
UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 20-F

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

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

For the fiscal year ended December 31, 2006

OR

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

For the transition period from _____ to _____

OR

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

Date of event requiring this shell company report.

Commission file number 000-20181

SAPIENS INTERNATIONAL CORPORATION N.V.

(Exact name of Registrant as specified in its charter)

(Translation of Registrant's name into English)

NETHERLANDS ANTILLES

(Jurisdiction of incorporation or organization)

Landhuis Joonchi

Kaya Richard J. Beaujon z/n

P.O. Box 837

Curaçao, Netherlands Antilles

(Address of principal executive offices)

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

Title of Class:

Name of each exchange on which registered:

Common Shares, par value €0.01 per share

NASDAQ Capital Market

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

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

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

As of December 31, 2006 the issuer had 15,153,852 Common Shares, par value €0.01 per share outstanding.

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

Yes No

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

Yes No

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

Yes No

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

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

Indicate by checkmark which financial statement item the registrant has elected to follow:

Item 17 Item 18

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

Yes No

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INTRODUCTION

Definitions

In this annual report, unless the context otherwise requires:

References to “Sapiens,” the “Company,” “us,” “we” and “our” refer to Sapiens International Corporation N.V. (the “Registrant”), a Netherlands Antilles company, and its consolidated subsidiaries.

References to “our shares,” “Common Shares” and similar expressions refer to the Registrant’s Common Shares, par value €0.01 per share.

References to “dollars”, “US dollar” or “\$” are to United States Dollars.

References to “NIS” are to New Israel Shekels, the Israeli currency.

Cautionary Statement Regarding Forward-Looking Statements

Certain matters discussed in this annual report are forward-looking statements that are based on our beliefs and assumptions as well as information currently available to us. Such forward-looking statements may be identified by the use of the words “anticipate,” “believe,” “estimate,” “expect,” “may,” “will,” “plan” and similar expressions. Such statements reflect our current views with respect to future events and are subject to certain risks and uncertainties. While we believe such forward-looking statements are based on reasonable assumptions, should one or more of the underlying assumptions prove incorrect, or these risks or uncertainties materialize, our actual results may differ materially from those described herein. Please read the risks discussed in Item 3 – “Key Information” under the caption “Risk Factors” and cautionary statements appearing elsewhere in this annual report in order to review conditions that we believe could cause actual results to differ materially from those contemplated by the forward-looking statements.

We undertake no obligation publicly to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties, and assumptions, the forward-looking events discussed in this annual report might not occur.

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 tables summarize certain selected consolidated financial data for the periods and as of the dates indicated. We derived the statement of operations financial data for the years ended December 31, 2004, 2005 and 2006 and the balance sheet data as at December 31, 2005 and 2006 from our consolidated financial statements included elsewhere in this annual report. The selected consolidated statement of operations financial data for the years ended December 31, 2002 and 2003 and the balance sheet data as of December 31, 2002, 2003 and 2004 are derived from our audited financial statements not included in this annual report. Certain financial data for 2003 were reclassified to conform to the 2004 presentation, certain financial data for 2004 were reclassified to conform to the 2005 presentation and certain financial data for 2005 were reclassified to conform to the 2006 presentation. You should read the selected consolidated financial data together with our consolidated financial statements included elsewhere in this annual report and with Item 5, "Operating and Financial Review and Prospects." Our consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP").

Note Regarding the Reverse Stock Split and Listing of our Securities:

We implemented a 1-for-5 reverse stock split of our Common Shares on June 16, 2003 to meet the listing requirements of the NASDAQ National Market (now known as the NASDAQ Global Market) ("NASDAQ"). On January 15, 2003, NASDAQ informed us that our Common Shares would be delisted from NASDAQ due to our failure to maintain compliance with the \$1.00 minimum bid price requirement for continued listing on NASDAQ (the "Minimum Bid Price Requirement"). We requested and were granted a hearing before a NASDAQ Listing Qualifications Panel in order to present a definitive plan to regain compliance with the Minimum Bid Price Requirement, and thereby avoid the delisting of the Common Shares from NASDAQ.

On February 18, 2003, our Board of Directors approved a definitive plan to regain compliance with the Minimum Bid Price Requirement by implementing a 1-for-5 reverse stock split of the Common Shares. We presented this plan to implement a reverse stock split to the NASDAQ Listing Qualifications Panel at a hearing on February 27, 2003. On March 25, 2003, NASDAQ notified us that it approved of our plan to implement the reverse stock split and that our Common Shares would continue to be traded on NASDAQ provided that we regained compliance with the Minimum Bid Price Requirement by June 16, 2003 and maintained compliance for at least ten consecutive days thereafter.

On June 11, 2003, at a Special General Meeting, our shareholders approved the implementation of the reverse stock split and amendments to our Articles of Association that were required to effect the reverse stock split. As a result of the reverse stock split, our authorized capital of €48,300,000 became divided into 20 million Common Shares (instead of 100 million) and the par value of the Common Shares was changed to €2.30 (instead of €0.46). On June 16, 2003, we achieved compliance with the Minimum Bid Price Requirement and we have maintained such compliance through the date of this annual report.

Although we maintained compliance with the Minimum Bid Requirement, at the end of the second quarter of 2005, our shareholders' equity was below \$10,000,000 which is the required minimum shareholders' equity for continued listing on NASDAQ. As a result of a notice we received from NASDAQ, we applied to transfer the listing of our Common Shares from NASDAQ, and on September 28, 2005, our Common Shares began to trade on the NASDAQ Capital Market (formerly known as the NASDAQ SmallCap Market).

At the end of the first quarter of 2006, our shareholders' equity was \$2.2 million. On June 5, 2006, we received a letter from NASDAQ indicating that we failed to comply with the minimum stockholders' equity requirement for continued listing on the NASDAQ Capital Market. On June 27, 2006, we submitted to NASDAQ a plan to achieve and sustain compliance with the minimum stockholders' equity requirement for continued listing on the NASDAQ Capital Market. On August 17, 2006, we received a letter from NASDAQ indicating that we had re-gained compliance with the minimum stockholders' equity requirement for continued listing.

On June 24, 2007, we received a letter from the Tel Aviv Stock Exchange (“TASE”) informing us that as of August 12, 2007, our Common Shares and warrants (Series 1) that are traded on the TASE, but not our debentures (Series A), will be included in a newly created list of “Illiquid Securities”. As a result, trades on the TASE of our Common Shares and warrants (Series 1) will only be executed twice a day, in the morning upon the commencement of trading, and at the end of day, at the end of trading. At this time we cannot be certain as to the effects, if any, that such listing change on the TASE will have on our Common Shares and warrants (Series 1), however, we do not believe such inclusion as an “Illiquid Security” on the TASE will have a material effect on our financial condition.

All historical share amounts and per share data in this annual report have been retroactively restated to reflect the reverse stock split.

On August 26, 2004, at the Annual General Meeting, our shareholders approved an increase in the number of authorized Common Shares to 30,000,000 and a change in the par value of all authorized shares to one Eurocent (€0.01). As a result, the total nominal capital of the Company is €10,000, reflecting 30,000,000 Common Shares and 1,000,000 Preferred Shares.

Selected Financial Data:	Year Ended December 31,				
	2002	2003	2004	2005	2006
	(In thousands, except per share data)				
Revenues:					
Products	\$ 42,008	\$ 32,580	\$ 26,781	\$ 13,295	\$ 10,423
Consulting and other services	22,820	19,738	21,023	26,109	33,888
Total revenues	64,828	52,318	47,804	39,404	44,311
Cost of revenues:					
Cost of products	21,561	16,628	15,274	8,809	6,302
Cost of consulting and other services	14,549	11,979	11,490	16,037	22,499
Impairment of capitalized software development costs	-	-	901	-	-
Total cost of revenues	36,110	28,607	27,665	24,846	28,801
Gross profit	28,718	23,711	20,139	14,558	15,510
Operating Expenses:					
Research and development, net	6,017	3,656	2,531	2,723	2,451
Selling, marketing, general and administrative	23,782	21,539	19,260	16,245	13,558
Restructuring Costs	481	-	-	1,113	758
Total operating expenses	30,280	25,195	21,791	20,081	16,767
Operating loss	1,562	1,484	1,652	5,523	1,257
Financial expenses, net	971	958	2,410	1,788	2,230
Other expenses (income), net	1,173	(244)	552	(12)	-
Loss before taxes on income	3,706	2,198	4,614	7,299	3,487
Taxes on income (benefit)	1,408	(19)	217	1,798	325
Minority interests in earnings of a subsidiary	39	8	11	2	13
Net loss	5,153	2,187	4,842	9,099	3,825
Settlement of redeemable shares in a subsidiary	-	-	299	-	-
Net loss to shareholders of Common Shares	\$ 5,153	\$ 2,187	\$ 5,141	\$ 9,099	\$ 3,825
Basic and diluted net loss per share	\$ 1.03	\$ 0.20	\$ 0.46	\$ 0.76	\$ 0.29
Weighted average number of shares used in computing basic and diluted loss per share	4,999	10,693	11,273	11,982	13,395

Balance Sheet Data:	At December 31, (in thousands)				
	2002	2003	2004	2005	2006
Cash and cash equivalents	\$ 22,001	\$ 31,775	\$ 10,942	\$ 6,699	\$ 3,108
Working capital (deficit)	9,615	20,373	2,767	(10,636)	(12,616)
Total assets	65,152	76,723	68,734	51,866	45,619
Long-term debt and other liabilities	7,787	24,783	23,281	15,603	13,235
Capital stock	106,421	105,908	108,635	110,645	113,683
Total shareholders' equity	15,895	13,929	12,080	3,632	3,929

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

We operate globally in a dynamic and rapidly changing environment that involves numerous risks and uncertainties. The following section lists some, but not all, of those risks and uncertainties that may have a material adverse effect on our business, financial position, results of operations or cash flows.

Risks Relating to Our Business and Our Industry

Implementing our strategy of focusing on the market for software solutions in the insurance industry has taken longer than anticipated, and we may not succeed in gaining acceptance in that market.

Our goal is to rise to a position of global leadership in delivering strategic business software solutions to the insurance industry. Achieving this goal requires us, among other things, to design appropriate software solutions, maintain sufficient sales and marketing resources, recruit, train and hire sufficient professional services personnel and face intense competition. We have experienced delays in penetration of the insurance industry, and such delays have contributed to a decline in our results. We expect that additional time will be required to achieve our goal. Our future efforts to gain acceptance for our solutions may still not succeed which could have a material adverse effect on our results.

We have a history of losses, and we anticipate that our revenues for the short term will not significantly increase while our expenses may increase as a result of maintaining our research and development and marketing efforts and increased interest costs.

We incurred net losses of approximately \$9.1 million and \$3.8 million for the years ended December 31, 2005 and December 31, 2006, respectively. We cannot predict that our losses will continue to decrease, or if we may become profitable on a sustained basis. Due to the delay in the implementation of our strategy of offering solutions to the insurance industry and possible decline in orders from existing customers, we have no assurance that our revenues in the short to medium term will significantly increase, if at all. At the same time, expenses may increase in the foreseeable future as we maintain our research and development, sales and marketing activities. In addition, following our offering of approximately \$17.1 million principal amount of convertible debentures in December 2003, and an additional \$1.5 million of convertible debentures in March 2004, upon the exercise by non-affiliates of the Company of options that were offered together with the original convertible debentures in December 2003, we have the obligation to pay the debenture holders interest and to pay the principal amount when the debentures are due, which currently amounts to approximately \$14.5 million. Our research and development, marketing and sales efforts may prove more costly than we currently anticipate, and we may not succeed in the long term in increasing our revenues sufficiently to offset the expenses of those efforts and of paying back the principal and paying the interest on the debentures. If our revenues fail to increase at a greater rate than our expenses, we will not be able to achieve profitability.

Our working capital has declined significantly and despite our recent financing activities, our working capital may continue to decrease and we may need to raise capital again.

Our liquidity has been reduced due to the drop in our cash reserves available. At December 31, 2006, we had negative working capital of \$12.6 million. In the recent past, we have needed to raise capital in order to continue financing our business activities, to pay back the principal and the interest on the debentures and to continue meeting our other obligations. Despite our recent gross capital raise of \$20 million (excluding finders' fees and out of pocket expenses), there is no assurance that our past trend of diminishing working capital will not continue. There is no assurance that we will be able to obtain additional financing, or if we do, that it will be on favorable terms. In addition, if we issue capital stock to investors, in order to raise cash, our existing shareholders will experience dilution.

As a result of an offering of convertible debentures, we have significant debt and the amount of the debt could hinder our activities and affect the flexibility needed for such activities.

In December 2003, we completed an offering of convertible debentures on the TASE. The offering resulted in gross proceeds to us of approximately \$17.1 million. The debentures were offered in units which included options to purchase additional debentures and with warrants to purchase our Common Shares. Options which were exercised by non-affiliates of the Company before their expiry date resulted in additional gross proceeds of approximately \$1.5 million to the Company in the first quarter of 2004. In December 2007, we must re-pay approximately \$4.6 million, approximately \$4.2 million for the second of the four annual re-payments of the principal of the debentures, and approximately \$0.4 million for the semi-annual interest payment. We have not created sufficient positive cash flow from operations to make such payment. In August 2006, a majority of the debenture holders approved changes to the amount and the timing of the first installment payment of the principal of the debentures, such that the payment of 50% of the first payment amount was deferred to December 5, 2009, and we were given the opportunity to either pay back the other 50% of the first payment amount, or to convert such amount into our Common Shares. On November 30, 2006, we announced our decision to pay the approximately \$2.4 million in cash, and on December 5, 2006, we made the payment. There can be no guarantee that the debenture holders will agree to any changes to the terms of the debentures in the future. In June 2007, we entered into a private placement transaction for an aggregate gross amount of \$20 million (excluding finders' fees and out of pocket expenses). Following the private placement transaction, in June 2007, we purchased an aggregate amount of NIS 15,000,000 nominal value of debentures, representing approximately \$3.5 million of the outstanding debentures. Pursuant to the terms of the prospectus governing the debentures, the amount repurchased by us was retired and removed from circulation. As a result, the total amount that we must pay in December 2007 was reduced to approximately \$4.6 million. We currently have enough funds to make the December 2007 payments. However, if we use those funds for other purposes in the future, we may not have enough funds to make the future principal and interest payments. We cannot be certain that our credit lines will be renewed in the future, and if they are, that they will be on favorable terms. If we are unable to obtain through other means the funds needed to make such payments, we could breach the terms of the debentures and of the Trust Deed which we entered into in connection with the offering. Even if we are able to make the payments required by the debentures, the amount of the debt could have a material adverse effect on our results of operations and financial position. For example, the debt could restrict our ability to obtain additional financing, restrict our flexibility in planning or in reacting to changes in the business, place us in a position inferior to that of competitors with lower debts or make us more vulnerable if there is a downturn in our revenues or in the economy in general. The amount of the debt could require us to dedicate a material part of our cash flow to payment of interest and repayment of principal and in addition reducing our ability to use the cash for other purposes such as working capital.

The failure of our new solutions to achieve market acceptance or continued delays in our current or future efforts to develop software solutions could erode our competitive position.

The failure to successfully develop, enhance or modify our software solutions, or the failure to do so on a timely basis, could limit our revenue growth and competitive position. We may need to rapidly develop and introduce additional software and enhancements to our existing solutions to satisfy our current customers and maintain our competitive position in the marketplace. We may also need to modify our software so that it can operate with new or enhanced software that may be introduced by other software vendors. The failure to introduce new, enhanced or modified software on a timely basis could prevent our solutions from achieving market acceptance. We have experienced in the past, and anticipate experiencing in the future, delays in the timing of the introduction of new solutions and market acceptance of those solutions. To support our software development, enhancement or modification, we may find it necessary to license or acquire new technologies, which may not be available to us on acceptable terms, if at all.

If we fail to remain technologically competitive, we could lose customers or market share.

The market for our solutions is characterized by rapidly changing business conditions and customer requirements. The introduction of solutions embodying new technology and the emergence of new customer requirements can render existing technology obsolete and unmarketable. Our ability to anticipate changes in technology and customer requirements and to successfully develop and introduce new and enhanced solutions on a timely basis will be significant factors in our ability to grow and to remain competitive. Substantial expenditures are required for research and development and the introduction of new products. There can be no assurance that we will have sufficient resources to make such investments, or that these investments will bring the full advantages or any advantage as planned. We have in the past experienced delays introducing our technology and enhancements, and there can be no assurance that we will not encounter technical or other difficulties that could delay introduction of new technologies or enhancements in the future. There can be no assurance that we will be successful in developing and marketing enhancements that incorporate new technology on a timely basis, or that its new solutions will adequately address the changing needs of the marketplace. Our failure, for technological or other reasons, to timely develop and market products incorporating new technologies could have a material adverse effect on our results of operations, financial condition and cash flows.

The software solutions market we address is expected to evolve rapidly, and if we are not able to accurately predict and respond to market developments or customer needs, our competitive position will be impaired.

The market for the solutions we provide is expected to evolve rapidly. However, estimates of our market's expected growth are inherently uncertain and are subject to many risks and assumptions. Moreover, many of our customers operate in markets characterized by rapidly changing technologies and business plans. Rapid changes in the needs of these customers and changing technologies make it difficult for us to predict their demands. We are particularly susceptible to those changes since our software is used in a wide array of operating environments, which are constantly evolving. As a result, we may not be able to develop, on a timely basis or at all, solutions that meet our customers' needs or desires. In addition, various sectors of our market are served by competitors who may respond more effectively to market developments and customer needs. There can be no assurance that the market for our solutions will grow or that we will be able to respond to changes in the market, evolving customer needs or our competition. If the market for our solutions does not develop as we expect or if we fail to respond to market and competitive developments, our business prospects and competitive position might be impaired.

If existing customers do not make subsequent purchases from us or if our relationships with our largest customers are impaired, our revenue could be negatively affected.

Our existing customers are a key asset of Sapiens, and we depend on repeat product and service revenues from our base of customers. Specifically, revenues from sales to Menora Mivtachim Insurance Ltd. ("Menora") and Synergy Insurance Services Holdings Limited ("Synergy") constituted 16.6% and 9.5%, respectively, of our consolidated revenues in 2006. There can be no assurance that our existing customers will enter into new project contracts with Sapiens or that they will continue using our enabling technologies. If our revenue stream from existing customers were to decline significantly, it would have a material adverse impact on our operating results. Indeed, in the beginning of 2007, Synergy reduced the scope of the project that we are performing for them, which resulted in a reduction of our expected revenues through the end of 2007 from this customer by approximately \$2.0 million.

The relationships with three large customers of our U.S. subsidiary – Texas Farm Bureau Insurance Companies, PZU and Occidental Fire & Casualty; three large customers of our subsidiary in the United Kingdom – Synergy Insurance Services Holdings Limited, EDS Credit Services and Liverpool Victoria; and a large customer of our subsidiary in Israel – Menora, are the sources of a large portion of the revenues of each of those three subsidiaries. During 2006, revenues from sales to the American customers specified above constituted 56.4% of the total revenues of the U.S. subsidiary (13% of our consolidated revenues); revenues from sales to the British customers specified above constituted 60.6% of the total revenues of the U.K. subsidiary (19% of our consolidated revenues); and revenues from sales to the Israeli customer specified above constituted 60.8% of the total revenues of the Israeli subsidiary (16.6% of our consolidated revenues). Our sales to Liverpool Victoria, EDS Credit Services and Occidental Fire & Casualty have declined in recent years, which negatively impacted our revenue stream. If we experience further reductions in sales to these customers, our revenue stream will be further negatively affected.

We compete against companies with significantly greater resources than our own.

The market for software solutions and related services, and for business solutions for the insurance industry, in particular, is highly competitive. Our principal competitors generally have significantly greater resources than we do. Our customers or potential customers could prefer suppliers that are larger than us and that have not experienced losses such as ours. There is no guarantee that our customers, present and future, will be confident in our financial stability going forward. Price reductions or declines in demand for our solutions and services, whether as a result of competition, technological change, changes in the level of application development, reengineering or maintenance performed internally by our customers or potential customers would have a material adverse effect on our results of operations, financial position and cash flows.

Our business involves long term, large projects, some of which are fixed-price projects that involve uncertainties, such as estimated project costs and profit margins.

Our business is characterized by relatively large projects or engagements that can have a significant impact on our total revenue and cost of revenue from quarter to quarter. A high percentage of our expenses, particularly employee compensation, is relatively fixed. Therefore, a variation in the timing of the initiation, progress or completion of projects or engagements, especially at or near the end of any quarter, can cause significant variations in operating results from quarter to quarter.

Some of our solutions are sold as fixed-price projects with delivery requirements spanning more than one year. If our actual cost-to-completion of these projects differs significantly from the estimated costs, there could be a material adverse effect on our results of operations and financial position. Similarly, delays in executing client contracts may affect our revenue and cause our operating results to vary widely. Some of our solutions may be priced in excess of \$1.0 million and are delivered over periods of time ranging from several months to a few years. Payment terms are generally based on periodic payments or on the achievement of milestones. Any delays in payment or in the achievement of milestones may have a material adverse impact on our results of operations, financial position or cash flows. The sales cycle for our solutions is long and variable, typically ranging between nine months to eighteen months from initial contact with the potential client to the signing of a contract. Occasionally, sales require substantially more time. This variability may adversely affect our operating results in any particular quarter.

Our business involves business-critical solutions which expose us to potential liability claims.

Our products focus on organizations' business-critical applications including those related to core business solutions for the insurance industry and we provide re-engineering and re-development services for customers' specialized needs. Since our customers rely on our software to operate, monitor and improve the performance of their critical software applications, they are sensitive to potential disruptions that may be caused by the use of, or any defects in, our software. As a result, we may be subject to claims for damages related to software errors in the future. Liability claims could require us to spend significant time and money in litigation or to pay significant damages. Regardless of whether we prevail, diversion of key employees' time and attention from the business, incurrence of substantial expenses and potential damage to our reputation might result. While the terms of our sales contracts typically limit our exposure to potential liability claims, and we carry errors and omissions insurance against such claims, there can be no assurance that such insurance will continue to be available on acceptable terms, if at all, or that such insurance will provide us with adequate protection against any such claims. A significant liability claim against us could have a material adverse effect on our results of operations and financial position.

Defects in our technology would harm our business and divert resources.

The quality of our products, enhancements and new versions is critical to our success. Since our software solutions are complex, they may contain errors that can be detected at any point in their life cycle. Any errors or defects in our technology could result in:

- delayed or lost revenue;
- failure to attract new customers or achieve market acceptance;

- claims against us;
- diversion of development resources;
- increased service, warranty and insurance costs; and
- negative publicity resulting in damage to our reputation.

While we continually test our products for errors and work with customers to identify and correct them, errors in our technology may be found in the future. Testing for errors is complicated because it is difficult to simulate the breadth of operating systems, user applications and computing environments that our customers use and because our software is becoming increasingly complex itself. The costs we may incur in addressing technology errors could be substantial and could impair our results of operations.

Although we protect our intellectual property rights vigorously, there can be no assurance that these measures will be successful.

In accordance with industry practice, we rely on a combination of contractual provisions and intellectual property law to protect our proprietary technology. We believe that due to the dynamic nature of the computer and software industries, copyright protection is less significant than factors such as the knowledge and experience of our management and personnel, the frequency of product enhancements and the timeliness and quality of our support services. We seek to protect the source code of our products as trade secret information and as an unpublished copyright work. We also rely on security and copy protection features in our proprietary software. We distribute our products under software license agreements that grant customers a personal, non-transferable license to use our products and contain terms and conditions prohibiting the unauthorized reproduction or transfer of our products. In addition, we attempt to protect trade secrets and other proprietary information through non-disclosure agreements with employees, consultants and distributors. Although we intend to protect our rights vigorously, there can be no assurance that these measures will be successful. Our failure to protect our rights, and the improper use of our products by others without licensing them from us, could have a material adverse effect on our results of operations and financial condition.

Our Sapiens eMerge™ solution is proprietary to us and if we need to hire programmers, maintenance and professional services providers, we would incur training costs and delays due to training.

Our Sapiens eMerge™ solution was designed by us and its use requires special knowledge and training. If our current employees leave the Company or if a new project is undertaken by the Company and we need to hire new programmers or people to provide maintenance and professional services to our customers, we would have to train the new employees and consultants in Sapiens eMerge™. As a result, we would incur training costs and would have to delay implementation of projects and services until such individuals were adequately trained. In addition, once these individuals are initially trained, they would still be inexperienced with Sapiens eMerge™ and would take additional time to develop efficiency and proficiency with Sapiens eMerge™. As a result of these costs and delays, there could be a negative impact on our results of operations, our financial condition, our cash flows and our relationships with our customers.

Some of our potential customers are reluctant to purchase proprietary solutions.

Some customers of information technology solutions are reluctant to purchase solutions that are not off-the-shelf or widely used by a broad customer base. Since our Sapiens eMerge™ solution and our Sapiens INSIGHT™ suite of solutions are proprietary to us and require special knowledge and training, we have faced reluctance by potential customers to purchase our proprietary solutions. Such reluctance could have a negative impact on our results of operations and our financial condition.

As part of our business strategy, we may make acquisitions that could disrupt our business and harm our results of operations and financial condition.

As part of our growth strategy, we may consider acquiring complementary technologies, products and businesses. If we use capital stock in connection with such acquisitions, our existing shareholders may experience dilution. If we use cash or debt financing, our financial liquidity will be reduced, the holders of our debt would have claims on our assets ahead of holders of our Common Shares and our business operations may be restricted by the terms of any debt. An acquisition may involve nonrecurring charges or amortization of significant amounts of intangible assets, which would adversely affect our ability to achieve and maintain profitability. Attempted acquisitions may divert management, operational and financial resources from the conduct of our core business, and we may not complete any attempted acquisition.

The terms of our bank debt include a number of restrictive covenants which, if breached, could result in acceleration of our obligation to repay our debt.

Our loan and credit line agreements contain a number of conditions and limitations on the ways in which we can operate our business, including limitations on our ability to raise debt, sell or acquire assets and pay dividends. Our loan and credit line agreements also contain various covenants which require us to maintain certain financial performance milestones related to shareholders' equity and operating results. These limitations and covenants may force us to pursue less than optimal business strategies or forego business arrangements which could have been financially advantageous to us or our shareholders. There can be no assurance that we will fulfill these covenants or, if we do not fulfill one or more of these covenants, that we will receive from our lender banks waivers of the necessity of fulfilling such covenants.

Our failure to comply with the covenants and restrictions contained in our loan and credit line agreements could lead to a default under the terms of these agreements. If a default occurs and we are unable to renegotiate the terms of the debt, the lenders could declare all amounts borrowed and all amounts due to them under the agreements due and payable. If we are unable to repay the debt, the lenders could foreclose on our assets that are subject to liens and sell our assets to satisfy the debt. As part of our loan agreements, the assets of our subsidiary in the United States are subject to a security interest and the assets of our subsidiaries in Israel and the United Kingdom are subject to a floating lien. Foreclosure on these assets could have a material adverse effect on our results of operations and financial condition.

Our liquidity may be negatively affected due to outstanding obligations to investors in the discontinued operations of a subsidiary.

In April 2000, F.I.D. Holdings Ltd. ("FID") and Israel Discount Bank Ltd. (the "Investors") invested \$15 million in eZoneXchange.com, Inc. ("eZone"), a subsidiary of the Company. The private placement to the Investors was accompanied by a Put/Call Agreement, according to which the Investors were granted the right to require us to repurchase their shares in the subsidiary beginning May 2004, in exchange for both cash and our Common Shares. In March 2004, we entered into a new agreement with the Investors which replaced the Put/Call Agreement and which restructured the remaining portion of the put option. Among other things, we agreed to pay the Investors in two annual installments a total of \$8.6 million plus interest at 7.5% a year by May 1, 2005. In May 2005, we entered into an agreement regarding the payment of the \$4.0 million due May 1, 2005. We paid \$2.0 million at the beginning of May 2005 and agreed to pay \$1.0 million on April 1, 2006 and \$1.0 million on August 1, 2006. In August 2006, we entered into an agreement with the Investors whereby the Investors converted the \$1.0 million payment that was due on April 1, 2006 into 781,250 Common Shares and the \$1.0 million payment that was due on August 1, 2006 was delayed to August 1, 2007. The Investors may, at their sole discretion, convert all or any portion of the \$1.0 million payment now payable on August 1, 2007 into our Common Shares, at a conversion price per each share of \$3.20. Payment of the final \$1.0 million may affect our liquidity by reducing the cash reserves needed for financing our business activities or for meeting our other obligations.

Our future results could be adversely affected by an impairment of the value of certain intangible assets.

The assets listed in our consolidated balance sheet include, among other things, goodwill valued at approximately \$8.6 million, capitalized software development costs valued at approximately \$13.5 million, long-term deferred income taxes valued at approximately \$2.7 million, short-term deferred income taxes valued at approximately \$907,000 and purchased technologies valued at \$823,000. The applicable accounting standards require that (a) goodwill be tested for impairment at least annually, and written down when impaired; (b) capitalized software costs 10 be assessed for recoverability on a regular basis, to determine whether the amortization of the asset over its remaining life can be recovered through undiscounted future operating cash flows from the specific software product sold, in accordance with Statement of Financial Accounting Standard No. 86 (“Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed”); (c) certain identifiable intangible assets such as deferred taxes be reviewed for impairment in certain circumstances; and (d) purchased technologies be assessed for recoverability on a regular basis, to determine whether the amortization of the asset over its remaining life can be recovered through undiscounted future operating cash flows from such asset. If our goodwill, capitalized software development costs, deferred tax assets, or purchased technologies were deemed to be impaired in whole or in part due to the Company not achieving its goals, we could be required to reduce or write off such assets, thus having to recognize additional expense in our statements of operations and to reduce our shareholders’ equity.

Our quarterly results may be impacted by multiple short-term factors.

Our revenue and operating results could vary widely from quarter to quarter as a result of several different factors, such as the budgeting and purchasing practices of our customers, the length of the customer product evaluation process, the timing of our customers’ system conversions, the timing and cost of new product introductions and product enhancements, and the timing of any acquisitions and associated costs. Employee hiring and the rate of utilization of such employees may also affect our revenues and results of operations.

Our international operations involve inherent risks, such as foreign currency fluctuations and compliance with various regulatory and tax regimes.

Most of our revenues are derived from international operations that are conducted in local currencies as well as dollars. Changes in the value of such local currencies or the dollar relative to such local currencies may affect our financial position and results of operations. Gains and losses on translations to dollars of assets and liabilities may contribute to fluctuations in our financial position and results of operations. In certain locations, we engage in currency-hedging transactions intended to reduce the effect of fluctuations in foreign currency exchange rates on our financial position and results of operations. However, there can be no assurance that any such hedging transaction, if entered into, will materially reduce the effect of fluctuation in foreign currency exchange rates on such results. In addition, if for any reason exchange or price controls or other restrictions on the conversion of foreign currencies were imposed, our financial position and results of operations could be adversely affected.

Other potential risks that may impact our international business activities include longer accounts receivable payment cycles, the burdens of complying with a wide variety of foreign laws and changes in regulatory requirements, although such factors have not had a material adverse effect on our financial position or results of operations to date.

Formula Systems (1985) Ltd. and its parent company Emblaze Ltd., may exercise control and influence corporate actions that are potentially in conflict with our other public shareholders.

Formula Systems (1985) Ltd. (“Formula”), whose ADR’s trade on NASDAQ and whose shares trade on the TASE, directly owned (as of June 27, 2007) 11,088,594, or approximately 53%, of our currently outstanding Common Shares.

In November 2006, Emblaze Ltd. (“Emblaze”), whose ordinary shares are traded on the London Stock Exchange (under the trading symbol: BLZ.L), purchased the controlling interest of Formula, and as a result, control of us. As of June 27, 2007, Emblaze owned 50.1% of the outstanding share capital of Formula and, therefore, has an indirect controlling influence over us.

Emblaze, through Formula, is and may continue to be in a position to exercise control over most matters requiring shareholder approval. Formula may use its share ownership or representation on our Board of Directors to substantially influence corporate actions that conflict with the interests of our other public shareholders including, without limitation, changing the size and composition of the Board of Directors and committees of our Board of Directors, causing the issuance of further securities, amending our governing documents or otherwise controlling the outcome of shareholder votes. Further, actions by Formula with respect to the disposition of the Common Shares it beneficially owns, or the perception that such actions may occur, may adversely affect the trading price of our Common Shares.

Eli Reifman and Guy Bernstein, both of Emblaze, and Gad Goldstein and Naamit Salomon, both of Formula, are members of our Board of Directors. As of January 1, 2007, Eli Reifman was elected as Chairman of our Board of Directors.

We may be classified as a passive foreign investment company and, as a result, our U.S. shareholders may suffer adverse tax consequences.

Generally, if for any taxable year, after applying certain look-through rules, 75% or more of our gross income is passive income, or at least 50% of the value of our assets are held for the production of, or produce, passive income, we may be characterized as a passive foreign investment company, or PFIC, for U.S. federal income tax purposes. This characterization could result in adverse U.S. tax consequences to our shareholders who are U.S. taxpayers, including gain realized on the sale of our Common Shares being treated as ordinary income rather than capital gain income and could result in punitive interest charges being applied to such sales proceeds. Rules similar to those applicable to distributions apply to amounts treated as “excess distributions.”

We believe we were not a PFIC in 2006. We currently expect that we will not be a PFIC in 2007. However, PFIC status is determined as of the end of the taxable year and is dependent on a number of factors. Therefore, there can be no assurance that we will not become a PFIC for the year ending December 31, 2007 or in a future year. U.S. shareholders should consult with their own U.S. tax advisors with respect to the U.S. tax consequences of investing in our Common Shares. For a discussion of how we might be characterized as a PFIC and related tax consequences, please see Item 10.E, “Additional Information – Taxation - U.S. Federal Income Tax Considerations - Tax Consequences if We Are a Passive Foreign Investment Company.”

Risks Relating to Conducting Business in Israel

Conducting business in Israel entails certain inherent risks that could harm our business.

Our corporate headquarters and research and development facilities are located in the State of Israel. Political, economic and military conditions in Israel directly affect our operations. We could be adversely affected by any major hostilities involving Israel, the interruption or curtailment of trade between Israel and its trading partners or a significant downturn in the economic or financial condition of Israel. In addition, several countries still restrict business with Israel and with companies doing business in Israel. We do not believe that the political and security situation has had any material impact on our business to date; however, we can give no assurance that security and political conditions will have no such effect in the future.

Since September 2000, there has been a marked 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. These developments have adversely affected the regional peace process, placed the Israeli economy under significant stress, and have negatively influenced Israel’s relationship with several Arab countries. The establishment in 2006 of a government in the Palestinian Authority by representatives of the Hamas militant group resulted in an escalation in violence among Israel, the Palestinian Authority and other groups and has created additional unrest and uncertainty in the region. Further, during the summer of 2006, Israel was engaged in a war with Hezbollah, a Lebanese Islamist Shiite militia group, which involved rockets being fired from Lebanon up to 50 miles into Israel and disrupted most day-to-day civilian activity in northern Israel. Any future armed conflict, political instability or violence in the region, including acts of terrorism, may have a negative effect on our business condition, harm our results of operations and adversely affect our share price.

Some of our executive officers and employees in Israel are obligated to perform military reserve duty, currently consisting of approximately 30 days of service annually. Additionally, they are subject to being called to active duty at any time upon the outbreak of hostilities. While we have operated effectively under these requirements since the establishment of Sapiens, no assessment can be made as to the full impact of such requirements on our business or work force and no prediction can be made as to the effect on us of any expansion of such obligations.

We intend to rely upon tax benefits from the State of Israel, benefits that in certain circumstances may not be available to us as anticipated.

Our subsidiary, Sapiens Technologies (1982) Ltd. (“Sapiens Technologies”), which is incorporated in Israel, was granted “Approved Enterprise” status by the Investment Center of the Israeli government for six investment programs in 1984, 1991, 1993, 1995, 1998 and 2000 under the Law for Encouragement of Capital Investments, 1959. We are eligible for certain tax benefits based on this status. In order to receive these tax benefits, Sapiens Technologies must comply with two material conditions: (a) it must invest a certain amount in property and equipment, and (b) it must finance a certain portion of these investments out of equity capital. We believe that Sapiens Technologies has complied with these conditions. If the Investment Center determines that we failed to comply with the conditions summarized above, these past benefits may be canceled, reduced or rendered unavailable to us, which could have a material adverse effect on our results of operations and financial condition. On April 1, 2005, an amendment to the Law for Encouragement of Capital Investments, 1959, came into force. See Note 13 of our consolidated financial statements for a description of the amendment to the Law for Encouragement of Capital Investments, 1959 and its possible effects on our results of operations and financial condition.

Risks Related to the Market for our Common Shares

Our Common Shares are traded on more than one market and this may result in price variations.

Our Common Shares are traded on the NASDAQ Capital Market and the TASE. Trading in our Common Shares on these markets will be made in different currencies (US dollars on the NASDAQ Capital Market and NIS on the TASE), and at different times (resulting from different time zones, different trading days and different public holidays in the U.S. and Israel). The trading prices of our Common Shares on these two markets may differ due to these and other factors. Any decrease in the trading price of our Common Shares on one of these markets could cause a decrease in the trading price of our Common Shares on the other market.

There is very little trading volume of our Common Shares, which causes the stock price to be volatile and which may lead to losses by investors.

There is very little trading volume of our Common Shares, both on the NASDAQ Capital Market and the TASE. As a result, our Common Shares have experienced significant market price volatility in the past and may experience significant market price and volume fluctuations in the future, in response to factors such as announcements of developments related to our business, announcements by competitors, quarterly fluctuations in our financial results and general conditions in the industry in which we compete.

On June 24, 2007, we received a letter from the TASE informing us that as of August 12, 2007, our Common Shares and warrants (Series 1) that are traded on the TASE, but not our debentures (Series A), will be included in a newly created list of “Illiquid Securities”. As a result, trades on the TASE of our Common Shares and warrants (Series 1) will only be executed twice a day, in the morning upon the commencement of trading, and at the end of day, at the end of trading. At this time we cannot be certain as to the effects, if any, that such listing change on the TASE will have on our Common Shares and warrants (Series 1), however, we do not believe such inclusion as an “Illiquid Security” on the TASE will have a material effect on our financial condition.

ITEM 4. INFORMATION ON THE COMPANY

A. History and Development of the Company

Corporate Details

Our legal and commercial name is Sapiens International Corporation N.V., and we were incorporated and registered in the Netherlands Antilles on April 6, 1990. We are a public limited liability company and operate under the provisions of the Netherlands Antilles Commercial Code. Our registered office is located at Landhuis Joonchi, Kaya Richard J. Beaujon z/n, Curaçao, Netherlands Antilles and our telephone number in Curaçao is + 5999-736-6277. United International Trust N.V. is the Company's agent in Curaçao and serves as a member of our Board of Directors. Our World Wide Web address is www.sapiens.com. The information contained on the web site is not a part of this annual report.

Important Business Developments since January 1, 2006

In May 2005, we entered into an agreement with F.I.D. Holdings Ltd. and Israel Discount Bank Ltd., the investors in eZone (the "Investors"), regarding the payment of the remaining \$4.0 million due to the Investors, pursuant to the March 2004 agreement between us and the Investors. We agreed to pay \$2.0 million on May 2, 2005, \$1.0 million by April 1, 2006 and \$1.0 million by August 1, 2006. In addition, the interest to be paid on the outstanding principal amount was changed to London Interbank Offered Rate ("LIBOR") plus 2.5%. The first installment of \$2.0 million was paid as required at the beginning of May 2005. In August 2006, we entered into an agreement with the Investors whereby the Investors converted the \$1.0 million payment that was due on April 1, 2006 into 781,250 Common Shares and the \$1.0 million payment that was due on August 1, 2006 was delayed to August 1, 2007. The Investors may, at their sole discretion, convert all or any portion of the \$1.0 million payment now payable on August 1, 2007 into our Common Shares, at a conversion price per each share of \$3.20.

(For further details about the transaction with the Investors, see Item 10, "Additional Information – Material Contracts – Agreements with FID and Israel Discount Bank Ltd.")

In August 2006 we convened a general meeting of the debenture holders, where a special resolution was adopted concerning the amount and the timing of the first installment payment of the principal of the debentures. A majority of the debenture holders approved that (a) 50% of the first payment amount, approximately \$2.4 million, will be deferred to December 5, 2009 (the last date of payment of the principal on the debentures), and (b) with respect to the other 50% of the first payment amount, the Company could choose from the following alternatives, in its sole discretion: (1) to convert such amount on December 5, 2006 into our Common Shares, at a conversion price per share of \$1.28, which reflects the average closing price for the 10 day period prior to July 17, 2006, or (2) to pay the approximately \$2.4 million amount to the debenture holders, in cash. On December 5, 2006, we made the payment in cash.

In December 2006, we entered into loan agreement with Bank Leumi Le-Israel whereby we borrowed an aggregate amount of approximately \$2.5 million. The proceeds of the loan enabled us to make the December 2006 principal and interest payment on the debentures. The loan was secured by a pledged deposit of Formula. The loan bears an annual interest rate equal to the prime rate of interest in Israel plus 0.5% (for a total of 6.5%) and the principal and interest are due on August 30, 2007.

(For further details about the loan from Bank Leumi, see Item 5, "Operating and Financial Review and Prospects - Liquidity and Capital Resources – Credit Lines.")

On June 27, 2006, we entered into agreements for a new revolving credit line facility for borrowings of up to \$9.2 million, until June 30, 2007. We are currently negotiating the extension of the credit line facility for another year. We cannot be certain that an agreement will be signed, though we expect that an agreement will be signed that extends the current credit line, on substantially similar terms, for an additional year.

(For further details about the credit lines, see Item 5, "Operating and Financial Review and Prospects - Liquidity and Capital Resources – Credit Lines.")

In August 2006, we entered into a share issuance agreement with Formula whereby Formula invested \$2.0 million in the Company, and we issued 1,562,500 Common Shares to Formula, at a purchase price per share of \$1.28, which was the average closing price for the 10 day period prior to July 17, 2006, and which was the same as the conversion price approved by the debentures holders at the August 2006 meeting.

(For further details about the Formula investment, see Item 10, "Additional Information – Material Contracts-Agreements with Formula.")

In June 2007, we entered into a private placement investment transaction with several institutional investors, private investors and Formula for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). As of June 27, 2007, we have held closings for \$17.5 million of the investment, \$5 million of which was by Formula. We issued to the investors an aggregate of 5,833,333 Common Shares (of which 1,666,667 Common Shares were issued to Formula), at a price per share of \$3.00 which reflected a premium of approximately 25% above the trading price of our Common Shares (as of the date our Board of Directors approved the investment). The closing for the remaining \$2.5 million, for an aggregate of 833,333 Common Shares, is expected by June 30, 2007. The investors were all non-US persons, and the Common Shares were issued to the investors pursuant to Regulation S. As a result, the issuance of the Common Shares to the investors was exempt from registration under the Securities Act.

In June 2007, we purchased an aggregate amount of NIS 15,000,000 nominal value, representing approximately \$3.5 million of the outstanding debentures. Pursuant to the terms of the prospectus governing the debentures, the amount repurchased by us was retired and removed from circulation. As a result, the total amount that we must pay in December 2007 was reduced to approximately \$4.6 million, approximately \$4.2 million for the second of the four annual re-payments of the principal of the debentures, and approximately \$0.4 million for the semi-annual interest payment.

Capital Expenditures and Divestitures since January 1, 2004

Our principal capital expenditures during the last three years related mainly to the purchase of computer equipment and software for use by our subsidiaries. These capital expenditures totaled \$442,000 in 2004, \$366,000 in 2005 and \$276,000 in 2006.

B. Business Overview

We are a global provider of information technology ("IT") solutions that modernize business processes to enable insurance and other leading companies to quickly adapt to change. Our solutions, sold as customizable software modules, align IT with business demands for speed, flexibility and efficiency. Our solutions are supplemented by our technology, methodology and consulting services, which address the complex issues related to the life-cycle of enterprise business applications. Our solutions include scalable insurance applications we have developed for leading organizations such as AXA, Norwich Union, Liverpool Victoria, IAT Group, ING, OneBeacon, Principal Financial Group, the Surplus Line Association of California, Allianz Group, Texas Farm Bureau Insurance Companies, Menora Mivtachim Insurance, PZU, Santam and Synergy Insurance. Our service offerings include a standard consulting offering that helps customers make better use of IT in order to achieve its business objectives.

Our core technology, Sapiens eMerge™, is a rules-based application development suite which enables rapid solution development for complex mission-critical enterprises to deliver new functionality, achieve legacy modernization and enterprise application integration. We believe that our understanding of the insurance marketplace and broad experience in mainframe-based legacy systems, backed by the high return on investment made possible by Sapiens eMerge™, help our customers gain a competitive edge in the rapidly changing business world while maximizing the value of their investments in existing IT systems.

