Consolidated Financial Statements 2002

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Financial Overview

1. General

2002 was another very successful year for SHL TeleMedicine. It was characterized by entering into new markets, which contributed significant growth in revenues, profits and cash flow.

In the international markets, in April 2002 we acquired Raytel Medical Corporation, a leading US healthcare services provider which operates in cardiac telemedicine services and diagnostic imaging services and which will provide a platform for SHL's expansion into the US market. In Europe, the joint venture with Philips Medical Systems enhanced its operations and is in process of signing up new subscribers.

In our home market, we continue to grow and to increase our market share. In addition, during the year, we launched the service of "Thin for Life", a new and unique telemedicine product aimed at combating obesity and the various problems associated with weight excess.

Despite the difficult economic environment internationally and in Israel, we achieved our best operating performance in our history. Revenues totaled USD 89.8 million, with EBITDA of USD 18.1 million, and EBIT of USD 11.7 million, compared to USD 30.6 million, USD 10.8 million, and USD 9 million, respectively in 2001. Net income for the year totaled USD 1.4 million, as against USD 12.1 million in the previous year.

2. Results of Operations

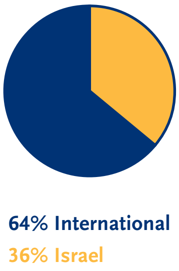
Revenues in 2002 totaled USD 89.8 million, a 193% increase over the revenues in 2001 of USD 30.6 million. The increase in revenues resulted mainly from the growth in international operations resulting from the Raytel acquisition as well as from growth in sales in our home market.

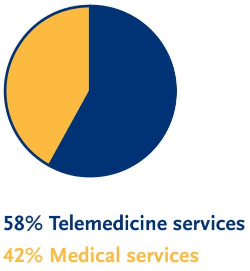
The Company now operates in two segments:

- the Telemedicine services segment which covers the provision of telemedicine services utilizing telephonic and Internet communication technology and the selling of related instruments through direct sales or by license and
- the Medical services segment which covers the operations of a network of imaging centers and cardiac facilities that provide diagnostic, therapeutic and patient management services primarily associated with cardiovascular disease. The segment also operates medical call centers, which provide 24-hours doctor "house-call" services.

Revenues from the Telemedicine services segment amounted to USD 52.4 million in 2002 comprising 58% of total revenues with revenues from the Medical services segment reaching USD 37.4 million – 42% of total revenues.

Geographically, revenues from the international market amounted to USD 57.4 million in 2002, compared to USD 6.7 million in 2001, with revenues from the local market amounting to USD 32.4 million in 2002, compared to USD 23.9 million in 2001, an increase of 35.6%.





Gross Profit

Gross profit in 2002 totaled USD 45.8 million compared to USD 20.0 million in 2001, representing a 129.0% increase. The gross margin for the year decreased to 51% from 65% in 2001 due primarily to the effect of the different product mix following the growth of the international operations which increased our revenues and profit but with lower margins.

Research and Development (R&D)

R&D expenditure for the year totaled USD 1.7 million, 1.9% of revenues, compared to USD 1.6 million, 4.4% of revenues, in 2001 representing an increase of 6%. The amount of R&D charged to the statement of operations for 2002, which reflects the capitalization and amortization of the R&D investment over the years, amounted to USD 0.42 million, 0.46% of revenues, compared to USD 0.47 million, 1.55% of revenues, in 2001.

Selling and Marketing Expenses

Selling and marketing expenses totaled USD 7.0 million, 7.8% of revenues in 2002, compared to USD 4.1 million and 3.4% of revenues in 2001. The increase in selling and marketing expenses is attributed primarily to Raytel's operations.

General and Administration Expenses (G&A)

G&A expenses totaled USD 26.7 million, 29.7% of revenues, in 2002 compared to USD 6.4 million and 20.8% of revenues in 2001. The increase in the amount of G&A expenses is also attributed primarily to Raytel's operations.

Earnings before Income Tax, Depreciation and Amortization (EBITDA), Earnings before Income Tax (EBIT)

EBITDA for the year increased by 67.6% to USD 18.1 million, 20.1% of revenues, compared to USD 10.8 million and 35.4% of revenues, in 2001. EBIT increased to USD 11.7 million,13.0% of revenues, compared to USD 9 million and 29.5% of revenues in 2001.

This growth in profitability resulted mainly from the Raytel acquisition and from the growth in our home market due to a continuing demand for our products.

Financial Income

Financial gains for the year amounted to USD 1.8 million as against USD 8.4 million in 2001 and represent one of the major causes in the reduction of the Company's net income compared to the previous year. This reduction was caused by the utilization of cash resources mainly for the Raytel acquisition and lower interest rates.

Taxes on Income

Taxes on income amounted to USD 3.2 million compared to USD 2.6 million in 2001. The increase in the provision of taxes despite the lower profit before tax is due to an increase of USD 0.7 million in non-deductible expenses and the utilization in the previous year of USD 0.9 million of carryforward tax losses.

Share in Losses and Provision against Shareholders Loan to Associate

In 2002, the Company made a provision of USD 7.4 million (USD 2.6 million in 2001) for its loan investment during the year in Philips HeartCare Telemedicine Services – the European joint venture that we established with Philips Medical Systems. This amount represents the extent of the Company's existing share in the losses associated with the start-up expenses of the joint venture, and a provision covering an additional share in the losses in the event of the Company exercising its option to increase its holding in the joint venture.

Net Profit

Net profit for the year amounted to USD 1.4 million, 1.6% of revenues, reflecting the events described above, compared to USD 12.1 million in 2001.

Earnings per share totaled USD 0.13 compared to USD 1.13 in 2001.

3. Deferred Revenues

Revenues from services are recognized ratably over customers' service contracts.

As at the end of December 2002, we have around USD 90 million of signed services contracts, not included in our balance sheet, to be recognized as revenues in future years.

4. Major Changes in Assets, Liabilities and Equity

At December 31, 2002, our current assets stood at USD 97.8 million compared to USD 75.7 million at year-end 2001, of which USD 51.8 million represents cash balances. The main reason for the increase in current assets is the consolidation of Raytel's trade and other receivables and other current assets.

Our long-term and fixed assets totaled USD 58.8 million compared to USD 38.4 million at the end of the previous year. Again the main reasons for this increase are the consolidation of Raytel's fixed assets and increase in postdated notes derived from the increase of sales of devices in the local market.

Other assets also increased to USD 51.3 million compared to USD 22.1 million at the end of 2001, mainly due to the increase in goodwill resulting from the acquisition of Raytel.

As a result, our total assets at the end of December 2002 totaled USD 207.9 million compared to USD 136.2 million at December 2001.

Current liabilities at December 31, 2002, amounted to USD 71.1 million compared to USD 27.4 million at year-end 2001. Of this amount, bank credit lines utilized at the end of the year amounted to USD 47.6 million compared to USD 20.1 million in 2001. The main reasons for the increase reflect the consolidation of Raytel's loans, trade payables and other payables and bank financing.

Total equity at the end of 2002 amounted to USD 90.5 million compared to USD 95.1 million at the end of 2001. This decrease resulted from the effect of the devaluation of the NIS against the USD on the translated share and paid-in capital.

At December 31, 2002, equity represents some 43.5% of the total assets of the Company.

5. Cash Flow Movement

In 2002, we generated positive cash flow from operating activities in an amount of USD 2.2 million compared to a negative cash flow of USD 1.2 million in 2001. This increase was mainly due to the increased revenues and profitability of the Company.

The Company's investment activities included USD 25 million, in acquiring Raytel, USD 6 million in the joint venture with Philips and USD 4.6 million in other capital expenditure and other assets. In addition USD 3.9 million was eroded due to the devaluation of the NIS against the USD. Most of these amounts were financed by bank credit lines.

At year-end 2002 we held USD 51.8 million in cash against USD 60.2 million, at year-end 2001.

Erez Termechy

Erez Termechy
Vice President and Chief Financial Officer

Auditors' Report to the shareholders of SHL TeleMedicine Ltd.

