because they believe this will enable them to negotiate a more favorable price. Therefore, revenues from system sales may be concentrated at the end of each fiscal quarter making it difficult for Given Imaging to determine the success of each quarter until its end and resulting in lower than expected quarterly revenues if external or other events cause a large number of potential customers to defer their purchasing decisions even for a short period of time. Furthermore, Given Imaging believes that demand for systems and capsules may be affected by seasonal factors during the summer months when physicians and administrators are more likely to postpone purchasing decisions relating to systems due to summer vacations and patients are more likely to postpone non-essential diagnostic procedures until later in the year. Both of these factors may result in fluctuations in Given Imaging's quarterly operating results.

Future sales of Given Imaging's ordinary shares in the public market and low trading volume could adversely affect its share price. As of May 31, 2005, Given Imaging had approximately 27,818,411 million ordinary shares outstanding. Approximately 50% of these shares are available for resale subject, however, to volume limitations under Rule 144. Future sales of these shares, or the perception that these sales could occur, could adversely affect the market price of Given Imaging's ordinary shares. In addition, all of Given Imaging's ordinary shares are available for resale on the Tel Aviv Stock Exchange, subject to compliance with Regulation S under the U.S. Securities Act of 1933. Future sales of these restricted shares, or the perception that these sales could occur, could adversely affect the market price of Given Imaging's ordinary shares. Given Imaging has periodically experienced a low trading volume of its ordinary shares, and if one or a small number of parties buys or sells a large number of its ordinary shares, Given Imaging may experience volatility in its share price and its share price may be adversely affected. Share price fluctuations may be affected by changes in trading practices in Given Imaging's ordinary shares, such as short selling and hedging transactions, which occurs periodically.

Given Imaging may be unable to maintain or increase its profitability. Given Imaging was formed in 1998 and recorded initial sales of the Given System in the third quarter of 2001. Given Imaging achieved positive cash flow in the fourth quarter of 2003 and became profitable in the second quarter of 2004; however, Given Imaging has significant operating expenses and must continue increasing its revenues from sales of the Given System and of the PillCam capsules at a higher rate than the increase in its expenses in order to maintain and grow its profits. If Given Imaging fails to do so, it may be unable to maintain or increase its profitability.

If Given Imaging is unable to achieve broader penetration of the Given System among gastroenterologists, it may not be able to maintain its current growth rate. Given Imaging's principal product is the Given System, consisting of the PillCam capsule and the related data recorder and computer workstation. In 2004, Given Imaging sold 654 Given Systems and approximately 90,400 PillCam Small Bowel or PillCam SB capsules compared to 631 Given Systems and approximately 51,400 PillCam SB capsules in 2003. At the end of November 2004, Given Imaging began marketing its new PillCam ESO capsule for visualising the esophagus following receipt of marketing clearance from the U.S. Food and Drug Administration, or FDA. As of December 31, 2004, Given Imaging had sold approximately 2,290 systems and 172,000 PillCam SB capsules. If Given Imaging is unable to increase reimbursement coverage, expand the indications for which reimbursement is granted and convince more physicians to adopt the Given System, future penetration of the Given System among gastroenterologists may not be sufficient to maintain Given Imaging's current growth rate.

Given Imaging's future growth depends in part on its ability to market the Given System and the PillCam SB capsule for a variety of disorders of the small intestine. The Given System and the the PillCam SB capsule have been cleared by the FDA for the detection of abnormalities of the small intestine. However, in order to achieve sustained long-term growth, Given Imaging must successfully market the Given System for detection of a variety of disorders of the small intestine with high prevalence. Use of the Given System is highly dependent on the availability of third party reimbursement. Initially, most reimbursement policies issued for the Given System in the United States by third party payors covered its use only for detection of suspected bleeding in the small intestine, which represents a small part of the total population with suspected disorders of the small intestine. Currently, however, most reimbursement policies cover other prevalent indications in the small intestine, such as suspected Crohn's disease. Given Imaging's ability to expand the use of the Given System to other disorders of the small intestine depends substantially on its ability to demonstrate to additional governmental and private third-party payors the diagnostic and cost-effectiveness of the Given System for other disorders of the small intestine.

Given Imaging's future growth also depends in part on the success of Ethicon Endo-Surgery in marketing its new PillCam ESO video capsule, particularly in the United States. In May 2004, Given Imaging entered into an exclusive sales representation and co-promotion agreement with Ethicon Endo-Surgery, a Johnson & Johnson company. InScope, a division of Ethicon Endo-Surgery established to market products to the gastroenterology market, has exclusive rights to market our PillCam ESO capsule in the United States. Given Imaging depends on the success of InScope in marketing the PillCam ESO capsule and obtaining reimbursement coverage for this capsule. If InScope is not successful, sales of the PillCam ESO capsule may be lower than expected and Given Imaging's revenues may suffer.

Given Imaging currently depends on the Given System and the PillCam SB and its new PillCam ESO capsules for substantially all of its revenues. Sales of the Given System and its PillCam SB capsule for visualization of the small intestine currently account for substantially all of Given Imaging's revenues. In addition, in the third quarter of 2004, Given Imaging launched its new PillCam ESO video capsule in Europe and in the fourth quarter of 2004, Given Imaging launched this new capsule in the United States. If Given Imaging is unable to manufacture, market or sell the Given System or the PillCam SB and PillCam ESO video capsules, its financial condition and results of operations would be materially adversely affected.

Given Imaging may be unable to introduce other products for use in other parts of the gastrointestinal tract. Given Imaging's objective is to expand the use of the Given System by developing and introducing new capsules for visualizing other parts of the gastrointestinal tract, including the stomach and the colon. There can be no assurance of widespread market acceptance of the Given System as superior to existing technologies for detection of abnormalities in other parts of the gastrointestinal tract or that Given Imaging will succeed in marketing and selling capsules for use in other parts of the gastrointestinal tract. In addition, Given Imaging will be required to obtain FDA clearance in the United States and other regulatory approvals outside of the United States before commercially distributing the Given System for use in other parts of the gastrointestinal tract or introducing new products for use in the gastrointestinal tract. If future clinical trials indicate that the Given System is not as clinically or cost-effective in these parts of the gastrointestinal tract as current methods, or that it causes unexpected complications or other unforeseen negative effects, Give Imaging may not obtain regulatory clearance to market and sell the Given System for use in other parts of the gastrointestinal tract or obtain reimbursement coverage, and its growth would be adversely affected.

Any disruption in the United States market, the primary market for Given Imaging's products, may result in a material reduction in Given Imaging's revenues and negatively affect its results of operations.

Since Given Imaging began selling the Given System in 2001, most of its revenues have been generated from sales in the United States. Sales in the United States accounted for 15.6 million, or 54%, of its revenues in 2002, 26.2 million, or 65%, of its revenues in 2003 and 46.7 million, or 72%, of its revenues in 2004. Any disruption to Given Imaging's market in the United States resulting from adverse changes in reimbursement policies, regulatory requirements, macro-economic changes and other events, many of which are outside Given Imaging's control, may result in a material reduction in its revenues and negatively affect its results of operations.

Given Imaging has experienced rapid growth and its failure to manage this growth could harm its business. Given Imaging’s revenues have grown rapidly, and it faces significant challenges and risks in building and managing its sales and marketing team, including managing geographically dispersed sales efforts and adequately training its sales people in the use and benefits of the Given System and managing its growth by implementing effective planning.

Given Imaging relies on local distributors to market and distribute its products. With the exception of Australia, France, Germany, Israel and the United States, Given Imaging relies on distributors for the marketing and distribution of the Given System. Given Imaging’s success in generating sales in countries or regions where it has engaged local distributors depends in part on the efforts of others whom it does not control. If a distributor is terminated by Given Imaging or goes out of business, Given Imaging’s ability to sell the Given System in that distributor’s country or region could be adversely affected.

Given Imaging’s reliance on sole source suppliers could harm its ability to meet demand for the Given System in a timely manner or within budget. Given Imaging depends on sole source suppliers for some of the components necessary for the production of the Given System. Specifically, Micron Technology, Inc., through its Micron Imaging Group and other wholly-owned subsidiaries, is currently the sole supplier of the imaging sensor and the packaging for the sensor, and Zarlink Semiconductors is currently the sole supplier of the transmitter that is integrated into the PillCam capsules. If the supply of these components is disrupted or terminated, or if these suppliers are unable to supply the quantities of components that Given Imaging requires, it may not be able to find alternative sources for these key components. If Given Imaging is required to change the manufacturer of any of these key components of the Given System, there may be a significant delay in locating and/or verifying a suitable alternative manufacturer. Furthermore, in the event that the manufacturer of a key component of Given Imaging's product ceases operations or otherwise ceases to do business with Given Imaging, Given Imaging may not have access to the information necessary to enable another supplier to manufacture the component.

Risks Affecting Our Holdings in Oncura

Oncura may face integration risks. Oncura was formed as the result of the merger in July 2003 between the urology business of Galil Medical and the brachytherapy urology business of Amersham, plc, (NYSE, LSE, OSE: AHM), a subsidiary of General Electric Company (NYSE: GE) conducted through Mediphysics, or MPI, a wholly owned subsidiary of Amersham. Galil Medical and MPI hold 25% and 75% respectively of Oncura. At the time of its formation and through the present, Oncura has placed significant reliance on its shareholders and their affiliates for the provision of certain manufacturing, customer service, research and development and other administrative services. Although Oncura has long-term services agreements with its shareholders, it is in the process of creating its own management and information systems infrastructure to perform these services internally. Failure to successfully establish, integrate and manage these services internally could have a material adverse effect on Oncura's business, financial condition and results of operations and on our results of operations.

Oncura expects to derive a significant portion of its future revenues from its cryotherapy products, which could fail to achieve broad market acceptance or generate significant revenue growth. Oncura expects that revenues from its cryotherapy products will grow significantly over time. Accordingly, Oncura's success is in large part dependent on acceptance by physicians and patients of its cryotherapy products. Although cryotherapy has existed for many years, it has not been widely accepted due to a variety of factors including concerns over the safety and efficacy of the technology and the availability of alternative therapies. If Oncura's cryotherapy products do not achieve broad market acceptance, Oncura may not be able to achieve the revenue growth necessary to achieve and maintain profitability.

Oncura is dependent on its two shareholders, MPI and Galil Medical, to manufacture a majority of its products and the loss of either of these suppliers could harm its business. Oncura depends primarily on MPI and Galil Medical for manufacturing its products. Although Oncura has long-term supply agreements with each of MPI and Galil Medical, its business could be seriously harmed if it were unable to maintain these relationships or if MPI or Galil Medical were unable to continue to manufacture the company's products.

Oncura relies on affiliates of General Electric to market and distribute its products in certain markets. Oncura is currently heavily dependent on affiliates of General Electric to distribute its products in many of its markets outside North America. Oncura is in the process of establishing its own independent distribution network in most of its major markets. However, it may take time in certain markets to establish necessary legal entities and to obtain trading and regulatory licenses required to independently distribute its products. Although Oncura has long-term distribution agreements with General Electric, its business could be adversely affected if it were unable to maintain these relationships or if General Electric was unable to continue to distribute Oncura's products.

Oncura may incur future losses and be unable to achieve long-term profitability. Oncura was formed in 2003 and has generated net losses from the commencement of its operations in July 2003 through December 31, 2004. Oncura has significant operating expenses and anticipates that its operating expenses will continue to increase as it expands its sales, marketing and distribution capabilities and increases its research and development activities.

Oncura is reliant on its shareholders to fund working capital deficits. Oncura's operations from inception through December 31, 2004 have not generated positive cash flows and its corresponding working capital deficits have been financed by loans from its shareholders. If Oncura is not able to secure a suitable third-party credit facility to fund its working capital deficits, the company will continue to need to rely on its shareholders to provide necessary financing until such time as the company becomes cash flow positive or can obtain necessary financing from a third-party.

Risks Affecting Our Holdings in Partner

The following risk factor sections have been condensed for the purposes of this Annual Report. The risks associated with Partner are more fully described in documents filed by Partner with the SEC.

We are restricted in our ability to freely dispose of our holdings in Partner. Almost all of our shares in Partner are subject to transfer restrictions stipulated by Partner's license which requires that at least 5% of the economic and voting interest of Partner be owned by Israeli citizens and residents ("Minimum Israeli Percentage"). Pursuant to the relationship agreement between the founding shareholders of Partner, each Israeli party to the relationship agreement, including us, has undertaken to maintain such portion of the shares as is necessary to maintain the Minimum Israeli Percentage. These restrictions limit our ability to freely dispose of our shares in Partner.

Partner expects its subscriber growth rate, and consequently its revenue growth rate, to slow because Israel's mobile telephone services market is highly penetrated, making it more difficult to obtain new subscribers than in the past. Because the Israeli market for mobile telephones is highly penetrated, future demand for Partner's services will not grow at the same rate as it has in the past, and Partner's subscriber growth will not develop at the same rate as in the past and will depend significantly on Partner's ability to retain existing subscribers in its network and to attract subscribers from the other mobile telephone network operators. While Partner's market share, based on internal estimates, has increased from approximately 13% of Israeli mobile subscribers at December 31, 1999 to approximately 32% at December 31, 2004, Partner's market share growth has slowed since 2003 and Partner expects this trend to continue.

Competition from existing competitors may require Partner to increase its subscriber acquisition costs and customer retention costs and increase its churn rate. Partner competes primarily with Cellcom and Pelephone, two of the other mobile telephone network operators in Israel. Because of the ease of switching between cellular operators, Partner has already faced and may continue to face an increase in its churn rate and may be forced to increase its customer retention costs, including subsidies towards upgrades of subscribers' handsets, in order to retain subscribers.

Partner also competes with Bezeq, which is the only incumbent public fixed-line operator in Israel. In addition, a company jointly owned by the three cable companies in Israel recently received a fixed-line telephone service license. Partner may also face competition from additional fixed-line operators, if additional fixed-line licenses are granted. If any of Partner's existing competitors is granted a fixed-line telephone service license or acquires or cooperates with a fixed-line operator, Partner may be at a competitive disadvantage relative to those operators who may be able to offer combined packages of fixed-line, mobile telephone and other telecommunication services. The Ministry of Communications may also choose to grant additional mobile telephone operator licenses, which may further intensify competition in the mobile market in Israel. Furthermore, competition may limit Partner's ability in the future to increase tariffs or cause Partner to reduce tariffs.

Risk Affecting Our Holdings in NetVision

The market for the supply of Internet access services and value added services in Israel is very competitive. The supply of Internet access services requires a special license from the Israeli Ministry of Communications whose policy is to encourage competition and therefore does not place any material barriers to entry into the market. Since the beginning of 2004, competition in the market has focused on broadband Internet services. NetVision continues to experience increased competition in gaining broadband communication market share, mainly from companies such as Internet Gold (Nasdaq:IGLD), Bezeq International, Barak I.T.C. (1995) Ltd., or Barak, and 012 Golden Lines Ltd., or Golden Lines. As of December 31, 2004, NetVision estimates that it held approximately 25% of the broadband Internet communication market in Israel. Competition from existing and new competitors may require NetVision to reduce its tariffs and increase its subscriber acquisition and retention costs as a result of which NetVision's results of operations could be adversely impacted. Due to the intense competition, there has been a slow down in the increase of NetVision's subscriber base.

The market for the supply of international telephone services in Israel is very competitive The market for international telephony services, which NetVision entered in November 2004, is very competitive. The three major competitors are Bezek International, Golden Lines and Barak. Such competition may result in a decrease in prices to a level which will make penetration for NetVision more difficult, decrease NetVision's profits or even result in losses for NetVision, from these activities. In such event, NetVision's investment in its international telephone activities will be negatively impacted which in turn will negatively affect NetVision's results of operations.

NetVision relies on certain third-parties for leased lines. NetVision relies on certain third-party service providers including local and long distance telecommunications companies, such as Bezeq and Med Nautilus, for leased lines. Internet access by NetVision's customers is dependent on the telecommunications infrastructure owned and maintained by Bezeq and the local cable companies. If NetVision's subscribers' access to Israel's fixed-line telecommunications infrastructure is disrupted, it would significantly impact the services that NetVision provides to its subscribers and could result in a substantial reduction in Internet access volume and revenue. Furthermore an increase in the cost of access to Israel's fixed-line telecommunications infrastructure could also adversely impact NetVision's results of operations.

Item 4. Information on the Company

A. History and Development of the Company

We are a high technology operational holding company that operates through our group companies in two reportable segments, namely: (i) the systems and projects segment, through Elron TeleSoft Ltd. and Elron Telesoft Export Ltd., together Elron Telesoft,; and (ii) other holdings and our corporate operations, which includes our holdings in our group companies, engaged in various fields of advanced technology, and our corporate operations, which provide strategic and operational support to our group companies. Our group companies include both publicly traded and privately held companies.

Founded in 1962, we have been a major force in the development of the Israeli high technology industry by building Israeli and Israel-related companies with technologies in the fields of medical devices, advanced defense electronics, telecommunications, semiconductors, software products and services and advanced materials. Historically, most of our group companies were established together with entrepreneurs or started as activities within Elron and were subsequently spun-off. In addition, some of our group companies grew out of our subsidiary, RDC, established by us (through our subsidiary, DEP) together with Rafael, the largest research and development organization of Israel’s Ministry of Defense,pursuant to an agreement entered into in July 1993 for the purposes of exploiting Rafael’s technology in non-military markets. RDC has first rights to exploit commercially technologies of Rafael in non-military markets, which rights are dependent primarily upon RDC’s identification of new and existing military technology developed by Rafael, for commercial exploitation in non-military markets. Potential projects and opportunities are identified through mutual cooperation and ongoing liaison between RDC and their professional advisors and members of Rafael's research and development team. Following the identification of a project, RDC commercially exploits the project, initially using its own finance and management resources and thereafter obtains external financing. Given Imaging and Galil Medical are examples of companies that grew out from this cooperation with Rafael.

We expect to continue to build and realize value for our shareholders through the sale of a portion or all of our holdings in, or the issuance of shares by any of our group companies to third parties, while simultaneously pursuing the acquisition of, or investment in, new and existing companies at different stages of development including early stage and more mature companies, and building our group companies. We believe that this strategy provides the ability to increase shareholder value as well as capital to support the growth of our group companies.

Our activities range from complete operational control over the business of our group companies to involvement in the management of our group companies in which we maintain controlling or significant holdings, and, in a limited number of cases, minority holdings. We participate in the management of most of our group companies by means of active membership on their boards of directors and board committees. As a result, we are involved in matters of policy, strategic planning, marketing, selecting and manning senior management positions, approving investments and budgets, financing and the overall ongoing monitoring of our group companies' performance. In addition to our representation on the boards of directors of our group companies, we provide hands-on assistance to the group companies' management in support of their growth. We view our hands-on involvement in the operations of our group companies as a key element of our business. Our group companies therefore benefit from the experience of our management team in various areas in which they need support and leadership, including, but not limited to, market analysis, risk management, identifying joint venture opportunities, introductions to potential customers and investors, business plan preparation, budgetary control and strategic planning and research and development guidance.

Both our legal name and our commercial name is Elron Electronic Industries Ltd. We were incorporated in Israel in 1962 under the name of Elron Electronic Industries Ltd. The principal legislation under which we operate is the Israeli Companies Law, 1999. Our shares are publicly traded on Nasdaq National Market under the symbol "ELRN" and on the Tel Aviv Stock Exchange. Elron's corporate headquarters and registered office is located at 3 Azrieli Center, 42nd Floor, Tel-Aviv 67023, Israel, Tel. 972-3-607-5555, Fax. 972-3-607-5556, e-mail: elron@elron.net. Our web site address is www.elron.com. Information contained on our web site is not part of this Annual Report.

The following are significant transactions and events which we and our group companies have completed or which took place since January 1, 2004, in chronological order:

- **Purchase of shares of 3DV Systems Ltd.**

  On February 1, 2004, we and our subsidiary, RDC purchased approximately 47% of the outstanding share capital of 3DV Systems Ltd., or 3DV, in which we and RDC previously together held 48%, from the majority of the other shareholders of 3DV in consideration for an option, which has since expired, to receive up to 40% of the share capital of a new company to be established. Following the transaction, we and RDC together hold 95% of 3DV.

- **Sale of KIT eLearning Ltd.**

  In March 2004, KIT eLearning Ltd., or KIT, a provider of online academic programs, in which we held a 45% ownership interest, was sold to Online Higher Education, a subsidiary of Laureate Education, Inc., or Laureate (Nasdaq: LAUR) (formerly known as Sylvan Learning Systems, Inc.), a global leader in higher education, for an immediate cash payment of $9.4 million and a future payment of up to an additional $10.0 million based on earnings of KIT in 2006 and 2007 (of which our share will be up to $5.7 million). The other selling shareholders of KIT were our largest shareholder, DIC and Kidum IT Ltd., a privately held Israeli company. From the $9.4 million immediate proceeds of the sale, we received an amount of approximately $5.7 million and we recorded a gain of approximately $5.3 million.

- **Investment in ChipX Corporation**

  In March 2004, ChipX Corporation, or ChipX, a manufacturer of late-stage programmable application-specific integrated circuits raised $12.0 million in a private placement, in which we invested approximately $2.6 million. Following the investment, our holding in ChipX decreased from approximately 33% to approximately 27%.

- **Given Imaging secondary offering**

  On June 23, 2004, Given Imaging completed its secondary public offering of 2,880,750 ordinary shares at $32.00 per share, of which 1,500,000 shares were sold by Given Imaging and 1,380,750 shares were sold by selling shareholders, including 300,000 shares sold by our subsidiary, RDC. Given Imaging received net proceeds from the offering of approximately $44.3 million. We also hold a direct interest in Given Imaging, but did not participate in the offering.

  As a result of the sale of Given Imaging's shares by RDC and the decrease in our direct and indirect interest (through our holdings in RDC) in Given Imaging to approximately 15%, we recorded a gain in 2004, net of tax and minority interest, of approximately $6.7 million.

- **Additional investment in A.M.T Advanced Metal Technologies Ltd.**

  On June 30, 2004, we invested $3 million in A.M.T. Advanced Metal Technologies Ltd. or AMT, as part of an aggregate round of financing of $6 million in which an international strategic partner participated. In addition, AMT shareholders, including us, converted shareholder loans in the aggregate amount of approximately $2.7 million of which we converted approximately $1.6 million. As a result of the transaction, we increased our ownership interest from approximately 28% to approximately 35% on a fully diluted basis.

- **Sale of all of our holdings in Elbit Systems Ltd.**

  On July 28, 2004, we sold all of our holdings in Elbit Systems Ltd., or Elbit Systems, (Nasdaq: ESLT), constituting approximately 19.6% of the outstanding share capital of Elbit Systems, to the Federmann group, following the exercise of its right of first refusal, for approximately $196.6 million. As a result, we recorded in 2004 a gain, net of tax, of approximately $91.5 million.

- **Purchase of additional shares of Given Imaging**

  In August and November 2004, we purchased an additional aggregate amount of approximately 1.4 million shares of Given Imaging in various transactions for an aggregate amount of approximately $44 million. As a result of these purchases, our direct and indirect ownership interest in Given Imaging (through our holdings in RDC) increased from approximately 15% to approximately 20% and our beneficial ownership to approximately 25%.

- **Tender offer to purchase 7.5% of our shares**

  On August 22, 2004 we announced that DIC completed a tender offer to purchase 2,203,425 of our ordinary shares for $15 per share, net to the seller in cash, less any required withholding taxes and without interest. Following consummation of the tender offer, DIC owned approximately 46% of our outstanding shares.

- **Investment of $3 million in Starling Advanced Communications Ltd.**

  On October 21, 2004, we completed an investment of $3 million in preferred shares of Starling Ltd., or Starling, of which $1.5 million was invested immediately and an additional $1.5 million was invested in April, 2005. Following the investment, our direct interest in Starling is approximately 33% and our beneficial ownership (directly and through RDC) is approximately 66%.

- **Investment of $6.7 million in Jordan Valley Semiconductor Ltd.**

  On October 21, 2004, we invested approximately $6.7 million in Jordan Valley Semiconductor Ltd., or Jordan Valley, for preferred shares constituting 25% of Jordan Valley on a fully diluted basis, as part of an aggregate amount of approximately $9 million raised by Jordan Valley. Our holding is subject to adjustment based upon Jordan Valley's performance for the period July 1, 2004 until June 30, 2005. Should our shareholding fall below 25% as a result of the adjustment, we have an option to make an additional investment on the same terms as the original investment so as to enable us to hold 25% after the adjustment. The balance of the aggregate investment in Jordan Valley was invested indirectly by Clal Industries and Investments Ltd., or Clal, by way of conversion of previously granted loans. Jordan Valley is an Israeli private company engaged in developing solutions for advanced in-line thin film metrology for the semiconductor industry. Jordan Valley is 40% owned (indirectly) by Clal, a subsidiary of IDBD, which owns, as of May 31, 2005, approximately 67% of DIC. Clal, IDBD and DIC are publicly traded on the Tel Aviv Stock Exchange. Our investment in Jordan Valley was approved (in accordance with Israeli law) by the shareholders of Elron and Clal on October 21, 2004.

- **Investment of $7.3 million in Impliant, Inc.**

  On December 28, 2004, we invested approximately $7.3 million in consideration for preferred shares of Impliant, Inc., or Impliant, constituting approximately 20% of, Impliant on a fully diluted basis, as part of a financing round of approximately $18 million from new and existing investors of Impliant. Impliant is a privately held medical device company, engaged in the development of a novel posterior motion preservation system for spine surgery.

- **Investment in Semiconductor Engineering Laboratories Ltd.**

  On March 27, 2005, we invested approximately $0.5 million and RDC invested $0.8 million in preferred shares of Semiconductor Engineering Laboratories Ltd., or SELA, in an aggregate round of financing of approximately $1.4 million. Following the investment, our direct interest in SELA is approximately 12% and our beneficial ownership (directly and through RDC) is approximately 66%.

- **Sale of Partner shares**

  On April 20, 2005 we completed the sale to Partner of 12,765,190 Partner shares for approximately $94 million, as part of the sale together with the other Israeli founding shareholders of Partner of an aggregate of approximately 33.3 million Partner shares to Partner for aggregate consideration of approximately $245 million.

  As a result of the sale, we will record in the second quarter of 2005 an estimated gain, after tax, of approximately $35 million. Our beneficial holding in Partner after the sale is approximately 2%. Our shares in Partner are no longer pledged to the banks providing financing to Partner but almost all of our holding is still subject to certain transfer restrictions under Partner's Israeli communications license.

- **Investment of $2.9 million in NuLens Ltd.**

  On April 21, 2005, we invested approximately $1.7 million in prefered shares of NuLens Ltd., or NuLens, an Israeli medical devices company operating in the field of intra-ocular lenses mainly for cataract and presbyopia procedures, for approximately 17% of NuLens on a fully diluted basis and agreed to invest an additional amount of approximately $1.2 million subject to the achievement of a certain milestone. Our investment in NuLens was part of an aggregate round of financing of $3.4 million. Following our additional investment if the milestone is achieved, we will hold approximately 25% of NuLens, on a fully diluted basis.

- **Investment of $16 million in Teledata Networks Ltd.**

  On May 8, 2005, we completed an investment of $16 million in Teledata Networks Ltd., or Teledata, in consideration for preferred shares constituting approximately 21% of Teledata, on a fully diluted basis. The investment is part of an aggregate round of financing of $19 million, in which FBR Infinity II Ventures, a related venture capital fund, or Infinity, invested $3 million, for approximately 4% of Teledata, on a fully diluted basis and with whom we entered into a voting agreement. (See Item 7b-"Related Party Transactions"). Teledata provides innovative access products and solutions for both traditional and next generation networks to telecom operators and service providers.

- **Sale of holdings in Oren Semiconductor**

  On May 10, 2005, Zoran Corporation, or Zoran (NASDAQ: ZRAN), acquired Oren Semiconductor, Inc., or Oren, in which we held a 41% interest. From the proceeds of the acquisition, Elron received cash of approximately $12.5 million (of which approximately $2 million is held in escrow under the terms of the agreement) and Zoran shares with an estimated value of approximately $7.5 million based on Zoran's share price on the completion date of the acquisition. As a result of the transaction, we will record an estimated gain in the second quarter of 2005, net of taxes, of approximately $16 million.

- **NetVision Initial Public Offering**

  On May 19, 2005, NetVision completed its initial public offering on the Tel Aviv Stock Exchange, or TASE in Israel for the sale of shares and convertible securities in consideration for aggregate immediate net proceeds of approximately NIS135 million (approximately $31 million). In addition, future proceeds from the exercise of options to be sold in the proposed offering may amount to approximately NIS28.8 million (approximately $6.6 million). DIC, which also holds approximately 47% of our shares, is the other major shareholder of NetVision. We and DIC each converted approximately $3.1 million of loans into equity of NetVision immediately prior to the offering and $2.2 million in loans was repaid to each of us from the proceeds of the offering. As a result of the initial public offering our holding in NetVision decreased from 45.7% to approximately 39% (27.4% on a fully diluted basis taking into account the possible exercise of the convertible securities) resulting in an estimated gain for Elron to be recorded in the second quarter of 2005 of approximately $3 million.

The following are the significant investments and divestitures which we and companies in our group completed in 2002 and 2003, in chronological order:

- **Sale of the Government Activity of Elron TeleSoft to Elbit Systems**

  In January 2002, Elron TeleSoft completed the sale of its net assets and activities in the government field to Elbit Systems for approximately $5.7 million, with no material effect on our consolidated results of operations.

- **Merger with Elbit**

  On May 15, 2002, we completed our merger with Elbit. , in which we previously held 44% of the outstanding shares. Pursuant to the Agreement and Plan of Merger signed on October 31, 2001, Elbit merged with us and we issued to Elbit’s shareholders (other than us) 5,617,601 of our shares, based on an exchange ratio of 0.45 of one of our ordinary shares for each ordinary share of Elbit. The value of our ordinary shares issued, then amounted to approximately $70.2 million.

- **DEP Share Purchase**

  On May 6, 2002, we completed the share purchase of DIC's shares in DEP, a technology holding company in which we previously held 33% of the outstanding share capital. Pursuant to the share purchase agreement signed on November 19, 2001 with DIC, we issued 2,261,843 ordinary shares to DIC in exchange for all of the shares held by DIC in DEP, representing 67% of the outstanding share capital of DEP, and DIC's rights to loans provided by DIC to RDC. The aggregate value of our ordinary shares issued then amounted to approximately $29.5 million.

- **Acquisition of controlling interest in Galil Medical**

  During 2002, we and RDC converted notes of Galil Medical, in the amount of approximately $3.2 million which were granted during November and December of 2001, into preferred shares.

  In addition, we and RDC together invested in convertible notes of Galil Medical an amount of approximately $3.7 million and $5.7 million in 2002 and 2003, respectively.

  On June 27, 2002, we purchased an additional 10.75% of Galil Medical's outstanding shares from Lumenis Ltd., in consideration for $0.8 million. In the same transaction, DIC also purchased an additional 10.75% of Galil Medical's outstanding shares from Lumenis under the same terms and conditions.

  Folllowing these transactions, our ownership interest increased to approximately 15% directly and approximately 37% indirectly through RDC, as of June 27, 2002, thereby giving us directly and indirectly, through RDC, a controlling voting interest in Galil Medical.

- **Investment in AMT**

  In August 2002, we completed a new investment of approximately $5.0 million in convertible notes of AMT for approximately 28% of AMT on a fully diluted and as converted basis. The investment formed part of an aggregate investment in AMT of approximately $8.7 million, of which the existing shareholders of AMT invested $3.7 million. The convertible notes are convertible into preferred shares of AMT or its group companies.

- **Sale of Elbit VFlash**

  On September 23, 2002, Elbit VFlash Ltd., or Elbit VFlash, a wholly-owned subsidiary of Elbit, sold a significant portion of its assets to 24/7 Real Media Inc., or 24/7 (Nasdaq: TFSM), in exchange for 4,100,000 shares of common stock of 24/7. 24/7 provides marketing and technology solutions to online marketers and publishers. Of the 4,100,000 shares of common stock of 24/7 it received, Elbit VFlash undertook to grant a beneficial interest in approximately 725,000 shares of common stock to former employees in recognition of services they rendered to Elbit VFlash prior to the sale. Concurrently with the above sale, we invested $1.0 million in consideration for 100,000 convertible preferred shares of 24/7 which were subsequently converted into 4,840,271 shares of common stock of 24/7. As a result of this transaction, we recorded a gain, net of tax, of approximately $2.0 million.

As of December 31, 2003, we sold all of our shares of 24/7 for approximately $5.2 million resulting in an additional gain of approximately $0.8 million.

In December 2004, Elbit VFlash was voluntarily dissolved.

- **Sale of 380,000 Shares of Elbit Systems**

In the fourth quarter of 2002, we sold 380,000 shares of Elbit Systems for approximately $5.9 million. As a result, we recorded a gain, before tax, of approximately $1.8 million.

- **Investment in Notal Vision, Inc.**

In January 2003, we completed an investment of $2.0 million in Notal Vision, Inc. , or Notal, an Israeli related medical device company operating in the field of early detection of Age Related Macular Deterioration (AMD) for an approximately 24% ownership interest. Our investment formed part of an aggregate investment by other investors in Notal of approximately $4.5 million, including an investment by an existing shareholder, Innomed Ventures (Israel) L.P., or Innomed, in which we also hold an interest.