Our primary goal is to rise to a position of global leadership in delivering strategic business software solutions to the insurance industry, selling Sapiens INSIGHT™, our suite of modular business software solutions. Our mission is to drive customer profitability in the global insurance industry through thought leadership and the proven delivery methodology of our innovative solutions. We plan to achieve this objective by combining our insurance expertise and extensive experience in implementing feature-rich, robust, high volume solutions in order to deliver to our clients customizable software products for life insurance, pensions and annuities, general insurance, reinsurance and specialized underwriting. The primary building block of our Sapiens INSIGHT™ solution remains Sapiens eMerge™, our business rules engine that has evolved and matured over the course of thousands of man-years of research and development efforts. Sapiens eMerge™, which serves over 100 of our clients worldwide, reduces the cost of business software development and maintenance.

We market our solutions globally through our direct sales force and through marketing alliances with global IT providers, such as IBM Corporation and Electronic Data Systems Corporation. We have cooperated with IBM Corporation for over 10 years at what IBM refers to as a “Premier Business Partner” level. Currently, we work with IBM on solutions, joint development, testing, validation and marketing. Through this and other business alliances, we have developed extensive knowledge in mainframe and mid-range systems, including CICS, DB2, MQ and the WebSphere e-business platform. We are also a member of IBM’s Insurance Application Architecture (IAA) group and the ISV Advantage Program for the Small and Medium Business insurance market segment. These alliances enable us to reach a broader base of customers while complementing our partners’ offerings.

Industry Background

The global insurance industry is at a crossroads; facing increased underwriting risks, a highly competitive landscape, new regulations, complicated sales channels and demanding customers.

The insurance industry is struggling to meet heightened needs of intermediaries and customers that have grown to expect information and answers immediately on request. Increased competition, demographic trends, legislative and regulatory requirements and escalating operational costs add to the complex challenges insurance organizations face today.

While insurance companies’ current systems may not be appropriate for current challenges and may be outdated, they are still an important part of an organization because of the vast amounts of information they contain. Replacing them could cause a significant loss of business productivity.

Businesses try to address these challenges in a variety of ways. Certain companies choose to dedicate significant in-house IT resources to address these issues. In many cases, however, organizations lack the requisite internal resources and know-how. As a result, many of these organizations rely on the expertise of external IT service providers.

Our Business Solutions for the Insurance Industry

Our management has focused the Company’s resources on delivering solutions to help the insurance industry become more agile in the face of the new and rapidly changing business environment described above, while simultaneously reducing IT costs.

By creating cross-functional teams and working with leading insurance companies, we have formulated Sapiens INSIGHT™, a suite of modular business software solutions that make use of existing assets to quickly and cost-effectively modernize business processes that are the key to survival in the current, challenging insurance landscape. Our Sapiens INSIGHT™ insurance solutions suite is already helping enterprises adapt to the marketplace’s time and cost pressures.

We collaborate with our customers to tailor the Sapiens INSIGHT™ solutions to achieve the unique operational performance goals of each organization. In addition, we have executed independent projects for the insurance market, providing enhanced information access and visibility to empower the sales, agent and broker community, thus accelerating transaction processing for improved customer service and business efficiency. Our insurance solutions, which include the Sapiens INSIGHT™ family, are based on Sapiens eMerge™, our rules-based rapid application development (RAD) suite, which enables rapid solution development and maintenance. The Sapiens INSIGHT™ modules therefore allow the codifying of carriers' implicit business rules into explicit, executable technical rules. The transition to a rules-based system allows for rapid interactive development by technical and business personnel, allowing business users to make changes using everyday language rules rather than application code. Our insurance solutions are compatible with a variety of platforms including IBM System z, IBM System i and HP UNIX at the host-side and Intel-based Web servers. They are also compatible with open architecture standards such as .NET, Java EE, XML, Web Services and application server platforms such as IBM's WebSphere™.

Sapiens INSIGHT™ is designed for the general (property and casualty) and life insurance markets. These solutions can be customized to match specific legacy systems and business requirements, while providing pre-configured functionality. These solutions can be used independently or together as follows:

*** Sapiens INSIGHT™ for Property & Casualty**

INSIGHT™ for Property & Casualty (formerly known as Policy INSIGHT™) is a fully functional, general insurance policy administration solution that makes it easier for brokers and agents to do business with carriers. By automating the process, this web-enabled solution reduces the cost of doing business and optimizes risk selection through the use of rules based underwriting. Sapiens INSIGHT™ for Property & Casualty is designed to improve internal efficiencies and simplify and accelerate the cycle of new business, and property and casualty policy processing and administration, by automating policy lifecycle processes and by allowing business analysts to quickly respond to changing rate and regulation issues. The solution also provides functionality supporting the rapid development and launch of new products to keep pace with competitive pressures and market opportunities. Sapiens INSIGHT™ for Property & Casualty is available as a complete package, or in individual modules. Some of the individual modules are: Policy Administration, Billing, Claims, Commissions and Reinsurance.

*** Sapiens INSIGHT™ for Life & Pensions (INSIGHT™ for Life & Health)**

Sapiens INSIGHT™ for Life & Pensions, known in the United States as Sapiens INSIGHT™ for Life & Health, is a powerful and comprehensive framework-based life and pensions solution that serves companies administering life insurance, pension funds, health insurance and saving plans.

Sapiens INSIGHT™ for Life & Pensions is dynamic, highly customizable and can be easily accommodated to administer changes in processes. It is fully web-enabled, prepared to utilize the advantages of the Internet and intranets.

Sapiens INSIGHT™ for Life & Pensions consists of the following independent modules that can be implemented together or only individually:

- Processes Management - An efficient processes management module, very easy to build and maintain
- Products Management - Set of tools that enables minimum time-to-market
- Dossier Administration
- Surrender Value and Paid-Up policies processes
- Billing and Collection
- Funds Revaluation
- Investment Gateway

*** Sapiens INSIGHT™ for Underwriting**

Sapiens INSIGHT™ for Underwriting (formerly MediRisk INSIGHT™) is an underwriting solution for life, health and disability insurance. It reduces a customer's costs by automating a larger portion of the process of evaluating the risks of new business and by streamlining the procedures for handling new business. By using this solution, an insurance company can make underwriting assessments on new cases earlier in the business cycle and achieve greater consistency in its decision-making. We market Sapiens INSIGHT™ for Underwriting on the basis of 17 licensing and distribution agreements with MediRisk Solutions Ltd. which developed and holds the intellectual property rights to the solution.

*** Sapiens INSIGHT™ for Reinsurance**

Sapiens INSIGHT™ for Reinsurance is a sophisticated solution for the insurance market, designed to support carriers and reinsurers in the management of all types of reinsurance for the general (property and casualty) insurance market, according to the rapidly changing requirements of the international reinsurance market. This state-of-the-art, web-enabled solution streamlines and reduces the cost of handling all reinsurance functions through automation, is based on ACORD standards and B2B XML technology, and is designed for a multi-language, multi-currency, multi-company environment.

*** Sapiens INSIGHT™ for Claims**

Sapiens INSIGHT™ for Claims is a solution that effectively manages and streamlines the information flow of claim handling across an insurance provider's entire organization. The claims handled include disability and maturity claims (annuities, pensions), death claims and health claims. This solution uses highly accessible business rules and messaging standards and allows the use of a company's existing information assets. Thus, the solution improves operational efficiency and enables better and more versatile customer service capabilities, with the goal of providing faster return on investment by reducing the total claims payout.

*** Sapiens INSIGHT™ for Closed Books**

Sapiens INSIGHT™ for Closed Books, also known as LifeLite, is a solution for life insurance companies and pension funds seeking ways to reduce the cost of maintaining long-term closed books of business, that is, lines of business that are no longer current. We provide customizable solutions that enable companies to efficiently and more effectively administer policies and claims relating to closed books. Lower ongoing cost of ownership is achieved by replacing "old" systems (which reflect out-dated business models and working practices with long processing cycles and limited on-line functionality) with modern technology and a Web browser user interface. In September 2004, we purchased the technologies underlying the Sapiens INSIGHT™ for Closed Books solution from Liverpool Victoria Friendly Society Limited.

Our Core Technology - Sapiens eMerge™

Our solutions are built on Sapiens eMerge™. Sapiens eMerge™ is a data-driven, rules-based, enterprise-scale transaction engine that facilitates business process integrity, application scalability and high performance. Its foundation is a rules-based development tool and repository that imposes easily-coded business rules, lending unconventional speed, visibility, agility and cost-effectiveness to the business software lifecycle. The use of Sapiens eMerge™ reduces the complexity of programming so that new applications and modifications of existing ones can be produced in a much shorter time frame than through conventional programming.

Another key advantage of Sapiens eMerge™ is the ability to extend the productive life of older computer systems, while at the same time providing the basis for using new generation Internet and service-oriented technologies. The use of rapid application development allows enterprise-specific enhancements to be made in a shorter time and with a greatly reduced maintenance burden when compared to other technologies.

Sapiens eMerge™ is based on a multi-level architecture and operates in multi-platform environments, encompassing many hardware vendors, operating system environments and databases. Host-side platforms supported include IBM's System z (zSeries), System i (iSeries), HP-UNIX and Linux. Sapiens eMerge™ supports databases such as DB2, VSAM, IMS, DB2/400 and Oracle. Since Sapiens eMerge™ exemplifies open systems and cross-platform capabilities, solutions developed with it can be seamlessly migrated from platform to platform and from database to database.

Development, deployment, integration and administration of applications are all accomplished through the technology components of Sapiens eMerge™, providing customers with flexible, scalable and feature-rich systems.

Services

Outsourcing of Application Maintenance. Our outsourcing services developed from our strong, long-term relationships with our customers. We are currently servicing multi-year outsourcing contracts with blue-chip customers involving mission-critical systems. The outsourcing projects are performed either on or off the customers' premises.

IT Services. We provide customers with specialized IT services in many areas, including project management and technical assistance. Our personnel work with the customer for the duration of the entire project, collectively undertaking design, development and deployment tasks, coupled with hands-on-training, to achieve a rapid software solution that matches the customer's business and IT goals.

Key Benefits of our Technology to our Customers

- **Fast Time to Market and High Return on Investment.** Our combination of a Rapid Application Development (RAD) methodology, rules-based development tools and experienced consultants has resulted in significant productivity increases at customer sites. Declarative development with business rules replaces traditional programming methods, addressing the full application life cycle, meaning that no programming code development is required. Sapiens eMerge™ also employs a "positive inference" engine that streamlines application development by requiring only the definition of standard situations, while automatically generating the logic required to handle the non-standard ones. This represents a reduction in logic specification and application maintenance and greatly enhances the quality of the delivered application compared to conventional development environments where most "bugs" arise in the non-standard logic.
- **Strong Technical Competence.** Our solutions enable organizations to capitalize on their existing large-scale applications and data by non-intrusively integrating them with modern applications and technologies. Our solutions not only extend the productive life of older computer systems but simultaneously provide a migration path to next-generation technologies. Our solutions are designed for an extensive list of computing platforms and technologies including IBM zSeries and iSeries, HP-Unix at the host server-side and Windows 2000 / XP Web Servers. Due to the separation between business logic, data access logic and presentation logic, applications developed for a particular computing platform and database are seamlessly portable to other supported computing platforms and databases. The platform-independent nature of our solutions allows them to be scaled according to the needs of the organization. Sapiens eMerge™ has proven to be extremely scalable, allowing the daily execution of hundreds of millions of business rules for tens of thousands of concurrent users.

Customers

Sapiens INISGHT™

We market our Sapiens INISGHT™ suite of solutions to insurance carriers in four main categories: Property & Casualty (known as General Insurance in Europe); Life and Pensions (known as Life and Health in the United States), Reinsurance and Medical Underwriting. Our customers and target markets have direct written premiums in the range of \$80 million to \$5 billion per year. However, given the flexibility and modularity of the Sapiens INISGHT™ suite of solutions, our offerings can accommodate most situations and budgets.

Sapiens eMerge™

We market Sapiens eMerge™ primarily to corporate clients and government entities with large information technology budgets and ongoing maintenance and development needs. Our corporate customers include, among others, insurance companies, banks and other companies offering financial services, as well as companies in the manufacturing and transportation sectors.

The principal markets in which we compete are located in North America, Europe, Israel and Japan. As of December 31, 2006, we had approximately 140 customers in all the geographical areas in which we operate. Of these, the primary customers were Menora Mivtachim Insurance, Synergy, PZU, EDS Credit Services Limited, Texas Farm Bureau Insurance Companies, Liverpool Victoria Friendly Society Limited, Occidental Fire and Casualty Company of North Carolina and AXA Corporation, accounting for 52% of our gross revenues during 2006.

Competition

The market for enterprise software solutions is highly competitive and characterized by rapidly changing technology, evolving industry standards and customer requirements, and frequent innovations. On the operational level, insurance companies are focusing their business in an attempt to reduce costs and maximize efficiency, and to respond to frequent changes in regulations. Insurance companies need a solution that provides flexible management of business processes, support for rapid changes in regulations and fast time to market. The INSIGHT™ suite of solutions was designed to answer those challenges.

The following is a breakdown of the competition that we face in each of our primary markets:

Sapiens INSIGHT™ - Insurance

Our competitors in the market for solutions offered to the insurance industry fall into several categories: vendors of complete systems, vendors of insurance software products, large multinational integrators and local integrators in the various territories in which we operate. Examples of these competitors are:

In the United States:	CSC, Camilion, SOLCORP, Fineos, SAP, SunGard, Navisys, Fiserv, OneShield, Ascendant One, Insurity, IDP, The Innovation Group, Duck Creek and AQS;
In the United Kingdom:	Unisys, SunGard, FIS Software (an affiliate of Formula) and RebusIs;
In Germany:	Falmeyer (FJA) and COR AG Insurance Technologies.

Examples of large integrators in the insurance field are Electronic Data Systems and CSC (companies that also have customer or alliance relationships with Sapiens in other fields). An example of a competitor that is a local integrator is Ness Technologies in Israel.

In addition, we face competition from our customers' and our potential customers' internal IT departments, who often prefer to develop solutions in-house.

We differentiate ourselves from our competition with a few key factors:

- (i) Sapiens INSIGHT™ is innovative and modern, rich in functionality and Internet compatible.
- (ii) As a result of the Sapiens INSIGHT™ architecture, customers may implement the full solution or parts of it, and readily integrate it into existing "legacy" systems.
- (iii) Sapiens INSIGHT™ is agile and flexible to use, based on its product configurator and its business rule technology.

Sapiens eMerge™ - Business Rules Engines

There has been an infusion of new vendors and new features into the business rules engine and management marketplace. Our competitors in the business rules engines and management marketplace include, among others, Fair Isaac (Blaze), Pegasystems, ILOG, Computer Associates, Haley, Corticon, Versata, RuleBurst and ESI.

We differentiate ourselves from our competition with a few key factors:

- (i) Our ability, utilizing Sapiens eMerge™ technology, to deliver a comprehensive IT solution, including an automatically generated Web presentation layer and interfaces with various databases, legacy systems and third party software. Most competing business rules engines are characterized by delivery of specialized, decision support capabilities that must be later framed into an enterprise's overall architecture at additional investment costs.

- (ii) Sapiens eMerge™ is highly optimized for performance of data-intensive tasks that characterize many enterprises' transactional environments.

Sapiens eMerge™ - IT Solution Delivery

By leveraging our differentiating characteristics mentioned above, we compete in the much larger IT solution delivery market, carving out for ourselves a niche attractive to mid-size enterprises seeking rapid and cost-effective custom software solutions. Our competitors in this domain include, among others: IBM, EDS, CSC, Accenture, Unisys, and India-based system integrators such as Tata, Infosys, and WiPro.

International Advisory Board

In May 2007, we disbanded our International Advisory Board that was created during 2004, as part of our cost-cutting efforts. Previously, we disbanded our Americas Advisory Board and our UK Vision Board.

Sales and Marketing

To reach the broadest potential customer base, we use multiple distribution channels, including a direct sales force and relationships with system integrators and, in certain geographic areas, distributors.

We have marketing and sales personnel located at our offices in the United States, the United Kingdom, Japan and Israel. The direct sales force focuses on large organizations within select industries. It also coordinates sales activities with system integrators such as EDS and IBM. These partnerships allow us to further expand our own solutions and to gain access to specific types of businesses.

We employ a variety of business development and marketing techniques to communicate directly with current and prospective clients. These techniques include exhibiting at trade shows and industry conferences, disseminating product brochures and other literature, direct-mail marketing, authoring articles, and hosting business forums for customers and prospective customers on technology and industry issues.

Customer Maintenance and Support

We believe that a high level of post-contract customer support is important to the successful marketing and sale of our solutions. We employ a team of technical specialists who provide a full range of maintenance and support services to our customers. The typical direct sale to a client includes initial maintenance, training and consulting services. In addition, substantially all of our clients for which we have developed applications elect to enter into an ongoing maintenance and support contract with us. The term of such a contract is usually twelve months. A maintenance contract entitles the customer to technology upgrades, when made generally available, and technical support. In addition, we offer introductory and advanced classes and training programs available at our offices and at customer sites.

Our authorized distributors and system integrators also provide customers with training, product support and consulting services. Each of our software distributors is capable of providing training in its respective country. In addition, many international partners and distributors, particularly independent software vendors, operate their own technology training programs.

Geographical Distribution of Revenues

The following is a breakdown of our revenues by geographical areas based on our geographic markets, both in thousands of dollars and as a percentage of total revenues for the years indicated:

	<u>2004</u>		<u>2005</u>		<u>2006</u>	
United Kingdom	\$ 18,217	38.1%	\$ 12,604	32.0%	\$ 13,805	31.2%
North America	12,381	25.9	10,046	25.5	9,895	22.3
France	1,352	2.8	1,131	2.9	902	2.0
Germany	1,814	3.8	1,414	3.6	837	1.9
Israel	8,910	18.6	9,147	23.2	12,072	27.2
Japan	3,147	6.6	3,902	9.9	4,491	10.1
Other	1,983	4.2	1,160	2.9	2,309	5.3
Total	\$ 47,804	100.0%	\$ 39,404	100.0%	\$ 44,311	100.0%

For details of revenues by category of activity, see the table entitled "Selected Financial Data" under Item 3, "Key Information."

Seasonality

Even if not reflected in our 2005 or 2006 results, traditionally, the first and third quarters of the fiscal year have tended to be slower quarters for us and the industries that we target. The first quarter usually reflects a lull following an active fourth quarter as companies rush to complete deals and utilize budgets before the end of the fiscal year. The slowdown in the third quarter reflects the summer months, which usually have reduced activities in many of the regions where our customers are located.

Intellectual Property

In accordance with industry practice, we rely on a combination of contractual provisions and intellectual property law to protect our proprietary technology. We believe that due to the dynamic nature of the computer and software industries, copyright protection is less significant than factors such as the knowledge and experience of our management and personnel, the frequency of product enhancements and the timeliness and quality of our support services. We seek to protect the source code of our products as trade secret information and as an unpublished copyright work. We also rely on security and copy protection features in our proprietary software. We distribute our products under software license agreements which grant customers a personal, non-transferable license to use our products and contain terms and conditions prohibiting the unauthorized reproduction or transfer of our products. In addition, we attempt to protect trade secrets and other proprietary information through agreements with employees, consultants and distributors. We do not believe that patent laws are a significant source of protection for our products and we do not hold any patents.

Our trademark rights include rights associated with our use of our trademarks, and rights obtained by registration of our trademarks. Our use and registration of our trademarks do not ensure that we have superior rights to others that may have registered or used identical or related marks on related goods or services. We have registrations for the mark "Sapiens" in the United States, Israel, Brazil and a number of countries in Europe. The initial terms of the registration of our trademarks range from 10 to 20 years and are renewable thereafter.

Our Sapiens INSIGHT™ group of solutions include our proprietary technology as well as technology licensed by customers (such as Liverpool Victoria, OneBeacon Insurance Company, Allianz Suisse and Menora) or strategic partners (MediRisk Solutions).

C. Organizational Structure

Sapiens International Corporation N.V. is the parent company of the Sapiens group of companies. We have a number of subsidiaries in Israel and throughout the world. The significant subsidiaries are as follows:

Sapiens International Corporation B.V. ("Sapiens B.V."): incorporated in The Netherlands and 100% owned by Sapiens. Unless otherwise indicated, the other subsidiaries of Sapiens listed below are all 100% owned by Sapiens B.V.:

Sapiens Israel Software Systems Ltd.: incorporated in Israel
Sapiens Technologies (1982) Ltd.: incorporated in Israel
Sapiens Americas Corporation: incorporated in New York
Sapiens (UK) Limited: incorporated in England
Sapiens France S.A.S.: incorporated in France
Sapiens Deutschland GmbH: incorporated in Germany
Sapiens (Schweiz) AG: incorporated in Switzerland
Sapiens Japan Co.: incorporated in Japan and 90% held by Sapiens B.V.

We are a member of the Formula Systems (1985) Ltd. Group (NASDAQ: FORTY and TASE: FORT). Formula is a holding and managing company of publicly traded companies and their subsidiaries. Formula companies provide IT solutions worldwide, developing and implementing innovative, proprietary software, services and solutions, turnkey projects and outsourcing services as well as software distribution and support. As of June 27, 2007, Formula beneficially owned approximately 53% of our outstanding Common Shares.

In November 2006, Emblaze purchased the controlling interest in Formula, and as a result, controls us. As of June 1, 2007, Emblaze beneficially owned 50.1% of the outstanding share capital of Formula.

Based on Formula's beneficial holding of over 50% of the outstanding Common Shares of the Company, and based on Emblaze's beneficial holding of over 50% of the outstanding share capital of Formula, both Formula and Emblaze may be considered to control us.

D. Description of Property

We lease office space in Israel, the United States, the United Kingdom, France and Germany. The lease terms are generally five to ten years. In Israel, we lease approximately 45,350 square feet of office space; in the United States, approximately 8,400 square feet; in the United Kingdom, approximately 13,800 square feet; and smaller areas in the other locations. In 2006, our rent costs totaled \$1.68 million in the aggregate for all of our leased offices. Our corporate headquarters are located in Israel and our core research and development activities are performed at our offices in Israel. Our sales, marketing and general and administrative activities are performed in each of our offices. We believe that our existing facilities are adequate for our current needs.

ITEM 4A. UNRESOLVED STAFF COMMENTS

Not Applicable.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following management's discussion and analysis of financial condition and results of operations should be read in conjunction with our consolidated financial statements and the notes thereto.

Overview

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and result of operations is based upon our consolidated financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of our financial statements required us to make estimations and judgments, in accordance with U.S. GAAP, that affect the reporting amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates, including those related to revenue recognition, bad debts, goodwill and other intangible assets, foreign currency fluctuation, capitalized software development costs, deferred taxes, income taxes, restructurings and legal contingencies. We based our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis of making judgments about the values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. More detailed descriptions of these policies are provided in Note 2 to the consolidated financial statements.

We believe the following critical accounting policies affect the estimates and judgments that we made in preparing our consolidated financial statements.

Revenue Recognition

Our revenue recognition approach for software licensing requires that, in accordance with Statement of Position No. 97-2 "Software Revenue Recognition" (as amended), four basic criteria must be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services rendered; (3) the fee is fixed and determinable; and (4) collectibility is reasonably assured. Determination of criteria (3) and (4) is based on management's judgments regarding the fixed nature of the fee charged for services rendered and products delivered, and the collectibility of those fees. Should changes in conditions cause management to determine these criteria are not met for certain future transactions, revenue recognized for any reporting period could be adversely affected.

Revenues under multiple-element arrangements, which may include software licenses, support and maintenance, and training and consulting services, are allocated to each element based on their respective fair values based on vendor-specific objective evidence of the respective undelivered elements. This objective evidence represents the price of products and services when sold separately. When vendor-specific objective evidence of fair value exists for undelivered elements but does not exist for delivered elements of a software arrangement, we use the residual method for recognition of revenues, when all other revenue recognition criteria are met. Under the residual method, we defer revenues related to the undelivered elements based on their vendor-specific objective evidence of fair value and recognize the remaining arrangement fee for the delivered elements. When vendor-specific objective evidence of fair value for undelivered elements does not exist, revenues from the entire arrangement are recognized over the term of the agreement.

We recognize revenue from consulting services ratably over the contractual period or as the services are performed. We recognize revenue from support and maintenance agreements ratably over the term of the agreement, which is typically one year. We recognize revenues from training arrangements as the services are performed.

We generally do not grant a right of return to our customers. When we do grant a right of return, we defer the recognition of revenue until the right of return expires, provided that all other revenue recognition criteria are met.

Amounts collected or billed prior to satisfying the above revenue recognition criteria are reflected as deferred revenue. Deferred revenue represents deferred maintenance revenue, and to a lesser extent, deferred software license revenues.

Our project business derives a significant portion of its revenue from fixed price contracts. Revenues from fixed-price contracts are recognized based on Statement of Position No. 81-1 "Accounting for Performance of Construction Type and Certain Production Type Contracts," which requires the accurate estimation of the cost, scope and duration for each project. Revenue and related cost for these projects are recognized on percentage of completion, using the input measure or output measure to assess the percent completed with revisions to estimates reflected in the period in which changes become known. If we do not accurately estimate the resources required or the scope of work to be performed, or do not manage the project properly within the projected periods of time or satisfy our obligations under the contract, project margins may be significantly and negatively affected, which may result in losses on existing contracts. Any such resulting reductions in margins or contract losses in a large, fixed-price contract may have a material adverse impact on our results of operations.

Bad Debt

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. If the financial condition of our customers was to deteriorate, resulting in an impairment of their ability to make payments, additional allowances would be required.

Goodwill and other identifiable intangible assets

SFAS No. 142, "Goodwill and Other Intangible Assets" requires that goodwill be tested for impairment on adoption and at least annually thereafter. Goodwill is required to be written down when impaired, rather than amortized as previous accounting standards required. Goodwill is tested for impairment by comparing the fair value of the reporting unit with its carrying value. Fair value is generally determined using market capitalization.

We selected December 31st as the date on which we will perform our annual goodwill and intangible assets with an indefinite life impairment tests. Through December 31, 2006, no impairment was required.

In accordance with SFAS No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets," our long-lived assets are reviewed for impairment annually and 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 the assets to the future undiscounted cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. In measuring the recoverability of assets, we are required to make estimates and judgments in assessing our forecast and cash flows and compare that with the carrying amount of the assets. Additional significant estimates used by management in the methodologies used to assess the recoverability of our long-lived assets include estimates of future cash-flows, future short-term and long-term growth rates, market acceptance of products and services, and other judgmental assumptions, which are also affected by factors detailed in our Risk Factors section in this Annual Report (*see Item 3, "Key Information – Risk Factors"*). If these estimates or the related assumptions change in the future, we may be required to record impairment charges for our long-lived assets.

Share-Based Payments

Effective January 1, 2006, we adopted Statement of Financial Accounting Statement No. 123 (revised 2004), "Share-Based Payment" ("SFAS 123 (R)"), which is a revision of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123") which requires the measurement and recognition of compensation expense based on estimated fair values for all share based payments awards made to employees and directors. In March 2005, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 ("SAB 107") relating to SFAS 123 (R). We have applied the provisions of SAB 107 in our adoption of SFAS 123 (R).

SFAS 123 (R) requires us to estimate the fair value equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the awards that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company's consolidated statement of operations. Prior to the adoption of SFAS 123 (R), we accounted for equity based awards under the fair value recognition provisions of SFAS 123.

We adopted SFAS 123 (R) using the Modified Prospective Method. Under that transition method, compensation cost recognized in the year ended December 31, 2006 included: (a) compensation cost for all share-based payments granted prior to, but not yet vested as of, January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all share-based payments granted subsequent to January 1, 2006 based on the grant-date fair value estimated in accordance with the provisions of the SFAS 123 (R). In December 2005, primarily as a result of the issuance of SFAS No. 123 (R), we accelerated the vesting of all unvested stock options held by employees and directors.

Beginning on the date of adoption of SFAS 123 (R), we estimate forfeitures based on historical experience and other factors; previously, we recorded forfeitures as they occurred.

Foreign Currency Fluctuation

We expect that, in addition to the US dollar, a significant portion of our revenues will continue to be denominated in the British pound (the "GBP") and in the NIS and a smaller portion will be denominated in the Euro and Japanese yen. As a result, movements in the exchange rates between the US dollar and the GBP, the US dollar and the NIS, and to a lesser extent the US dollar and the Euro and the US dollar and the Japanese yen, could have a material adverse impact on our revenues and results of operations within Europe, Israel and Japan. We regularly assess our currency exchange exposures and determine whether to adjust or hedge our position. We may use derivative instruments to hedge or adjust our exposures. As a matter of policy we do not enter into transactions of a speculative or trading nature. Foreign exchange exposures are monitored by tracking actual and projected commitments and through the use of sensitivity analysis.

Capitalized Software Development Costs

Our policy on capitalized software costs determines the timing of our recognition of certain development costs. Software development costs incurred from the point of reaching technological feasibility until the time of general product release should be capitalized. We define technological feasibility as the completion of a detailed program design. The determination of technological feasibility requires the exercise of judgment by our management. Since we sell our products in a market that is subject to rapid technological changes, new product development and changing customer needs, changes in circumstances and estimations may significantly affect the timing and the amounts of software development costs capitalized and thus our financial condition and results of operations.

Deferred Taxes

Management judgment is required in determining our future taxable income for purposes of assessing our ability to realize any future benefits from our deferred tax assets. We record a valuation allowance to reduce our deferred tax assets to the amount that is more likely than not to be realized. If actual results differ from these estimates or we adjust these estimates in future periods, our operating results and financial position could be materially affected. If we determine that we will be able to realize the deferred tax assets in the future in excess of their net recorded amount, an adjustment to the deferred tax asset would increase income in the period in which such determination is made. On the other hand, should we determine that we will not be able to realize all or part of the net deferred tax assets in the future, an adjustment to the deferred tax assets will be charged to expenses in the period in which such determination is made. In 2006, we increased our deferred income tax assets resulting from loss carry-forward and other tax credits by \$1.9 million and increased the related valuation allowance by \$2.0 million.

Income Taxes

Through our operating subsidiaries, we operate within multiple tax jurisdictions and may be subject to tax audits in these jurisdictions. These tax audits can involve complex issues, which may require an extended period of time to resolve. In management's opinion, adequate provisions for income taxes have been made for all years. However, though our income tax reserves are based on our best knowledge, we may be subject to unexpected audits by tax authorities in the various countries where we have subsidiaries, which may result in material adjustments to the reserves established in our consolidated financial statements and have a material adverse effect on our results of operations.

Legal Contingencies

We are currently involved in certain legal proceedings and claims that arose in the ordinary course of business, as discussed in Note 11 of our consolidated financial statements. As of December 31, 2006, we have accrued our estimate of the probable costs for the resolution of those claims where we believe it is probable that we will incur a loss. This estimate has been developed in consultation with outside counsel handling our defense in these matters and is based upon an analysis of potential results, assuming a combination of litigation and settlement strategies. We do not expect these claims and/or proceedings to have a material adverse effect on our consolidated financial position. It is possible, however, that future results of operations or cash flows for any particular quarterly or annual period could be materially affected by changes in our assumptions related to these claims and proceedings.

Restructurings

In February 2006, we began to implement a restructuring plan for the purpose of reducing costs and restoring profitability. The restructuring plan includes the termination of the employment of approximately 25 employees.

In addition, in February 2005, we implemented a restructuring plan which resulted in the termination of approximately 40 employees.

The Company's restructuring plans in 2006 and 2005 resulted in costs of \$758,000 and \$1.1 million, respectively.

Recent Accounting Pronouncements

SFAS 157 – Fair Value Measurements

In September 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). This Statement defines fair values, establishes a framework for measuring fair values in generally accepted accounting principles and expands disclosures about fair values measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. We believe that SFAS 157 will not have a material effect on our consolidated financial statements.

FIN 48 – Accounting for Income Taxes

In June 2006, the FASB issued interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"), an interpretation of SFAS No. 109, "Accounting for Income Taxes". FIN 48 prescribes a comprehensive model for how companies should recognize, measure, present and disclose in their financial statements uncertain tax position taken or expected to be taken on a tax return. Under FIN 48, tax positions shall initially be recognized in the financial statement when it is more-likely-than-not that the position will be sustained upon examination by the tax authorities. Such tax position shall initially and subsequently be measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement with the tax authority assuming full knowledge of the position and all relevant facts. FIN 48 also revises disclosure requirements to include an annual tabular roll forward of unrecognized tax benefits. The provisions of this interpretation are required to be adopted for fiscal periods beginning after December 15, 2006. We will be required to apply the provisions of FIN 48 to all tax positions upon initial adoption with any cumulative effect adjustments to be recognized as an adjustment to retained earnings. The adoption of FIN 48 does not have a material impact on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS No. 159"), which permits companies to choose to measure certain financial instruments and other items at fair value that are not currently required to be measured at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. We have not yet determined the effect that the adoption of SFAS No. 159 will have on our consolidated financial statements.

A. Operating Results

Years ended December 31, 2005 and 2006

Revenues. Revenues from the sale of products are comprised of sales of Sapiens eMerge™ licenses, license upgrades, specially designed products for the insurance industry such as "Sapiens INSIGHT™ for Property & Casualty," "Sapiens INSIGHT™ for Closed Books," "Sapiens INSIGHT™ for Life & Pensions," "Sapiens INSIGHT™ for Reinsurance," "Sapiens INSIGHT™ for Underwriting," and "Sapiens INSIGHT™ for Claims" application development, re-engineering computer systems and converting operating systems. These specially designed products are provided to customers either on a fixed-price or time and materials basis. Revenues from services include mainly consulting on a time and materials basis, maintenance and support.

Total revenues in 2006 increased 12.4% to \$44.3 million from \$39.4 million in 2005. Product revenues in 2006 decreased 21.8% to \$10.4 million in 2006 from \$13.3 million in 2005. Consulting and other service revenues in 2006 increased 29.9% to \$33.9 million from \$26.1 million in 2005.

Our product revenues for the year 2006 decreased mainly due to changes in the contract terms with our major customer Menora. As a result of these contractual changes, we changed certain revenue classifications from product to consulting. The increase in consulting and other service revenues came as a result of the change to the Menora contract mentioned above. In addition, we started consulting projects with two new customers (PZU in Central Europe and Synergy in the United Kingdom, for a total of \$6.9 million).

Cost of Revenues and Gross Profit. Cost of revenues increased 16.1% to \$28.8 million in 2006 from \$24.8 million in 2005. Cost of revenues relating to products is comprised of salaries and other personnel-related expenses of software consultants and engineers (\$4.0 million, or 63.5% of our total costs of products in 2006, and \$5.7 million, or 64.8% in 2005), amortization of capitalized software development costs (\$1.1 million or 17.5% in 2006 and \$1.3 million or 14.8% in 2005), royalties to the Office of the Chief Scientist of the Ministry of Industry, Trade and Labor of Israel ("OCS") (\$534,000 or 7.9% in 2006, and \$1.1 million or 12.5% in 2005) and other costs (\$677,000 or 11.1% in 2006, and \$726,000 or 8.0% in 2005). Cost of revenues relating to consulting and other services is comprised of salaries and other personnel-related expenses, and amortization of capitalized software development costs. Salaries and other personnel-related expenses amounted to \$19.0 million in 2006, an increase of 40.7% from \$13.5 million in 2005, mainly because of the new projects. Amortization of capitalized software development costs amounted to \$3.5 million or 15.6% of our cost of revenues related to consulting in 2006 and \$2.5 million or 15.6% in 2005.

Our gross profit in 2006 increased 6.2% to \$15.5 million from \$14.6 million in 2005. The gross profit margin decreased by 5.2% to 35.0% from 36.9% in 2005. Gross margin decreased as a result of the \$1.4 million decrease in revenue from license sales, which reflected 58% of the 5.2% decrease in our gross margin.

Gross profit from product revenues decreased 8.9% in 2006 to \$4.1 million from \$4.5 million in 2005. Gross margin from product revenues was 39.5% in 2006, an increase of 17.2% from 33.7% in 2005. The increase in product gross margin was due to projects with higher margins.

Gross profit from consulting, maintenance and other services increased 12.9% to \$11.4 million in 2006 from \$10.1 million in 2005. Gross margin from consulting, maintenance and other services decreased 13.0% in 2006 to 33.6% from 38.6% in 2005. The decrease in the gross margin from consulting, maintenance and other services is due to the change in the nature of our relationship with certain customers (including Menora) in 2006 and the transfer of certain revenues from product to consulting, which had smaller gross margins.

Amortization of capitalized software development costs increased 21.1% to \$4.6 million in 2006 from \$3.8 million in 2005. The increase is due to the release for sale of a new Sapiens eMerge™ version at the beginning of 2006.

Research and Development, net. Research and development (“R&D”) costs are mainly comprised of labor costs and depreciation of property and equipment, reduced by grants from the OCS and capitalization of software development costs. Net R&D expenses decreased 7.4% in 2006 to \$2.5 million from \$2.7 million in 2005. The decrease in spending on R&D recorded in 2006, as compared with the previous year, resulted from the reduction in the number of R&D employees.

A portion of our R&D expenditures is funded by the OCS in accordance with programs entitling the government of Israel to receive royalties on sales of products and services developed as a result of R&D projects so funded. In 2006 we had no R&D expenditure that benefited from OCS funding. In 2005 our net R&D expenditure that benefited from OCS funding was \$520,000.

Capitalized software development costs increased 9.3% to \$4.7 million in 2006 compared with \$4.3 million in 2005. This increase reflected our development efforts on Sapiens INSIGHT™ products.

Selling, Marketing, General and Administrative expenses, net. Selling, marketing, general and administrative, net expenses (“SG&A expenses”) decreased 16% in 2006 to \$13.6 million from \$16.2 million in 2005. SG&A expenses consist primarily of salaries and other personnel-related expenses, which in 2006 amounted to \$8.1 million, or 59.6% of total SG&A expenses, and in 2005 to \$10.3 million or 63.6% of total SG&A expenses as well as other costs associated with our sales and marketing efforts and our general and administrative activities such as rent which amounted to \$2.4 million in 2006, accounting, legal and other public company expenses in the amount of \$0.7 million, depreciation costs of \$0.3 million, marketing costs, including tradeshows and design, in the amount of \$0.4 million and other miscellaneous costs amounting to \$1.6 million. General and administrative expenses include offices and office maintenance, communications, external consultants and other expenses. The decrease in SG&A expenses in 2006 was the result of planned and consistent efficiency measures implemented by our management, which resulted in reduced expenses, particularly reduced salary as a result of the February 2006 restructuring, which resulted in a reduction of annual direct labor costs of \$2.6 million. In addition, in the third quarter of 2006, the Company wrote-off \$360,000 due to bad debts.

Restructuring Costs. Restructuring costs in 2006 were \$758,000 as a result of the restructuring we implemented in February 2006, which resulted in the termination of approximately 25 employees. Restructuring costs in 2005 were \$1.1 million, as a result of the restructuring we implemented in February 2005, which resulted in the termination of approximately 40 employees. There are no restructuring costs from the 2006 terminations that have not been recorded in our consolidated financial statements.

Financial expenses, net. Our financial expenses, net, increased 22.2% to \$2.2 million in 2006 from \$1.8 million in 2005. The increase is due to the sale of our marketable securities which resulted in a decrease of \$187,000 in financial income and the net effect of currency fluctuations in the amount of \$235,000.

Taxes on Income. Our net tax expenses in 2006 were \$325,000 compared with \$1.8 million in 2005, due to the fact that in 2005 our deferred tax asset and tax advances were reduced by a total of \$1.6 million as compared to 2006 when they were reduced by \$160,000. In addition, in 2006 we incurred current tax expenses of \$165,000, of which \$104,000 were in Japan.

Our provision for taxes on income relates to operations in jurisdictions other than the Netherlands Antilles. The effective income tax rate varies from period to period as a result of the various jurisdictions in which we operate and where each one has its own system of taxation (not only with respect to the nominal rate, but also with respect to the allowance of deductions, credits and other benefits). We record a valuation allowance if we believe that it is more likely than not that the deferred income taxes regarding the loss carry forwards and other temporary differences, on which a valuation allowance has been provided, will not be realized in the foreseeable future. We did not recognize a majority of the deferred tax assets relating to the net operating losses of our subsidiaries worldwide due to the uncertainty of the realization of such tax benefits in the foreseeable future.

Net Loss. Net loss to shareholders of Common Shares for 2006 was \$3.8 million, a decrease of 58% compared with a net loss to shareholders of \$9.1 million in 2005. The decrease in net loss to shareholders in 2006 was primarily the result of planned and consistent efficiency measures implemented by our management, which resulted in a reduction of \$4.3 million in our operating losses, and the reduction in our tax expenses in the amount of \$1.5 million.

Years ended December 31, 2004 and 2005

As a result of the changes we made in 2006 to the classification of our amortization of capitalized software costs between product sales and consulting services, we have reclassified some of the 2005 and 2004 numbers to conform to the 2006 presentation above and in our consolidated financial statements.

Revenues. Total revenues in 2005 decreased 17.6% to \$39.4 million from \$47.8 million in 2004. Product revenues in 2005 decreased 50.4% to \$13.3 million in 2005 from \$26.8 million in 2004. Consulting and other service revenues in 2005 increased 24.3% to \$26.1 million from \$21.0 million in 2004.

Our product revenues for the year 2005 decreased mainly due to the completion of multi-year projects for two of our customers – EDSCS and Liverpool Victoria in the United Kingdom, which amounted to a decline of \$4.3 million, or 32% of the decline in our product revenue, and two of our customers CSC and OneBeacon in the United States, which amounted to a decline of \$3.1 million, or 23% of the decline in our product revenue, and the decision of such customers not to place follow-on orders. Product revenues also declined as a result of the prolonged periods of time required to negotiate with our customers, particularly in the insurance industry. The increase in consulting and other service revenues came as a result of higher revenues from consulting, were mainly due to the fact that the nature of our relationship with certain customers changed from project delivery to consulting services. As a result of a decrease in sales of new licenses, maintenance revenues decreased in the United Kingdom, the United States, Germany, Japan and Switzerland where the decrease from 2004 amounted to \$359,000, \$481,000, \$154,000, \$135,000 and \$151,000, respectively.

Cost of Revenues and Gross Profit. Cost of revenues decreased 10.5% to \$24.8 million in 2005 from \$27.7 million in 2004. Cost of revenues relating to products, is comprised of salaries and other personnel-related expenses of software consultants and engineers (\$5.7 million, or 64.8% of our total costs of products in 2005, and \$11.7 million or 76.5% in 2004), amortization of capitalized software development costs (\$1.3 million or 14.8% in 2005 and \$1.7 million or 11.1% in 2004), royalties to the OCS (\$1.1 million or 12.5% in 2005, and \$1.6 million or 10.5% in 2004) and other costs (\$726,000 or 8.0% in 2005, and \$323,000 or 2.0% in 2004). Salaries and other personnel-related expenses relating to consulting and other services amounted to \$13.5 million in 2005, an increase of 32.3% from \$10.2 million in 2004, mainly due to increased consulting revenues, which occurred primarily as a result of the change in the nature of our relationship with certain customers from project delivery to consulting services. Amortization of capitalized software development costs amounted to \$2.5 million or 15.6% in 2005, and \$1.3 million or 11.3% in 2004.

Our gross profit in 2005 decreased 27.4% to \$14.6 million from \$20.1 million in 2004. The gross profit margin decreased by 12.4% to 36.9% from 42.1% in 2004. Gross margin decreased, even though we reduced our expenses, since the influence of our 2005 restructuring plan was only felt late in the year while revenues declined throughout the year, and since our revenues decreased at a greater rate than our reduction in expenses.

Gross profit from product revenues decreased 57.5% in 2005 to \$4.5 million from \$10.6 million in 2004. Gross margin from product revenues was 33.7% in 2005, a decrease of 14.9% from 39.6% in 2004. The decrease in product gross margin is due to three main reasons. The first was that the nature of our relationship with certain customers changed in the United Kingdom in 2005, which resulted in the transition of revenues from products to consulting, which represented 24% of the decline in our gross margin from products. The second was due to the decrease in revenue from license sales which amounted to \$900,000 which had a 7% effect on our product gross margin. The third was the decrease in the profitability of our projects in Israel, the United Kingdom and the United States.

Gross profit from consulting, maintenance and other services increased 6.3% to \$10.1 million in 2005 from \$9.5 million in 2004. At the same time, gross margin from consulting, maintenance and other services decreased 14.9% in 2005 to 38.6% from 45.3% in 2004. The decrease in the gross margin from consulting, maintenance and other services was due to the decrease in higher margin maintenance revenue, to \$7.9 million in 2005 from \$9.2 million in 2004.