We have audited the accompanying consolidated balance sheets of SHL TeleMedicine Ltd. and its consolidated companies (the Group) as of December 31, 2002 and 2001, and the related consolidated statements of income, cash flows and changes in the Group's equity for each of the three years in the period ended December 31, 2002. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We did not audit the financial statements of associate, the investment in which on the equity basis of accounting totaled USD 2.0 million and USD 2.6 million as of December 31, 2002 and 2001, respectively, and the Company's share in losses and provision against shareholders' loan totaled USD 7.4 million and USD 2.6 million for the years ended December 31, 2002 and 2001, respectively. These financial statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to data included for this certain associate, is based solely on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards in Israel, including those prescribed by the Auditors' Regulations (Auditor's Mode of Performance), 1973 (as applicable to these financial statements, those standards are practically identical to the international standards on auditing of the International Federation of Accountants [IFAC]). An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of the other auditors, the consolidated financial statements referred to above give a true and fair view of the consolidated financial position of the Group as of December 31, 2002 and 2001, and of the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2002, in accordance with International Financial Reporting Standards.

Tel Aviv, Israel, March 5, 2003

Kost Forer and Gabbay

KOST FORER and GABBAY
A Member of Ernst & Young
Global

Consolidated Balance Sheet US dollars in thousands

assets

	Note	2001	2002
current assets:			
Cash and cash equivalents		57,146	36,609
Short-term deposits	4	3,041	15,210
Trade receivables	5	4,123	23,649
Postdated notes	6	5,410	6,338
Prepaid expenses	7	1,978	3,664
Other accounts receivable	8	739	6,255
Inventory	2e	3,274	6,085
		75,711	97,810
long-term assets:			
Postdated notes	6	22,960	32,678
Prepaid expenses	7	9,723	11,998
Investment in associate	9	2,646	2,031
Deferred taxes	18d	411	607
		35,740	47,314
fixed assets:	10		
Cost		5,731	16,510
Less – accumulated depreciation		(3,065)	(5,069)
		2,666	11,441
intangible assets, net:	11	22,114	51,327
		136,231	**207,892**

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

liabilities and shareholders' equity

	Note	2001	2002
current liabilities:			
Credit from banks and others	12	20,087	47,559
Trade payables	13	2,040	6,375
Other accounts payable	14	5,279	17,186
		27,406	71,120
long-term liabilities:			
Long-term loans and leases from banks and others, net	16	12,611	42,578
Accrued severance pay	2q	1,141	1,474
Deferred taxes	18d	–	660
		13,752	44,712
minority interest:	17g	–	1,601
shareholders' equity:	2a(5),21		
Ordinary shares of NIS 0.01 par value each:			
Authorized: 14,000,000 shares at December 31, 2001 and 2002;			
Issued and outstanding: 10,663,373 shares at December 31, 2001 and 2002		31	22
Additional paid-in capital		91,594	78,142
Treasury shares		–	(196)
Cumulative reporting currency translation adjustments		(5,719)	1,913
Retained earnings		9,167	10,578
		95,073	90,459
		136,231	**207,892**

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

March 5, 2003
Date of approval of the financial statements

y. Alroy

Yariv Alroy
Co-President

y. Alroy

Yoram Alroy
Chairman of the Board of Directors
and Chief Executive Officer

Consolidated Statement of Operations US dollars in thousands (except per share amounts)

	Note	2000	2001	2002
Revenues from sales of devices and services	22a	19,537	30,615	89,804
Cost of sales of devices and services	22b	7,632	10,636	44,053
Gross profit		11,905	19,979	45,751
Research and development costs, net	22c	243	474	415
Selling and marketing expenses	22d	2,289	4,106	7,005
General and administrative expenses	22e	4,999	6,367	26,676
Operating income		4,374	9,032	11,655
Financial expenses (income):				
Exchange rate differences from cash and deposits		243	(5,180)	(4,694)
Income from short-term deposits, net	4b	–	(1,572)	(344)
Other financial expenses (income), net		1,991	(1,664)	3,257
		2,234	(8,416)	(1,781)
Other expenses (income), net	22f	(66)	150	17
Income before taxes on income		2,206	17,298	13,419
Taxes on income	18b	1,119	2,598	3,230
		1,087	14,700	10,189
Minority interest		93	–	(1,425)
Share in losses and provision against shareholders' loan to associate	9	–	(2,644)	(7,353)
Net income for the year		**1,180**	**12,056**	**1,411**
Net basic earnings per share	**23**	**0.18**	**1.13**	**0.13**
Net diluted earnings per share	**23**	**0.18**	**1.13**	**0.13**

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

Statement of Changes in Shareholders' Equity

US dollars in thousands

	Share capital	Additional paid-in capital	Treasury shares	Cumulative reporting currency translation adjustments	Retained earnings (deficit)	Total
Balance at January 1, 2000	1	1,657	–	2,186	(4,069)	(225)
Issuance of bonus shares	24	(24)	–	–	–	–
Issuance of Ordinary shares, net	6	90,379	–	–	–	90,385
Reporting currency translation adjustments	–	–	–	433	–	433
Net income for the year	–	–	–	–	1,180	1,180
Balance at December 31, 2000	31	92,012	–	2,619	(2,889)	91,773
Issuance expenses	–	(418)	–	–	–	(418)
Reporting currency translation adjustments	–	–	–	(8,338)	–	(8,338)
Net income for the year	–	–	–	–	12,056	12,056
Balance at December 31, 2001	31	91,594	–	(5,719)	9,167	95,073
Treasury shares	–	–	(196)	–	–	(196)
Reporting currency translation adjustments from first adoption of SIC-30 (see Note 2a[5])	(7)	(7,772)	–	7,779	–	–
Reporting currency translation adjustments	(2)	(5,680)	–	(147)	–	(5,829)
Net income for the year	–	–	–	–	1,411	1,411
Balance at December 31, 2002	**22**	**78,142**	**(196)**	**1,913**	**10,578**	**90,459**

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

Consolidated Statement of Cash Flows US dollars in thousands

	2000	2001	2002
cash flows from operating activities:			
Net income for the year	1,180	12,056	1,411
Adjustments required to reconcile net income to net cash provided by (used in) operating activities (a)	(5,200)	(13,243)	804
Net cash provided by (used in) operating activities	(4,020)	(1,187)	2,215
cash flows from investing activities:			
Investment in associate	–	(144)	–
Shareholders' loan to associate	–	(4,839)	(5,955)
Purchase of fixed assets	(1,175)	(1,302)	(3,181)
Loans to related party, net	13	–	–
Payment for acquisition of consolidated company, net of cash acquired (b)	11	(7,272)	(25,017)
Investment in intangible assets	(801)	(1,831)	(1,417)
Proceeds from sale of fixed assets	166	663	5
Investment in short-term deposits	(13,133)	–	(15,000)
Proceeds from short-term deposits	–	13,024	–
Net cash used in investing activities	(14,919)	(1,701)	(50,565)
cash flows from financing activities:			
Proceeds from issuance of Ordinary shares, net	79,316	(837)	–
Proceeds from long-term loans from banks and others, net	47,565	119	45,154
Repayment of long-term loans from related parties	(366)	(381)	(142)
Repayment of long-term loans from banks and others	(55,189)	(3,343)	(5,606)
Short-term bank credit, net	(2,299)	18,902	(6,620)
Income distributions to limited partners	–	–	(900)
Treasury shares acquired	–	–	(196)
Net cash provided by financing activities	69,027	14,460	31,690
Effect of exchange rate changes on cash and cash equivalents	205	(4,805)	(3,877)
Increase (decrease) in cash and cash equivalents	50,293	6,767	(20,537)
Cash and cash equivalents at the beginning of the year	86	50,379	57,146
Cash and cash equivalents at the end of the year	**50,379**	**57,146**	**36,609**

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

a adjustments required to reconcile net income to net cash provided by (used in) operating activities:

	2000	2001	2002
Income and expenses not involving cash flows:			
Share in losses and provision against shareholders' loan to associate	–	2,644	7,353
Minority interest	(93)	–	1,425
Equity losses in unconsolidated companies	–	–	26
Depreciation and amortization	1,342	1,798	6,595
Amortization of goodwill, related to carryforward tax losses for which deferred tax benefits were not recorded in prior years	–	1,050	–
Deferred taxes, net	886	175	236
Accrued severance pay	52	127	410
Capital loss (gain) from sale of fixed assets	(57)	124	19
Erosion of principal of long-term liabilities, net	(8)	(303)	1,159
Erosion of principal of short-term deposits	224	–	–
	2,346	5,615	17,223
Changes in operating asset and liability items:			
Decrease (increase) in short-term deposits, net	–	(3,483)	3,062
Decrease (increase) in trade receivables	671	(1,632)	4,961
Increase in postdated notes	(4,886)	(12,779)	(12,565)
Increase in prepaid expenses	(2,565)	(2,743)	(3,453)
Decrease (increase) in other accounts receivable	(140)	115	(963)
Increase in inventory	(926)	(1,344)	(3,031)
Increase (decrease) in trade payables	353	306	(883)
Increase (decrease) in other accounts payable	9	2,702	(3,547)
Decrease in deferred revenues, net of notes	(62)	–	–
	(7,546)	(18,858)	(16,419)
	(5,200)	**(13,243)**	**804**

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

b acquisition of newly consolidated companies:

	2000 [3]	2001 [2]	2002 [1]
Working capital (excluding cash)	1,025	(559)	(6,488)
Long-term assets	(1,015)	(224)	(467)
Fixed assets, net	(44)	(583)	(9,002)
Long-term liabilities	2,977	1,094	22,581
Minority interest	–	–	1,076
Goodwill upon acquisition	(3,030)	(5,981)	(37,329)
Non-competition agreement	–	(1,019)	–
Liability regarding the acquisition of newly consolidated company	98	–	4,612
	11	**(7,272)**	**(25,017)**

[1] During the second quarter of 2002, SHL TeleMedicine North America Inc. purchased all of the shares of Raytel Medical Corporation Inc. (see Note 3).

[2] On December 31, 2001, the Company purchased all of the shares of Bikurofe Ltd. in consideration of USD 7.8 million (see Note 17d).

[3] On January 1, 2000, the Company purchased all of the shares of Shahal-Rishon Le-Zion, Rehovot Medical Services Ltd. in consideration of USD 105 (see Note 17c).

c significant non-cash transactions:

	2000	2001	2002
Issuance of shares against acquisition of minority interest in a consolidated company	11,488	–	–
Share issuance expenses, not yet paid	419	–	–
Acquisition of newly consolidated company	–	–	4,612

d supplemental disclosure of cash flows activities:

	2000	2001	2002
Interest received	**695**	**2,491**	**2,513**
Interest paid	**2,640**	**3,202**	**5,756**
Income taxes paid	**–**	**–**	**2,433**

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

Notes to Consolidated Financial Statements

note 1 | General

a company description:

SHL TeleMedicine Ltd. ("the Company") and its consolidated companies ("the Group") operate medical call centers for patient monitoring and diagnosis. In Israel, the Company also operates and dispatches ambulances from its call centers to patients for emergency treatment and dispatches other ambulances it does not own. The Company sells medical equipment and related communication equipment to subscribers and related companies.

On April 1, 2002, SHL TeleMedicine North America Inc. ("NA"), indirect wholly owned subsidiary purchased all of the shares of Raytel Medical Corporation Inc. ("Raytel"). Raytel is a US provider of remote cardiac monitoring, testing and information services and diagnostic therapeutic and patient management services (see Note 3).

b definitions:

In these financial statements:

The Company

SHL TeleMedicine Ltd.

Consolidated companies

Companies whose financial statements are fully consolidated with those of the Company.

Associate

A company over which the Company exercises significant influence and is not a consolidated company and the Company's investment therein is presented using the equity method of accounting.

The Group

SHL TeleMedicine Ltd. and its consolidated companies.

Related parties

As defined in IAS 24 of IASB.

note 2 | Significant accounting policies

The significant accounting policies applied in the preparation of the financial statements are as follows:

a basis of preparation:

1. The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS), which comprise standards and interpretations approved by the IASB, and International Accounting Standards and Standing Interpretations Committee interpretation approved by the IASC that remain in effect.

2. The consolidated financial statements have been prepared on an historical cost basis.

3. The significant accounting policies applied in the financial statements of the Company in the prior years are applied consistently in these consolidated financial statements.

4. Financial statements in US dollars – the reporting currency:

The majority of sales of SHL TeleMedicine ("the Company") that operates in Israel is made in NIS and the majority of the cost is paid in NIS. The NIS is the currency of the primary economic environment of the Company, hence the functional currency of the Company is the NIS.

The Company has selected the US dollar for its reporting currency, rather than using its functional currency as its reporting currency, because an increasing proportion of its revenues and expenses are incurred in US dollars and the Company believes that most of the users of its financial statements are more familiar with the US dollar than the NIS.

Because the Company selected the reporting currency to be the US dollar, the financial statements have been translated from the functional currency

(NIS) to the reporting currency, in accordance with the principles set forth in IAS 21, SIC-19 and SIC-30 as follows:

All the assets, liabilities, share capital and additional paid-in capital of the Company are translated into US dollars at the closing rate existing at the date of the balance sheet presented, and revenues and expenses are translated at average monthly exchange rates. The results from translation adjustments are recorded in a separate component of shareholders' equity.

Philips Healthcare Telemedicine Services Europe ("JV"), associate, is considered a "Foreign Entity" according to IAS 21. The functional currency of JV is the Euro. JV prepares its financial statements in Euro.

SHL TeleMedicine B.V. ("BV") and SHL TeleMedicine Global Trading Ltd. ("GT"), consolidated companies, are considered "Foreign Entities" according to IAS 21. The functional currency of BV is the Euro and the functional currency of GT is the US dollar. BV and GT prepare their financial statements in Euro.

SHL TeleMedicine North America ("NA"), a consolidated company, is considered a "Foreign Entity" according to IAS 21. The functional currency of NA is the US dollar. NA prepares its financial statements in US dollars.

The Company uses the following procedures in translating the financial statements of "Foreign Entities" for incorporation in the Company's financial statements: assets and liabilities, both monetary and non-monetary, of the foreign entity are translated into the NIS at the closing rate existing at the date of the balance sheet presented, and revenues and expenses are translated at average monthly exchange rates. All resulting exchange differences are classified as equity until the disposal of the investment.

The exchange rate difference of loans which were received for the direct financing of the investment in the foreign entities and that are stated in or linked to the respective functional currency of those entities are also carried within shareholders' equity.

5. Impact of recently issued interpretation for accounting standards:

According to a new publication of the Standing Interpretations Committee, SIC-30 "Accounting for Reporting Currency – Translation from Measurement Currency to Presentation Currency", which was effective on January 1, 2002, share capital and additional paid-in capital is translated into US dollars at the closing rate existing at the date of the balance sheet presented. In previous periods, the Company had translated those items using the exchange rate of the date of the transaction, in accordance with the treatment in IAS 21 and SIC-19.

The effect of the change is only a classification between different items in the shareholders' equity. The change has no effect on the balance sheet, statement of income and the statement of cash flows.

The effect of the change up to December 31, 2001, reflects a decrease in the share capital and additional paid-in capital of USD 7,779 against an increase in cumulative reporting currency translation adjustments in the same amount.

b principles of consolidation:

The consolidated financial statements include the accounts of the Company and its consolidated companies. Significant intercompany transactions and balances between the Company and its consolidated companies were eliminated in consolidation.

Consolidated companies are consolidated from the date on which control is transferred to the Group and cease to be consolidated from the date on which control is transferred out of the Group. Acquisition of consolidated companies is accounted for using the purchase method of accounting.

The financial statements of consolidated companies are prepared for the same reporting periods as the parent company, using consistent accounting policies.

c investment in associate:

Investments in associate over which the Company exercises significant influence, are accounted for under the equity method of accounting.