- **Galil Medical and Amersham Health Plc merge urology therapy units**

On July 1, 2003, the merger between the urology business of our subsidiary, Galil Medical, and the brachytherapy business of Amersham plc, now a subsidiary of General Electric Company, was completed. According to the merger agreement, a new company, Oncura, was incorporated. Oncura provides minimally invasive treatment options for prostate cancer using brachytherapy (radio-active seeds) and cryotherapy (hyper-cooling) technologies. At the closing, Amersham, through its subsidiary, MPI, and Galil Medical each contributed the related operations and assets necessary for Oncura to conduct the brachytherapy business and the cryotherapy business, respectively, in the urology field, and in exchange for such assets, MPI received 78% and Galil Medical received 22%, of the outstanding shares of Oncura. In addition, at the closing, Galil Medical purchased 3% of Oncura from MPI in consideration for $4.5 million in cash, which was paid in full as of April 26, 2004, resulting in Galil Medical's aggregate ownership interest of 25% of Oncura. In addition, Galil Medical has an option to purchase an additional 3% of Oncura from MPI in consideration for $5.4 million, exercisable until 45 days following the closing of an initial public offering of Oncura. As a result of the transaction, a gain in the amount of $21.2 million was recorded in 2003. Our share in this gain (net of minority interest and income taxes) amounted to $4.4 million.

- **Sale of Shares of Given Imaging by RDC**

  In 2003, RDC sold, in a series of transactions, 753,600 shares of Given Imaging for a total consideration of approximately $7.8 million, resulting in a gain of approximately $4.4 million ($0.1 million net of tax and minority interest).

- **Purchase of Shares of Given Imaging from RDC**

  In May 2003, a Share Purchase Agreement was signed between RDC, Elron and Rafael, according to which RDC sold two million unregistered shares of Given Imaging, representing 7.9 % of Given Imaging's then outstanding shares, to Elron and Rafael (one million or 3.95% each) for total consideration of $12.2 million. RDC used $5.0 million of the proceeds to repay shareholders' loans to Rafael and Elron. This transaction did not have any effect on our consolidated results of operations.

- **Sale of approximately 6.3 million Shares of Partner**

  In the second and third quarters of 2003, we sold, in a series of transactions, an aggregate amount of approximately 6.3 million shares of Partner, representing approximately 3% of Partner's then outstanding shares, to Israeli institutional investors for approximately $29.3 million, as a result of which we recorded in 2003 an aggregate gain, net after tax, of approximately $7.1 million.

- **Investment in Oren**

  In July 2003, we invested $3.0 million in Oren as part of an aggregate investment of $8.0 million from existing shareholders and from Zoran. In addition to this investment, we and other existing shareholders converted all the loans previously granted to Oren, in the amount of approximately $8.4 million, of which our part was approximately $4.4 million. Following the investment and the loan conversion, our interest in Oren increased from 17% to approximately 41%.

- **Investment in Wavion, Inc.**

  During 2003, we invested $3.0 in Wavion, Inc., or Wavion, out of an aggregate amount of $12.5 million raised by Wavion in a private placement from us and new investors. In addition to this investment, we converted the loans previously advanced to Wavion in the aggregate amount of $1.5 million into Wavion preferred stock. As a result, our ownership interest in Wavion decreased from 45% to approximately 38%.

- **Sale of Elron SW, Inc. (formerly Elron Software, Inc)**

  On September 2, 2003, our subsidiary, Elron SW Inc., or ESW, sold substantially all of its assets and business to Zix Corporation, or Zix (Nasdaq: ZIXI) , a global provider of e-messaging protection and transaction services, in consideration for 1,709,402 shares of Zix's common stock, then with a market value of approximately $6.0 million and a 5.75% convertible note ("the Note") of $1.0 million. Of the 1,709,402 shares of Zix common stock, ESW granted a beneficial interest in approximately 85,000 common shares to certain of its former employees in recognition of services rendered to ESW. In addition, Zix assumed certain liabilities of ESW in the net amount of approximately $1.0 million. The transaction resulted in a gain of approximately $4.1

million. Simultaneously with the closing of the sale, we purchased the 1,709,402 shares of Zix common stock and the Note from ESW for approximately $6.2 million, based on the principal amount of the Note and the last closing sale price of Zix shares on the Nasdaq National Market prior to the closing.

As of December 31, 2004, we sold all our shares of Zix (including 262,454 shares resulting from the conversion of the Note) for approximately $17 million, and recognized an aggregate gain of approximately $10.2 million ($6.8 million net of tax).

In December 2004, ESW was voluntarily dissolved.

Business Overview

The business overview discussed below is presented in accordance with our two reportable segments, the systems and projects segment and other holdings and corporate operations.

The Systems and Projects Segment – Elron TeleSoft,

Elron TeleSoft focuses on the development and marketing of revenue assurance software products for the telecommunication market. Elron Telesoft also provides its network management system, call performance management product (CPM) and professional services as well as distributes Agilent Technology’s Signaling Systems number 7 (SS#7) based products in the local Israeli and international market.

Elron TeleSoft’s annual revenues amounted to $5.1 million in 2004 ($4.3 million in Israel and $0.8 million in the rest of the world); $7.4 million in 2003 ($5.7 million in Israel and $1.7 million in the rest of the world) and $10.1 million in 2002 ($8.0 million in Israel and $2.1 million in the rest of the world). Elron TeleSoft’s customers in the telecommunications service provider market consist of Israeli operators (Bezeq, Cellcom, Partner, Pelephone, Bezeq International, Barak and Mirs) and international operators either directly (such as MobilTel Bulgaria and Cyta Cyprus) or in cooperation with international system integrators (such as E-Plus Germany).

<u>Products</u>

Elron TeleSoft’s product portfolio focuses on its revenue assurance product line with its Revenue Assurance Process Control, or RAP, and the Switch-to-Bill reconciliation, or ESSB, products as described below:

<u>RAP – Revenue Assurance Process Control</u>

The RAP identifies revenue leaks in order to provide telecommunication companies with automatic and systematic tools in order to monitor its processes. Risk points are identified, monitored and managed and leaks are sealed. The RAP provides functionality and methodology to build, control and validate processes within both wireline and wireless operators.

ESSB - Switch-to-Bill Reconciliation Tool

The ESSB collects different formats of unbilled and incorrect data records from various sources such as switches, billing, mediation and signaling systems. ESSB compares the various sources with different multi-cycled keys, analyzes the discrepancies and fixes them by adding the relevant (missed or mistaken) information.

Competition

Elron TeleSoft faces competition from both Israeli and global system integrators and software vendors such as CVidya, ECtel and TTI Telecom in Israel and Azure (UK), Cape Technologies (Ireland), Visualwireless (Sweden), Wedo (Portugal), Vibrant (USA), Sotas (India) and other local in-country software houses and consulting competitors which operate in these fields.

Sales and Marketing

Elron TeleSoft's sales and marketing activities include the following steps:

- Early contacts and discussions with potential customers and partners directly or through indirect channels;
- Understanding the customer's needs and constructing the installation, customization and implementation plan;
- Solutions may incorporate the licensing of Elron TeleSoft's products, third party products, software development and system integration capabilities;
- Preparation of proposals and contract negotiations; and
- Case study publications.

Research and Development

Elron TeleSoft's research and development efforts are currently primarily directed toward revenue assurance products (RAP and ESSB), functionality enhancements and the development of new modules intended to broaden Elron TeleSoft's product portfolio in the Revenue Assurance field.

Maintenance and Support

Elron TeleSoft provides maintenance and support packages to its customers adjusted to the specific needs and requirements of each customer in accordance with Elron TeleSoft's standard terms and with the applicable terms of its suppliers/subcontractors. Such maintenance packages vary among customers and may include working hours coverage, 24 hours a day - seven days a week coverage, bug fixing, updates, upgrades, third party coverage including updates/upgrades and consultation.

Other Holdings and Corporate Operations

This segment includes holdings in other companies in our group and our corporate operations, which provides strategic and operational support to the group companies. Through our corporate operations, we are involved in our group companies regarding matters of policy, strategic planning, marketing, selecting and manning senior management positions, approving investments and budgets, financing and the overall ongoing monitoring of our group companies' performance. In addition to our representation on the boards of directors of our group companies, we provide hands-on assistance to the group companies' management in support of their growth.

Our group companies are engaged in four main fields of advanced technology, namely: (i) medical devices; (ii) telecommunication; (iii) semiconductors and (iv) advanced materials. The business overview of this reportable segment is presented, for the purposes of convenience only, according to the four main fields listed above, none of which is considered a separate reportable segment.

1. Medical Devices

Our activities in the field of medical devices consist mainly of our holdings in the following companies:

- Given Imaging, in which we beneficially own approximately 37% of the outstanding shares representing all shares owned by us, RDC and DIC (which we may be deemed to beneficially own as a result of the voting agreement between DIC and us), or approximately 20% representing our direct holding and our share in the holding of RDC;
- Galil Medical, in which we beneficially own approximately 59% of the outstanding shares representing all shares owned by us and RDC, or approximately 39%, representing our direct holding and our share in the holding of RDC;
- Oncura, in which we beneficially own approximately 25% of the outstanding shares representing shares owned by Galil Medical, or approximately 10%, representing our share in the holding of Galil Medical;
- Notal, in which we hold approximately 26% of the outstanding shares;
- Impliant, in which we hold approximately 28% of the outstanding shares; and
- Nulens, in which we hold approximately 22% of the outstanding shares.

Given Imaging

Given Imaging is an Israeli company that develops, manufactures and markets innovative diagnostic products for disorders of the gastrointestinal tract. It pioneered capsule endoscopy, a proprietary approach to visual examination of the gastrointestinal tract through the use of a miniaturized video camera contained in a disposable capsule.

Given Imaging was incorporated in Israel by our subsidiary, RDC, in January 1998. Its initial public offering and listing on the Nasdaq National Market occurred in October 2001. In March 2004, Given Imaging also listed its shares on the TASE. In June 2004, Given Imaging completed its secondary public offering raising $44.3 million.

Given Imaging's principal product, which incorporates its core technology, is the Given System, a proprietary wireless imaging system which uses disposable video capsules, referred to as the PillCam capsules. The PillCam video capsules are easily ingested by the patient and move naturally through the gastrointestinal tract without discomfort while wirelessly transmitting high quality color images and data to a portable recorder. Given Imaging believes that capsule endoscopy provides a patient-friendly solution that addresses a significant market opportunity and overcomes many of the shortcomings of traditional diagnostic tools for gastrointestinal disorders.

In 2001, Given Imaging commenced marketing the Given System, its capsule endoscopy platform, with the M2A capsule (which Given Imaging rebranded in 2004 as the PillCam Small Bowel capsule, or PillCam SB), for detection of disorders of the small bowel. As of December 31, 2004, Given Imaging had an installed base of approximately 2,290 Given Systems and had sold approximately 172,000 PillCam SB capsules in over 50 countries worldwide.

In November 2004, Given Imaging received FDA marketing clearance for its second PillCam capsule, the PillCam ESO capsule, for visualizing the esophagus. Given Imaging markets the PillCam ESO video capsule through a strategic marketing and sales alliance formed in May 2004 with InScope, a division of Ethicon Endo-Surgery, a Johnson & Johnson company.

Given Imaging has also developed the Patency Capsule and system, which is a dissolvable capsule that enables physicians to determine whether there are obstructions or strictures in the gastrointestinal tract. Given Imaging launched the Patency Capsule and system in Europe in November 2003 and is conducting clinical trials for the Patency Capsule and system in the United States and, if results are favorable, plans to pursue FDA clearance.

Given Imaging recorded revenues of $65.0 million in 2004, $40.5 million in 2003 and $28.9 million in 2002.

Given Imaging estimates that as of December 31, 2004, reimbursement for the Given System was available worldwide to approximately 327 million people, of which approximately 206 million are located in the United States. Prior to the beginning of 2003, all of the policies in the United States covered capsule endoscopy with PillCam SB capsules for suspected small intestinal bleeding. The number of policies covering other small bowel pathologies and indications has grown steadily since then and as of December 31, 2004 approximately 167 million people in the United States have expanded coverage for suspected Crohn's disease, suspected small bowel tumors and other small bowel pathologies. In Europe, reimbursement for capsule endoscopy was available for approximately 102 million people as of December 31, 2004 compared to approximately 40 million people at the end of 2003, and the number of people with the right to reimbursement for expanded indications, such as Crohn's disease and other small bowel disorders grew from 24 million at the end of 2003 to 87 million at the end of 2004.

Given Imaging currently markets and sells the Given System through a combination of direct sales through its subsidiaries, and through independent distributors in over 50 jurisdictions. Currently, Given Imaging markets the Given System directly in Australia, France, Germany**,** the United States and Israel through approximately 80 sales and marketing personnel employed by Given Imaging and its subsidiaries in those jurisdictions. In the United States, which accounted for 65% of Given Imaging's revenues in 2003 and 72% of its revenues in 2004**,** Given Imaging markets its products through its wholly-owned subsidiary, Given Imaging, Inc. As of December 31, 2004**,** Given Imaging had a direct sales force in the United States of approximately 45 personnel.

Sales to Given Imaging's local distributors worldwide accounted for approximately 15% of its revenues in 2004. Under the terms of Given Imaging's distribution agreements, Given Imaging generally grants to one distributor in each particular country or region the right to market the Given System for an initial period of approximately three years. During this period, the distributor is required to meet minimum sales targets set out in each distribution agreement. Given Imaging may, in its sole discretion, upon prior written notice, terminate a distribution agreement with a distributor in the event that a distributor fails to meet its minimum sales targets.

The Given System consists of Pillcam capsules, a portable data recorder and sensor array, and a dedicated computer workstation. Given Imaging manufactures the PillCam capsules at its facilities in Yoqneam, Israel using three semi-automated production lines. Given Imaging purchased its first production line from Pemstar, Inc., a U.S. electronics manufacturing service and equipment company, and it became operational in 2002. Given Imaging installed ~~a~~ two additional semi-automated production lines, which became operational in the second half of 2003 and the second half of 2004, respectively. Two of these production lines are used to manufacture the PillCam SB capsule and one to manufacture the PillCam ESO capsule. Each semi-automatic production line in Yoqneam, Israel facility has a capacity to manufacture approximately 180,000 PillCam capsules per year. As of December 31, 2004, Given Imaging had manufactured and sold approximately 172,000 PillCam SB capsules and approximately 3,400 PillCam ESO capsules, substantially all of which were produced on these semi-automated production lines. Given Imaging has also installed at Pemstar's facilities in Ireland, a semi-automated production line of the PillCam SB capsule for backup purposes. Each of these backup production lines has a capacity to manufacture an additional 180,000 PillCam capsules per year**.** Current production capacity is sufficient to support sales in the foreseeable future.

In June 2002, Given Imaging also entered into a one year non-exclusive technical services agreement with Pemstar, pursuant to which Pemstar is providing Given Imaging with technical services relating to the manufacture of the PillCam capsules on the single semi-automated production line purchased from Pemstar in 2001. In June 2004, Given Imaging extended this agreement until December 31, 2005 and thereafter has an option to extend the agreement for two additional terms of two years each.

The portable data recorders are manufactured externally and assembled and tested at Given Imaging's facilities. The sensor arrays are manufactured and assembled externally and are tested at Given Imaging's facilities. The computer workstation is an off-the-shelf computer workstation pre-loaded with Given Imaging's RAPID softwareGiven Imaging's research and development activities are conducted internally by its research and development staff, primarily at its facilities in Yoqneam, Israel.

Given Imaging's research and development efforts are focused primarily on developing improvements to its existing products and developing new capsules to be used in the detection of abnormalities in other areas of the gastrointestinal tract. For example, Given Imaging has recently announced progress in the development of the PillCam(TM) COLON, designed as an ingestible video capsule for screening the colon, leveraging on the RAPID platform. Given Imaging plans to submit the product for clearance by FDA and launch it in Europe in 2006.

Given Imaging basic issued patents in the United States and Israel are on an in vivo video camera system. Given Imaging acquired the rights to these issued U.S. and Israeli patents in January 1998 under a technology purchase and license agreement with Rafael. These issued patents in the United States and Israel expire in January 2014 and January 2015, respectively. Given Imaging holds 15 additional issued patents in Australia, France, South Korea, Israel and the United States covering different elements of its technology and expiring between July 2014 and August 2022. As of December 31, 2004, Given Imaging had 285 patent applications worldwide based on 157 priority applications relating to various elements and functions of its product and enhancements.

In August 2001, Given Imaging received clearance from the FDA to market the Given System in the United States for adjunctive use in the detection of abnormalities of the small intestine. In 2003, the FDA approved the removal of the adjunctive labeling, with the result that the Given System can now be marketed in the United States as a standalone tool for the detection of abnormalities of the small intestine. In 2003, Given Imaging received two further clearances from the FDA, first for a suspected blood indicator, a new feature of the Given System which automatically marks images that contain the color red and which therefore correlate with the existence of suspected bleeding, and, second, for use of the PillCam capsule in children aged 10 through 18. In November 2004, Given Imaging received FDA marketing clearance for its PillCam ESO video capsule and for the advanced RAPID software and data recorder. Any new medical device that Given Imaging wishes to commercially distribute in the United States will likely require either 510(k) clearance or premarket application approval from the FDA prior to commercial distribution. 510(k) clearance or amendment to premarket application is also required when a change is made to a legally marketed device or to expand the product label.

Galil Medical

Galil Medical , an Israeli company established by RDC in 1997, is a provider of minimally invasive temperature based therapies for the treatment of benign and malignant diseases. Since 1999, Galil was focused on developing products to address specific urologic diseases including prostate and kidney cancer. In July 2003, Galil Medical completed the merger of its urology related cryotherapy business with Amersham Health's brachytherapy business, which created Oncura. Galil Medical holds 25% of Oncura. (see below, "Oncura"). In addition to its urology activities for Oncura, Galil Medical is now focusing on developing minimally invasive cryotherapy solutions for woman's health conditions such as uterine fibroids and breast fibroadenoma.

Galil Medical has entered into supply and R&D services agreements with Oncura, pursuant to which Galil Medical provides Oncura with certain exclusive supply, manufacturing and R&D services in the urology field, upon a cost plus basis.

Galil Medical’s research and development and manufacturing facilities are based in Yoqneam, Israel.

Galil Medical’s intellectual property consists of intellectual property, which was received from Rafael, and intellectual property developed by Galil Medical’s research and development team. Galil Medical has 13 patents and 22 new pending applications.

As of December 31, 2004, Galil Medical had over 380 SeedNet™ machines installed worldwide. Galil Medical recorded annual revenues of $7.6 million in 2004, $7.6 million in 2003 and $5.0 million in 2002. Revenues for the years 2002 and the first half 2003 represented sales to the end user customer, while the majority of the revenues for the second half of 2003 and for the year 2004 represented sales to Oncura.

Oncura

Oncura, a Delaware corporation, markets and sells therapeutic device systems and related consumables used primarily in the performance of minimally-invasive, urologic cancer treatment. Oncura's products include implantable radioactive seeds and cryotherapy devices and related disposable kits used in the treatment of prostate and other urologic cancers.

Oncura’s formation was the result of a merger, completed July 1, 2003, between the urology business of Galil Medical, and the brachytherapy business of Amersham plc, now a subsidiary of General Electric Company conducted through its subsidiary, MPI, as a result of which Galil Medical and MPI acquired 78% and 22% of the issued and outstanding shares of Oncura, respectively. Galil Medical purchased an additional 3% of Oncura from MPI for $4.5 million, resulting in Galil Medical's owning an aggregate interest of 25% in Oncura. In addition, Galil Medical has an option to purchase an additional 3% of Oncura from MPI for $5.4 million, exercisable until 45 days following the closing of an initial public offering of Oncura.

Oncura is headquartered in Plymouth Meeting, Pennsylvania, a suburb of Philadelphia. In addition, Oncura has an international management office located in Amersham, United Kingdom.

Oncura does not manufacture any of the products it sells. A majority of Oncura’s products are manufactured by its two shareholders, MPI and Galil, and sold to Oncura under long-term supply agreements. Oncura also purchases certain products, principally a type of radioactive seed not manufactured by MPI, from a third-party supplier.

Oncura markets and distributes its products directly and indirectly to numerous international markets, including, the United States, Canada, Europe, Russia, Israel, Greece, Korea, Philippines, Hong Kong, Australia, New Zealand, and portions of South America. In the United States, Oncura sells principally through its direct sales force. Outside of the United

States, Oncura sells through its direct sales force along with a network of affiliated and independent distributors and agents. In several markets outside the United States Oncura's products are distributed under long-term distribution agreements with affiliates of General Electric.

Oncura has also entered into services and research and developments agreements with its shareholders and affiliates for the provision of certain administrative and research and development services.

Oncura terminated a majority of its existing service arrangements and certain of its distributor arrangements with its shareholders in 2004. Oncura expects to terminate most of the remaining services and distributor arrangements with its shareholders in 2005. Upon termination, the services currently provided by shareholders under these agreements will be performed by Oncura or will be provided by third-party vendors.

Oncura's intellectual property consists primarily of product brand names and product patented technology that it either owns or is licensed to Oncura by MPI and Galil Medical under exclusive licensing agreements.

As of April 30, 2005, Oncura has approximately 120 employees.

Oncura's activities in the marketing and distribution of cancer therapy products are subject to extensive laws, regulations, regulatory approvals and guidelines. Within the United States, the Company's products must comply with the U.S. Federal Food Drug and Cosmetic Act, which is enforced by the FDA. Oncura must also comply with the regulations of the Competent Authorities of the European Union for any products sold in the member nations of the European Union. Oncura is also subject to various other regulations, regulatory approvals and guidelines in other markets in which it distributes its products. Oncura is not presently licensed to handle radioactive materials. Oncura's radioactive seeds are manufactured by MPI and third-party vendors and physical handling and delivery of all radioactive seeds to customers, including those manufactured by third parties, is the exclusive responsibility of MPI.

Oncura's revenues were approximately $68.8 million in 2004 and approximately $31.4 million for the period from commencement of operations in July 1, 2003 through December 31, 2003.

Notal

Notal is a medical device company founded in 2000, operating mainly in the field of early detection of Age Related Macular Degeneration (AMD). AMD is a common eye disease that gradually destroys central visual function, manifested in two forms: dry AMD, a mild form of the disease, and wet AMD, a progression of dry AMD, which often leads to rapid, severe visual deterioration and blindness. To address the growing need for early detection of wet AMD and for the continuous monitoring of patients with dry AMD, Notal Vision has developed the patented Preferential Hyperacuity Perimetry (PHP), designed to detect and monitor the progression of the disease in a non-invasive manner. Notal has launched, together with Carl Zeiss Meditec, or Zeiss, the Preview PHP device, intended for professional use by ophthalmologists and optometrists in their clinics. The current diagnostic device enables early detection of wet AMD among the at-risk population, those already diagnosed with the dry form of the disease. Future versions may also target for screening purposes the full population at risk (e.g., anyone over the age of 55) who may be unaware that they may have dry AMD, as well as patients already treated for wet AMD for post-treatment follow-up. Post treatment follow-up is intended to identify the recurrence of the disease and confirm the stage of the disease. Sales of the Preview PHP device to end-users started in the third quarter of 2004.

Based on the PHP technology, Notal is also developing the “Home Device,” a monitoring device intended for home use. The monitoring device will enable patients with dry AMD to monitor themselves at home on a more frequent basis, ensuring timely intervention by a physician should the disease progress to the wet form. In May 2005, Notal appointed TLC Vision Corporation, or TLC, as it exclusive distributor for the sale and distribution of the "Home Device" in North America. TLC also signed an investment agreement with Notal, pursuant to which TLC committed to invest $4.25 million in Notal (of which $1 million has already been invested) subject to achievement of milestones, primarily for the purpose of funding the development of the Home Device.

Notal commenced sales in 2003 and recorded $0.9 million in revenues in 2003, and $1.0 million in 2004. Notal’s ability to generate significant revenues will depend largely on it obtaining and maintaining applicable regulatory approvals for its products, reimbursement of its products by healthcare payors and the success of its strategic alliances with Zeiss and TLC.

Innomed, 14% held by us, is also a shareholder of Notal (see below, "Other Holdings in Medical Devices".)

Impliant

Impliant is a developer of posterior motion preservation spine implants. The company’s TOPS™ System—Total Posterior Spine™ System, is a mobile spine implant that addresses the major degenerative spine diseases of the posterior spinal column. The TOPS™ System supports a range of motion, including axial rotation, lateral bending, flexion and extension. Impliant recently began clinical trials on the device.

Impliant holds the rights to a unique family of polycarbonate urethane materials to develop cushion-bearing spine implants. Impliant believes that this family of materials has successfully passed biocompatibility tests consistent with FDA requirements, and is already utilized in other approved long-term implants.

Impliant has 20 employees. Impliant's headquarters are located in Milford, Connecticut, with research and development activities taking place in Ramat Poleg, Israel. Impliant has 10 patent applications..

Impliant will need to comply with the U.S. Federal Food Drug and Cosmetic Act, which is enforced by the FDA. Impliant must also comply with the regulations of the competent authorities of the European Union for any products sold in the member nations of the European Union.

Innomed, 14% held by us, is also a shareholder of Impliant (see below, "Other Holdings in Medical Devices").

NuLens

NuLens , established in September 2002, operates in the field of intra-ocular lenses or IOL mainly for cataract and presbyopia. NuLens is focused on exploiting the novel technologies in its patents and developing a real accommodative IOL ("RA-IOL") with the capacity of providing over 10 Diopters in real accommodative power to the cataract and presbyopia markets. NuLens is currently in the process of pre-clinical trials.

NuLens' has two patents and six pending patent applications.

Within the United States, NuLens will need to comply with the U.S. Federal Food Drug and Cosmetic Act, which is enforced by the FDA. NuLens must also comply with the regulations of the competent authorities of the European Union for any products sold in the member nations of the European Union.

NuLens' offices are located in Herzliya, Israel and Alicante, Spain. NuLens has eight employees.

Other Holdings in Medical Devices

Our other holding in the medical devices field is in Innomed, which is a seed stage fund that initiates and invests in Israeli and Israeli related companies in the field of medical devices and life sciences. We hold, through our subsidiary DEP, approximately 14% of the partnership interest in Innomed. Innomed is a member of the Jerusalem Global Ventures Group of venture capital funds.

3. Communications

Our activities in the field of communications consist of our holdings in the following main companies:

- Partner, in which we hold approximately 2% of the outstanding shares;
- NetVision, in which we hold approximately 39% of the outstanding shares;
- Teledata, in which we hold approximately 21% of the outstanding shares and Infinity, a related venture capital fund, holds approximately 4% of the outstanding shares;
- Wavion, in which we hold approximately 38% of the outstanding shares;
- Starling, in which we beneficially own approximately 66% of the outstanding shares representing all shares owned by us and RDC, or approximately 50%, representing our direct holding and our share in the holding of RDC;

- Pulsicom Israel Technologies Ltd., or Pulsicom, in which we hold approximately 18% of the outstanding shares; and
- CellAct Ltd., or CellAct, in which we hold approximately 45% of the outstanding shares.

Partner

Partner is a publicly traded, Israel-based company. Its shares are traded on the Tel Aviv Stock Exchange under the symbol "PTNR". American Depositary Shares, or ADSs, each representing one of the Company's ordinary shares are quoted on the Nasdaq National Market under the symbol "PTNR" and are traded on the London Stock Exchange under the symbol "PCCD". Partner was the first Global System for Mobile Communications, or GSM, mobile telephone network operator in Israel and is one of four cellular service providers in Israel.

On April 20, 2005, we completed the sale to Partner of 12,765,190 Partner shares for approximately $94 million, as part of the sale together with the other Israeli founding shareholders of Partner of an aggregate of approximately 33.3 million Partner shares to Partner for an aggregate consideration of approximately $245 million. As a result of the sale, we will record, in the second quarter of 2005, an estimated gain, after tax, of approximately $35 million. Our remaining shares, constituting approximately 2% of Partner's outstanding shares, are no longer pledged to the banks providing financing to Partner. However, under Partner's Israeli communications license, the Israeli founding shareholders are required to maintain such amount of shares to ensure that at least 5% of Partner's shares are held by Israeli citizens and residents. In addition, the Israeli founding shareholders are required to appoint, generally, 10% of Partner's board of directors. On April 20, 2005, the Israeli founding shareholders, including us, entered into a Restated Relationship Agreement among themselves and Partner's controlling shareholder, Hutchison BV, and a shareholders agreement among themselves to regulate the above issues as between them. For a description of the material terms of these agreements, See Item 9C - "Material Contracts".

Partner's principal business is the provision of mobile telephone services in Israel. Partner currently operates in the 900 MHz and 1800 MHz bands. Its services include standard and enhanced GSM services, as well as value added services and products such as voice mail, voice messaging, color picture messaging, icon, ringtone and game downloads, information services, High Speed Circuit Switched Data or HSCSD, General Packet Radio Services, or GPRS, which enables the packet transfer of data in an "always on" mode at a speed of up to 20-30 Kbps, personal numbering and data and fax transmission services. Partner also offers its subscribers the ability to roam using their mobile phones outside Israel.

Partner's 3G network, which as of the end of 2004 covered approximately 60%, and as of April 2005 covered approximately 85%, of the Israeli population, offers a wide range of new services, such as video calls, a new portal of content services including a broad selection of video-based services under the "obox live" brand, and the transmission of data at speeds of up to 384 Kbps.

Partner distributes its services primarily through direct sales through Partner-owned sales centers and business sales representatives and indirect sales through traditional networks of specialist dealers and non-traditional networks of retail chains and stores, which account for a majority of Partner’s sales. Partner also offers 24-hour, seven days a week customer service, as well as handset repair and replacement services, to subscribers who acquire these services.

Partner is subject to extensive regulation related to the spectrum and its ability to operate mobile telephone service in Israel. The Israeli Ministry of Communications controls the granting of licenses to operate mobile telephone service in Israel. It has granted licenses to several companies to operate such mobile networks, and may grant additional licenses in the future. Additionally, Partner must erect antennae that carry its network transmissions in order to maintain the coverage of the Israeli population required in its license. The erection and operation of these antennae must comply with local, regional and national regulations.

Partner is also dependent on a number of licenses and agreements to operate its mobile telephone network, and Partner maintains contracts with a number of dealers through which its products are sold and has contracts with Nortel, Nokia and Ericsson to provide it with equipment to run its network. Such equipment is available only through a limited number of suppliers. Partner also leases most of its transmission capacity from Bezeq. Partner maintains agreements with mobile telephone network operators in foreign countries through which it provides its customers with international service.

As of December 31, 2004, Partner had approximately 2,340,000 subscribers, an increase of approximately 237,000 subscribers during 2004. According to its internal statistics, Partner believes that its market share rose to approximately 32% of the Israeli cellular market in 2004, from 31% in 2003.

Partner’s revenues were approximately NIS 5.14 billion ($1.19 billion) in 2004, NIS 4.47 billion ($1.04 billion) in 2003, and NIS 4.05 billion ($941 million) in 2002. The dollar amounts are based on the shekel-dollar representative rate of exchange on December 31, 2004 of NIS4.308 equal to $1.00.

NetVision

NetVision, based in Israel, is one of the largest Internet service and solutions providers in Israel, as well as a developer of Internet solutions. As of November 2004, NetVision also provides international telephone services. On May 19, 2005, NetVision completed its initial public offering on the Tel Aviv Stock Exchange in which it sold shares and convertible securities for the aggregate net consideration of NIS135 million (approximately $31 million). In addition, future proceeds from the exercise of options sold in the offering may amount to up to approximately NIS28.8 million (approximately $6.6 million).

NetVision’s total revenues were $70.5 million in 2004, $65.5 million in 2003 and $61.5 million in 2002 based on the shekel-dollar representative rate of exchange as of December 31, 2004 of NIS 4.308 equal to $1.00.

NetVision’s activities in the Internet area focus on providing Internet connectivity and related services and products, content and electronic commerce services and the establishment and supply of Internet-based applications. NetVision provides international telephone services, which are provided using Voice Over Internet Protocol (“VOIP”) technology, a technology that enables voice transmission over the Internet infrastructure.

According to NetVision's estimates, as of December 31, 2004, NetVision's share of the Internet connectivity market in Israel was approximately 25%, with 390,000 customers receiving Internet connectivity services from NetVision.

NetVision also provides various content and electronic commerce services. In July 1999, NetVision launched "Nana", a portal which provides a variety of content and e-commerce services, such as news and content, chat rooms, forums and blogs, search engines, Web site indexing for both local and international sites, shopping and advertising. "Nana"'s index and search applications can be operated in Hebrew.

NetVision has been involved in e-commerce activity since 1998, and currently operates through two sites, "Netaction" and "Nanasale", which enable e-commerce through various sale methods - auction, public sale and group purchases.

NetVision is dependent on the communication services provided by Bezeq which has a monopoly for domestic telecommunications in Israel. NetVision is also dependent on maintaining its operating license granted by the Israeli Ministry of Communications.

NetVision's headquarters are located in Haifa, Israel. As of April, 2005, NetVision has 1,284 employees.

Teledata

Teledata offers innovative access products and solutions for traditional and Next Generation Networks, or NGN, to telecom operators and service providers worldwide. The company's solutions allow operators to provide a wide variety of wireline services, including Voice, Data and Video (Triple Play) for business and residential subscribers. Teledata's products enable a smooth migration path from existing legacy networks to IP and softswitch based NGNs.

Teledata has two product lines:
BroadAccess™ - a carrier-class Integrated Multiservice Access Platform (IMAP) providing integration into both ATM and IP networks.
HighPGate™ - a Multiservice Access Gateway designed to enable conversion to NGN for voice, data and video traffic.

Teledata was established in 1981. Its headquarters are based in Herzelia, Israel, with subsidiaries in the Netherlands, Australia and Brazil. Teledata has 150 employees worldwide. Teledata has 12 patents and 40 patent applications, primarily in the United States.

Teledata sells its products both directly and through distributors in Europe, Asia, Africa and South America.

Teledata's revenues were $39 million in 2004, $21 million for the period November 2002 to October 2003 and $32.8 million for the period October 2001 to November 2002.