Amortization of capitalized software development costs increased 26.7% to \$3.8 million in 2005 from \$3.0 million in 2004. Since we released for sale a new Sapiens eMerge™ solution at the end of 2004, the amortization of this solution only began to have an impact in 2005.

Research and Development, net. Net R&D expenses increased 8.0% in 2005 to \$2.7 million from \$2.5 million in 2004. The increase in spending on R&D recorded in 2005, as compared with the previous year, resulted from the higher participation of the OCS in 2004, which decreased our R&D expenses in that year. Our net R&D expenditure benefited from OCS funding in the amounts of \$520,000 in 2005 and \$833,000 in 2004.

Capitalized software development costs decreased 8.5% to \$4.3 million in 2005 compared with \$4.7 million in 2004. This decrease reflected a restructuring executed in February 2005 which resulted in a reduction of R&D employees.

Selling, Marketing, General and Administrative expenses, net. SG&A expenses decreased 16.1% in 2005 to \$16.2 million from \$19.3 million in 2004. SG&A expenses consist primarily of salaries and other personnel-related expenses, which in 2005 amounted to \$10.3 million, or 63.6% of total SG&A expenses, and in 2004 to \$12.7 million or 65.8% as well as other costs associated with our sales and marketing efforts and our general and administrative activities such as rent which amounted to \$2.4 million in 2005, accounting, legal and other public company expenses in the amount of \$0.7 million, depreciation costs of \$0.4 million, marketing costs, including tradeshow and design, in the amount of \$0.3 million and other miscellaneous costs amounting to \$2.1 million. The decrease in SG&A expenses in 2005 was the result of planned and consistent efficiency measures implemented by our management, which resulted in reduced expenses, particularly reduced salary as a result of the February 2005 restructuring, which resulted in a reduction of direct labor costs of \$2.1 million.

Restructuring Costs. Restructuring costs in 2005 were \$1.1 million, as a result of the restructuring we implemented in February 2005, which resulted in the termination of approximately 40 employees. We did not incur any restructuring costs in 2004.

Financial expenses, net. Our financial expenses, net, decreased 25.0% to \$1.8 million in 2005 from \$2.4 million in 2004. The decrease resulted from a reduction in the amount of (short and long term) loans outstanding, from \$16.8 million at the end of 2004 to \$11.8 million at the end of 2004, which led to a reduction in the amount of interest incurred or paid during 2005. In addition, in 2005, we capitalized \$100,000 of financial expenses related to software development, in accordance with SFAS No. 86 which further reduced our financial expenses, and there was a reduction in the amount of bank fees we paid from \$249,000 in 2004 to \$84,000 in 2005.

Taxes on Income. Our net tax expenses in 2005 were \$1.8 million compared with \$217,000 in 2004. In 2005, we increased our deferred income tax assets resulting from loss carry-forward and other tax credits by \$658,000 and increased the related valuation allowance by \$1.5 million. We also recorded a write-off of tax advances, which were included in current assets, in the amount of \$783,000. As a result, our deferred tax asset and tax advances were reduced by a total of \$1.6 million. In addition, we wrote off \$80,000 of current tax expenses in Japan and \$118,000 of tax advances in other territories.

Net Loss. Net loss to shareholders of Common Shares for 2005 was \$9.1 million, an increase of 78.4% compared with a net loss to shareholders of \$5.1 million in 2004. The increase in loss to shareholders in 2005 was primarily due to the decline in our total revenues, which was not matched by a similar decline in expenses and due to the restructuring expense in 2005 of \$1.1 million and the reduction of our deferred tax asset and tax advances by a total of \$1.6 million.

Accelerated Options. In December 2005, we accelerated the vesting of all unvested stock options held by employees and directors. All of the options were considered out-of-the-money since the stated option exercise price was greater than the closing price of our Common Shares on the day we approved the acceleration (\$1.50). Unvested options to purchase approximately 1.7 million Common Shares became exercisable as a result of the vesting acceleration. Our decision to accelerate the vesting of those options was based primarily upon the issuance of SFAS No. 123(R) (revised 2004), which requires the Company to treat all unvested stock options as compensation expense effective January 1, 2006. The vesting acceleration did not result in the recognition of compensation expense in the year ended December 31, 2005. We prepared pro-forma results for 2005 as if we had recorded a compensation expense for the accelerations performed in December 2005. Such pro-forma results appear in the footnotes to our consolidated financial statements and reflect approximately \$1.9 million of compensation expense for the year ended December 31, 2005, resulting from the vesting acceleration. See Notes 2t and 2u of our consolidated financial statements for a description of SFAS No. 123(R) and its effect on our losses and losses per share.

B. Liquidity and Capital Resources

Cash, cash equivalents, marketable securities and short-term deposits at the end of 2006 were \$3.1 million, compared with \$12.0 million at the end of 2005. The decrease was due mainly to the repayment of loans in the net amount of \$2.9 million payment of convertible debt in the amount of \$2.4 million, investment in research and development activity of \$4.7 million and cash used in operating activities. The decrease was partially offset by the \$2.0 million investment by Formula in August 2006.

Net cash used in operating activities was \$0.9 million in 2006 compared with net cash provided by operating activities in 2005 of \$0.3 million. This change reflects the net loss for 2006 of \$3.8 million, the increase in trade receivables of \$2.2 million, and the decrease in deferred revenue of \$1.9 million. All of these were offset by depreciation and amortization charges of \$5.8 million, deferred issuance expenses and discount amortization of \$0.5 million, and a decrease in other receivables of \$1.6 million.

Net cash provided by investing activities was \$0.2 million in 2006, compared with net cash provided by investing activities in 2005 of \$0.9 million. In 2006, we generated \$5.4 million cash from the sale of marketable securities, which was offset by investments in software development of \$4.7 million, the purchase of property and equipment of \$0.3 million, and the investment in Sapiens Solutions, an affiliate of Sapiens Japan Co., of \$0.2 million.

Net cash used in financing activities totaled \$3.4 million in 2006, compared with \$4.9 million used in investing activities in 2005. In 2006, we received gross proceeds of \$2.0 million from the investment by Formula in August 2006. The outlay of cash used in financing activities in 2006 was \$2.9 million, net, in repayment of short term loans, and \$2.4 million in payment of convertible debt. In 2005, we received gross proceeds of \$2.0 million from the investment by Formula in the Company in return for the issuance of 1,041,667 Common Shares pursuant to a share purchase agreement (see Item 10, "Additional Information – Material Contracts – Agreements with Formula).

Credit Lines

We have a revolving credit line facility for borrowings of up to \$9.2 million, available until June 30, 2007. We are currently negotiating the extension of the credit facility for another year. We cannot be certain that an agreement will be signed, though we expect that an agreement will be signed that extends the current credit line, on substantially similar terms, for an additional year.

As a condition for receiving the current credit lines from our lender banks, we undertook, among other things, (a) not to charge or sell our assets to any entity whatever without the advance written consent of the banks, (b) that the total of our debts and obligations to the banks will not at any time exceed \$9.5 million, and (c) that the total of our accounts receivable from customers will not be less than \$6.0 million. In addition, we undertook that our quarterly earnings before income tax, depreciation and amortization will be positive through June 30, 2007 and that our aggregate earnings before income tax, depreciation and amortization for each of the year ended December 31, 2006, and the six-month period ended June 30, 2007, will not be less than \$1.0 million. We also undertook that our shareholders' equity will not be less than \$3.0 million. In addition, we undertook, on behalf of each of our subsidiaries, to provide the banks with cross guarantees from each subsidiary to secure our performance and fulfillment of any of our or our subsidiaries' obligations under the facilities. Among themselves, the banks are entitled to repayment of our debts in proportion to our debts to each bank. As a result of negotiations regarding the extension of our loan agreements, the assets of our subsidiary in the United States will be subject to a UCC-1 security interest and the assets of our subsidiaries in Israel and the United Kingdom will be subject to floating liens. Under the credit lines, borrowings in US dollars bear interest at rates ranging between LIBOR plus 2% to plus 2.25% and borrowings in NIS bear interest at the prime rate of interest in Israel plus 0.7%.

In December 2006, we entered into loan agreement with Bank Leumi Le-Israel whereby we borrowed an aggregate amount of approximately \$2.5 million. The proceeds of the loan enabled us to make the December 2006 principal and interest payment on our debentures. The loan was secured by a pledged deposit of Formula. The loan bears an annual interest rate equal to the prime rate of interest in Israel plus 0.5% (for a total of 6.5%) and the principal and interest are due on August 30, 2007. There can be no assurance that we will fulfill the covenants we undertook or, if we do not fulfill one or more of the covenants that we will receive from our lender banks waivers of the necessity of fulfilling such covenants.

In August 2006 we convened a general meeting of the debenture holders, where a special resolution was adopted concerning the amount and the timing of the first installment payment of the principal of the debentures. A majority of the debenture holders approved that (a) 50% of the first payment amount, approximately \$2.4 million, will be deferred to December 5, 2009 (the last date of payment of the principal on the debentures), and (b) with respect to the other 50% of the first payment amount, the Company could chose from the following alternatives, in its sole discretion: (1) to convert such amount on December 5, 2006 into Common Shares, at a conversion price per share of \$1.28, which reflects the average closing price for the 10 day period prior to July 17, 2006, or (2) to pay the approximately \$2.4 million to the debenture holders, in cash. In December 2006, we made the payments in cash.

In August 2006, we entered into a share issuance agreement with Formula pursuant to which Formula invested \$2.0 million in the Company and received 1,562,500 Common Shares. The purchase price per share was \$1.28, which was the average closing price for the 10 day period prior to July 17, 2006, and which was the same as the conversion price approved by the debentures holders at the August 2006 meeting.

In August 2006, we entered into an agreement with F.I.D. Holdings Ltd. and Israel Discount Bank Ltd., regarding the conversion of the \$1.0 million payment that was due to them on April 1, 2006 into 781,250 Common Shares, at a conversion price per share of \$1.28, which was the average closing price for the 10 day period prior to July 17, 2006, and the delay until August 1, 2007 of the \$1.0 million payment that was then due on August 1, 2006.

In June 2007, we entered into a private placement investment transaction with several institutional investors, private investors and Formula for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). As of June 27, 2007, we have held closings for \$17.5 million of the investment, \$5 million of which was by Formula. We issued to the investors an aggregate of 5,833,333 Common Shares (of which 1,666,667 Common Shares were issued to Formula), at a price per share of \$3.00 which reflected a premium of approximately 25% above the trading price of our Common Shares (as of the date our Board of Directors approved the investment). The closing for the remaining \$2.5 million, for an aggregate of 833,333 Common Shares, is expected by June 30, 2007.

In June 2007, we purchased an aggregate amount of NIS 15,000,000 nominal value, representing approximately, \$3.5 million of the outstanding debentures. Pursuant to the terms of the prospectus governing the debentures, the amount repurchased by us was retired and removed from circulation. As a result, the total amount that we must pay in December 2007 was reduced to approximately \$4.6 million, approximately \$4.2 million for the second of the four annual re-payments of the principal of the debentures, and approximately \$0.4 million for the semi-annual interest payment.

(For further details on certain of these transactions, see Item 10, "Additional Information – Material Contracts.")

Management believes that the proceeds of the \$20 million private placement investment will be sufficient for our present requirements, and at least until December 31, 2007, to support our operating and financing requirements. However, future operating requirements may necessitate the need for us to issue additional equity securities in connection with capital raising which could dilute the ownership interest of our existing shareholders.

C. Research and Development

See section A. "Operating Results" above.

D. Trend Information

The global insurance industry is constantly transforming as a result of regulatory changes. Insurance companies must comply with regulations such as the Sarbanes-Oxley Act of 2002 in the United States and Solvency II in Europe and other directives regarding transparency. In addition, many individual countries have increased supervision over local insurance companies.

Particularly in the reinsurance and the property and casualty markets, insurance companies have had to make large pay outs because of events such as September 11, 2001 and other terrorist incidents as well as great natural disasters such as Hurricane Katrina in the United States.

Globally, the insurance industry has witnessed cross-border mergers and acquisitions, and the entry of international insurance companies into new emerging markets.

In Europe, regulators and insurers have been very active and creative, motivated by past financial crises and the need for pension restructuring. Distribution of policies is being optimized with the increasing use of Bancassurance (selling of insurance through a bank's established distribution channels), supermarkets and kiosks (insurance stands). Nevertheless, European insurers, and to some extent North American insurers, are cautiously approaching spending increases and most companies have not decided to change their software.

Finally, in recent years there has been constant significant growth in income from annual premiums.

We believe that the insurance market is changing and the reasons that contributed to the delays we experienced in penetration of the insurance industry are gradually fading away.

However, we expect that additional time will be required to fully implement our strategy of focusing on the insurance industry, and that our results of operations and financial condition could continue to be adversely affected. We are addressing the challenges posed by the market environment by focusing our marketing and selling efforts and by further reducing the expenses of our operation.

E. Off-Balance Sheet Arrangements

We had no off-balance sheet concentration of credit risk such as foreign exchange contracts, options contracts or other foreign hedging arrangement as of December 31, 2006.

F. Contractual Obligations

The following table sets forth information on our short-term and long-term contractual obligations as at December 31, 2006 (in thousands of dollars):

	<u>Total</u>	<u>Less than 1 year</u>	<u>1 to 3 years</u>	<u>3 to 5 years</u>	<u>Over 5 years</u>
Convertible debentures	\$ 16,175	\$ 4,450	\$ 11,725	\$ --	\$ --
Short-term bank credit	4,728	4,728	--	--	--
Short-term bank loans	4,570	4,570	--	--	--
Long-term loan-investors	1,000	1,000	--	--	--
Long-term liability-third party	1,291	854	437	--	--
Accrued severance pay	924	--	--	--	924
Operating leasing	9,238	2,581	5,791	866	--
Total	\$ 38,016	\$ 10,183	\$ 17,953	\$ 866	\$ 924

G. Safe Harbor

The safe harbor provided in Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”) shall apply to forward-looking information provided in Items 5.E and F.

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. Directors and Senior Management

The following table sets forth certain information regarding the current executive officers and directors of the Company.

<u>Name</u>	<u>Age</u>	<u>Position</u>
Eli Reifman	37	Chairman of the Board of Directors
Ron Al Dor	46	President, Chief Executive Officer and Director
Guy Bernstein (1)	39	Director
Elior Brin *	51	Executive Vice President and Chief Financial Officer
Rami Doron	49	Chief Operating Officer
Yacov Elinav (2)	62	Director
Uzi Netanel (2)	71	Director
Gad Goldstein (1)	48	Director
Ido Schechter (1) (2)	46	Director
Naamit Salomon	43	Director
Ron Zuckerman **	50	Director
United International Trust N.V. (3)		Director

(1) Member of Compensation Committee

(2) Member of Audit Committee

(3) United International Trust N.V. is a corporate body organized under the laws of the Netherlands Antilles. The Articles of Incorporation of the Company provide that a corporate body may be a member of the Board of Directors.

* On June 17, 2007, we announced that, as of June 30, 2007, Mr. Brin will be replaced by Mr. Ron Giladi as Chief Financial Officer of the Company.

** As of July 1, 2007, Mr. Zuckerman will be replaced by Ms. Hadas Gazit Kaiser as a director of the Company.

Eli Reifman has served as Chairman of the Board of Directors since January 1, 2007. Mr. Reifman is a Co-founder and President of Emblaze. Prior to his appointment as President of Emblaze in December 2006, Mr. Reifman served as Chief Executive Officer of Emblaze from 2000 to 2006. Emblaze was established as GEO Interactive Ltd. ("GEO"), which was co-founded by Mr. Reifman in 1994. Prior to founding GEO, Mr. Reifman was the head of the Technical Development Department and acting head of all production in the Training Development Center of the Israeli Defense Forces, where he was responsible for producing high-end military simulators.

Ron Al Dor joined the Company as President and Chief Executive Officer in November 2005. Prior to joining the Company, from August 1996 until 2004, Mr. Al Dor served as President of TTI Team Telecom International Ltd. ("TTI"), a global supplier of operations support systems to communications service providers. Prior to that, Mr. Al Dor served as TTI's Co-President from November 1995 until August 1996 and its Vice President from September 1992 to November 1995. During his service in the Israeli Air Force, Mr. Al Dor worked on projects relating to computerization in aircrafts. Mr. Al Dor is a graduate of the military computer college of the Israeli Air Force, studied computer science and management at Bar Ilan University and attended the Israel Management Center for Business Administration.

Guy Bernstein has served as a director of the Company since January 1, 2007. Mr. Bernstein joined the Emblaze Group as Chief Financial Officer and member of the Board of Directors in April 2004 and was appointed Group Chief Executive Officer in December 2006. Prior to joining Emblaze, Mr. Bernstein served as Chief Financial and Operations Officer of Magic Software Enterprises ("Magic") (NASDAQ: MGIC), a position he held since 1999. He also acted as the Interim CEO for Magic's subsidiaries: MSE Israel Ltd. and Coretech Consulting Group. Mr. Bernstein joined Magic from Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global, where he acted as senior manager from 1994 to 1997. Mr. Bernstein is a Certified Licensed Public Accountant and holds a BA in Accounting and Economics from Tel Aviv University.

Elior (Ori) Brin joined the Company as Executive Vice President and Chief Financial Officer in March 2005. In addition to his position at the Company, Mr. Brin also serves as a director of Modelim Kranot Neemanut Ltd., a mutual funds management company, a position he has filled since 2005 and also filled from 1996 through 2003. Prior to joining the Company, he served as Chief Financial Officer of publicly traded companies such as VCON Telecommunications Ltd. (1998-2001), NICE Systems Ltd. (1997-1998), and B.V.R. Technologies Ltd. (1989-1996). Mr. Brin has an MBA from the Recanati School of Business Administration, Tel Aviv University.

Rami Doron joined the Company as Chief Operating Officer in February 2007. Prior to joining the Company, Mr. Doron led a business unit at Comverse Ltd. from January 2006 until February 2007. Prior to that, Mr. Doron was one of the founders of TTI where he led the professional services, R&D and existing customers' sales units from December 1993 until May 2005. At TTI, Mr. Doron was involved in defining and building support systems, and was responsible for delivering, maintaining and enlarging the business with worldwide customers. Prior to founding TTI, Mr. Doron led the software division at TEAM Computers Ltd. ("TEAM") from October 1985 until December 1993, where he was responsible for supporting a large customer base in Israel with TEAM's R&D and system support. Mr. Doron also has a software development background, having served as a database expert for several years. During his service in the Israeli Air Force, Mr. Doron was an electronics officer for six years. Mr. Doron is a graduate of Hadassah College with a degree in Software Engineering and he studied management at Bar-Ilan University.

Gad Goldstein has served as a director of the Company since 2002. He has served as President of Formula since 1995 and a director since 1985. Between 1985 and 1995, Mr. Goldstein was Vice President of Formula. Mr. Goldstein is Chairman of the Board of BluePhoenix Solutions Ltd. ("BluePhoenix") and serves as a director of Matrix IT Ltd., Magic, Formula Vision Technologies Ltd. and other companies in the Formula Group. Mr. Goldstein holds a BA in economics and an MA in business administration, both from Tel Aviv University.

Naamit Salomon has served as a director of the Company since September 2003. She has held the position of Vice President, Finance of Formula since August 1997. Ms. Salomon also serves as a director of Magic and BluePhoenix. From 1990 through August 1997, Ms. Salomon was a controller of two large, privately held companies in the Formula Group. Ms. Salomon holds a BA in economics and business administration from Ben Gurion University and an LL.M. from the Bar-Ilan University.

Yacov Elinav has served as a director of the Company since March 2005. For over 30 years, Mr. Elinav served in various positions at Bank Hapoalim B.M., which is listed on the London and Tel Aviv Stock Exchanges, including over 10 years as a member of the Board of Management, responsible for subsidiary and related companies. From 1992 through 2006, Mr. Elinav served as Chairman of the Board of Directors of Diur B.P. Ltd., the real estate subsidiary of Bank Hapoalim. Since August 2004, Mr. Elinav has served as Chairman of the Boards of Directors of DS Securities and Investments, Ltd. and DS Provident Funds Ltd. Mr. Elinav also serves on the Board of Directors of several other public and private companies.

Uzi Netanel has served as a director of the Company since March 2005. He has served as Chairman of the Board of Directors of Maccabi Group Holdings Ltd. since 2005, as Chairman of the Board of Directors of MLL Software & Computers Industries Ltd. since 2004 and as Chairman of the Executive Committee of Carmel Olephines since 2004. From 2001 through 2003, Mr. Netanel served as a partner in the FIMI Opportunity Fund. From 1993 through 2001, he served as Active Chairman of Israel Discount Capital Markets and Investments Ltd. From 1997 to 1999, Mr. Netanel served as Chairman of Poliziv Plastics Company (1998) Ltd. Mr. Netanel also serves on the Board of Directors of Israel Oil Refineries, Frutarom Industries and Caeserea-Vardinon Textiles.

Ido Schechter has served as a director of the Company since June 2006. He has served as the Chief Executive Officer of Top Image Systems Ltd. ("TIS") since January 2002 and has been a director of TIS since December 2004. From January 2001 until he became CEO, Dr. Schechter was Vice President of TIS' ASP, an initiative of TIS to offer data collection services via the Internet. Prior to that Dr. Schechter served as TIS's Vice President of Sales from August 1996 until January 2001. From January 1995 until August 1996, Dr. Schechter served as General Manager of Super Image, a former affiliate of TIS, which operated a form processing service bureau. From August 1993 to December 1994, Dr. Schechter oversaw the start-up of automatic form processing services at Israel Credit Cards, Ltd. From 1991 to 1993, Dr. Schechter was a research scientist at the Horticultural Research Institute of Ontario, Canada. Dr. Schechter received his Ph.D. and M.Sc. in Plant Physiology from the University of Guelph in Ontario, Canada and his BS from the Hebrew University in Israel.

Ron Zuckerman has served as a director of the Company since May 1991 and served as Chairman of the Board of Directors from January 1998 until December 2006. He served as Chief Executive Officer of the Company from January 1995 until March 31, 2000. Mr. Zuckerman served as Chief Operating Officer of the Company from its incorporation until April 1994. Mr. Zuckerman was a founder and served as Chairman of Precise Software Solutions Ltd. until it was acquired by Veritas in June 2003 and serves as a director of Attunity Ltd. and Tamir Fishman Ventures Ltd. Mr. Zuckerman serves as an advisor to Magnum Communications Fund and the First Israeli Turnaround Fund.

United International Trust N.V. (“UIT”) is a corporate body organized and existing under the laws of the Netherlands Antilles. It, or one of its predecessor entities, has provided the Company with corporate-related services since April 1990, including serving as the Company’s transfer agent and register, maintaining the corporate-related records of the Company, and filing various corporate documents and the annual corporate tax return with the governmental authorities in the Netherlands Antilles. UIT was established by former shareholders of Intertrust (Curaçao) N.V., which subsequently operated under the names of MeesPierson Intertrust (Curaçao) N.V. and Fortis Intertrust (Curaçao) N.V.

Hadas Gazit Kaiser shall serve as a director of the Company beginning July 1, 2007. She has served as the Chief Financial Officer and Finance Director of Emblaze since December 2006. From August 2005 until she became CFO, Ms. Gazit Kaiser served as the Vice President-Finance of Emblaze and the Chief Financial Officer of Emblaze Mobile. From August 2003 to August 2005, Ms. Gazit Kaiser served as the Budget Control Manager of TTI. From August 2000 to August 2003, Ms. Gazit Kaiser acted as a manager at Kost, Forer Gabbay & Kasierer. Ms. Gazit Kaiser holds a BA in Economics and Accounting and an MBA degree in Finance, both from Tel Aviv University, and is a Certified Public Accountant in Israel.

The Board of Directors must have a minimum of three, and a maximum of 24, directors. Directors of the Company are appointed by the General Meeting of Shareholders and hold office until they resign or are suspended or dismissed by the General Meeting of Shareholders. The Board of Directors may appoint up to four additional directors, and any such appointment shall be effective until the next General Meeting of Shareholders. The Board of Directors may fill any vacancies on the Board of Directors, whether as a result of the resignation or dismissal of a director, or as a result of a decision of the Board of Directors to expand the Board of Directors.

Our executive officers are appointed by, and serve at the discretion of, the Board of Directors of the Company.

There are no family relationships among the executive officers or directors of the Company.

B. Compensation of Directors and Officers

The aggregate amount of compensation paid by the Company during the fiscal year ended December 31, 2006, to all directors and executive officers as a group for services in all capacities was \$529,000. This amount does not include amounts expended by the Company for automobiles made available to its officers or expenses (including business travel and professional and business association dues) reimbursed to such officers. The aggregate amount set aside or accrued by the Company during its fiscal year ended December 31, 2006, to provide pension, retirement severance and similar benefits for directors and executive officers of the Company was \$55,000. The foregoing amounts also exclude stock option grants to the Company’s directors and officers pursuant to the Company’s 1992 Stock Option and Incentive Plan, the Company’s 2003 Share Option Plan and the Company’s 2005 Special Incentive Share Option Plan, which are described below.

The Company has employment agreements with its officers. The Company, in the ordinary course of its business, enters into confidentiality agreements with its personnel and has entered into non-competition and confidentiality agreements with its officers and high-level technical personnel. The Company does not maintain key person life insurance on any of its executive officers.

Board Fees and Expenses

The Company reimburses all Board of Directors members for reasonable out-of-pocket expenses incurred in connection with their attendance at Board of Directors or committee meetings.

The Company grants to each of its independent directors a fee for attending or participating in Board of Directors meetings and committee meetings, and participating in unanimous written consents.

In the past, the Company has granted to each of its independent directors options to purchase 4,000 Common Shares annually. The options were granted at an exercise price equal to the fair market value of the Company's Common Shares on the date of grant. The term of the options is 10 years and the options become exercisable in four equal, annual installments, beginning with the first anniversary of the grant date. In 2005 and 2006, the Company did not grant any options to its independent directors.

The Company has no current intent or plan to change its compensation arrangements with respect to directors for serving on the Board of Directors.

Stock Option and Incentive Plan

In 1992, our Board of Directors and shareholders approved the 1992 Stock Option and Incentive Plan (the "1992 Stock Plan") pursuant to which our officers, directors and employees are eligible to receive awards of stock options and restricted stock. In February 2003, the Board of Directors authorized the extension of the 1992 Stock Plan until April 2012 and our shareholders approved that extension. In 2003, our Board of Directors and shareholders approved the 2003 Share Option Plan (the "2003 Option Plan"), pursuant to which our officers, directors, employees, consultants and contractors are eligible to receive awards of stock options. In the following description, the 1992 Stock Plan and 2003 Option Plan will be referred to together as the "Incentive Plans" and may be referred to individually as an "Incentive Plan."

Options granted under the 1992 Stock Plan may be "incentive stock options" ("ISOs"), within the meaning of section 422 of the Internal Revenue Code of 1986, as amended (the "Code"), or non-qualified stock options ("non-Qualified Stock Options"). Restricted stock may be granted in addition to or in lieu of any other award granted under the 1992 Stock Plan. Option grants under the 2003 Option Plan are intended to comply with, and benefit from, applicable tax laws and regulations in Israel.

Each of the Incentive Plans is administered by the compensation committee (the "Committee") established by the Board of Directors. Subject to the provisions of each Incentive Plan, the Committee determines the type of award, when and to whom awards will be granted and the number of shares covered by each award. The Committee also determines the terms, provisions, and kind of consideration payable (if any), with respect to awards. The Committee has discretionary authority to interpret the Incentive Plans and to adopt rules and regulations related thereto. In determining the persons to whom awards shall be granted and the number of shares covered by each award, the Committee takes into account the contribution to the management, growth and/or profitability of the business of the Company by the respective persons and such factors as the Committee shall deem relevant, including the length of employment of the respective persons, the nature of their responsibilities to the Company, and their flexibility with regard to location of their employment and other employment-related factors.

An option may be granted on such terms and conditions as the Committee may approve, and generally may be exercised for a period of up to 10 years from the date of grant. Options granted under the Incentive Plans become exercisable in four equal, annual installments, beginning with the first anniversary of the date of the grant, or pursuant to such other schedule as the Committee may provide in the option agreement. The exercise price of such options generally will be not less than 100% of the fair market value per share of the Common Shares at the date of the grant. In the case of ISOs, certain limitations will apply with respect to the aggregate value of option shares which can become exercisable for the first time during any one calendar year, and certain additional limitations will apply to "Ten Percent Stockholders" (as defined in the 1992 Stock Plan). The Committee may provide for the payment of the option price in cash, by delivery of other Common Shares having a fair market value equal to such option exercise price, by a combination thereof or by any method in accordance with the terms of the option agreements. The Incentive Plans contain special rules governing the time of exercise of options in the case of death, disability, or other termination of employment. Options are not transferable except by will or pursuant to applicable laws of descent and distribution upon death of the employee.

The 1992 Stock Plan also provides for the granting of restricted stock awards, which are awards of Common Shares that may not be disposed of, except by will or the laws of descent and distribution, for such period as the Committee determines (the "restricted period"). The Committee may also impose such other conditions and restrictions on the shares as it deems appropriate, including the satisfaction of performance criteria. The Committee may provide that such restrictions will lapse with respect to specified percentages of the awarded shares on successive anniversaries of the date of the award. During the restricted period, the grantee is entitled to receive dividends with respect to, and to vote the shares awarded to him or her. If, during the restricted period, the grantee's continuous employment with the Company terminates for any reason, any shares remaining subject to restrictions will be forfeited. The Committee has the authority to cancel any or all outstanding restrictions prior to the end of the restricted period, including cancellation of restrictions in connection with certain types of termination of employment.

As of December 31, 2006, we had 1,310,686 Common Shares available for future issuance of awards under the Incentive Plans. As of December 31, 2006, options to purchase 2,441,050 Common Shares, 1,510,000 of which were held by officers and directors, were outstanding. As of that date, there were 22,280 shares of restricted stock that the Company had granted to employees and other eligible grantees (none of which were held by current and former officers and directors), and all of which had vested (prior to 1998) under the restricted stock awards.

In 2005, the Company's Board of Directors authorized a new Incentive Stock Option Plan (the "Special Plan") and our shareholders approved the Special Plan in 2006. The number of Common Shares available for grants pursuant to the Special Plan was set at 2,000,000 shares. The Special Plan is intended to be used solely to attract or retain senior management and/or members of the Board of Directors. Unless otherwise determined by the Committee, options granted pursuant to the Special Plan will have an exercise price of \$3.00 per share, shares issued upon exercise will be locked for up to five years following the grant date, and the right to obtain shares will be contingent upon the optionee providing services to the Company throughout the entire five year period. In the event of a change of control of the Company, any unvested options will be accelerated.

The Special Plan is administered by the Committee. Subject to the provisions of the Special Plan, the Committee determines the type of award, when and to whom awards will be granted and the number of shares covered by each award. The Committee also determines the terms and provisions with respect to awards. The Committee has discretionary authority to interpret the Special Plan and to adopt rules and regulations related thereto.

Pursuant to the Special Plan, in November 2005 the Company's President and Chief Executive Officer was granted options to purchase 1,000,000 Common Shares. In December 2005, as a result of the issuance of SFAS No. 123(R), we accelerated the vesting of all 1,000,000 options. In 2007, the Company's Chief Operating Officer was granted options to purchase 250,000 Common Shares, pursuant to the Special Plan.

C. Board Practices

Members of the Company's Board of Directors are elected by a vote at the annual general meeting of shareholders and serve for a term of one year. Directors may serve multiple terms and are elected by a majority of the votes cast at the meeting. The Chief Executive Officer serves until his removal by the Board of Directors or resignation from office. Non-employee directors do not have agreements with the Company for benefits upon termination of their service as directors.

Audit Committee

The Audit Committee of the Board of Directors is comprised of three independent directors, nominated by the Board of Directors: Yacov Elinav, Uzi Netanel and Dr. Ido Schechter. The Board of Directors has determined that Mr. Elinav meets the definition of an audit committee financial expert. The primary function of the Audit Committee is to assist the Board of Directors in fulfilling its oversight responsibilities by reviewing financial information, internal controls and the audit process. In addition, the Committee is responsible for oversight of the work of our independent auditors. The Committee is governed by a Charter and meets at regularly scheduled quarterly meetings.

Compensation Committee

The Compensation Committee of the Board of Directors is comprised of three directors, nominated by the Board of Directors: Gad Goldstein, Dr. Ido Schechter and Guy Bernstein. Dr. Schechter is an independent director. On January 1, 2007, Mr. Guy Bernstein replaced Mr. Zuckerman as a member of the Compensation Committee. The primary function of the Compensation Committee is to manage the Company's Stock Option Plan and review and approve all matters relating to the compensation of the Company's officers and directors. The Committee is governed by a Charter and meets at regularly scheduled quarterly meetings.

NASDAQ Exemptions for a Controlled Company

We are a controlled company within the meaning of NASDAQ Marketplace Rule 4350(c)(5), or Rule 4350(c)(5), since Formula holds more than 50% of our voting power.

Under Rule 4350(c)(5), a controlled company is exempt from the following requirements of NASDAQ Marketplace Rule 4350(c) as of July 31, 2005:

- The majority of the company's board of directors must qualify as independent directors, as defined under NASDAQ Marketplace Rules; and
- The compensation of the chief financial officer and all other executive officers must be determined, or recommended to the board of directors for determination, either by (i) a majority of the independent directors or (ii) a compensation committee comprised solely of independent directors. Director nominees must either be selected or recommended for the board of directors' selection, either by (a) a majority of independent directors or (b) a nominations committee comprised solely of independent directors.

NASDAQ Exemption for a Foreign Private Issuer

We are a foreign private issuer within the meaning of NASDAQ Marketplace Rule 4350(a), since we are incorporated in the Netherlands Antilles.

Pursuant to NASDAQ Marketplace Rule 4350(a), a foreign private issuer may follow a home country practice in lieu of one or more provisions of Rule 4350.

We have elected to follow our home country practice in lieu of the requirements set forth in NASDAQ Marketplace Rule 4350(b)(1)(A) which requires a company to distribute to its shareholders copies of an annual report containing its audited financial statements. Instead of distributing copies of our annual report by mail, we have made our annual report available to shareholders on our website (http://www.sapiens.com/en/investors/annual_reports/).

We have also submitted to NASDAQ a written statement from our independent Netherlands Antilles counsel which certified that our practice of not mailing the annual report, but rather making it available on our website, was not prohibited by Netherlands Antilles law.

D. Employees

As of December 31, 2006, we had a total of 319 employees, a 12.4% decrease from the end of 2005.

In February 2006, we began to implement a restructuring plan for the purpose of reducing costs and restoring profitability. The restructuring plan included the termination of the employment of approximately 25 employees.

The following table sets forth the number of employees in (1) research and development, (2) consulting, delivery and technical support and (3) SG&A at the end of each of the past three years, as well as their geographic area of employment:

	<u>Total Employees</u>	<u>Research & Development</u>	<u>Consulting, Delivery & Technical Support</u>	<u>SG&A</u>
2006	319	53	217	49
2005	364	52	235	77
2004	405	57	252	96

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Israel	198	218	214
United States	43	50	54
United Kingdom	49	52	82
Japan	23	24	24
France	4	15	25
Germany	1	5	5
Switzerland	1	-	1
Total Employees	319	364	405

E. Share Ownership

	Shares Beneficially Owned	
	Number	Percent (1)
Eli Reifman (2)	11,163,131	53.8
Gad Goldstein (3)	11,163,131	53.8
Ron Zuckerman (4)	289,700	1.4
Roni Al Dor (5)	240,000	*
All directors and executive officers as a group (12 persons) (6)	11,850,831	56.0

* less than 1.0%

- (1) Unless otherwise indicated below, the persons in the above table have sole voting and investment power with respect to all shares shown as beneficially owned by them. The percentages shown are based on 20,678,187 Common Shares outstanding as of June 27, 2007 plus such number of Common Shares as the indicated person or group had the right to receive upon the exercise of options which are exercisable within 60 days of June 27, 2007.
- (2) Includes 11,088,594 Common Shares and NIS 2,012,500 par value of our debentures (convertible into 74,537 Common Shares) held by Formula. Emblaze beneficially owns 50.1% of the outstanding share capital of Formula. Messrs. Naftali Shani and Eli Reifman, directors of Emblaze, hold 13.8% and 8.6% of the outstanding share capital of Emblaze, respectively. Eli Reifman is a director and President of Emblaze and may be deemed to share with Emblaze the power to vote and dispose of our Common Shares beneficially owned by Formula. Eli Reifman disclaims beneficial ownership of the Common Shares beneficially owned by Formula. See Item 7, "Major Shareholders and Related Party Transactions – Major Shareholders."
- (3) Includes 11,088,594 Common Shares and NIS 2,012,500 par value of our debentures (convertible into 74,537 Common Shares) held by Formula. Gad Goldstein, President and director of Formula, disclaims beneficial ownership of these shares. See Item 7, "Major Shareholders and Related Party Transactions – Major Shareholders."
- (4) Includes (i) 97,700 Common Shares held by Lako Enterprises S.A. ("Lako") as to which Mr. Zuckerman disclaims beneficial ownership (see below); (ii) 140,000 Common Shares held by Meister Software N.V. ("Meister"), a Netherlands Antilles corporation, which shares may be deemed to be beneficially owned by Mr. Zuckerman (see below); (iii) 24,000 Common Shares held of record by Mr. Zuckerman; and (iv) options to purchase 28,000 Common Shares held by Lako as to which Mr. Zuckerman disclaims beneficial ownership. 14,000 of the options have an exercise price of \$0.005 and 14,000 have an exercise price of \$32.50 per share, and all 28,000 expire in October 2008. A trust (the Bornali Foundation) for the benefit of the estate of Mr. Zuckerman owns all the outstanding voting shares of Lako. Mr. Zuckerman disclaims beneficial ownership of the Common Shares held by Lako.

Lako owns 97,700 Common Shares of the Company and 50% of the voting shares of Century Holdings, Inc., a Panamanian corporation ("Century"). Century owns approximately 33% of the voting stock of Meister. By virtue of Lako's ownership of Century, Mr. Zuckerman may be deemed to have ownership of Century and thus may be deemed to beneficially own all of the Common Shares held by Meister.
- (5) Includes options to purchase 240,000 Common Shares at an exercise price of \$1.74 per share which expire in November 2015. Does not include the option to purchase 1,000,000 Common Shares granted pursuant to the Special Plan, which expire in November 2015. See Item 6, "Directors, Senior Management and Employees - Compensation of Directors and Officers."
- (6) Each of the directors and executive officers not separately identified in the above table beneficially own less than 1% of our outstanding Common Shares (including options held by each such party and which are vested or will become vested within 60 days of June 27, 2007) and have therefore not been separately disclosed. The options held by the directors and executive officers not separately identified in the above table have exercise prices ranging from \$1.50 to \$2.24 per share, and none of which expire before 2015.

ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. Major Shareholders

The following table sets forth, as of June 27, 2007, certain information with respect to the beneficial ownership of the Company's Common Shares by each person known by the Company to own beneficially more than 5% of the outstanding Common Shares, based on information provided to us by the holders or disclosed in public filings with the Securities and Exchange Commission.

Name and Address	Shares Beneficially Owned	
	Number	Percent (1)
Formula Systems (1985) Ltd. (2) 3 Abba Eban Boulevard Herzlia 46725, Israel	11,163,131	53.8
Highbridge International LLC c/o Harmonic Fund Services The Cayman Corporate Centre, 4th Floor 27 Hospital Road Grand Cayman Cayman Islands, British West Indies	2,166,667	10.5
Magnum Technology Limited (3) c/o Rothschild Corporate Fiduciary Services Limited St. Peter's House, Le Bordage St. Peter's Port, Guernsey, Channel Islands	1,204,819	5.8
F.I.D. Holdings Ltd. (4) Rubinstein House, Floor 29 37 Petach Tikva Road Tel Aviv 67137, Israel	2,193,750	10.3

- (1) The percentages shown are based on 20,678,187 Common Shares outstanding as of June 27, 2007 plus such number of Common Shares as the indicated person or group had the right to receive upon the exercise of options which are exercisable within 60 days of June 27, 2007.
- (2) Includes 11,088,594 Common Shares and NIS 2,012,500 par value of our debentures (convertible into 74,537 Common Shares). Emblaze beneficially owns 50.1% of the outstanding share capital of Formula. Messrs. Naftali Shani and Eli Reifman, directors of Emblaze, hold 13.8% and 8.6% of the outstanding share capital of Emblaze, respectively. Gad Goldstein is a director and President of Formula but holds no outstanding shares of Formula. Gad Goldstein may be deemed to share with Formula the power to vote and dispose of our Common Shares beneficially owned by Formula. Gad Goldstein disclaims beneficial ownership of the Common Shares beneficially owned by Formula.
- (3) Yarnfield International Limited ("Yarnfield"), which acquired the shares in 2001, has since been liquidated and our Common Shares held by Yarnfield were transferred to Magnum Technology Limited (the parent company of Yarnfield).
- (4) Includes (i) 1,531,250 Common Shares, (ii) warrants to purchase 350,000 Common Shares and (iii) 312,500 Common Shares issuable upon conversion of the \$1.0 million loan due August 1, 2007.

Significant changes in holdings of major shareholders

1. Formula

In June 2005, we entered into a share purchase agreement with Formula, whereby Formula invested \$2.0 million in the Company and we issued 1,041,667 Common Shares to Formula at a purchase price per share of \$1.92, which was the average closing price for the 10 day period prior to the execution of the agreement. As a result of the \$2.0 million investment in June 2005, Formula became the holder of approximately 58% of our outstanding Common Shares at that time.

In August 2006, we entered into a share issuance agreement with Formula whereby Formula invested \$2.0 million in the Company, and we issued 1,562,500 Common Shares to Formula, at a purchase price per share of \$1.28, which was the average closing price for the 10 day period prior to July 17, 2006, and which was the same as the conversion price approved by the debentures holders at the August 2006 meeting. As a result of the \$2.0 million investment in August 2006, Formula became the holder of approximately 60% of our outstanding Common Shares at that time.

From time to time, Formula has increased its beneficial shareholding in the Company through market purchases of additional Common Shares. From June 25, 2006 through June 28, 2007, Formula increased its holding of our Common Shares by approximately 198,240 Common Shares through purchases on the public market.

In June 2007, we entered into a private placement investment transaction with several institutional investors, private investors and Formula for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). As of June 27, 2007, we have held closings for \$17.5 million of the investment, \$5 million of which was by Formula. As a result, we issued to Formula 1,666,667 Common Shares, at a price per share of \$3.00 which reflected a premium of approximately 25% above the trading price of our Common Shares (as of the date our Board of Directors approved the investment). The closing for the remaining \$2.5 million, for an aggregate of 833,333 Common Shares, is expected by June 30, 2007.

As of June 27, 2007, Formula was the holder of approximately 53% of our outstanding Common Shares.

In November 2006, Emblaze purchased the controlling interest of Formula, and as a result, control of us. As of June 24, 2007, Emblaze owned 50.1% of the outstanding share capital of Formula and, therefore, has an indirect controlling influence over us.

(For further details about the transactions with Formula, see Item 10, "Additional Information – Material Contracts.")

2. FID and Israel Discount Bank

As a result of the agreement entered into as of March 16, 2004 among the Company and the Investors, FID became the beneficial holder of approximately 9.1% of the Company's share capital.

In May 2005, we entered into an agreement with the Investors, regarding the payment of the remaining \$4.0 million due to the Investors, pursuant to the March 2004 agreement between us and the Investors. We agreed to pay \$2.0 million on May 2, 2005, \$1.0 million by April 1, 2006 and \$1.0 million by August 1, 2006. The first installment of \$2.0 million was paid as required at the beginning of May 2005.

In August 2006, we entered into an agreement with the Investors whereby the Investors converted the \$1.0 million payment that was due on April 1, 2006 into 781,250 Common Shares and the \$1.0 million payment that was due on August 1, 2006 was delayed to August 1, 2007. The Investors may, at their sole discretion, convert all or any portion of the \$1.0 million payment now payable on August 1, 2007 into our Common Shares, at a conversion price per each share of \$3.20.

(For further details about the transactions with the Investors, see Item 10, "Additional Information – Material Contracts – Agreements with FID and Israel Discount Bank Ltd.")

3. Highbridge International LLC

In June 2007, we entered into a private placement investment transaction with several institutional investors, private investors and Formula for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). Pursuant to such private placement investment, Highbridge International LLC invested \$6.5 million in the Company in return for the issuance of 2,166,667 Common Shares, which equaled 10.5% of our outstanding Common Shares.

The major shareholders disclosed above do not have different voting rights.

As of June 14, 2007, there were 176 holders of record of the Company's Common Shares, including 125 holders of record with addresses in the United States. The number of record holders in the United States is not representative of the number of beneficial holders, nor is it representative of where such beneficial holders are resident because many of these ordinary shares were held of record by brokers or other nominees.