The Company's investment in associate consists of an ownership interest in Philips Healthcare Telemedicine Services Europe ("JV") (see Note 9). The Company's equity in losses of associate are included up to the amount of the investment in the capital of the associate.

d cash equivalents:

Cash equivalents are considered by the Company to be unrestricted highly liquid investments which include short-term bank deposits originally purchased with maturities of three months or less.

e inventory:

Inventory of devices is presented at the lower of cost or market value. Cost is determined using the "first-in, first-out" method.

f trade receivables and postdated notes:

Trade receivables are recognized and carried at original invoice amount less an allowance for doubtful accounts.

Postdated notes that are linked to the Israeli CPI and do not bear interest, are presented at their present value, according to the market interest rate prevailing on the date on which they were issued.

g allowance for doubtful accounts:

The allowance for doubtful accounts is computed as a percentage of trade receivables balance, and in respect of specific debts whose collection is doubtful.

h prepaid expenses:

Prepaid expenses which are related to cost of sales of services are amortized in the statement of income, over the service contract.

i fixed assets:

1. Fixed assets are stated at cost less accumulated depreciation. Generally, depreciation is computed using the straight-line method on the basis of the estimated useful life of the asset. The carrying amounts are reviewed at each balance sheet date to assess whether they are recorded in excess of their recoverable amounts, and where carrying values exceed this estimated recoverable amount, assets are written down to their recoverable amount.

2. Assets leased under financial lease are presented as purchases. Future lease payments, excluding financial expenses not yet accumulated, are included among long-term liabilities.

3. The annual depreciation rates are as follows:

	%
Computers and communication equipment	15 – 33
Medical equipment	10 – 15
Office furniture and equipment	6 – 15
Motor vehicles and ambulances	15 – 20
Leasehold improvements	over the term of the lease
Leased devices	10

j intangible assets:

1. Research and development costs are expensed as incurred, except for development costs which relate to the design and testing of new or improved products which are recognized as an asset to the extent that it is expected that such assets will generate future economic benefits.

Deferred development costs are amortized from the date of commercial production of the product. Such costs are amortized using the straight-line method over a period of up to 5 years.

At each balance sheet date, the Company assesses whether there is any indication of impairment. If any such indication exists, the recoverable amount is estimated.

2. Goodwill represents the excess of acquisition cost over the fair value of identifiable net assets of a consolidated company at the date of acquisition. Goodwill is amortized using the straight-line method over a period of up to 20 years.

Tax benefits as a result of tax losses from the time in which the investment was acquired, and which could not be taken into account in order to determine the amount for goodwill, are recognized on an ongoing basis at the time in which a tax benefit is utilized, and the balance for goodwill is adjusted accordingly.

3. Non-competition agreement is amortized using the straight-line method over the useful life, which is 3 years.

k deferred taxes:

1. Deferred taxes are provided using the liability method for temporary differences at balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. The main components in respect of which deferred taxes have been included are as follows: inventory, fixed assets, other assets, provision for vacation, accrued severance pay, doubtful accounts and carryforward tax losses. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or subsequently enacted at balance sheet date.

2. Taxes that would apply in the event of the realization of investments in subsidiaries have not been taken into account in computing the deferred taxes, as it is the Company's intention to hold these investments. Similarly, taxes that would apply in the event of the distribution of earnings by subsidiaries as dividends have not been taken into account in computing deferred taxes, since the distribution of dividend does not involve an additional tax liability.

l revenue recognition:

Revenue is recognized to the extent that it is probable that the economic benefits will pass to the Company and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

1. Revenues from sales of devices are recognized when the significant risks and benefits of ownership of the devices have passed to the buyer.

2. Revenues from services are recognized ratably over the service contract.

m exchange rates and linkage basis:

1. Assets and liabilities in or linked to foreign currency are included in the financial statements according to the representative exchange rate as published by the Bank of Israel on December 31, 2002.

2. Assets and liabilities linked to the Israeli CPI are included in the financial statements according to the relevant index for each asset or liability.

Below are Israeli CPI's and exchange rates of one US dollar:

For the year ended	Exchange rate of one US dollar	Israeli CPI*
December 31, 2002	NIS 4.737	182.0 points
December 31, 2001	NIS 4.416	170.9 points
December 31, 2000	NIS 4.041	168.5 points
Changes during the year		
2002	7.3%	6.5%
2001	9.3%	1.4%

* Index on an average basis of 1993 = 100.

n use of estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

o fair value of financial instruments:

The carrying amounts of cash and cash equivalents, short-term deposits, trade receivables, post-dated notes, other accounts receivable, credit from banks and others, trade payables, other accounts payable and long-term loans approximate their fair value.

p concentrations of credit risk:

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash, cash equivalents and trade receivables. Cash and cash equivalents are deposited with major banks. Management believes that the financial institutions that hold the Company's investments are financially sound, and, accordingly, minimal credit risk exists with respect to these investments. The Company's trade receivables are mainly derived from sales to customers in Israel and Europe. The Company has adopted credit policies and standards intended to accommodate industry growth and inherent risk. Management believes that credit risks are moderated by the diversity of its end customers and geographic sales areas. The Company performs ongoing credit evaluations of its customers' financial condition and requires collateral as deemed necessary.

q accrued severance pay:

The Group's liability for severance pay for Israeli resident employees is calculated pursuant to Israeli severance pay law based on the most recent salary of the employees multiplied by the number of years of employment as of the balance sheet date. The Group's liability for all of its employees is funded through insurance policies. The net amount of the severance liability presented in the balance sheet represents the Group liability for severance to its employees as of balance sheet date.

The amounts accumulated in managers' insurance policies in the name of the employees and their respective liabilities are not presented in the balance sheet since they are not under the Group's control and management.

Raytel has a defined contribution pension plan, which covers substantially all employees. Contributions to the plan are based upon a percentage of an employee's covered compensation, as defined. Expense under the plan was USD 336 for the period from April 1, 2002, to December 31, 2002.

Raytel also has a tax-qualified "401(k) plan" which covers substantially all employees. Eligible employees may make salary deferral (before tax) contributions up to a specified maximum. Raytel makes a matching contribution of 25% of the amount deferred. Expense under the plan was USD 134 for the period from April 1, 2002, to December 31, 2002.

The number of the Group's employees as of December 31, 2001 and 2002, was 732 and 1,389, respectively.

Amounts paid to insurance policies for covering severance pay liability for the years ended December 31, 2000, 2001 and 2002, was USD 380, USD 419 and USD 619, respectively.

r leases:

Financial leases, which effectively pass to the Company substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the present value of the minimum lease payments at the inception of the lease term and disclosed as leased fixed assets. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability.

s earnings per share:

The earnings per share are calculated according to the provisions of the IAS 33.

note 3 Acquisition of Raytel Medical Corporation ("Raytel")

a

SHL TeleMedicine North America, Inc. ("NA"), a wholly owned subsidiary of SHL TeleMedicine International ("STI"), purchased in a tender offer all the issued and outstanding shares of Raytel Medical Corporation ("Raytel") at total cost of USD 35.1 million. Payment has not yet been effected with regard to about 15% of Raytel's outstanding shares out of which holders of about 13% of Raytel's outstanding shares have initiated an appraisal rights process under the applicable law. This appraisal process is in its initial stage. As of December 31, 2002, the financial statements reflect USD 4.3 million due to former Raytel shareholders.

The cost of the Raytel acquisition was allocated to its assets and liabilities based on their fair values.