Wavion

Wavion is a Delaware corporation with research and development facilities in Israel. Wavion commenced development of its products in the second quarter of 2000. Wavion develops and delivers wireless LAN access points for indoor and outdoor applications. Wavion's proprietary signal processing algorithms provide significant performance gains in system capacity, operating range, data rate, interference mitigation, and multipath mitigation. The modular technology can be customized to meet the requirements of most equipment vendors and integrates easily into any wireless communication system.

In 2002, as a result of the downturn in the broadband wireless communications market, which delayed the release of Wavion's products, Wavion significantly reduced its research and development expenses and began to sell subcontracting services for the development of wireless sub-systems. Wavion recorded development service revenues of $1.8 million in 2003 and $1.7 million in 2002. Following the completion of a $12.5 million financing round in 2003, Wavion directed resources away from its subcontracting activities towards development of its technology and therefore Wavion recorded insignificant revenues in 2004.

Wavion does not expect to commence product sales prior to 2006.

Starling

Founded at the end of 2003 and headquartered in Yoqneam, Israel, Starling is a provider of innovative connectivity solutions for the broadband access market for aircraft. Its antenna and SATCOM (satellite communications) systems are based on proven technology developed at Rafael and Elbit Systems. Starling provides a unique connectivity solution that makes possible the delivery of advanced Internet services and applications for Voice over IP communication (VOIP), security, entertainment and operations on all three major categories of aircraft, namely, business jets, narrow-body and wide-body. The Starling MIJET product line incorporates a Ku-band low profile antenna with a proprietary SATCOM resource allocation system that effectively utilizes satellite transponder capacity. The solution enables the delivery of high speed Internet services on a broadband connection of up to 40 Mbps (megabits per second).

Starling does not expect to commence sales prior to the middle of 2006.

Pulsicom

Pulsicom Israel Technologies Ltd. develops high accuracy, real time locating and tracking systems for confined spaces. Pulsicom's technology employs short-pulse technologies, including very-and ultra-wideband and sophisticated position-determination algorithms.

Pulsicom is an early stage development company, which has not yet completed its commercial product development. In order to generate revenues, Pulsicom provides development services to different customers. Pulsicom has limited resources and its continued operations depend on its ability to raise additional capital. There is no assurance that Pulsicom will be successful in its efforts to raise additional capital.

Cellact

Cellact Ltd. is a developer of cellular messaging platforms and applications, based on proprietary technology. Cellact's main product, Large Account gateway, was first commercially released in July 2001. The Large Account gateway is a product aimed at mobile operator, virtual mobile operators and mobile service providers. The Large Account provides the operator with the ability to easily connect and manage content providers and enterprises to its SMS and MMS systems. Cellact's customers come from a variety of industries, including telecom, finance and call centers

Cellact's revenues were $1.2 million in 2004, and $1.0 million in 2003. Prior thereto,Cellact's revenues were not significant.

4. Semiconductors

Our activities in the field of semiconductors consist of our holdings in the following companies:

- ChipX, in which we hold approximately 26% of the outstanding shares.
- Jordan Valley, in which we hold approximately 28% of the outstanding shares;
- SELA, in which we beneficially own approximately 66% of the outstanding shares representing all the shares owned by us and RDC, or approximately 39%, representing our share in the holding of RDC;
- 3DV, in which we beneficially own approximately 95% of the outstanding shares representing all shares owned by us and RDC, or approximately 71%, representing our direct holding and our share in the holding of RDC; and

ChipX

ChipX is a manufacturer of late stage programmable structured ASICs (Application Specific Integrated Circuits). ChipX's innovative, patented technology consolidates wafer manufacture tooling, reduces time-to-market and minimizes the cost of initial production. In 2004, ChipX discontinued the low volume OneMask business to focus on specific higher volume vertical markets with their future products. The products in development will be released during the second half of 2005, with initial customer productions commencing in 2006. ChipX also discontinued the back end production processes relating to low volume production, in effect becoming a totally fabless operation.

ChipX's Structured ASIC solution specifically addresses applications with medium to high production volumes. Along with standard cell ASIC vendors, ChipX primarily addresses the hard-wired ASIC market serving a wide variety of end markets, including automotive, computer, consumer, industrial and communications markets.

ChipX depends upon third-party manufacturers to manufacture its products. ChipX uses a wide range of parts and raw materials in the production of its semi-conductors, including silicon wafers, and electronic and mechanical components.

ChipX generally does not have guaranteed supply arrangements with its suppliers and does not maintain an extensive inventory of parts and materials for manufacturing.

ChipX's patented structured ASIC technology is protected by several core patents on its basic architecture, special logic cell and metal configurable memory. In addition, ChipX has internally developed routing software and metal programmable input/output cells to take advantage of its proprietary technology.

ChipX's total revenues were $16.2 million in 2004, $13.7 million in 2003 and $16.5 million in 2002.

ChipX's headquarters are located in Santa Clara, California with research and development operations taking place in Haifa, Israel. ChipX has 75 employees.

Jordan Valley

Jordan Valley, an Israeli company, offers inline metrology solutions with ultra thin film measurement capability and wide range of application coverage based on X-ray technology. The company's JVX® platform exploits various X-ray-based schemes to provide a broad range of measurement capabilities including thickness, density, roughness, and composition of metals and dielectric films. The platform features small spot size, non-destructive, enabling product wafer metrologies.

Jordan Valley operates two business divisions: analytic division and semiconductor division. Jordan Valley focuses in the semiconductor industry, selling, directly in the United States and via distributors in Japan, Europe, Taiwan and China.

Jordan Valley's headquarters, manufacturing, and R&D facilities are located in Migdal Haemek, Israel. Marketing offices are located in the United States. Jordan Valley has 75 employees.

In the field of X-Ray metrology, Jordan Valley holds 10 U.S. patents with 12 applications pending, as well as 3 patents with 15 applications pending in foreign jurisdictions.

Jordan Valley's revenues were $8.2 million in 2004, $3.2 million in 2003 and $3.2 million in 2002.

SELA

SELA develops and manufactures yield enhancing and automation equipment for the semiconductor and optical component industries. SELA is dedicated to the development and marketing of solutions for failure analysis and process monitoring in the semiconductor industry. SELA's automated sample preparation systems are used primarily by semiconductor manufacturers to prepare samples for scanning electron microscopy and transmission electron microscopy.

SELA has 6 patents and 2 applications.

SELA’s revenues amounted to $5.1 million in 2004, $4.3 million in 2003 and $3.5 million in 2002.

SELA's headquarters are located in Yoqneam, Israel and it maintains a marketing office in Sunnyvale, California. SELA has 35 employees.

3DV

3DV designs and develops three dimensional image sensors chip sets that generate both color and depth information, for each object captured by a camera, in real time. 3DV's business is currently focussed on applications in the medical field.

3DV is a development-stage company without any material revenues and its ability to continue to operate is dependent upon financial support from its shareholders.

5. Advanced Materials

Our activities in the field of amorphous metals consist of our holding in AMT in which we hold approximately 41% of the outstanding shares on an as converted basis.

AMT

AMT operates through its group companies in developing, marketing and licensing technologies for amorphous and nano-crystalline advance materials, as a solution for a wide range of commercial applications. Amorphous materials exhibit magnetic, electrical, mechanical and chemical properties that enable the enhancement of existing products and applications, as well as the introduction of new products and solutions for various industrial and high-tech applications and markets. AMT operates in four fields: heating, sensoring (authentication and anti-shop lifting), micro wires and electronic elements. AMT’s current main focus is in the field of heating through A.H.T. Advanced Heating Technology Ltd., or AHT, and in the sensoring field (authentication and anti-shop lifting) through A.C.S. Advanced Coding Systems Ltd, or ACS. The continued operations of AMT’s group companies are largely dependent upon their ability to generate sufficient revenues or raise additional capital to finance their continued operations.

AHT

AHT, in which AMT holds 77% of the outstanding shares, is engaged in the development and production of heating applications based on amorphous materials**.** AHT holds a global patent on using amorphous ribbons for heating products. AHT has developed a variety of heating products for domestic, outdoor, agricultural and pipe heating markets. AHT’s heating element enables the heating of very large surface areas at lower temperatures and higher efficiency and therefore at a lower cost and presents competitive advantages over other heating alternatives. AHT currently focuses on two principal markets: under floor heating and outdoor heating.

In 2004 AHT's revenues were $1.2 million and in 2003, AHT's revenues were $0.8 million. Prior thereto, AHT's revenues were not significant.

ACS

ACS, in which AMT holds directly and indirectly 61% of the outstanding shares, develops, markets and sells products using amorphous material for brand protection against counterfeiting and theft and electronic article surveillance tags for anti-shoplifting. ACS competes in the electronic article surveillance tags, data and authentication tags markets.

In 2004 ACS's revenues were $ 0.8 million, and in 2003 ACS's revenues were $0.6 million. Prior thereto, ACS's revenues were not significant.

Other Holdings

EVS

Elbit Vision Systems Ltd., or EVS, [OTCBB: EVSNF.OB], in which we hold approximately 10% of the outstanding shares, designs, develops, manufactures, markets and supports automatic visual inspection and quality monitoring systems for a broad range of industries. EVS' automatic in-line inspection and quality monitoring systems are designed to increase the accuracy, consistency and speed of detection of defects in the manufacturing process in order to reduce labor costs, improve product quality and increase manufacturing efficiency. EVS' Microelectronic Division provides optical and laser-based inspection and correction systems for the manufacture of liquid crystal displays, flat panel displays and bare silicon wafers. EVS's, Industrial Division provides automatic optical inspection (AOI) and non-destructive ultrasound inspection systems for "heavy" manufacturing industries (automotive, aeronautics, steel and others) and industrial materials (textiles, non-wovens, plastic, paper and others).

During 2004, EVS has implemented new automatic optical inspection (AOI) products for composite materials including carbon and for other materials such as screens, film, nonwoven, glass, tire cord and narrow stripes (vehicle seat belts).

EVS maintains a global sales force and service coverage with over 850 inspection systems installed in 25 countries and has more than 100 customers.

EVS's revenues were $11.0 million in 2004, $6.3 million in 2003 and $7.2 million in 2002

EVS is headquartered in Yoqneam, Israel, with offices in the United States and Korea.

C. Organizational Structure

As of June 28, 2005, DIC, an Israeli company, holds approximately 47.5% of our total outstanding shares. For additional information about DIC, please see "Major Shareholders" in

Item 7 below. For our holdings in our group companies, please see the discussion in this Item 4 above.

D. Property, plants and equipment

Our corporate headquarters and executive offices are located in Tel-Aviv, Israel. These offices, which measure approximately 980 square meters, are leased at an annual rent, including management fees to the landlord, of approximately $0.3 million.

We believe that the above facilities are adequate for our operations as currently conducted. In the event that additional facilities are required, we believe that we could obtain such additional facilities at commercially reasonable prices.

In addition, we have contractual rights to long-term leases in property located in Karmiel, in northern Israel, totaling approximately 15,760 square meters, consisting of building facilities. These premises are currently leased to Elbit Systems. (See Item 7, "Related Party Transactions”.)

Item 5. <u>Operating and Financial Review and Prospects</u>

OVERVIEW

We are a high technology operational holding company that operates through subsidiaries and affiliated companies, referred to as our group companies. Founded in 1962, we have been a major force in the development of the Israeli high technology industry by building Israeli and Israel-related companies with technologies in the fields of medical devices, advanced defense electronics, telecom, semiconductors, software products and services and advanced materials. Historically, most of our group companies were established together with entrepreneurs or started as activities within Elron and were subsequently spun-off.

In addition, some of our group companies grew out of our subsidiary, RDC, established with Rafael, the largest research and development organization of Israel's Ministry of Defense. RDC was established pursuant to an agreement entered into in July 1993 for the purposes of exploiting Rafael's technology in non-military markets. RDC has first rights to commercially exploit technologies of Rafael in non-military markets, which rights are dependent primarily upon RDC’s identification of new and existing military technology developed by Rafael.

Our group companies include both publicly traded and privately held companies.

Our activities range from complete operational control over the business to involvement in the management of our group companies in which we maintain controlling or significant holdings, and, in a limited number of cases, non-significant holdings. We participate in the management of most of our group companies by means of active membership on their boards of directors and board committees. As a result, we are involved in matters of policy, strategic planning, marketing, selecting and manning senior management positions, approving investments and budgets, financing and the overall ongoing monitoring of our group companies’ performance. In addition to our representation on the boards of directors of our group companies, we provide hands-on assistance to the group companies' management in support of their growth. We view our hands-on involvement in the operations of our group companies as a key element of our business. Our group companies therefore benefit from the experience of our management team in various areas in which they need support and leadership, including, but not limited to, strategic planning, research and development guidance, identifying joint venture opportunities, introductions to potential customers and investors, risk management, market analysis, business plan preparation, budgetary control, and legal support.

Technology industries are characterized by the high degree of risk inherent in their products, their continuous technological innovation and their penetration into world markets, which requires investment of considerable resources and continuous development efforts. The future success of our group companies is dependent upon their technological quality, prices and nature of their products in comparison to their competitors and their ability to introduce new products to the markets at the right time, while offering cost effective solutions suitable to their customers' needs as well as their ability to raise financing and the condition of the capital markets.

We expect to continue to build and realize value for our shareholders through the sale to third parties of a portion or all of our holdings in, or the issuance of shares by, our group companies, while simultaneously pursuing the acquisition of, or investment in, new and existing companies at differents stages of development including early stage and more mature companies. We believe that this strategy provides the ability to increase shareholder value as well as to create capital to support the growth of our group companies and to invest in new opportunities. The nature of our business, therefore, will result in some volatility in our results of operations, depending on the transactions that take place within a particular period.

Our net income (or loss) in any given period is due, for the most part, to the results of operations of our group companies (which are accounted by us under the consolidation or equity method of accounting) and dispositions and changes in our holdings of group companies. As most of our group companies are technology companies which have not yet generated significant revenues and which invest considerable resources in research and development and in marketing activities, we have experienced, and expect to continue to experience, losses in respect of these companies. However, as a result of new accounting pronouncements described below under "CRITICAL ACCOUNTING POLICIES", some of our group companies and new companies in which we may invest may be accounted for at cost, thereby not affecting our results of operation. We anticipate this change may have a significant effect on our results of operations.

Our capital resources in any given period are primarily affected by the extent of our investment in existing and new companies and the realization of certain holdings. The results of operations of our group companies, and consequently, our results of operations and capital resources, are affected by general economic conditions as well as by factors specifically related to the technology markets, which also affect the ability of our group companies to raise financing and our ability to dispose of holdings and realize gains from our holdings.

TREND INFORMATION

Technology industries are affected by economic trends and the condition of the capital markets. The downturn in the world economy and, in particular, in the technology sector, during 2001 and through the middle of 2003, affected our group companies' ability to raise additional financing from other sources, the results of operations of our group companies and our ability to successfully "exit" some of our group companies and record gains at the same level that we experienced in the years prior to the downturn.

Since the second half of 2003, there has been a recovery in the technology sector and capital markets. This trend was reflected in the improvement in the results of operations of most of our group companies as well as the raising of funds from new strategic and other investors in private placements completed by some of our group companies. In addition, we recorded gains from realizing certain of our holdings, mainly in 2004, as a result of the sale of our holdings in Elbit Systems, and we will record a significant gain in the second quarter of 2005 from the sale of most of our shares in Partner and the sale of all of our shares in Oren (see Item 4 "Information on the Company"). Should the recovery in the world economy and, in particular, the technology sector, continue, we anticipate that it will have a positive effect on our group companies and their ability to raise additional capital.

We also anticipate increasing our investments in new companies in our main areas of operation, and we are currently considering investments in new companies in different stages of their life cycle including early stage and more mature companies, mainly in the fields of medical devices and telecommunications. In this regard, new companies in which we invested in 2004 and since the beginning of 2005 include a $6.7 million investment in Jordan Valley, operating in the field of semiconductors, a $3.0 million investment in Starling, operating in the field of broadband communication, a $7.3 million investment in Impliant, a medical device company, a $1.7 million in NuLens, a medical devices company, and a $16 million investment in Teledata, a telecommunication company (see Item 4 "Information on the Company").

CRITICAL ACCOUNTING POLICIES

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States (“US GAAP”). Our significant accounting policies are more fully described in Note 2 to our consolidated financial statements. Certain accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions upon which we rely are reasonable based upon information available to us at the time that these estimates, judgments and assumptions are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities as of the date of the financial statements, as well as the reported amounts of revenues and expenses during the periods presented. To the extent there are material differences between these estimates, judgments or assumptions and actual results, our financial statements will be affected. The significant accounting policies that we believe are the most critical to aid in fully understanding and evaluating our reported financial results include the following:

- Principles of accounting for holdings in group companies
- Business combinations and purchase price allocation

- Impairment of goodwill and other intangible assets
- Other-than-temporary decline in value of investments in group companies
- Revenue recognition
- Accounting for income taxes
- Non-monetary transactions

Principles of Accounting for Holdings in Group Companies

The various holdings that we have in our group companies are accounted for under several methods, based among others, on our level of ownership and the type and form of our holdings in our group companies, as described below.

Consolidation. Companies over which we have control are accounted for under the consolidation method of accounting. Control is usually assumed when we own and/or our subsidiary owns more than 50% of the outstanding voting securities of a company. However, whether or not we control a group company also depends on an evaluation of several factors, including, among others, our representation on the board of directors, the level of financing provided by us to the group company and any minority rights and other factors which require management to make judgment and involve the use of significant estimates and assumptions.

Under the consolidation method, a controlled company's assets and liabilities are included within our consolidated balance sheet and its income and expense items are included within our consolidated statements of operations. The share of other shareholders in the net assets and in the net income or losses of a consolidated company is reflected in minority interest in our consolidated balance sheet and in our consolidated statements of operations, respectively. The minority interest amount adjusts our consolidated net income (loss) to reflect only our share in the earnings or losses of any consolidated company.

Notwithstanding the above, in January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities – An Interpretation of Accounting Research Bulletin No. 51" ("FIN 46"), relating to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. In December 2003, the FASB issued FASB Interpretation No. 46 (revised December 2003) ("FIN 46R"), which replaced FIN 46. FIN 46R defines the provisions under which a Variable Interest Entity ("VIE") should be consolidated. FIN 46R provides several exceptions to its scope, such as that an entity that is deemed to be a business need not be evaluated to determine if it is a VIE unless one of the conditions specified in FIN 46R exists.

As an operational holding company, we have made investments in and granted loans to companies that are engaged in various fields of high technology. Some of these companies are in their early stages of development and will require substantial external investments until they can finance their activities without additional support from other parties and may be considered VIEs. These companies are currently primarily funded with financing from venture capital funds, other holding companies and private investors.

FIN 46 was effective immediately for VIEs created after January 31, 2003. For VIEs created before January 31, 2003, FIN 46R was adopted as of March 31, 2004. Upon the adoption of the Interpretation, and upon certain events which require a reassessment, we assessed and will reassess our investments in our group companies. Assessment of whether a group company is within the scope of FIN 46R, whether a group company is a VIE and the determination of the primary beneficiary is judgmental in nature and involves the use of significant estimates and assumptions regarding the fair value of certain entities and their variable interests. The estimates and assumptions include, among others, forecasted cash flows, their respective probabilities and the economic value of certain preference rights.

Equity Method. Group companies which we do not control, but over whom we exercise significant influence and in which we hold common stock or in-substance common stock as defined in EITF 02-14 (which is further described below), are accounted for under the equity method of accounting. Significant influence is usually assumed when we hold 20% or more of a group company’s voting securities, however, whether or not we exercise significant influence with respect to a group company also depends on an evaluation of several additional factors, including, among others, our representation on the board of directors, agreements with other shareholders, our participation in policy making processes, the existence of material intercompany transactions and technological dependency, the extent of ownership by an investor in relation to the concentration of other shareholdings, and other factors which may require management to make certain judgmental decisions regarding significant influence.

In July 2004, the EITF reached a consensus on Issue No. 02-14, "Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock” ("EITF 02-14"), according to which the equity method of accounting should be applied to investments in common stock and in in-substance common stock if the investor has the ability to exercise significant influence over the operating and financial policies of the investee. EITF 02-14 defines in-substance common stock as an investment with similar risk and reward characteristics to common stock. The provisions of EITF 02-14 were effective beginning in the fourth quarter of 2004. For investments that are not common stock or in-substance common stock, but were accounted for under the equity method of accounting prior to the effective date of EITF 02-14, the equity method of accounting should be discontinued at the effective date. Previously recognized equity method earnings and losses should not be reversed. In certain group companies we invested, among others, in preferred shares which include rights, among others, such as cumulative and participating dividends, dividend preferences and liquidation preferences. Upon adoption of EITF 02-14, we evaluated the impact of its provisions and found that there are no investments that were previously accounted for by the equity method which are not considered to be in-substance-common stock, nor are there investments that are in-substance common stock that were not accounted for under the equity method of accounting prior to the effective date of EITF 02-14 and which should be accounted as such in accordance with EITF 02-14. However, new companies in which we invested in the fourth quarter of 2004, namely Jordan Valley and Impliant, are accounted for at cost notwithstanding our significant influence in such companies, as the investment in these companies is not considered to be in-substance-common stock. In 2005, we invested in Teledata and NuLens. These investments may also be accounted for at cost as these investments may not be considered to be in-substance-common stock. Any assessment of whether we hold in substance common stock in a group company is judgmental in nature and involves the use of significant estimates and assumptions such as assessing the fair value of the subordinated equity of the group company.

We also account for our interests in private equity funds under the equity method of accounting, based on our holding percentage.

Under the equity method of accounting, a group company's assets and liabilities are not included within our consolidated balance sheet and their results of operations are not reflected within our consolidated statements of operations. However, our share in the net income or losses of the group company is reflected as an equity income (loss) in our consolidated statements of operations. The share of income or losses is generally based upon our ownership level of the outstanding share capital of the group company. Notwithstanding the above, in circumstances where the equity method is being applied and our ownership in an investee is in the form of a preferred security or other senior security, we recognize equity method losses based on our ownership level in the particular investee security or loan held by us to which the equity method losses are being applied.

Other Methods. Our holdings in companies that we do not account for under either the consolidation or the equity method of accounting are accounted for under three different methods:

- Non-marketable securities are presented at cost. Under this method, our share in the income or losses of these entities is not included in our consolidated statements of operations.
- Marketable securities, which are classified as trading securities, are presented at fair market value and the changes in the market value are reflected in our results of operations during each reporting period.
- Marketable securities which are classified as available-for-sale are presented at fair market value and the effect of any unrealized change in market value is reflected in other comprehensive income (loss). When realized, realized gain or loss is included in our results of operations.

Business Combinations and Equity Method Purchase Price Allocation

Business combinations are accounted for using the purchase method of accounting, under which the total purchase price is allocated to the acquired company's assets and liabilities, based on their estimated fair values, and the remainder, if any, is attributed to goodwill.

The aggregate purchase price of the shares of Given Imaging purchased during 2004 (see Item 4- "Information on the Company") of approximately $43.9 million has been allocated as follows: $4.4 million to Given Imaging identifiable net assets, $30.4 million to intangible assets other than goodwill, such as customer base and technology, $1.7 million to in-process research and development activities, and $7.4 million to goodwill. Products which had not received marketing clearance by regulatory authorities as of the acquisition dates, were considered to be incomplete and accordingly the amount allocated to such products was considered to be in-process research and development activities ("IPR&D"). The amount allocated to IPR&D was charged immediately to our results of operations in accordance with FASB Interpretation No. 4, "Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method" ("FIN 4"). The amounts allocated to intangible assets other than goodwill are amortized on a straight-line basis over their weighted average expected useful life of 12 years.

The amortization of the identifiable intangible assets as well as the write-off of the IPR&D, (which amounted in 2004 to approximately $3.2 million), were included as part of our share in the income or losses of our equity investments.

In 2002 we allocated the aggregate purchase price of approximately $103.5 million, resulting from the merger with Elbit and the share purchase of DEP’s shares, to Elbit's and DEP's assets based on their estimated fair values. The majority of the purchase price was allocated to Elbit's holding in Partner and to DEP's holdings accounted for under the equity method (including holdings through its subsidiary, RDC). An amount of $19.0 million was allocated to goodwill which reflected the anticipated synergies resulted from the combined entity, including anticipated reductions in operational and management costs, the creation of an enhanced platform, a more simplified and efficient organizational structure and greater resources and scope of operations, which would benefit the group companies. Subsequently to the acquisition date and through December 31, 2004, goodwill was reduced by $14.3 million as a result of the reversal of a valuation allowance recorded at the acquisition date in respect of Elbit’s carry forward losses that had accumulated through that date, due to final tax assessments for previous years.

Estimating the fair value of certain assets acquired and liabilities assumed is judgmental in nature and often involves the use of significant estimates and assumptions, mainly with respect to intangible assets. While there are a number of different methods for estimating the value of intangibles acquired, the primary method used was the discounted cash flow approach. Some of the more significant estimates and assumptions inherent in the discounted cash flow approach include projected future cash flows, including their timing, a discount rate reflecting the risk inherent in the future cash flows and a terminal growth rate. Another area which required judgment which can impact our results of operations was estimating the expected useful lives of the intangible assets. To the extent intangible assets are ascribed with longer useful lives, there may be less amortization expenses recorded in any given period. As we and our group companies operate in industries which are rapidly evolving and extremely competitive, the value of the intangible assets, including goodwill, their respective useful lives and the investments in companies is exposed to future adverse changes which can result in a charge to our results of operations. In 2004 and 2003, we recorded impairment losses in respect of certain investments of Elbit and DEP, to which we allocated a portion of the purchase price at the time of the aforementioned acquisitions, in the amounts of $1.1 million and $2.5 million, respectively (See also “Other-Than-Temporary Decline in Value of Investments in Group Companies”).

Impairment of Goodwill and Other Intangible Assets

We conduct a goodwill impairment review at least annually and on an interim basis whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors that we consider important which could trigger an impairment review include significant underperformance relative to historical or expected future operating results and significant negative industry or economic trends. We test for impairment at a level referred to as a reporting unit. Determining fair value involves the use of significant estimates and assumptions. These estimates and assumptions could have an impact on whether or not an impairment charge is recognized. To determine fair value, we may use a number of valuation methods including quoted market prices, discounted cash flows and revenue multipliers. As mentioned above, these approaches, mainly the discounted cash flow method and revenue multiples method, use estimates and assumptions including projected future cash flows, discount rate and terminal growth rate. In 2004, a goodwill impairment charge in the amount of $2.0 million was recorded with respect to the operation of Elron TeleSoft in light of its results of operation in 2004, using the discounted cash flow method to determine the fair value of Elron TeleSoft. As we operate in industries which are rapidly evolving and extremely competitive, it is possible that our estimates could change in the near term and there can be no assurance that future goodwill impairment review will not result in an additional charge to our results of operations. At December 31, 2004, consolidated goodwill amounted to approximately $10.3 million.

Other intangible assets with definite useful lives are 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 the future undiscounted cash flows expected to be generated by the asset. If an asset is considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair value. In the evaluation of fair value and recoverability, we use significant estimates and assumptions such as projected future cash flows which are subject to high degree of judgment. In 2004 we recorded impairment charges of other intangible assets of $7.1 million, mainly with respect to Elron TeleSoft in light of its results of operations in 2004 and MediaGate N.V, or MediaGate due to our revised estimate about future royalties to be received in consideration for the sale of its technology. As we operate in industries which are rapidly evolving and extremely competitive, changes in the assumptions and estimates may affect the carrying value of the intangible assets, and could result in an additional impairment charge to our results of operations. At December 31, 2004, consolidated intangible assets, other than goodwill, amounted to approximately $3.0 million.

Other-Than-Temporary Decline in Value of Investments in Group Companies

At the end of each reported period we evaluate whether an other-than-temporary decline in value of an investment in a group company has been sustained. This evaluation is judgmental in nature. If it has been determined that an investment has sustained an other-than-temporary decline in its fair value relative to its carrying value, the investment is written down to its fair value by a charge to our results of operations.

An evaluation of fair value is dependent upon specific facts and circumstances. Factors that are considered by us in this determination include financial information (including, among others, budgets, business plans and financial statements), the value at which independent third parties have invested or have committed to invest and independent appraisals, if available. Factors indicative of an other-than-temporary decline include recurring operating losses, credit defaults, and subsequent rounds of financing at an amount below the cost basis of the investment. This list is not all inclusive, and we weigh all quantitative and qualitative factors in determining if an other-than-temporary decline in value of an investment has occurred. As we operate in industries which are rapidly evolving and extremely competitive, it is possible that our estimates could change in the near term, and there can be no assurance that an additional write-down or write-off of the carrying value will not be required in the future. In 2004 and 2003 we recorded write-downs in the amounts of $1.5 million and $4.2 million, respectively, with respect to certain group companies, in 2004 mainly with respect to Textology, Inc., or Textology, 3DV and Ingeneo Ltd. and in 2003 mainly with respect to Cellenium M.C.S Ltd., or Cellenium, and Textology.

Revenue Recognition

Our revenues are derived from our consolidated subsidiaries. Revenues in 2004 and 2003 amounted to $16.3 million and $16.5 million, respectively. Revenues from sales of products and services are recognized after all of the following occurs: the product is delivered, collection is probable, fees are fixed or determinable, vendor-specific objective evidence exists to allocate the total fee to elements of an arrangement and persuasive evidence of an arrangement exists. The determination whether collection is probable is judgmental in nature and based on a variety of factors, including the payment and other terms of the individual customer contract, credit history of the customer, prior dealings with specific customers, and certain other factors. Maintenance revenue is recognized on a straight-line over the term of the contract period.

Income and profit derived from projects related to software development are recognized upon the percentage of completion method, based on the ratio of hours performed to date to estimated total hours at completion. Estimated gross profit or loss may change due to changes in estimates resulting from differences between actual performance and original forecasts. Estimates are reviewed periodically, and the effect of any change in the estimated gross profit for a project is recorded in results of operations in the period in which the change becomes known on a cumulative catch-up basis. Anticipated losses on projects are charged to earnings when identified. A number of internal and external factors affect our subsidiaries cost estimates, including labor rates, revised estimates of uncompleted work, efficiency variances, customers' specifications and testing requirements changes. If any of these factors were to change, or if different assumptions are used, our results of operations may be affected. In addition, estimates are made as to the total hours at completion. The number of hours may change due to the actual progress on the project. Change in estimates regarding the percentage of completion may affect the results of operations.

Accounting for Income Taxes

At the end of each reported period, we are required to estimate our income taxes. This process requires us to estimate our actual current tax liabilities and make an assessment of temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be realized through future taxable income and, to the extent we believe that realization is not likely, we must establish a valuation allowance. Management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. Our judgment as to the probability to realize our net deferred tax assets is largely based upon interpretations of certain tax laws and estimates and assumptions mainly with respect to our ability to realize investments in our group companies. Our ability to realize investments is mainly dependent upon factors such as the condition of the securities markets and other general economic conditions. As the securities markets for our group companies are highly volatile, changes in our assumptions and estimates may require us to increase the valuation allowance and therefore we may be required to include an expense within the tax provision in our statement of operations.

As of December 31, 2004, net deferred tax assets with respect to the carryforward losses that are more likely than not to be realized in future years amounted to approximately $12.0 million ($7.6 million in 2003). In 2004 we reduced the previous valuation allowance by $29.7 million in respect of losses incurred in prior periods mainly due to the sale of our shares in Elbit Systems and due to final tax assessments for previous years. In 2003 we reduced the previous valuation allowance by $7.3 million, mainly as a result of the merger of the urology units of Galil and Amersham. In addition, in 2003, we reduced the previous valuation allowance by $8.5 million, the majority of which was recorded as a reduction of goodwill since the deferred tax assets related to carryforward losses in Elbit incurred in periods prior to the acquisition of Elbit (see also "Business Combinations and Purchase Price Allocation").

Deferred tax liabilities amounted as of December 31, 2004, to $47.7 million, mainly with respect to our investment in Partner which is accounted for as available-for-sale securities.

During 2004, we recorded tax expenses in the amount of $15.1 million which was mainly due to the sale of our shares in Elbit Systems. The tax from the sale was largely offset by decreasing our valuation allowance as discussed above. During 2003, we recorded tax expenses of $6.8 million mainly by realizing our deferred taxes due to the sale of shares of Partner, Given Imaging, Zix and 24/7.

Non-Monetary Transactions

The basic principle in APB 29, "Accounting for Non-monetary Transactions" is that the accounting for non-monetary transactions should be based on the fair values of the assets exchanged. The cost of a non-monetary asset acquired in exchange for another non-monetary asset is the fair value of the asset received or the fair value of the asset surrendered to obtain it (if more clearly evident than the asset received). However, in an exchange of similar productive assets, since the culmination of an earning process has not occurred, the exchange should not be recorded at fair value and the asset received should be recorded at the recorded amount of the assets given up. According to EITF 01-2, "Interpretations of APB Opinion No. 29", transactions by SEC registrants that involve the exchange of a business for any non-monetary asset, including an equity method investment that is not an interest in a joint venture, are not exchanges of productive assets and must be accounted for at fair value unless fair value is not determinable within reasonable limits. In determining whether the asset given up constitutes a business, the guidance in EITF 98-3, "Determining whether a non-monetary transaction involved receipt of productive assets or of a business" should be followed.

Determining whether the assets transferred constitute a business requires significant judgment and is dependent on the particular facts and circumstances, mainly regarding the determination of the degree of difficulty or level of investment necessary to obtain access or to acquire missing elements in the set of assets transferred. In addition, determining the fair value of the transaction is judgmental in nature and often involves the use of significant estimates and assumptions.

In determining the fair value of the business transferred by Galil Medical to Oncura , a method of discounted cash flow was used, which includes significant estimates and assumptions. As Oncura operates in an industry which is rapidly evolving and extremely competitive, its value, as well as the value of its intangible assets, including goodwill, can be exposed to future adverse changes which can result in a charge to its, and in turn, to our results of operations.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets, an amendment of APB Opinion No. 29" ("SFAS 153"). SFAS 153 amends APB 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. A nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS 153 is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. The Company does not expect that the adoption of SFAS 153 will have a material effect on its financial position or results of operations.