Based on Formula's beneficial holding of over 50% of the outstanding Common Shares of the Company, and based on Emblaze's beneficial holding of over 50% of the outstanding share capital of Formula, both Formula and Emblaze may be considered to control the Company.

B. Related Party Transactions

Red Coral

On April 4, 2001, we entered into a share purchase and loan agreement with Red Coral Holdings, Inc. ("Red Coral"), a company owned by Itzick Sharir, then our President and Chief Executive Officer. According to the terms of the agreement, Red Coral purchased 300,000 Common Shares for a purchase price of \$975,000. As part of the agreement, the Company granted to Red Coral a loan in the amount of \$975,000 for the purpose of acquiring the Common Shares. The term of the loan was six years, with accrued interest at a rate of 4% per year. The interest amount was initially fully-recourse and fixed. To secure payment of the loan, Red Coral granted to the Company a lien and security interest on all of the Common Shares of the Company that it owns. To secure fulfillment of the terms of the agreement, the Common Shares were held in escrow by the General Counsel of the Company.

Following the departure of Mr. Sharir, we postponed the due date of the January 15, 2006 and the January 15, 2007 interest payments until the due date for repayment of the principal amount of the loan (April 4, 2007), and converted the final two interest payments from fully-recourse to non-recourse. The remaining terms of the loan were not changed.

On April 4, 2007, the term of the loan expired, without Red Coral having repaid the principal amount or the final two interest payments. In May 2007, we foreclosed our lien on the 300,000 Common Shares owned by Red Coral, and we now hold such shares as treasury shares. As a result, the loan agreement was terminated and Red Coral has no further obligations to us under the loan agreement.

In November 2005, upon the termination of his employment with the Company, Mr. Sharir was granted options to purchase 50,000 Common Shares at a price \$1.74 per share, which expire in November 2008.

FID and Israel Discount Bank

As a result of the agreement entered into as of March 16, 2004 among the Company and the Investors, FID became the beneficial holder of approximately 9.1% of the Company's share capital.

In May 2005, we entered into an agreement with the Investors regarding the payment of the remaining \$4.0 million due to the Investors, pursuant to the March 2004 agreement between us and the Investors. We agreed to pay \$2.0 million on May 2, 2005, \$1.0 million by April 1, 2006 and \$1.0 million by August 1, 2006. The first installment of \$2.0 million was paid as required at the beginning of May 2005.

In August 2006, we entered into an agreement with the Investors whereby the Investors converted the \$1.0 million payment that was due on April 1, 2006 into 781,250 Common Shares and the \$1.0 million payment that was due on August 1, 2006 was delayed to August 1, 2007. The Investors may, at their sole discretion, convert all or any portion of the \$1.0 million payment now payable on August 1, 2007 into Common Shares, at a conversion price per each share of \$3.20.

(For further details about the transactions with the Investors, see Item 10, "Additional Information – Material Contracts – Agreements with FID and Israel Discount Bank Ltd.")

Formula

In June 2005, we entered into a share purchase agreement with our major shareholder, Formula, whereby Formula invested \$2.0 million in the Company, and we issued 1,041,667 Common Shares to Formula, at a purchase price per share of \$1.92, which was the average closing price for the 10 day period prior to the execution of the agreement. The Common Shares issued pursuant to the June 2005 agreement were granted "piggyback" registration rights, similar to those granted to Formula and Yarnfield International Limited (now Magnum Technology Limited) in their 2001 investment.

In August 2006, we entered into a share issuance agreement with Formula whereby Formula invested \$2.0 million in the Company, and we issued 1,562,500 Common Shares to Formula, at a purchase price per share of \$1.28, which was the average closing price for the 10 day period prior to July 17, 2006, and which was the same as the conversion price approved by the debentures holders at the August 2006 meeting. As a result of the \$2.0 million investment in August 2006, Formula became the holder of approximately 60% of our outstanding Common Shares at that time.

In December 2006, we entered into a loan agreement with Bank Leumi Le-Israel whereby we borrowed an aggregate amount of approximately \$2.5 million. The proceeds of the loan enabled us to make the December 2006 principal and interest payment on the debentures. The loan was secured by a pledged deposit of Formula. The loan bears an annual interest rate equal to the prime rate of interest in Israel plus 0.5% (for a total of 6.5%) and the principal and interest are due on August 30, 2007.

In June 2007, we entered into a private placement investment transaction with several institutional investors, private investors and Formula for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). As of June 27, 2007, we have held closings for \$17.5 million of the investment, \$5 million of which was by Formula. As a result, we issued to Formula an aggregate of 1,666,667 Common Shares, at a price per share of \$3.00. Following the initial closing of the \$17.5 million investment, Formula's holdings were reduced to approximately 53% of our outstanding Common Shares. The closing for the remaining \$2.5 million, for an aggregate of 833,333 Common Shares, is expected by June 30, 2007.

(For further details about the transactions with Formula, see Item 10, "Additional Information – Material Contracts.")

C. Interests of Experts and Counsel

Not applicable.

ITEM 8. FINANCIAL INFORMATION

A. Consolidated Statements and Other Financial Information

Financial Statements

See the Consolidated Financial Statements and related notes in Item 18.

Export Sales

In 2006, 72.8% of our revenues were from customers located outside of Israel. For information on our revenues breakdown by geographic market for the past three years, see Item 4, "Information on the Company – Business Overview - Geographical Distribution of Revenues."

Dividend Policy

We have never declared or paid any cash dividends on our Common Shares and we do not anticipate paying cash dividends in the foreseeable future. It is the present intention of our Board of Directors to retain all earnings in the Company in order to support the future growth of its business. Any determination in the future to pay dividends will be dependent upon our consolidated results of operations, financial condition, cash requirements, future prospects and other factors. For more information about distribution of dividends and various tax implications, see Item 10, "Additional Information - Memorandum and Articles of Association;" Item 10, "Additional Information – Exchange Controls," and Item 10, "Additional Information – Taxation."

Legal Proceedings

The Company is subject to certain legal and governmental proceedings and claims that arise in the conduct of its business. In the opinion of management, the amount of liability, if any, as a result of these claims and proceedings is not likely to have a material effect on the financial condition or results of operations of the Company.

B. Significant Changes

The following significant changes have occurred since the date of our annual consolidated financial statements:

In June 2007, we entered into a private placement investment transaction with several institutional investors, private investors and Formula for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). As of June 27, 2007, we have held closings for \$17.5 million of the investment, \$5 million of which was by Formula. We issued to the investors an aggregate of 5,833,333 Common Shares (of which 1,666,667 Common Shares were issued to Formula), at a price per share of \$3.00 which reflected a premium of approximately 25% above the trading price of our Common Shares (as of the date our Board of Directors approved the investment). The closing for the remaining \$2.5 million, for an aggregate of 833,333 Common Shares, is expected by June 30, 2007. The investors were all non-US persons, and the Common Shares were issued to the investors pursuant to Regulation S. As a result, the issuance of the Common Shares to the investors was exempt from registration under the Securities Act.

In June 2007, we purchased an aggregate amount of NIS 15,000,000 nominal value, representing approximately, \$3.5 million of the outstanding debentures. Pursuant to the terms of the prospectus governing the debentures, the amount repurchased by us was retired and removed from circulation. As a result, the total amount that we must pay in December 2007 was reduced to approximately \$4.6 million, approximately \$4.2 million for the second of the four annual re-payments of the principal of the debentures, and approximately \$0.4 million for the semi-annual interest payment.

On June 27, 2006, we entered into agreements for a new revolving credit line facility for borrowings of up to \$9.2 million, until June 30, 2007. We are currently negotiating the extension of the credit facility for another year. We cannot be certain that an agreement will be signed, though we expect that an agreement will be signed that extends the current credit line, on substantially similar terms, for an additional year.

(See also Item 5, "Operating and Financial Review and Prospects - Liquidity and Capital Resources – Credit Lines.")

ITEM 9. THE OFFER AND LISTING**A. Offer and Listing Details**

The Company's Common Shares are quoted on the NASDAQ Capital Market and on the TASE under the symbol "SPNS".

The table below sets forth the high and low market prices for our Common Shares on the NASDAQ National Market (now known as the NASDAQ Global Market) until September 27, 2005 and the NASDAQ Capital Market thereafter on an annual basis for the years 2002 through 2006 and on a quarterly basis for the years 2005 and 2006, and the first quarter of 2007. On June 16, 2003, the Company carried out the Reverse Stock Split (see Note under Item 3.A "Selected Consolidated Financial Data"). All share prices have been adjusted to reflect the Reverse Stock Split by multiplying historical prices by five.

	<u>HIGH</u>	<u>LOW</u>
2002 (Annual)	\$6.85	\$3.00
2003 (Annual)	6.01	3.30
2004 (Annual)	5.25	1.48
2005 (Annual)	2.89	1.00
2006 (Annual)	2.10	1.02
2007 (Annual) (through June 25, 2007)	3.66	1.35
2005		
First Quarter	\$2.89	\$1.85
Second Quarter	2.41	1.52
Third Quarter	2.09	1.30
Fourth Quarter	1.86	1.00
2006		
First Quarter	\$1.60	\$1.14
Second Quarter	1.54	1.06
Third Quarter	2.10	1.09
Fourth Quarter	1.57	1.02
2007		
First Quarter	\$2.00	\$1.35
Second Quarter (through June 25, 2007)	3.66	1.51

The table below sets forth the high and low market prices for our Common Shares on the NASDAQ Capital Market during the most recent six-month period:

	<u>HIGH</u>	<u>LOW</u>
December 2006	\$1.55	\$1.22
January 2007	2.00	1.35
February 2007	1.95	1.52
March 2007	1.74	1.52
April 2007	2.24	1.51
May 2007	2.95	1.56
June 2007 (through June 25, 2007)	3.66	2.21

Our Common Shares began trading on the TASE effective March 6, 2003. Under current Israeli law, the Company will satisfy its reporting obligations in Israel by furnishing to the applicable Israeli regulators only those reports the Company is required to file in the United States. The table below sets forth the high and low market prices for our Common Shares on TASE on an annual basis for the years 2003 through 2006 and on a quarterly basis for the years 2005 and 2006, and the first quarter of 2007. The conversion from NIS into US dollars for the following two tables is based on the average monthly representative rate of exchange published by the Bank of Israel then in effect for the month in which such high or low was recorded, except for the month of June 2007 where the conversion is based on the representative rate of exchange as published by the Bank of Israel for the specific date recorded.

	<u>HIGH</u>	<u>LOW</u>
2003 (Annual from March 6)	\$6.01	\$3.56
2004 (Annual)	5.29	1.75
2005 (Annual)	2.74	1.19
2006 (Annual)	1.57	1.14
2007 (Annual) (through June 25, 2007)	3.82	1.42
2003		
Second Quarter	\$4.99	\$4.33
Third Quarter	5.06	3.58
Fourth Quarter	6.01	3.56
2004		
First Quarter	\$5.29	\$3.62
Second Quarter	3.64	2.28
Third Quarter	2.54	1.75
Fourth Quarter	2.42	1.85
2005		
First Quarter	\$2.74	\$2.06
Second Quarter	2.28	1.76
Third Quarter	2.03	1.55
Fourth Quarter	1.73	1.19
2006		
First Quarter	\$1.57	\$1.24
Second Quarter	1.42	1.23
Third Quarter	1.37	1.14
Fourth Quarter	1.48	1.19
2007		
First Quarter	\$1.83	\$1.42
Second Quarter (through June 25, 2007)	3.82	1.50

The table below sets forth the high and low market prices for our Common Shares on TASE during the most recent six-month period:

	<u>HIGH</u>	<u>LOW</u>
December 2006	\$1.48	\$1.40
January 2007	1.82	1.42
February 2007	1.83	1.54
March 2007	1.76	1.76
April 2007	1.72	1.70
May 2007	1.99	1.50
June 2007 (through June 25, 2007)	3.82	2.36

On June 24, 2007, we received a letter from the TASE informing us that as of August 12, 2007, our Common Shares and warrants (Series 1) that are traded on the TASE, but not our debentures (Series A), will be included in a newly created list of "Illiquid Securities". As a result, trades on the TASE of our Common Shares and warrants (Series 1) will only be executed twice a day, in the morning upon the commencement of trading, and at the end of day, at the end of trading. At this time we cannot be certain as to the effects, if any, that such listing change on the TASE will have on our Common Shares and warrants (Series 1), however, we do not believe such inclusion as an "Illiquid Security" on the TASE will have a material effect on our financial condition.

B. Plan of Distribution

Not applicable.

C. Markets

The Company's Common Shares are quoted on the NASDAQ Capital Market and on the TASE under the symbol "SPNS".

D. Selling Shareholders

Not applicable.

E. Dilution

Not applicable.

F. Expenses of the Issue

Not applicable.

ITEM 10. ADDITIONAL INFORMATION

A. Share Capital

Not applicable.

B. Memorandum and Articles of Association (the “Articles”)

1. Registration and Purposes. The Company is organized and existing under the laws of the Netherlands Antilles. Its registered number is 53368.

The objects and purposes of the Company, which are itemized in Article II of the Articles, may be summarized as follows:

- to establish, participate in or have any other interest in business enterprises concerned with the development and commercial operation of software;
- to finance directly or indirectly the activities of the Company, its subsidiaries and affiliates;
- to borrow and to lend moneys;
- to engage in the purchase and sale of securities, futures, real estate, business debts, commodities and intellectual property;
- to undertake, conduct and promote research and development;
- to guarantee, pledge, mortgage or otherwise encumber assets as security for the obligations of the Company or third parties; and
- to do all that may be useful or necessary for the attainment of the above purposes.

2. Board of Directors. A member of the Board of Directors may vote on a proposal or transaction in which he/she has a material interest if the material facts as to the director’s self-interest are disclosed to the Board of Directors. Neither the Articles nor Netherlands Antilles law requires a majority of the disinterested directors to authorize the proposal or transaction. Members of the Board of Directors have the power to vote compensation to themselves, even if they lack an independent quorum.

The Articles do not grant borrowing powers to directors; nor do they require directors to resign at a certain age or to purchase a certain number of shares of the Company’s common stock.

3. Rights and Preferences. The Company has only one class of shares of common stock, the Common Shares, currently outstanding. All previous issuances of preferred shares have been converted into Common Shares. The rights and preferences of the holders of Common Shares are summarized below. The Articles authorize a class of undefined preferred shares (the “Blank Preferred Shares”). There are no rights associated with the Blank Preferred Shares and none have been issued.

(a) Common Shares

Holders of the Common Shares are entitled to one vote for each whole share on all matters to be voted upon by shareholders, including the election of directors. Holders of the Common Shares do not have cumulative voting rights in the election of directors. All Common Shares are equal to each other with respect to liquidation and dividend rights. Holders of the Common Shares are entitled to receive dividends, subject to shareholder approval, out of funds legally available under Netherlands Antilles law. See “Dividend Policy” below. In the event of the liquidation of the Company, all assets available for distribution to the holders of the Common Shares are distributable among them according to their respective holdings, subject to the preferences of any shares having a preference upon liquidation that may be then outstanding. Holders of the Common Shares have no preemptive rights to purchase any additional, unissued Common Shares. The foregoing summary of the Common Shares does not purport to be complete and is subject to, and qualified in its entirety by, the provisions of the Articles.

(b) **Dividend Policy**

The Company has never declared or paid any cash dividends on its Common Shares and does not anticipate paying cash dividends in the foreseeable future. It is the present intention of the Company's Board of Directors to retain all earnings in the Company in order to support the future growth of its business. Any determination in the future to pay dividends will be dependent upon the Company's consolidated results of operations, financial condition, cash requirements, future prospects and other factors. In addition, the ability of the Company to pay dividends is subject to the limitations of the Corporate Law of the Netherlands Antilles, which provides, among other things, that dividends, while permitted to be paid periodically during a fiscal year, are subject to being proposed by the Board of Directors of the Company and approved thereafter at the General Meeting of Shareholders. The Corporate Law of the Netherlands Antilles also provides that a distribution of dividends can only occur if, at the moment of distribution, the equity of the Company equals at least the nominal capital of the Company and, as a result of the distribution, will not fall below the nominal capital. Nominal capital is the sum of the par values of all of the issued shares in the Company's capital stock at any moment in time.

(c) **The Blank Preferred Shares**

There are no preferences or any rights whatsoever associated with the Blank Preferred Shares. These shares are unissued and are not owned by any of the current shareholders of the Company. Any issuance of these preferred shares is solely within the discretion of the Company's Board of Directors. The Company has undertaken toward the TASE that so long as shares of its Common Stock are listed for trading on the TASE, the Company shall not issue or grant any shares of a different class of shares than those that are listed for trading on the TASE. This undertaking does not apply to Preferred Shares as defined in Section 46B(b) of the Israel Securities Law, on the condition that such Preferred Shares are issued in accordance with the conditions set forth in Section 46A(1) therein.

4. **Changing the Rights of the Shareholders.** The general meeting of shareholders decides upon any change in the Articles. A resolution to amend the Articles requires the approval of the absolute majority of all shares outstanding and entitled to vote.
5. **General Meetings.** At least one general meeting of shareholders must be held each year. General meetings must be held in Curaçao. Special general meetings of shareholders may be called at any time by the Chairman of the Board or by the Board of Directors upon no less than 10 nor more than 60 days' written notice to the Company's shareholders. Every shareholder has the right to attend any meeting of shareholders in person or by proxy and to address the meeting. No action may be taken at any meeting of shareholders unless a quorum consisting of holders of at least one-half of the shares outstanding and entitled to vote are present at the meeting in person or by proxy.
6. **Limitations to Own Securities.** The Articles contain no limits on the right to own securities.
7. **Change of Control.** The Articles contain no provisions that would prevent or delay a change of control of the Company.
8. **Disclosure of Ownership.** By-laws do not exist under Netherlands Antilles law. The Articles contain no provisions requiring a shareholder to disclose his or her interest at a certain time; however holders of our shares are subject to the reporting provisions of the Securities and Exchange Commission.

C. Material Contracts

1. Convertible Debentures and Trust Deed

On December 11, 2003, we completed an offering of securities in Israel, resulting in gross proceeds of approximately \$17.1 million. We sold 100,000 units of securities, each unit consisting of 800 debentures (Series A), two options (Series A) exercisable into debentures (Series A) and six warrants (Series 1) exercisable into Common Shares of the Company.

The debentures are linked to the US dollar and bear annual interest at the rate of 6.0%, payable on the 5th of June and the 5th of December each year commencing on June 5, 2004 and ending on December 5, 2009. Principal is payable in four installments on the 5th of December of the years 2006-2009. During the period beginning 45 days after the registration of the debentures (Series A) for trading on the TASE and ending November 21, 2009, the debentures (Series A) are convertible in Common Shares at a conversion rate of one Common Share per each NIS 27 (currently approximately \$6.43) amount of the debentures. The conversion rate is subject to certain adjustments. The debentures (Series A) are unsecured.

Options (Series A) which were exercised by non-affiliates of the Company before their expiry date resulted in additional gross proceeds of approximately \$1.6 million to the Company in the first quarter of 2004.

Each warrant (Series 1) is exercisable into one Common Share of the Company until November 21, 2007 for an exercise price of approximately \$6.43.

In accordance with chapter E1 of the Israel Securities Law, we offered the debentures after nominating a trustee for the debenture holders. The trustee is Ubank Trust Company Ltd. (formerly Investec Trust Company (Israel) Ltd.) and the date of the Trust Deed is December 2, 2003. The Trust Deed includes, among other things, the duties of the trustee, the circumstances in which the trustee can demand immediate repayment of the outstanding debentures, the circumstances in which the trustee or the Company can call meetings of debenture holders and the procedures for such meetings.

In August 2006 we convened a general meeting of the debenture holders, where a special resolution was adopted concerning the amount and the timing of the first installment payment of the principal of the debentures. A majority of the debenture holders approved that (a) 50% of the first payment amount, approximately \$2.4 million, will be deferred to December 5, 2009 (the last date of payment of the principal on the debentures), and (b) with respect to the other 50% of the first payment amount, the Company could choose from the following alternatives, in its sole discretion: (1) to convert such amount on December 5, 2006 into our Common Shares, at a conversion price per share of \$1.28, which reflects the average closing price for the 10 day period prior to July 17, 2006, or (2) to pay the approximately \$2.4 million amount to the debenture holders, in cash. In December 2006, we made the payments, in cash.

Following the \$20 million private placement investment in June 2007, we purchased an aggregate amount of NIS 15,000,000 nominal value, representing approximately \$3.5 million of the outstanding debentures. Pursuant to the terms of the prospectus governing the debentures, the amount repurchased by us was retired and removed from circulation. As a result, the total amount that we must pay in December 2007 was reduced to approximately \$4.6 million, approximately \$4.2 million for the second of the four annual re-payments of the principal of the debentures, and approximately \$0.4 million for the semi-annual interest payment.

2. Agreements with FID and Israel Discount Bank Ltd.

In April 2000, the Investors invested \$15 million in eZone, a subsidiary of the Company. The private placement to the Investors was accompanied by a Put/Call Agreement, according to which the Investors were granted the right to require us to repurchase their shares in eZone beginning May 2004 in exchange for both cash and our Common Shares. In February 2001, management decided to discontinue the operations of eZone. During the same period, we agreed to a partial exercise of the Investors' put option, resulting in a payment to them of \$4.5 million.

On March 16, 2004, we entered into a new agreement with the Investors which replaced the Put/Call Agreement and which restructured the remaining portion of the put option. We agreed to issue the Investors, in a private placement, 750,000 Common Shares and warrants to purchase 350,000 additional Common Shares that are exercisable through December 31, 2007. In addition, we agreed to pay the Investors in two annual installments a total of \$8.6 million plus interest at 7.5% a year by May 1, 2005. The first installment of \$4.6 million was paid as required at the beginning of May 2004.

In May 2005, we entered into an agreement with the Investors regarding the payment of the remaining \$4.0 million due to the Investors, pursuant to the March 2004 agreement between us and the Investors. We agreed to pay \$2.0 million on May 2, 2005, \$1.0 million by April 1, 2006 and \$1.0 million by August 1, 2006. In addition the interest to be paid on the outstanding principal amount was changed to LIBOR plus 2.5%. The first installment of \$2.0 million was paid as required at the beginning of May 2005.

In August 2006, we entered into an agreement with the Investors whereby the Investors converted the \$1.0 million payment that was due on April 1, 2006 into 781,250 Common Shares and the \$1.0 million payment that was due on August 1, 2006 was delayed to August 1, 2007. The Investors may, at their sole discretion, convert all or any portion of the \$1.0 million payment now payable on August 1, 2007 into Common Shares, at a conversion price per each share of \$3.20.

3. Agreements with Formula

In June 2005, we entered into a share purchase agreement with Formula, whereby Formula invested \$2.0 million in Sapiens, and we issued 1,041,667 Common Shares to Formula, at a purchase price per share of \$1.92, which was the average closing price for the 10 day period prior to the execution of the agreement. The Common Shares issued pursuant to the June 2005 were granted "piggyback" registration rights, similar to those granted to Formula and Yarnfield International Limited (now Magnum Technology Limited) in their 2001 investment.

In August 2006, we entered into a share issuance agreement with Formula whereby Formula invested \$2.0 million in the Company, and we issued 1,562,500 Common Shares to Formula, at a purchase price per share of \$1.28, which was the average closing price for the 10 day period prior to July 17, 2006, and which was the same as the conversion price approved by the debentures holders at the August 2006 meeting.

4. Loan Agreement

In December 2006, we entered into loan agreement with Bank Leumi Le-Israel whereby we borrowed an aggregate amount of approximately \$2.5 million. The proceeds of the loan enabled us to make the December 2006 principal and interest payment on the debentures. The loan was secured by a pledged deposit of Formula. The loan bears an annual interest rate equal to the prime rate of interest in Israel plus 0.5% (for a total of 6.5%) and the principal and interest are due on August 30, 2007.

D. Exchange Controls

Although there are Netherlands Antilles laws which may impose foreign exchange controls on the Company and may affect the payment of dividends, interest or other payments to non-resident holders of the Company's securities, including the Common Shares, the Company has been granted an exemption from such foreign exchange control regulations by the Central Bank of the Netherlands Antilles. Other jurisdictions in which the Company conducts operations may have various currency or exchange controls. In addition, the Company is subject to the risk of changes in political conditions or economic policies which could result in new or additional currency or exchange controls or other restrictions being imposed on the operations of the Company. As to the Company's securities, Netherlands Antilles law and the Articles impose no limitations on the right of non-resident or foreign owners to hold or vote such securities.

E. Taxation

See Item 5, “Operating and Financial Review and Prospects – Operating Results – Taxes on Income” for disclosure regarding the reduction of our deferred tax assets and tax advances balances, in 2006.

Israeli Tax Considerations and Government Programs

General

The following is a general discussion only and is not exhaustive of all possible tax considerations. It is not intended, and should not be construed, as legal or professional tax advice and should not be relied upon for tax planning purposes. In addition, this discussion does not address all of the tax consequences that may be relevant to purchasers of our Common Shares in light of their particular circumstances, or certain types of purchasers of our Common Shares subject to special tax treatment. Examples of this kind of investor include residents of Israel and traders in securities who are subject to special tax regimes not covered in this discussion. Each individual/entity should consult its own tax or legal advisor as to the Israeli tax consequences of the purchase, ownership and disposition of our Common Shares.

To the extent that part of the discussion is based on new tax legislation, which has not been subject to judicial or administrative interpretation, we cannot assure you that the tax authorities or the courts will accept the views expressed in this section.

The following summary describes the current tax structure applicable to companies in Israel, with special reference to its effect on us. The following also contains a discussion of the material Israeli tax consequences to holders of our Common Shares.

Taxation of Companies

General Corporate Tax Structure

Generally, Israeli companies are subject to corporate tax at the rate of 31% on taxable income for the year 2006 and are subject to capital gains tax at a rate of 25% on capital gains (other than gains derived from the sale of listed securities that are taxed at the prevailing corporate tax rates) derived after January 1, 2003. However, the effective tax rate payable by a company that derives income from an approved enterprise (as discussed below) may be considerably lower. Depending on the relevant tax treaties at issue, dividends or interest received by an Israeli company from foreign subsidiaries are generally subject to tax regardless of the company’s status as an approved enterprise. Under recently adopted legislation, taxes paid by Israeli companies will be gradually reduced to a rate of 29% for the 2007 tax year, 27% for the 2008 tax year, 26% for the 2009 tax year and 25% for the 2010 tax year and thereafter.

Law for the Encouragement of Industry (Taxes), 1969.

According to the Law for the Encouragement of Industry (Taxes), 1969 (“Industry Encouragement Law”), industrial companies are entitled to the following tax benefits, among others:

- deduction of purchases of know-how and patents over an eight-year period for tax purposes;
- expenses involved with the issuance and listing of shares on the TASE or on a recognized stock market outside of Israel, are deductible over a three-year period;
- the right to elect, under specified conditions, to file a consolidated tax return with other related Israeli industrial companies; and
- accelerated depreciation rates on equipment and buildings.

According to the law, an “industrial company” is defined as a company resident in Israel, at least 90% of the income of which, in any tax year, determined in Israeli currency (exclusive of income from government loans, capital gains, interest and dividends) is derived from an “industrial enterprise” owned by it. An “industrial enterprise” is defined as an enterprise whose major activity in a given tax year is industrial production activity. Eligibility for benefits under the Industry Encouragement Law is not subject to receipt of prior approval from any governmental authority.

We believe that our subsidiary, Sapiens Technologies (1982) Ltd, currently qualifies as an industrial company within the definition under the Industry Encouragement Law. However, we cannot give any assurance that we will continue to qualify as an “industrial company” or that the benefits described above will be available in the future.

Law for the Encouragement of Capital Investments, 1959.

The Law for the Encouragement of Capital Investments, 1959, as amended (the “Investments Law”), provides that a capital investment in eligible facilities may, upon application to the Investment Center of the Ministry of Industry, Trade and Labor of the State of Israel, be designated as an “Approved Enterprise.” Each certificate of approval for an approved enterprise relates to a specific investment program, delineated both by the financial scope of the investment and by the physical characteristics of the facility or the asset. An approved enterprise is entitled to benefits including Israeli government cash grants and tax benefits in specified development areas. The extent of the tax benefits available under the Investments Law and the period for which tax benefits are available are determined by the geographic location of the enterprise. The benefits are dependent upon the fulfillment of conditions stipulated in the Investments Law and its regulations, including the criteria set forth in the specific certificate of approval. The tax benefits from any certificate of approval relate only to taxable profits attributable to the specific approved enterprise. If a company has more than one approval or only a portion of its enterprise is approved, its effective tax rate is the result of a weighted average of the applicable rates (such weighted average is calculated in accordance with the guidelines of the Investment Law).

Tax benefits given under the Investment Law also apply to income generated by a company from the grant of a usage right with respect to know-how developed by the approved enterprise, income generated from royalties, and income derived from a service which is auxiliary to such usage right or royalties, provided that such income is generated in the course of the approved enterprise’s ordinary course of business.

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 law, the specific objectives of the applicant company set forth in such application and certain financial criteria of the applicant company. Accordingly, there can be no assurance that any future application will be approved. In addition, as described above, the benefits available to an approved enterprise are dependent upon the fulfillment of certain conditions stipulated in the Investments Law and its regulations and the criteria set forth in the specific certificate of approval. In the event that these conditions are violated, in whole or in part, we would be required to refund the amount of tax benefits, with the addition of the Israeli consumer price index linkage adjustment and interest.

Our subsidiary, Sapiens Technologies (1982) Ltd., which is incorporated in Israel, was granted approved enterprise status by the Investment Center for six investment programs in 1984, 1991, 1993, 1995, 1998 and 2000 under the Investments Law.

We believe our approved enterprise operates in substantial compliance with all such conditions and criteria.

On April 1, 2005, a comprehensive amendment to the Investments Law came into effect. As the amended Investments Law does not retroactively apply to investment programs having an approved enterprise approval certificate issued by the Investment Center prior to December 31, 2004, our current tax benefits are subject to the provisions of the Investments Law prior to its revision. Our approved plans subsequent to 2005 and others that may be received in the future will be subject to the provisions of the Investments Law, as amended. Accordingly, the following description includes a summary of the Investments Law prior to its amendment as well as the relevant changes contained in the Investments Law.

Under the terms of our approved enterprise, once we begin generating taxable net income, we will be entitled to a tax exemption with respect to the income derived from our approved enterprise program for two years and will be subject to a reduced company tax rate of between 10% and 25% for the following five to eight years, depending on the extent of foreign (non-Israeli) investment in our company during the relevant year. The tax rate will be 20% if the foreign investment level is more than 49% but less than 74%, 15% if the foreign investment level is more than 74% but less than 90%, and 10% if the foreign investment level is 90% or more. The lowest level of foreign investment during a particular year will be used to determine the relevant tax rate for that year. The period in which we receive these tax benefits is limited to 12 years from the year in which operations or production by the enterprise commenced or 14 years from the year in which approval was granted, whichever is the earlier. Dividends distributed from tax-exempt income would be taxed according to the company tax rate that would have been applicable had the company not been exempt from taxation that year. This rate is generally 10% to 25% depending on the extent of foreign investment in the company.

Dividends paid out of income generated by an approved enterprise (or out of dividends received from a company whose income is generated by an approved enterprise) are generally subject to withholding tax at the rate applicable to dividends from approved enterprises (15%), unless a different rate is provided according to a treaty between Israel and the shareholder's country of residence (if the dividend is distributed out of income derived during the tax exemption period or within 12 years thereafter). The company must withhold this tax at source.

The Investments Law also provides that an approved enterprise is entitled to accelerated depreciation on its property and equipment that are included in an approved investment program. We have not utilized this benefit.

Pursuant to the amendment to the Investments Law, effective as of April 1, 2005, the basic condition for receiving the benefits (both under the grant and the tax benefits programs) is the enterprise's contribution to the economic independence of the State of Israel and its contribution to the gross domestic product. In order to fulfill these conditions, the enterprise is required to be categorized as an industrial enterprise which complies with any of the following:

- its major activity is in the field of biotechnology or nano-technology;
- its revenues during the applicable tax year from any single market (i.e. country or a separate customs territory) do not exceed 75% of the privileged enterprise's aggregate revenues during such year; or
- 25% or more of its revenues during the applicable tax year are generated from sales into a single market (i.e. country or a separate customs territory) with a population of at least 12 million residents.

It should be noted that the amendment to the Investments Law further addresses benefits that are being granted to enterprises and the length of the benefits period.

We cannot assure you that we will comply with the above conditions in the future, or that we will be entitled to any additional benefits under the amended Investments Law.

According to the amendment to the Investments Law, only approved enterprises receiving cash grants require the approval of the Investment Center. Approved enterprises, which do not receive benefits in the form of governmental cash grants, such as benefits in the form of tax benefits, are no longer required to obtain this approval (such enterprises are referred to as "privileged enterprises"). In order to be eligible for the tax benefits, privileged enterprises are required to comply with certain requirements and make certain investments as specified in the amended Investments Law. The privileged enterprises are subject to the responsibility of the Israeli Tax Authority and may, at their discretion, in order to provide greater certainty, elect to apply for a pre-ruling from the Israeli tax authorities confirming that they are in compliance with the provisions of the amended Investments Law and therefore are entitled to receive the benefits provided under the amended Investments Law as was recently obtained by us as detailed above. The amended Investments Law also specifies which income of the privileged enterprise is entitled to tax benefits (for example income generated from the sale of products that were manufactured by the privileged enterprise, income generated from usage right with respect to know-how developed by the privileged enterprise, etc.).

We cannot assure you that we will comply with the conditions required for privileged enterprises under the amended Investments Law in the future or that we will be entitled to any additional benefits under the amended Investments Law.

In addition, the amended Investments Law changed the definition of "foreign investment" according to the Investments Law so that the definition, instead of a foreign currency investment, now requires a minimal investment of NIS 5 million by foreign investors. Furthermore, such definition now also includes the purchase of shares of a company from another shareholder (secondary market purchase), provided that the company's outstanding and paid-up share capital exceed NIS 5 million. Such changes to the aforementioned definition will take effect retroactively from 2003.

Special Provisions Relating to Taxation Under Inflationary Conditions.

The Income Tax Law (Inflationary Adjustments), 1985, generally referred to as the Inflationary Adjustments Law, represents an attempt to overcome the problems presented to a traditional tax system by an economy undergoing rapid inflation. The Inflationary Adjustments Law is highly complex. The features that are material to us can be described as follows:

- When the value of a company's equity, as calculated under the Inflationary Adjustments Law, exceeds the depreciated cost of its fixed assets (as defined in the Inflationary Adjustments Law), a deduction from taxable income is permitted equal to the excess multiplied by the applicable annual rate of inflation. The maximum deduction permitted in any single tax year is 70% of taxable income, with the unused portion permitted to be carried forward, linked to the increase in the consumer price index.
- If the depreciated cost of the company's fixed assets exceeds its equity, then the 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 Israeli consumer price index.

The Minister of Finance may, with the approval of the Knesset Finance Committee, determine by decree, during a certain fiscal year (or until February 28th of the following year) in which the rate of increase of the Israeli consumer price index would not exceed or did not exceed 3%, that some or all of the provisions of the Inflationary Adjustments Law shall not apply with respect to such fiscal year, or, that the rate of increase of the Israeli consumer price index relating to such fiscal year shall be deemed to be 0%, and to make the adjustments required to be made as a result of such determination. The Minister made no such determination in respect of 2006, even though the price index in 2006 declined by 0.1%.

The Israeli Tax Ordinance and regulations promulgated thereunder allow "Foreign-Invested Companies," (as defined in the Investments Law) that maintain their accounts in US dollars in compliance with regulations published by the Israeli Minister of Finance, to base their tax returns on their operating results as reflected in their US dollar financial statements or to adjust their tax returns based on exchange rate changes rather than changes in the Israeli consumer price index, in lieu of the principles set forth by the Inflationary Adjustments Law. For these purposes, a Foreign-Invested Company is a company (1) more than 25% of whose share capital, in terms of rights to profits, voting and appointment of directors are held by persons who are not residents of Israel, and (2) more than 25% of whose combined share and loan capital is held by persons who are not residents of Israel. A company that elects to measure its results for tax purposes based on the US dollar exchange rate cannot change such election for a period of three years following the election. Our Israeli subsidiaries have elected to measure our results for tax purposes based on the US dollar exchange rate as of January 1, 2005.

Transfer Pricing

As part of the Israeli 2003 tax reform, the Israeli Tax Ordinance was amended to include section 85A, dealing with international transactions transfer pricing. Section 85A provides that regardless of the actual conditions of an international transaction between related parties, the transaction shall be reported and taxed, based on the arm's length standard, *i.e.*, based on market conditions in similar transactions between unrelated parties. On October 30, 2006, the Income Tax Regulations (Determination of Market Conditions), hereinafter referred to as the Regulations, which provide instructions for the implementation of section 85A, came into effect.

In accordance with the Regulations, a transaction shall be considered an international transaction if one of the parties is a "foreign resident" as defined thereunder or if the income generated from such transaction, in all or in part, is taxed both in and outside of Israel. The Regulations establish acceptable methods for comparison between transactions, and methods for calculating the price range against which the transaction is measured.

Taxpayers are required to include in their yearly income tax returns a report regarding their international transactions at arm's length prices.

The following discussion is a summary of certain anticipated tax consequences of an investment in the Common Shares under US federal income tax laws and Netherlands Antilles tax laws. The discussion does not deal with all possible tax consequences relating to an investment in the Common Shares. In particular, the discussion does not address the tax consequences under state, local and other (e.g., non-US, non-Netherlands Antilles) tax laws. Accordingly, each prospective investor should consult its tax advisor regarding the tax consequences of an investment in the Common Shares. The discussion is based upon laws and relevant interpretations thereof in effect as of the date of this annual report on Form 20-F, all of which are subject to change.

Netherlands Antilles Taxation

Under the laws of the Netherlands Antilles as currently in effect, a holder of Common Shares who is not resident of, and during the taxable year has not engaged in trade or business through a permanent establishment in, the Netherlands Antilles will not be subject to Netherlands Antilles income tax on dividends paid with respect to the Common Shares or on gains realized during that year on sale or disposal of such shares; the Netherlands Antilles does not impose a withholding tax on dividends paid by the Company. Under Netherlands Antilles law, no gift or inheritance taxes are levied if, at the time of such gift or at the time of death, the relevant holder of Common Shares was not domiciled in the Netherlands Antilles.

U.S. Federal Income Tax Considerations

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

- an individual who is a citizen or resident of the U.S. for U.S. federal income tax purposes;
- a corporation (or another entity taxable as a corporation for U.S. federal income tax purposes) created or organized under the laws of the United States, any political subdivision thereof, or the District of Columbia;
- 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 (a “non-U.S. holder”) and considers only U.S. holders that will own the Common Shares as capital assets (generally, for investment).

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 Common Shares as part of a hedging, straddle or conversion transaction, U.S. holders whose functional currency is not the U.S. dollar, U.S. holders that acquired our Common Shares upon the exercise of employee stock options or otherwise as compensation, insurance companies, real estate investment trusts, regulated investment companies, grantor trusts, individual retirement and tax-deferred accounts, certain former citizens or long-term residents of the U.S., tax-exempt organizations, financial institutions, “financial service entities” 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 Common 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 Common Shares.

Taxation of Distributions on Common 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 Common 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. 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% through taxable years beginning on or before December 31, 2010), provided that such dividends meet the requirements of “qualified dividend income.” For this purpose, qualified dividend income generally includes dividends paid by a foreign corporation if certain holding period and other requirements are met and either (a) the stock of the foreign corporation with respect to which the dividends are paid is “readily tradable” on an established securities market in the U.S. (e.g., the NASDAQ Capital Market) or (b) the foreign corporation is eligible for benefits of a comprehensive income tax treaty with the U.S. which includes an information exchange program and is determined to be satisfactory by the U.S. Secretary of the Treasury. The United States Internal Revenue Service (“IRS”) has determined that the U.S.-Netherlands Antilles income tax treaty is not a comprehensive income tax treaty for this purpose. 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 (i) if the U.S. holder held the Common 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 Common Share (or substantially identical securities); or (ii) 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 Common 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), or “PFIC”, for any taxable year, dividends paid on our Common Shares in such year or in the following taxable year would not be qualified dividends. See the discussion below regarding our PFIC status under “Tax Consequences if We Are a Passive Foreign Investment Company.” In addition, a non-corporate U.S. holder will be able to take qualified dividend income 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 income 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 Common Shares to the extent thereof, and then as capital gain from the deemed disposition of the Common Shares. Corporate holders will not be allowed a deduction for dividends received in respect of the Common Shares.

Distributions of current or accumulated earnings and profits paid in foreign currency to a U.S. holder will be includible in the income of a U.S. holder in a U.S. dollar amount calculated by reference to the exchange rate on the day the distribution is received. A U.S. holder that receives a foreign currency distribution and converts the foreign currency into U.S. dollars subsequent to receipt will have foreign exchange gain or loss based on any appreciation or depreciation in the value of the foreign currency against the U.S. dollar, which will generally be U.S. source ordinary income or loss.

Taxation of the Disposition of Common 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 Common 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 Common Shares. The gain or loss recognized on the disposition of the Common Shares will be long-term capital gain or loss if the U.S. holder held the Common Shares for more than one year at the time of the disposition and is eligible for a reduced rate of taxation for individuals (currently a maximum rate of 15% for taxable years beginning on or before December 31, 2010). Capital gain from the sale, exchange or other disposition of Common Shares held for one year or less is short-term capital gain and taxed as ordinary income. Gain or loss recognized by a U.S. holder on a sale, exchange or other disposition of Common Shares will be treated as U.S. source income or loss. The deductibility of capital losses is subject to limitation.

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 that uses the accrual method 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 Common 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 would be a passive foreign investment company (a "PFIC") if (taking into account certain "look-through" rules with respect to the income and assets of our corporate subsidiaries) either 75% or more of our gross income for the taxable year was passive income or the average percentage (by value) of our passive assets during the taxable year was at least 50%. As discussed below, we believe that we were not a PFIC for 2006.

If we were a PFIC, each U.S. holder would (unless it made one of the elections discussed below on a timely basis) be taxable on gain recognized from the disposition of our Common Shares (including gain deemed recognized if our Common Shares are used as security for a loan) and upon receipt of certain excess distributions (generally, distributions that exceed 125% of the average amount of distributions in respect to such shares received during the preceding three taxable years or, if shorter, during the U.S. holder's holding period prior to the distribution year) with respect to our Common Shares as if such income had been recognized ratably over the U.S. holder's holding period for the shares. The U.S. holder's income for the current taxable year would include (as ordinary income) amounts allocated to the current taxable year and to any taxable year prior to the first day of the first taxable year for which we were a PFIC. Tax would also be computed at the highest ordinary income tax rate in effect for each other taxable year to which income is allocated, and an interest charge on the tax as so computed would also apply. The tax liability with respect to the amount allocated to the taxable year prior to the taxable year of the distribution or disposition cannot be offset by any net operating losses. Additionally, if we were a PFIC, U.S. holders who acquire our Common Shares from decedents (other than nonresident aliens) dying before 2010 would be denied the normally-available step-up in basis for such shares to fair market value at the date of death and, instead, would have a tax basis in such shares equal to the decedent's basis, if lower.

As an alternative to the tax treatment described above, a U.S. holder could elect to treat us as a “qualified electing fund” (a “QEF”), in which case the U.S. holder would be taxed, for each taxable year that we are a PFIC, on its pro rata share of our ordinary earnings and net capital gain (subject to a separate election to defer payment of taxes, which deferral is subject to an interest charge). Special rules apply if a U.S. holder makes a QEF election after the first taxable year in its holding period in which we are a PFIC. We have agreed to supply U.S. holders with the information needed to report income and gain under a QEF election if we were a PFIC. Amounts includable in income as a result of a QEF election will be determined without regard to our prior year losses or the amount of cash distributions, if any, received from us. A U.S. holder’s basis in its Common Shares will increase by any amount included in income and decrease by any amounts not included in income when distributed because such amounts were previously taxed under the QEF rules. So long as a U.S. holder’s QEF election is in effect with respect to the entire holding period for its Common Shares, any gain or loss realized by such holder on the disposition of its Common Shares held as a capital asset ordinarily will be capital gain or loss. Such capital gain or loss ordinarily would be long-term if such U.S. holder had held such Common Shares for more than one year at the time of the disposition. For non-corporate U.S. holders, long-term capital gain is generally subject to a maximum federal income tax rate of 15% for taxable years beginning on or before December 31, 2010. The QEF election is made on a shareholder-by-shareholder basis, applies to all Common Shares held or subsequently acquired by an electing U.S. holder and can be revoked only with the consent of the IRS.