Subsequent to the purchase of Raytel shares, NA merged with Raytel.

b

The fair values of the identifiable assets and liabilities of Raytel which were purchased, were:

Cash and cash equivalents	5,471
Trade receivables	24,767
Other accounts receivable	448
Prepaid expenses and other	1,299
Fixed assets, net	9,002
Investment in associate	56
Intangible assets	411
Goodwill upon acquisition	37,329
	78,783
Trade payables	(5,356)
Other accounts payable	(11,794)
Long-term loans	(25,457)
Minority interest	(1,076)
Fair value of net assets	**35,100**

Consideration:

Cost of shares, at fair value	31,416
Costs associated with the acquisition	3,684
	35,100

The cash outflow on acquisition is as follows:

Cash of Raytel	5,471
Cash paid up to December 31, 2002	(30,488)
Net cash outflow	**(25,017)**

Liability to former Raytel shareholders	**4,282**

Raytel's results of operations were fully consolidated since April 1, 2002, and Raytel has contributed a USD 763 loss to the net income of the Group.

note 4 Short-term deposits

	2001	2002
Short-term deposit [a]	–	15,210
Deposits, net: [b]		
Short-term deposit	30,000	36,000
Less – short-term loan	(28,084)	(36,824)
Accumulated interest, net	1,125	596
	3,041	(228)
Classified to other accounts payable	–	228
	3,041	–
	3,041	**15,210**

a The short-term deposit is linked to the US dollar and bears interest of 2.5% per annum, maturing in June 2003.

b In order to eliminate balance sheet currency exposure, the Company took loans in New Israeli Shekel, equal to a sum of USD 36 million to be repaid in March 2003. Loan equal to USD 11 million is unlinked and bearing interest of 5.85% and loan equal to USD 25 million is linked to Israeli CPI and bearing interest of 3.85% per annum. At the same time, the Company invested the money in US dollar deposits account, bearing an average interest of 2.87% per annum, maturing in March 2003. The deposits are pledged against the loans.

On March 31, 2001, the Company took a loan in New Israeli Shekel, equal to a sum of USD 30 million, and at the same time, invested the money in a US dollar deposit account. The loan and the deposit matured in March 2002.

note 5 Trade receivables

	2001	2002
In Israel	1,698	2,193
Abroad	327	21,456
Associate	2,098	–
	4,123	**23,649**
Net of allowance for doubtful accounts	**555**	**11,595**

note 6 Postdated notes

Postdated notes represent deferred receipts, up to 9 years, which were received from customers in respect of sales of devices. The postdated notes are composed of notes by authorization, notes receivables, and postdated payments from credit cards companies. (See also Note 2f)

note 7 Prepaid expenses

Most of the prepaid expenses are related to sale of services for subsequent periods. The realization of prepaid expenses subsequent to balance sheet date, is as follows:

	2001	2002
First year prepaid expenses – short-term	1,978	3,664
Second year	1,437	1,940
Third year	1,439	1,990
Fourth year	1,302	1,820
Fifth year	1,337	1,828
Thereafter	4,208	4,420
Prepaid expenses – long-term	9,723	11,998
	11,701	**6,255**

note 8 Other accounts receivable

	2001	2002
Government authorities	99	3,350
Employees	142	170
Deferred taxes *	418	1,947
Others	80	788
	739	**6,255**

*** See Note 18d.**

note 9 Investment in associate

a

In January 2001, a wholly owned subsidiary of the Company, STI (see Note 17b), entered into several agreements with Philips Medical Systems Netherlands B.V. and its related companies ("Philips") according to which STI, together with Philips, will form a Dutch company ("JV") which will engage, on its own or through its consolidated companies, in the provision of telemedicine services in various countries throughout Europe. JV was established in May 2001.

STI holds 19.9% of JV's shares and Philips holds 80.1%. STI was granted an option, for a period of 5 years, beginning May 4, 2001, to increase its share in JV to 35% in consideration of a payment amounting to USD 164. Philips has the right to cause STI to exercise the option after three or four years, depending upon the JV progress.

STI is committed to provide JV with its entire know-how, support, computer software and any other material possessed by the Company, which is necessary for JV's operations. In return, STI is entitled to a service revenue share, based on the number of JV's subscriptions.

In 2001, minimum royalties of USD 5.3 million were determined, and recorded in the Company's books.

In addition, STI will provide JV with medical equipment at prices as agreed upon in the agreement. STI has an exclusive right to supply the equipment for three years and a right of final offer for an additional two years.

STI invested in JV's share capital USD 144 and, in addition, provided JV with loans in an aggregate amount of USD 12.6 million. The loan is linked to the Euro and is repayable no later than December 21, 2010.

b comprised as follows:

	2001	2002
Investment in JV share capital	144	144
Accumulated losses	(144)	(144)
	–	–
Shareholders' loan	5,021	12,607
Provision against shareholders' loan *	(2,375)	(10,607)
	2,646	2,000
Other associate	–	31
	2,646	**2,031**

* Due to JV losses in the aggregate amount of USD 37,3 million as of December 31, 2002, the Company decided to provide against the loan that was given to JV.

note 10 Fixed assets

cost:

Balance at January 1, 2002

Additions during the year

Additions for newly consolidated company (see Note 3)

Disposals during the year

Reporting currency translation adjustments

Balance at December 31, 2002

accumulated depreciation:

Balance at January 1, 2002

Additions during the year

Disposals during the year

Reporting currency translation adjustments

Balance at December 31, 2002

Depreciated cost at December 31, 2002

Depreciated cost at December 31, 2001

As for charges, see Note 20.

note 11 Intangible assets

At January 1, 2002, net of accumulated amortization

Additions during the year

Additions for newly consolidated company (see Note 3)

Amortization during the year

Realized income tax benefits subsequent to the acquisition of newly consolidated company

Reporting currency translation adjustments

At December 31, 2002, net of accumulated amortization

At December 31, 2002, net of accumulated amortization

Cost

Accumulated amortization

Net carrying amount

* See Note 17d.

Computers and communication equipment	Medical equipment	Office furniture and equipment	Motor vehicles and ambulances	Leasehold improvements	Leased devices	Total
2,020	1,297	596	1,078	506	234	5,731
1,192	627	153	78	799	332	3,181
1,998	3,831	609	–	2,564	–	9,002
–	(635)	(7)	(10)	(372)	–	(1,024)
(129)	(87)	(40)	(74)	(34)	(16)	(380)
5,081	5,033	1,311	1,072	3,463	550	16,510
1,340	1,264	120	148	176	17	3,065
1,098	1,086	273	207	495	45	3,204
–	(616)	(7)	(5)	(372)	–	(1,000)
(84)	(85)	(8)	(11)	(12)	–	(200)
2,354	1,649	378	339	287	62	5,069
2,727	**3,384**	**933**	**733**	**3,176**	**488**	**11,441**
680	**33**	**476**	**930**	**330**	**217**	**2,666**

Research and development costs	Goodwill	Non-competition agreement *	Others	Total
2,599	17,830	1,019	666	22,114
1,236	–	–	181	1,417
–	37,329	–	(210)	37,119
(415)	(2,440)	(316)	(220)	(3,391)
–	(4,439)	–	–	(4,439)
(174)	(1,203)	(70)	(46)	(1,493)
3,246	**47,077**	**633**	**371**	**51,327**
4,318	54,013	949	406	59,686
(1,072)	(6,936)	(316)	(35)	(8,359)
3,246	**47,077**	**633**	**371**	**51,327**

note 12 Credit from banks and others

	Interest rate for 2002 IN %	2001	2002
Credit from banks:			
NIS – unlinked	10.6	18,559	3,568
NIS – linked to the dollar	Libor + 2.6	–	7,000
		18,559	10,568
Current maturities of long-term loans (see Note 16)		1,376	36,991
Current maturities of long-term loans – related parties (linked to the Israeli CPI)	3.6	152	–
		20,087	**47,559**

As for charges, see Note 20.

note 13 Trade payables

	2001	2002
Open accounts	1,930	6,209
Notes payable	110	166
	2,040	**6,375**

note 14 Other accounts payable

	2001	2002
Liabilities to employees and other liabilities for wages and salaries	1,475	3,997
Accrued liabilities	2,403	7,952
Government authorities	1,379	847
Former Raytel shareholders (see Note 3)	–	4,282
Others	22	108
	5,279	**17,186**

note 15 | Deferred revenues, net of notes

The deferred revenues represent future income from service contracts.

a deferred revenues:

	2001	2002
Deferred revenues	83,852	88,505
Less – postdated notes	(83,852)	(88,505)
	–	–

b composition of deferred revenues subsequent to balance sheet date:

	2001	2002
First year – current maturities	10,710	11,724
Second year	10,271	11,420
Third year	9,788	11,707
Fourth year	10,091	12,013
Fifth year	10,368	12,063
Thereafter	37,624	29,578
	83,852	**88,505**

note 16 | Long-term loans and leases from banks and others

a composed as follows:

	Interest rate for 2002 in %	2001	2002
Loans from banks:			
NIS – unlinked	Prime* -0.24	11,717	17,332
NIS – linked to Israeli CPI	5.7	1,295	10,787
NIS – linked to the dollar	3.365	–	13,943
NIS – linked to the Euro	Libor+1.82	–	9,941
NIS – linked to the Yen	Libor+1.75	199	–
Dollar, net **1.**	US Libor+0.57	–	5,000
		13,211	57,003
Less – current maturities		1,078	21,672
		12,133	35,331
Lease obligations:			
Lease obligations of vehicles – NIS – linked to Israeli CPI	7	271	192
Capital lease obligations and nonrecourse notes **2.**	2.3–13.5	–	1,784
		271	1,976
Less – current maturities		78	1,011
		193	965
Other long-term loans:			
NIS – linked to Israeli CPI	5.45	505	282
Revolving credit facility **3.**	US prime** +1	–	12,308
US Federal Government **4.**	7	–	8,000
		505	20,590
Less – current maturities		220	14,308
		285	6,282
		12,611	**42,578**

* The prime rate as of December 31, 2002 – 10.4%.
**The US prime rate as of December 31, 2002 – 5.25%.

1. As security for long-term loans from banks of USD 24,000 received in connection with the financing of the Raytel acquisition, the Company pledged to banks certain liquid assets, including cash deposit of USD 19,000. In the balance sheet this deposit has been offset against the loan.

2. The capital lease obligations and non-recourse notes are due in varying amounts, including interest at rates ranging from 2.3% to 13.5% through 2007.

3. Under the revolving credit facility, Raytel may borrow up to USD 15.0 million based on a prescribed formula, with interest at the US prime rate plus 1% (5.25% as of December 31, 2002). All borrowings are due on November 30, 2003.

4. The settlement due the US Federal Government is payable in annual installments of USD 2.0 million including interest of 7%, through June 30, 2006. (See Note 20c)

b The long-term loans are repayable in the following years subsequent to the balance sheet date:

	2001	2002
First year – current maturities	1,376	36,991
Second year	12,132	8,178
Third year	142	7,195
Fourth year	77	6,977
Fifth year	–	4,939
Repayment date has not yet been determined	260	15,289
	12,611	42,578
	13,987	**79,569**

c

The Company is required to maintain certain financial covenants and is currently in compliance with all such requirements.

d

As for charges see Note 20.

note 17 Investments in subsidiaries

Name of company	Country of incorporation	Percentage in equity interest	
		2001	2002
Shahal Haifa – Medical Services Ltd. (a)	Israel	100	100
SHL TeleMedicine International Ltd. (b)	Israel	100	100
Shahal-Rishon Le-Zion, Rehovot Medical Services Ltd. (c)	Israel	100	100
Bikurofe Ltd. (d)	Israel	100	100
SHL TeleMedicine B.V. (e)	Netherlands	100	100
SHL TeleMedicine Global Trading Ltd. (f)	Ireland	100	100
SHL TeleMedicine North America Inc. (g)	USA	100	100

a Shahal Haifa – Medical Services Ltd.:

On December 31, 1996, the Company purchased all the shares in Shahal Haifa – Medical Services in consideration of USD 700. The Company recorded goodwill in the amount of USD 2.9 million representing the excess of the aggregate acquisition cost over the fair value of the identifiable net assets at date of acquisition.

b SHL TeleMedicine International Ltd. (STI):

During September 1997, the Company established STI. STI has the rights to develop and market the “Shahal Method” outside of Israel.

According to a preferred share purchase agreement dated September 9, 1997, Vertex I.I.F. Limited Partnership (“Vertex”) purchased 17.4% of STI share capital in consideration of USD 4.5 million. In an agreement entered into in April 2000 and amended and signed on August 30, 2000, between the Company, Vertex and STI, Vertex agreed to exchange all of its shares in STI for 7.15 % of the shares of the Company. After the exchange, which was held on September 21, 2000, the Company holds 100% of STI.

The Company recorded goodwill in the amount of USD 11.3 million representing the excess of the aggregated acquisition cost over the fair value of the identifiable net assets at date of acquisition.

c Shahal-Rishon Le-Zion, Rehovot Medical Services Ltd.:

On January 1, 2000, the Company purchased all the shares of Shahal-Rishon Le-Zion, Rehovot Medical Services Ltd., a related company, in consideration of USD 105.

The Company recorded goodwill in the amount of USD 3 million representing the excess of the aggregate acquisition cost over the fair value of the identifiable net assets at date of acquisition.

d Bikurofe Ltd.:

On December 31, 2001, the Company purchased all the shares of Bikurofe Ltd., Israeli medical call centers service provider, in consideration of USD 7.8 million. This amount includes USD 1 million for non-competition agreement.

The Company recorded goodwill in the amount of USD 5.9 million representing the excess of the aggregate acquisition cost over the fair value of the identifiable net assets at date of acquisition.

e SHL TeleMedicine B.V. (BV):

During May 2001, STI established BV, which holds 19.9% of the shares of JV (see Note 9) and holds 100% of the shares of SHL TeleMedicine Global Trading Ltd. (see f.).

f SHL TeleMedicine Global Trading Ltd. (GT):

GT was incorporated on October 23, 2001. GT was established in order to distribute innovative medical devices and to perform research and development activities.

g SHL TeleMedicine North America Inc. (NA) (see Note 3):

NA holds, indirectly, through Raytel Medical Corporation less than 100% in several entities.

The minority interest in these entities was presented in the financial statements in “Minority interest”.

note 18 Taxes on income

a taxation under inflationary conditions:

According to the Income Tax (Inflationary Adjustments) Law, 1985 in Israel, the results for tax purposes are calculated in real terms based on the changes in the Israeli CPI.

b

Non-Israeli consolidated companies are taxed based upon tax according to the applicable laws in their countries of residence.

c taxes on income included in the statement of operations:

	2000	2001	2002
Current taxes	233	1,093	2,862
Deferred taxes	886	1,505	236
Taxes in respect of previous years	–	–	132
	1,119	**2,598**	**3,230**

d deferred taxes:

Composition and changes in deferred taxes, as presented in the consolidated balance sheet are as follows:

	In respect of balance sheet items				
	Fixed assets and other assets	Provision for employee rights	Carryforward tax losses	Others	Total
Balance at January 1, 2002	(505)	998	247	89	829
Amounts charged to statement of income	(172)	19	(172)	89	(236)
Additions for newly consolidated company	39	–	–	1,317	1,356
Cumulative foreign currency translation adjustments	35	(67)	(17)	(6)	(55)
Balance at December 31, 2002	**(603)**	**950**	**58**	**1,489**	**1,894**

The balance is presented as follows:

	2001	2002
Among current assets	418	1,947
Among long-term assets	411	607
Among long-term liabilities	–	(660)
	829	**1,894**

e a reconciliation of theoretical tax expense assuming all income is taxed at the statutory rate applicable to the income of companies in Israel, and the actual tax expense is as follows:

	2000	2001	2002
Income before taxes on income, as reported in the consolidated statements of income	2,206	17,298	13,419
Statutory tax rate in Israel	36%	36%	36%
Theoretical tax expense	794	6,227	4,831
Increase (decrease) in taxes resulting from:			
Losses for which deferred taxes were not provided	127	–	11
Tax adjustment in respect of inflation in Israel	12	(370)	(387)
Non-deductible expenses	313	425	1,121
Decrease in taxes resulting from realization of carryforward tax losses for which deferred taxes were not recorded in prior years	–	(863)	–
Tax exempt income	(149)	(2,821)	(2,035)
Different tax rates for non-Israeli consolidated companies	–	–	61
Taxes in respect of previous years	–	–	132
Tax on minority interest in earnings of consolidated entities	–	–	(513)
Others	22	–	9
	1,119	**2,598**	**3,230**

f carryforward losses for tax purposes:

The consolidated carryforward losses for tax purposes for the year ended December 31, 2002, amount to USD 161. An asset in respect of deferred taxes in Raytel, amounting to USD 8.7 million, was not included in the balance sheet as the timing of its realization in the foreseeable future is uncertain.

g tax assessments:

Final assessments or assessments considered as final, were received by the Company through tax year 1999. Shahal Haifa – Medical Services Ltd., Shahal-Rishon Le-Zion, Rehovot Medical Services Ltd., STI and Bikurofe Ltd. received final assessments or assessments considered as final through tax year 1998.

note 19 Transactions with related parties

	2000	2001	2002
revenues:			
Sales and services to associate	–	6,287	3,169
Interest and linkage differentials from associate	–	447	–
	–	**6,734**	**3,169**
expenses:			
Salaries to officers and directors	934	1,607	1,742
Rental expenses to shareholders	134	131	124
Interest to shareholder	22	20	–
Management fees to related party	66	–	–
	1,156	**1,758**	**1,866**

note 20 | Charges, guarantees and contingent liabilities

a charges:

As collateral for the Company and its consolidated companies' liabilities, fixed charges were placed on motor vehicles and insurance rights and fixed and floating charges were placed on specific notes collectible and other assets of the Group.

For charges on cash deposits see Notes 4b and 16a(1).

b lease commitments:

The facilities of the Company and its consolidated companies are rented under operating leases for periods ending in 2009.

Future minimum lease commitments under operating leases for the years ended December 31, are as follows:

Year	
2003	5,148
2004	4,116
2005	2,807
2006	2,303
Thereafter	1,526
	15,900

c contingent liabilities:

1. Raytel and a consolidated company of Raytel were the subject of a US Government investigation that began in June 2000. In June 2001, Raytel reached an agreement with the Government to resolve the issues that were the subject of the investigation. In addition, in September 2001, Raytel entered into a settlement agreement with the Government to resolve related civil claims under which Raytel agreed to pay USD 11.5 million over a period of 5 years. Through December 31, 2002, USD 3.5 million has been paid. The settlement agreement did not release Raytel or the consolidated company from any future claims arising out of their other business operations, including the transtelephonic pacemaker operations conducted at its New Jersey facility that had not complied in all respects with certain technical requirements relating to the duration of testing sessions. Raytel's financial statements include an accrual which it believes is adequate for all anticipated claims and costs in connection with this matter.

2. Raytel, former members of its Board of Directors and other individuals have been named as defendants in a purported class action lawsuit opposing the merger transaction between Raytel and NA. The plaintiff has expanded this lawsuit to include additional defendants, including some Company's nominated Raytel Board members. The plaintiff generally alleges that the individual defendants breached their fiduciary duties of loyalty, good faith, and independence in connection with the proposed merger transaction by engaging in self-dealing. Raytel believes that the complaint lacks merit and intends to vigorously defend the lawsuit. As such no provision has been made in Raytel's financial statements for this matter. Moreover, any award to the plaintiffs is expected to be covered by insurance.

3. The Company and its subsidiaries are, from time to time, a party to various other claims and disputes associated with various aspects of its ongoing business operations. In management's opinion, none of these other claims or disputes are expected, either individually or in the aggregate, to have a material adverse effect on the Company's financial position, results of operations or cash flows.

note 21 Share capital

a the share capital after giving retroactive effect to the split and the bonus shares is composed as follows:

	Authorized		Issued and outstanding	
	2001	2002	2001	2002
	Number of shares			
Ordinary shares of NIS 0.01 par value each	14,000,000	14,000,000	10,663,373	10,663,373

Each of the Company's shares confers upon their holders the following rights:

1. Equal rights to participate in the distribution of a dividend, whether a cash dividend or bonus shares, in the distribution of assets or any other distribution according to ratio of the paid-in capital or credit as paid in over the nominal value of the share.

2. Equal rights to participate and vote in the Company's general meetings.

3. Equal rights regarding capital and participation in the distribution of the Company's surplus assets in a liquidation event, according to the ratio of the amounts of paid-in capital or credit as paid in over their nominal value.

b treasury shares:

During 2002, the Company purchased 29,347 shares of its own shares in aggregate amount of USD 196.

Shares held by the Company are treated and presented in the balance sheet as deduction from equity.

c changes in share capital structure:

On September 19, 2000, the Company increased its authorized share capital by NIS 137,360, so that following such action, the Company's authorized share capital consisted of NIS 140,000 divided into 139,000 Ordinary shares of NIS 1.00 nominal value each and 1,000 Preferred A shares of NIS1.00 nominal value each.

On September 21, 2000, the Company allotted 208 Ordinary shares of NIS 1.00 nominal value each to Vertex in exchange for Vertex's holdings in STI (see Note 17b).

On September 21, 2000, the Company allotted 621 Preferred A shares of NIS 1.00 nominal value each to Philips Venture Capital Fund in consideration of its investment of about USD 39 million (before issuance expenses). On September 25, 2000, the Company allotted additional 86 Preferred A shares of NIS 1.00 nominal value each to Philips Venture Capital Fund in consideration of their nominal value as an antidilution protection against reserving Ordinary shares of the Company for the ESOP (see section d. below).

On September 26, 2000, all Preferred A shares were converted into Ordinary shares.

On September 26, 2000, the Company effected a stock split according to which each NIS 1.00 nominal value share was split into 100 shares, each having nominal value of NIS 0.01.

On September 26, 2000, 7,871,873 bonus shares of NIS 0.01 nominal value each were issued and allotted to shareholders in order to maintain all pro-rata holdings in the share capital of the Company.

On November 15, 2000, 2,500,000 Ordinary shares of nominal value NIS 0.01 were issued in a public offering.

d share option plan:

In September 2000, the Company adopted an option plan for the issuance of options to its employees, directors and consultants (the “ESOP”). The Company approved a maximum pool of up to 856,627 shares reserved for issuance upon exercise of options which may be granted pursuant to the ESOP. All options to be issued under the ESOP shall be subject to a four-year vesting schedule which provides for 50% of the options to be vested in the second anniversary of the date of grant and an additional 25% to be vested in each of the following third and forth anniversary of the date of grant.

In November 2000, after the completion of the public offering, the Company has granted to the Company’s employees and consultants 496,202 options to purchase shares of the Company in the price of CHF 34 (the public offering price) under the terms of the ESOP.

During 2001, a further 23,340 options to purchase shares were granted under the terms of the ESOP. In December 2001, the Company has granted to employees and consultants a further 97,975 options to purchase shares in the price of CHF 22.65 (the market price at the date of the approval) under the terms of the ESOP. The aforesaid options are subject to a three-year vesting schedule which provides for one third of the options to be vested in each of the following first, second and third anniversary of the date of the grant.

In July 2002, the Company adopted the 2002 International Issuance of Options plan to non-Israeli employees, directors, officers and consultants of the Company and any of its consolidated companies under the term of the ESOP.

Information with respect to the number of options granted under the ESOP is as follows:

	2001		2002	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Outstanding at beginning of year	496,202	CHF 34.00	617,517	CHF 32.20
Granted	23,340	CHF 34.00	–	–
Granted	97,975	CHF 22.65	–	–
Cancelled	–	–	(102,430)	CHF 34.00
Outstanding at end of year	**617,517**	CHF 32.20	**515,087**	CHF 31.84

note 22 | Supplementary information to statements of income

a revenues from sales of devices and services:

	2000	2001	2002
Sale of services in Israel	10,820	11,115	19,553
Sale of devices in Israel	7,408	12,767	12,840
Sale of services abroad	274	5,721*	54,389*
Sale of devices abroad	1,035	1,012**	3,022**
	19,537	**30,615**	**89,804**

* Includes royalties and service fees from associate in the amount of USD 0.2 million and USD 5.7 million for the years ended December 31, 2002 and 2001, respectively (see Note 9).