A. Operating Results

Basis of Presentation

Consolidation. Our consolidated financial statements include the accounts of Elron and all of our direct or indirect (through Elbit and DEP) controlled subsidiaries. The following are our main subsidiaries:

Year ended December 31,		
2004	**2003**	**2002**
ESW[1]	ESW[1]	ESW[1]
Elron TeleSoft	Elron TeleSoft	Elron TeleSoft
RDC	RDC	RDC
Galil Medical	Galil Medical	Galil Medical[4]
MediaGate	MediaGate	MediaGate[5]
3DV[2]		
SELA[3]		
Starling		

1 Elron SW Inc., formerly Elron Software Inc., has been liquidated as of December 31, 2004.

2 3DV was consolidated following the purchase of a controlling interest during the first quarter of 2004 from other shareholders of 3DV.

3 Following the conversion of shareholder loans granted by RDC to SELA at the end of the second quarter of 2004.

4 Galil Medical was consolidated following the purchase of a controlling interest during the third quarter of 2002.

5 Mediagate was consolidated following the purchase of a controlling interest during the third quarter of 2002.

Equity Method. Our main group companies held by us or through Elbit, DEP and/or RDC accounted for under the equity method of accounting include by us:

Year ended December 31,					
2004		2003		2002	
Elbit Systems[1]	SELA[1]	Elbit Systems	KIT	Elbit Systems	KIT
Given Imaging	Pulsicom	Given Imaging	3DV	Elbit[3]	Galil
Oncura	Cellact	Oncura[2]	Cellact	DEP[3]	Medical[5]
NetVision		Netvision	Pulsicom	Given Imaging	Avantry
ChipX		ChipX	Avantry	NetVision	3DV
Wavion		Wavion	SELA	MediaGate[4]	Cellenium
Oren Semiconductor		Oren Semiconductor		ChipX	Pulsicom
AMT		AMT		Wavion	CellAct
Notal		Notal		Oren Semiconductor	SELA
				AMT	

1 Through June 30, 2004
2 Since July 1, 2003
3 Through the completion of the merger with Elbit and purchase of DEP in May 2002
4 Through June 30, 2002

Year Ended December 31, 2004 compared to Year Ended December 31, 2003.

The following tables set forth our results of operations in the reported period:

	Year ended December 31,	
	2004	2003
	(millions of $, except per share data)	
Net income (loss)…………………………….	84.1	(7.2)
Net income (loss) per share………………….	2.87	(0.25)

The net income we reported in 2004 included the following main factors:

(i) a gain, net of tax, of approximately $91.5 million resulting from the sale of our holdings in Elbit Systems for approximately $196.6 million. This gain includes approximately $21.6 million resulting from a decrease in our previous valuation allowance in respect of losses incurred in prior periods. The decrease in our previous valuation allowance was made in light of the transaction, following which we revised our estimate about the realizability of deferred tax;

(ii) a gain, net of tax and minority interest, of approximately $6.7 million from the sale of Given Imaging's shares by RDC and the decrease in our direct and indirect interest in Given Imaging following the completion of Given Imaging's secondary public offering;

(iii) a gain of approximately $5.3 million resulting from the sale of our shares in KIT to a subsidiary of Laureate

(iv) a gain, net after tax, of approximately $3.6 million resulting from the sale of 854,701 Zix shares for an aggregate consideration of $8.1 million; and

(v) a tax benefit in the amount of approximately $2.9 million due to the change in the corporate tax rate in Israel enacted in 2004.

Additional factors that positively affected 2004 results were the following:
(i) The sale of the businesses of ESW and MediaGate in 2003 and the sale of our holding in KIT (our share in the losses of these companies accounted for an aggregate loss of $10.4 million in 2003);
(ii) the decrease of $3.2 million in our share in Galil Medical's operating losses following the formation of Oncura as a result of the merger of its urology unit and that of Amersham plc (Amersham was subsequently acquired by General Electric Company ; and
(iii) our share in the net income reported for the first time by Given Imaging in the amount of $0.5 million in 2004, compared to $1.8 million loss in 2003.

These were offset by the following factors:
(i) a write-off of IPR&D related to the acquisition of additional shares of Given Imaging in the amount of $1.7 million;
(ii) an increase in Elron Telesoft's losses from $2.1 million in 2003 to $7.9 million in 2004 which include impairment charges in the amount of $4.9 million;
(iii) a $2.7 million loss, net of tax, resulting from the write-off of future royalties to be received by MediaGate from Telrad in connection with the sale of MediaGate business to Telrad in 2003;
(iv) a $2.0 million loss representing the funding of NetVision's previous years' losses; and
(v) the effect of the sale of our holding in Elbit Systems in the third quarter of 2004, following which we ceased including our share in its net income (Elbit Systems accounted for $9.1 million of income in 2003 and for $4.7 million of income in 2004 through the date of its sale).

Reportable Segments

Subsequent to the sale of the business of ESW on September 2, 2003 to Zix, our reportable segments are i) The Systems and Projects Segment - Elron TeleSoft; and ii) Other holdings and the corporate operations, which includes our holdings in subsidiaries, affiliates and other companies, engaged in various fields of advanced technology, and corporate operations, which provide the strategic and operational support to the group companies. Prior to September 2, 2003, we operated through ESW in a third business segment – Internet Products – which has been reclassified as discontinued operations. ESW has been liquidated as of December 31, 2004.

At December 31, 2004, our main group companies were classified into the following segments:

	Systems and projects	Other holdings and corporate operations
Consolidated	Elron TeleSoft	RDC; Galil Medical; 3DV, Starling; SELA; MediaGate
Equity basis		Given Imaging; Oncura; NetVision; ChipX; Oren; Notal ; Wavion; AMT; Pulsicom; CellAct.
Cost		Jordan Valley; Impliant; Avantry
Available-for-sale		Partner, Elbit Vision Systems

The following tables reflect our consolidated data by reported segments:

	Systems and projects - Elron TeleSoft	Other holdings and corporate operations	Discontinued operations of Internet products - Elron SW	Consolidated
	(millions of $)			
	Year ended December 31, 2004			
Income*………………………	5.1	137.9	-	143.0
Costs and expenses…………..	13.0	26.2	-	39.2
Income (loss) from continuing operations……………………..	(7.9)	92.5	-	84.6
Net income (loss) ……………	(7.9)	92.5	**(0.5)	84.1
	Year ended December 31, 2003			
Income*………………………	7.4	40.9	-	48.3
Costs and expenses…………....	9.5	28.0	-	37.5
Loss from continuing operations…………………….	(2.1)	(4.8)	-	(6.9)
Net loss………………………	(2.1)	(4.4)	**(0.7)	(7.2)

* Income in the other holdings and corporate operations includes net losses from equity investments.

** The composition of the discontinued operation of ESW is as follows:

	Year ended December 31,	
	2004	2003
	(millions of $)	
Loss from operations…………..	(0.5)	(4.8)
Gain on disposal………………..	-	4.1
Loss from discontinued operations………………………	(0.5)	(0.7)

Systems and Projects - Elron TeleSoft

Elron TeleSoft is focused on telecommunications network management and revenue assurance products. The following table sets forth the operating results of Elron TeleSoft:

	Year ended December 31,	
	2004	2003
	(millions of $)	
Net revenues……………………….	5.1	7.4
Cost of revenues…………………...	3.4	4.6
Gross profit ………………………..	1.7	2.8
Operating expenses*………………	3.1	2.6
Amortization of other assets……….	0.6	0.8
Restructuring charges, net…………	0.2	-
Impairment of long-lived assets……	2.9	-
Impairment of goodwill…………….	2.0	-
Operating loss……………………...	(7.1)	(0.6)
Finance expenses, net……………...	0.8	1.5
Net loss……………………………	(7.9)	(2.1)

*Excluding amortization of other assets, impairment charges and restructuring charges which are presented separately.

Net Revenues. Elron TeleSoft's net revenues in 2004 decreased by $2.3 million, or 31%, to $5.1 million, compared to $7.4 million in 2003. The decrease resulted mainly from the decrease in revenues derived from sale of third parties' products as well as in license and project revenues, mainly due to longer sale cycles in its efforts to penetrate the international market with its new revenue assurance line of products.

Cost of revenues. Cost of revenues of Elron TeleSoft in 2004 were $3.4 million, representing a gross margin of 33%, compared to $4.6 million in 2003, representing a gross margin of 38%. The decrease in the gross margin resulted mainly from changes in revenue mix.

Operating expenses. Elron TeleSoft's operating expenses (excluding amortization of other assets, impairment charges and restructuring charges which are presented separately) in 2004 were $3.1 million, an increase of 19% over the $2.6 million in 2003. The increase in operating expenses resulted from an increase in development expenses of the company's new revenue assurance line of products and an increase in sales and marketing expenses associated with launching these products to the international market.

Restructuring expenses. In response to its operating results and in an effort to adjust its operations to the decrease in revenues, Elron TeleSoft underwent a restructuring program in the third quarter of 2004 which included workforce reduction of 15% across all functions of the organization. Restructuring expenses amounted to $0.2 million.

Impairment charges. In light of Elron TeleSoft's results of operations and its difficulties in penetrating international markets, Elron Telesoft tested for impairment its technology and fixed assets and subsequently the goodwill associated with its operations, resulting in an impairment loss of $2.9 million and $2.0 million relating to the technology and property and equipment and goodwill, respectively.

Operating loss. As a result of all the above, Elron TeleSoft's operating loss increased to $7.1 million in 2004 compared to $0.6 million in 2003.

Finance expense, net. Finance expenses decreased to $0.8 million in 2004 compared to approximately $1.5 million in the same periods in 2003. The decrease in finance expenses resulted mainly from the significant decrease in loan balances following the repayment of $51.1 million of bank loans by Elron TeleSoft (financed by an investment by us) during 2004.

The ability of Elron TeleSoft to increase its revenues and improve its operating results in the near future is dependent upon general economic conditions and, in particular, on an increase in telecom capital expenditure, its ability to penetrate the international market and whether its efforts to bring enhanced and new products to market are successful.

Other Holdings and Corporate Operations Segment

The other holdings and corporate operations segment includes our holdings in subsidiaries, affiliates and other companies engaged in various fields of advanced technology, and corporate operations which provide strategic and operational support to the group companies. The following table sets forth this segment's operating results:

	Year ended December 31,	
	2004	2003
	(millions of $)	
Net revenues…………………………….	11.3	9.2
Net loss from equity investments……….	(10.5)	(8.7)
Gain from disposals of businesses and affiliated companies and changes in holdings in affiliated companies, net…………………………	132.4	25.8
Other income, net……………………….	4.7	14.6
Total income…………………………….	137.9	40.9
Cost of revenues………………………...	6.3	5.6
Operating expenses*……………………	17.0	22.9
Amortization of other assets……………	0.1	0.3
Impairment of long-lived assets………...	4.2	-
Finance income, net…………………….	(1.4)	(0.8)
Total costs and expenses……………….	26.2	28.0
Income from continuing perations before tax on income…………………	111.7	12.9
Tax on income…………………………	(15.1)	(6.8)
Minority interest………………………..	(4.1)	(10.9)
Income (loss) from continuing perations	92.5	(4.8)
Gain from discontinued operations…….	-	0.4
Net gain (loss)…………………………..	92.5	(4.4)

*Excluding amortization of other assets and impairment charges which are presented separately.

Income

Net revenues. Net revenues of the other holdings and corporate operations segment consisted of sales of products and services by our subsidiaries, mainly Galil Medical and SELA (which results have been consolidated since July 1, 2004). The following table sets forth the segment revenues:

	Year ended December 31,	
	2004	2003
	(millions of $)	
Galil Medical……………………..	7.6	7.6
SELA……………………………..	3.3	-
MediaGate………………………..	-	1.5
Other……………………………..	0.4	0.1
	11.3	9.2

Galil Medical's revenues are derived mainly from the supply of cryo products and R&D services to Oncura, in which it has a 25% ownership interest, as a result of the merger of the urology therapy units of Galil Medical and GE on July 1, 2003.

SELA recorded revenues of $5.1 million in 2004 (of which $3.3 million were in the second half of 2004) compared to $4.3 million in 2003.

Share in net losses of affiliated companies. Our share in net losses of affiliated companies resulted from our holdings in certain investments that are accounted for under the equity method (see above under "Basis of Presentation"). The share in net losses of affiliated companies amounted to $10.5 million in 2004, as compared to $8.7 million in 2003.

As a result of the completion of the sale of our holding in Elbit Systems during the third quarter of 2004, our share in net income of Elbit Systems was included through the end of the second quarter of 2004 based on Elbit Systems' unaudited financial report as of June 30, 2004 and amounted to $4.7 million. Our share in the net income of Elbit Systems in 2003 amounted to $9.1 million. Elbit Systems revenues in 2004 through the end of the second quarter amounted to $445.3 million as compared to $420.9 million in the first half of 2003 and its net income amounted to $24.0 million as compared to $21.5 million in the same periods of 2003.

Highlights of the Results of Operations of Our Major Affiliates:

Given Imaging (a 20% holding directly and indirectly through RDC). Given Imaging's revenues in 2004 were $65.0 million, an increase of 60.4% over the revenues recorded in 2003 of $40.5 million. As of December 31, 2004, cumulative unit sales of Given Imaging capsule for the small intestine had reached 171,800 and its installed base reached more than 1,300 workstations in the United States and approximately 2,300 worldwide. Given Imaging's gross profit increased to 72.7% of revenues in 2004 compared to 66.6% in 2003 and it reported for the first time in its history net income of $2.9 million in 2004, compared to a net loss of $9.6 million in 2003.

During the second quarter of 2004, Given Imaging completed a secondary offering to the public in which it raised net proceeds of $44.3 million. In addition, Given Imaging entered into an exclusive sales representation and co-promotion agreement with Ethicon Endo-Surgery, Inc., a Johnson & Johnson company, according to which Ethicon has exclusive rights to market Given Imaging's Pillcam™ ESO video capsule for visualization of the esophagus. Following FDA clearance to market the PillCam™ ESO in late November and through December 31, 2004, more than 3,400 PillCam ESO capsules were sold.

Oncura (a 25% holding through Galil). Oncura commenced its operations on July 1, 2003 following the completion of the merger of the urology therapy units of Galil and GE which created Oncura. Oncura markets and sells therapeutic device systems and related consumables used primarily in the performance of minimally-invasive, urologic cancer treatment. Oncura's revenues in 2004 amounted to $68.8 million and its net loss amounted to $2.2 million. Oncura's revenues in the period since commencing operation and trough December 31, 2003 amounted to $31.4 million and its net loss amounted to $0.9 million.

Notal (a 26% holding). Notal, a medical device company operating in the field of early detection of Age Related Macular Deterioration (AMD), formally launched its product in October 2004 through Carl Zeiss Meditec Inc., one of the leading manufacturers of professional optics equipment. In 2004 Notal's revenues amounted to approximately $1.0 million, as compared to $0.9 million in 2003, and its net loss amounted to $1.6 million, the same as in 2003.

NetVision (a 46% holding as of December 31, 2004). NetVision provides Internet services and solutions in Israel. The other major shareholder of NetVision is our largest shareholder, DIC, which also holds 46% of NetVision, following DIC's purchase of NetVision shares from Tevel International Communications Ltd., or Tevel, in March 2004. In 2004 NetVision continues to experience increased competition in gaining broadband Internet services market share, resulting from the transition of customers to broadband Internet services. Nonetheless, NetVision revenues increased in 2004 by 7.6% to $70.5 million from $65.5 million in 2003 and its customer base at December 31, 2004 reached approximately 390,000 (of which approximately 225,000 were connected through broadband) compared to 341,000 at December 31, 2003 (of which approximately 146,000 were connected through broadband). NetVision's operating income increased by 47.2% to $7.3 million in 2004 compared to $5.0 million in 2003 and its net income increased to $4.3 million in 2004 compared to $1.0 million in 2003. NetVision's operating currency is the New Israeli Shekel (NIS) and accordingly, all figures above are translations for convenience purposes of NetVision's NIS figures into US dollars at the representative rate of exchange prevailing December 31, 2004 according to which $1.00 equaled NIS 4.308.

NetVision’s future period results will continue to be affected mainly by the highly competitive broadband market environment in Israel, and whether Internet access prices will continue to decrease or will stabilize.

On August 3, 2004, NetVision received a license from the Israeli Ministry of Communications to provide international telephony services, which NetVision commenced to provide through Voice over IP technology (VoIP) in the fourth quarter of 2004.

During 2004, we and DIC each granted NetVision a $5.3 million loan, in order to enable NetVision to repay its line of credit to one of its lending banks and to set up its international telephony services. As a result of the extension of the original repayment period of the loans and in accordance with EITF 02-18, we recorded a portion of the loan, in the amount of $2.0 million, as a loss, representing the funding of NetVision's previous years' losses.

On May 19, 2005, NetVision completed its initial public offering on the TASE in Israel of shares and convertible securities. We and DIC each converted approximately $3.1 million of loans into equity of NetVision immediately prior to the offering, and NetVision repaid the balance of the loans to us and DIC in the amount of $2.4 million each following completion of the offering (see under Item 4, Information on the Company). As of May 31, 2005, we held approximately 39% of NetVision**.**

Wavion (a 38% holding). Wavion is a developer of broadband wireless access systems for wireless LANs. Following a financing round led by Sequoia Seed Capital in which Wavion raised $12.5 million in the second half of 2003, Wavion directed resources away from its subcontracting activities to R&D activities, resulting in a decrease in revenues from subcontracting services in 2004 to $0.1 million compared to $1.8 million in 2003 and an increase in its net loss which amounted to $6.3 million in 2004 compared to $1.7 million in 2003.

ChipX (a 27% holding). ChipX is a manufacturer of late stage programmable application-specific integrated circuits, or structured ASICs. ChipX's revenues in 2004 increased by 18% to $16.2 million from $13.7 million in 2003, primarily due to the launch of new products and the recovery in the semiconductor industry, and its net loss in 2004 decreased to $5.6 million from $7.8 million in 2003. In March 2004, ChipX raised $12.0 million in a private placement, led by a new investor, Vantage Point Venture Partners, the proceeds of which are being used to finance its sales and marketing efforts and development investments in its structured ASIC technology.

Oren (a 41% holding as of December 31, 2004). On June 12, 2005, we sold all of our holdings in Oren (see item 4, Information on the Company). Oren is a developer of integrated circuits for digital broadcasting. In 2004, Oren’s revenues amounted to $3.1 million, compared to $4.4 million in 2003, mainly as a result of a decrease in product revenues due to delay in product development, and its net loss in 2004 amounted to $4.8 million compared to $4.6 million in 2003. In 2003, Oren completed an $8.0 million financing round from existing shareholders and from Zoran Corporation, the second strategic investor in Oren after Sony Corporation invested in April 2001. Zoran and Oren have agreed to cooperate to sell Oren’s front-end solution with Zoran’s back-end chips to major players in the digital television market.

AMT (a 40% holding). The AMT group develops technologies and products based on amorphous metals. AMT's two main operating subsidiaries are AHT, which uses amorphous metals for heating products, and ACS, which uses amorphous metals for identification, authentication and anti-shoplifting solutions. During 2004 AMT completed a private placement of $6.0 million, in which an international strategic partner invested $3.0 million and we invested an additional $3.0 million. AMT’s consolidated revenues in 2004 amounted to $2.6 million, compared to $1.3 million in 2003 and its net loss in 2004 amounted to $3.0 million, compared to $3.5 million in 2003.

We expect that most of our group companies will continue to recognize losses in future periods, as they invest significant resources in research and development and sales and marketing activities and have not yet generated significant revenues. Therefore, we anticipate that our share in the results of our group companies will continue to negatively affect our results of operations to the extent they are reported under the equity or consolidation method of accounting. In addition, following the sale of our holding in Elbit Systems in 2004 which positively contributed to our net income in previous periods, and in light of expected investments in new companies, to the extent they will be accounted for under the equity method of accounting, our share in the net losses of our group companies is expected to increase.

Results of operations of significant group companies which are accounted for other than under the equity method of accounting.

Partner (an 8.6% holding as of December 31, 2004). Our investment in Partner is accounted for as available-for-sale securities, and Partner's results do not affect our results of operations. Partner is a Global System for Mobile Communications, or GSM, mobile telephone network operator in Israel. At December 31, 2004, the market value of our investment in Partner amounted to approximately $136.2 million; however, as described under Item 4, Information on the Company, on April 20, 2005, we completed the sale to Partner of 12,765,190 Partner shares for approximately $94 million. As of May 31, 2005, following the sale, our beneficial holding in Partner was approximately 2% with a market value of approximately $25.8 million, almost all of which is subject to transfer restrictions under Partner's Israeli communications license but are no longer pledged.

The following are highlights of the results of operations of Partner for 2004 (all figures below are convenience translations of Partner's nominal New Israeli Shekel (NIS) figures into US dollars at the rate of the exchange prevailing at December 31, 2004 according to which $1.00 equaled NIS 4.308):

- Partner's revenues in 2004 increased to $1,193.3 million, up 15.1% from $1,037.1 million in 2003. The increase was mainly due to increased revenues from services (including data and content) and equipment. Partner's subscriber base at the end of 2004 was 2,340,000 as compared to 2,103,000 at the end of 2003. At the end of 2004 Partner launched its 3G network in the central part of Israel.
- Partner's operating income in 2004 increased to $236.6 million from $198.4 million in 2003, an increase of 19.2%. Operating income in 2004, as a percentage of revenues, increased to 19.8% versus 19.1% in 2003.
- Partner's income before tax in 2004 increased to $176.1 million from $122.9 million in 2003, an increase of 43.3%.
- Partner's net income in 2004 was $109.5 million, as compared to $269.9 million in 2003. The decrease in Partner's net income in 2004 resulted primarily from the utilization of its accumulated tax loss carry forward and the creation of deferred tax asset in 2003 in the amount of $146.9 million.

Jordan Valley (a 28% holding). Jordan Valley is engaged in developing solutions for advanced in-line thin film metrology for the semiconductor industry. Jordan Valley's revenues in

2004 increased to $8.3 million from $3.2 million in 2003, primarily due to the launch of new products for the semiconductor industry, and its net loss in 2004 decreased to $0.7 million from $2.5 million in 2003.

Impliant (a 28% holding). Impliant is engaged in the development of an innovative posterior motion preservation system for spine surgery and a line of cushion-bearing joint arthroplasty products. Impliant's net loss in 2004 amounted to $3.3 million, compared to $2.3 million in 2003, mainly as a result of increase in research and development expenses.

Gains from Disposals of Businesses and Affiliated companies and Changes in Holdings in Affiliated Companies. Our gains from disposals of businesses and affiliated companies and changes in holdings in affiliated companies amounted to $132.4 million in 2004 compared to $25.8 million in 2003.

The gain in 2004 consisted primarily from the following: (i) a $104.6 million gain (which after income taxes amounted to $91.5 million) resulting from the sale of our holding in Elbit Systems (we used Elbit Systems' unaudited financial report as of June 30, 2004 in order to record the carrying value of our investment in Elbit Systems as of the date of sale and to determine the gain resulting from the sale); (ii) a $15.2 million gain (which after minority interest and income taxes amounted to $6.7 million) resulting from the sale of 300,000 shares of Given Imaging by RDC and the decrease in our direct and indirect interest in Given Imaging following Given Imaging's secondary public offering; (iii) a $5.3 million gain from the sale of our share of KIT to a subsidiary of Laureate for a cash payment of $9.4 million (from which we received $5.7 million) and a potential future payment of up to an additional $10.0 million based on earnings of KIT in 2006 and 2007 (from which our share will be up to $5.7 million); (iv) a gain of $5.8 million (which after minority interest and income taxes amounted to $1.4 million) resulting from the sale of 200,000 shares of Given Imaging in connection with the purchase by RDC of treasury shares amounting to approximately 3% of its outstanding shares from one of its shareholders (a former senior executive of RDC) ; and (v) a gain of $0.6 million resulting from the exercise of a call option granted to the chairman of our board of directors to purchase 21,751 shares of Given Imaging for the aggregate exercise price of approximately $49,000.

The gain in 2003 was mainly due to the gain from the merger of the urology therapy business of Galil Medical and GE in the amount of approximately $21.2 million (which after minority interest and income taxes amounted to $4.4 million) and the $4.5 million gain from the sale of 753,600 shares of Given Imaging held by RDC for approximately $7.8 million and changes in holding in Given Imaging as a result of exercise of options.

Other Income (expenses), net. Other income, net, amounted to $4.7 million in 2004 compared to $14.6 million in 2003. The gain in 2004 included mainly a $5.4 million gain, before tax, from the sale of 854,701 shares of Zix (Nasdaq: ZIXI) which were received in consideration for ESW's assets and business sold to Zix in 2003, a $0.5 million loss representing the funding of 3DV's previous years' losses and $0.8 million write down of investment, mainly with respect to Textology.

The gain in 2003 resulted primarily from the following: (i) the sale of 6,278,226 Partner shares for approximately $29.3 million which resulted in a $11.1 million gain before tax; (ii) the sale of 1,117,155 shares of Zix for approximately $9.0 million which resulted in a $4.8 million gain before tax; and (iii) a $2.0 million gain, before tax, from the sale of all the shares of 24/7 Real Media shares (Nasdaq: TFSM) for approximately $5.2 million. These gains were partially offset by $3.7 million of write-downs mainly with respect to Cellenium and Textology.

Finance income, net. Finance income, net, amounted to $1.4 million in 2004 compared to $0.8 million in 2003. The increase in finance income was primarily due to the increase in cash balances following the completion of the sale of our holding in Elbit Systems for $196.6 million.

Expenses

Cost of revenues. Cost of revenues amounted to $6.3 million, compared to $5.6 million in 2003, which consisted primarily of expenses related to salaries, materials, subcontractors and hardware associated with delivering products and services of our subsidiaries, mainly Galil Medical, MediaGate, 3DV (the results of which have been consolidated since January 1, 2004) and SELA (the results of which have been consolidated since July 1, 2004).

Operating expenses. Operating expenses are comprised of research and development expenses, sales and marketing and general and administrative expenses of our subsidiaries, mainly Galil Medical, MediaGate, 3DV (the results of which have been consolidated since January 1, 2004) and SELA (the results of which have been consolidated since July 1, 2004), and of our and RDC's corporate operations. The following table sets forth the segment operating expenses. The operating expenses presented below for 2004 exclude impairment and amortization of other assets in the amount of $0.1 million ($0.3 million in 2003), which also constitute part of operating expenses under US GAAP but for presentation purposes is included as a separate item:

	Year ended December 31,	
	2004	2003
	(millions of $)	
Corporate……………	7.3	7.1
Galil Medical……….	2.8	10.7
SELA……………….	1.6	-
MediaGate………….	-	3.1
Starling……………..	1.6	-
3DV…………………	1.2	-
Other (mainly RDC)...	2.5	2.0
	17.0	22.9

Operating expenses of Galil Medical in 2004 decreased to $2.8 million from $10.7 million in 2003, resulting in operating loss of $0.1 million, compared to $7.6 million in 2003. The decrease in Galil Medical's operating expenses and operating loss was mainly due to the merger of the urology therapy units of Galil Medical and Amersham, which resulted in a significant decrease in Galil Medical's marketing and selling expenses. Galil started at the end of 2004 to develop its cryotherapy technology for application in the women's health field and its results of operations in 2005 will be affected by the increase in research and developments costs relating to the development of the new cryotherapy applications.

The decrease in MediaGate's operating expenses resulted from the sale of its assets and business to Telrad in January 2004, following which MediaGate ceased its operations.

SELA's operating expenses amounted to $2.9 million in 2004 (of which $1.6 million were incurred in the second half of 2004), compared to $2.4 million in 2003 and its net income amounted to $0.2 million, compared to $0.1 million.

Impairment. An impairment charge of $4.2 million ($2.7 million net of tax) was recorded with respect to future royalties to be received by MediaGate from Telrad in connection with the sale of MediaGate's business in January 2004 to Telrad. The write-off was due to our revised estimate about the realizability of future royalties. However, MediaGate's bank loan in the amount of approximately $2.6 million, which is secured by a first ranking pledge over these future royalties and which is not guaranteed by us, was not written-off even though it can only be repaid from royalties to be received from Telrad. This is in accordance with SFAS 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities - A Replacement of FASB Statement 125", which allows derecognition of a liability only if it has been extinguished, either through payment or when the debtor is legally released from being the primary obligor under the liability. We are currently holding discussions with the bank as to reaching an agreement that will legally release Mediagate from being the primary obligor under the loan. If and when the loan is extinguished, we could record a gain in the amount of the loan of up to approximately $2.6 million.

Income Taxes. Income taxes, net, in 2004 were $15.1 million, which included mainly $13.1 million of income taxes with respect to the gain resulted from the sale of our holdings in Elbit Systems (which includes an offset of $21.6 million due to the reduction in our valuation allowance with respect to previous years' losses), $6.7 million resulting from the secondary public offering of Given Imaging and the purchase of treasury stock in RDC in consideration for distribution of Given Imaging's shares and $1.8 million resulting from the sale of Zix shares. These amounts were offset primarily by a tax benefit in the amount of $2.9 million due to the change in the Israeli tax rate enacted in 2004, which gradually reduces the corporate tax rate in Israel from 36% in 2003 to 30% in 2007, a $2.4 million tax benefit with respect to corporate expenses, net and $1.5 million tax benefit related to the impairment of future royalties to be received by MediaGate from Telrad.

Income taxes, net, in 2003 were $6.8 million, which included mainly $7.0 million of income taxes with respect to the sale of shares of Partner, Given Imaging and 24/7 as well as with respect to the merger of the urology therapy units of Galil Medical and Amersham and a tax benefit of $1.7 million mainly with respect to corporate expenses, net.

Year Ended December 31, 2003 compared to Year Ended December 31, 2002

The following tables set forth our results of operations in the reported period:

	Year ended December 31,	
	2003	2002
	(millions of $, except per share data)	
Net loss	(7.2)	(41.6)
Net loss per share	(0.25)	(1.58)

Our net loss in 2003 decreased significantly as compared to the net loss in 2002 mainly as a result of the following factors:

(i) a gain, net after tax, of approximately $7.1 million, resulting from the sale of 6,278,226 Partner shares in 2003;
(ii) our share in the gain resulting from the merger in 2003 of the urology therapy units of Galil Medical and Amersham in the amount of approximately $4.4 million;
(iii) a gain of approximately $4.1 million resulting from the sale of substantially all of ESW assets and business to Zix in 2003 in consideration for 1,709,402 Zix shares and a $1.0 million convertible note and a gain, net after tax, of approximately $3.2 million resulting from the subsequent sale of 1,117,155 Zix shares, including 262,454 shares resulting from the conversion of the note; and
(iv) a decrease, net, of approximately $19.7 million in losses recorded with respect to our group companies, of which $12.7 million was due to a decrease in losses with respect to certain group companies which were sold or discontinued their operations in the second half of 2002 as part of the reorganization of Elron, Elbit, and DEP group companies following the completion of our merger with Elbit and the acquisition of DEP shares. The remainder of the decrease reflects the improvements in the results of operation of most of our group companies, mainly Given Imaging as a result of its revenue growth, and the decrease in the net losses of ESW (which business was sold on September 2, 2003) and Elron TeleSoft, as a result of restructuring and cost reduction programs undertaken by them.

Pro forma results. Pro forma net loss for 2002, which gives effect to the merger with Elbit, the share purchase of DEP and the acquisition of a controlling interest in Galil Medical and in MediaGate as if these transactions had been in effect at January 1, 2002, amounted to approximately $54.6 million, or $1.88 per share, compared to the net loss in 2003 of approximately $7.2 million, or $0.25 per share. The following factors contributed to the significant decrease in net loss:

(i) an increase in gains we recorded with respect to realization of investments by way of selling shares in the open market and by way of merger and acquisition transactions as mentioned above;
(ii) the decrease, net, in losses with respect to our group companies in the amount of $30.6 million, of which $20.9 million was due to a decrease in losses with respect to certain group companies which were sold or discontinued their operations in the second half of 2002 as part of the reorganization of Elron, Elbit, and DEP group companies following the completion of our merger with Elbit and the acquisition of DEP;
(iii) non-recurring merger expenses in the amount of $3.6 million which are reflected in the pro forma net loss in 2002; and
(iv) the corporate operating expenses in 2003 were lower by $0.9 million than the pro-forma corporate operating expenses in 2002.

Reportable Segments

Subsequent to the sale of ESW on September 2, 2003 our reportable segments are i) The Systems and Projects Segment - Elron TeleSoft; and ii) Other holdings and the corporate operations.. Prior to September 2, 2003, we operated indirectly through ESW in a third business segment – Internet Products – which has been reclassified as discontinued operations.

At December 31, 2003, the main group companies were classified into the following segments:

	Internet products (Discontinued operations)	Systems and projects	Other holdings and corporate operations
Consolidated	ESW	Elron TeleSoft	RDC; Galil Medical; MediaGate
Equity basis			Elbit Systems; NetVision; ChipX; Wavion; KIT; Pulsicom; Given Imaging; Witcom; 3DV; CellAct; AMT; Notal; Oren; Oncura
Marketable securities presented as available-for-sale			Partner; Elbit Vision System; Zix

The following tables reflect our consolidated data by reported segments:

	Internet products - Elron SW (Discontinued operations)	Systems and projects - Elron TeleSoft	Other holdings and corporate	Consolidated
	(millions of $)			
	Year ended December 31, 2003			
Income*…………………………	-	7.4	40.9	48.3
Costs and expenses………………	-	9.5	28.0	37.5
Loss from continuing operations...	-	(2.1)	(4.8)	(6.9)
Income (loss) from discontinued operations……………………...	(0.7)	-	0.5	0.2
Net loss…………………………..	(0.7)	(2.1)	(4.4)	(7.2)

	Internet products - Elron SW (Discontinued operations)	Systems and projects - Elron TeleSoft	Other holdings and corporate	Consolidated
	(millions of $)			
	Year ended December 31, 2002			
Income*………………………….	-	10.1	(13.0)	(2.9)
Costs and expenses………………	-	15.9	17.1	33.0
Loss from continuing operations...	-	(5.9)	(24.3)	(30.2)
Loss from discontinued operations	(8.6)	-	(2.8)	(11.4)
Net loss………………………....	(8.6)	(5.9)	(27.1)	(41.6)

* Income in the Other holdings and corporate operations includes net losses from equity investments

Internet Products - ESW – Discontinued operations

ESW, which was focused on web access control and e-mail content filtering for organizations, sold substantially all of its assets and business to Zix, and accordingly, its 2003 results of operations and the gain on the sale have been classified as discontinued operations and prior periods have been reclassified respectively.