As an alternative to making a QEF election, a U.S. holder of PFIC stock that is “marketable stock” (e.g., “regularly traded” on the NASDAQ Capital Market) may, in certain circumstances, avoid certain of the tax consequences generally applicable to holders of stock in a PFIC by electing to mark the stock to market as of the beginning of such U.S. holder’s holding period for our Common Shares. As a result of such an election, in any taxable year that we are a PFIC, a U.S. holder would generally be required to report gain or loss to the extent of the difference between the fair market value of the Common Shares at the end of the taxable year and such U.S. holder’s tax basis in such shares at that time. Any gain under this computation, and any gain on an actual disposition of our Common Shares, would be treated as ordinary income. Any loss under this computation, and any loss on an actual disposition of our Common Shares, generally would be treated as ordinary loss to the extent of the cumulative net-mark-to-market gain previously included. Any remaining loss from marking Common Shares to market will not be allowed, and any remaining loss from an actual disposition of Common Shares generally would be capital loss. A U.S. holder’s tax basis in its Common Shares is adjusted annually for any gain or loss recognized under the mark-to-market election. There can be no assurances that there will be sufficient trading volume with respect to our Common Shares for the Common Shares to be considered “regularly traded” or that our Common Shares will continue to trade on the NASDAQ Capital Market. Accordingly, there are no assurances that our Common Shares will be marketable stock for these purposes. As with a QEF election, a mark-to-market election is made on a shareholder-by-shareholder basis, applies to all Common Shares held or subsequently acquired by an electing U.S. holder and can only be revoked with consent of the IRS (except to the extent our Common Shares no longer constitute “marketable stock”).

Based on an analysis of our assets and income, we believe that we were not a PFIC for 2006 or 2005. The tests for determining PFIC status are applied annually and it is difficult to make accurate predictions of future income and assets, which are relevant to this determination. Accordingly, there can be no assurance that we will not become a PFIC. U.S. holders who hold Common Shares during a period when we are a PFIC will be subject to the foregoing rules, even if we cease to be a PFIC, subject to certain exceptions for U.S. holders who made QEF, mark-to-market or certain other special elections. U.S. holders are urged to consult their tax advisors about the PFIC rules, including the consequences to them of making a mark-to-market or QEF election with respect to our Common Shares in the event that we qualify as a PFIC.

Non-U.S. holders of Common Shares

Except as provided below, a non-U.S. holder of Common Shares will not be subject to U.S. federal income or withholding tax on the receipt of dividends on, or the proceeds from the disposition of, our Common Shares, unless, in the case of U.S. federal income taxes, 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, such 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 certain other conditions are met.

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% (through 2010) with respect to dividend payments on, or receipt of the proceeds from the disposition of, our Common 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, certifies that such holder is not subject to backup withholding or otherwise establishes an exemption. Non-U.S. holders are not subject to information reporting or backup withholding with respect to dividend payments on, or receipt of the proceeds from the disposition of, our Common Shares in the U.S., or by a U.S. payor or U.S. middleman, provided that such non-U.S. holder provides a taxpayer identification number, certifies to its foreign status, 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 holder, or alternatively, the 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 IRS.

F. Dividends and Paying Agents

Not applicable.

G. Statement by Experts

Not applicable.

H. Documents on Display

We are currently subject to the information and periodic reporting requirements of the Exchange Act that are applicable to foreign private issuers. 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. Our SEC filings are filed electronically on the EDGAR reporting system and may be obtained through that medium. You may inspect without charge and copy at prescribed rates such filings, including any exhibits and schedules, at the public reference facilities maintained by the SEC, 100 F Street, N.E., Washington, D.C. 20549. You may also obtain copies of such materials from the SEC at prescribed rates. You may call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. The Exchange Act file number for our Securities and Exchange Commission filings is 000-20181.

The Company's Common Shares are quoted on the NASDAQ Capital Market. You may inspect reports and other information concerning the Company at the offices of the National Association of Securities Dealers, Inc., 9513 Key West Avenue, Rockville, MD 20850.

Information about Sapiens is also available on its website at <http://www.sapiens.com>. Such information on our website is not part of this annual report.

I. Subsidiary Information

Not applicable.

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Market risks relating to our operations result primarily from changes in exchange rates, interest rates or weak economic conditions in the markets in which we sell our products and services. We have been and we are actively monitoring these potential exposures. To manage the volatility relating to these exposures, we may enter into various forward contracts or other hedging instruments. Our objective is to reduce, where it is deemed appropriate to do so, fluctuations in earnings and cash flows associated with changes in foreign currency rates and interest rates.

Foreign Currency Risk. We conduct our business in various foreign currencies, primarily those of Israel and to a lesser extent of Japan, Europe and Canada. A devaluation of the NIS, GBP, Euro and the Japanese Yen in relation to the US dollar has the effect of reducing the US dollar amount of any of our expenses or liabilities which are payable in those currencies (unless such expenses or payables are linked to the US dollar) and increasing the US Dollar amount of any of our revenues which are payable in those currencies.

Because exchange rates between the NIS, GBP, Euro and the Japanese Yen and the US dollar fluctuate continuously, exchange rate fluctuations and especially larger periodic devaluations will have an impact on our profitability and period-to-period comparisons of our results. The effects of foreign currency re-measurements are reflected as financial expenses in our consolidated financial statements.

We monitor our foreign currency exposure and, from time to time, may enter into currency forward contracts or put/call currency options to hedge balance sheet exposure. In 2006 we did not enter into forward exchange contracts to hedge transactions denominated in foreign currencies.

We may use such contracts to hedge exposure to changes in foreign currency exchange rates associated with balance sheet balances denominated in a foreign currency and anticipated costs to be incurred in a foreign currency.

Market Risk. We currently do not invest in, or otherwise hold, for trading or other purposes, any financial instruments subject to market risk.

Interest Rate Risk. We pay interest on our credit facilities, convertible notes and short-term loans based on LIBOR, for dollar-denominated loans, and the prime interest rate in Israel, for some of our NIS-denominated loans. As a result, changes in the general level of interest rates directly affect the amount of interest payable by us under these facilities. However, we expect our exposure to risk from changes in interest rates to be minimal and not material. Therefore, no quantitative tabular disclosures are required.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

None.

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

None.

ITEM 15. CONTROLS AND PROCEDURES

A. Disclosure Controls and Procedures. The President and Chief Executive Officer of the Company and Executive Vice President and Chief Financial Officer of the Company have evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this annual report (the "Evaluation Date"). Based on such evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that the Company files or submits under the Exchange Act is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decision regarding disclosure and is recorded, processed, summarized and reported within the periods specified by the SEC's rules and forms.

B. Internal Controls. Since the Evaluation Date, there have not been any significant changes in the Company's internal controls over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

All internal control systems and disclosure controls and procedures, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective may not prevent or detect misstatements and can provide only reasonable assurance with respect to the ability to detect or uncover all failures of persons within the Company to disclose material information required to be set forth in the Company's reports. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

ITEM 16A. AUDIT COMMITTEE FINANCIAL EXPERT

Our Board of Directors determined that Mr. Yacov Elinav meets the definition of an "audit committee financial expert," as defined under the applicable rules promulgated by the SEC. All members of the Audit Committee are independent directors.

ITEM 16B. CODE OF ETHICS

We have adopted a Code of Ethics that applies to our principal executive officer, principal financial officer and corporate controller, as well as to our directors and other employees. The Code of Ethics is publicly available on our website at www.sapiens.com. Written copies are available upon request. If we make any substantive amendments to the Code of Ethics or grant any waivers, including any implicit waiver, from a provision of this code to our chief executive officer, principal financial officer or corporate controller, we will disclose the nature of such amendment or waiver on our website.

ITEM 16C. PRINCIPAL ACCOUNTANT FEES AND SERVICES**Policies and Procedures**

Our Audit Committee has adopted a policy and procedures for the approval of audit and non-audit services rendered by our independent auditors, Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global. The policy generally requires the Audit Committee's approval of the scope of the engagement of our independent auditors or on an individual basis. The policy prohibits retention of the independent auditors to perform the prohibited non-audit functions defined in Section 201 of the Sarbanes-Oxley Act of 2002 or the rules of the SEC, and also considers whether proposed services are compatible with the independence of the public auditors. During 2005 and 2006, 100% of the fees for services rendered by the Company's independent auditors were approved by the Audit Committee.

Fees Paid to Independent Auditors

The following table sets forth, for each of the years indicated, the aggregate fees billed by our independent auditors for types of services indicated:

	Year ended December 31,	
	2005	2006
	(in thousands)	
Audit Fees (1)	\$ 149	\$ 163
Audit Related Fees (2)	13	-
Tax Fees (3)	56	73
All Other Fees (4)	34	-
Total	\$ 253	\$ 236

- (1) Audit Fees consist of fees billed for the annual audit and the quarterly reviews of the Company's consolidated financial statements and consist of services that would normally be provided in connection with statutory and regulatory filings or engagements, including services that generally only the independent auditors can reasonably provide.
- (2) Audit Related Fees consist of fees billed for assurance and related services that traditionally were only performed by the independent auditor, and include the review of documents filed with the SEC, accounting consultation and consultation concerning financial accounting and reporting standards.
- (3) Tax Fees relate to tax compliance, planning and advice.
- (4) All Other Fees consist of services related to stock options and value added tax (VAT) related matters.

ITEM 16D. EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES

Not applicable.

ITEM 16E. PURCHASE OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATED PURCHASERS

During 2006, neither we nor an affiliated purchaser engaged in the purchasing of our Common Shares.

PART III

ITEM 17. FINANCIAL STATEMENTS

See Item 18.

ITEM 18. FINANCIAL STATEMENTS

The Consolidated Financial Statements and related notes required by this item are contained on pages F-1 through F-46 hereof.

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ITEM 19. EXHIBITS

- 1.1 Articles of Association of Sapiens International Corporation N.V., as amended on March 17, 2005 – incorporated by reference to registrant's Form 20-F, filed on June 29, 2005.
- 2.(b)1 Trust Deed between Sapiens International Corporation N.V. and Investec Trust Company (Israel) Ltd., dated December 2, 2003 –incorporated by reference to registrant's Form 20-F, filed on June 10, 2004.
- 4.(a)1 Amendment to Share Purchase Agreement by and between Sapiens International Corporation and Formula Systems (1985) Ltd. – incorporated by reference to registrant's Form 20-F, filed on July 3, 2001.
- 4.(a)2 Agreement among Sapiens International Corporation N.V., F.I.D. Holdings Ltd. and Israel Discount Bank Ltd., dated March 16, 2004 – incorporated by reference to registrant's Form 20-F, filed on June 10, 2004.
- 4.(a)3 Agreement among Sapiens International Corporation N.V., F.I.D. Holdings Ltd. and Israel Discount Bank Ltd., dated May 2, 2005 - incorporated by reference to registrant's Form 20-F, filed on June 29, 2005.
- 4.(a)4 Share Purchase Agreement between Sapiens International Corporation N.V. and Formula Systems (1985) Ltd., dated June 27, 2005 - incorporated by reference to registrant's Form 20-F, filed on June 29, 2005.
- 4.(a)5 Agreement among Sapiens International Corporation N.V., F.I.D. Holdings Ltd. and Israel Discount Bank Ltd., dated August 10, 2006.
- 4.(a)6 Share Issuance Agreement between Sapiens International Corporation N.V. and Formula Systems (1985) Ltd., dated August 10, 2006.
- 4(c)1 Sapiens International Corporation N.V. 1992 Stock Option and Incentive Plan, as amended and restated – incorporated by reference to registrant's Registration Statement of Form S-8 (No. 33-64208), filed on June 9, 1993, and to registrant's Registration Statement of Form S-8 (No. 333-10622), filed on July 22, 1999.
- 4(c)2 Sapiens International Corporation N.V. 2003 Share Option Plan.
- 4(c)3 Sapiens International Corporation N.V. 2005 Special Incentive Share Option Plan.

- 8.1 List of Subsidiaries
- 10.1 Consent of Kost Forer Gabbay & Kasierer, Independent Registered Public Accounting Firm
- 12.1 Certification by Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 12.2 Certification by Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 13.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 13.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

SAPIENS INTERNATIONAL CORPORATION N.V.
AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2006

IN U.S. DOLLARS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

SAPIENS INTERNATIONAL CORPORATION N.V.

We have audited the accompanying consolidated balance sheets of Sapiens International Corporation N.V. and its subsidiaries (the "Company") as of December 31, 2005 and 2006 and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Sapiens International Corporation N.V. and its subsidiaries as of December 31, 2005 and 2006 and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles.

Tel-Aviv, Israel
June 26, 2007

/s/ Kost Forer Gabbay & Kasierer
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands

	December 31,	
	2005	2006
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 6,699	\$ 3,108
Marketable securities (Note 3)	5,337	32
Trade receivables (net of allowance for doubtful accounts of \$662 and \$1,148 at December 31, 2005 and 2006, respectively) (Note 4)	8,339	11,010
Other receivables and prepaid expenses (Note 5)	1,520	1,689
Total current assets	21,895	15,839
PROPERTY AND EQUIPMENT, NET (Note 6)	1,716	1,495
OTHER ASSETS:		
Capitalized software development costs, net of accumulated amortization of \$31,075 and \$38,648 at December 31, 2005 and 2006, respectively (Note 7a)	12,219	13,467
Goodwill	8,621	8,621
Deferred income taxes (Note 13d)	3,573	2,747
Other, net (Note 7b)	3,842	3,450
Total other assets	28,255	28,285
Total assets	\$ 51,866	\$ 45,619

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

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands (except share and per share data)

	December 31,	
	2005	2006
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Short-term bank credit (Note 9a)	\$ 11,950	\$ 9,298
Current maturities of long-term liabilities and convertible debt (Notes 9 and 10)	7,162	6,305
Trade payables	1,910	2,019
Deferred revenues	4,867	3,463
Other liabilities and accrued expenses (Note 8)	6,742	7,370
Total current liabilities	32,631	28,455
LONG-TERM LIABILITIES:		
Convertible debt and warrants (Note 9b)	14,019	11,796
Other long-term liabilities (Note 10)	1,584	1,439
	15,603	13,235
COMMITMENTS AND CONTINGENT LIABILITIES (Note 11)		
SHAREHOLDERS' EQUITY (Note 14):		
Share capital:		
Preferred shares: Authorized - 1,000,000 of €0.01 par value at December 31, 2005 and 2006; Issued and outstanding - None at December 31, 2005 and 2006	-	-
Common shares: Authorized - 30,000,000 of €0.01 par value at December 31, 2005 and 2006; Issued - 12,851,896 and 15,195,646 at December 31, 2005 and 2006, respectively; Outstanding: 12,810,102 and 15,153,852 at December 31, 2005 and 2006, respectively	155	185
Additional paid-in capital	110,490	113,498
Treasury shares	(2,423)	(2,423)
Note receivable from a related party shareholder	(975)	(975)
Accumulated other comprehensive loss	(3,901)	(2,817)
Accumulated deficit	(99,714)	(103,539)
Total shareholders' equity	3,632	3,929
Total liabilities and shareholders' equity	\$ 51,866	\$ 45,619

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

CONSOLIDATED STATEMENTS OF OPERATIONS

U.S. dollars in thousands (except per share data)

	Year ended December 31,		
	2004	2005	2006
Revenues:			
Products	\$ 26,781	\$ 13,295	\$ 10,423
Consulting and other services	21,023	26,109	33,888
Total revenues	47,804	39,404	44,311
Cost of revenues:			
Products	15,274	8,809	6,302
Consulting and other services	11,490	16,037	22,499
Impairment of capitalized software development costs (Note 2i)	901	-	-
Total cost of revenues	27,665	24,846	28,801
Gross profit	20,139	14,558	15,510
Operating expenses:			
Research and development, net (Note 16a)	2,531	2,723	2,451
Selling, marketing, general and administrative	19,260	16,245	13,558
Restructuring costs (Note 1b)	-	1,113	758
Total operating expenses	21,791	20,081	16,767
Operating loss	1,652	5,523	1,257
Financial expenses, net (Note 16b)	2,410	1,788	2,230
Other expenses (income), net	552	(12)	-
Loss before taxes on income	4,614	7,299	3,487
Taxes on income (Note 13)	217	1,798	325
Minority interest in earnings of a subsidiary	4,831	9,097	3,812
	11	2	13
Net loss	4,842	9,099	3,825
Settlement of redeemable shares in a subsidiary (Note 1c)	299	-	-
Net loss to shareholders of Common shares	\$ 5,141	\$ 9,099	\$ 3,825
Basic and diluted net loss per share (Note 2t)	\$ 0.46	\$ 0.76	\$ 0.29
Weighted-average number of shares used in computing basic and diluted net loss per share	11,273	11,982	13,395

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands (except share data)

	Common shares		Additional paid-in capital	Treasury shares	Note receivable from a shareholder	Accumulated other comprehensive loss	Accumulated deficit	Total shareholders' equity
	Shares	Amount						
Balance as of January 1, 2004	10,993,935	\$ 23,788	\$ 82,120	\$ (2,423)	\$ (975)	\$ (3,107)	\$ (85,474)	\$ 13,929
Total comprehensive loss:								
Net loss	-	-	-	-	-	-	(4,842)	(4,842)
Other comprehensive income:								
Unrealized losses on available-for-sale marketable securities, net	-	-	-	-	-	(99)	-	(99)
Foreign currency translation adjustments	-	-	-	-	-	664	-	664
Other comprehensive income								565
Total comprehensive loss								(4,277)
Deemed dividend in conjunction with a settlement of redeemable shares in a subsidiary	-	-	-	-	-	-	(299)	(299)
Employee stock options exercised	5,000	15	5	-	-	-	-	20
Shares issued in conjunction with a settlement of redeemable shares in a subsidiary	750,000	2,093	614	-	-	-	-	2,707
Change in Common shares par value	-	(25,754)	25,754	-	-	-	-	-
Balance as of December 31, 2004	11,748,935	142	108,493	(2,423)	(975)	(2,542)	(90,615)	12,080
Accumulated unrealized losses from available-for-sale marketable securities						\$ (75)		
Accumulated foreign currency translation adjustments						(2,467)		
Accumulated other comprehensive loss						\$ (2,542)		

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands (except share data)

	Common shares		Additional paid-in capital	Treasury shares	Note receivable from a shareholder	Accumulated other comprehensive loss	Accumulated deficit	Total shareholders' equity
	Shares	Amount						
Balance as of January 1, 2005	11,748,935	142	108,493	(2,423)	(975)	(2,542)	(90,615)	12,080
Total comprehensive loss:								
Net loss	-	-	-	-	-	-	(9,099)	(9,099)
Other comprehensive income:								
Unrealized gains on available-for-sale marketable securities, net	-	-	-	-	-	117	-	117
Foreign currency translation adjustments	-	-	-	-	-	(1,476)	-	(1,476)
Other comprehensive loss								(1,359)
Total Comprehensive loss								(10,458)
Stock-based compensation related to warrants issued to consultants	-	-	10	-	-	-	-	10
Employee stock options exercised	19,500	*) -	*) -	-	-	-	-	-
Shares issued to Formula Systems (1985) Ltd	1,041,667	13	1,987	-	-	-	-	2,000
Balance as of December 31, 2005	12,810,102	155	110,490	(2,423)	(975)	(3,901)	(99,714)	3,632
Accumulated unrealized gains from available-for-sale marketable securities						\$ 42		
Accumulated foreign currency translation adjustments						(3,943)		
Accumulated other comprehensive loss						\$ (3,901)		

*) Less than \$ 1 thousand.

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

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands (except share data)

	Common shares		Additional paid-in capital	Treasury shares	Note receivable from a shareholder	Accumulated other comprehensive loss	Accumulated deficit	Total shareholders' equity
	Shares	Amount						
Balance as of January 1, 2006	12,810,102	155	110,490	(2,423)	(975)	(3,901)	(99,714)	3,632
Total comprehensive loss:								
Net loss	-	-	-	-	-	-	(3,825)	(3,825)
Other comprehensive income:								
Unrealized losses on available-for-sale marketable securities, net	-	-	-	-	-	(22)	-	(22)
Foreign currency translation adjustments	-	-	-	-	-	1,106	-	1,106
Other comprehensive income								1,084
Total comprehensive loss								(2,741)
Stock-based compensation related to warrants issued to consultants	-	-	38	-	-	-	-	38
Shares issued	2,343,750	30	2,970	-	-	-	-	3,000
Balance as of December 31, 2006	15,153,852	\$ 185	\$ 113,498	\$ (2,423)	\$ (975)	\$ (2,817)	\$ (103,539)	\$ 3,929
Accumulated unrealized gains from available-for-sale marketable securities						\$ 20		
Accumulated foreign currency translation adjustments						(2,837)		
Accumulated other comprehensive loss						\$ (2,817)		

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2004	2005	2006
Cash flows from operating activities:			
Net loss	\$ (4,842)	\$ (9,099)	\$ (3,825)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	4,250	5,226	5,807
Revaluation of Warrants (Series 1)	(266)	(79)	(46)
Amortization of convertible debt issuance expenses	247	42	230
Amortization of convertible debt discount	348	338	220
Impairment of capitalized software development costs	901	-	-
Loss (gain) on disposal of property and equipment	64	(1)	(75)
Stock-based compensation related to warrants issued to consultants	-	10	37
Decrease (increase) in trade receivables	(412)	885	(2,153)
Decrease in other receivables and prepaid expenses	1,427	2,420	664
Decrease in deferred income taxes, net	-	814	160
Decrease in trade payables	(20)	(583)	(41)
Increase (decrease) in deferred revenues	(257)	1,965	(1,900)
Decrease in other liabilities and accrued expenses	(4,568)	(1,710)	76
Accrued interest on redeemable shares in a subsidiary	64	-	-
Loss (gain) on marketable securities and bonds	67	71	(20)
Minority interests in earnings of a subsidiary	11	2	13
Net cash provided by (used in) operating activities	(2,986)	301	(853)
Cash flows from investing activities:			
Purchase of property and equipment	(442)	(366)	(276)
Increase in capitalized software development costs	(4,750)	(4,323)	(4,699)
Purchase of marketable securities and short-term deposits	(13,622)	(4,683)	(16)
Proceeds from sales of marketable securities and short-term deposits	3,353	10,318	5,319
Proceeds from sale of property and equipment	5	14	2
Investment in equity method investee	-	-	(168)
Other investment	(75)	(17)	-
Net cash provided by (used in) investing activities	(15,531)	943	162

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2004	2005	2006
Cash flows from financing activities:			
Increase (decrease) in short-term bank credit, net	(241)	2,822	(2,962)
Proceeds from employee stock options exercised	20	-	-
Proceeds from issuance of Common shares	-	2,000	2,000
Proceeds from Options (Series A) exercise	1,492	-	-
Payment of convertible debt	-	-	(2,411)
Principal payments of long-term loans	(4,742)	(9,678)	-
Proceeds from long-term bank loans	567	-	-
Convertible debt issuance expenses	(32)	-	-
Net cash used in financing activities	(2,936)	(4,856)	(3,373)
Effect of exchange rate changes on cash and cash equivalents	620	(631)	473
Decrease in cash and cash equivalents	(20,833)	(4,243)	(3,591)
Cash and cash equivalents at the beginning of year	31,775	10,942	6,699
Cash and cash equivalents at the end of year	\$ 10,942	\$ 6,699	\$ 3,108
Supplemental cash flow activities:			
Cash paid during the year for:			
Interest	\$ 2,917	\$ 2,281	\$ 2,132
Income taxes	\$ 176	\$ 144	\$ 221
Non-cash investing and financing activities:			
Purchase of technology usage rights (Note 7b)	\$ 1,695	\$ -	\$ -
Settlement of redeemable shares in a subsidiary (Note 1c)	\$ 11,569	\$ -	\$ -
Conversion of loan to shares	\$ -	\$ -	\$ 1,000

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 1: GENERAL

a. General:

1. The Company is a global provider of information technology ("IT") solutions that modernize business processes to enable insurance and other leading companies to quickly adapt to change. The Company's solutions, sold as customizable software modules, align IT with business demands for speed, flexibility and efficiency. The Company's solutions are supplemented by the Company's technology, methodology and consulting services, which address the complex issues related to the life-cycle of enterprise business applications. The Company's solutions include scalable insurance applications the Company has developed for leading insurance organizations. The Company's service offerings include a standard consulting offering that helps customers make better use of IT in order to achieve its business objectives.

The Company's core technology, Sapiens eMerge™, is a rules-based application development suite which enables rapid solution development for complex mission-critical enterprises to deliver new functionality, achieve legacy modernization and enterprise application integration.

Revenues from a major customer accounted for 16%, 11% and 17% of total revenue in the years ended December 31, 2004, 2005 and 2006, respectively. In addition, in the year ended December 31, 2005, there were additional revenues derived from one more major customer who accounted for another 11% of total revenues.

2. Subsequent to balance sheet date, in June 2007, the Company entered into a private placement investment transaction with several institutional investors, private investors, and its controlling shareholder for an aggregate gross investment amount of \$20 million (excluding finders' fees and out of pocket expenses). As of June 26, 2007, the Company consummated closings for \$17.5 million, \$5 million of which was by its controlling shareholder. The Company issued to the investors an aggregate of 5,833,333 Common Shares, at a price per share of \$3.00. The closing for the remaining \$2.5 million, for an aggregate of 833,333 Common Shares, is expected to occur by June 30, 2007.

In addition, in June 2007, the Company re-purchased an aggregate amount of NIS 15 million nominal value, representing approximately \$3.5 million of the outstanding debentures, that were retired and removed from circulation on the Tel-Aviv Stock Exchange ("TASE").

b. Restructuring costs:

In 2006, the Company recorded restructuring charges of approximately \$0.8 million. The restructuring costs consisted of employee termination benefits associated with the involuntary termination of approximately 25 employees, accounted for in accordance with Statement of Financial Accounting Standard No. 146, "Accounting with Exit Disposal Activities".

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 1: GENERAL (Cont.)

c. Investment in eZoneXchange:

In April 2000, the Company completed a private placement of 600,000 shares of Common stock ("investors' shares") in its wholly-owned subsidiary, eZoneXchange.com, Inc. ("eZoneXchange"), for \$15 million. The investors also received a warrant to purchase an additional 2.25% of the Common stock of eZoneXchange at the same private placement share price of \$25 per share. As part of the transaction, the Company entered into a Put/Call Agreement pursuant to which the investors were granted the right (exercisable in whole or in part) to cause the Company during the put option exercise period (May 4, 2004 through May 3, 2005) to repurchase the investors' shares at the principal amount of the investors' investment plus 5% annual interest accrued thereon from May 4, 2000.

The Put/Call Agreement provided that 50% of the consideration from the investors' shares would be paid in cash and 50% in the Company's Common shares to be valued according to the average closing market price of the Company's Common share over the 14-day trading period preceding the date of issuance of the put consideration. The agreement also included a call option which granted the Company the option to purchase the investors' shares at a price of \$30 in the first two years after the investment date, \$37.5 in the third year, and \$45 in the fourth year. The purchase price would be multiplied by the percentage of shares purchased. The exercise period would last until the earlier of the fifth anniversary of the investment date, an acquisition of, or an IPO by eZoneXchange.

During February 2001, the Company decided to close the operations of eZoneXchange, and repurchased 173,100 of the investors' shares with a cash repayment of \$4.5 million for principal and interest, according to an amendment to the Put/Call Agreement. As a result, the amount of the principal portion of the redeemable shares in a subsidiary to be repaid in cash was decreased by \$4.2 million, net of expenses. In addition, in accordance with the amendment, if the market price of the Company's Common share reaches \$10 per share, the investors will have the right to put 192,333 shares of its eZoneXchange stocks in return for the Company's 363,776 Common shares at a price of \$13.75 per share. No interest is accrued for the amended portion of the investment. The remaining portion of the investment to be repaid in shares (approximately \$2.5 million) would continue to be subject to the original terms of the Put/Call Agreement. The amendment terminated the Company's call option.

As of March 16, 2004, the balance of the Redeemable Shares in a Subsidiary totaled approximately \$11.6 million, including interest accrued through that date.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 1: GENERAL (Cont.)

On March 16, 2004, the Company and the investors signed an agreement according to which, among other terms specified in the agreement, the Company would redeem the remaining eZoneXchange Common shares and eZoneXchange warrants held by the investors by three means:

- Issuance of shares* - Sapiens issued to the investors an aggregate of 750,000 of the Company's Common shares on March 26, 2004.

The investors were granted a right to demand the registration of the Common shares issued such right to be effective no earlier than March 31, 2005. As of the date of these financial statements, the investors did not exercise their demand right to register the Common shares issued.

The Common shares issued were valued at approximately \$2.7 million, based on the Company's stock market price on the date of issuance (March 26, 2004).
- Loan payable* - the Company agreed to pay an amount of \$8.6 million to the investors, bearing annual interest of 7.5% compounded annually on the outstanding principal from January 1, 2004, to be paid semi-annually, with principal payments of \$4.6 million by no later than May 1, 2004, and \$4.0 million by no later than May 1, 2005. The May 1, 2004 payment was made by the Company during May 2004. See below for change in terms of payments of the remaining balance.

The 7.5% interest rate was considered as market interest rate for debt with similar risk, and accordingly, the fair value of the loan payable was determined to be its carrying value.
- Warrants* - the Company issued to the investors warrants to purchase 350,000 Common shares at an exercise price of \$4.00 per Common share of the Company, exercisable at any time and from time to time during the period from issuance to December 31, 2007.

The warrants were valued at \$560 using the Black-Scholes option pricing model with the following assumptions: exercise price \$4.00, fair value of the underlying shares of \$3.65, interest rate 2.5%, dividend yield 0%, and volatility of 60%.

The difference between the fair value of the three components, equal to \$11,868, and the carrying amount of the liability before the modification of \$11,569, in the amount of \$299, was recorded as a Settlement of Redeemable Shares in a Subsidiary deemed dividend in the 2004 consolidated statements of operations.

Pursuant to an evaluation of the terms of the agreement under the provisions of EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and potentially settled in, a Company's Own Stock", the Company has classified all the above derivative financial instruments issued in connection with the private placement as liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 1: GENERAL (Cont.)

On May 29, 2005, the Company entered into an agreement with the investors regarding the payment of the remaining \$4.0 million originally due on May 1, 2005. It was agreed that the Company would pay \$2.0 million on May 1, 2005, \$1.0 million on April 1, 2006 and \$1.0 million on August 1, 2006. The investors may, at their sole discretion, convert all or any portion of the \$1.0 million payable on August 1, 2006 into the Company's Common shares, at a conversion price per each share of \$3.20. In addition, the interest due on the remaining amount was changed to Libor + 2.5% (7.8% as of December 31, 2006). The first installment of \$2.0 million was paid as required at the beginning of May 2005.

In August 2006, the Company entered into an agreement with the investors, whereby the investors received 781,250 Common shares as a conversion of the \$1.0 million payment that was due on April 1, 2006. In addition, the payment of the \$1.0 million payment originally payable on August 1, 2006, was extended to August 1, 2007.

The modification of the loan terms was accounted for as debt extinguishment in accordance with EITF 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments", due to the addition of a conversion option to the debt instrument which was considered substantial. The difference between the fair value of the modified loan and the book value of the original loan was de minimis.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP").

a. Use of estimates:

U.S. GAAP requires management to make certain estimates, judgments and assumptions. Management believes that the estimates, judgments and assumptions upon which it relies, are reasonable based upon information available at the time that these estimates, judgments and assumptions were made. To the extent that there are material differences between these estimates and actual results, the financial statements may be affected.

b. Financial statements in U.S. dollars:

A substantial portion of the financing of the Company's activities is made in U.S. dollars ("dollar"). In addition, a substantial portion of the Company's and certain of its subsidiaries' costs is incurred in dollars. A majority of the revenues of the Company and certain of its subsidiaries is generated in dollars. Company's management believes that the dollar is the primary currency of the economic environment in which the Company and those subsidiaries operate.

Thus, the functional and reporting currency of the Company and these subsidiaries is the dollar.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Accordingly, monetary accounts maintained in currencies other than the dollar are remeasured into dollars in accordance with Statement of the Financial Accounting Standard Board No. 52, "Foreign Currency Translation" ("SFAS No. 52"). All transaction gains and losses of the re-measurement of monetary balance sheet items are reflected in the consolidated statements of operations as financial income or expenses as appropriate.

The financial statements of foreign subsidiaries, whose functional currency is not the dollar, have been translated into dollars. All balance sheet accounts have been translated using the exchange rates in effect at the balance sheet date. Statements of operations amounts have been translated using the average exchange rate for the period. The resulting translation adjustments are reported as accumulated other comprehensive income (loss), in shareholders' equity.

Foreign currency translation differences included in financial expenses (income), net, amounted to approximately \$(159), \$(139) and \$(96), for the years ended December 31, 2004, 2005 and 2006, respectively.

c. Principles of consolidation:

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All intercompany balances and transactions have been eliminated upon consolidation.

d. Cash equivalents:

Cash equivalents are short-term highly liquid investments that are readily convertible to cash, with maturities of three months or less at the date of acquisition.

e. Short-term bank deposits:

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

f. Marketable securities:

Management determines the proper classification of investments in marketable debt at the time of purchase and reevaluates such designations as of each balance sheet date. All securities covered by Statement of Financial Accounting Standard No. 115, "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS No. 115"), were designated as available-for-sale. Accordingly, these securities are stated at fair value, with unrealized gains and losses reported in a separate component of shareholders' equity, accumulated other comprehensive loss. Realized gains and losses on sales of investments, as determined on a specific identification basis, are included in the consolidated statement of operations as financial expenses, net.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

g. Property and equipment, net:

Property and equipment are stated at cost, net of accumulated depreciation using the straight-line method over the estimated useful lives of the assets as follows:

Equipment and furniture	4 - 15 years
Computer equipment and software	3 years
Motor vehicles	7 years
Leasehold improvements	Over the shorter of the term of the lease or the estimated useful life of the asset

h. Impairment of long-lived assets:

The Company's long-lived assets and certain identifiable intangibles are reviewed for impairment in accordance with Statement of Financial Accounting Standard No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("SFAS No. 144"), 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 assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. During 2004, 2005 and 2006, no impairment losses have been identified.

i. Capitalized software development costs:

Research and development costs incurred in the process of developing new products or product improvements, are charged to expense as incurred, net of participation by the Office of the Chief Scientist in Israeli's Ministry of Industry and Trade (the "OCS").

Statement of Financial Accounting Standard No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed" ("SFAS No. 86"), requires capitalization of certain software development costs subsequent to the establishment of technological feasibility. Based on the Company's product development process, technological feasibility is established upon completion of a detailed program design.

Significant costs incurred by the Company and its subsidiaries between the establishment of technological feasibility and the point at which the product is ready for general release, have been capitalized, net of participation by the OCS.

As for finance expenses capitalization, see Note 7a.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Capitalized software costs are amortized by the greater of the amount computed using: (i) the ratio that current gross revenues from sales of the software bear to the total of current and anticipated future gross revenues from sales of that software, or (ii) the straight-line method over three years, which is the estimated useful life of the software product. The Company assesses the recoverability of this intangible asset on a regular basis by determining whether the amortization of the asset over its remaining life can be recovered through undiscounted future operating cash flows from the specific software product sold.

As of December 31, 2004, the unamortized capitalized costs exceeded the net realizable value of this intangible asset by the amount of \$901 and therefore the Company included an impairment of capitalized software development costs in the amount of \$901 which is presented in cost of revenues.

As of December 31, 2006 and 2005, based on its most recent analysis, management believes that no additional impairment of capitalized software development costs exists.

j. Goodwill:

Goodwill represents excess of the costs over the net assets of businesses acquired. Under SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142") goodwill acquired in a business combination should not be amortized. SFAS No. 142 requires goodwill to be tested for impairment at least annually or between annual tests in certain circumstances, and written down when impaired, rather than being amortized as previous accounting standards required. Goodwill is allocated to one reporting unit and fair values are determined using market capitalization.

Through 2006, no impairment losses were identified.

k. Intangible assets:

Intangible assets are stated at cost less accumulated amortization. Amortization is computed using the straight-line method as follows:

Prepaid royalties	15 years
Distribution rights	7 years
Technology, usage rights and other intangible assets	4-8 years

During 2004, 2005 and 2006, no impairment losses have been identified.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

1. Revenue recognition:

Product revenues include software license sales and implementation and customization services (which include the sale of software technology and services).

The Company recognizes revenue from software license sales in accordance with Statement of Position (“SOP”) 97-2, “Software Revenue Recognition,” and SOP 98-9, “Modification of SOP 97-2, Software Revenue Recognition, With Respect to Certain Transactions.” Under SOP 97-2, revenues from software product licenses are recognized upon delivery of the software provided there is persuasive evidence of an agreement, the fee is fixed or determinable and collection of the related receivable is probable and no further obligations exist. Revenues under multiple-element arrangements, which may include software licenses, support and maintenance, and training and consulting services, are allocated to each element based on their respective fair values based on vendor-specific objective evidence. This objective evidence represents the price of products and services when sold separately. When vendor-specific objective evidence of fair value exists for undelivered elements but does not exist for delivered elements of a software arrangement, the Company uses the residual method for recognition of revenues, when all other revenue recognition criteria are met. Under the residual method, the Company defers revenues related to the undelivered elements based on their vendor-specific objective evidence of fair value and recognizes the remaining arrangement fee for the delivered elements.

When vendor-specific objective evidence of fair value for undelivered elements does not exist, revenues from the entire arrangement are recognized over the term of the agreement.

Revenues from support and maintenance agreements are recognized ratably over the term of the agreement, which is typically one year. Revenues from training arrangements are recognized as the services are performed.

The Company generally does not grant a right of return to its customers. When a right of return exists, revenue is deferred until the right of return expires, at which time revenue is recognized provided that all other revenue recognition criteria are met.

Amounts collected prior to satisfying the above revenue recognition criteria are reflected as deferred revenue. Deferred revenue represents deferred maintenance revenue, and to a lesser extent, deferred software license revenues.

Under certain circumstances, license revenue consists of license fees received whereby under the terms of these license agreements the Company’s software is modified to that customer’s specific requirements. Fees are payable upon completion of agreed-upon milestones, such as delivery of specifications and technical documentation. Each license is designed to meet the specific requirements of the particular customer.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Revenues from license fees that involve implementation and customization of the Company's software to customer specific requirements are generated from fixed-price or time-and-materials contracts. Such revenues are recognized in accordance with Statement of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts". Fixed-price contracts revenues are recognized using contract accounting on a percentage-of-completion method, over the period from signing of the license through to customer acceptance, in accordance with the "Input Method" or "Output Method". The amounts of revenues recognized are based on the total license fees under the license agreement and the percentage to completion achieved. According to the "Input Method", the percentage to completion is measured by monitoring progress using records of actual time incurred to date in the project compared to the total estimated project requirement, which corresponds to the costs related to earned revenues. According to the "Output Method", the percentage to completion is determined by using technological or time-based milestones methods.

Estimates of total project requirements are based on prior experience of customization, delivery and acceptance of the same or similar technology, and are reviewed and updated regularly by management. After delivery, if uncertainty exists about customer acceptance of the software, license revenue is not recognized until acceptance. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract. As of December 31, 2006, \$93 of estimated losses were identified. Under time-and-materials contracts, the Company is reimbursed for labor hours at negotiated hourly billing rates.

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

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

Consulting and other services revenues also include training and post-contract maintenance services. Revenues from consulting and training services are recognized ratably over the contractual period or as services are performed.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

m. Equity method investments:

The company's investments in a Company that is held to the extent of 20% or more and with respect to which it has the ability to exercise significant influence over operating and financial policies are accounted for under the equity method. The Company applies Emerging Issues Task Force 99-10, "Percentage Used to Determine the Amount of Equity Method Losses". Accordingly, losses of investee are recognized based on the ownership level of the particular investee security or loans held by the investor.

n. Advertising expenses:

Advertising expenses are charged to the statement of operations as incurred.

o. Government grants:

Royalty-bearing grants from the Government of Israel for the funding of research and development projects are recognized at the time the Company is entitled to such grants on the basis of the related costs incurred, and are recorded as a reduction of research and development costs, or as a reduction of capitalized software development costs.

p. Income taxes:

The Company and its subsidiaries account for income taxes in accordance with Statement of Financial Accounting Standard No. 109, "Accounting for Income Taxes" ("SFAS No. 109").

This Statement prescribes the use of the asset and liability method, whereby deferred tax assets and liability account balances are determined based on the differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company and its subsidiaries provide a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value.

q. Concentrations of credit risk:

Financial instruments that potentially subject the Company and certain of its subsidiaries to concentrations of credit risk consist principally of cash and cash equivalents, marketable securities and trade receivables.

The Company's cash and cash equivalents are invested in deposits with major international financial institutions. Such deposits in the United States may be in excess of insured limits and are not insured in other jurisdictions. 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.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company's trade receivables are generally derived from sales to large and solid organizations located mainly in Europe, North America and Israel. The Company performs ongoing credit evaluations of its customers and has established an allowance for doubtful accounts based upon factors surrounding the credit risk of specific customers and other information. In certain circumstances, the Company may require letters of credit, other collateral or additional guarantees. From time to time, the Company sells certain of its accounts receivable to financial institutions, within the normal course of business. Where receivables are sold without recourse to the Company, the relevant receivable is de-recognized and cash recorded. Where receivables are sold with full or partial recourse to the Company, the receivable is not de-recognized and a liability reflecting the obligation to the financial institution is recorded within financial debts until the Company's liability is discharged through the financial institution receiving payment from the customer.

No off-balance sheet concentrations of credit risk exist.

r. Fair value of financial instruments:

The estimated fair value of financial instruments has been determined by the Company using available market information and valuation methodologies. Considerable judgment is required in estimating fair values. Accordingly, the estimates may not be indicative of the amounts the Company could realize in a current market exchange. The carrying amounts of cash and cash equivalents, trade accounts receivable, short-term bank credit and trade accounts payable approximate their fair values due to the short-term maturity of such instruments. The fair value for marketable securities is based on quoted market prices and does not significantly differ from a carrying amount.

The fair value of the convertible debentures with a carrying value in the amount of \$16,175 as of December 31, 2006 according to the quoted price in the TASE is \$12,357. The fair value of the traded warrants does not significantly differ from their carrying amount.

s. Derivatives and hedging:

The Company accounts for derivatives and hedging based on Financial Accounting Standards Board Statement No. 133, "Accounting for Derivative Instruments and Hedging Activities" as amended ("SFAS No. 133"). SFAS 133 requires companies to recognize all of its derivative instruments on the balance sheet at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship.

The Company enters into forward exchange contracts to hedge certain transactions denominated in foreign currencies. The purpose of the Company's foreign currency hedging activities is to protect the Company from risk that the eventual dollar cash flows from international activities will be adversely affected by changes in the exchange rates. The Company's forward contracts did not qualify as hedging instruments under SFAS No. 133.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Changes in the fair value of forward contracts are reflected in the consolidated statements of operations as financial income or expense.

In 2004 and 2005, the Company entered into forward currency agreements in the amount of \$1.5 million, that effectively convert a portion of its floating currency liabilities to a fixed rate basis for a 3 month period, thus reducing the impact of the currency changes on the Company's cash flow. The agreements were settled in 2005 and 2006, resulting in a total gain of \$67 and \$19.5, respectively, presented in the statements of operations as financial income.

t. Basic and diluted net loss per share:

Basic net loss per share is computed based on the weighted average number of Common shares outstanding during each year. Diluted net earnings per share is computed based on the weighted average number of Common shares outstanding during each year, plus dilutive potential Common shares considered outstanding during the year, in accordance with Statement of Financial Accounting Standard No. 128, "Earnings Per Share" ("SFAS No. 128").

In 2004, 2005 and 2006, all outstanding stock options, convertible subordinate notes, convertible debt and warrants have been excluded from the calculation of the diluted net loss per Common share because all such securities were anti-dilutive for the period presented. The total weighted average number of shares related to the outstanding stock options, convertible subordinated notes, convertible debt and warrants excluded from the calculations of diluted net loss per share was 103,409, 69,207 and 59,000 for the years ended December 31, 2004, 2005 and 2006, respectively.

u. Stock-based compensation:

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" ("SFAS 123 (R)"), which is a revision of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123") which requires the measurement and recognition of compensation expense based on estimated fair values for all shared based payments awards made to employees and directors. In March 2005, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 107 ("SAB 107") relating to SFAS 123 (R). The Company has applied the provisions of SAB 107 in its adoption of SFAS 123 (R).

SFAS 123 (R) requires companies to estimate the fair value equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the awards that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company's consolidated statement of operations. Prior to the adoption of SFAS 123 (R), the Company accounted for equity based awards under the fair value recognition provisions of SFAS 123.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company adopted SFAS 123 (R) using the Modified Prospective Method. Under that transition method, compensation cost recognized in the year ended December 31, 2006, included: (a) compensation cost for all shared-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123, and (b) compensation cost for all shared-based payments granted subsequent to January 1, 2006 based on the grant-date fair value estimated in accordance with the provisions of the SFAS 123 (R). Results for prior periods have not been restated.