** Includes sale of devices to associate in the amount of USD 3 million and USD 0.6 million for the years ended December 31, 2002 and 2001, respectively.

b cost of sales of devices and services:

	2000	2001	2002
Salaries and related benefits	3,323	3,906	18,666
Cost of devices sold	1,977	4,410	4,442
Payment to service providers	–	–	5,431
Depreciation	285	276	2,440
Maintenance of ambulances and motor vehicles	346	363	353
Rental fees and maintenance	478	482	4,405
Materials and components	205	163	3,258
Communications, postage and freight	114	110	2,199
Others	904	926	2,859
	7,632	**10,636**	**44,053**

c research and development costs, net:

	2000	2001	2002
Salaries and related benefits	362	592	651
Amortization of research and development costs	193	474	415
Medical consulting	86	109	106
Others	403	431	479
	1,044	1,606	1,651
Less – capitalization of development costs	801	1,132	1,236
	243	**474**	**415**

d selling and marketing expenses:

	2000	2001	2002
Salaries and related benefits	1,116	1,833	3,345
Advertising	213	897	936
Depreciation	155	141	157
Rental fees and maintenance	154	204	282
Maintenance of motor vehicles	330	392	731
Others	321	639	1,554
	2,289	**4,106**	**7,005**

e general and administrative expenses:

	2000	2001	2002
Salaries and related benefits	1,708	2,507	11,232
Rental fees, maintenance and office expenses	572	519	5,049
Professional fees	265	740	2,491
Depreciation and amortization	709	827	3,397
Doubtful accounts and bad debts	1,216	901	3,387
Others	529	873	1,120
	4,999	**6,367**	**26,676**

f other expenses (income), net:

Capital (gain) loss from sale of fixed assets	(57)	124	19
Expenses (income) in respect of prior years	(9)	26	380
Other	–	–	(382)
	(66)	**150**	**17**

note 23 Earnings per share

a basic earnings per share:

	2000	2001	2002
Income (numerator)	1,180	12,056	1,411
Shares (denominator)	6,554,050	10,663,373	10,634,026
Per share amount	0.18	1.13	0.13

b diluted earnings per share:

Income (numerator)	1,180	12,056	1,411
Shares (denominator)	6,564,656	10,663,525	10,634,026
Per share amount	0.18	1.13	0.13

note 24 Segments information

a

1. The Company and its consolidated companies operate in two business segments:

Telemedicine services – providing monitoring services utilizing telephonic and Internet communication technology and selling related instruments through direct sales or by franchises.

Medical services – operating a network of imaging centers and cardiac facilities that provide diagnostic, therapeutic and patient management services primarily associated with cardiovascular disease. The segment also operates medical call center services which provide 24-hours doctor "house-call" services and medical consultation over the phone.

2. The Company and its consolidated companies also operate in several geographic segments. The segments are determined based on the location of the customers.

3. The assets of the segments include all of the operational assets which are used by the segments and are comprised primarily of cash and cash equivalents, short-term deposits, trade receivables, other accounts receivable, postdated notes, prepaid expenses, inventory, fixed assets and intangible assets. The liabilities of the segments primarily include trade payables, other accounts payable and accrued severance pay.

The assets and the liabilities of the segments do not include deferred taxes.

b business segments:

The following tables present revenue and profit information, and certain asset and liability information regarding business segments.

		Telemedicine services	
	2000	2001	2002
Segment revenues:			
Sales to external customers	19,537	30,615	52,409
Operating income	4,374	9,032	9,442
Share in losses and provision against shareholders' loan to associate	–	(2,644)	(7,353)
Segment result	4,374	6,388	2,089
Unallocated expenses			
Operating income *			
Financial income (expenses)			
Other income (expenses), net			
Taxes on income			
Minority interest			
Net income for the year			
Other business information:			
Segment assets		126,180	143,073
Other assets			
Segment liabilities		(6,549)	(14,074)
Other liabilities			
Capital expenditure	1,976	3,453	3,534
Depreciation and amortization	1,342	2,848	3,052

* **Includes share in losses and provision against shareholders' loan to an affiliate company.**

Medical services			Consolidated		
2000	2001	2002	2000	2001	2002
–	–	37,395	19,537	30,615	89,804
–	–	4,126	4,374	9,032	13,568
–	–	–	–	(2,644)	(7,353)
–	–	4,126	4,374	6,388	6,215
			–	–	(1,913)
			4,374	6,388	4,302
			(2,234)	8,416	1,781
			66	(150)	(17)
			(1,119)	(2,598)	(3,230)
			93	–	(1,425)
			1,180	12,056	1,411
	8,815	58,370		134,995	201,443
				1,236	6,449
				136,231	207,892
	(1,911)	(10,961)		(8,460)	(25,035)
				(32,698)	(92,398)
				(41,158)	(117,433)
–	–	1,064	1,976	3,453	4,598
–	–	3,543	1,342	2,848	6,595

c geographic segments:

1. The following is segment revenue from external customers by geographical area, based on the geographical location of the customers:

	2000	2001	2002
Israel	18,228	23,882	32,393
Europe	1,309	6,733	3,286
USA	–	–	54,125
	19,537	**30,615**	**89,804**

2. The following is the total carrying amount of segment assets by geographical location of assets:

	2001	2002
Israel	129,913	129,740
Europe	5,082	2,427
USA	–	73,171
	134,995	**205,338**

3. The following is the total cost incurred during the year, to acquire segment assets that are expected to be used during more than one year (fixed assets and intangible assets) by geographical location of assets:

	2000	2001	2002
Israel	1,976	3,453	2,801
Europe	–	–	123
USA	–	–	1,674
	1,976	**3,453**	**4,598**

note 25 Linkage terms of monetary balances

Linkage terms of monetary balances in the consolidated balance sheet of the Group are as follows:

December 31, 2001	In or linked to: foreign currency (mainly US dollars)	In or linked to: Israeli CPI	Unlinked	Total
assets:				
Cash and cash equivalents	56,529	–	617	57,146
Short-term deposits	3,041	–	–	3,041
Trade receivables	2,425	144	1,554	4,123
Postdated notes	–	28,370	–	28,370
Other accounts receivable	–	188	133	321
Shareholders' loan to associate	2,646	–	–	2,646
	64,641	**28,702**	**2,304**	**95,647**
liabilities:				
Credit from banks and others	–	–	18,559	18,559
Trade payables	714	–	1,326	2,040
Other accounts payable	323	–	4,956	5,279
Long-term loans and leases from banks and others (including current maturities)	199	2,071	11,717	13,987
Long-term loans from related parties (including current maturities)	–	152	–	152
	1,236	**2,223**	**36,558**	**40,017**

December 31, 2002				
assets:				
Cash and cash equivalents	36,129	–	480	36,609
Short-term deposits	15,210	–	–	15,210
Trade receivables	21,456	200	1,993	23,649
Postdated notes	–	39,016	–	39,016
Other accounts receivable	3,765	271	272	4,308
Shareholders' loan to associate	2,000	–	–	2,000
	78,560	**39,487**	**2,745**	**120,792**
liabilities:				
Credit from banks and others	7,000	–	3,568	10,568
Trade payables	5,418	–	957	6,375
Other accounts payable	11,606	–	5,580	17,186
Long-term loans and leases from banks and others (including current maturities)	50,976	11,261	17,332	79,569
	75,000	**11,261**	**27,437**	**113,698**

note 26 Subsequent events

On January 1, 2003, the Company entered into an agreement with Hashmira Medical Ltd. and S.Y. Protected Communities and Nursing Ltd. ("the sellers") for the acquisition of their rights in their business activities including distress buttons, doctor calls services, dispatch call center services, etc.

The consideration for the transaction amounted to USD 1.6 million to be paid in 18 equal monthly installments linked to the CPI. The consideration shall be adjusted according to the number of subscribers who will pay full subscription fees during a period of three months after the closing date but in any case the consideration will not exceed USD 1.6 million.