The following table sets forth the composition of the discontinued operating of ESW:

	Year ended December 31,	
	2003	2002
	(millions of $)	
Gain (loss) from discontinued operations:		
Loss from operations.......................	(4.8)	(8.6)
Gain on disposal..............................	4.1	-
Loss from discontinued operations...	(0.7)	(8.6)

The decrease in loss from operations in the reported period was primarily due to a decrease in operating expenses as a result of restructuring and cost reduction programs implemented by ESW at the end of 2002 and at the beginning of 2003.

Systems and Projects - Elron TeleSoft

Elron TeleSoft is focused on telecommunications network management and revenue assurance products. The following table sets forth the operating results of Elron TeleSoft:

	Year ended December 31,	
	2003	2002
	(millions of $)	
Net revenues	7.4	10.1
Cost of revenues	4.6	8.0
Gross profit	2.8	2.1
Operating expenses*	2.6	4.3
Amortization of other assets	0.8	0.8
Restructuring charges, net	-	1.3
Operating loss	(0.6)	(4.3)
Finance expenses, net	1.5	1.5
Tax on income	-	0.1
Net loss	(2.1)	(5.9)

* Excluding amortization of other assets and restructuring charges, net, which are presented separately.

Net Revenues. Elron TeleSoft's net revenues in 2003 decreased by $2.7 million, or 27%, to $7.4 million, compared to $10.1 million in 2002, mainly as a result of the decrease in revenues derived from sale of third parties' products.

Cost of revenues. Cost of revenues of Elron TeleSoft in 2003 were $4.6 million, representing a gross margin of 38%, compared to $8.0 million in 2002, representing a gross margin of 21%. The increase in gross margins in 2003 is mainly due to change in revenue mix as revenues derived from Elron TeleSoft's products with higher gross margins increased relative to revenues derived from sale of third parties' products, as well as due to increased efficiency as a result of the restructuring programs implemented by Elron TeleSoft.

Operating loss. Elron TeleSoft's operating loss decreased by $3.7 million, or 86%, to $0.6 million in 2003, compared to $4.3 million in 2002. The decrease in operating loss, notwithstanding the decrease in revenues, was primarily due to the higher gross margin as well as the decrease in operating expenses as a result of restructuring and cost reduction programs implemented by Elron TeleSoft which enabled Elron TeleSoft to adjust its operating expenses to the decreased revenue levels.

Other Holdings and Corporate Operations Segment

The following table sets forth this segment's operating results:

	Year ended December 31,	
	2003	2002
	(millions of $)	
Net revenues	9.2	5.1
Net loss from equity investments	(8.7)	(24.2)
Gain from disposals of businesses and affiliated companies and changes in holdings in affiliated companies, net	25.8	6.9
Other income (expenses), net	14.6	(0.8)
Total income (loss)	40.9	(13.0)
Cost of revenues	5.6	2.7
Operating expenses*	22.9	15.3
Amortization of other assets	0.3	0.2
Restructuring charges, net	-	0.4
Finance income, net	(0.8)	(1.5)
Total costs and expenses	28.0	17.1
Income (loss) from continuing operations before tax benefit (taxes on income)	12.9	(30.1)
Tax benefit (taxes on income)	(6.8)	3.0
Minority interest	(10.9)	2.8
Loss from continuing operations	(4.8)	(24.3)
Gain (loss) from discontinued operations	0.4	(2.8)
Net loss	(4.4)	(27.1)

* Excluding amortization of other assets and restructuring charges, net, which are presented separately.

Income

Net revenues. Net revenues of the other holdings and corporate operations segment consisted of sales of products and services by our subsidiaries, Galil Medical and MediaGate, which were consolidated for the first time in the second half of 2002. The following table sets forth the segment revenues:

	Year ended December 31,	
	2003	2002
	(millions of $)	
Galil Medical*	7.6	3.0
MediaGate*	1.5	2.1
Other	0.1	-
	9.2	5.1

* Through June 30, 2002 the results of these companies were presented under the equity method.

Galil Medical recorded revenues of $7.6 million in 2003 compared to $5.0 million in 2002. The increase in revenues was mainly due to the growing awareness and acceptance of the cryotherapy technology by physicians and patients as an effective treatment for prostate cancer. Following the merger of the urology therapy units of Galil Medical and Amersham, Galil

Medical's revenues derived mainly from supplying of cryo products and R&D services to Oncura, in which it has a 25% ownership interest.

MediaGate's revenues from selling advanced messaging systems decreased to approximately $1.5 million in 2003 compared to $2.6 million in 2002 as a result of the slow adoption of advanced messaging technology by telecommunications operators as well as by the competition from more established companies in the market with larger resources, which led MediaGate to sell its technology and related intellectual property assets to Telrad at the beginning of 2003.

Share in net losses of affiliated companies

Our share in net losses of affiliated companies resulted from our holdings in certain investments that are accounted for under the equity method (see above under "Basis of Presentation"). The share in net losses of affiliated companies amounted to $8.7 million in 2003 compared to $24.2 million in 2002.

The decrease in our share in net losses of our affiliated companies in 2003, compared to 2002, resulted mainly from the following:

(i) Following the completion of the merger between Elron, Elbit and DEP, and subsequent to the acquisition of a controlling interest in MediaGate and in Galil Medical, we consolidated these companies' results of operations into our results of operations and ceased accounting for them under the equity method of accounting. Equity losses recorded in 2002 with respect to these companies for the period in which they were not consolidated amounted to $12.8 million.

(ii) The decrease in losses we recorded with respect to affiliated companies which were sold in the amount of $4.2 million and the decrease in our share in net losses of group companies whose results improved, mainly Given Imaging and Oren, in the amount of $1.5 million.

The above decrease was partially offset by a $2.6 million increase in our share in the losses of new group companies which are accounted under the equity method, mainly AMT, Notal Vision and Oncura.

Highlights of the Results of Operations of Our Major Affiliates (All percentages of holdings are shown as of December 31, 2003):

Elbit Systems (a 20% holding). Elbit Systems develops, manufactures and integrates advanced high-performance defense electronic systems. Our share in the net income of Elbit Systems amounted to $9.1 million in 2003, compared to $9.5 million in 2002.

The following are highlights of the results of operations of Elbit Systems:

- Elbit Systems' revenues increased in 2003 by 8.5% to $898.0 million from $827.5 million in 2002. The main increase in revenues was in the armored vehicles systems area of Elbit Systems' operation.
- As of December 31, 2003, Elbit Systems' backlog of orders was $1,752 million, of which approximately 80% is scheduled to be performed in 2004 and 2005. Elbit Systems' backlog of orders as of December 31, 2002 was $1,689 million.

- Elbit Systems' operating income in 2003 was $54.3 million (6% of revenues) compared to $57.8 million (7% of revenues) in 2002.
- Elbit Systems' net income in 2003 was $45.9 million (5.1% of revenues) compared to $45.1 million (5.5% of revenues) in 2002.

Given Imaging (a 17% holding directly and indirectly through RDC). Given Imaging recorded revenues of $40.5 million in 2003, an increase of 40.3% over the revenues recorded in 2002 of $28.9 million, and a gross profit of 66.6%, compared to 58.8% in 2002. Revenue growth was driven by continued installations of new systems, expansion in reimbursement coverage and the removal of the "adjunctive tool" qualifier from its label, enabling Given Imaging to market its product as a first line tool in diagnosing disorders of the small bowel. Given Imaging's net loss decreased in 2003 to $9.6 million, compared to $18.3 million in 2002, resulting mainly from increased revenues. In the fourth quarter of 2003, Given Imaging had sales of $12.5 million, a net loss of $0.6 million and positive cash flow for the first time in its history of $0.9 million.

Notal (a 24% holding). In January 2003, we completed a new investment of $2.0 million, out of $4.5 million raised by Notal. In 2003, Notal commenced selling its product pursuant to its distribution agreement with its strategic partner, Carl Zeiss Meditec Inc., one of the leading manufacturers of professional optics equipment, and recorded revenues of $0.9 million, and its net loss amounted to $1.6 million, consisting mainly of research and development costs.

Oncura (a 25% holding by Galil Medical). Oncura commenced its operations on July 1, 2003 following the completion of the merger of the urology therapy units of Galil Medical and Amersham which created Oncura. Oncura's revenues since commencing operations and through December 31, 2003, amounted to $31.4 million. Oncura's net loss amounted to $0.9 million, which resulted primarily from integration costs arising from combining the urology units of Amersham and Galil Medical and amortization of intangible assets.

NetVision (a 46% holding). In 2003 NetVision changed its operating currency to NIS. Accordingly, all figures below are translations for convenience purposes of NetVision's NIS figures into U.S. dollars at the representative rate of exchange prevailing at December 31, 2003 according to which $1.00 equaled NIS 4.379.

In 2003, NetVision experienced increased competition in gaining broadband communication market share resulting from the transition of customers to broadband communication from narrow-band dial-up connections. Nevertheless, NetVision recorded an increase of 8% in revenues to $64.6 million, from $59.8 million in 2002 and its operating income increased to $4.7 million, compared to $3.4 million in 2002. However, due to higher finance expenses in 2003, NetVision's net income decreased to $0.8 million compared to $2.9 million in 2002. As of December 31, 2003, NetVision had a customer base of approximately 357,000 compared to 340,000 at the end of 2002.

Wavion (a 38% holding). In 2002, as a result of the downturn in the broadband wireless communications market, which delayed the release of Wavion's products, Wavion significantly reduced its research and development expenses and began to sell subcontracting services for the development of wireless sub-systems. In 2003, Wavion completed a financing round led by Sequoia Seed Capital, raising $12.5 million out of which we invested $3 million, and subsequently directed resources away from its subcontracting activities and its revenues in 2003 amounted to $1.8 million, similar to revenues recorded in 2002 of $1.7 million. The increase in its research and development costs resulted in an increase in Wavion's net loss which amounted to $1.7 million in 2003, compared to a net loss of $0.6 million in 2002.

KIT (a 45% holding). In 2003 we invested $2.0 million in KIT (formerly Kidum Holding B.V) as part of an aggregate investment round of $4.0 million, the balance of which was invested by DIC, which then held approximately 38.5% of our shares. KIT was previously the operating subsidiary of Kidum Elron IT Ltd., or Kidum Elron in which we held approximately 29%.

KIT's revenues increased in 2003 by 106% to $7.0 million, compared to $3.4 million in 2002, as a result of the increase in student enrollments. KIT's operating loss decreased to $3.3 million compared to $6.1 million in 2002, primarily due to the increase in revenues. At December 31, 2003, KIT had approximately 1,700 students, mainly from the United Kingdom, Holland, Canada, Germany, China and Singapore, as compared to approximately 1,100 students at the end of 2002. In the first quarter of 2004, we sold our shares in KIT to a subsidiary of Laureate. (See Item 4, "Information on the Company").

ChipX (formerly Chip Express) (a 36% holding). ChipX's revenues in 2003 amounted to $13.7 million, compared to $16.5 million in 2002. The decrease in revenues resulted mainly from the slowdown in the semiconductor industry through the first half of 2003. In light of the recovery in this industry in the second half of 2003, ChipX revenues increased to $7.4 million during the second half of 2003, as compared to $6.4 million in the first half of 2003 and $6.6 million in the second half of 2002. ChipX's net loss in 2003 amounted to $7.8 million, compared to $6.4 million in 2002. However, as a result of an increase in revenues during the second half of 2003, ChipX's net loss decreased to $3.2 million as compared to $4.6 million in the first half of 2003 and $4.7 million in the second half of 2002.

Oren (a 41% holding). In 2003, Oren's revenues increased to $4.4 million from $2.0 million in 2002, due to a combined increase in product sales as well as in revenues derived from development projects. As a result of the increased revenues, Oren's net loss in 2003 decreased to $4.6 million compared to $6.1 million in 2002.

AMT (a 28% holding). Since our investment in AMT in August 2002, AMT's two operating companies, namely AHT and ACS, commenced introducing their amorphous metals technology-based products to the market and built up their operating and manufacturing infrastructure. AMT's consolidated revenues in 2003 amounted to $1.3 million compared to $0.3 million in 2002 and its net loss in 2003 amounted to $3.5 million compared to $4.3 million in 2002.

Results of operations of significant group companies which are accounted for other than under the equity method of accounting

Partner (a 9% holding). At December 31, 2003, the market value (equal to its carrying value) of our investment in Partner amounted to $124.3 million. In 2002, Partner reached a significant milestone, as it became a profitable company and generated cash flow. In 2003, Partner continued to improve its financial performance and demonstrate its ability to sustain revenue growth, profitability and positive cash flow. The following are highlights of the results of operations of Partner for 2003 (all figures below are convenience translations of Partner's nominal New Israeli Shekel (NIS) figures into U.S. dollars at the rate of the exchange prevailing at December 31, 2003 according to which $1.00 equaled NIS 4.379):

- Partner's revenues in 2003, driven primarily by subscriber growth of 14.5%, increased to $1,020.3 million, up 10.2% from $925.9 million in 2002. Partner's subscriber base at the end of 2003 was 2,103,000 as compared to 1,837,000 at the end of 2002.
- Partner's operating income in 2003 increased to $195.2 million from $121.8 million in 2002, an increase of 60.3%. Operating income in 2003, as a percentage of revenues, increased to 19.1% versus 13.2% in 2002.
- Partner's net income in 2003 was $265.5 million, which include a $144.6 million tax benefit resulting from its accumulated carryforward taxes losses. In 2002, Partner's net income was $19.2 million.

As of December 31, 2003, Partner had a line of credit agreement with a consortium of banks that provided for borrowings of up to $683 million of which $282 million had been drawn. The line of credit was guaranteed by shares held by the original shareholders of Partner, pro rata to their respective original holdings. All of the shares held by us as of December 31, 2003, amounting to approximately 15.9 million shares, were pledged by us in favor of the consortium of banks. On April 20, 2005, we completed the sale to Partner of 12,765,190 shares and the remaining shares are no longer pledged (see Item 4 – Information on the Company").

Gains from Disposals of Businesses and Affiliated companies and Changes in Holdings in Affiliated Companies

Our gains from disposals of businesses and affiliated companies and changes in holdings in affiliated companies amounted to $25.8 million in 2003 compared to $6.9 million in 2002. The gain in 2003 was mainly due to the gain from the merger of the urology therapy business of Galil Medical and Amersham in the amount of approximately $21.2 million (which after minority interest and income taxes amounted to $4.4 million) and $4.5 million gain from the sale of 753,600 shares of Given Imaging held by RDC for approximately $7.8 million and changes in holding in Given Imaging as a result of exercise of options.

The gain in the comparable period in 2002 was mainly due to a $5.3 million gain from the sale of Given Imaging shares and a $1.6 million gain from the sale of 380,000 shares of Elbit Systems.

Other Income (expenses), net. Other income, net, amounted to $14.6 million in 2003 compared to an expense of $0.8 million in 2002. The increase in 2003 resulted primarily from the following: (i) the sale of 6,278,226 Partner shares for approximately $29.3 million which resulted in a $11.1 million gain before tax; (ii) the sale of 1,117,155 shares of Zix for approximately $9.0 million which resulted in a $4.8 million gain before tax; and (iii) a $2.0 million gain, before tax, from the sale of all the shares of 24/7 for approximately $5.2 million. These gains were partially offset by $3.7 million of write-downs, mainly with respect to Cellenium and Textology.

Other expenses in 2002 resulted mainly from a $1.6 million write-downs of certain investments as well as a decrease in the market value of certain marketable securities, which were partially offset by $0.7 million gain from the sale of other marketable securities, primarily of NetManage Inc. (Nasdaq: NETM) held by us at that time.

Expenses

Operating expenses. Operating expenses were comprised of research and development expenses, sales and marketing and general and administrative expenses of our subsidiaries, mainly Galil Medical and MediaGate, which were consolidated for the first time in the second half of 2002 as well as our and RDC's corporate operations expenses. The following table sets forth the segment operating expenses. The operating expenses presented below exclude restructuring expenses and amortization of other assets, in the amount of $0.3 million in 2003, and $0.6 million in 2002, which also constitute part of operating expenses under US GAAP but for presentation purposes, are included as a separate item:

	Year ended December 31,	
	2003	2002
	(millions of $)	
Corporate...............	7.1	6.1
Galil Medical*.......	10.7	7.4
MediaGate*............	3.1	1.8
Other......................	2.0	-
	22.9	15.3

* In the first half of 2002, the company's results were presented under the equity method.

Our corporate operating costs, which following the merger with Elbit in May 2002 represent the costs of the combined management, were $7.1 million in 2003, compared to $6.1 million in 2002. The increase in the corporate costs resulted mainly from the increase in costs related to the company's employee stock option plans and insurance costs. With respect to employee stock options granted in 2003, we adopted FASB Statement No.123 "Accounting for Stock-Based Compensation", according to which compensation expenses are measured under fair value method (instead of intrinsic value method) using the Black & Scholes option-pricing model. Amortization of deferred stock compensation amounted in 2003 to $0.4 million compared to $0.2 million in 2002.

Operating expenses of Galil Medical in 2003 were $10.7 million compared to $13.0 million in 2002. Operating expenses in 2003 included approximately $1.2 million of non-recurring costs related to the merger of the urology therapy units of Galil Medical and Amersham. Galil Medical's operating loss in 2003 decreased to $7.6 million compared to $9.8 million in 2002 mainly as a result of the merger of the urology therapy units of Galil Medical and Amersham which resulted in a significant decrease in marketing and selling expenses.

Operating expenses of MediaGate in 2003 were $3.1 million compared to $4.2 million in 2002. MediaGate's operating loss in 2003 amounted to $2.4 million compared to $3.6 million in 2002. The decrease in the operating loss of MediaGate resulted primarily from the decrease in operating expenses due to cost reduction programs implemented by MediaGate during 2002 and 2003. Following the sale of MediaGate's assets and intellectual property to Telrad, Mediagate ceased its operations.

Other operating expenses include mainly the operating expenses of RDC. At the end of 2003, RDC launched a new company, Starling, in which RDC and Elbit Systems held 50% each. Starling's research and development costs were included through its incorporation in RDC's results of operations.

Income Taxes. Income taxes, net, in 2003 were $6.8 million, which were mainly due to income taxes with respect to the sale of shares of Partner, Given Imaging, Zix and 24/7, as well as with respect to the merger of the urology therapy units of Galil Medical and Amersham. In 2002, we recorded a tax benefit of $3.0 million mainly with respect to corporate expenses.

Loss from Discontinued Operations. Loss from discontinued operations of $2.8 million in 2002 was mainly with respect to our subsidiary, Elbit VFlash which sold substantially all of its assets and business to 24/7 in exchange for shares of 24/7, resulting in a gain of $2.0 million which was partially offset by the results of operations of Elbit VFlash in the amount of $1.9 million. Also included in this item are the net losses of other subsidiaries which were sold, such as Textology, in the aggregate amount of $2.9 million.

B. Liquidity and Capital Resources

Consolidated cash, debentures and deposits at December 31, 2004 were approximately $188.6 million compared with $114.6 million at December 31, 2003. At December 31, 2004, the corporate cash, debentures and deposits were $175.7 million compared with $107.3 million at December 31, 2003. The increase in consolidated and corporate cash and other liquid instruments resulted primarily from the sale of our holding in Elbit Systems for approximately $196.6 million. This increase was offset mainly by the repayment of approximately $67.8 million of loans of Elron Telesoft and ESW and investments in and loans to new and existing companies in the aggregate amount of $74.8 million. As of December 31, 2004, total bank loans which were guaranteed by us amounted to $1.7 million, consisting of bank loans granted to Elron TeleSoft, as compared to $67.5 million at December 31, 2003 (which consisted of bank loans granted to Elron TeleSoft and ESW).

The main sources of corporate cash and other liquid instruments in 2004, were approximately $196.6 million of proceeds from the sale of all of our shares in Elbit Systems, $5.7 million of proceeds from the sale of all of our shares in KIT eLearning, $8.1 million proceeds from the sale of Zix shares and a $1.7 million dividend received from Elbit Systems prior to the sale of our holding.

The main uses of corporate cash and other liquid instruments in 2004, were the $67.8 million repayment of bank loans and $74.8 million of investments in and loans to existing and new group companies. The following table sets forth investments and loans made during 2004 by Elron (in millions of $):

Given Imaging……………………….	43.9
Impliant………………………………	7.3
Jordan Valley………………………...	6.7
NetVision*…………………………...	5.3
AMT…………………………………	3.4
ChipX………………………………..	2.6
Starling**…………………………….	1.5
Galil Medical(*)(**)…………………	1.0
Innomed……………………………...	1.0
Oren*…………………………………	0.8
3DV*…………………………………	0.7
Notal………………………………….	0.4
Other*………………………………..	0.2
	74.8

* loans

**Subsidiaries of the company. Cash invested in subsidiaries does not constitute a cash outflow in the consolidated financial statements.

Consolidated working capital at December 31, 2004 amounted to $158.8 million compared to $57.0 million at December 31, 2003. The increase is due primarily to the proceeds received from the sale of our shares in Elbit Systems.

Consolidated loans at December 31, 2004, were approximately $9.1 million, of which $1.7 million was attributed to Elron TeleSoft, compared to $73.2 million at December 31, 2003, of which $67.5 million were attributed to Elron Telesoft and ESW. During 2004 we repaid Elron TeleSoft's and ESW's loans to the lending banks in the amount of approximately $67.8 million. As a result of the repayment of the loans, the line of credit of ESW was closed and the line of credit of Elron TeleSoft was reduced from $53.6 million at December 31, 2003, to $2.7 million (of which $1.7 million was drawn as of December 31, 2004). Elron TeleSoft's lines of credit are guaranteed to the banks by us. In addition, we have provided to a certain lending bank a comfort letter pursuant to which we undertook not to reduce our holding in Elron Telesoft below a certain percentage.

MediaGate's bank loan in the amount of approximately $2.6 million has been secured by a first ranking pledge over the future proceeds to be received as royalties as a consideration for the sale of its technology to Telrad. The loan is not guaranteed by us. We are currently discussing with the bank ways to release Mediagate from the loan.

Following the sale of Partner shares on April 20, 2005, as described under Item 4, "Information on the Company", the majority of the remaining Partner shares held by us, amounting to approximately 3.1 million shares, are subject to certain transfer restrictions under Partner's Israeli communications license but are no longer pledged to Partner's lending banks.

Subsequent to December 31, 2004 and through May 31, 2005 we have invested an additional aggregate amount of approximately $22.5 million, including mainly a $16 million investment in Teledata (see Item 4, " Information on the Company").

The corporate cash, debentures and deposits as of May 31, 2005 amounted to approximately $230 million.

Our investment policy for managing our funds is in general to invest in time deposits and U.S. government securities with high liquidity.

We believe that our existing capital will be sufficient to fund our and our subsidiaries' operations and our investment plan in existing and new companies for at least the next twelve months.

Shareholders' equity at December 31, 2004, was approximately $389.1 million representing approximately 78% of our total assets compared with $296.1 million representing approximately 66% of total assets at December 31, 2003.

Market Risk

Market risks relating to our operations result primarily from changes in interest rates, exchange rates and equity prices. In order to limit our exposure, we may enter, from time to time, into various derivative transactions. Our objective is to reduce exposure and fluctuations in earnings and cash flows associated with changes in interest rates, foreign currency rates and equity prices. We do not use financial instruments for trading purposes. It is our policy and practice to use derivative financial instruments only to limit exposure. As part of this policy, in February 2005, we hedged the dollar value to be received from the sale of our shares in Partner by the purchase of call options and by selling put options, at a dollar/NIS exchange rate ranging from $4.36 to $4.44 for a period of 81 days.

Interest Rate Risks. We are exposed to market risks resulting from changes in interest rates, relating primarily to our debentures and deposits. We do not use derivative financial instruments to limit exposure to interest rate risk. At December 31, 2004, all of our deposits and debentures were fixed rate based with a weighted average rate of approximately 2.4% and a weighted average maturity of approximately one year.

Exchange Rate Risk. Since most of our group companies are Israeli-related, our main exposure, if any, results from changes in the exchange rate between the New Israeli Shekel and the U.S. dollar. Our functional currency, as well as that of our principal subsidiaries and affiliated companies, is the U.S. dollar. Our policy is to reduce exposure to exchange rate fluctuations by having most of our and our subsidiaries' assets and liabilities, as well as most of the revenues and expenditures in U.S. dollars, or U.S. dollar linked. Therefore, we believe that the potential loss that would result from an increase or decrease in the exchange rate is immaterial to our business and net assets. In order to hedge the dollar value that was received from the sale of our shares in Partner, in February 2005, we purchased call options and sold put options, at a dollar/NIS exchange rate ranging from $4.36 to $4.44. The hedge transaction resulted with no material effect on our cash resources.

Equity Price Risk. We are exposed to fluctuations in the equity price of our holdings in publicly traded companies. At December 31, 2004 we directly and indirectly held shares of the following publicly traded companies: Given Imaging, Partner and Elbit Vision Systems Ltd. Stock prices in the industries of these companies, and of these companies themselves, have experienced significant historical volatility. Changes in the market value of our publicly traded holdings, including holdings through our affiliates, which are accounted under the equity method of accounting or as available-for-sale securities will not affect our results of operations but may have a significant effect on our market value. We view the risks of reduction in market price of these companies as part of our business risks and we examine, from time to time, the possibility of having a partial hedge against equity price risks. Based on closing market prices at December 31, 2004, the fair market value of our holdings in public securities was approximately $383.0 million, of which approximately $110 million was attributed to Partner shares which were sold on April 20, 2005 for approximately $94 million (see under Item 4, "Information on the Company"). At December 31, 2004 no financial instruments were used to hedge against equity price fluctuations.

Changes in the market value of our available-for-sale securities (Partner and EVS) are reported in other comprehensive income, which is included as a component of shareholders' equity, and not as part of our results of operations. The market value of our available-for-sale securities as of December 31, 2004 amounted to $137.2 million.

C. Research and Development

Since we, through our group companies, engage in fields of high-technology, our group companies invest significant resources in research and development ("R&D") activities.

The combined R&D costs of all group companies amounted to $58.1 million in 2004, $85.1 million in 2003 and $99.1 million in 2002, the majority of which (in each year) was spent by Elbit Systems. The decrease in R&D costs in 2004 as compared to 2003 was primarily due to the sale or discontinued operations of some of our group companies during 2003 and 2004 (mainly Elbit Systems in July 2004, ESW and MediaGate), which was partially set off by an increase in R&D expenses in some of our group companies (mainly Wavion, Starling and ChipX). The decrease in research and development costs in 2003 as compared to 2002 was primarily due to the decrease in R&D expenses in some of our group companies (mainly Elbit Systems, Given Imaging and Elron TeleSoft) and the sale or discontinued operations of some of our group companies during 2002 and 2003.

Our consolidated research and development costs, incurred mainly by Elron TeleSoft, Galil Medical, Starling and 3DV, amounted to $3.7 million, $3.8 million and $3.4 million in 2004, 2003 and 2002, respectively.

Elron TeleSoft's research and development team's efforts are currently primarily directed toward its main product line of revenue assurance products (ESSB).

Following the completion of the merger of Galil Medical's urology business with Amersham's brachytherapy business, Galil Medical's R&D team continues to support the urology business and is now focused on the application of its cryotherapy technology in the women's health field such as uterine fibroids, and breast fibro adenoma.

D. Trend Information

"Trend Information" pertaining to our group companies and us is incorporated by reference to Item 4, "Information on the Company" of this Report and this Item 5 under "Results of Operations".

E. Off Balance Sheet Arrangements

There is no principal amount of off balance sheet transactions.

F. Tabular Disclosure of Financial Obligations

At December 31, 2004, we and our subsidiaries had no material contractual obligations which are expected to affect our consolidated cash flow in future periods, except for lease obligations and payments of bank credits, bank loans and loans from others, including short term loans taken by our subsidiaries, in each case due in future periods as set forth in the table below (in million of $):

Type of Obligation	2005	2006	2007	2008	With no specified maturity date	Total
Loans from banks	2.9	0.1	-	-	2.6	5.6
Loans from other	2.2	1.3	-	-		3.5
Leases	0.6	0.5	0.3	0.2	-	1.6

For additional details, see Item 5, Liquidity and Capital Resources.

Item 6. Directors, Senior Management and Employees

A. Directors and Senior Management

Our executive officers and directors are as follows:

Name	Age	Position
Ami Erel (4)	58	Chairman of the Board of Directors
Avraham Asheri (1)	67	Director
Dr. Gabi Barbash	55	Director
Prof. Yair Be'ery	48	Director
Nochi Dankner(4) (5)	50	Director
Avraham Fischer(4)	48	Director
Yaacov Goldman (1)(2)(3)	49	External Director
Zehavit Joseph(4)	41	Director
Oren Lieder(4)	56	Director
Shay Livnat(4) (5)	46	Director
Dori Manor(4) (5)	38	Director
Professor Daniel Sipper(1)(2)	72	External Director

Doron Birger	54	President and CEO
Moshe Fourier	57	Vice President, Chief Technology Officer
Tal Raz	43	Vice President, Chief Financial Officer
Shmuel Kidron	55	Vice President
Avishai Friedman	39	Vice President, Business Development
Assaf Topaz [(6)]	35	Vice President

1. Member of our audit committee.
2. External director under the Israeli Companies Law.
3. Designated Financial Expert under Sarbanes-Oxley Act of 2002.
4. Director or Officer of IDBH, IDBD and/or DIC.
5. See Item 7A – "Major Shareholders".
6. Assaf Topaz is the husband of Michal Topaz, daughter of Ruth and Isaac Manor. See Item 7A – "Major Shareholders."

Avraham Asheri joined Elron as a director in December 1999. He serves as the Chairman of the Company's Audit Committee. He is an economic and financial advisor. Mr. Asheri is a member of the boards of directors of Discount Mortgage Bank Ltd., Kardan Nadlan Ltd., Africa Israel Investments Ltd., Elbit Systems Ltd. and Scitex Corporation Ltd. Mr. Asheri was the President and Chief Executive Officer of Israel Discount Bank from November 1991 until July 1998. Prior to joining Israel Discount Bank in 1983 as Senior Executive Vice President and a member of its management committee, Mr. Asheri held the position of Director General of the Ministry of Industry and Trade. During his 23 years at the Ministry of Industry and Trade and at the Ministry of Finance, Mr. Asheri held several key offices in Israel and abroad, including: Managing Director of the Investment Center in Israel, and Trade Commissioner of Israel to the United States. Mr. Asheri holds a bachelors degree in economics and political science from the Hebrew University in Jerusalem.

Ami Erel has served as the Chairman of the Board of Directors of Elron since November 1999 and served as the Company's Chief Executive Officer from November 1999 to December 2001. Mr. Erel has served as President and Chief Executive Officer of DIC since June 1, 2001. Mr. Erel is also Chairman of the board of directors of Scitex Corporation Ltd. and serves as a director of Property and Building Corporation Ltd., Super-Sol Ltd. and Ham-let (Israel Canada) Ltd. Mr Erel also serves as the Chairman or a member of the boards of various other subsidiaries and affiliates of DIC and Elron. From 1997 to 1999, Mr. Erel served as President and Chief Executive Officer of Bezeq-The Israel Telecommunications Corp. Ltd. From 1997 to 1998, he was Chairman of the board of directors of PelePhone Communications Ltd. From January 2000 to January 2004, Mr. Erel served as Chairman of the Board of Israel Association of Electronics & Information Industries. Mr. Erel holds a B.Sc. in electrical engineering from the Technion, Israel Institute of Technology.

Prof. Gabi Barbash joined Elron as a director in May 2003. Since 1999, Prof. Barbash has been Director General of the Tel-Aviv Sourasky Medical Center and between 2000 and 2003 he served as Chairman of the Board of Directors of Teuza Venture Capital Fund. Between 1998 and 2000, Prof. Barbash was the Chairman of the Israeli National Transplant Center. Between 1996 and 1999, Prof. Barbash was the Director General of the Israeli Ministry of Health. Between 1995 and 1998, Prof. Barbash was a member of the Scientific Committee of the Interdisciplinary Center for Technological Analysis and Forecasting at Tel-Aviv University. Between 1993 and 1996, Prof. Barbash was the Director General of the Sourasky Medical Center. Between 1986 and 1993, Prof. Barbash was the Deputy Director of the Sheba Medical Center and from 1990 to 1993, he was Director of the Rehabilitation Hospital of the Sheba Medical Center. Prof. Barbash holds an M.D. degree from the Hebrew University, Jerusalem, Hadassah Medical School and a masters degree in public health from Harvard University.