Beginning on the date of adoption of SFAS 123 (R), forfeitures are estimated based on historical experience and other factors; previously, forfeitures were recorded as they occurred.

On December 28, 2005, the Company's Compensation Committee of the board of directors approved an acceleration of the vesting of all unvested stock options held by current employees, including executive officers and directors. All of the options were considered out-of-the-money since the stated option exercise price was greater than the closing price of the company Common stock on the day the Compensation Committee approved the acceleration (\$1.50). Unvested options to purchase approximately 1.7 million shares became exercisable as a result of the vesting acceleration. The accelerated vesting was effective as of December 28, 2005.

The Company's decision to accelerate the vesting of those options was based primarily upon the issuance of SFAS No. 123(R). The Company believes that the acceleration of vesting of those options will enable the Company to avoid recognizing stock-based compensation expense associated with these options in future periods. Additional purpose of the acceleration was to make the options more attractive to the recipients.

The vesting acceleration did not result in the recognition of additional compensation expense in the year ended December 31, 2005. The pro-forma results presented in the table below include approximately \$1.9 million of compensation expense for the year ended December 31, 2005 resulting from the vesting acceleration.

In 2006, the Company granted 20,000 stock options to employees.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The Company estimates the fair value of stock options on the grant date using the Black-Scholes option-pricing model with the following weighted average assumptions:

	Year ended December 31, 2006
Expected term	3 years
Dividend yield	0%
Expected volatility	67.4%
Risk-free interest rate	6%
Estimated forfeitures	0%

The risk-free interest rate assumption is based on the yield from U.S. Treasury zero-coupon bonds with an equivalent term as of the Company's employee stock options. The dividend yield assumption is based on the Company's historical and expectation of future dividend payouts and may be subject to substantial change in the future. The expected term of the options represents the period of time that the options are expected to be outstanding and is based on the Company's historical information, with respect to employee options exercised. The Company used its historical volatility for calculating volatility in accordance with SFAS 123 (R). Estimated forfeitures are based on actual historical pre-vesting forfeitures.

Stock-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense on a straight-line basis over the requisite service period for each of the awards.

For options granted prior to January 1, 2006, the Company accounted for its stock-based employee compensation plans using the intrinsic-value method of accounting set forth in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), but disclosed the pro forma effects on net loss and net loss per share had the fair value of the options been expensed. In accordance with APB 25 and related interpretations, compensation expense for stock options is recognized in income based on the excess, if any, of the fair value of the share at the grant date of the award or other measurement date over the amount an employee must pay to acquire the share.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The fair value of each option granted was estimated at the day of grant using a Black-Scholes options pricing model with the following weighted average assumptions:

	2004	2005
Dividend yield	0%	0%
Expected volatility	65%	83%
Risk-free interest	3.74%	4.41%
Expected life of up to	2.5 years	6.9 years

Pro forma information under SFAS No. 123 is as follows:

	Year ended December 31,	
	2004	2005
Net loss to shareholders of Common shares - as reported	\$ 5,141	\$ 9,099
Less - stock-based employee compensation - intrinsic value	-	-
Add - stock-based employee compensation - fair value	637	2,587
Pro forma net loss	\$ 5,778	\$ 11,686
Basic and diluted net loss per share - as reported	\$ 0.46	\$ 0.76
Pro forma basic and diluted net loss per share	\$ 0.51	\$ 0.98

The Company applied SFAS No. 123 and EITF No. 96-18, "Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services," with respect to options and warrants issued to non-employees. SFAS No. 123 requires the use of option valuation models to measure the fair value of the options and warrants at the measurement date as defined in EITF No. 96-18.

v. Accrued severance pay:

The liability of the Company's subsidiaries in Israel for severance pay 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. Employees are entitled to one month's salary for each year of employment or a portion thereof. The liability for all of its employees in Israel is fully provided by monthly deposits with insurance policies and by an accrual. The value of these policies is recorded as an asset in the Company's consolidated balance sheet.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The deposited funds include profits accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfillment of the obligation pursuant to Israeli severance pay law or labor agreements. The value of the deposited funds is based on the cash surrendered value of these policies, and includes immaterial profits.

Severance expense for the years 2004, 2005 and 2006 amounted to approximately \$893, \$547 and \$773 respectively.

In addition, the Company has various defined contribution plans for employees of its subsidiaries around the world. Most of the plans are those required according to the laws of the country in which the subsidiary operates. Contributions made under the plans are invested with financial institutions. Benefits under the plans are based on contributions from employees and the Company and earnings on insurance contracts or other investment instruments in which the contributions are invested.

Expense for contributions made to these plans was \$570, \$518 and \$568 for 2004, 2005 and 2006, respectively.

w. Recently issued Accounting Standards:

In September 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 157, "Fair Value Measurements". This Standards defines fair values, establishes a framework for measuring fair values in generally accepted accounting principles and expands disclosures about fair values measurements. SFAS No. 157 is affective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Management believe this Standard will not have a material effect on its consolidated financial statements.

In June 2006, the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN 48"), an interpretation of SFAS No. 109, "Accounting for Income Taxes". FIN 48 prescribes a comprehensive model for how companies should recognize, measure, present and disclose in their financial statements uncertain tax positions taken or expected to be taken on a tax return. Under FIN 48, tax positions shall initially be recognized in the financial statements when it is more-likely-than-not that the position will be sustained upon examination by the tax authorities. Such tax position shall initially and subsequently be measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon ultimate settlement with the tax authority assuming full knowledge of the position and all relevant facts. FIN 48 also revises disclosure requirements to include an annual tabular roll forward of unrecognized tax benefits. The provisions of this interpretation are required to be adopted for fiscal periods beginning after December 15, 2006. The Company will be required to apply the provisions of FIN 48 to all tax positions of FIN 48 upon initial adoption with any cumulative effect adjustments to be recognized as an adjustment to retained earnings. The adoption of FIN 48 does not have a material impact on the Company's financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (Cont.)

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" ("SFAS No. 159"), which permits companies to choose to measure certain financial instruments and other items at fair value that are not currently required to be measured at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. The Company has not yet determined the effect that the adoption of SFAS No. 159 will have on its consolidated financial statements.

x. Reclassification:

Certain amounts from prior years have been reclassified to conform to current period presentation.

NOTE 3: MARKETABLE SECURITIES

The Company invests in marketable securities, which are classified as available-for-sale and are carried at fair value. The following is a summary of marketable debt securities:

	December 31,							
	2005				2006			
	Amortized cost	Unrealized gains	Unrealized losses	Market value	Amortized cost	Unrealized gains	Unrealized losses	Market value
	U.S. dollars in thousands							
Available-for-sale:								
Government debentures	\$ 70	\$ 10	\$ -	\$ 80	\$ -	\$ -	\$ -	\$ -
Commercial debentures	5,225	72	(40)	5,257	12	20	-	32
Total available-for-sale marketable securities	\$ 5,295	\$ 82	\$ (40)	\$ 5,337	\$ 12	\$ 20	\$ -	\$ 32

During 2006, the Company received proceeds from sales of marketable securities in the amount of \$5,529 and realized gains of \$20 presented in financial expenses, net.

The available-for-sale investments as of December 31, 2005 and 2006 mature in one to five years.

NOTE 4: TRADE RECEIVABLES

The Company's net trade receivables are composed of accounts receivable in the amounts of \$4.4 million and \$7.0 million as of December 31, 2005 and 2006, and unbilled receivables in the amounts of \$3.9 million and \$4.0 million as of December 31, 2005 and 2006, respectively.

Bad debt expense totaled \$231, \$213 and \$562 for the years ended December 31, 2004, 2005 and 2006, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 5: OTHER RECEIVABLES AND PREPAID EXPENSES

	December 31,	
	2005	2006
Sales and other taxes receivable	\$ 445	\$ 204
Prepaid expenses	734	435
Deferred income taxes	241	907
Government grants	65	62
Employees receivables	21	23
Other	14	58
	\$ 1,520	\$ 1,689

NOTE 6: PROPERTY AND EQUIPMENT, NET

	Cost		Accumulated depreciation	
	December 31,			
	2005	2006	2005	2006
	U.S. dollars in thousands			
Equipment and furniture	\$ 2,176	\$ 2,383	\$ 1,734	\$ 1,992
Computer equipment and software	10,777	11,895	10,080	11,323
Motor vehicles	117	151	110	126
Leasehold improvements	2,072	2,296	1,502	1,790
	\$ 15,142	\$ 16,726	\$ 13,426	\$ 15,231

Depreciation expense totaled \$1,011, \$876 and \$690 for the years 2004, 2005 and 2006, respectively.

As for pledges see Note 12.

NOTE 7: OTHER ASSETS

- a. Amortization expense for capitalized software development costs for 2004, 2005 and 2006, were \$3.0 million, \$3.8 million and \$4.6 million, respectively. Amortization expense is included in cost of revenues.

See Note 2(i) for impairment of capitalized software development costs in 2004.

In 2005 and 2006, \$113 and \$523 respectively, of interest expense was capitalized to software development costs.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 7: OTHER ASSETS (Cont.)

b. Other assets, net, are comprised of the following:

	Cost		Accumulated amortization		Other assets, net	
	December 31,					
	2005	2006	2005	2006	2005	2006
Prepaid royalties	\$ 2,074	\$ 2,074	\$ 1,759	\$ 1,890	\$ 315	\$ 184
Technologies and usage rights (1)	1,745	1,586	796	947	949	639
Intangible assets and other	156	-	156	-	-	-
Deferred debt issuance costs (2)	1,528	1,528	304	534	1,224	994
	<u>\$ 5,503</u>	<u>\$ 5,188</u>	<u>\$ 3,015</u>	<u>\$ 3,371</u>	<u>\$ 2,488</u>	<u>\$ 1,817</u>

In addition, other assets include:

Severance pay fund		1,015	1,099
Long-term deposits		246	275
Investment in equity method investee		-	168
Other		93	91
		<u>1,354</u>	<u>1,633</u>
		<u>\$ 3,842</u>	<u>\$ 3,450</u>

(1) In September 2004, the Company purchased the technologies underlying the INSIGHT™ for Closed Books solution, for a minimum amount of approximately \$1.6 million to be paid in 4 annual installments, beginning December 31, 2005. Under certain conditions set forth in the agreement, the consideration may increase in the future, based on the number of policies administered by such solution. Subsequent to balance sheet date the December 31, 2006 payment of \$392 was paid.

The technologies are amortized over a 4 year period, which is the estimated useful life of the technologies.

(2) Related to the issuance of Debentures, Options (Series A) and Warrants (Series 1) (see Note 9b).

Amortization of other assets charged to expenses was \$148, \$623 and \$791 for 2004, 2005 and 2006, respectively.

As for impairments of long-lived assets, see Note 2h.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 7: OTHER ASSETS (Cont.)

- c. Estimated amortization expense of prepaid royalties, technologies and usage rights, distribution rights and other intangible assets for the years ending:

December 31,	
2007	765
2008	707
2009	345
	1,817

NOTE 8: OTHER LIABILITIES AND ACCRUED EXPENSES

	December 31,	
	2005	2006
Employee and related payroll accruals	\$ 2,680	\$ 3,003
Sales and other taxes payable	753	733
Accrued royalties to the OCS (Note 11a)	1,014	1,685
Accrued expenses and other liabilities	2,295	1,949
	\$ 6,742	\$ 7,370

NOTE 9: DEBT

- a. Short-term bank credit:

As of December 31, 2006, the Company and its subsidiaries have a revolving credit line facility for borrowings of up to a total of \$9.2 million, available until June 30, 2007. As of December 31, 2006, the Company has an unutilized credit line of \$2.4 million. Under the terms of these credit line agreements, the Company and several of its subsidiaries recorded floating charges in favor of the banks over all the assets of Sapiens Technologies (1982) Ltd. and Sapiens Israel Software Systems Ltd. The Company also issued cross guaranties in support of the credit line facilities. Additionally, the Company is required to maintain certain financial ratios and results. In 2006, the Company fulfilled the covenant contained in its loan agreements pertaining to maintenance of cumulative, quarterly earnings at certain levels.

The Company is currently negotiating the extension of the credit line facility for an additional year.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 9: DEBT (Cont.)

	Linkage	Weighted average interest		December 31,	
		December 31,		2005	2006
		2005	2006	2005	2006
		%			
Credit lines	NIS *)	5.9	6.7	\$ 1,830	\$ 4,728
Short-term loans	U.S. dollar	5.6	7.3	10,120	4,570
				\$ 11,950	\$ 9,298

*) New Israeli Shekel, including immaterial amounts linked to other currencies.

In December 2006, the Company entered into loan agreement with Bank Leumi Le-Israel ("Bank Leumi") whereby the Company borrowed an aggregate amount of approximately \$2.5 million. The Company used the proceeds of this loan to make the December 2006 principal and interest payment of the Debentures. The loan was secured by a guarantee granted to Bank Leumi by the Company's principal shareholder. The loan bears an annual interest rate of 6.5% and is due on August 30, 2007.

b. Convertible Debentures, Warrants and Options:

During December 2003, the Company completed an offering of securities in the Tel-Aviv Stock Exchange ("TASE") in Israel, resulting in gross proceeds of NIS 75.2 million (approximately \$17.1 million). The price per unit was NIS 752 (approximately \$171.14) with 100,000 units sold. Each of the units consists of 800 Debentures (Series A), two Options (Series A) exercisable into Debentures (Series A) and six Warrants (Series 1) exercisable into Common shares of the Company.

The Debentures (Series A) are linked to the U.S. dollar and bear annual interest at the rate of 6.0%, payable on the 5th of June and the 5th of December each year commencing on June 5, 2004 and ending on December 5, 2009. According to the original terms, principal is payable in four installments on the 5th of December of the years 2006-2009. During the period beginning 45 days after the registration of the Debentures (Series A) for trading on TASE and ending November 21, 2009, the Debentures (Series A) are convertible into Common shares at a conversion rate of one Common share per each NIS 27 (approximately \$6.14) amount of the Debentures, linked to the NIS/dollar exchange rate. The conversion rate is subject to standard anti-dilution provisions, which have no accounting implications (stock dividend, stock split, reverse split). The Debentures (Series A) are unsecured.

Each Option (Series A) was exercisable into 100 Debentures (Series A) no later than March 3, 2004 at an exercise price of NIS 96 (approximately \$21.85). Through March 3, 2004, 179,663 Options (Series A) were exercised into Convertible Debentures, with a total exercise price of approximately \$3.8 million. 105,225 of the Options (Series A), with a total exercise price of approximately \$2.3 million, were exercised by one of the Company's subsidiaries in Israel. The remaining balance expired.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 9: DEBT (Cont.)

Each Warrant (Series 1) is exercisable into one Common share of the Company during the period beginning 45 days after the registration of the Debentures (Series A) for trading on TASE and ending November 21, 2007 at an exercise price of NIS 27 (approximately \$6.14) linked to the U.S. dollar.

As of December 31, 2006, 600,000 Warrants (Series 1) are outstanding.

The Convertible Debentures and Warrants are, and the Options were, traded on TASE only. Any Common shares issued upon conversion of the Debentures (Series A) or exercise of the Warrants (Series 1) will be traded on both TASE and NASDAQ. The offering was made to the public in Israel only in accordance with Israeli securities laws. It was not open to persons residing in the United States or to other U.S. persons (other than distributors). The securities offered have not been registered under the Securities Act of 1933, as amended, and may not be offered or sold in the United States absent registration under such Act or an applicable exemption from registration.

In accordance with APB No. 14, "Accounting for Convertible debt and Debt Issued with Stock Purchase Warrants", EITF 98-5, "Accounting for Convertible Securities with Beneficial Conversion features or Contingently Adjustable Conversion Ratios", and EITF 00-27, "Application of issue No. 98-5 to Certain Convertible Instruments" ("EITF 00-27"), a portion of the proceeds of debt securities issued with detachable warrants was allocated to the Options (Series A) and the Warrants (Series 1), based on the relative fair values of the securities at time of issuance. Amounts allocated to the Options (Series A) and the Warrants (Series 1) are accounted for as liabilities, in accordance with EITF 00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled In a Company's Own Stock" ("EITF 00-19"), and are marked to market, based on their fair values in the TASE at each reporting date, against financial income (expense).

Pursuant to an evaluation of the terms of the agreement under the provisions of EITF 00-19, the Company has classified all the above derivative financial instruments issued in connection with issuance of the convertible debentures, Warrants and Options as liabilities.

In August, 2006 the Company modified the terms of the first payment of the Debentures (Series A) that was due in December, 2006 as follows: (a) 50% of the first payment amount, approximately \$2.4 million, will be deferred to December 5, 2009 (the last day of payment of the principal on the debentures), and (b) with respect to other 50% of the first payment amount, the Company can choose from the following alternatives, in its sole discretion: (1) to convert such amount on December 5, 2006 into Company's Common shares, at a conversion price per share of \$1.28, which reflects the average closing price for the 10 day period prior to July 17, 2006, or (2) to pay the approximately \$2.4 million amount to the debenture holders.

On December 5, 2006, an amount of approximately \$2.4 million was paid to the debenture holders.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 9: DEBT (Cont.)

The modification of the terms of the first payment of the Debentures (Series A) was accounted for in accordance with FAS 15 "Accounting by Debtors and Creditors for Troubled Debt Restructurings". Accordingly, the Company calculated the new effective borrowing rate of the debt, which effected the amortization rate of the unamortized discount and unamortized issuance expenses as of the date of the restructuring.

As of December 31, 2005 and 2006, the long-term outstanding balance of the convertible debt and warrants are as follows:

	December 31,	
	2005	2006
Debentures:		
Par value	\$ 22,295	\$ 19,508
Deemed discount, net *)	(1,065)	(812)
	21,230	18,696
Less -debentures purchased by one of the Company's subsidiaries	(2,864)	(2,521)
Warrants (Series 1)	117	71
Less – current maturities of debentures	(4,464)	(4,450)
	\$ 14,019	\$ 11,796

*) The deemed discount is amortized over a period of 72 months, the term of the debentures (Series A), using the effective interest method. Amortization of the deemed discount charged to expenses was \$338 and \$254 for 2005 and 2006, respectively.

The share issuance expenses, which are classified to other assets (Note 7b), are amortized over the term of the Debentures (Series A), using the effective interest rate method.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 10: OTHER LONG-TERM LIABILITIES

	Linkage	Interest	Maturity	December 31,	
				2005	2006
		%			
Loan payable eZoneXchange *)	U.S. Dollar	Libor+2.5	Through 8/2007	\$ 2,000	\$ 1,000
Other long-term liability **)	GBP	-	Through 12/2008	1,366	1,291
Other long-term debt	Japanese Yen	2.1-2.8	2/2006	8	-
				<u>3,374</u>	<u>2,291</u>
Less - current maturities of long-term liabilities				(2,698)	(1,854)
				676	437
Accrued severance pay				768	924
Warrants issued as part of a settlement of redeemable shares in a subsidiary (Note 1c)				75	-
Minority interest				65	78
				<u>\$ 1,584</u>	<u>\$ 1,439</u>

*) See Note 1c.

***) See Note 7(b)(1).

Long-term debt maturities in 2008 are \$437.

Interest expense was \$1.0 million, \$0.8 million and \$0.3 million for 2004, 2005 and 2006, respectively.

NOTE 11: COMMITMENTS AND CONTINGENT LIABILITIES

- a. Sapiens Technologies (1982) Ltd. ("Technologies"), a subsidiary incorporated in Israel, partially finances its research and development expenditures under programs sponsored by the OCS for the support of certain research and development activities conducted in Israel.

In exchange for participation in the programs by the OCS, the Company agreed to pay 3%-3.5% of total net consolidated license and maintenance revenue and 0.35% of the net consolidated consulting services revenue related to the software developed within the framework of these programs. The royalties will be paid up to a maximum amount equaling 100%-150% of the grants provided by the OCS, linked to the dollar, and for grants received after January 1, 1999, bear annual interest at a rate based on LIBOR. Repayment of such grants is not required in the event that there are no sales of products developed within the framework of such funded programs.

Royalties paid or accrued amounted to \$1.6 million, \$1.1 million and \$0.5 million in 2004, 2005 and 2006, respectively, and are included in cost of revenues.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 11: COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

As of December 31, 2006, the Company had a contingent liability to pay royalties of approximately \$9.5 million.

- b. The Company and its subsidiaries lease various office equipment, office space, and motor vehicles through operating leases. Future minimum lease payments for the next five years and thereafter are as follows:

	Operating leases	
2007	\$	2,581
2008		2,360
2009		1,846
2010		1,585
2011 and thereafter		866
<u>Total</u> future minimum lease payments	\$	9,238

Rent expense for the years 2004, 2005 and 2006 was \$2.4 million, \$2.2 million and \$2.3 million, respectively.

- c. In July 2006, the city council of Rehovot, Israel, notified the Company of (a) an increase in the annual property taxes payable by the Company and (b) a claim for \$895 for property taxes due for the years 2000 through 2006. In March 2007, the Company filed an appeal against the increase and the claim for taxes due for previous years. Based on the opinion of legal counsel, the Company believes that it is probable that the amount being claimed retroactively (for the period of 2000 through 2006) will be cancelled. The Company does not believe that the claim reflects a probable loss contingency, in accordance with Statement of the Financial Accounting Standard Board No. 5, "Accounting for Contingencies".

A former employee has threatened to sue the Company for the amount that such employee was required to pay to the Israel Tax Authorities as the result of his exercise of stock options. In the event that such employee would decide to file a claim in court, the Company believes that such threatened claim lacks merit and the Company, based on the advice of its legal counsel, believes that it has a reasonable defense. The Company does not believe that the claim reflects a probable loss contingency, in accordance with Statement of the Financial Accounting Standard Board No. 5, "Accounting for Contingencies".

The Company is a party to various other legal proceedings and claims that arise in the ordinary course of business. The total aggregate amount of such proceeding and claims, together with the above mentioned claim, is approximately \$720. The Company does not believe that the claims reflect a probable loss contingency, in accordance with Statement of the Financial Accounting Standard Board No. 5, "Accounting for Contingencies".

- d. As for tax assessments, see Note 13(c).
- e. See Note 7(b)(1) for a contingent liability related to a purchased technology.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 12: SECURITY INTERESTS AND PLEDGES

The Company and several of its subsidiaries granted floating charges to certain financial institutions and issued cross guarantees in support of the credit facilities described in Note 9a above.

The Company's leased assets are pledged to the finance companies that provided the lease financing and the banks providing credit lines. The pledges are for various terms depending on the asset leased.

The Company has provided bank guarantees in the amount of approximately \$328 as security for the rent to be paid for its leased offices in Israel. The lease is valid for approximately six years ending 2010. If the Company were to breach certain terms of its lease, the lessor could demand that the banks providing the guarantees pay amounts claimed to be due.

The Company has provided bank guarantees in the amount of approximately \$2.3 million as security for the performance of various contracts with customers. If the Company were to breach certain terms of such contracts, the customers could demand that the banks providing the guarantees pay amounts claimed to be due.

The Company has provided guarantees to banks in support of the credit facilities extended to two subsidiaries. In the case of the Company's U.S. subsidiary, the guarantee is for \$100; in the case of the Company's U.K. subsidiary, the guarantee is for £100. Each such guarantee is provided for the term of the credit facility, such term being generally one year. If a subsidiary whose credit line has been guaranteed by the Company were to breach certain terms of its credit agreement, the lending bank could demand that the Company pay amounts claimed to be due. Subsequent to balance sheet date, in January 2007, the Company cancelled the \$100 guarantee, which was provided for its U.S. subsidiary.

NOTE 13: TAXES ON INCOME

a. Net operating losses carryforward:

At December 31, 2006, the Company's subsidiary in the U.S. had net operating loss carryforward for U.S. federal income tax purposes of approximately \$5.8 million, and tax credits of approximately \$200 which are available to offset future federal taxable income and expire in 2009 to 2023.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 13: TAXES ON INCOME (Cont.)

In addition, the Company had net operating losses carryforwards relating to non-U.S. subsidiaries totaling approximately \$52 million, which is available to offset future taxable income. Generally, a majority of such amounts have no expiration date. However, in some cases, amounts expire in 2007 to 2011.

b. Israeli income tax:

Sapiens Technologies (1982) Ltd. ("Technologies"), an Israeli subsidiary of the Company, has been granted "Approved Enterprise" status for six investment programs approved in 1984, 1991, 1993, 1995, 1998 and 2000, by the Israeli Government under the Law for Encouragement of Capital Investments, 1959 ("the Capital Investments Law").

Undistributed Israeli income derived from the "Approved Enterprise" programs entitle Technologies to a tax exemption for a period of two to four years and to a reduced tax rate of 10% - 25% for an additional period of three to eight years (depending on the level of foreign-investment in Technologies). These tax benefits are subject to a limitation of the earlier of twelve years from commencement of operations, or fourteen years from receipt of the approval. This limitation does not apply for the years of tax exemption. Technologies completed the implementation of the 1984, 1991, 1993, 1995, 1998 and 2000 investment programs. As of December 31, 2005, the Investment Center has granted final approval for the implementation of the 1995 and 1998 plans. Technologies has used all the tax benefits under the 1984, 1991 and 1993 plans and is entitled for additional benefits under the 1995 plan (the benefits period commenced in 1998 and will expire in December 2008). The benefits have not yet commenced for the 1998 and the 2000 plans. The law also grants entitlement to claim accelerated depreciation on machinery and equipment used by the "Approved Enterprise", during the first five years, which the Company claims.

Income from sources other than the "Approved Enterprise" during the benefit period is subject to tax at the regular corporate tax rate of 34% in 2005, 31% in 2006, 29% in 2007, 27% in 2008, 26% in 2009, and 25% in 2010 and thereafter.

The entitlement to the above benefits is conditional upon the Company fulfilling the conditions stipulated by the Capital Investments Law, regulations published thereunder and the Instruments of approval for the specific investments in "Approved Enterprises".

In the event of failure to comply with these conditions, the benefits may be cancelled and the Company may be required to refund the amount of the benefits, in whole or in part, including interest. In the event of a distribution of such tax-exempt income including, among other things, a cash dividend, the Company will be required to pay tax at the rate of 10%-25% on the gross amount distributed. In addition, these dividends will be subject to a 15% withholding tax.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 13: TAXES ON INCOME (Cont.)

Technologies have decided not to declare dividends out of such tax-exempt earnings. Accordingly, no deferred income taxes have been provided on earnings attributable to Technologies' "Approved Enterprise".

On April 1, 2005, an amendment to the Capital Investments Law came into effect ("the Amendment") and has significantly changed the provisions of the Capital Investments Law. The Amendment limits the scope of enterprises which may be approved by the Investment Center by setting criteria for the approval of a facility as a Privileged Enterprise, such as provisions generally requiring that at least 25% of the Privileged Enterprise's income will be derived from export. Additionally, the Amendment enacted major changes in the manner in which tax benefits are awarded under the Capital Investments Law so that companies no longer require Investment Center approval in order to qualify for tax benefits.

However, the Capital Investments Law provides that terms and benefits included in any certificate of approval already granted will remain subject to the provisions of the law as they were on the date of such approval. Therefore, the Company's existing Approved Enterprise will generally not be subject to the provisions of the Amendment.

As a result of the Amendment among others, tax-exempt income generated under the provisions of the new law, will subject the Company to taxes upon distribution or liquidation and the Company may be required to record deferred tax liability with respect to such tax-exempt income. As of December 31, 2006, the Company did not generate income under the Amendment.

Commencing 2005, the Company's Israeli subsidiaries have elected to file their tax returns under the Israeli Income Tax Regulations 1986 (Principles Regarding the Management of Books of Account of Foreign Invested Companies and Certain Partnerships and the Determination of Their Taxable Income). Such an election obligates the Company's Israeli subsidiaries for the first three years. Accordingly, commencing 2005, results for tax purposes are measured in terms of U.S. dollars.

c. Tax assessments:

Technologies and some of the Company's group entities have final tax assessments through the year 1999.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 13: TAXES ON INCOME (Cont.)

d. Deferred income taxes:

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company and its subsidiaries' deferred tax assets are as follows:

	December 31, 2005		December 31, 2006	
	Current	Non-current	Current	Non-current
Gross deferred tax assets	\$ 241	\$ 14,603	\$ 907	\$ 15,814
Less - valuation allowance	-	(11,030)	-	(13,067)
Net deferred tax asset	\$ 241	\$ 3,573	\$ 907	\$ 2,747

During the year ended December 31, 2006, the Company and its subsidiaries have increased the deferred income taxes assets resulting from tax loss carryforwards and other tax credits by \$1,877 and the related valuation by \$2,037. Management currently believes that it is more likely than not that the deferred income taxes regarding the loss carryforwards and other temporary differences, on which a valuation allowance has been provided, will not be realized in the foreseeable future.

Provisions for income tax expense are comprised of the following:

	Year ended December 31,		
	2004	2005	2006
Current (foreign)	\$ 217	\$ 198	\$ 165
Deferred (foreign)	-	*) 1,600	160
	\$ 217	\$ 1,798	\$ 325

*) Including the write off of tax advances in the amount of \$783.

The Company's entire provision for taxes on income relates to operations in jurisdictions other than the Netherlands Antilles. The effective income tax rate varies from period to period because each jurisdiction in which the Company and its subsidiaries operate has its own system of taxation (not only with respect to the nominal rate, but also with respect to the allowance of deductions, credits and other benefits).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 13: TAXES ON INCOME (Cont.)

The main reconciling items from the statutory tax rate of the Company to the effective tax rate is the non-recognition of tax benefits from accumulated net operating losses carryforward among the various subsidiaries worldwide due to the uncertainty of the realization of such tax benefits, an increase in the valuation allowance, and a write off of tax advances

- e. Loss before taxes on income is comprised as follows:

	Year ended December 31,		
	2004	2005	2006
Domestic	\$ 5,019	\$ 2,683	\$ 2,450
Foreign	(405)	4,616	1,037
	\$ 4,614	\$ 7,299	\$ 3,487

NOTE 14: SHAREHOLDERS' EQUITY

- a. In August 2004, the Company's shareholders approved amendments to the Company's Articles of Association, and thereby (a) increased the number of authorized Common shares to 30,000,000, while the number of authorized preferred shares remained 1,000,000, and (b) changed the par value of all authorized shares to one Eurocent (€0.01) each, from two and three tenths Euros (€2.30) each, such that the total nominal capital of the Company became €310 thousand.
- b. On June 27, 2005, the Company entered into a share purchase agreement with Formula Systems (1985) Ltd. ("Formula"), whereby Formula invested \$2.0 million in the Company and the Company issued 1,041,667 Common shares to Formula, at a purchase price per share of \$1.92, which was the average closing price for the 10 day period prior to the execution of the agreement.
- c. In August 2006, the Company entered into an agreement with Formula, whereby Formula invested \$2.0 million in the Company and the Company issued 1,562,500 Common shares to Formula, at a price per share of \$1.28 which was the average closing price over the 10 day period prior to July 17, 2006.

In August 2006, the Company entered into an agreement with the investors in eZoneXchange, whereby the investors converted the \$1.0 million payment that was due on April 1, 2006 into 781,250 Common shares at a conversion price per share of \$1.28, which was the average closing price over the 10 day period prior to July 17, 2006.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 14: SHAREHOLDERS' EQUITY (Cont.)

- d. On April 4, 2001, the Company entered into a share purchase and loan agreement with Red Coral Holdings, Inc. ("Red Coral"), a company owned by the Company's then President and Chief Executive Officer. According to the terms of the share purchase agreement, Red Coral purchased 300,000 Common shares of the Company for a purchase price of \$975. As part of the loan agreement, the Company granted to Red Coral a loan in the amount of \$975 for the purpose of acquiring the Common shares. The term of the loan was six years, with accrued interest at a rate of 4%, which was payable on January 15th of each calendar year. The interest amount is fully-recourse and fixed. To secure payment of the loan, Red Coral granted to the Company a lien and security interest on the 300,000 Common shares of the Company that it owned. To secure fulfillment of the terms of the agreement, the Common shares were held in escrow by the General Counsel of the Company. The issuance of Common shares was recorded in the shareholders' equity and the loan amount was deducted from the shareholders' equity as a Note receivable from a related party shareholder.

In accordance with EITF 95-16, "Accounting for Stock Compensation Arrangements with Employer Loan Features under APB Opinion No. 25", the transaction was accounted for as a fixed award.

On November 10, 2005, the Company's former President and Chief Executive Officer was replaced by its current President and Chief Executive Officer. Following the departure of the former President and Chief Executive Officer, the Company postponed the due date of the January 15, 2006 and 2007 interest payments, until the due date for repayment of the principal amount of the loan (April 4, 2007), and to convert the final two interest payments from fully-recourse to non-recourse.

On April 4, 2007, the term of the loan expired, without Red Coral having repaid the principal amount or the final two interest payments. In May 2007, the Company foreclosed its lien on the 300,000 Common shares of the Company owned by Red Coral, and the Company holds such shares as treasury shares. As a result, the loan agreement was terminated and Red Coral has no further obligations to the Company.

- e. Common shares confer upon their holders voting rights, the right to receive cash dividends and the right to share in excess assets upon liquidation of the Company.

- f. Stock option plan:

Stock options granted under the Company's 1992 Stock Option and Incentive Plan ("the Plan") to employees, directors and service providers are exercisable at the fair market value of the Company's Common shares on the date of grant and, subject to termination of employment, expire ten years from the date of grant and are generally exercisable in four equal annual installments commencing one year from the date of grant.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 14: SHAREHOLDERS' EQUITY (Cont.)

In 2003, the Company's Board of Directors and shareholders authorized the extension of the Sapiens International Corporation N.V. 1992 Stock Option and Incentive Plan (the "1992 Stock Plan") until April 2012. Also in 2003, the Company's Board of Directors and shareholders approved the 2003 Share Option Plan (the "2003 Option Plan"), including the reservation of 500,000 Common Shares for grant pursuant to such plan. The 1992 Stock Plan and the 2003 Option Plan are referred together as "the Plan".

In August 2004, the Company's shareholders approved an increase of the number of Common shares available for grant pursuant to the Plan by an additional 500,000 Shares.

In November 2005, the Company's Board of Directors approved a new Incentive Stock Option Plan (the "Special Plan"). The number of Common shares available for grants pursuant to the Special Plan was set at 2,000,000 shares. The Special Plan is intended to be used solely to attract or retain senior management and/or Board members. Options granted pursuant to the Special Plan will have an exercise price of \$3.00, will be locked for up to five years, and will be contingent upon the optionee providing services to the Company throughout the entire five year period. In the event of a change of control of the Company, the vesting of such options will be accelerated. The Special Plan was approved by the Company's shareholders, at the 2006 Annual General Meeting of Shareholders.

In November 2005, the Company's current President and Chief Executive Officer was granted options to purchase 240,000 shares pursuant to the 2003 Option Plan and additional options to purchase 1,000,000 shares pursuant to the Special Plan, which was approved by the shareholders in November 2006.

On December 28, 2005, the 240,000 options under the 2003 Option Plan and the 1,000,000 options under the Special Plan were accelerated and became fully exercisable. See Note 2u.

As of December 31, 2006, 1,310,686 options to Common shares of the Company are still available for future grant. Any options, which are forfeited or cancelled before expiration, become available for future grant under the Plan.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 14: SHAREHOLDERS' EQUITY (Cont.)

A summary of the stock options activities in 2006, is as follows:

	Year ended			
	December 31, 2006			
	Amount of options	Weighted average exercise price	Weighted average remaining contractual life (Years)	Aggregate intrinsic value
Outstanding -beginning of year	*) 2,812,212	\$ 5.54	7.14	\$ 0
Granted	20,000	\$ 171	3.98	\$ 0
Exercised	-	\$ -		
Expired, cancelled and forfeited	(391,162)	\$ 10.76	5.10	\$ 0
Outstanding at end of year	*) 2,441,050	\$ 4.68	6.45	\$ 0
Vested and expected to vest at end of year	2,441,050	\$ 4.68	6.45	\$ 0
Exercisable options at end of year	2,437,050	\$ 4.68	6.45	\$ 0

*) Including 62,300 and 59,000 options repriced to zero, as of December 31, 2005 and 2006, respectively.

The aggregate intrinsic value is the difference between the Company's closing stock price on the last trading day of the fiscal year 2006 and the exercise price, multiplied by the number of in-the-money options that would have been received by the option holders had all option holders exercised their options on December 31, 2006. This aggregate intrinsic value changes based on the fair market value of the Company's shares.

The options outstanding as of December 31, 2006, have been classified by range of exercise price, as follows:

Exercise price	Options outstanding as of December 31, 2006	Weighted average remaining contractual life (years)	Weighted average exercise price	Options exercisable as of December 31, 2006	Weighted average exercise Price
\$0	59,000	0.45	\$ 0	59,000	\$ 0
\$1.34 - \$1.74	309,000	7.83	\$ 1.73	305,000	\$ 1.73
\$1.80 - \$2.63	352,950	6.94	\$ 2.33	352,950	\$ 2.33
\$3.00	1,000,000	8.86	\$ 3.00	1,000,000	\$ 3.00
\$3.28 - \$3.75	93,100	1.96	\$ 3.59	93,100	\$ 3.59
\$4.06 - \$5.70	519,050	3.01	\$ 4.56	519,050	\$ 4.56
\$11.25 - \$16.875	8,100	0.12	\$ 13.40	8,100	\$ 13.40
\$19.375 - \$29.375	19,000	3.49	\$ 28.68	19,000	\$ 28.68
\$32.5 - \$47.5	59,850	1.95	\$ 38.53	59,850	\$ 38.53
\$61.25 - \$69.375	21,000	2.57	\$ 66.98	21,000	\$ 66.98
	2,441,050		\$ 4.68	2,437,050	\$ 4.68

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 14: SHAREHOLDERS' EQUITY (Cont.)

The weighted average grant date fair values of the options granted during the years ended December 31, 2004, 2005 and 2006 were \$1.98, \$1.61 and \$0.52, respectively. The total intrinsic value of options exercised during the years ended December 31, 2004, 2005 and 2006 was \$0. Compensation expense recognized amounted to \$0, \$0 and \$32 for the years ended December 31, 2004, 2005 and 2006, respectively.

As of December 31, 2006, there was \$0 of total unrecognized compensation cost related to nonvested options granted under the Plan.

Upon exercise of options by employees, the Company satisfies the requirements by issuing newly issued shares.

g. During 2004 and 2005, the Company decided to extend the exercise period for certain former employees. The extension was accounted for in accordance with FIN 44 by applying a new measurement date, which resulted in no additional compensation expenses. Total options extended during 2004, 2005 and 2006 were 54,000, 313,250 and 86,800 respectively.

h. Warrants:

In 2005, warrants were granted to advisor board members. As of December 31, 2006, warrants are outstanding as follows:

Warrants to Common shares	Weighted average exercise price per share	Warrants exercisable	Exercisable through
11,000	\$ 2.00	11,000	May 2015
17,000	2.24	17,000	February 2015
<u>28,000</u>	<u>\$ 2.15</u>	<u>28,000</u>	

These warrants were measured at fair value (according to Black-Scholes option pricing model) with the following assumptions: Risk free rate of 4.5%, dividend yields of 0%, expected volatility of 80% and contractual life of the warrants of ten years. Total compensation expense amounted to \$23, of which \$10 and \$6 were recorded in 2005 and 2006, respectively.

i. As for warrants granted to investors as part of the settlement of redeemable shares in a subsidiary, see Note 1c.

j. As for 600,000 Warrants (Series 1) offered to the public, see Note 9b.

k. The Company does not intend to pay cash dividends in the foreseeable future.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 15: GEOGRAPHIC INFORMATION

a. The Company operates in a single segment as a provider of software solutions. See Note 1 for brief description of the Company's business. The data below is presented in accordance with Statement of Financial Accounting Standard No. 131, "Disclosure about Segments of an Enterprise and Related Information".

b. Geographic information:

The following is a summary of operations within geographic markets.

		Year ended December 31,		
		2004	2005	2006
1.	Revenues:			
	U.K.	\$ 18,217	\$ 12,604	\$ 13,805
	North America	12,381	10,046	9,895
	Israel	8,910	9,147	12,072
	France	1,352	1,131	902
	Germany	1,814	1,414	837
	Japan	3,147	3,902	4,491
	Switzerland	1,983	1,160	2,309
		\$ 47,804	\$ 39,404	\$ 44,311
		December 31,		
		2005	2006	
2.	Long-lived assets:			
	Israel		\$ 14,344	\$ 15,025
	France		477	496
	Dutch Antilles		317	184
	Other		400	445
			\$ 15,538	\$ 16,150

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands (except share and per share data)

NOTE 16: SELECTED STATEMENTS OF OPERATIONS DATA

a. Research and development expenses:

	Year ended December 31,		
	2004	2005	2006
Total costs	\$ 8,114	\$ 7,566	\$ 7,150
Less - capitalized software development costs, net of royalties bearing grants	(4,750)	(4,323)	(4,699)
Less - royalty-bearing grants	(833)	(520)	-
	\$ 2,531	\$ 2,723	\$ 2,451

b. Financial expenses, net:

	Year ended December 31,		
	2004	2005	2006
Financial income:			
Interest	\$ 358	\$ 309	\$ 122
Re-evaluation of Warrants (Series 1) which are classified as liabilities	266	79	46
Foreign currency transaction differences	10,057	7,467	2,037
Income on sale of marketable securities and bonds	-	-	20
	10,681	7,855	2,225
Financial expenses:			
Interest *)	2,282	1,780	1,640
Foreign currency transaction differences	9,898	7,328	2,133
Bank charges and others	249	84	198
Loss on sale of marketable securities and bonds	67	71	-
Amortization of issuance expenses and discount on convertible notes	595	380	484
	13,091	9,643	4,455
Financial expenses, net	\$ 2,410	\$ 1,788	\$ 2,230

*) For capitalization of interest expenses, see Note 7a.

SIGNATURES

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

SAPIENS INTERNATIONAL CORPORATION N.V.

By: /s/ Ron Al Dor

Ron Al Dor
President & Chief Executive Officer

Date: June 28, 2007

Agreement

THIS AGREEMENT (the "**Agreement**") is entered into as of August 10, 2006 (the "**Effective Date**"), by and among (i) Sapiens International Corporation N.V. ("**Sapiens**"), a public company organized under the laws of the Netherlands Antilles whose shares are traded on NASDAQ and the Tel-Aviv Stock Exchange, (ii) F.I.D. Holdings Ltd., a private company organized under the laws of the State of Israel ("**FID**") and (iii) Israel Discount Bank Ltd. ("**IDB**" and, collectively with FID, the "**Investors**").

WITNESSETH

WHEREAS, on April 14, 2000, FID entered into (i) a Share Purchase Agreement with eZoneXchange.com, Inc. and Sapiens, and (ii) a Put/Call Agreement with Sapiens (the "**Original Put/Call Agreement**");

WHEREAS, on May 3, 2000, FID assigned 9.33% of its rights and obligations under the agreements referred to in the previous paragraph to IDB;

WHEREAS, on February 13, 2001, the parties entered into a letter agreement in which the parties, among other things, agreed to amend the Original Put/Call Agreement (such original agreement, as amended, the "**Put/Call Agreement**");

WHEREAS, on March 16, 2004, the parties entered into an Agreement (the "**March 2004 Agreement**") which settled all of the obligations of Sapiens to the Investors under the Put/Call Agreement in consideration for the terms and provisions more fully set forth therein;

WHEREAS, on May 2, 2005, the parties entered into an Agreement (the "**May 2005 Agreement**") which set forth the payment terms of the remaining US\$ 4,000,000 due to the Investors;

WHEREAS, Sapiens paid the Investors an aggregate amount of US\$ 2,000,000, pursuant to the May 2005 Agreement.

WHEREAS, Sapiens (a) wishes to delay the payment of US\$ 1,000,000 due by it under the May 2005 Agreement and (b) to convert the other US\$ 1,000,000 due to the Investors into common shares, and the Investors agree to do so, upon the general principles more fully set forth herein;

WHEREAS, accordingly, Sapiens wishes and the Investors agree to amend the May 2005 Agreement, and thereby the March 2004 Agreement, in accordance with the general principles more fully set forth herein.