Prof. Yair Be'ery joined Elron as a director in January 2004. Since 1985, Prof. Be'ery has been with the Department of Electrical Engineering at Tel Aviv University and served as its Chairman from 1999 until 2003. From 1998 until 2005, Prof. Be'ery worked with Benny Steinmetz's Group and co-founded STI Ventures, a high technology venture investment company. From 1989 until 1996, Prof. Be'ery served as Vice President of Advanced Technology of the DSP Group Inc. Prof. Be'ery serves as a member of the board of directors of Teledata, one of our group companies. Prof. Be'ery is also a member of the advisory boards of ChipX, Inc., Tehuti Networks Ltd. and Mplicity Ltd. Prof. Be'ery served previously on the boards of directors and advisory boards of numerous Israel-related technology companies. Prof. Be'ery holds B.Sc., M.Sc. and Ph.D. degrees (Electrical Engineering) from Tel Aviv University, Israel.

Nochi Dankner joined Elron as a director in June 2005. Mr. Dankner is the Chief Executive Officer and Chairman of the board of directors of IDBH and serves as Chairman of the board of directors of IDBD, DIC and Clal Industries and Investments Ltd. Mr. Dankner is the founder of the Ganden Group and serves as a director of companies in the Ganden Group which holds investments in companies operating primarily in the fields of real estate, tourism and technologies, including as Chairman of Ganden Holdings Ltd. and Ganden Investments (2000) Ltd. and as Co-Chairman of Ganden Tourism and Aviation Ltd. and Israir Ltd. In addition, Mr. Dankner serves as a director of Clal Insurance Company Ltd., Nesher-Israeli Cement Enterprises Ltd., Property and Building Corporation Ltd., Azorim Investments, Development and Construction Company Ltd., Super-Sol Ltd. and other public and private companies in the IDB group. Mr. Dankner is Chairman of the IDB Fund "For the Community" and is a member of "Matan - Your Way to Give", a non-profit organization. Mr. Dankner also serves as a member of the Board of Governors of Ichilov Hospital, as a member of the Board of Trustees of the Tel Aviv University. Mr. Dankner holds an LL.B. degree from the Tel Aviv University and a Bachelor of Arts degree in Political Science from Tel Aviv University.

Avraham Fischer joined Elron as a director in August 2003. He is the Executive Vice President of IDBH, the deputy Chairman of IDBD, Co-Chief Executive Officer of Clal Industries and Investments Ltd. and Chairman of Clal Biotechnology Industries Ltd. In addition, he is a partner of Fischer, Behar, Chen & Co., a leading Israeli law firm. Mr. Fischer is the co-founder and co-Chairman of Ganden Tourism and Aviation Ltd., a company holding investments in Israeli companies, operating primarily in the field of tourism, and is the co-founder and Vice-Chairman of Ganden Holdings Ltd., a company holding investments in companies operating primarily in the fields of real estate and technologies. He serves as a director of Clal Industries & Investments Ltd., DIC, Scitex Corporation Ltd., ECI Telecom Ltd., American Israeli Paper Mills Ltd., Vyyo Inc. and several other companies. Mr. Fischer is a co-chairman of "Matan – Your

Way to Give", a non-profit organization. Mr. Fischer holds an LL.B. degree from the Tel Aviv University and is a member of the Israeli bar association.

Yaacov Goldman joined Elron as an external director in March 2003. He serves as a member of our Audit Committee and is our designated financial expert on the audit committee. Mr. Goldman also serves as a director of Bank Leumi Le'Israel B.M., Mer Telemanagement Solutions Ltd. and Golden House Ltd. Mr. Goldman serves as the Professional Secretary of the Peer Review Institute of the Certified Public Accountants Institute in Israel. Commencing in 1981 Mr. Goldman worked for Kesselman & Kesselman (member firm of PriceWaterhouseCoopers) for 19 years, and from 1991 until 2000, as a partner and then senior partner of such firm. From September 2000 until November 2001, Mr. Goldman served as managing director of Argoquest Holdings, LLC. From March 2002 until October 2002, Mr. Goldman acted as a consultant to a private equity initiative with Poalim Capital Markets & Investments Ltd. Mr. Goldman is a certified public accountant in Israel, having received his Bachelor of Economics and Accounting from the Tel Aviv University.

Zehavit Joseph joined Elron as a director in June 2005 and has been the Executive Vice President and Chief Financial Officer of IDBD and Chief Financial Officer of IDBH, since 1998. Since 1998, Ms. Joseph has been a Senior Fellow of Finance and Accounting at the Wharton School, Philadelphia. From 1996 to 1998, Ms. Joseph was a management consultant at ZHM Corporation in New York. From 1990 to 1996, Ms. Joseph held the position of Vice-President, Treasury at Chase Manhattan Bank, New York. From 1989 to 1990, Ms. Joseph worked as the Manager, Mergers and Acquisitions, at Coopers and Lybrand, New York. Ms. Joseph is a member of various non-profit organizations and is member of the Israeli CFO Forum Steering Committee, Chairman of the CFO Reporting Committee and member of the Audit Committee of The College of Management Academic Studies. Ms. Joseph holds a Doctorate degree from The Wharton School, University of Pennsylvania and Lasalle University, a Masters in Business Administration degree from the Katz School of Business, University of Pittsburgh and a Bachelor of Arts degree in Accounting from the School of Business, Duquesne University.

Oren Lieder joined Elron as a director in January 2003. Since January 2003, he has been the Chief Financial Officer of DIC. Prior to joining DIC, from 1997 until 2002, Mr. Lieder was the Chief Financial Officer of Bezeq and from 1989 until 1996, he was the Chief Financial Officer of Zim Israel Navigation Co. Ltd. He is a director and chairman of the audit committe of Super-Sol Ltd., Property and Building Corporation Ltd. and American-Israeli Paper Mills Ltd., NetVision, Scitex Vision Ltd. and other companies of the IDB group of companies. Between 2000 and 2002, Mr. Lieder was a director of DBS Satellite Services (1998) Ltd. and between 1998 and 2002, he was a director of Pelephone Communications Ltd. Between 1994 and 1996, he was the Chairman of Ramon–Granit Insurance Brokers, Ramon International Insurance Brokers and Layam Ltd. Since 1995, he has been a member of the Board of Trustees and Investment Committee of the University of Haifa. Mr. Lieder holds a degree in economics and statistics from the University of Haifa.

Shay Livnat joined Elron as a director in June 2005 and is the founder, President & Chief Executive Officer of Zoe Holdings Ltd. He is also the founder and co-chairman of UPS Israel and UTI (Isuzu) Israel. Since 2004, Mr. Livnat has been a director of IDBD, Clal Industries and Investments Ltd., Clal, Scitex Corporation Ltd. and Scitex Vision Ltd. Since 1992, Mr Livnat has been a director of Taavura Holdings Ltd. Between 1988 and 1998, Mr. Livnat was the Managing Director of Tashtit Ltd (DAF, Liebherr) and Vice-President of the Taavura Group. Mr. Livnat holds a Bachelor of Science in Electrical Engineering, Fairleigh Dickinson University.

Dori Manor joined Elron as a director in August 2003. He has served as Chief Executive Officer of David Lubinski Ltd., a group of automotive companies, since 2000, and was the Vice President from 1997 until 2000 and Assistant Director from 1994 until 1996. During 1994 and 1995, he served as a director of Morasco Ltd. During 1992 and 1993, he was engaged as an Industrial Engineering consultant for Factory Design Ltd. Mr. Manor serves as a director of IDBH, IDBD, DIC and Clal Industries and Investments Ltd. Mr. Manor received an MBA degree from the European Institute of Business Administration (INSEAD) in Fontainebleau, France, in 1996 and a Bachelor of Science degree in Industrial Engineering from Tel Aviv University in 1993.

Professor Daniel Sipper joined Elron as an external director in February 2001. Professor Sipper serves on our Audit Committee. Professor Sipper serves in the faculty of the Department of Industrial Engineering at Tel-Aviv University. He received his bachelor of science from the Technion, Israel Institute of Technology, a masters of science degree from Columbia University and a Ph.D. in Industrial Engineering from the Georgia Institute of Technology.

Doron Birger joined Elron in 1994 as Vice President of Finance. Mr. Birger has served as President and Chief Executive Officer of Elron since August 2002, President since September 2001, Chief Financial Officer from 1994 to May 2002 and Corporate Secretary from 1994 to September 2001. Mr. Birger is Chairman of Given Imaging Ltd. and ChipX Corporation as well as a director of RDC, NetVision, Teledata and various others of our group companies. From 1991 to 1994, Mr. Birger was Vice President-Finance at North Hills Electronics Ltd., an advanced electronics company. From 1990 to 1991, Mr. Birger served as Chief Financial Officer of Middle-East Pipes Ltd., a manufacturer in the metal industry. From 1988 to 1990, Mr. Birger served as Chief Financial Officer of Maquette Ltd., a manufacturer and exporter of fashion items. From 1981 to 1988, Mr. Birger was Chief Financial Officer and director at Bateman Engineering Ltd. and I.D.C. Industrial Development Company Ltd. From 1979 to 1981, Mr. Birger was the Chief Financial Officer of Fibronics Ltd. Mr. Birger is a member of "Young Entrepeneurs", a non-profit organization, and a director of the National Science & Technology Museum in Haifa. Mr. Birger holds a B.A. and an M.A. in economics from the Hebrew University, Jerusalem.

Tal Raz was appointed as our Vice President and Chief Financial Officer as of May 2002. Prior to joining us, Mr. Raz was the acting President and Chief Executive Officer of Elbit Ltd. from October 2001. Mr. Raz was appointed Vice President of Elbit in June 1998, and served as Chief Financial Officer of Elbit since he joined Elbit in April 1997, having previously served in the same capacity at Agentsoft Ltd., Jerusalem, and Paul Winston Corporation, New York. Prior thereto he was a senior auditor at Deloitte & Touche LLP’s New York office. He also serves as a director and a member of the executive committee of Partner Communications Company Ltd., and as a director of RDC, NetVision, AMT, Elron Telesoft and Cellact. Mr. Raz is a member of the Israeli CFO Forum Steering Committee. Mr. Raz is a certified public accountant, and holds BA and MA degrees in accounting and business administration from Baruch College, City University, New York.

Moshe Fourier was appointed as our Chief Technical Officer on June 1, 2000. From 1999 to 2000, he served as the Chief Operations Officer for Terayon Communications' broadband voice division, one of the leading companies that provides cable modems and telecommunications solutions over the cable television infrastructure. From December 1993 until 1999, he joined the founder of Telegate and jointly initiated this start-up providing telecommunications equipment for delivering voice, data and video over cable television infrastructure, and served as Deputy Chief Executive Officer and Vice President of Research and Development and Technology. In June 1992, he joined RADA Electronic Industries as Vice President of Engineering. In August 1975, Mr. Fourier joined Astronautics Corporation of America - the Israeli division, as the first engineer and was promoted in 1978 to Vice President of Engineering. Mr. Fourier holds a bachelor of science degree in electrical engineering (BSEE) and an associated electrical engineering degree from the Technion, Israel Institute of Technology.

Shmuel Kidron was appointed as our Vice President in June 2000. Since October 2002 Mr. Kidron has been Vice-Chairman of Elron TeleSoft. From 1993 to 2000, Mr. Kidron was the President and Chief Executive Officer of Tadiran Electronic Systems Ltd. From 1990 to 1993, Mr. Kidron was a Business Unit Manager in Tadiran Electronic Systems. From 1980 to 1990, Mr. Kidron fulfilled various managerial and engineering positions in Tadiran Electronic Systems. Mr. Kidron holds a Bachelor of Science degree in Electrical Engineering from the Technion, Israel Institute of Technology.

Avishai Friedman joined Elron in January 2002 as Director of Business Development and in January 2004 was appointed Vice President, Business Development. In addition, Mr. Friedman serves as a director in several companies in the Elron Group. From 1997 to 2001, Mr. Friedman was Chief Executive Officer of Nano-Size Ltd. From 1991 to 1995, Mr. Friedman was Chief Executive Officer of Ganor, the private investments arm of the Rothschild Group in Israel. Mr. Friedman holds a BA degree in Marketing and Finance and an MA degree in Business Administration (summa cum laude) from the Tel-Aviv University.

Assaf Topaz joined Elron in April 2004 as Director of Business Development and in April 2005, was appointed as Vice President. Prior to joining Elron, from 1998 to 2002, Mr. Topaz was co-founder and Chief Operations Officer of Gilian Technologies, Inc, a technology company engaged in the web security market. From 1996 to 1998, Mr. Topaz was a business development executive for Euro Tel Aviv, an advertising agency. From 1995 to 1996, Mr. Topaz was an account executive at McCann Erickson-Kesher Advertising Ltd. Mr. Topaz holds a B.A., Economics and Geography from the Hebrew University of Jerusalem, Israel and an MSC from Stanford University.

B. Compensation

During the year ended December 31, 2004, we paid aggregate remuneration to our directors and officers as a group who served in the capacity of director or executive officer during such year of approximately $1,980,000. This amount does not include amounts expended by us for automobiles made available to our officers in the aggregate amount of approximately $33,000.

The following table sets forth the approximate aggregate compensation paid by us during the fiscal year ended on December 31, 2004 to all our directors and officers.

	Cash and Cash-Equivalent Forms of Compensation (in thousands of U.S. $)	
	Salaries, Fees, Directors' Fees, Commissions and Bonuses	**Securities(2) or Property, Insurance Benefits or Reimbursements and Personal Benefits**
2004 (1)		
All Directors	191	-
All Officers	1,489	300

(1) Does not include an increase in provision for vacation in the amount of approximately $100,000.

(2) See "Share Ownership" under this Item 6 and "Compensation of the Chairman under Item 7- Related Party Transactions.

C. Board Practices

None of our directors have service contracts with us or any of our group companies providing for benefits upon termination of employment. Compensation of our officers is recommended by our senior management and approved by the board of directors or a committee of the board of directors. Compensation of all other employees is determined by our senior management.

Board of Directors

Our Articles of Association provide for a board of directors of not less than five members and no more than fifteen members, including external directors. Each director, other than external directors, is elected to serve until the end of the first annual meeting following their appointment. However, if no directors are elected at such annual meeting, the then present directors shall continue in office. The board of directors may appoint additional directors, provided that the total number of directors does not exceed the maximum number of fifteen as mentioned above. A director appointed as such shall serve until the end of the next annual meeting held following his or her appointment and he or she shall be eligible for re-appointment. Notwithstanding any of the above, any director, other than external directors, may be removed from office by an ordinary resolution of a general shareholders meeting or by two thirds of the directors. A director need not hold any of our shares to qualify as one of our directors. Our Articles provide that our board of directors may delegate its powers to its committees, subject to limitations determined by the Israeli Companies Law.

Substitute Directors

Our Articles of Association provide that any director may, by written notice to us, appoint another person to serve as a substitute director and may cancel such appointment. The identity of a substitute director requires the approval of the board of directors. Under the Israeli Companies Law, there shall not be appointed as a substitute director, any person who is not himself qualified to be appointed as a director or a person who is already serving as a director or a person who is already serving as a substitute director for another director. Nevertheless, a director may be appointed as a substitute director for a committee of the board of directors if he or she is not already serving as a member of the committee. Under the Israeli Companies Law, there shall not be appointed a substitute director for an external director.

The term of appointment of a substitute director may be for one meeting of the board of directors or for a specified period or until notice is given of the cancellation of the appointment. To our knowledge, no director currently intends to appoint any other person as a substitute director, except if the director is unable to attend a meeting of the board of directors.

External Directors

The Israeli Companies Law requires Israeli companies with shares that have been offered to the public in or outside of Israel (public companies) to appoint two external directors. No person may be appointed as an external director if the person or the person's spouse, siblings, parents, grandparents, descendants, spouses descendants and the spouses of any of the foregoing (referred to as a relative), partner, employer or any entity under the person's control, has or had, within the two years preceding the date of the person's appointment to serve as external director, any affiliation with the company or any entity controlling, controlled by or under common control with the company. The term "affiliation" includes:

- an employment relationship;
- a business or professional relationship maintained on a regular basis;
- control; and
- service as an office holder, as defined below in Item 10, excluding service as a director for a period of not more than three months, during which the company initially offered shares to the public.

No person may serve as an external director if the person's position or other business activities create, or may create, a conflict of interest with the person's responsibilities as an external director or may otherwise interfere with the person's ability to serve as an external director. If, at the time external directors are to be appointed, all current members of the board of directors are of the same gender, then at least one external director must be of the other gender.

Pursuant to a 2005 amendment to the Companies Law, a public company shall be required to appoint as an external director a person, who has "professional capability" or a person, who has "financial and accounting expertise", provided that at least one of the external directors shall have "financial and accounting expertise". This provision will come into effect when regulations determining the requirements for "financial and accounting expertise" and for "professional capability", are issued. In addition, pursuant to the same amendment to the Companies Law, the board of directors of a public company shall be required to determine the number of directors with "financial and accounting expertise", serving on at the board of directors.

External directors are to 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-third of the shares held by non-controlling shareholders, or their representatives, which voted at the meeting, vote in favor of election of the director without taking abstentions into account. According to the Israeli Companies Law, a controlling shareholder is defined as a person who has the ability to direct the activities of a company, other than if this power derives solely from its position on the board of directors or any other position with the company. A person is presumed to be a controlling shareholder if he holds half or more of the following: (1) voting rights in the general meeting, or (2) rights to appoint directors or the Chief Executive Officer; or

- the total number of shares held by non-controlling shareholders voted against the election of the director does not exceed one percent of the aggregate voting rights in the company.

The initial term of an external director is three years and may be extended for an additional three years. External directors may be removed only in a general meeting, by the same percentage of shareholders as is required for their election, or by a court, and in both cases only if the external directors cease to meet the statutory qualifications for their appointment or if they violate their duty of loyalty to the company. Each committee of a company's board of directors must include at least one external director and all of the external directors must be members of the audit committee.

An external director is entitled to compensation in accordance with the regulations adopted under the Israeli Companies Law and is otherwise prohibited from receiving any other compensation, directly or indirectly, in connection with service provided as an external director.

Audit Committee

The Israeli Companies Law requires public companies to appoint an audit committee. The responsibilities of the audit committee include identifying irregularities in the management of the company's business and approving related party transactions as required by law. An audit committee must consist of at least three directors, including, as mentioned, all of the external directors of the company. The Chairman of the board of directors, any director employed by or otherwise providing services to the company, and a controlling shareholder or any relative of a controlling shareholder, may not be a member of the audit committee.

Our two external directors serve on the audit committee of the board of directors. All members of our audit committee meet the definition of independent directors under the Sarbanes Oxley Act of 2002 and the Nasdaq Marketplace Rules. None of them is an affiliated person of us or has received any consulting, advisory or other compensatory fee from us, other than in their capacity as directors. Yaacov Goldman is our designated financial expert under the Sarbanes-Oxley Act of 2002.

Internal Auditor

Under the Israeli Companies Law, the board of directors of public companies must appoint an internal auditor, nominated by the proposal of the audit committee. The role of the internal auditor is to examine, among other matters, whether the company's actions comply with the law and orderly business procedure. Under the Israeli Companies Law, the internal auditor may be an employee of the company but not an office holder (as defined below in Item 10), an interested party, a relative of an office holder or an interested party, and he may not be the company's independent accountant or its representative. According the Israeli Companies Law, an interested party is defined as a shareholder who holds 5% or more of the outstanding share capital or the voting power, a director, a general manager or a shareholder who has the right to appoint at least one director or the general manager. Doron Cohen of Fahn Kane, a member of Grant Thornton International, is our internal auditor.

D. Employees

All of our employees are located in Israel. The following table sets forth, for the last three financial years, the number of our employees broken down into categories.

Period ended December 31,	2004	2003	2002
Administration and Management	22	22	20

The following table sets forth for the last three financial years the number of employees of Elron TeleSoft broken down into categories.

Period ended December 31,	2004	2003	2002
Research and development	16	11	8
Marketing and sales	6	5	5
Software projects and engineering	16	28	31
Administration and Management	10	12	18
Total	48	56	62

The above information excludes details of employees of our other subsidiaries, Galil Medical, SELA, RDC and 3DV.

Certain provisions of the collective bargaining agreements between the Histadrut (General Federation of Labor in Israel) and the Coordination Bureau of Economic Organizations (including the Industrialists' Associations) are applicable to employees in Israel by order of the Israeli Ministry of Labor. These provisions concern principally the length of the work day, minimum daily wages for professional workers, insurance for work-related accidents, procedures for dismissing employees, determination of severance pay, and other conditions of employment. We generally provide employees with benefits and working conditions beyond the minimum requirements.

Israeli law generally requires severance pay, which may be funded by Managers' Insurance described below, upon the retirement or death of an employee or termination of employment without cause (as defined in the law). The payments thereto amount to approximately 8.33% of wages. Furthermore, Israeli employees and employers are required to pay predetermined sums to the National Insurance Institute, which is similar to the United States Social Security Administration. Such amounts also include payments for national health insurance. The payments to the National Insurance Institute are equal to approximately 16.3% of the wages, of which the employee contributes approximately 66% and the employer contributes approximately 34%.

A general practice followed by us and some of our group companies although not legally required, is the contribution of additional funds on behalf of most of the employees to a fund known as Managers' Insurance. This fund provides a combination of savings plan, insurance and severance pay benefits to the employee, giving the employee a lump sum payment upon retirement and securing the severance pay, if legally entitled, upon termination of employment.

The employer decides which employees are entitled to participate in the plan, and each employee who agrees to participate contributes an amount equal to 5% of his or her salary and the employer contributes between 13.3% and 15.8% of the employee's salary.

Share Ownership

The number of our ordinary shares beneficially owned by each of our directors, and by our directors and officers as a group, as of May 31, 2005, is as follows:

Director	Ordinary Shares
Ami Erel, Chairman[1]	10,214[2]
Avraham Asheri	0
Prof. Gabi Barbash	0
Prof. Yair Be'ery	0
Nochi Dankner[1]	0
Avraham Fischer[1]	0
Yaacov Goldman	0
Zehavit Joseph	0
Oren Lieder[1]	0
Shay Livnat	0
Dori Manor[1]	0
Prof. Daniel Sipper	0
All officers and directors as a group	108, 985[3]

(1) Director or officer of DIC. Ownership excludes shares beneficially owned by DIC.

(2) Consists solely of options to purchase our ordinary shares, based on our share price as of May 31, 2005. See below Series 9 and Series 11 under "Stock Option Plans".

(3) Includes options to purchase 107,745 of our ordinary shares currently exercisable or exercisable within 60 days of May 31, 2005.

Stock Option Plans

As of May 31, 2005, 552,818 options to purchase our ordinary shares granted to our officers and employees were outstanding. Details concerning these options are as follows:

Series 9 Options

The Chairman of our board of directors was granted 58,154 options to purchase our ordinary shares (the “Series 9 Options”). The Series 9 Options were granted ratably over a period of three years commencing on February 2000 and are exercisable for a period of three years, commencing two years after the date of grant. The 19,384 Series 9 Options granted in February 2000 have expired.

The per share exercise price of the Series 9 Options granted in February 2001 is $21.38. The per share exercise price of the Series 9 Options granted in February 2002 is $13.01. Upon exercise of the Series 9 Options, the option holder is granted a number of shares reflecting the benefit component of the options exercised, as calculated at the exercise date.

Series 10 Options

There are outstanding options to purchase an aggregate of 33,000 of our ordinary shares of which options to purchase an aggregate of 20,000 shares are held by one of our officers (the (“Series 10 Options"). The Series 10 Options are exercisable at a price of $29.38 per share. The optionholders are entitled to exercise 25% of the amount granted, each year, starting in October 2001. The Series 10 Options will expire in October 2007.

Series 11 Options

The Chairman of our board of directors was granted 58,000 options to purchase our ordinary shares (the “Series 11 Options”). The Series 11 Options were granted ratably over a period of three years commencing in June 2001 and are exercisable for a period of three years, commencing two years after the date of grant. The first amount of 19,333 Series 11 Options was granted in June 2001. The per share exercise price of the Series 11 Options granted in June 2001 is $19.05. The second amount of 19,333 Series 11 Options was granted in June 2002 and were exercised in December 2004 into 8,623 shares based upon a per share exercise price of $8.337. The third amount of 19,334 Series 11 Options was granted in June 2003. The per share exercise price of the Series 11 Options granted in June 2003 is $8.437.

Upon exercise of the Series 11 Options, the option holder is granted a number of shares reflecting the benefit component of the options exercised, as calculated at the exercise date.

Series 12 Options

There are outstanding options to purchase an aggregate of 42,000 of our ordinary shares held by two of our officers (the “Series 12 Options”). The Series 12 Options are exercisable at a price per share of $18.87 per share. The officers are entitled to exercise 25% of the amount granted, each year, starting in February 2002. The Series 12 Options will expire in June 2008.

Series 14 Options

There are outstanding options to purchase an aggregate of 7,500 of our ordinary shares of which options to purchase an aggregate of 5,000 shares are held by one of our officers (the “Series 14 Options”). The Series 14 Options are exercisable at a price of $11.69 per share. The optionholders are entitled to exercise 25% of the amount granted, each year, starting in July 2002. The Series 14 Options will expire in September 2008.

Series 15 Options

There are outstanding options to purchase an aggregate of 39,500 of our ordinary shares of which options to purchase an aggregate of 35,000 shares are held by three of our officers (the "Series 15 Options"). The Series 15 Options are exercisable at a price of $10.38 per share. The optionholders are entitled to exercise 25% of the amount granted, each year, starting in September 2002. The Series 15 Options will expire in October 2007.

Series 16 Options

There are outstanding options to purchase an aggregate of 4,500 of our ordinary shares. (the "Series 16 Options"). The Series 16 Options are exercisable at a price of $11.15 per share. The optionholder is entitled to exercise 25% of the amount granted each year, starting in October 2002. The Series 16 Options will expire in November 2007.

Series 17 Options

There are outstanding options to purchase an aggregate of 12,500 of our ordinary shares, of which options to purchase an aggregate of 10,000 shares are held by one of our officers (the "Series 17 Options"). The Series 17 Options are exercisable at a price of approximately $7.77 per share. The optionholders are entitled to exercise 25% of the amount granted each year, starting in May 2003. The Series 17 Options will expire in July 2008.

2003 Option Plan

During May, 2003, our Board of Directors adopted the 2003 Option Plan which was subsequently ratified by our shareholders on November 30, 2003. Pursuant to the 2003 Option Plan, under which options to purchase an aggregate of up to 500,000 ordinary shares may be granted, we issued options to purchase 272,000 ordinary shares (including options granted to our officers to purchase 210,000 ordinary shares) at an exercise price of $8.00 per share to our officers and employees. In December 2004, we issued options to purchase an additional 20,000 ordinary shares to one of our officers at an exercise price per share of $12.41. The 2003 Option Plan provides that the exercise price per share shall be reduced by an amount equal to the amount of any dividend per share distributed. The optionees are entitled to exercise 25% of the amount granted, each year, commencing on the date of grant and expiring 5 years later. In granting the options, the Board of Directors selected the capital gains tax track pursuant to the new tax reform legislation which came into effect on January 1, 2003. (For more details – see Item 10 – "Taxation" – "Employee Stock Options.").

Elbit Ltd. Options

As part of our merger with Elbit, we assumed each outstanding option to purchase ordinary shares of Elbit. Each such option was deemed to be an option to purchase our ordinary shares. Each assumed option entitles the optionholder to acquire, on substantially the same terms and conditions applicable under the original Elbit option plan and agreements, the number of our ordinary shares equal to the number of Elbit ordinary shares subject to the option, multiplied by the exchange ratio of 0.45. Any fractional interests resulting from the assumption of options for each optionholder will be aggregated and rounded up to the nearest whole number. With these exceptions, the existing Elbit option plan and agreements remain in full force and effect. The Elbit option plan provides that each option becomes exercisable as to 50% of the shares on the second anniversary of the date of grant, 25% of the shares on the third anniversary of the date of grant, and the remaining 25% on the fourth anniversary of the date of grant.

As of May 31, 2005, options to acquire 44,381 of our shares by virtue of the Elbit options were outstanding. The exercise price of these options range from $13.33 to $18.09 and their expiration dates range from August 2005 to December 2006.

Options of certain officers to acquire shares in our private group companies

During 2001, the Board of Directors approved the grant of options to certain of our officers to acquire between 1% and 2% of our investments in certain private companies. The options are exercisable at the weighted average price of our investments. The options vest ratably over a three year period and are exercisable for an additional three years.

These options are in addition to those granted to our Chairman, Mr. Ami Erel. See Item 7 – "Major Shareholders and Related Party Transactions - Compensation of Chairman."

Item 7. Major Shareholders and Related Party Transactions

A. Major Shareholders

The following table sets forth, as of May 31, 2005, unless otherwise specified, the number of ordinary shares beneficially owned by all shareholders known to us to beneficially own more than 5% of our ordinary shares. The voting rights of our major shareholders do not differ from the voting rights of other holders of our ordinary shares. As of May 31, 2005, there were a total of 443 holders of record of our ordinary shares, of which 327 were registered with addresses in the United States. Such United States holders represented as of such date, holders of record of approximately 6% of our then outstanding ordinary shares.

Name and Address	Number of Ordinary Shares	Percent of Ordinary Shares
Discount Investment Corporation Ltd. (1) Tel Aviv, Israel…………………………………	13,443,658	*45.70%
Bank Leumi Group (2) Tel Aviv, Israel………………………………	1,935,742	6.58%
Bank Hapoalim Group (3) Tel Aviv, Israel………………………………	1,737,252	5.91%
Clal Insurance Group (4) Tel Aviv, Israel………………………………..	240,317	0.82%
All Officers and Directors as a group (5) ………..	108,415	0.37%

*Between June 19 and 30, 2005, DIC purchased an additional aggregate of 565,111 of our ordinary shares thereby increasing its percentage to approximately 47.6%.

(1) IDBH is the parent of IDBD, which, in turn, is the parent of DIC and Clal Insurance Enterprise Holdings Ltd. ("Clal"). IDBH, IDBD, DIC and Clal are public companies traded on the Tel Aviv Stock Exchange.

As of May 31, 2005, approximately 51.7% of the outstanding share capital of IDBH was owned by a group comprised of: (i) Ganden Investments I.D.B. Ltd. ("Ganden Investments"), a private Israeli company controlled by Nochi Dankner and his sister, Shelly Bergman, which held 31.02% of the equity of and voting power in IDBH; (ii) Manor Investments-IDB Ltd. ("Manor Investments"), a private Israeli company controlled by Ruth Manor, which held 10.34% of the equity of and voting power in IDBH; and (iii) Avraham Livnat Investments (2002) Ltd. ("Livnat Investments"), a private Israeli company controlled by Avraham Livnat, which held 10.34% of the equity of and voting power in IDBH. Ganden Investments, Manor Investments and Livnat Investments, owning in the aggregate approximately 51.7% of the equity of and voting power in IDBH, entered into a Shareholders Agreement relating, among other things, to their joint control of IDBH, the term of which is until May 19, 2023 ("IDB Shareholders Agreement"). Ganden Investments, Manor Investments and Livnat Investments pledged their shares of IDBH to a financial institution as collateral for the repayment of loans borrowed to purchase such shares.

In addition, as of June 2, 2005, (i) Ganden Holdings Ltd. ("Ganden Holdings"), another private Israeli company controlled by Nochi Dankner and his sister, Shelly Bergman, which is the parent company of Ganden Investments, held approximately 7.07% of the equity and voting power of IDBH, (ii) Shelly Bergman held, though a wholly owned company, approximately 7.23% of the equity of and voting power in IDBH, (iii) another private Israeli company controlled by Ruth Manor, which is the parent company of Manor Investments, held approximately 0.03% of the equity and voting power in IDBH and (iv) another private Israeli company controlled by Avraham Livnat, which is the parent company of Livnat Investments, held approximately 0.04% of the equity and voting power in IDBH. Substantially all of the additional shares of IDBH set forth in (i) and (ii) above held directly by Ganden Holdings and Shelly Bergman's wholly owned company, were acquired with borrowed funds and are pledged to each each respective shareholder's lending institution. None of the shares set forth in (i) –(iv) above are subject to the IDB Shareholders Agreement.

Nochi Dankner is Chairman of IDBH, IDBD and DIC and a director of Clal and Elron. Shelly Bergman and Zvi Livnat (a son of Avraham Livnat) are directors of IDBH, IDBD and DIC. Shay Livnat (a son of Avraham Livnat) is a director of IDBD and Elron. Isaac Manor (the husband of Ruth Manor) is a director of IDBH, IDBD, DIC and Clal and Dori Manor (the son of Isaac and Ruth Manor) is a director of IDBH, IDBD, DIC and Elron.

DIC's address is 3 Azrieli Center, 44th floor, Tel Aviv 67023, Israel.

(2) The Bank Leumi Group is comprised of the holdings of mutual and provident funds that are controlled by Bank Leumi. As of May 31, 2005, the State of Israel held approximately 28.28% of the outstanding shares of Bank Leumi. The balance of the shares of Bank Leumi were held as follows: (i) Shlomo Eliahu Holdings Ltd. and affiliated companies held approximately 9.98% of Bank Leumi's shares; (ii) mutual funds of the Bank Hapoalim group

held approximately 5.16% of Bank Leumi’s shares; and (iii) the public held the remainder of Bank Leumi’s shares.

The Bank Leumi’s address is P.O.B 2 Tel-Aviv 6100, Israel (Principal branch, 19 Herzl St. Tel-Aviv, Israel)

(3) The Bank Hapoalim Group is comprised of the holdings of mutual and provident funds that are controlled by Bank Hapoalim B.M. As of April 21, 2005, the shares of Bank Hapoalim were held as follows: (1) Arison Holdings (1998) Ltd. held approximately 16.49% of Bank Hapoalim's shares; (2) Israel Salt Industries (1998) Ltd. held approximately 7.03% of Bank Hapoalim's shares; (3) Alliance Capital Management L.P. held approximately 7.1% of Bank Hapoalim's shares; (4) the public held approximately 61.50% of Bank Hapoalim's shares; and (5) other shareholders each held less than 5% of Bank Hapoalim's shares.

(4) The Clal Insurance Group is comprised of Clal and its subsidiary companies, which are deemed to be major shareholders of the Company. Clal is majority owned by IDBD, the parent company of DIC, which in turn is a controlling shareholder of the Company. As of May 31 2005, the other major shareholders of Clal were Bank Hapoalim, which held approximately 18.71% of Clal’s shares (including holdings of mutual and provident funds that are controlled by Bank Hapoalim B.M.), and mutual and provident funds that are controlled by Bank Leumi, which held approximately 6.98%. None of the remaining shareholders of Clal held more than 5% of its shares.

The Clal Insurance Group’s address is 48 Menachem Begin Rd., Clal Development Bldg., Tel Aviv, Israel.

(5) This amount includes 107,745 shares underlying options that are currently exercisable or that will become exercisable within 60 days of May 31, 2005. This amount does not include any shares that may be deemed to be beneficially owned by directors by virtue of their affiliation with DIC.

B. Related Party Transactions

Directors’ Compensation

Under the Companies Law and Regulations, we, being a dual listed company, are permitted to pay an annual fee of up to NIS100,000 (approximately $22,900) per director and up to NIS3,000 (approximately $690) per director for participation in each meeting of the board of directors or any committee thereof, in each case, adjusted to the Israeli Consumer Price Index from time to time. However, in each of 2003, 2004 and 2005, we agreed to grant compensation to all of our directors for the fiscal years 2003, 2004 and 2005 respectively, according to the amount then permitted according to the Israeli Companies Regulations (Rules Regarding Compensation and Expenses for an External Director), 2000 (the “External Director Regulations”), for companies of the same classification in relation to its shareholder’s equity, which were as of May 31, 2005, in addition to reimbursement of expenses, approximately NIS

45,896 (approximately $10,500) per director for one year and in addition approximately NIS 1,765 (approximately $400) per director for participation in each meeting of the board of directors or any committee thereof.

Compensation of the Chairman

Mr. Ami Erel has options to acquire up to 1.5% of any shares or other securities acquired by us in Wavion, Inc. and up to 0.75% of any shares or other securities acquired by us and through DEP in Galil Medical Ltd. (each an "Invested Company") (together, the “Option”). The Option shall be exercisable at the weighted average price of investments made by us with respect to any such Invested Company until the date of exercise of the Option. The Option shall be exercisable for a period of three years commencing on the later of January 1, 2000 or the date of the latest investment by us in the relevant Invested Company, provided that at the time of the Option exercise Mr. Erel is a director or an employee of ours and that we have not sold or otherwise transferred to a third party our securities in the relevant Invested Company.

Mr. Erel shall be entitled to participate in a sale by us of shares which were, or are, subject to Mr. Erel’s Option hereunder, by selling the same proportion of his shares along with us. We may require Mr. Erel to sell such shares together with a sale of shares by us. Sales by Mr. Erel of shares acquired upon exercise of the foregoing Options, which are not publicly traded, will require our approval. To date, none of the foregoing options have been exercised.

On May 30, 2004, Mr. Erel exercised his option to purchase 21,751 ordinary shares of Given Imaging from us for the aggregate exercise price of $49,380.

Acquisition of 67% of the shares of DEP

On May 6, 2002, we completed the purchase of DIC’s holding of 67% of the shares of DEP. Pursuant to the share purchase agreement with DIC dated November 19, 2001 we issued 2,261,843 ordinary shares to DIC in exchange for all of the shares held by DIC in DEP, including DIC’s rights to loans provided by DIC to RDC. We and DIC received written opinions from our respective financial advisors that the number of shares issued to DIC in the transaction was fair from a financial point of view, and the transaction was approved by our shareholders at a special meeting held on April 28, 2002.

Merger with Elbit

On May 15, 2002, we completed our merger with Elbit, which prior to the merger, was 44% owned by us.. Pursuant to the Agreement and Plan of Merger dated October 31, 2002, Elbit merged with us and we issued to Elbit’s shareholders (other than us) approximately 5,617,600 Elron shares, based on an exchange ratio of 0.45 of our ordinary shares for each ordinary share of Elbit. We and Elbit received written opinions from our respective financial advisors that the exchange ratio was fair from a financial point of view. The merger was approved by our and Elbit’s shareholders, creditors and optionholders on April 28, 2002 and April 29, 2002, respectively, and by the District Court of Tel-Aviv-Jaffa.

Investments in or acquisition of Shares of Galil Medical Ltd.

During 2002 and through May 31, 2005, we, our subsidiary RDC, and our parent company DIC, invested in and provided loans to Galil Medical.

On June 27, 2002, we purchased an additional 10.75% of Galil Medical's outstanding shares from Lumenis Ltd., in consideration for approximately $0.8 million. In the same transaction, DIC also purchased an additional 10.75% of Galil Medical's outstanding shares from Lumenis under the same terms and conditions.

All of these transactions were approved by our Audit Committee and our Board of Directors due to DIC's participation in the transactions.

Lease Agreement with Elbit Systems.

Elbit Systems, in which we held 19.6% through July 2004, currently leases from Elbit Ltd. approximately 15,760 square meters of office and manufacturing space in Karmiel, Israel. The lease expires in October 2006 and may be terminated earlier by Elbit Systems upon twelve months' prior written notice. The monthly rent is an amount in NIS equal to approximately $5.4 per square foot linked to the U.S. dollar and the U.S. CPI, payable quarterly at the beginning of each quarter. In the event that the area leased is substantially reduced, the monthly rent will be determined by the parties. In 2004, we sold our shares in Elbit Systems.

Grant of Letters of Exemption and Indemnification

In 2001, following the approval of our audit committee, board of directors and shareholders, and in accordance with the provisions of the Companies Law, we granted letters of indemnification to our directors and officers. The aggregate indemnification shall not exceed 25% of our shareholders equity according to our consolidated financial statements for the year ended December 31, 2000, for all persons and cases to be indemnified. In addition, we undertook to exempt our directors and officers, to the extent permitted by law, from any liability towards us for any damage caused or that may be caused to us by them, if caused or that may be caused following a breach of their duty of care towards us.

We continue to grant letters of indemnification and exemption to our directors and officers in accordance with the above terms.

Directors and Officers Insurance Policy

In April 2005, following the resolution and recommendation of our Audit Committee and Board of Directors, our shareholders approved and ratified the purchase of a directors' and officers' liability insurance policy (the "Policy") for our directors and officers from Clal Insurance Company Ltd., a related party and separately approved the application of the Policy to Dori Manor, one of our directors, and any future director or officer of the Company who may currently be considered a "Controlling Shareholder" under the Companies Law, 1999. The principal terms of the Policy are as follows:

(1) The Policy was for a period beginning on January 1, 2005 and ending on June 30, 2006.

(2) The coverage under the Policy was limited to $30 million per claim and in the aggregate during the Policy period.

(3) The annual premium to be paid with respect to the Policy was approximately $475,000.

In addition, our shareholders approved: (i) any renewal and/or extension of the Policy for all our directors and officers; and (ii) the purchase of any other directors’ and officers’ liability insurance policy for our directors and officers upon the expiration of the Policy; provided that any such renewal, extension or purchase referred to in clauses (i) and (ii) above is for the benefit of our previous and/or current and/or future directors and officers and on terms substantially similar to those of the Policy; and that the premium will not increase by more than 25% in any year, as compared to the previous year.

In April 2003, the shareholders approved the purchase of a directors’ and officers’ liability insurance policy covering the period January to December 2003 with a coverage of $20 million in consideration for a premium of approximately $1 million. In December 2003, our audit committee and board of directors approved the renewal of such policy for the period January to December 2004 at a premium of $650,000.

Purchase of Shares of Given Imaging from RDC

On May 13, 2003, we and Rafael, the minority shareholder of RDC, purchased 2,000,000 shares of Given Imaging (1,000,000 each) from RDC for total consideration of approximately $12.2 million. Of the proceeds, a total of $5.0 million was used by RDC to repay shareholders’ loans to each of Rafael and us and $2.5 million was used to repay its bank loan.

Voting Agreement with DIC regarding Given Imaging

On September 29, 2003, we and DIC entered into a voting agreement pursuant to which, among other things, DIC agreed to vote all of its ordinary shares in favor of nominees to the board of directors of Given Imaging proposed by us. The voting agreement is for a term of one year and renews automatically each year thereafter unless terminated by notice of either party to the other party no later than August 30 in each year. This agreement was approved by our Audit Committee and our Board of Directors.

Investment in Jordan Valley

On October 21, 2004, we invested approximately $6.7 million in Jordan Valley, in consideration for 25% of Jordan Valley on a fully diluted basis, as part of an aggregate investment of approximately $9 million raised by Jordan Valley. The balance of the aggregate investment in Jordan Valley was invested by Clal by way of conversion of previously granted loans. Jordan Valley is 40% owned (indirectly) by Clal, an approximately then 64% held subsidiary of IDBD, which also then owned approximately 67% of DIC. Our investment in Jordan Valley was approved by our audit committee, board of directors and shareholders.

Voting Agreement with Infinity regarding Teledata

On May 8, 2005, as part of our investment in Teledata, we and Infinity, a related venture capital fund, entered into a voting agreement pursuant to which we agreed to vote in concert with each other at meetings of shareholders of Teledata. Clal, a subsidiary of IDBD, is the largest limited partner of Infinity. DIC, our largest shareholder, is also a subsidiary of IDBD. This agreement was approved by our Audit Committee and our Board of Directors as part of our investment in Teledata.

Loans to NetVision

During 2004, we and DIC each advanced loans to NetVision in the amount of $5.3 milion each. These loans were approved by our Audit Committee and our Board of Directors. We and DIC each converted approximately $3.1 million of these loans into equity of NetVision immediately prior to NetVision's initial public offering in May 2005 and $2.2 million in loans was repaid to each of us from the proceeds of the offering.

Shareholders Agreement with DIC regarding NetVision

On May 10, 2005, immediately prior to the NetVision initial public offering, we and DIC entered into a shareholders agreement pursuant to which we and DIC agreed to vote all of our shares in favor of our respective nominees to the board of directors of NetVision. In addition, under the agreement, we and DIC have rights of first refusal and co-sale rights on the sale of our respective shares subject to and in accordance with the mechanisms set forth in the agreement. The agreement shall terminate upon the earlier of our mutual consent or either us or DIC holding less than 10% of NetVision. This agreement was approved by our Audit Committee and our Board of Directors.

C. Interests of Experts and Counsel

Not Applicable.

Item 8. Financial Information

A. Consolidated Statements and Other Financial Information

Our consolidated financial statements and other financial information are incorporated herein by reference to Item 18 below.

Legal Proceedings

Gesser Claim

On September 8, 1999, we received a copy of a statement of claim, along with a court order requiring a motion to approve this claim as a class action, submitted by David Gesser, a shareholder of Elscint Ltd., or Elscint, The motion requests that this claim be approved as class action instead of the previous claim submitted by Yonatan Aderet. This claim names as defendants Elscint, Elbit, our company, and Emmanuel Gill, Uzia Galil, Dov Tadmor, Micha Angel and Yigal Baruchi, former directors of Elscint, and Yonatan Aderet, the former President and director of Elscint. The motion was submitted by the applicant on behalf of all existing shareholders of Elscint who held Elscint's shares on February 18, 1999. The plaintiff seeks damages of approximately $158.0 million.

The claim alleges that the defendants, by their decisions regarding the sale of Elscint's assets, caused damage to Elscint and its minority shareholders. The plaintiff seeks a court order requiring Elscint, or the other defendants, to purchase from each of the members of the represented class all shares held by them at a price of $27.46 per share. The lawsuit has been suspended pursuant to an arrangement reached by the parties pending the outcome of the appeal in the Investors claim described below. The arrangement provides that if the appeal as described in the "Investors Claim" immediately below is accepted, then the proceedings to recognize the lawsuit as a class action will proceed. Otherwise, the application to recognize the claim as a class action suit will be dismissed.

Investors Claim

On November 2, 1999, we received a statement of claim and an application to claim as a class action against Europe Israel (M.M.S.) Ltd. (EIL), Elbit Medical Imaging, Elscint, Control Centers Ltd. (the controlling shareholder of EIL), Marina Herzliya Limited Partnership 1988 (which is controlled by Control Centers) and against us and 25 past and present officers of the above companies, including our officers.

The claim was submitted by a number of investors and others, who hold shares in Elscint, while the application to approve the claim as a class action was submitted on behalf of shareholders who held shares in Elscint on September 6, 1999 and continued to hold such shares on the date of application, excluding the respondents.

The allegations, which the claimants raised against us and our officers, relate to the period prior to the sale of our holdings in Elbit Medical Imaging to EIL. These allegations include, among others, that (i) we and our officers gave preference to the interests of our company and the personal interests of our officers over the interests of Elscint and its minority shareholders; (ii) we and our officers did not act in order to enable the minority shareholders of Elscint to participate in the proceeds of the sale of Elscint's assets; and (iii) general allegations against the transactions whereby we sold our holdings in Elbit Medical Imaging to EIL. Further allegations were raised against the other respondents.

The plaintiffs seek a court order pursuant to which Elbit Medical Imaging would be compelled to execute the alleged buy-out of shares at $14 per share. Alternatively, the claimants have requested additional remedies set forth in the statement of claim, including a remedy requested also from us and our officers regarding compensation for the damages that they allege were suffered by them and/or by Elscint. Certain of the remedies have been requested also as derivative claims on behalf of Elscint. The maximum liability in this claim is not specified by the plaintiffs.

On August 16, 2000, the Haifa District Court dismissed the application to recognize the claim as a class action. Some of the claimants requested and were granted permission to appeal to the Supreme Court of Israel. The appeal to the Supreme Court is still pending. In addition, the claimants submitted an amended claim in February 2001, which was not recognized as a class action suit. The allegations are similar to those in the previous claim.

We deny all the allegations set forth in the above claims and are defending and intend to continue defending against such claims.

Lease Claim

In July 2003, ESW terminated the lease of its premises in the United States alleging defects in the premises and the lessor's failure to repair the defects. The lessor rejected the termination of the lease and is seeking to enforce the lease and to claim all amounts due under the lease from ESW and us, as guarantor of the lease. The balance of the rental under the lease amounts to approximately $2 million. ESW is counterclaiming damages caused by the lessor. We believe that ESW has good defense arguments and that the above claim will not have a material effect on our results of operations.

Other than the above matters, we are not a party to any material litigation and we are not aware of any pending or threatened litigation that would have a material adverse effect on us or on our business.

Dividend Policy

Currently we do not have any fixed dividend policy. The declaration of dividends is determined by the board of directors taking into consideration our financial status, profitability, realization of assets and our investment requirements.

B. Significant Changes

Except as otherwise disclosed in this Annual Report, no significant change has occurred since December 31, 2004.

Item 9. <u>The Offer and Listing</u>

A. Offer and Listing Details

Markets and Share Price History

Our ordinary shares are traded on the Nasdaq National Market, where our shares are listed and traded on the under the symbol “ELRN”. Our shares are also traded on the Tel Aviv Stock Exchange (TASE) in Israel. The following table sets forth, for the periods indicated, the high and low reported sales prices of our Ordinary Shares on the Nasdaq National Market and, in New Israeli Shekels (NIS), on the Tel Aviv Stock Exchange:

To be Updated Period	NASDAQ High (US	NASDAQ Low (US	TASE High (NIS)	TASE Low (NIS)

	dollars)	dollars)		
2000	55.12	25.00	216.68	104.40
2001	27.00	10.55	105.00	47.51
2002	14.83	5.50	65.80	27.71
First Quarter 2003	6.81	4.92	31.30	24.48
Second Quarter 2003	9.70	6.32	39.83	29.60
Third Quarter 2003	10.30	7.47	42.50	34.88
Fourth Quarter 2003	11.42	8.85	44.13	33.98
First Quarter 2004	14.15	11.32	63.50	51.60
Second Quarter 2004	14.66	12.42	66.00	57.90
Third Quarter 2004	14.93	13.32	67.33	60.98
Fourth Quarter 2004	15.23	12.44	66.71	55.62
December 2004	15.23	14.45	66.71	62.40
January 2005	16.14	14.5	70.36	64.12
February 2005	16.2	15.17	70.21	65.82
March 2005	16.49	15.00	71.16	66.85
April 2005	15.7	14.6	69.53	63.63
May 2005	16.15	14.62	69.47	64.93

B. Plan of Distribution

Not Applicable.

C. Markets

As noted above, our Ordinary Shares are traded on the Nasdaq National Market under the symbol "ELRN". Our shares are also traded on the Tel Aviv Stock Exchange in Israel.

D. Selling Shareholders

Not Applicable.

E. Dilution

Not Applicable.

F. Expenses of the Issue

Not Applicable.

Item 10. Additional Information

A and B. Share Capital; Memorandum and Articles of Association

Articles of Association; Israel Companies Law

Our shareholders approved the adoption of our new Articles of Association in March 2001. The objective of Elron as stated in our Articles and in our Memorandum of Association is to engage in any lawful activity.

We have currently outstanding only one class of securities, our ordinary shares, par value NIS 0.003 per share. No preferred shares are currently authorized.

Holders of ordinary shares have one vote per share, and are entitled to participate equally in the payment of dividends and share distributions and, in the event of our liquidation, in the distribution of assets after satisfaction of liabilities to creditors. According to our Articles, any modification of the Articles requires the approval of a special majority at a general meeting. A special majority is defined in our Articles as at least a majority of 67% of the shareholders who voted at the general meeting, without taking abstaining votes into account.

The Israeli Companies Law and our Articles require that we hold our annual general meeting of shareholders each year no later than 15 months from the last annual meeting, at a time and place determined by the board of directors, upon at least 21 days prior notice to our shareholders. Under the Israeli law and regulations and our Articles of Association, notice of the meeting is required to be published in two widely distributed daily newspapers published in Hebrew and to be sent to shareholders whose names appear in the shareholders register if their registered shares are not in Israel. No business may be commenced until a quorum of two or more shareholders holding at least one third of the voting rights are present in person or by proxy. The Israeli Companies Law provides that the record date for the participation of shareholders of a company whose shares are traded or registered outside of Israel such as us may be no more than 40 but no less than 4 days prior to the meeting, provided that notice for said meeting is given prior to the record date. Resolutions regarding the following matters must be passed at a general meeting of shareholders:

- amendments to our Articles and Memorandum of Association;
- appointment or termination of our auditors;
- appointment and dismissal of directors;
- approval of interested party actions and transactions requiring general meeting approval as provided in sections 255 and 268 to 275 of the Israeli Companies Law;
- increase or reduction of our authorized share capital and alterations of our share capital;
- a merger as provided in section 320 of the Israeli Companies Law;
- the exercise of the board of directors' powers by a general meeting, if the board of directors is unable to exercise its powers and the exercise of any of its powers is vital for our proper management, as provided in section 52(a) of the Israeli Companies Law; and
- any matter that is required to be adopted by resolution of a general meeting pursuant to the Israeli Companies Law or in accordance with our Articles.

An extraordinary meeting of our shareholders shall be convened by the decision of the board, or at the request of any two directors or one quarter of the officiating directors, or by request of one or more shareholders holding at least 5% of the voting rights in our company.

Shareholders requesting an extraordinary meeting must submit their proposed resolution with their request. Within 21 days of receipt of the request, the board must convene an extraordinary meeting and send out notices setting forth the date, time and place of the meeting. Such notice must be given at least 21 days, but not more than 35 days, prior to the extraordinary meeting.

The Israeli Companies Law codifies the fiduciary duties and duty of care that office holders owe to a company. An office holder, is defined in the Israeli Companies Law, as a (i) director, (ii) general manager, (iii) chief business manager, (iv) deputy general manager, (v) vice general manager, (vi) executive vice president, (vii) vice president, (viii) another manager directly subordinate to the general manager or (ix) any other person assuming the responsibilities of any of the forgoing positions without regard to such person's title. Each person listed in the table under "Directors and Senior Management" in Item 6 above is an office holder.

The Israeli Companies Law requires that an office holder of a company promptly disclose, and no later than the first board meeting in which such transaction is discussed, any personal interest that he or she may have and all related material information known to him or her, in connection with any existing or proposed transaction by the company. In addition, if the transaction is an extraordinary transaction, the office holder must also disclose any personal interest held by the office holder's relative. An extraordinary transaction is defined as a transaction not in the ordinary course of business, not on market terms, or that is likely to have a material impact on the company's profitability, assets or liabilities.

In the case of a transaction in which an officer has a personal interest that is not an extraordinary transaction, after the office holder complies with the above disclosure requirement, board approval is required unless the Articles of Association of the company provide otherwise. Our Articles of Association provide that a transaction with one of our office holders or a transaction, in which an office holder has a personal interest which, in each case, is not regarded as an extraordinary transaction, requires the approval of the board or the audit committee or by such other organ empowered by the board for such purpose. If the transaction in which an officer has a personal interest is an extraordinary transaction, then, it must also be approved by the audit committee and by the board of directors.

Agreements regarding directors' terms of employment require the approval of audit committee, the board of directors and the shareholders. In all matters in which a director has a personal interest, including matters of his/her terms of employment, he/she shall not be permitted to vote on the matter or be present in the meeting in which the matter is considered. However, should a majority of the audit committee or of the board of directors have a personal interest in the matter then:

a) all of the directors shall be permitted to vote on the matter and attend the meeting in which the matter is considered; and

b) the matter requires approval of the shareholders at a general meeting.

According to the Israeli Companies Law, the disclosure requirements discussed above also apply to a controlling shareholder of a public company. The term "controlling shareholder" for these purposes also includes shareholders that hold 25% or more of the voting rights if no other shareholder owns more than 50% of the voting rights in the company. In general, extraordinary transactions with a controlling shareholder or in which a controlling shareholder has a personal interest, and agreements relating to employment and compensation terms of a controlling shareholder require the approval of the audit committee, the board of directors and the shareholders of the company.

Such shareholder approval must either include at least one-third of the shares held by disinterested shareholders who are present in person or by proxy at the meeting (without taking abstaining votes into account), or, alternatively, the total shareholdings of the disinterested shareholders who vote against the transaction must not represent more than one percent of the voting rights in the company. Under specified circumstances, such shareholder approval is not required.

Under the Israeli Companies Law, if a private placement will entail 20% or more of the voting rights of a company prior to the placement, and all or part of the private placement consideration is not in cash or in public traded securities or is not upon market terms and if as a result of the private placement the holdings of substantial shareholder shall increase or result in a person becoming a substantial shareholder, then the allotment must be approved by the board of directors and by the shareholders of the company. A “substantial shareholder” is defined as a shareholder that holds 5% or more of the company’s outstanding share capital, assuming the exercise of all of the securities convertible into shares held by that person. In order for the private placement to be on “market terms” the board of directors has to determine, on the basis of a detailed examination, that the private placement is on market terms, unless proved otherwise. Any placement of securities that does not fall within the above description may be issued at the discretion of the board of directors.

Under the Israeli Companies Law, a shareholder has a duty to act in good faith towards the company and other shareholders when exercising his rights and refrain from abusing his power in the company, including, among other things, voting in the general meeting of shareholders on the following matters:

- any amendment to the Articles of Association;
- an increase of the company’s authorized share capital;
- a merger; or
- approval of interested party acts and transactions that require general meeting approval as provided in sections 255 and 268 to 275 of the Israeli Companies Law.

In addition, any controlling shareholder, any shareholder who knows that it possesses power to determine the outcome of a shareholder vote and any shareholder who has the power to appoint or prevent the appointment office holder in the company is under a duty to act with fairness towards the company. The Israeli Companies Law does not describe the substance of this duty. The Israeli Companies Law requires that specified types of transactions, actions and arrangements be approved as provided for in a company’s articles of association and in some circumstances by the audit committee, by the board of directors and by the general meeting of the shareholders. The vote required by the audit committee and the board of directors for approval of these matters, in each case, is a majority of the directors participating in a duly convened meeting.

C. Material Contracts

1. ***Deed of Transfer for Sale of Shares of Elbit Systems***

On July 28, 2004, we signed a deed of transfer to sell all of our holdings in Elbit Systems, constituting approximately 19.6% of the outstanding share capital of Elbit Systems, to the Federmann group, for approximately $196.6 million.

2. ***Sale of shares of Partner***

Buyback

On April 20, 2005 we completed the sale to Partner of 12,765,190 Partner shares for approximately $94 million, as part of the sale together with the other Israeli founding shareholders of Partner of an aggregate of approximately 33.3 million Partner shares to Partner for an aggregate consideration of approximately $245 million, pursuant to the terms of an irrevocable offer letter February 7, 2005. Under the terms of the offer letter, we, Polar Communications Ltd. ("Polar") and Eurocom Communications Ltd. (“Eurocom”), offered to sell to Partner, severally and not jointly, all of our respective Ordinary Shares, for aggregate consideration of between NIS 984.6 million ($225.2 million) and NIS 1.02 billion ($233.6 million) (the “Buyback”). Matav Investments Ltd. ("Matav"), the remaining Israeli founding shareholder, had the option to participate in the Buyback which it exercised. The sale price formula of the Buyback reflected a 10% discount from the 20-trading day volume weighted average market price of the Partner ordinary shares on the Tel Aviv Stock Exchange prior to the meeting of Partner shareholders in which the Buyback is approved, up to a maximum price of NIS 32.22 per share ($7.37 based on the applicable exchange rate of NIS 4.372 per $1.00) but not below NIS 31.04 per share ($7.10 based on such exchange rate). The sale was completed at the maximum price per share.

Restatement of Relationship Agreement

On April 20, 2005, in connection with the completion of the Buyback, we, the other Israeli founding shareholders, Eurocom, Polar and Matav (the "Israeli Shareholders") together with Advent Investments Pte Ltd. and Hutchison Telecommunications International (Netherlands) B.V., entered into the Restated Relationship Agreement, which replaced the Relationship Agreement dated October 10, 1999 among the parties.

The Restated Relationship Agreement requires the Israeli Shareholders, severally but not jointly, based on their respective holdings in Partner as of April 20, 2005, to hold a sufficient number of Partner ordinary shares to comply with the minimum aggregate holdings by Israeli entities required under Partner's license and articles of association (the “Required Israeli Percentage”). The Required Israeli Percentage is currently 5% of the outstanding share capital of Partner. The number of Partner ordinary shares required to be held by the Israeli Shareholders to maintain the Required Israeli Percentage is calculated based on the number of Partner ordinary shares outstanding from time to time up to a maximum of 160,922,344 ordinary shares outstanding, as adjusted to reflect stock splits, stock dividends and similar changes that apply to all the ordinary shares.

The Restated Relationship Agreement also requires the Israeli Shareholders to transfer such ordinary shares that are subject to the holding requirement of Required Israeli Percentage (the "Restricted Shares") only in accordance with the transfer limitations provided by Partner's license and articles of association.

In addition, pursuant to the Restated Relationship Agreement, the Israeli Shareholders undertook to appoint and retain the number of Israeli directors of Partner that are required pursuant to applicable law (including its license and articles of association) to be appointed and retained by Israeli Shareholders (the "Israeli Director(s)"). Partner's license currently requires that at least 10% of its directors be Israeli Directors, but one Israeli director is sufficient so long as there are fewer than 15 directors. Based on the current size of Partner's board of directors, which is comprised of 13 directors, one Israeli Director is currently required.

Shareholders Agreement

On April 20, 2005, we together with the other Israeli Shareholders also entered into a shareholders agreement. The shareholders agreement sets forth the mechanism for appointing the Israeli Director(s). Specifically, the Israeli Director(s) will be appointed on a rotation basis.

D. Exchange Controls

The Israeli Currency Control Law, 1978 imposes certain limitations concerning foreign currency transactions and transactions between Israeli and non-Israeli residents, which limitations may be regulated or waived by the Controller of Foreign Exchange at the Bank of Israel, through "general" and "special" permits. In May 1998, a new "general permit" was issued pursuant to which substantially all transactions in foreign currency are permitted. Any dividends or other distributions paid in respect of ordinary shares and any amounts payable upon our dissolution, liquidation or winding up, as well as the proceeds of any sale in Israel of our securities to an Israeli resident are freely repatriable into non-Israeli currencies at the rate of exchange prevailing at the time of conversion, provided that Israeli income tax has been paid on (or withheld from) such payments.

E. Taxation

The following is a summary of the material provisions of the current tax law applicable to companies in Israel, with special reference to its effect on us and our group companies. The following also contains a discussion of material Israeli tax consequences to our shareholders and government programs from which we and some of our group companies benefit. To the extent that the discussion is based on tax legislation that has not been subject to judicial or administrative interpretation, we cannot assure you that the views expressed in the discussion will be accepted by the tax authorities in question.

In July 2002, the Israeli Parliament approved a law enacting extensive changes to Israel's tax law (the "Tax Reform Legislation") generally effective January 1, 2003. Among the key provisions of the Tax Reform Legislation are (i) changes which may result in the imposition of taxes on dividends received by an Israeli company from its foreign subsidiaries; and (ii) the introduction of the "controlled foreign corporation" concept according to which an Israeli company may become subject to Israeli taxes on certain income of a non-Israeli subsidiary if the subsidiary's primary source of income is passive income (such as interest, dividends, royalties, rental income or capital gains). 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 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 discussion is not intended, and should not be construed, as legal or professional tax advice and is not exhaustive of all possible tax considerations.

General Corporate Tax Structure

Israeli companies are generally subject to company tax at the rate of 35% (34% in 2005, 32% in 2006 and 30% in 2007 and thereafter) of taxable income. However, the effective tax rate payable by a company that derives income from an Approved Enterprise (as further discussed below) may be considerably less.

Law for the Encouragement of Capital Investments, 1959

From time to time, certain operations of our group companies have been granted Approved Enterprise status under the Law for the Encouragement of Capital Investments, 1959, as amended, or the Investment Law.

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.

Taxable income of a company derived from an Approved Enterprise is subject to company tax at the rate of up to 25% (rather than 35% as stated above) for a period of time termed the benefit period. The benefit period is a period of seven years commencing with the year in which the Approved Enterprise first generated 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 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 may elect to forego certain government grants extended to Approved Enterprises in return for what is termed an alternative package of tax benefits (referred to as the Alternative Package). Under the Alternative Package, a company's undistributed income derived from an Approved Enterprise will be exempt from company tax for a period of between two and ten years, depending on the geographic location the Approved

Enterprise within Israel. Such company will be eligible for the tax benefits under the Investment Law for the remainder of the benefit period.

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:

% of Foreign Ownership	**Tax Rate**
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 benefits 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 our group companies which enjoy Approved Enterprise benefits 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.

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.

On March 29, 2005, the Israeli Knesset (Parliament) passed an amendment to the Investment Law, that revamps the Israeli tax incentives for future industrial and hotel investments (“ 2005 amendment”). 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 mainly upon the level of foreign investment and the geographical location of the "Privileged Enterprise".

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”. 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 15 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 7 to 15 years.

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

Taxation under Inflationary Conditions

The Income Tax Law (Inflationary Adjustments), 1985 (referred to as the Inflationary Adjustments Law) is intended to neutralize the erosion of capital investments in business and to prevent tax benefits resulting from deduction of inflationary expenses. This law applies a supplementary set of inflationary adjustments to the normal taxable profits computed under regular historical cost principles. We and our group companies operating in Israel are taxed under this law.

Under the Inflationary Adjustments Law, results for tax purposes are measured in real terms, in accordance with the changes in the consumer price index. In addition, subject to certain limitations, depreciation of fixed assets and losses carried forward are adjusted for inflation on the basis of changes in the consumer price index.

The salient features of the Inflationary Adjustments Law can be described generally as follows:

A special tax adjustment for the preservation of equity whereby certain corporate assets are classified broadly into Fixed (inflation resistant) Assets and Non-Fixed (soft) Assets. Where a company's equity, as defined in such law, exceeds the depreciated cost of Fixed Assets, a deduction from taxable income that takes into account the effect of the applicable annual rate of inflation on such excess is allowed (up to a ceiling of 70% of taxable income in any single tax year, with the unused portion permitted to be carried forward on a linked basis to the following year and will be considered a business loss). If the depreciated cost of Fixed Assets exceeds a company's equity, then such excess multiplied by the applicable annual rate of inflation is added to taxable income.

Subject to certain limitations, depreciation deductions on Fixed Assets and losses carried forward are adjusted for inflation based on the increase in the consumer price index (from the beginning of the 1982 fiscal year, and as of the 1985 fiscal year, with respect to equipment); and gains on the sale of certain traded securities are taxable.

However, dealers in securities are subject to the regular tax rules applicable to business income in Israel.

Law for the Encouragement of Industry (Taxes), 1969

Certain of our group companies currently qualify as Industrial Companies within the definition of the Law for the Encouragement of Industry (Taxes), 1969 (referred to as the Industry Encouragement Law). According to the Industry Encouragement Law, an Industrial Company is a company resident in Israel, at least 90% of the income of which in any tax year (exclusive of income from defense 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 following preferred corporate tax benefits are available to Industrial Companies: (a) deduction of purchases of know-how and patents over an eight-year period for tax purposes; (b) under certain interpretations, deduction of expenses incurred in connection with a public issuance of securities over a three-year period; and (c) an election under certain conditions to file a consolidated tax return with additional related Israeli Industrial Companies and/or with a company that controls an Industrial Company and a specified percentage of its assets are invested in industrial companies.

Eligibility for the benefits under the Industry Encouragement Law is not subject to receipt of prior approval from any governmental authority. No assurance can be given that any of our group companies will qualify and/or continue to qualify as an Industrial Company or that the benefits described above will be available in the future.