NOW THEREFORE, the parties hereto agree as follows:

1. The provisions of Sections 1.2 and 1.3 of the May 2005 Agreement shall be replaced with the following provisions:

- “1.2. Within thirty (30) days of the Effective Date, Sapiens shall issue to the Investors 781,250 Common Shares of Sapiens, par value one Eurocent (€0.01) per share, reflecting a price per share equal to US\$1,000,000 divided by \$1.28 (the average closing price for the 10 day period prior to July 17, 2006). As a result of the foregoing issuance of shares, the amount that Sapiens shall owe the Investors shall be reduced by US \$1,000,000 (and the total amount due shall then be US\$1,000,000 which will be payable in accordance with Section 1.3 below); and
- 1.3. By no later than August 1, 2007 (the “**Date of Last Payment**”), Sapiens shall pay the Investors an aggregate amount of US\$ 1,000,000; *provided, however*, that subject to the receipt of Sapiens’ shareholders approval as required under applicable law (the “**Required Consent**”), the Investors may, at their sole discretion, convert all or any portion of the US\$1 million payable on the Date of Last Payment into shares of Common Stock of Sapiens, par value one Eurocent (€0.01) each, at a conversion price per each share of Common Stock of Sapiens equal to US\$ 3.20. Such conversion shall be effected by the Investors providing prior written notice of at least 60 days. Upon the receipt of such notice of exercise of conversion, Sapiens shall use its best efforts to obtain the Required Consent.”
2. For the avoidance of doubt, Sapiens shall continue to make payments of interest and value added tax with respect to \$1,000,000 principal payment set forth in Section 1 above, at the rate of LIBOR plus 2.5%, compounded annually on the outstanding principal of the Loan, and (ii) any interest accrued until the Date of Last Payment shall be paid on the Date of Last Payment and not on January 10, 2007.
3. All capitalized terms that are not otherwise defined in this Agreement shall have the respective meanings attributed to them in the May 2005 Agreement.
4. All other provisions set forth in the May 2005 Agreement which are not expressly amended herein shall remain unchanged.

IN WITNESS WHEREOF, the undersigned have caused this Agreement to be executed by their duly authorized representatives as of the date first written above.

Sapiens International Corporation N.V.

By: /s/ Roni Al-Dor

Name: Roni Al-Dor
Title: President and CEO

F.I.D. Holdings Ltd.

By: /s/

Name:
Title:

By: /s/ Elior Brin

Name: Elior Brin
Title: EVP and CFO

Israel Discount Bank Ltd.

By: /s/ Dorit Ben Simon

Name: Dorit Ben Simon
Title: EVP and CFO

SHARE ISSUANCE AGREEMENT

THIS SHARE ISSUANCE AGREEMENT (this "**Agreement**") is made as of August 10, 2006 (the "**Effective Date**"), by and between (i) Sapiens International Corporation N.V. ("**Sapiens**" or the "**Company**"), a company organized and existing under the laws of the Netherlands Antilles, whose shares are traded on Nasdaq and on the Tel-Aviv Stock Exchange (the "**TASE**"); and (ii) Formula Systems (1985) Ltd. (the "**Investor**"), an Israeli company.

WHEREAS, the Investor is a public company traded on the TASE and the Nasdaq;

WHEREAS, the Investor is the parent company of the Company and holds approximately 58% of the Company's outstanding share capital;

WHEREAS, the Investor desires to invest in the share capital of the Company, by purchasing the Purchased Shares (as defined below), upon the terms and subject to the conditions set forth in this Agreement.

WHEREAS, the Board of Directors of the Company (the "**Board**") has decided to issue to the Investor 1,562,500 common shares, par value 0.01 Euro per share, (the "**Ordinary Shares**" and the "**Purchased Shares**", accordingly), upon the terms and subject to the conditions set forth in this Agreement.

NOW, THEREFORE, in consideration of the mutual promises and covenants set forth herein, the parties hereto agree as follows:

1. **Purchase and Sale of Purchased Shares**

Upon the terms and subject to the conditions set forth in this Agreement, the Investor agrees to purchase, and the Company agrees to sell and issue to the Investor at the Closing the Purchased Shares, at a price per share of US\$ 1.28, which is the average closing price for the 10 day period prior to July 17, 2006 (the "**PPS**") and an aggregate purchase price of \$2,000,000 (the "**Purchase Price**") payable in United States Dollars.

2. **Closing of Issue and Purchase of Purchased Shares**

2.1 **The Closing**. The parties shall hold the closing (the "**Closing**") at the offices of the Investor, 3 Abba Eban Boulevard, Herzlia, Israel, on the 10th business day following the date on which all the conditions to Closing shall have been satisfied, or at such other date as the Company and the Investor shall agree (the "**Closing Date**").

2.2 **Transactions at the Closing**. At the Closing, the following transactions shall occur:

(1) The Investor shall receive from the Company the following documents:

- (a) A certificate duly executed on behalf the Company by an officer of the Company dated as of the Closing Date (the “**Compliance Certificate**”), in the form attached hereto as **Schedule 2.2 (1)(a)**; and
- (b) Copies of the Required Approvals and Notices (as defined below); and
- (c) An opinion of Netherlands Antilles counsel to the Company, substantially in the form attached hereto as **Schedule 2.2 (1)(c)**.

(2) The Investor shall pay the Purchase Price (or the remainder thereof, in the event that any portion of the Purchase Price was forwarded to the Company prior to the Closing Date) to the Company by SWIFT wire transfer of immediately available funds to the Company’s bank account at Bank HaPoalim, Swift Code POALILIT and the issuance of the Purchased Shares in the name of the Investor shall come into effect; and

(3) The parties shall execute the Deed of Issuance of Shares, attached hereto as **Schedule 2.2 (3)**.

(4) The Company will take all required actions in order to list the Purchased Shares on TASE and Nasdaq.

3. **Representations and Warranties of the Company**

The Company hereby represents and warrants to the Investor, and acknowledges that the Investor is entering into this Agreement in reliance thereon, as follows:

3.1 **Organization.** The Company is a corporation duly organized and validly existing under the laws of the Netherlands Antilles. The Company is duly qualified to conduct its business, and (with respect to those jurisdictions in which the concept of good standing is relevant) is in good standing, in each jurisdiction where the character of its properties owned, operated or leased or the nature of its activities makes such qualification necessary, except for such failures which would not reasonably be likely to have a Material Adverse Effect (as defined below). The Company has the requisite corporate power and authority and the necessary governmental authority, franchise, license or permit to own, operate, lease and otherwise to hold and operate its assets and properties and to carry on its businesses as now being conducted.

3.2 **Organizational Documents.** Set forth in **Schedule 3.2** is a complete and correct copy of the Articles of Association of the Company. All of such organizational documents are in full force and effect.

3.3 Capitalization.

(a) The registered share capital of the Company immediately prior to the Closing shall be Euro 310,000, which registered share capital is divided into 30,000,000 Ordinary Shares, of which 12,810,102 were issued and outstanding and 1,000,000 Preferred Shares, none of which were issued and outstanding, as of December 31, 2005. The capitalization table as of December 31, 2005 of the Company, on a fully diluted basis, is attached hereto as **Schedule 3.3(a)(1)**. Except as set forth in the Company's annual report on Form 20-F for the fiscal period ended December 31, 2005, which is referenced in **Schedule 3.3(a)(2)** (the "20-F") or in **Schedule 3.3(a)(3)** attached hereto, as of December 31, 2005, there are no other shares, convertible or other securities, outstanding warrants, options, or other rights to subscribe for, purchase, or acquire from the Company any securities of the Company, and there are not any contracts or binding commitments providing for the issuance of, or the granting of rights to acquire from the Company, any securities of the Company or under which the Company is, or may become, obligated to issue any of its securities.

(b) Except as set forth in the 20-F or **Schedule 3.3(b)(1)**, as of December 31, 2005, there are no bonds, debentures, notes or other indebtedness issued by the Company or granted by third parties that have the right to vote on any matters on which the Company's shareholders may vote. Except for agreements or other documents set forth in the 20-F or in **Schedule 3.3(b)(2)**, there are no outstanding contractual obligations of the Company to repurchase, redeem or otherwise acquire any of the Company's share capital. All of the issued and outstanding share capital of the Company has been duly authorized and validly issued and is fully paid and non-assessable.

(c) All of the Purchased Shares issuable in accordance with this Agreement shall be, when paid for and issued at the Closing as provided in this Agreement, duly authorized, validly issued, fully paid and non-assessable, shall not be subject to call, forfeiture or preemptive rights, and shall be delivered free and clear of all Encumbrances.

For purposes of this Agreement, the term "**Encumbrance**" means and includes any interest or equity of any person (including any right to acquire, option, or right of preemption) or any mortgage, charge, pledge, lien, or assignment, or any other encumbrance or security interest over or in the relevant property.

With respect to any representation and warranty made in this Section 3.3, as of December 31, 2005, there have not been any material changes from such date through the date hereof.

3.4 Authority. The Company has the necessary corporate power and authority to enter into this Agreement, certificates or other instruments required to be delivered hereunder by the Company at or prior to Closing, and to perform its obligations hereunder and to consummate the transaction contemplated hereby. The execution and delivery of this Agreement by the Company and the consummation by the Company of the transaction contemplated hereby shall have been, at the Closing Date, duly and validly authorized by all necessary corporate action, and no other corporate proceedings on the part of the Company shall be necessary to authorize this Agreement or to consummate the transaction contemplated hereby. This Agreement has been duly executed and delivered by the Company and, assuming the due authorization, execution and delivery by the Investor, constitutes a legal, valid and binding obligation of the Company, enforceable against the Company in accordance with its terms, except as such enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium and other similar laws of general applicability relating to or affecting creditors' rights generally and by the application of general principles of equity. This Agreement and any other documents pertaining hereto, when executed and delivered by the Company, shall have been duly executed and delivered by the Company and, assuming the due authorization, execution and delivery by each of the other parties hereto, shall constitute a legal, valid and binding obligation of the Company, enforceable against the Company in accordance with its terms, except as such enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium and other similar laws of general applicability relating to or affecting creditors' rights generally and by the application of general principles of equity.

3.5 No Conflict; Required Filings and Consents.

(a) The execution and delivery of this Agreement by the Company do not, and the performance by the Company of its obligations under this Agreement, will not, with or without the giving of notice or the lapse of time or both, (i) conflict with or violate the organizational documents of the Company, (ii) subject to obtaining the Required Approvals and Notices (as defined below), conflict with or violate any law, statute, ordinance, rule, regulation, order, judgment or decree applicable to the Company or by which any of its properties or assets is bound or affected, or (iii) result in any breach of or constitute a default under, or give to others any rights of termination, amendment, acceleration or cancellation of any material agreement to which the Company is a party, or result in the creation of any Encumbrance on the material properties or assets of the Company pursuant to, any note, bond, mortgage, indenture, contract, agreement, lease, license, permit, franchise or other instrument or obligation to which the Company is a party or by which the Company is bound.

(b) The execution and delivery of this Agreement by the Company do not, and the performance of this Agreement by the Company, will not, require any consent, approval, authorization or permit of or filing with or notification to, any Governmental Entity (as defined below), by or with respect to the Company, except (i) for applicable requirements, if any, of the consents, approvals, authorizations, permits or notification described in **Schedule 3.5** (the "**Required Approvals and Notices**"), and (ii) where failure to obtain the required consents, approvals, authorizations or permits, or to make such filings or notifications, (A) would not prevent or delay consummation of the transaction contemplated by this Agreement in any material respect, or otherwise prevent the Company from performing its obligations under this Agreement in any material respect, and (B) would not reasonably be likely to have a Material Adverse Effect. As used herein the term "**Governmental Entity**" means any Israeli or U.S. entity exercising executive, legislative, judicial, regulatory or administrative function of or pertaining to government.

3.6 SEC Filings; Financial Statements; Israeli Filings.

(a) During the two-year period immediately prior to the date hereof, the Company has filed all forms, reports, statements and other documents required to be filed with the Securities and Exchange Commission (“SEC”). The Investor has had access, in the form filed with the SEC, together with any amendments thereto, to all of the Company’s (i) Annual Reports on Form 20-F and (ii) proxy statements relating to meetings of shareholders (whether annual or special) (collectively, the “**Sapiens SEC Reports**”). In addition, the Company has published as a press release the unaudited and unreviewed financial statements for the first quarter of 2006, which have been previously delivered to counsel for the Investor (the “**2006 Financials**”). As of their respective filing or publication dates, the Sapiens SEC Reports complied as to form in all material respects with the requirements of the United States Securities Exchange Act of 1934 (the “**Exchange Act**”) applicable to the Company. The Sapiens SEC Reports did not at the time they were filed or published, as the case may be, contain any untrue statement of a material fact or omit to state a material fact required to be stated therein or necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading.

(b) The audited consolidated financial statements of the Company included in the Sapiens SEC Reports comply as to form in all material respects with applicable accounting requirements and with the published rules and regulations of the SEC with respect thereto as in effect at the time of filing. The financial statements, including all related notes and schedules, contained in the Sapiens SEC Reports (or incorporated by reference therein) and the 2006 Financials, present fairly in all material respects the consolidated financial position of the entity or entities covered therein as at the respective dates thereof and the consolidated results of operations and cash flows thereof for the periods indicated, in accordance with United States generally accepted accounting principles (GAAP), except that quarterly financial statements, which are unaudited, may not contain statements of cash flows or comprehensive footnotes and are subject to year-end audit adjustments and as otherwise set forth on **Schedule 3.6(b)**, which adjustments will not be material in amount or significance.

(c) Compliance with Israeli securities rules and regulations. During the two-year period immediately prior to the date hereof, the Company has been, in all material respects, in compliance with all applicable regulatory requirements, including without limitation, all filing requirements stipulated by the Securities Act, 1968 and the regulations promulgated thereunder in respect of “dual-listed” companies (the “**Israeli Filings**”).

3.7 Operations in the Ordinary Course. Except as set forth in **Schedule 3.7** attached hereto or otherwise disclosed in the Sapiens SEC Reports, Israeli Filings or the 2006 Financials, between March 31, 2006 and the date of this Agreement, the Company has operated its business in the usual and ordinary course consistent with past practices and there has been no event which resulted or is likely to result in a Material Adverse Effect.

For purposes of this Agreement, the term “**Material Adverse Effect**” means any material adverse effect on the business, as now conducted by, the assets, condition (financial or otherwise), liabilities or operations of, the Company and its Subsidiaries taken as a whole.

3.8 Litigation. Except as set forth in the 20-F or **Schedule 3.8** attached hereto, there are no claims, actions or proceedings pending or, to the Company’s knowledge, threatened against the Company, any of their respective properties (or any of their respective officers or directors, in such capacity) before any court, arbitral, mediation or regulatory authority or body, domestic or foreign, that individually or in the aggregate (i) would reasonably be likely to have a Material Adverse Effect, or (ii) challenge or seek to prevent, enjoin, alter or materially delay the transaction contemplated by this Agreement.

3.9 Licenses and Permits; Compliance with Laws. Without derogating from the above, the Company does not lack any permits, licenses, authorizations or approvals necessary to conduct their business, and are not in material violation of Applicable Law or any permits, licenses, authorizations and approvals that have been obtained by them, which the failure to obtain or such violation, as applicable, would reasonably be likely to have a Material Adverse Effect.

As used herein, the term “**Applicable Law**” means any provision of any statute, law, ordinance, rule, regulation, governmental decree, order, concession, grant, permit or license, or other governmental authorization or approval applicable to the Company.

3.10 Intellectual Property.

(a) The Company owns, free and clear of claims or rights or any other Person, with full right to use, or, to the knowledge of the Company, has acquired licenses or other rights to use, all Intellectual Property necessary for the conduct of its business as presently conducted (other than with respect to software which is generally commercially available and not used or incorporated into the Company’s products and open source software which may be subject to one or more “general public” licenses), except as would not be reasonably expected to have a Material Adverse Effect. All works that are used or incorporated into the Company’s services, products or services or products actively under development and which are proprietary to the Company were developed by or for the Company by its current or former employees, consultants or independent contractors or those of its predecessors in interest or purchased or licensed by the Company or its predecessors in interest.

(b) The business of the Company as presently conducted and the production, marketing, licensing, use and servicing of any products or services of the Company do not, to the knowledge of the Company, infringe or conflict with any patent, trademark, copyright, or trade secret rights of any third parties or any other Intellectual Property of any third parties in any material respect. The Company has not received written notice from any third party asserting that any Intellectual Property owned or licensed by the Company, or which the Company otherwise has the right to use, is invalid or unenforceable by the Company and, to the Company’s knowledge, there is no valid basis for any such claim (whether or not pending or threatened).

(c) No claim is pending or, to the Company's knowledge, threatened against the Company nor has the Company received any written notice or other written claim from any Person asserting that any of the Company's present or contemplated activities infringe or may infringe in any material respect any Intellectual Property of such Person and the Company is not aware of any infringement by any other Person of any material rights of the Company under any Intellectual Property Rights.

(d) All licenses or other agreements under which the Company is granted Intellectual Property (excluding licenses to use software utilized in the Company's internal operations and which is generally commercially available) are in full force and effect and, to the Company's knowledge, there is no material default by any party thereto. The Company has no reason to believe that the licensors under such licenses and other agreements do not have and did not have all requisite power and authority to grant the rights to the Intellectual Property purported to be granted thereby. The Company has complied in all material respects with its obligations pursuant to all agreements relating to Intellectual Property rights that are the subject of licenses granted by third parties, except for any non-compliance that has not had or would not reasonably be expected to have a Material Adverse Effect.

(e) All licenses or other agreements under which the Company has granted rights to Intellectual Property to others (including all end-user agreements) are in full force and effect, unless otherwise terminated in accordance with the terms of such licenses or arrangements, there has been no material default by the Company thereunder and, to the Company's knowledge, there is no material default by any other party thereto.

(f) The Company has taken all steps required in accordance with commercially reasonable business practice to establish and preserve its ownership in its owned Intellectual Property and to keep confidential all material technical information developed by or belonging to the Company which has not been patented or copyrighted. To the Company's knowledge, the Company is not making any material unlawful use of any Intellectual Property of any other Person, including, without limitation, any former employer of any past or present employees of the Company. To the Company's knowledge, neither the Company nor any of its employees has any agreements or arrangements with former employers of such employees relating to any Intellectual Property of such employers, which materially interfere or conflict with the performance of such employee's duties for the Company or result in any former employers of such employees having any rights in, or claims on, the Company's Intellectual Property. Each senior key employee of the Company who the Company believes ought to execute an agreement regarding confidentiality, proprietary information and assignment of inventions and copyrights to the Company has done so, each independent contractor or consultant of the Company who the Company believes ought to execute an agreement regarding confidentiality and proprietary information has done so, and the Company has not received written notice that any employee, consultant or independent contractor is in violation of any agreement or in breach of any agreement or arrangement relating to proprietary information or assignment of inventions. Without limiting the foregoing: (i) the Company has taken reasonable security measures to guard against unauthorized disclosure or use of any of its Intellectual Property; and (ii) the Company has no reason to believe that any Person (including, without limitation, any former employee or consultant of the Company) has unauthorized possession of any of its Intellectual Property, or any part thereof, or that any Person has obtained unauthorized access to any of its Intellectual Property.

For purposes of this Agreement, “**Person**” means any individual, corporation, trust, association, company, partnership, joint venture, limited liability company, joint stock company, Governmental Authority or other entity, and “**Intellectual Property**” means patents, patent rights, patent applications, trademarks, trade names, service marks, brand names, logos and other trade designations (including unregistered names and marks), trademark and service mark registrations and applications, copyrights and copyright registrations and applications, inventions, invention disclosures, protected formulae, formulations, processes, methods, trade secrets, computer software, computer programs and source codes, manufacturing research and similar technical information, engineering know-how, customer and supplier information, assembly and test data drawings or royalty rights.

3.11 Material Agreements. All material agreements that are required to be disclosed by the Company in its Form 20-F (collectively, the “**Material Agreements**”), are described in the 20-F or in **Schedule 3.11** attached hereto. Such Material Agreements are valid and in full force and effect on the date hereof, and, except as set forth in **Schedule 3.11** attached hereto, neither the Company nor, to the Company’s knowledge, any other party, has violated any provision thereof, or committed or failed to perform any act which with or without notice, lapse of time or both would constitute a default under the provisions of, any Material Agreement except for violations or defaults which would not reasonably be likely to have a Material Adverse Effect.

3.12 Taxation. In the Company’s judgment, the financial statements contained in the Sapiens SEC Reports make adequate provisions for taxation for which the Company was then liable or accountable, to the extent required under United States GAAP, and the Company has promptly paid or provided in its books of account for all such taxation liability.

3.13 No Finders Fee. No person or firm has, or will have, as a result of any act or omission by the Company or anyone acting on behalf of the Company, any right, interest or valid claim against the Company or the Investor for any commission, fee or other compensation as a finder or broker or in any similar capacity with respect to the transaction contemplated under this Agreement.

3.14 Debt. A complete list of the Company’s credit line facilities (including the name of the banking institution which provided the facility the aggregate credit amount made available by such banking institution and the actual amounts drawn on account of each such credit line as of July 15, 2006) and all other financial indebtedness is set forth in **Schedule 3.14** attached hereto. The Company is not in default under any of the financial or other covenants applicable to such credit lines or other financial indebtedness.

3.15 **Representations Complete.** None of the representations or warranties made by the Company herein or in any Schedule or Exhibit hereto contain or will contain at the Closing Date any untrue statement of a material fact, or omit or will omit at the Closing Date to state any material fact necessary in order to make the statements contained herein or therein, in the light of the circumstances under which they were made, not misleading.

4. **Representations and Warranties of the Investor**

The Investor hereby represents and warrants to the Company, and acknowledges that the Company is entering into this Agreement in reliance thereon, as follows:

4.1 This Agreement, when executed and delivered by the Investor, constitutes a valid, binding, and enforceable obligation of the Investor.

4.2 The Investor is public company which shares are traded on the TASE and the Nasdaq, and it is duly organized, and validly existing under the laws of the State of Israel, and has all requisite power and authority to carry out the transaction contemplated hereby, and the execution, delivery, and performance of the obligations of the Investor hereunder have been duly authorized by all necessary corporate action.

4.3 The Investor owns approximately 58% of the outstanding share capital of the Company.

4.4 The Investor understands, acknowledges and agrees that the Purchased Shares have not been registered under the securities laws of any jurisdiction, and may not be transferred without such registration or an exemption therefrom. Until registered under the Securities Act or otherwise permitted under the Securities Act, all certificates evidencing any of the Purchased Shares shall bear a legend, prominently stamped or printed thereon, reading substantially as follows:

“The securities represented by this certificate have not been registered under the Securities Act of 1933, as amended (the “Securities Act”) or applicable State securities laws. These securities have been acquired for investment and not with a view to distribution or resale, and may not be sold or otherwise transferred without an effective registration statement for such securities under the Securities Act and applicable State securities laws, or the availability of an exemption from the registration provisions of the Securities Act and applicable State securities laws”.

4.5 The execution and delivery of this Agreement and the consummation of the transaction herein contemplated will not (i) result in any conflict with, breach of, or default (or give rise to any right of termination, cancellation or acceleration or the loss of any benefit) under any of the terms, conditions or provisions of the Investor's organizational documents or of any material agreement, permit or other instrument or obligation to which the Investor is a party or is bound, or (ii) violate any law or regulation, or any order, injunction, or judgment of any court or any governmental bureau or agency, domestic or foreign applicable to the Investor. No consent or approval by any governmental authority or any third party is required in connection with the execution by the Investor of this Agreement or the consummation by the Investor of the transaction contemplated hereby except for such actions, consents or approvals as have been obtained prior to the execution of this Agreement.

4.6 No Finders Fee. No person or firm has, or will have, as a result of any act or omission by the Investor or anyone acting on its behalf, any right, interest or valid claim against the Company for any commission, fee or other compensation as a finder or broker or in any similar capacity, with respect to any of the transaction contemplated under this Agreement.

4.7 Nothing set forth in this Section 4 shall be deemed to detract from or otherwise prejudice the Investor's reliance on the Company's representations and warranties set forth in Section 3 above.

5. **Conditions to Closing**

5.1 Conditions Precedent to the Obligation of the Investor to Close. The obligation hereunder of the Investor to purchase the Purchased Shares and pay the Purchase Price is subject to the fulfillment at or before the Closing of the following conditions precedent, any one or more of which may be waived in writing, in whole or in part, by the Investor, which waiver shall be at the sole discretion of the Investor.

(a) Accuracy of the Company's Representations and Warranties. Each of the representations and warranties of the Company contained in this Agreement shall be true and correct in all material respects as of the date when made and, except for such changes as are attributable to the Company's ordinary course of business and do not, in the aggregate, have a Material Adverse Effect on its business or prospects, as of the Closing, as though made at that time.

(b) Performance by the Company. The Company shall have performed, satisfied and complied in all material respects with all covenants, agreements and conditions required by this Agreement to be performed, satisfied or complied with by the Company at or prior to the Closing.

(c) All Deliverables Ready. All documents and other items to be delivered to the Investor at the Closing as specified in Section 2.2 above, shall be duly executed, ready for delivery to the Investor.

(d) No Material Adverse Effect. The Company shall not have suffered a Material Adverse Effect with respect to the Company's business and prospects as of the date hereof.

5.2 Conditions Precedent to the Obligation of the Company to Close. The obligation hereunder of the Company to issue and sell the Shares to the Investor is subject to the fulfillment at or before the Closing of the following conditions precedent, any one or more of which may be waived in writing, in whole or in part, by the Company, which waiver shall be at the sole discretion of the Company.

(a) Accuracy of the Investor Representations and Warranties. Each of the representations and warranties of the Investor shall be true and correct in all material respects as of the date when made and as of the Closing, as though made at that time.

(b) Performance by the Investor. The Investor shall have performed, satisfied and complied in all material respects with all covenants, agreements and conditions required by this Agreement to be performed, satisfied or complied with by the Investor at or prior to the Closing.

6. **Registration Rights**

Clause 11.2 of the Share Purchase Agreement signed between the Company, the Investor and Yarnfield International Limited, dated January 24, 2001, shall apply to the Purchased Shares.

7. **Miscellaneous**

7.1 Further Assurances. Each of the parties hereto shall perform such further acts and execute such further documents as may reasonably be necessary to carry out and give full effect to the provisions of this Agreement and the intentions of the parties as reflected thereby.

7.2 Governing Law; Dispute Resolution. This Agreement shall be governed by and construed according to the laws of the State of Israel, without regard to the conflict of laws provision thereof. Any claim arising under or in connection with this Agreement shall be resolved exclusively in the appropriate court in Tel-Aviv, Israel. Each of the parties hereby irrevocably consents to the exclusive jurisdiction of such courts and waives and agrees not to assert any objection to the jurisdiction or convenience thereof.

7.3 Successors and Assigns; Assignment. Except as otherwise expressly stated to the contrary herein, the provisions hereof shall inure to the benefit of, and be binding upon, the successors, assigns under law ("*Ha' avara Al Pi Din*"), heirs, executors, and administrators of the parties. Except as otherwise expressly stated to the contrary herein, each of the parties hereto shall not assign or transfer any of its rights or obligations hereunder absent the consent of the other party, which consent shall not be unreasonably withheld.

7.4 Entire Agreement; Amendment and Waiver. This Agreement and the Exhibits and Schedules hereto constitute the full and entire understanding and agreement between the parties with regard to the subject matters hereof and thereof. All prior understandings and agreements among the parties (or anyone on their behalf) are void and of no further effect. Any term of this Agreement may be amended, waived, or discharged (either prospectively or retroactively, and either generally or in a particular instance), by a written instrument signed by all the parties to this Agreement.

7.5 Notices, etc. All notices and other communications required or permitted hereunder to be given to a party to this Agreement shall be in writing and shall be telecopied or mailed by registered or certified mail, postage prepaid, or otherwise delivered by hand or by messenger, addressed to such party's address as set forth below or at such other address in Israel as the party shall have furnished to each other party in writing in accordance with this provision:

If to the Investor:
Formula Systems (1985) Ltd.
3 Abba Eban Blvd.
Herzlia, Israel
Facsimile: +972-9-959-8877
Attn: General Counsel

If to the Company:
Sapiens International Corporation N.V.
Rabin Science Park
PO Box 4011
Nes Ziona 74140 Israel
Facsimile: +972-8-938-2730
Attn: General Counsel

All such notices shall be deemed to have been duly given to the addressee thereof (i) if hand delivered, on the day of delivery, (ii) if given by facsimile transmission, on the business day on which such transmission is sent and confirmed, (iii) if mailed by registered mail, return receipt requested, five business days following the date it was mailed, to such party's address.

7.6 Delays or Omissions. No delay or omission to exercise any right, power, or remedy accruing to any party upon any breach or default under this Agreement, shall be deemed a waiver of any other breach or default therefore or thereafter occurring. Any waiver, permit, consent, or approval of any kind or character on the part of any party of any breach or default under this Agreement, or any waiver on the part of any party of any provisions or conditions of this Agreement, must be in writing and shall be effective only to the extent specifically set forth in such writing. All remedies, either under this Agreement, or by law, or otherwise afforded to any of the parties, shall be cumulative and not alternative.

7.7 Severability. If any provision of this Agreement is held by a court of competent jurisdiction to be unenforceable under applicable law, then such provision shall be excluded from this Agreement and the remainder of this Agreement shall be interpreted as if such provision were so excluded and shall be enforceable in accordance with its terms; provided, however, that in such event this Agreement shall be interpreted so as to give effect, to the greatest extent consistent with and permitted by applicable law, to the meaning and intention of the excluded provision as determined by such court of competent jurisdiction.

7.8 Counterparts. This Agreement may be executed in any number of counterparts, each of which shall be deemed an original and enforceable against the parties actually executing such counterpart, and all of which together shall constitute one and the same instrument.

7.9 Heading, Preamble, and Exhibits. The titles and subtitles used in this Agreement are used for convenience only and are not to be considered in construing or interpreting this Agreement. The Preamble, Schedules and Exhibits are an integral and inseparable part of this Agreement.

7.10 Expenses. Each party hereto shall pay its own expenses in connection with the negotiation and preparation of this Agreement and the related agreements and the consummation of the transaction contemplated hereby and thereby. Any stamp duty payable with respect to this Agreement (including in connection with the issue of the Purchased Shares) will be borne by the Company.

7.11 Limitations on Rights of Third Parties. Nothing expressed or implied in this Agreement is intended or shall be construed to confer upon or give any person, other than the Company and the Investor, any rights or remedies under this Agreement.

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IN WITNESS WHEREOF the parties have signed this Share Issuance Agreement as of the date first hereinabove set forth.

Sapiens International Corporation N.V.

Formula Systems (1985) Ltd.

By: /s/ Roni Al-Dor

By: /s/ Gad Goldstein

Name: Roni Al-Dor
Title: President & CEO

Name: Gad Goldstein
Title: President

By: /s/ Elior Brin

Name: Elior Brin
Title: EVP and CFO



**Sapiens International Corporation N.V.
2003 Share Option Plan**

A. NAME AND PURPOSE

1. **Name:** This plan, as amended from time to time, shall be known as the “Sapiens International Corporation N.V. 2003 Share Option Plan” (the “**Plan**”).
2. **Purpose:** The purpose and intent of the Plan is to provide incentives to employees and directors, consultants and contractors of Sapiens International Corporation N.V., a company incorporated under the laws of the Netherlands Antilles (the “**Company**”), or any Affiliate thereof (as defined below) and any other entity which the Board of Directors of the Company (the “**Board**”) shall decide their services are considered valuable to the Company, by providing them with opportunities to purchase Common Shares, nominal value of 2.30 euro each (“**Shares**”) of the Company, pursuant to a plan approved by the Board which is designed to benefit from, and is made pursuant to, the provisions of either Section 102 or Section 3(9) of the Israeli Income Tax Ordinance [New Version] 1961 (the “**Ordinance**”), as applicable, and the rules and regulations promulgated thereunder.

“**Affiliate**” means any “employing company” within the meaning of Section 102(a) of the Ordinance.

B. GENERAL TERMS AND CONDITIONS OF THE PLAN

3. **Administration:**

3.1 The Board may appoint a Compensation Committee, which will consist of such number of directors of the Company, as may be fixed from time to time by the Board, but no fewer than two members of the Board. The Board shall appoint the members of the Committee, may from time to time remove members from, or add members to the Committee, and shall fill vacancies in the Committee however caused. Subject to applicable law and to the Company’s incorporation documents and at the Board’s sole discretion, the Compensation Committee will have the power to administer the Plan. However, notwithstanding the above, until the Board shall delegate administration to such committee, or if such delegation is not permitted by law, or if such committee shall cease to operate the Board will administer the Plan (the Compensation Committee or the Board, as applicable, shall hereinafter be referred to as the “**Committee**”).

3.2 The Committee shall select one of its members as its chairman (the “**Chairman**”) and shall hold its meetings at such times and places, as it shall determine. The Committee may appoint a Secretary, who shall keep records of its meetings and shall make such rules and regulations for the conduct of its business, as it shall deem advisable.

3.3 Subject to the general terms and conditions of this Plan and applicable law, the Committee shall have the full authority in its discretion, from time to time and at any time, to administer the Plan and to exercise all the powers and authorities either specifically granted to it under the Plan or necessary or desirable for, or incidental to, the administration of the Plan, including without limitation the authority to grant options to purchase Shares (the “**Options**”), to interpret the Plan and to determine (i) the persons (“**Grantees**”) to whom Options shall be granted, (ii) the number of Shares subject to each Option, (iii) the exercise price for such Options, (iv) the time or times at which the same shall be granted, (v) the type of consideration payable with respect to the exercise price of Options and (vi) the schedule and conditions on which such Options may be exercised and on which such Shares shall be paid for (vii) the Fair Market Value (as defined below) of the Shares covered by each Option, (viii) alter any restrictions and conditions of any Options or Shares subject to any Options, (ix) interpret the provisions and supervise the administration of the Plan, (x) accelerate the right of an Optionee to exercise in whole or in part, any previously granted Option, (xi) prescribe, amend and rescind rules and regulations relating to the Plan, and (xii) make all other determinations deemed necessary or advisable for the administration of the Plan.

“**Fair Market Value**” means as of any date, the value of a Share determined as follows:

(a) If the Shares are listed on any established stock exchange or a national market system, including without limitation the NASDAQ National Market system, or the NASDAQ SmallCap Market of the NASDAQ Stock Market, the Fair Market Value shall be the closing sales price for such Shares (or the closing bid, if no sales were reported), as quoted on such exchange or system for the last market trading day prior to time of determination, as reported in the Wall Street Journal, or such other source as the Committee deems reliable;

(b) Without derogating from the above, solely for the purpose of determining the tax liability pursuant to Section 102(b)(3) of the Ordinance, if at the Date of Grant the Company’s shares are listed on any established stock exchange or a national market system or if the Company’s shares are registered for trading within ninety (90) days following the Date of Grant, the Fair Market Value of a Share at the Date of Grant shall be determined in accordance with the average value of the Company’s shares on the thirty (30) trading days preceding the Date of Grant or on the thirty (30) trading days following the date of registration for trading, as the case may be;

(c) If the Shares are regularly quoted by a recognized securities dealer but selling prices are not reported, the Fair Market Value shall be the mean between the high bid and low asked prices for the Shares on the last market trading day prior to the day of determination, or;

(d) In the absence of an established market for the Shares, the Fair Market Value thereof shall be determined in good faith by the Committee.

3.4 Subject to the general terms and conditions of the Plan and the Ordinance, the Committee shall have the full authority in its discretion, to determine:

(a) with respect to the grant of 102 Options (as defined in Section 5.1(a)(i) below) – whether the Company shall elect the “**Ordinary Income Route**” under Section 102(b)(1) of the Ordinance (the “**Ordinary Income Route**”) or the “**Capital Gains Route**” under Section 102(b)(2) of the Ordinance (the “**Capital Gains Route**”) (each of the Ordinary Income Route or the Capital Gains Route – a “**Taxation Route**”) for the grant of 102 Options, and the identity of the trustee, subject to Board approval, who shall be granted such 102 Options in accordance with the provisions of this Plan and the then prevailing Taxation Route. If the Committee determines that the Company shall elect one of the Taxation Routes for the grant of 102 Options, the Company shall be entitled to change such election only following the lapse of one year from the end of the tax year in which 102 Options are first granted under the then prevailing Taxation Route; and

(b) with respect to the grant of 3(9) Options (as defined in Section 5.1(a)(ii) below) – whether or not 3(9) Options shall be granted to a trustee in accordance with the terms and conditions of this Plan, and the identity of the trustee who shall be granted such 3(9) Options in accordance with the provisions of this Plan.

(c) For the avoidance of doubt, all 102 Options must be held in trust by a Trustee (as defined in Section 5.1(c) below), and as described in Section 5.1(c) below.

3.5 Notwithstanding the aforesaid, the Committee may, from time to time and at any time, grant 102 Options that will not subject to a Taxation Route, as detailed in Section 102(c) of the Ordinance (“**102(c) Options**”).

3.6 The Committee shall have the authority to grant, at its discretion, to the holder of an outstanding Option, in exchange for the surrender and cancellation of such Option, a new Option having a purchase price equal to, lower than or higher than the purchase price of the original Option so surrendered and canceled and containing such other terms and conditions as the Committee may prescribe in accordance with the provisions of the Plan.

3.7 The Committee may, from time to time, adopt such rules and regulations for carrying out the Plan as it may deem necessary. The Committee may delegate to one or more of its members or to one or more agents such administrative duties as it may deem advisable, and the Committee or any person to whom it has delegated duties as aforesaid may employ one or more persons to render advice with respect to any responsibility the Committee or such person may have under the Plan. No member of the Board or of the Committee shall be liable for any act or determination made in good faith with respect to the Plan or any Option granted thereunder.

3.8 The interpretation and construction by the Committee of any provision of the Plan or of any Option thereunder shall be final and conclusive and binding on all parties who have an interest in the Plan or any Option or Share issuance thereunder unless otherwise determined by the Board.

4. **Eligible Grantees:**

4.1 The Committee, at its discretion, may grant Options to any Employees (as defined below) and/or Non-Employees (as defined below) of the Company or of any Affiliate, all in accordance with Section 5.1(a) below.

4.2 Anything in this Plan to the contrary notwithstanding, all grants of Options to directors and office holders shall be authorized and implemented only in accordance with the provisions of applicable law, as in effect from time to time.

4.3 The grant of an Option to a Grantee hereunder, shall neither entitle such Grantee to participate, nor disqualify him from participating, in any other grant of options pursuant to this Plan or any other share option plan of the Company or of its Affiliates.

5. **Grant of Options, Issuance of Shares, Dividends and Shareholder Rights:**

5.1 Grant of Options and Issuance of Shares.

(a) Subject to the provisions of the Ordinance and applicable law,

(i) all grants of Options to Employees (as defined below), shall be made only pursuant to the provisions of Section 102 of the Ordinance and the rules and regulations promulgated thereunder ("**102 Options**"), or any other section of the Income Tax Ordinance that will be relevant for such issuance in the future; and

(ii) all grants of Options to Non-Employees (as defined below) shall be made only pursuant to the provisions of Section 3(9) of the Ordinance and the rules and regulations promulgated thereunder ("**3(9) Options**"), or any other section of the Ordinance that will be relevant for such issuance in the future.

"**Employee**" shall mean a person who is employed by the Company or its Affiliates, including an individual who is serving as director or an office holder, but excluding Controlling Shareholder.

"**Non-Employee**" shall mean a consultant, adviser, service provider, Controlling Shareholder or any other person who is not an Employee.

"**Controlling Shareholder**" shall have the meaning ascribed to it in Section 32(9) of the Ordinance.

(b) Subject to Sections 7.1 and 7.2 hereof, the effective date of the grant of an Option (the "**Date of Grant**") shall be the date the Committee resolves to grant such Option or a later date specified by the Committee in its determination relating to the award of such Option and set forth in the Notice of Grant (as defined in Section 5.1(b) below). The Committee shall promptly give the Grantee written notice of the grant of an Option (the "**Notice of Grant**").

(c) Trust. In the event 102 Options are granted under the Plan and/or Shares allocated or issued upon exercise of such 102 Options and/or other shares received subsequently following any realization of rights, including without limitation bonus shares, shall be allocated or issued to a trustee designated by the Committee in accordance with the provisions of Section 3.4 hereof and approved by the Israeli Commissioner of Income Tax, all in accordance with the provisions of Section 102(a) of the Ordinance (the "**Trustee**"). The Trustee shall hold each such Option and/or the Shares issued upon exercise thereof in trust (the "**Trust**") for the benefit of the Grantee in respect of whom such Option was granted (the "**Beneficial Grantee**").

In accordance with and as required by Section 102 of the Ordinance and the rules and regulations promulgated thereunder, the tax treatment of 102 Options (and any Shares received upon exercise of such Options) in accordance with the Ordinary Income Route or Capital Gains Route, as applicable, shall be contingent upon the Trustee holding such 102 Options for a period (the "**Trust Period**") of at least (i) one year from the end of the tax year in which the 102 Options are granted, if the Company elects the Ordinary Income Route, or (ii) two years from the end of the tax year in which the 102 Options are granted, if the Company elects the Capital Gains Route, or (iii) such other period as shall be approved by the Israeli Commissioner of Income Tax. If the requirements for Approved 102 Options are not met, the Approved 102 Options may be treated as Unapproved 102 Options, all in accordance with the provisions of Section 102 and regulations promulgated thereunder.

A Grantee granted 102 Options shall not sell or release from trust any Shares received upon exercise of a 102 Option and/or any share received subsequently following any realization of rights, including without limitation, bonus shares, (the "**Exercised Shares**") or such 102 Options from the Trust prior to the lapse of the Trust Period as required under Section 102 of the Ordinance. Notwithstanding the aforesaid, if any such sale or release occurs prior to the lapse of the Trust Period, the sanctions under Section 102(b)(4) of the Ordinance and Section 7 of the rules and regulations promulgated under Section 102 of the Ordinance shall apply to and shall be borne by such Grantee.

Upon receipt of 102 Option, the Grantee will sign an undertaking to release the Trustee from any liability in respect of any action or decision duly taken and bona fide executed in relation with the Plan, or any 102 Option or Share granted to him thereunder.

All certificates representing Shares issued to the Trustee under the Plan, for the benefit of the Grantee, shall be deposited with the Trustee, and shall be held by the Trustee until such time that such Shares are released from the Trust as herein provided.

(d) Subject to the terms hereof, at any time after the Options have vested, with respect to any Options or Shares the following shall apply:

(i) Upon the written request of any Beneficial Grantee, the Trustee shall authorize release from the Trust the Options granted, and/or the Shares issued, on behalf of such Beneficial Grantee, by executing and delivering to the Company such instrument(s) as the Company may require, giving due notice of such release to such Beneficial Grantee;

(ii) Notwithstanding anything to the contrary and in addition, if the Company's Shares are listed on a stock exchange or admitted to trading on an electronic securities trading system (such as the Nasdaq Stock Market), upon the written instructions of the Beneficial Grantee to sell any Shares issued upon exercise of Options, the Company's designee shall effect such sale in accordance with the Beneficial Grantee's instructions. However, the Company's designee shall transfer such Shares and/or transfer any consideration received therefore only after receiving the Trustee's full authorization to such an act following which the Company's designee shall be obligated to act in accordance with the Trustee's instructions. The Trustee shall withhold from such proceeds the amounts of any and all taxes required to be paid in respect of such sale and the Trustee shall remit the amount so withheld to the appropriate tax authorities and shall transfer the balance thereof directly to the Beneficial Grantee.

5.2 **Dividend.** With respect to all Shares (but excluding, for avoidance of any doubt, any unexercised Options) allocated or issued upon the exercise of Options granted under the Plan by the Grantee and held by the Grantee or by the Trustee, as the case may be, shall entitle the Beneficial Grantee thereof to receive dividends with respect thereto in accordance with the quantity of such Shares, subject to the provisions of the Company's incorporation documents (and all amendments thereto) and subject to any applicable taxation on distribution of dividends, and when applicable subject to the provisions of Section 102 and the rules, regulations or orders promulgated thereunder.

5.3 **Shareholder Rights.** The holder of an Option shall have no shareholder rights with respect to the Shares subject to the Option until such person shall have exercised the Option, paid the exercise price and become the recordholder of the purchased Shares.

6. **Reserved Shares:** The Company has reserved 500,000 authorized but unissued Shares (par value 2.30 Euro per share) for purposes of the Plan and for the purposes of any other share option plans which have been adopted by the Company, subject to adjustments as provided in Section 11 hereof. Notwithstanding the aforesaid, the Committee shall have full authority in its discretion to determine that the Company may issue, for the purposes of this Plan, previously issued Shares that are held by the Company (treasury shares), from time to time. All Shares under the Plan, in respect of which the right hereunder of a Grantee to purchase the same shall, for any reason, terminate, expire or otherwise cease to exist, shall again be available for grant through Options under the Plan.

7. **Grant of Options:**

7.1 The implementation of the Plan and the granting of any Option under the Plan shall be subject to the Company's procurement of all approvals and permits required by regulatory authorities having jurisdiction over the Plan, the Options granted under it and the Shares issued pursuant to it.

7.2 Without derogating from the foregoing, the Committee in its discretion may, subject to the provisions of the Ordinance, award to Grantees Options available under the Plan, provided however, that 102 Options granted under one of the Taxation Routes may be granted to the Trustee to be held in trust for the benefit of the Grantee for the period of time as required by the Section 102 or any rules or regulations promulgated thereunder.