Capital Gains Tax

Israeli law imposes a capital gains tax on the sale of capital assets. The law distinguishes between the Real Gain and the Inflationary Surplus. The Real Gain is the excess of the total capital gain over the Inflationary Surplus, computed on the basis of the increase of the consumer price index between the date of purchase and date of sale. The Inflationary Surplus accumulated until December 31, 1993 is taxed at a rate of 10% for residents of Israel (reduced to no tax for non-residents if calculated according to the exchange rate of the foreign currency lawfully invested in shares of an Israeli resident company, instead of the consumer price index). Inflationary Surplus accumulated from and after December 31, 1993 is exempt from any capital gains tax, while the Real Gain is added to ordinary income, which effective until December 31 2002 is taxed at the marginal rate of up to 49% for individuals and 35% for corporations (in 2004). Effective January 1, 2003, the capital gains tax rate imposed upon sale of capital assets acquired after that date has been reduced to 25%; capital gains accrued from assets acquired before that date are subject to a blended tax rate based on the relative periods of time before and after that date that the asset was held.

Under current law, effective January 1, 2003 so long as our ordinary shares are listed on a stock exchange the sale of these shares is subject to 15% tax in case the shares were purchased after December 31, 2002, and in case the shares were purchased before that date the sale will be subject to a blended tax in which the portion of the gain accrued until December 31, 2002 will be exempt from Israeli capital gains tax and the portion of the real gain accrued from January 1, 2003 until the date of sale will be subject to 15% tax. The taxable real gain will be based on the difference between the adjusted average value of the shares during the last three trading days before January 1, 2003 (or the adjusted original cost if it is higher than the adjusted average value) and the value of the shares at the date of sale. In the event the above mentioned calculation creates a loss, such loss can only be offset against a capital gain from other traded securities according to the provisions of the Israeli law. The amount of the loss is limited to the difference between the adjusted average value and the value of the shares at the date of sale.

In addition, if our ordinary shares are traded on the Tel Aviv Stock Exchange (or listed on a stock exchange recognized by the Israeli Ministry of Finance), gains on the sale of ordinary shares held by non-Israeli tax resident investors will generally be exempt from Israeli capital gains tax. Notwithstanding the foregoing, dealers in securities in Israel and companies taxed under the Inflationary Adjustment Law are taxed at regular tax rates applicable to business income.

Employee Stock Options

Effective from January 1, 2003, the Tax Reform Legislation enables a company to grant options through one of three tax tracks:

(a) the income tax track through a trustee pursuant to which the optionee pays income tax rate (according to the marginal tax rate of the optionee- up to 49% tax) plus payments to the National Insurance Institute and health tax on the profit gained upon the earlier to occur of the transfer of the options or the underlying shares from the trustee to the optionee or the sale of the options or the underlying shares by the trustee, and the company may recognize expenses pertaining to the options for tax purposes. The options (or upon their exercise, the underlying shares), must be held by a trustee for a period of 12 months commencing from the end of the year in which the options were granted; or

(b) the capital gains tax track through a trustee pursuant to which the optionee pays capital gains tax at a rate of 25% on the profit upon, the earlier to occur of the transfer of the options or the underlying shares from the trustee to the optionee or the sale of the options or the underlying shares by the trustee (in this track the optionee is not required to make payments to the National Insurance Institute and health tax) and the Company may not recognize expenses pertaining to the options for tax purposes. The options (or upon their exercise, the underlying shares), must be held by a trustee for a period of 24 months commencing from the end of the year in which the options were granted; or

(c) the income tax track without a trustee pursuant to which the optionee pays income tax rate (according to the marginal tax rate of the optionee- up to 49% tax) plus payments to the National Insurance Institute and health tax on the profit upon the sale of the underlying shares, and the company may not recognize expenses pertaining to the options for tax purposes.

In accordance with the provisions of the Tax Reform Legislation, if a company has selected the capital gains track, the company must continue granting options under the selected capital gains track until the end of the year following the year in which the first grant of options under that trustee track will be made. Notwithstanding the above, the company may at any time also grant options under the provisions of the income tax track without a trustee.

The above rules apply only to employees, including officer holders but excluding controlling shareholders.

U.S.-Israel Tax Treaty

Pursuant to the Convention Between the Government of the United States of America and the Government of Israel with Respect to Taxes on Income (referred to as the U.S.-Israel Tax Treaty), the sale, exchange or disposition of ordinary shares by a person who qualifies as a resident of the United States within the meaning of the U.S.-Israel Tax Treaty and who is entitled to claim the benefits afforded to such resident by the U.S.-Israel Tax Treaty (called a Treaty U.S. Resident) will not be subject to Israeli capital gains tax unless (a) such Treaty U.S. Resident is an individual and was present in Israel for more than 183 days during the relevant taxable year or (b) such Treaty U.S. Resident holds, directly or indirectly, shares representing 10% or more of the voting power of a company during any part of the 12-month period preceding such sale, exchange or disposition. A sale, exchange or disposition of shares by a Treaty U.S. Resident who is an individual and was present in Israel for more than 183 days during the relevant taxable year or who holds, directly or indirectly, shares representing 10% or more of the voting power of a company at any time during such preceding 12-month period would be subject to such Israeli tax, to the extent applicable, unless the aforementioned exemption from capital gain tax for shares listed on the Tel-Aviv Stock Exchange applies; however, in case under the U.S.-Israel Tax Treaty and the Israeli tax law a Treaty U.S. Resident will be subject to capital gain tax in Israel, such Treaty U.S. Resident would be permitted to claim a credit for such taxes against the U.S. income tax imposed with respect to such sale, exchange or disposition, subject to the limitations in U.S. laws applicable to foreign tax credits.

Taxation of Non-Residents

Non-residents of Israel are subject to income tax on income accrued or derived from sources in Israel. Such sources of income include passive income such as dividends, royalties and interest, as well as non-passive income from services rendered in Israel and capital gain as mentioned above. On distributions of dividends other than bonus shares (stock dividends), income tax at the rate of 25% is withheld at source, unless a different rate is provided in a treaty between Israel and the shareholder's country of residence. For example, the tax rate would be 12.5% if the non-resident is a company which holds 10% or more of our voting power (during the part of our tax year which precedes the date of payment of the dividend and during the entire prior tax year) which pursuant to the U.S.-Israel Tax Treaty. Under the U.S.-Israel Tax Treaty, the maximum tax on dividends paid to a holder of ordinary shares who is a resident of the United States will be 25%. However, under the Investment Law, dividends generated by an Approved Enterprise in any case are taxed at the rate of 15%.

U.S. Federal Income Tax Considerations

Subject to the limitations described herein, this discussion summarizes the material U.S. federal income tax consequences of the purchase, ownership and disposition of our ordinary shares to a U.S. holder. A U.S. holder is a holder of our ordinary shares who is:

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

Unless otherwise specifically indicated, this discussion does not consider the U.S. tax consequences to a person that is not a U.S. holder and considers only U.S. holders that will own the ordinary shares as capital assets.

This discussion is based on current provisions of the Internal Revenue Code of 1986, as amended (the "Code"), current and proposed Treasury regulations promulgated under the Code and administrative and judicial interpretations of the Code, all as currently in effect and all of which are subject to change, possibly with a retroactive effect. This discussion does not address all aspects of U.S. federal income taxation that may be relevant to any particular U.S. holder based on the U.S. holder's particular circumstances. In particular, this discussion does not address the U.S. federal income tax consequences to U.S. holders who are broker-dealers or who own, directly, indirectly or constructively, 10% or more of our outstanding voting shares, U.S. holders holding the ordinary shares as part of a hedging, straddle or conversion transaction, U.S. holders whose functional currency is not the U.S. dollar, insurance companies, tax-exempt organizations, financial institutions and persons subject to the alternative minimum tax, who may be subject to special rules not discussed below. Additionally, the tax treatment of persons who are, or hold the ordinary shares through, a partnership or other pass-through entity is not considered, nor is the possible application of U.S. federal estate or gift taxes or any aspect of state, local or non-U.S. tax laws.

You are advised to consult your tax advisor with respect to the specific U.S. federal, state, local and foreign income tax consequences to you of purchasing, holding or disposing of our ordinary shares.

Taxation of Distributions on Ordinary Shares

Subject to the discussion below under "Tax Consequences If we are a Passive Foreign Investment Company," a distribution paid by us with respect to the ordinary shares to a U.S. holder will be treated as dividend income to the extent that the 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 with respect to the ordinary shares will equal the amount of cash and the fair market value of any property distributed and will also include the amount of any Israeli taxes withheld as described above under "Taxation of Non-Residents." Dividends that are received by U.S. holders that are individuals, estates or trusts will be taxed at the rate applicable to long-term capital gains (a maximum rate of 15%), provided that such dividends meet the requirements of “qualified dividend income.” Dividends that fail to meet such requirements, and dividends received by corporate U.S. holders are taxed at ordinary income rates. No dividend received by a U.S. holder will be a qualified dividend (1) if the U.S. holder held the ordinary share with respect to which the dividend was paid for less than 61 days during the 121-day period beginning on the date that is 60 days before the ex-dividend date with respect to such dividend, excluding for this purpose, under the rules of Code section 246(c), any period during which the U.S. holder has an option to sell, is under a contractual obligation to sell, has made and not closed a short sale of, is the grantor of a deep-in-the-money or otherwise nonqualified option to buy, or has otherwise diminished its risk of loss by holding other positions with respect to, such ordinary share (or substantially identical securities); or (2) to the extent that the U.S. holder is under an obligation (pursuant to a short sale or otherwise) to make related payments with respect to positions in property substantially similar or related to the ordinary share with respect to which the dividend is paid. If we were to be a “passive foreign investment company” (as such term is defined in the Code) for any year, dividends paid on our ordinary shares in such year or in the following year would not be qualified dividends. In addition, a non-corporate U.S. holder will be able to take a qualified dividend into account in determining its deductible investment interest (which is generally limited to its net investment income) only if it elects to do so; in such case the dividend will be taxed at ordinary income rates.

The amount of any distribution which exceeds the amount treated as a dividend will be treated first as a non-taxable return of capital, reducing the U.S. holder’s tax basis in its ordinary shares to the extent thereof, and then as capital gain from the deemed disposition of the ordinary shares. Corporate holders will not be allowed a deduction for dividends received in respect of the ordinary shares.

Dividends paid by us in NIS will be included in the income of U.S. holders at the dollar amount of the dividend (including any Israeli taxes withheld therefrom), based upon the spot rate of exchange in effect on the date the distribution is included in income, U.S. holders will have a tax basis in the NIS for U.S. federal income tax purposes equal to that dollar value. Any subsequent gain or loss in respect of the NIS arising from exchange rate fluctuations will generally be taxable as U.S. source ordinary income or loss.

Subject to the limitations set forth in the Code and the Treasury regulations thereunder, U.S. holders may elect to claim as a foreign tax credit against their U.S. federal income tax liability the Israeli income tax withheld from dividends received in respect of the ordinary shares. The limitations on claiming a foreign tax credit include, among others, computation rules under which foreign tax credits allowable with respect to specific classes of income cannot exceed the U.S. federal income taxes otherwise payable with respect to each such class of income. In this regard, dividends paid by us will be foreign source “passive income” for U.S. foreign tax credit purposes or, in the case of a financial services entity, “financial services income”(and, for tax years beginning after December 31, 2006, as "general category income"). U.S. holders that do not elect to claim a foreign tax credit may instead claim a deduction for the Israeli income tax withheld if they itemize deductions. The rules relating to foreign tax credits are complex, and you should consult your tax advisor to determine whether and to what extent you would be entitled to this credit. A U.S. holder will be denied a foreign tax credit for Israeli income tax withheld from a dividend received on the ordinary shares (i) if the U.S. holder has not held the ordinary shares for at least 16 days of the 30 day period beginning on the date which is 15 days before the ex-dividend date with respect to such dividend or (ii) to the extent the U.S. holder is under an obligation to make related payments with respect to positions in substantially similar or related property. Any days during which a U.S. holder has substantially diminished its risk of loss on the ordinary shares are not counted toward meeting the required 16 day holding period. Distributions of current or accumulated earnings and profits will be foreign source passive income for U.S. foreign tax credit purposes.

Taxation of the Disposition of Ordinary Shares

Subject to the discussion below under “Tax Consequences if We are a Passive Foreign Investment Company,” 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 the amount realized on the disposition and the U.S. holder’s tax basis in the ordinary shares. The gain or loss recognized on the disposition of the ordinary shares will be long-term capital gain or loss if the U.S. holder held the ordinary shares for more than one year at the time of the disposition and is eligible for a maximum 15% rate of taxation for individuals. Capital gain from the sale, exchange or other disposition of ordinary shares held for one year or less is short-term capital gain and taxed as ordinary income at a maximum rate of 35%. Gain or loss recognized by a U.S. holder on a sale, exchange or other disposition of ordinary shares will be treated as U.S. source income or loss for U.S. foreign tax credit purposes.

A U.S. holder that uses the cash method of accounting calculates the dollar value of the proceeds received on the sale as of the date that the sale settles. However, a U.S. holder that uses the accrual method of accounting is required to calculate the value of the proceeds of the sale as of the trade date and may therefore realize foreign currency gain or loss. A U.S. holder may avoid realizing foreign currency gain or loss by electing to use the settlement date to determine the proceeds of sale for purposes of calculating the foreign currency gain or loss. In addition, a U.S. holder that receives foreign currency upon disposition of ordinary shares and converts the foreign currency into dollars after the settlement date or trade date (whichever date the U.S. holder is required to use to calculate the value of the proceeds of sale) will have foreign exchange gain or loss based on any appreciation or depreciation in the value of the foreign currency against the dollar, which will generally be U.S. source ordinary income or loss.

Tax Consequences if We are a Passive Foreign Investment Company

We will be a passive foreign investment company, or PFIC, if either (1) 75% or more of our gross income in a taxable year is passive income; or (2) 50% or more of the value, determined on the basis of a quarterly average, of our assets in a taxable year are held for the production of passive income. If we own (directly or indirectly) at least 25% by value of the stock of another corporation, we will be treated for purposes of the foregoing tests as owning our proportionate share of the other corporation's assets and as directly earning our proportionate share of the other corporation's income. If we are a PFIC, a U.S. holder must determine under which of three alternative taxing regimes it wishes to be taxed:

The "QEF" regime applies (to the exclusion of the "excess distribution" regime, described below) if the U.S. holder elects to treat us as a "qualified electing fund" ("QEF") for the first taxable year in which the U.S. holder owns our ordinary shares during which we are a PFIC, and if we comply with certain reporting requirements. If the QEF regime applies, then each year that we are a PFIC such U.S. holder will include in its gross income a proportionate share of our ordinary earnings (which is taxed as ordinary income) and net capital gain (which is taxed as long-term capital gain), subject to a separate election to defer payment of taxes, which deferral is subject to an interest charge. These amounts would be included in income by an electing U.S. holder for its taxable year in which our taxable year ends, whether or not such amounts are actually distributed to the U.S. holder. A U.S. holder's basis in our ordinary shares for which a QEF election has been made would be increased to reflect the amount of any taxed but undistributed income. Generally, a QEF election allows an electing U.S. holder to treat any gain realized on the disposition of his ordinary shares as capital gain.

Once made, the QEF election applies to all subsequent taxable years of the U.S. holder in which it holds our ordinary shares and for which we are a PFIC and can be revoked only with the consent of the Internal Revenue Service. A shareholder makes a QEF election by attaching a completed Internal Revenue Service Form 8621, including the PFIC annual information statement, to a timely filed United States federal income tax return. Even if a QEF election is not made, a U.S. person who is a shareholder in a PFIC must file a completed Internal Revenue Service Form 8621 every year.

If a QEF election is made by the U.S. holder after the first taxable year in which the U.S. holder holds our ordinary shares during which we are a PFIC, then both the QEF regime and the excess distribution regime, defined below, will apply simultaneously unless the U.S. holder makes a special election.

A second regime, the "mark-to-market" regime, may be elected so long as our ordinary shares are publicly traded. Pursuant to this regime, an electing U.S. holder's ordinary shares are marked-to-market each year in which we are a PFIC, and the U.S. holder recognizes as ordinary income or loss an amount equal to the difference as of the close of the taxable year between the fair market value of our ordinary shares and the U.S. holder's adjusted tax basis in our ordinary shares. Losses are allowed only to the extent of net mark-to-market gain previously included by the U.S. holder under the election for prior taxable years. An electing U.S. holder's adjusted basis in our ordinary shares is increased by income recognized under the mark-to-market election and decreased by the deductions allowed under the election.

Under the mark-to-market election, as long as we are a PFIC, gain on the sale of our ordinary shares is treated as ordinary income, and loss on the sale of our ordinary shares, to the extent the amount of loss does not exceed the net mark-to-market gain previously included, is treated as ordinary loss. The mark-to-market election applies to the tax year for which the election is made and all later tax years in which we are a PFIC, unless the ordinary shares cease to be marketable or the Internal Revenue Service consents to the revocation of the election.

If the mark-to-market election is made after the first taxable year in which a U.S. holder holds our ordinary shares and we are a PFIC, then special rules would apply.

A U.S. holder making neither the QEF election nor the mark-to-market election is subject to the “excess distribution” regime. Under this regime, “excess distributions” are subject to special tax rules. An excess distribution is either (1) a distribution with respect to shares that is greater than 125% of the average distributions received by the U.S. holder from us over the shorter of either the preceding three years or such U.S. holder’s holding period for our shares, or (2) 100% of the gain from the disposition of our shares (including gain deemed recognized if the ordinary shares are used as security for a loan).

Excess distributions must be allocated ratably to each day that a U.S. holder has held our ordinary shares. A U.S. holder must include amounts allocated to the current taxable year, as well as amounts allocated to taxable years prior to the first year in which we were a PFIC, in its gross income as ordinary income for that year. All amounts allocated to prior years of the U.S. holder during which we were a PFIC would be taxed at the highest tax rate applicable to ordinary income for each such prior year. The U.S. holder also would be liable for interest on the deferred tax liability for each such prior year calculated as if such liability had been due with respect to each such prior year. A U.S. holder that is an individual is not allowed a deduction for interest on the deferred tax liability. The portions of gains and distributions that are not characterized as “excess distributions” are subject to tax in the current year under the normal tax rules of the Code.

A U.S. person who inherits shares in a foreign corporation that was a PFIC in the hands of the decedent (who was not a nonresident alien and did not make either of the elections described above), is denied the otherwise available step-up in the tax basis of such shares to fair market value at the date of death. The U.S. person steps into the shoes of the decedent and will be subject to the rules described above.

Concurrently with the announcement of the sale of our shares in Elbit Systems Ltd. in July 2004, we announced that, as a result of the transaction, we may be characterized as a PFIC for 2004. At the time we filed our Form 6-K with the Securities and Exchange Commission regarding this matter, however, we believed, and our tax advisors concurred, that for 2004 we could potentially rely on the “change of business” exception to PFIC status provided under Section 1298(b)(3) of the U.S. Internal Revenue Code of 1986, as amended. Pursuant to this exception, in order to avoid PFIC status in 2004, among other requirements, we cannot be a PFIC in 2005 or 2006 (which cannot be determined at this time) or in any year prior to 2004 (which we believe was not the case). The tests for determining PFIC status are impacted, by among other factors, changes in our holdings and in the value of our group companies which are difficult to predict.Moreover, the sale of our shares in Partner in 2005, generated significant passive income. As a result, we believe that it is reasonably possible that we will be treated as a PFIC in 2005 and, as a result, in 2004 as well. The ultimate determination of our PFIC status in 2005 will depend on the composition of our gross income and assets for the entire year and the values of those assets, which are difficult to predict at this time and the appropriate value of our ownership interest in our group companies. Therefore, it is unclear whether the "change of business" exception would ultimately be satisfied for 2004.

We cannot assure you that the Internal Revenue Service will not challenge our reliance on the "change of business" exception or our assumptions and methodologies used in determining our percentage of passive assets and income. If there were such challenges, we could be classified as a passive foreign investment company for 2004, even if we are not a PFIC in 2005 or 2006.

With respect to subsequent years, the tests for determining passive foreign investment company status are applied annually and it is difficult to make accurate predictions of future income and assets, which are relevant to this determination. As described above, the tests are impacted, by, among other factors, changes in value of our group companies which are difficult to predict at this time and the appropriate value of our ownership interest in our group companies. Accordingly, there can be no assurance that we will not become a PFIC for the current fiscal year ending December 31, 2005 or in a future year. We will notify U.S. holders in the event we conclude that we will be treated as a PFIC for any taxable year to enable U.S. holders to consider whether or not to elect to treat us as a QEF for U.S. federal income tax purposes or to "mark to market" the ordinary shares or to become subject to the "excess distribution" regime.

U.S. holders are urged to consult their tax advisors regarding the application of the PFIC rules, including eligibility for and the manner and advisability of making, the QEF election or the mark-to-market election.

Information Reporting and Backup Withholding

A U.S. holder generally is subject to information reporting and may be subject to backup withholding at a rate of up to 28% with respect to dividend payments and receipt of the proceeds from the disposition of the ordinary shares. Backup withholding will not apply with respect to payments made to exempt recipients, including corporations and tax-exempt organizations, or if a U.S. holder provides a correct taxpayer identification number (or certifies that he has applied for a taxpayer identification number), certifies that such holder is not subject to backup withholding or otherwise establishes an exemption. 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, or alternatively, the U.S. holder may be eligible for a refund of any excess amounts withheld under the backup withholding rules, in either case, provided that the required information is furnished to the Internal Revenue Service.

Non-U.S. holders of Ordinary Shares

Except as provided below, a non-U.S. holder of ordinary shares (except certain former U.S. citizens and long-term residents of the United States) will not be subject to U.S. federal income or withholding tax on the receipt of dividends on, and the proceeds from the disposition of, an ordinary share, unless that item is effectively connected with the conduct by the non-U.S. holder of a trade or business in the United States and, in the case of a resident of a country which has an income tax treaty with the United States, that item is attributable to a permanent establishment in the United States or, in the case of an individual, a fixed place of business in the United States. In addition, gain recognized by an individual non-U.S. holder will be subject to tax in the United States if the non-U.S. holder is present in the United States for 183 days or more in the taxable year of the sale and other conditions are met.

Non-U.S. holders will not be subject to information reporting or backup withholding with respect to the payment of dividends on ordinary shares unless the payment is made through a paying agent, or an office of a paying agent, in the United States. Non-U.S. holders will be subject to information reporting and backup withholding at a rate of up to 28% with respect to the payment within the United States of dividends on the ordinary shares unless the holder provides its taxpayer identification number, certifies to its foreign status, or otherwise establishes an exemption.

Non-U.S. holders will be subject to information reporting and backup withholding at a rate of up to 28% on the receipt of the proceeds from the disposition of the ordinary shares to, or through, the United States office of a broker, whether domestic or foreign, unless the holder provides a taxpayer identification number, certifies to its foreign status or otherwise establishes an exemption. Non-U.S. holders will not be subject to information reporting or backup withholding with respect to the receipt of proceeds from the disposition of the ordinary shares by a foreign office of a broker; provided, however, that if the broker is a U.S. person or a “U.S. related person,” information reporting (but not backup withholding) will apply unless the broker has documentary evidence in its records of the non-U.S. holder’s foreign status or the non-U.S. holder certifies to its foreign status under penalties of perjury or otherwise establishes an exemption. For this purpose, a “U.S. related person” is a broker or other intermediary that maintains one or more enumerated U.S. relationships. Backup withholding is not an additional tax and may be claimed as a credit against the U.S. federal income tax liability of a non-U.S. holder, or alternatively, the non-U.S. holder may be eligible for a refund of any excess amounts withheld under the backup withholding rules, in either case, provided that the required information is furnished to the Internal Revenue Service.

F. Dividends and Paying Agents

Not Applicable.

G. Statement by Experts

Not Applicable.

H. Documents on Display

We are required to file reports and other information with the Securities and Exchange Commission, or SEC, under the Securities Exchange Act of 1934 and the regulations thereunder applicable to foreign private issuers. Reports and other information filed by us with the SEC may be inspected and copied at the SEC’s public reference facilities described below. Although as a foreign private issuer we are not required to file periodic information as frequently or as promptly as United States companies, we generally do publicly announce our quarterly and year-end results promptly and file periodic information with the SEC under cover of Form 6-K. As a foreign private issuer, we are also exempt from the rules under the Exchange Act prescribing the furnishing and content of proxy statements and our officers, directors and principal shareholders are exempt from the reporting and other provisions in Section 16 of the Exchange Act.

You may review a copy of our filings with the SEC, including any exhibits and schedules, at the SEC's public reference facilities in Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549 and at the regional offices of the SEC. You may also obtain copies of such materials from the Public Reference Section of the SEC, Room 1024, Judiciary Plaza, 450 Fifth Street, N.W., Washington, D.C. 20549, at prescribed rates. You may call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. You may read and copy any reports, statements or other information that we file with the Securities and Exchange Commission at the facilities listed above. In addition, certain of our filings are available to the public at the SEC's website at http://www.sec.gov. We also generally make available on our own web site (www.elron.com) all our quarterly and year-end financial statements as well as other information. Our website is not part of this Annual Report.

Any statement in this Annual Report about any of our contracts or other documents is not necessarily complete. If the contract or document is filed as an exhibit to this Annual Report, the contract or document is deemed to modify the description contained in this Annual Report. We urge you to review the exhibits themselves for a complete description of the contract or document.

I. Subsidiary Information

Not Applicable.

Item 11. Quantitative and Qualitative Disclosures About Market Risk

For disclosures regarding our market risk exposures, see Item 5 Operating and Financial Review and Prospects above.

Item 12. Descriptions of Securities Other than Equity Securities

Not Applicable.

PART II

Item 13. Defaults, Dividend Arrearages and Delinquencies

Not Applicable.

Item 14. Material Modifications to the Rights of Security Holders and Use of Proceeds

Not Applicable.

Item 15. <u>Controls and Procedures</u>

Our Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e)of the Securities Exchange Act of 1934, as amended), have concluded that, as of December 31, 2004, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure and is recorded, processed, and reported within the periods specified by the SEC's rules and forms. There were no changes in our internal controls over financial reporting identified with the evaluation thereof that occurred during the period covered by this annual report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 16. [Reserved]

Item 16A. Audit Committee Financial Expert

The board of directors has determined that Mr. Yaacov Goldman is the audit committee financial expert serving on its audit committee.

Item 16B. Code of Ethics

We have adopted a code of ethics applicable to our employees, officers and directors as well as to employees, officers and directors of our wholly owned subsidiary, Elron TeleSoft. A copy of the code of ethics was filed as an Exhibit 11.1 to our Annual Report on Form 20F filed with the Securities Exchange Commission on June 29, 2004, and is also available on our website, *www.elron.com*.

Item 16C. Principal Accountant Fees and Services

The following table sets forth the total remuneration that was paid by us and our subsidiaries to our principal accountants Kost Forer Gabbay & Kasierer (a member of Ernst & Young Global) and our former principal accountants Luboshitz Kasierer (an affiliate member of Ernst & Young International) in each of our previous two fiscal years:

	2003	2004
	(in thousands)	
Audit fees (1)	234	250
Tax fees (2)	127	209
All other fees (3)	17	-
Total	378	459

(1) Audit Fees consist of fees billed for the annual audit services engagement and other audit services, which are those services that only the external auditor can reasonably provide, and include statutory audits; comfort letters and consents; and assistance with and review of documents filed with the SEC.

(2) Tax Fees include fees billed for tax compliance services, including the preparation of original and amended tax returns and claims for tax refund; tax consultations, such as assistance and representation in connection with tax audits and appeals, and requests for rulings or technical advice from taxing authority; and tax planning services.

(3) All other fees include permissible services provided by the independent auditors that do not fall into the above-mentioned categories.

Our audit committee's policy is to pre-approve each audit and non-audit service to be performed by our independent auditors for us and our subsidiaries.

Item 16D. Exemptions from the Listing Standards for Audit Committees

Not yet Applicable

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

On August 22, 2004, DIC completed a tender offer to purchase 2,203,425 of our ordinary shares for $15 per share, net to the seller in cash, less any required withholding taxes and without interest thereby increasing its shareholding to approximately 46%.

Between June 19 and 30, 2005, DIC purchased an additional aggregate of 565,111 of our ordinary shares on the TASE thereby increasing its shareholding to approximately 47.6%.

Except as aforesaid, neither we nor any affiliated purchaser purchased any of our equity securities during the period covered by this Annual Report.

PART III

Item 17. Financial Statements

Not Applicable.

Item 18. Financial Statements

The financial statements follow the certifications following the signature page of this Annual Report.

Item 19. <u>Exhibits</u>

1.1 Articles of Association (English translation) approved by the registrant's shareholders on March 19, 2000, incorporated by reference to Exhibit 1.1 to the registrant's Form 20-F for the year ended December 31, 2000, filed with the Commission on June 8, 2001.

1.2 Memorandum of Association of Elron Electronic Industries Ltd., incorporated by reference to Exhibit 1.2 to the registrant's Form 20-F for the year ended December 31, 2000, filed with the Commission on June 8, 2001.

4.1 Agreement dated as of April 1993 among Discount Investment Corporation Ltd., PEC Israel Economic Corporation, Rafael Armament Development Authority Ltd., Galram Technology Industries Limited, incorporated by reference to Exhibit 10.4 to Amendment No. 5 to the registrant's Registration Statement on Form F-4, filed with the Commission on March 14, 2002 ("RDC Joint Venture Agreement").

4.2 License from the Israeli Ministry of Communications issued to Partner Communications Company Ltd. on April 8, 1998, incorporated by reference to Exhibit 4.5 to the Annual Report on Form 20-F/A of Elbit Ltd., filed with the Commission on March 15, 2002 as may be amended from time to time and incorporated in subsequent filings by Partner with the Commission.

4.3 Agreement and Plan of Merger between Elron Electronic Industries Ltd. and Elbit Ltd. dated October 31, 2001, incorporated by reference to Exhibit 2.1 to the registrant's Registration Statement on Form F-4, filed with the Commission on November 15, 2001.

4.4 Share Purchase Agreement dated as of November 19, 2001, between Elron Electronic Industries Ltd. and Discount Investment Corporation Ltd., incorporated by reference to Exhibit 10.1 to the registrant's Registration Statement on Form F-4, filed with the Commission on November 15, 2001.

4.5 Addendum to Agreement dated June 16, 2003 among DEP Technology Holdings Ltd., Rafael Armament Development Authority Ltd., Galram Technologies Industries Ltd. and RDC Rafael Development Corporation Ltd. incorporated by reference to Exhibit 4.17 of the registrant's Form 20-F, filed with the Commission on June 30, 2003.

4.6 Irrevocable Offer Letter dated February 7, 2005 by Elbit Ltd., Eurocom Communications Ltd. Polar Comunications Ltd., Matav Investments Ltd. and Matav Cable Systems Media Ltd setting forth the terms of the Buyback Offer to Partner Communications Company Ltd. incorporated by reference to Exhibit 1 to amendment no. 2 to registrant's filing on Form 13 D filed with the Commission on March 1, 2005.

4.7 Restatement of Relationship Agreement dated April 20, 2005 by and among Hutchison Telecommunications International (Netherlands) B.V., Advent Investments Pte Ltd., Elbit Ltd., Eurocom Communications Ltd. Polar Comunications Ltd., Matav Investments Ltd., Matav Cable Systems Media Ltd. and Tapuz Cellular Systems Ltd. incorporated by reference to Exhibit 1 to amendment no. 3 to registrant's filing on Form 13 D filed with the Commission on May 16, 2005.

4.8 Shareholders Agreement dated April 20, 2005 by and among Elbit Ltd., Eurocom Communications Ltd. Polar Comunications Ltd., Matav Investments Ltd. and Matav Cable Systems Media Ltd.incorporated by reference to Exhibit 2 to amendment no.3 to registrant's filing on Form 13 D filed with the Commission on May 16, 2005.

4.9 English Translation of Deed of Transfer to the Federmann Group dated July 28, 2004.
8.1 List of subsidiaries
11.1 Code of Ethics. incorporated by reference to Exhibit 11.1 to the registrant's Annual Report on Form 20-F., filed with the Commission on June 30, 2004.
12.1 Certification of Chief Executive Officer of the Registrant pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
12.2 Certification of Chief Financial Officer of the Registrant pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
13.1 Certification of Chief Executive Officer of the Registrant pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
13.2 Certification of Chief Financial Officer of the Registrant pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
15.1 Consent of Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global, for Elron Electronic Industries Ltd.
15.2 Consent of Luboshitz Kasierer, an affiliate member of Ernst & Young International, for Elron Electronic Industries Ltd.
15.3 Consent of Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global, for Elbit Systems Ltd.
15.4 Consent of Luboshitz Kasierer, an affiliate member of Ernst & Young International, for Elbit Systems Ltd.
15.5 Consent of Brightman Almagor & Co., a member of Deloitte Touche Tohmatsu, for A.M.T. Advanced Metal Technologies Ltd.
15.6 Consent of Somekh Chaikin, a member of KPMG International, for Given Imaging Ltd.
15.7 Consent of Somekh Chaikin, a member of KPMG International, for DEP Technology Holdings Ltd.
15.8 Consent of PricewaterhouseCoopers LLP for ChipX Incorporated.
15.9 Consent of Kesselman & Kesselman CPA(Isr.) a member of PricewaterhouseCoopers Intenational Limited for Notal Vision, Inc.
15.10 Consent of PriceWaterhouseCoopers LLP for Oncura, Inc.
15.11 Consent of Kesselman & Kesselman CPA(Isr.) a member of PricewaterhouseCoopers Intenational Limitedfor Pulsicom Israel Technologies Ltd.
15.12 Consent of Kesselman & Kesselman CPA(Isr.) a member of PricewaterhouseCoopers Intenational Limited for Ingenio Technologies Ltd.

* This document is being furnished in accordance with SEC Release No. 33-8212 and 34-47551.

SIGNATURES

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

Dated: July 13, 2005

ELRON ELECTRONIC INDUSTRIES LTD.

By: /s/ Doron Birger
Name: Doron Birger
Title: President & Chief Executive Officer

By: /s/ Tal Raz
Name: Tal Raz
Title: Vice President & Chief Financial Officer