7.3 The Notice of Grant shall state, *inter alia*, the number of Shares subject to each Option, the Vesting Period (as defined below), the dates when the Options may be exercised, the exercise price, whether the Options granted thereby are 102 Options (and under which Taxation Route the Options are granted) or 3 (9) Options, and such other terms and conditions as the Committee at its discretion may prescribe, provided that they are consistent with this Plan. Each Notice of Grant evidencing a 102 Option shall, in addition, be subject to the provisions of the Ordinance applicable to such options.

The term "**Vesting Period**" of an Option means, for the purpose of the Plan and its related instruments, the period between the date of grant and the date on which the holder of an Option may exercise the Option.

7.4 **Validity of Options.** Without derogating from the rights and powers of the Committee under Section 7.3 hereof, and without derogating from the provisions of Section 10 hereof, unless otherwise specified by the Committee, the Options shall be valid for a term of ten (10) years. The schedule pursuant to which such Options shall vest, and the Grantee thereof shall be entitled to pay for and acquire the Shares, shall be determined by the Committee.

7.5 **Acceleration of Vesting.** Anything herein to the contrary in this Plan notwithstanding, the Committee shall have full authority to determine any provisions regarding the acceleration of the Vesting Period of any Option or the cancellation of all or any portion of any outstanding restrictions with respect to any Option upon certain events or occurrences, and to include such provisions in the Notice of Grant on such terms and conditions as the Committee shall deem appropriate.

8. **Exercise Price:** The exercise price per Share subject to each Option shall be determined by the Committee in its sole and absolute discretion; provided, however, that such exercise price shall not be less than the par value of the Shares into which such Option is exercisable.

The exercise price shall be payable upon the exercise of the Option in a form satisfactory to the Committee, including without limitation, by cash or check. The Committee shall have the authority to postpone the date of payment on such terms as it may determine.

The exercise price shall be denominated in the currency of the primary economic environment of, either the Company or the Grantee (that is the functional currency of the Company or the currency in which the Grantee is paid) as determined by the Company.

9. **Exercise of Options:**

9.1 Options shall be exercisable pursuant to the terms under which they were awarded and subject to the terms and conditions of the Plan.

9.2 The exercise of an Option shall be made by a written notice of exercise (the "**Notice of Exercise**") in such form and method as may be determined by the Company and when applicable, by the Trustee in accordance with the requirements of Section 102, which exercise shall be effective upon delivery of such notice by the Grantee to the Company or its designee at its principal executive office, specifying the number of Shares to be purchased and containing such other terms and conditions as the Committee shall prescribe from time to time.

9.3 Anything herein to the contrary notwithstanding, but without derogating from the provisions of Section 10 hereof, if any Option has not been exercised and the Shares subject thereto not paid for within ten (10) years after the Date of Grant (or any shorter period set forth in the Notice of Grant), such Option and the right to acquire such Shares shall terminate, all interests and rights of the Grantee in and to the same shall ipso facto expire, and, if in connection therewith any Options are still held in the Trust as aforesaid, the Trust with respect thereto shall ipso facto expire, and the Shares subject to such Options shall again be available for grant through Options under the Plan, as provided for in Section 6 herein.

9.4 Each payment for Shares shall be in respect of a whole number of Shares, and shall be effected in cash or by a bank's check payable to the order of the Company, or such other method of payment acceptable to the Company.

10. **Termination of Employment or Relationship:**

10.1 Except as provided in this Section 10.1 and in Section 10.2 hereof, an Option may not be exercised unless the Grantee is then in the service or employ of the Company or any of its Affiliates (or a company or a parent or affiliate of such company issuing or assuming the Option in a transaction to which Section 11.3 hereof applies), and unless the Grantee has remained continuously so employed or has continuously performed such services since the date of grant of the Option. If the employment of a Grantee shall terminate or Grantee shall cease performance of services for the Company or an Affiliate thereof (in either event, other than by reason of death or Disability, as the latter is defined below), all Options of such Grantee that are exercisable at the time of such termination or cessation may, unless earlier terminated in accordance with their terms, be exercised within ninety (90) days after the date of such termination or cessation; provided, however, that if a Grantee shall voluntarily cease employment or performance of services or the Company shall terminate the Grantee's employment for cause (as determined by the Committee), all Options theretofore granted to such Grantee shall, to the extent not theretofore exercised, terminate on the date of such termination or cessation unless otherwise determined by the Committee.

10.2 Death or Disability of Grantee.

(a) "**Disability**" shall mean the inability of a Grantee to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or that has lasted or can be expected to last for a continuous period of not less than 12 months.

(b) If a Grantee shall die while employed by, or performing services for, the Company or an Affiliate thereof, or within ninety (90) days after the date of cessation of such Grantee's employment or performance of services other than as a result of termination for cause (or within such longer period as the Committee may provide), or if the Grantee's employment shall terminate or performance of services shall cease by reason of Disability, all Options theretofore granted to such Grantee (to the extent otherwise exercisable) may, unless earlier terminated in accordance with their terms, be exercised by the Grantee or by the Grantee's estate or by a person who acquired the right to exercise such Options by bequest or inheritance or otherwise by reason of the death or Disability of the Grantee, at any time within one year after the date of death or Disability of the Grantee. If an Option granted hereunder shall be exercised by the legal representatives of a deceased or former Grantee, written notice of such exercise shall be accompanied by a certified copy of letters testamentary or equivalent proof of the right of such legal representative to exercise such Option.

10.3 With respect to 102(c) Option, if the Grantee ceases to be employed by the Company or any Affiliate, the Grantee shall provide to the Company and/or its Affiliate a security or guarantee for the payment of tax due at the time of sale of Shares, all in accordance with the provisions of Section 102 and the rules, regulation or orders promulgated thereunder.

11. **Effect of Certain Changes:**

11.1 If there is any change in the Shares through the declaration of extraordinary dividends, stock dividends, recapitalization, stock splits, or combinations or exchanges of such shares, or other similar transactions, the number of Shares available for awards, the number of such shares covered by outstanding awards, and the price per share of Options shall be proportionately adjusted by the Committee to reflect such change in the issued Shares; provided, however, that any fractional shares resulting from such adjustment shall be eliminated.

11.2 Unless otherwise provided by the Board, in the event of the proposed dissolution or liquidation of the Company or in the event of any proposed corporate separation or division, including, but not limited to, split-up, split-off or spin-off or in the event of other similar transactions, all outstanding Options will terminate immediately prior to the consummation of such proposed action. In such case, the Committee may provide that each award granted under the Plan shall terminate as of a date to be fixed by the Committee and that not less than thirty (30) days' written notice of the date so fixed shall be given to each Grantee, who shall have the right, during the period of thirty (30) days preceding such termination, to exercise his Option, including any Option which would not otherwise be exercisable.

11.3 In the event of a proposed sale of all or substantially all of the assets of the Company or the merger of the Company with or into another corporation, any award then outstanding shall be assumed or an equivalent award shall be substituted by such successor corporation or a parent or subsidiary of such successor corporation, unless such successor corporation does not agree to assume the award or to substitute an equivalent award, in which case the Committee shall, in lieu of such assumption or substitution, provide for the realization of such outstanding awards in the manner set forth in Section 11.2 above.

11.4 In the event of a change in the Company's Shares as presently constituted that is limited to a change of all of its authorized shares of Common Stock into the same number of shares with a different par value or without par value, the shares resulting from any such change shall be deemed to be the Shares within the meaning of the Plan.

11.5 Except as herein before expressly provided in this Section 11, the Grantee of an award hereunder shall have no rights by reason of any subdivision or consolidation of shares of stock of any class or the payment of any stock dividend or any other increase or decrease in the number of shares of stock of any class or by reason of any dissolution, liquidation, merger, or consolidation or spin-off of assets or stock of another company; and any issue by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall not affect, and no adjustment by reason thereof shall be made with respect to, the number or price of Shares subject to an award. The grant of an award pursuant to the Plan shall not affect in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes of its capital or business structures or to merge or to consolidate or to dissolve, liquidate or sell, or transfer all or part of its business or assets or engage in any similar transactions.

12. **Limitations on Transfer:** No Option shall be assignable or transferable by the Grantee to whom granted otherwise than by will or the laws of descent and distribution, and an Option may be exercised during the lifetime of the Grantee only by such Grantee or by such Grantee's guardian or legal representative. The terms of such Option shall be binding upon the beneficiaries, executors, administrators, heirs and successors of such Grantee.

Any such action made directly or indirectly, and whether intended to take effect immediately or at a future date, shall be void.

As long as the Shares are held by the Trustee on behalf of the Grantee, all rights of the Grantee over the Shares are personal, cannot be transferred, assigned, pledged or mortgaged, other than by will or pursuant to the laws of descent and distribution.

13. **Term and Amendment of the Plan:**

13.1 The Plan shall become effective as of the date approved by the Board, subject to the approval of the Plan by the shareholders of the Company, and terminate on the earlier of (i) the tenth anniversary of such date or (ii) the termination of all outstanding Options as provided in Section 11 hereof. All Options outstanding at the time of a clause (i) termination event shall continue to have full force and effect in accordance with the provisions of the Plan and the documents evidencing such Options.

13.2 Subject to applicable laws, the Board shall have complete and exclusive power and authority to amend, modify, suspend or terminate the Plan in any or all respects. Notwithstanding the foregoing, and without limiting the circumstances in which shareholder approval may be required by applicable laws, rules or regulations, any amendment that would materially increase the aggregate number of Shares as to which awards may be granted under the Plan, materially increase the benefits accruing to Grantees under the Plan, materially modify the requirements as to eligibility for participation in the Plan or expand the types of awards available under the Plan shall be subject to the approval of the holders of a majority of the Shares issued and outstanding, except that any such increase or modification that may result from adjustments authorized by Section 11 shall not require such approval. Except as provided in Section 11 hereof, no such amendment or modification shall adversely affect any rights and obligations with respect to Options at the time outstanding under the Plan, unless the Grantee consents to such amendment or modification.

13.3 The Company shall obtain the approval of the Company's shareholders for the adoption of this Plan or for any amendment to this Plan, if shareholders' approval is necessary or desirable to comply with any applicable law including without limitation the securities law of the United States or the securities laws of other jurisdiction applicable to Options granted to Grantees under this Plan, or if shareholders' approval is required by any authority or by any governmental agencies or national securities exchanges including without limitation the US Securities and Exchange Commission.

14. **Withholding and Tax Consequences:** The Company's obligation to deliver Shares upon the exercise of any Options granted under the Plan shall be subject to the satisfaction of all applicable income tax and other compulsory payments withholding requirements. All tax consequences and obligations (of the Company or the Grantee) regarding any other compulsory payments arising from the grant or exercise of any Option, from the payment for Shares covered thereby or the subsequent disposition of Shares subject thereto or from any other event or act (of the Company and/or its Affiliates, the Trustee or the Grantee) hereunder, shall be borne solely by the Grantee. The Company and/or its Affiliates and/or the Trustee shall withhold taxes according to the requirements under the applicable laws, rules, and regulations, including withholding taxes at source. Furthermore, the Grantee shall indemnify the Company and/or its Affiliates and/or the Trustee, as applicable, and hold them harmless against and from any and all liability for any such tax or other compulsory payment, or interest or penalty thereon, including without limitation, liabilities relating to the necessity to withhold, or to have withheld, any such tax or other compulsory payment from any payment made to the Grantee.

The Company and/or, when applicable, the Trustee shall not be required to release any Share certificate to a Grantee until all required payments have been fully made.

15. **Miscellaneous:**

15.1 Continuance of Employment. Neither the Plan nor the grant of an Option thereunder shall impose any obligation on the Company or any of its Affiliates to continue the employment or service of any Grantee. Nothing in the Plan or in any Option granted thereunder shall confer upon any Grantee any right to continue in the employ or service of the Company or any of its Affiliates for any period of specific duration, or interfere with or otherwise restrict in any way the right of the Company to terminate such employment or service at any time, for any reason, with or without cause.

15.2 Governing Law. The Plan and all instruments issued thereunder or in connection therewith, shall be governed by, and interpreted in accordance with, the laws of the State of Israel.

15.3 Use of Funds. Any proceeds received by the Company from the sale of Shares pursuant to the exercise of Options granted under the Plan shall be used for general corporate purposes of the Company.

15.4 Multiple Agreements. The terms of each Option may differ from other Options granted under the Plan at the same time, or at any other time. The Committee may also grant more than one Option to a given Grantee during the term of the Plan, either in addition to, or in substitution for, one or more Options previously granted to that Grantee. The grant of multiple Options may be evidenced by a single Notice of Grant or multiple Notices of Grant, as determined by the Committee.

15.5 Non-Exclusivity of the Plan. The adoption of the Plan by the Board shall not be construed as amending, modifying or rescinding any previously approved incentive arrangement or as creating any limitations on the power of the Board to adopt such other incentive arrangements as it may deem desirable, including, without limitation, the granting of stock options otherwise than under the Plan, and such arrangements may be either applicable generally or only in specific cases.

15.6 Government Regulations. This Plan, the grant and exercise of Options hereunder, and the obligation of the Company to sell and deliver shares under such Options, shall be subject to all applicable laws, rules, and regulations, whether of the State of Israel or of the United States or any other State having jurisdiction over the Company and the Grantee including the registration of the shares under the United States Securities Act of 1933, and to such approvals by any governmental agencies or national securities exchanges as may be required.

**Sapiens International Corporation N.V.
2005 Special Incentive Share Option Plan**

A. NAME AND PURPOSE

1. **Name:** This plan, as amended from time to time, shall be known as the “Sapiens International Corporation N.V. 2005 Special Incentive Share Option Plan” (the “**Plan**”).

2. **Purpose:** The purpose and intent of the Plan is to provide incentives to senior executive employees and directors, consultants and contractors (both Israeli and non-Israeli) of Sapiens International Corporation N.V. (“Sapiens”), a company incorporated under the laws of the Netherlands Antilles, or any Affiliate thereof (as defined below) (collectively the “**Company**”) and any other entity which the Board of Directors of the Company (the “**Board**”) shall decide their services are considered valuable to the Company, by providing them with opportunities to purchase Common Shares, par value of 0.01 Euro each (“**Shares**”) of Sapiens, pursuant to a plan approved by the Board which is designed to benefit from, and is made pursuant to, the provisions of either Section 102 or Section 3(9) of the Israeli Income Tax Ordinance [New Version] 1961 (the “**Ordinance**”), as applicable, and the rules and regulations promulgated thereunder, as well as, with respect to non-Israeli residents, pursuant to the applicable law in their respective countries of residence.

“**Affiliate**” means any “employing company” within the meaning of Section 102(a) of the Ordinance.

B. GENERAL TERMS AND CONDITIONS OF THE PLAN

3. **Administration:**

3.1 The Board may appoint a compensation committee, which will consist of such number of directors of the Company, as may be fixed from time to time by the Board, but no fewer than two members of the Board (the “**Compensation Committee**”). The Board shall appoint the members of the Compensation Committee, may from time to time remove members from, or add members to the Compensation Committee, and shall fill vacancies in the Compensation Committee however caused. Subject to applicable law and to the Company’s incorporation documents and at the Board’s sole discretion, the Compensation Committee will have the power to administer the Plan. However, notwithstanding the above, until the Board shall delegate administration to the Compensation Committee, or if such delegation is not permitted by law, or if such committee shall cease to operate, the Board will administer the Plan (the Compensation Committee or the Board, as applicable, individually or together, shall hereinafter be referred to as the “**Committee**”).

3.2 The Committee shall select one of its members as its chairman (the “**Chairman**”) and shall hold its meetings at such times and places, as it shall determine. The Committee may appoint a Secretary, who shall keep records of its meetings and shall make such rules and regulations for the conduct of its business, as it shall deem advisable.

3.3 Subject to the general terms and conditions of this Plan and applicable law, the Committee shall have the full authority in its discretion, from time to time and at any time, to administer the Plan and to exercise all the powers and authorities either specifically granted to it under the Plan or necessary or desirable for, or incidental to, the administration of the Plan, including without limitation the authority to grant options to purchase Shares (the “Options”), to interpret the Plan and (a) to determine (i) the persons (“Grantees”) to whom Options shall be granted, (ii) the number of Shares subject to each Option, (iii) the exercise price for such Options, (iv) the time or times at which the same shall be granted, (v) the type of consideration payable with respect to the exercise price of Options, (vi) the schedule and conditions, including performance conditions, on which such Options may be exercised and on which such Shares shall be paid for, (vii) the rules and provisions, as may be necessary or appropriate to permit eligible Grantees who are not Israeli residents to participate in the Plan and/or to receive preferential tax treatment in their country of residence, with respect to the Options granted hereunder, and (viii) the Fair Market Value (as defined below) of the Shares covered by each Option, and (b) subject to Section 13.2 hereinafter, to alter any restrictions and conditions of any Options or Shares subject to any Options, (c) to interpret the provisions and supervise the administration of the Plan, (d) to accelerate the right of a Grantee to exercise in whole or in part, any previously granted Option, (e) to prescribe, amend and rescind rules and regulations relating to the Plan, and (f) to make all other determinations deemed necessary or advisable for the administration of the Plan. Unless determined otherwise by the Committee for a specific grant or grants of Options, each Option shall be exercised for one Share of Sapiens.

“Fair Market Value” means as of any date, the value of a Share determined as follows:

(a) If the Shares are listed on any established stock exchange or a national market system, including without limitation the NASDAQ Global Market system, or the NASDAQ Capital Market of the NASDAQ Stock Market, the Fair Market Value shall be the closing sales price for such Shares (or the closing bid, if no sales were reported), as quoted on such exchange or system for the last market trading day prior to time of determination, as reported on www.nasdaq.com, or such other source as the Committee deems reliable;

(b) If the Shares are regularly quoted by a recognized securities dealer but selling prices are not reported, the Fair Market Value shall be the mean between the high bid and low asked prices for the Shares on the last market trading day prior to the day of determination, or;

(c) In the absence of an established market for the Shares, the Fair Market Value thereof shall be determined in good faith by the Committee.

3.4 Subject to the general terms and conditions of the Plan, the Ordinance, and any other applicable laws and regulations, the Committee shall have the full authority in its discretion, to determine:

(a) with respect to the grant of 102 Options (as defined in Section 5.1(a)(i) below) – whether the Company shall elect the “Ordinary Income Route” under Section 102(b)(1) of the Ordinance (the “Ordinary Income Route”) or the “Capital Gains Route” under Section 102(b)(2) of the Ordinance (the “Capital Gains Route”) (each of the Ordinary Income Route or the Capital Gains Route – a “Taxation Route”) for the grant of 102 Options, and the identity of the trustee, subject to Board approval, who shall be granted such 102 Options in accordance with the provisions of this Plan and the then prevailing Taxation Route. If the Committee determines that the Company shall elect one of the Taxation Routes for the grant of 102 Options, the Company shall be entitled to change such election only following the lapse of one year from the end of the tax year in which 102 Options are first granted under the then prevailing Taxation Route; and

(b) with respect to the grant of 3(9) Options (as defined in Section 5.1(a)(ii) below) – whether or not 3(9) Options shall be granted to a trustee in accordance with the terms and conditions of this Plan, and the identity of the trustee who shall be granted such 3(9) Options in accordance with the provisions of this Plan.

(c) For the avoidance of doubt, all 102 Options granted pursuant to a Taxation Route must be held in trust by a Trustee (as defined in Section 5.1(c) below), and as described in Section 5.1(c) below.

3.5 Notwithstanding the foregoing, the Committee may, from time to time and at any time, grant 102 Options that will not subject to a Taxation Route, as detailed in Section 102(c) of the Ordinance (“**102(c) Options**”).

3.6 The Committee shall have the authority to grant, at its discretion, to the holder of an outstanding Option, in exchange for the surrender and cancellation of such Option, a new Option having a purchase price equal to, lower than or higher than the purchase price of the original Option so surrendered and canceled and containing such other terms and conditions as the Committee may prescribe in accordance with the provisions of the Plan.

3.7 The Committee may, from time to time, adopt such rules and regulations for carrying out the Plan as it may deem necessary. The Committee may delegate to one or more of its members or to one or more agents such administrative duties as it may deem advisable, and the Committee or any person to whom it has delegated duties as aforesaid may employ one or more persons to render advice with respect to any responsibility the Committee or such person may have under the Plan. No member of the Board or of the Compensation Committee shall be liable for any act or determination made in good faith with respect to the Plan or any Option granted thereunder.

3.8 The interpretation and construction by the Committee of any provision of the Plan or of any Option thereunder shall be final and conclusive and binding on all parties who have an interest in the Plan or any Option or Share issuance thereunder unless otherwise determined by the Board.

4. **Eligible Grantees:**

4.1 The Committee, at its discretion, may grant Options to any Employees (as defined below) and/or Non-Employees (as defined below) of the Company or of any Affiliate, all in accordance with Section 5.1(a) below.

4.2 Anything in this Plan to the contrary notwithstanding, all grants of Options to directors and office holders shall be authorized and implemented only in accordance with the provisions of applicable law, as in effect from time to time.

4.3 The grant of an Option to a Grantee hereunder, shall neither entitle such Grantee to participate, nor disqualify him from participating, in any other grant of options pursuant to this Plan or any other share incentive plan of the Company or of its Affiliates.

5. **Grant of Options, Issuance of Shares, Dividends and Shareholder Rights:**

5.1 Grant of Options and Issuance of Shares.

(a) Subject to the provisions of the Ordinance and applicable law (it being understood that, unless otherwise determined by the Committee, the following shall not apply to Options granted to non-Israeli Grantees),

(i) all grants of Options to Israeli Employees (as defined below), shall be made only pursuant to the provisions of Section 102 of the Ordinance and the rules and regulations promulgated thereunder ("**102 Options**"), or any other section of the Ordinance that will be relevant for such issuance in the future; and

(ii) all grants of Options to Israeli Non-Employees (as defined below) shall be made only pursuant to the provisions of Section 3(9) of the Ordinance and the rules and regulations promulgated thereunder ("**3(9) Options**"), or any other section of the Ordinance that will be relevant for such issuance in the future.

"**Employee**" shall mean a person who is employed by the Company or its Affiliates, including an individual who is serving as director or an office holder, but excluding a Controlling Shareholder.

"**Non-Employee**" shall mean a consultant, adviser, service provider, Controlling Shareholder or any other person who is not an Employee.

"**Controlling Shareholder**" shall have the meaning ascribed to it in Section 32(9) of the Ordinance.

(b) Subject to Sections 7.1 and 7.2 hereof, the effective date of the grant of an Option (the "**Date of Grant**") shall be the date the Committee resolves to grant such Option or a later date specified by the Committee in its determination relating to the award of such Option and set forth in the Notice of Grant (as defined below). The Committee shall promptly give the Grantee written notice of the grant of an Option (the "**Notice of Grant**").

(c) Trust. In the event that 102 Options are granted under the Plan pursuant to a Taxation Route, and/or Shares are allocated or issued upon exercise of such 102 Options, and/or other shares are received subsequently, following any realization of rights, including without limitation bonus shares, then all such Shares and/or Options shall be allocated or issued to a trustee, designated by the Committee in accordance with the provisions of Section 3.4 hereof and approved by the Israeli Commissioner of Income Tax, all in accordance with the provisions of Section 102(a) of the Ordinance (the "**Trustee**"). The Trustee shall hold each such Option and/or the Shares issued upon exercise thereof in trust (the "**Trust**") for the benefit of the Grantee in respect of whom such Option was granted (the "**Beneficial Grantee**").

In accordance with, and as required by, Section 102 of the Ordinance and the rules and regulations promulgated thereunder, the preferable tax treatment of 102 Options (and any Shares received upon exercise of such Options) in accordance with the Ordinary Income Route or Capital Gains Route, as applicable, shall be contingent upon the Trustee holding such 102 Options in Trust for the applicable period of time in respect of such Options and Exercised Shares (as defined below), as prescribed by the Ordinance (as may be amended, from time to time), or approved by the Israeli tax authorities (the “**Trust Period**”). If the requirements for Approved 102 Options are not met, the Approved 102 Options may be treated as Unapproved 102 Options, each as defined in the Ordinance and all in accordance with the provisions of Section 102 of the Ordinance and the regulations promulgated thereunder.

A Grantee granted 102 Options shall not sell or release from trust any Shares received upon exercise of a 102 Option and/or any share received subsequently following any realization of rights, including without limitation, bonus shares, (the “**Exercised Shares**”) or such 102 Options from the Trust prior to the lapse of the Trust Period as required under Section 102 of the Ordinance. Notwithstanding the aforesaid, if any such sale or release occurs prior to the lapse of the Trust Period, the sanctions under Section 102(b)(4) of the Ordinance and Section 7 of the rules and regulations promulgated under Section 102 of the Ordinance shall apply to and shall be borne by such Grantee.

Upon receipt of a 102 Option, the Grantee will sign an undertaking to release the Trustee from any liability in respect of any action or decision duly taken and bona fide executed in relation with the Plan, or any 102 Option or Share granted to the Trustee thereunder.

All certificates representing Shares issued to the Trustee under the Plan, for the benefit of the Grantee, shall be deposited with the Trustee, and shall be held by the Trustee until such time that such Shares are released from the Trust as herein provided.

(d) Subject to the terms hereof, at any time after the 102 Options granted pursuant to a Taxation Route have vested, with respect to any Options or Shares, the following shall apply:

(i) Upon the written request of any Beneficial Grantee, the Trustee shall authorize release from the Trust the Options granted, and/or the Shares issued, on behalf of such Beneficial Grantee, by executing and delivering to the Company such instrument(s) as the Company may require, giving due notice of such release to such Beneficial Grantee;

(ii) Notwithstanding anything to the contrary and in addition, if the Company’s Shares are listed on a stock exchange or admitted to trading on an electronic securities trading system (such as the Nasdaq Stock Market), upon the written instructions of the Beneficial Grantee to sell any Shares issued upon exercise of Options, the Company’s designee shall effect such sale in accordance with the Beneficial Grantee’s instructions. However, the Company’s designee shall transfer such Shares and/or transfer any consideration received therefore only after receiving the Trustee’s full authorization to such an act following which the Company’s designee shall be obligated to act in accordance with the Trustee’s instructions. The Trustee shall withhold from such proceeds the amounts of any and all taxes required to be paid in respect of such sale and the Trustee shall remit the amount so withheld to the appropriate tax authorities and shall transfer the balance thereof directly to the Beneficial Grantee.

5.2 **Dividend.** All Shares (but excluding, for avoidance of any doubt, any unexercised Options) allocated or issued upon the exercise of Options granted under the Plan and held by the Grantee or by the Trustee, as the case may be, shall entitle the Beneficial Grantee thereof to receive dividends with respect thereto in accordance with the quantity of such Shares, subject to the provisions of the Company's incorporation documents (and all amendments thereto) and subject to any applicable taxation on distribution of dividends, and when applicable subject to the provisions of Section 102 and the rules, regulations or orders promulgated thereunder. Cash dividends shall be paid or distributed directly to such Beneficial Grantee, whereas other rights received in respect of Exercised Shares, shall be deposited with the Trustee, unless applicable law allows or requires otherwise.

5.3 **Shareholder Rights.** The holder of an Option shall have no shareholder rights with respect to the Shares subject to the Option until such person shall have exercised the Option, paid the exercise price and become the recordholder of the purchased Shares.

6. **Reserved Shares:** The Company has reserved 2,000,000 authorized but unissued Shares (par value 0.01 Euro per share) for purposes of the Plan and for the purposes of any other share incentive plans which have been adopted by the Company, subject to adjustments as provided in Section 11 hereof. Notwithstanding the aforesaid, the Committee shall have full authority in its discretion to determine that the Company may issue, for the purposes of this Plan, previously issued Shares that are held by the Company (treasury shares), from time to time. All Shares under the Plan, in respect of which the right hereunder of a Grantee to purchase the same shall, for any reason, terminate, expire or otherwise cease to exist, shall again be available for grant through Options under the Plan.

7. **Grant of Options:**

7.1 The implementation of the Plan and the granting of any Option under the Plan shall be subject to the Company's procurement of all approvals and permits required by applicable law and regulatory authorities having jurisdiction over the Plan, the Options granted under it and the Exercised Shares issued pursuant to it.

7.2 The Notice of Grant shall state, *inter alia*, the number of Shares subject to each Option, the Vesting Period (as defined below), the dates when the Options may be exercised, the exercise price, whether the Options granted thereby are 102 Options (and whether such 102 Options are granted under a Taxations Route (and if so, under which Taxation Route the Options are granted) or as 102(c) Options) or 3(9) Options, and such other terms and conditions as the Committee in its discretion may prescribe, provided that they are consistent with this Plan. Each Notice of Grant evidencing a 102 Option shall, in addition, be subject to the provisions of the Ordinance applicable to such options.

The term "**Vesting Period**" of an Option means, for the purpose of the Plan and its related instruments, the period between the Date of Grant and the date on which the holder of an Option may exercise the Option.

Unless otherwise determined by the Committee or unless certain conditions set forth in the Notice of Grant are met: (a) Options granted pursuant to the Plan will have an exercise price of \$3.00 per Share, (b) no portion of the Options granted pursuant to the Plan will be available for exercise for a period of 5 years following the Date of Grant (i.e. the Vesting Period for each Option shall be five (5) years from the Date of Grant), and (c) the Grantee must be employed by and/or provide services to the Company throughout the entire five (5) year Vesting Period for the Option to be exercisable at the end of the Vesting Period.

7.3 **Validity of Options.** Without derogating from the rights and powers of the Committee under Section 7.2 hereof, and without derogating from the provisions of Section 10 hereof, unless otherwise specified by the Committee, the Options shall be valid for a term of ten (10) years. The schedule pursuant to which such Options shall vest, and the Grantee thereof shall be entitled to pay for and acquire the Shares, shall be determined by the Committee.

7.4 **Acceleration of Vesting.** Anything herein to the contrary in this Plan notwithstanding, the Committee shall have full authority to determine any provisions regarding the acceleration of the Vesting Period of any Option or the cancellation of all or any portion of any outstanding restrictions with respect to any Option upon certain events or occurrences, and to include such provisions in the Notice of Grant on such terms and conditions as the Committee shall deem appropriate.

8. **Exercise Price:** The exercise price per Share subject to each Option shall be determined by the Committee in its sole and absolute discretion; provided, however, that such exercise price shall not be less than the par value of the Shares into which such Option is exercisable.

The exercise price shall be payable upon the exercise of the Option in a form satisfactory to the Committee, including without limitation, by cash or check. The Committee shall have the authority to postpone the date of payment on such terms as it may determine.

The exercise price shall be denominated in the currency of the primary economic environment of, either the Company or the Grantee (that is the functional currency of the Company or the currency in which the Grantee is paid) as determined by the Company.

9. **Exercise of Options:**

9.1 Options shall be exercisable pursuant to the terms under which they were awarded and subject to the terms and conditions of the Plan.

9.2 The exercise of an Option shall be made by a written notice of exercise (the "**Notice of Exercise**") in such form and method as may be determined by the Company and when applicable, by the Trustee in accordance with the requirements of Section 102, which exercise shall be effective upon delivery of such notice by the Grantee (or the Beneficial Grantee, if applicable) to the Company at its principal executive office or to its designee at such location specified by the designee, specifying the number of Shares to be purchased, accompanying by the exercise price in respect thereto, and containing such other terms and conditions as the Committee shall prescribe from time to time.

9.3 Notwithstanding the provisions of Section 9.2 above, and unless otherwise provided by the Committee, all Options shall be exercised using the following method (the "**Net Exercise**"):

(a) The Company shall issue to the Grantee (or to the Trustee, as applicable) a number of Shares having an aggregate Fair Market Value (as defined above) equal to the Benefit Amount (as defined below) (the “**Net Exercise Shares**”);

For the purposes of this Section the “**Benefit Amount**” shall mean the difference between:

(i) (A) the Fair Market Value of a Share, multiplied by (B) the number of Shares subject to the Options for which a Notice of Exercise has been delivered to the Company; and

(ii) (A) the exercise price per Share, multiplied by (B) the number of Shares subject to the Options for which a Notice of Exercise has been delivered to the Company.

(b) The Grantee shall not be required to pay to the Company any sum with respect to the exercise of such Options, other than a sum equal to the aggregate par value of the Net Exercise Shares (the “**Par Value Sum**”). However, the Company shall have the full authority in its discretion to determine at any time that the Par Value Sum shall not be paid and that the Company shall capitalize applicable profits or take any other action to ensure that it meets any requirement of applicable law regarding issuance of Shares for consideration that is lower than the nominal value of such Shares;

(c) No fractional Shares will be issued to the Grantee and the number of Shares granted to the Grantee under the Plan shall be rounded off (upward or downward) to the nearest whole number.

9.4 Anything herein to the contrary notwithstanding, but without derogating from the provisions of Section 10 hereof, and unless the Committee determines otherwise, if any Option has not been exercised and the Shares subject thereto not paid for within ten (10) years after the Date of Grant (or any shorter period set forth in the Notice of Grant), such Option and the right to acquire such Shares shall terminate, all interests and rights of the Grantee in and to the same shall ipso facto expire, and, if in connection therewith any Options are still held in the Trust as aforesaid, the Trust with respect thereto shall ipso facto expire, and the Shares subject to such Options shall again be available for grant through Options under the Plan, as provided for in Section 6 above.

9.5 Each payment for Shares shall be in respect of a whole number of Shares, and shall be effected in cash or by a bank’s check payable to the order of the Company, or such other method of payment acceptable to the Company.

10. **Termination of Employment or Relationship:**

10.1 Except as provided in this Section 10.1 and in Section 10.2 below, an Option may not be exercised unless the Grantee is then in the service or employ of the Company or any of its Affiliates (or a company or a parent or affiliate of such company issuing or assuming the Option in a transaction to which Section 11.3 hereof applies), and unless the Grantee has remained continuously so employed or has continuously performed such services since the Date of Grant. If the employment of a Grantee shall terminate or Grantee shall cease performance of services for the Company or an Affiliate thereof (in either event, other than by reason of death or Disability, as the latter is defined below), all Options of such Grantee that are exercisable at the time of such termination or cessation may, unless earlier terminated in accordance with their terms, be exercised within ninety (90) days after the date of such termination or cessation; provided, however, that if a Grantee shall voluntarily cease employment or performance of services or the Company shall terminate the Grantee’s employment for cause (as determined by the Committee), all Options theretofore granted to such Grantee shall, to the extent not theretofore exercised, terminate on the date of such termination or cessation unless otherwise determined by the Committee.

10.2 Death or Disability of Grantee.

(a) “**Disability**” shall mean the inability of a Grantee to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or that has lasted or can be expected to last for a continuous period of not less than 12 months.

(b) If a Grantee shall die while employed by, or performing services for, the Company or an Affiliate thereof, or within ninety (90) days after the date of cessation of such Grantee’s employment or performance of services other than as a result of termination for cause (or within such longer period as the Committee may provide), or if the Grantee’s employment shall terminate or performance of services shall cease by reason of Disability, all Options theretofore granted to such Grantee (to the extent otherwise exercisable) may, unless earlier terminated in accordance with their terms, be exercised by the Grantee or by the Grantee’s estate or by a person who acquired the right to exercise such Options by bequest or inheritance or otherwise by reason of the death or Disability of the Grantee, at any time within one year after the date of death or Disability of the Grantee. If an Option granted hereunder shall be exercised by the legal representatives of a deceased or former Grantee, written notice of such exercise shall be accompanied by a certified copy of letters testamentary or equivalent proof of the right of such legal representative to exercise such Option.

10.3 With respect to a 102(c) Option, if the Grantee ceases to be employed by the Company or any Affiliate, the Grantee shall provide to the Company and/or its Affiliate a security or guarantee for the payment of tax due at the time of sale of Shares, all in accordance with the provisions of Section 102 and the rules, regulation or orders promulgated thereunder.

11. **Effect of Certain Changes:**

11.1 If there is any change in the Shares through the declaration of extraordinary dividends, stock dividends, recapitalization, stock splits, or combinations or exchanges of such shares, or other similar transactions, the number of Shares available for awards, the number of such shares covered by outstanding awards, and the price per share of Options shall be proportionately adjusted by the Committee to reflect such change in the issued Shares; provided, however, that any fractional shares resulting from such adjustment shall be eliminated.

11.2 Unless otherwise provided by the Board, in the event of the proposed dissolution or liquidation of the Company or in the event of any proposed corporate separation or division, including, but not limited to, split-up, split-off or spin-off or in the event of other similar transactions, all outstanding Options will terminate immediately prior to the consummation of such proposed action. In such case, the Committee may provide that each award granted under the Plan shall terminate as of a date to be fixed by the Committee and that not less than thirty (30) days’ written notice of the date so fixed shall be given to each Grantee, who shall have the right, during the period of thirty (30) days preceding such termination, to exercise his or her Option, including any Option which would not otherwise be exercisable.

11.3 In the event of a proposed sale of all or substantially all of the assets of the Company or the merger of the Company with or into another corporation, any award then outstanding shall be assumed or an equivalent award shall be substituted by such successor corporation or a parent or subsidiary of such successor corporation, unless such successor corporation does not agree to assume the award or to substitute an equivalent award, in which case the Committee shall, in lieu of such assumption or substitution, provide for the realization of such outstanding awards in the manner set forth in Section 11.2 above.

11.4 In the event of a change in the Company's Shares as presently constituted that is limited to a change of all of its authorized shares of Common Stock into the same number of shares with a different par value or without par value, the shares resulting from any such change shall be deemed to be the Shares within the meaning of the Plan.

11.5 Except as herein before expressly provided in this Section 11, the Grantee of an award hereunder shall have no rights by reason of any subdivision or consolidation of shares of stock of any class or the payment of any stock dividend or any other increase or decrease in the number of shares of stock of any class or by reason of any dissolution, liquidation, merger, or consolidation or spin-off of assets or stock of another company; and any issue by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall not affect, and no adjustment by reason thereof shall be made with respect to, the number or price of Shares subject to an award, except as provided herein. The grant of an award pursuant to the Plan shall not affect in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes of its capital or business structures or to merge or to consolidate or to dissolve, liquidate or sell, or transfer all or part of its business or assets or engage in any similar transactions.

12. **Limitations on Transfer:**

12.1 No Option shall be assignable or transferable by the Grantee to whom granted otherwise than by will or the laws of descent and distribution, and an Option may be exercised during the lifetime of the Grantee only by such Grantee or by such Grantee's guardian or legal representative. The terms of such Option shall be binding upon the beneficiaries, executors, administrators, heirs and successors of such Grantee.

Any such action made directly or indirectly, and whether intended to take effect immediately or at a future date, shall be void.

As long as the Shares are held by the Trustee on behalf of the Grantee, all rights of the Grantee over the Shares are personal, cannot be transferred, assigned, pledged or mortgaged, other than by will or pursuant to the laws of descent and distribution.

12.2 **Underwriter's Lock-up.** The Grantee's rights to sell Exercised Shares may be subject to certain limitations (including a lock-up period), as will be requested by the Company or its underwriters, from time to time, or upon a specific occurrence, and the Grantee unconditionally agrees and accepts any such limitations.

13. **Term and Amendment of the Plan:**

13.1 The Plan shall become effective as of the date approved by the Board, subject to the approval of the Plan by the shareholders of the Company, and terminate on the earlier of (i) the tenth anniversary of such date or (ii) the termination of all outstanding Options as provided in Section 11 hereof. All Options outstanding at the time of a clause (i) termination event shall continue to have full force and effect in accordance with the provisions of the Plan and the documents evidencing such Options.

13.2 Subject to applicable laws, the Board shall have complete and exclusive power and authority to amend, modify, suspend or terminate the Plan in any or all respects. In addition, in the event the Committee wishes to grant Options to non-Israeli Grantees, the Board may adopt, as part of this Plan and based on it, sub-plans, in order to comply with all relevant and applicable laws and regulations of the country of residence of such Grantees. Notwithstanding the foregoing, and without limiting the circumstances in which shareholder approval may be required by applicable laws, rules or regulations, any amendment that would materially increase the aggregate number of Shares as to which awards may be granted under the Plan, materially increase the benefits accruing to Grantees under the Plan, materially modify the requirements as to eligibility for participation in the Plan or expand the types of awards available under the Plan shall be subject to the approval of the holders of a majority of the Shares issued and outstanding, except that any such increase or modification that may result from adjustments authorized by Section 11 shall not require such approval. Except as provided in Section 11 hereof, no such amendment or modification shall adversely affect any rights and obligations with respect to Options at the time outstanding under the Plan, unless the Grantee consents to such amendment or modification.

13.3 The Company shall obtain the approval of the Company's shareholders for the adoption of this Plan or for any amendment to this Plan, if shareholders' approval is necessary or desirable to comply with any applicable law including without limitation the securities law of the United States or the securities laws of other jurisdiction applicable to Options granted to Grantees under this Plan, or if shareholders' approval is required by any authority or by any governmental agencies or national securities exchanges including without limitation the US Securities and Exchange Commission.

14. **Withholding and Tax Consequences:** The Company's obligation to deliver Shares upon the exercise of any Options granted under the Plan shall be subject to the satisfaction of all applicable income tax and other compulsory payments withholding requirements. All tax consequences and obligations (of the Company or the Grantee) regarding any other compulsory payments arising from the grant or exercise of any Option, from the payment for Shares covered thereby or the subsequent disposition of Shares subject thereto or from any other event or act (of the Company and/or its Affiliates, the Trustee or the Grantee) hereunder, shall be borne solely by the Grantee. The Company and/or its Affiliates and/or the Trustee shall withhold taxes according to the requirements under the applicable laws, rules, and regulations, including withholding taxes at source. Furthermore, the Grantee shall indemnify the Company and/or its Affiliates and/or the Trustee, as applicable, and hold them harmless against and from any and all liability for any such tax or other compulsory payment, or interest or penalty thereon, including without limitation, liabilities relating to the necessity to withhold, or to have withheld, any such tax or other compulsory payment from any payment made to the Grantee.

The Company and/or, when applicable, the Trustee shall not be required to release any Share certificate to a Grantee until all required payments have been fully made.

15. **Miscellaneous:**

15.1 Continuance of Employment. Neither the Plan nor the grant of an Option thereunder shall impose any obligation on the Company or any of its Affiliates to continue the employment or service of any Grantee. Nothing in the Plan or in any Option granted thereunder shall confer upon any Grantee any right to continue in the employ or service of the Company or any of its Affiliates for any period of specific duration, or interfere with or otherwise restrict in any way the right of the Company to terminate such employment or service at any time, for any reason, with or without cause.

15.2 Governing Law. The Plan and all instruments issued thereunder or in connection therewith, shall, with the exception of the provisions of the Plan specifically relating to non-Israeli Grantees, be governed by, and interpreted in accordance with, the laws of the State of Israel.

15.3 Use of Funds. Any proceeds received by the Company from the sale of Shares pursuant to the exercise of Options granted under the Plan shall be used for general corporate purposes of the Company.

15.4 Multiple Agreements. The terms of each Option may differ from other Options granted under the Plan at the same time, or at any other time. The Committee may also grant more than one Option to a given Grantee during the term of the Plan, either in addition to, or in substitution for, one or more Options previously granted to that Grantee. The grant of multiple Options may be evidenced by a single Notice of Grant or multiple Notices of Grant, as determined by the Committee.

15.5 Non-Exclusivity of the Plan. The adoption of the Plan by the Board shall not be construed as amending, modifying or rescinding any previously approved incentive arrangement or as creating any limitations on the power of the Board to adopt such other incentive arrangements as it may deem desirable, including, without limitation, the granting of stock options otherwise than under the Plan, and such arrangements may be either applicable generally or only in specific cases.

15.6 Government Regulations. This Plan, the grant and exercise of Options hereunder, and the obligation of the Company to sell and deliver shares under such Options, shall be subject to all applicable laws, rules, and regulations, whether of the State of Israel or of the United States or any other State having jurisdiction over the Company and the Grantee including the registration of the shares under the United States Securities Act of 1933, and to such approvals by any governmental agencies or national securities exchanges as may be required.

15.7 The provisions of this Plan shall not be construed as deviating from any applicable laws rules and regulations.

The Company's Subsidiaries

Sapiens International Corporation B.V.: incorporated in The Netherlands
Sapiens Israel Software Systems Ltd.: incorporated in Israel
Sapiens Technologies (1982) Ltd.: incorporated in Israel
Sapiens Americas Corporation: incorporated in New York
Sapiens (UK) Limited: incorporated in England
Sapiens France S.A.S.: incorporated in France
Sapiens Deutschland GmbH: incorporated in Germany
Sapiens Japan Co.: incorporated in Japan
Sapiens (Schweiz) AG: incorporated in Switzerland

Consent of Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statement (Forms S-8 No.s 33-64208 and 333-10622) pertaining to 1992 Stock Option and Incentive Plan of Sapiens International Corporation N.V. of our report dated June 26, 2007, with respect to the consolidated financial statements of Sapiens International Corporation N.V. included in the Annual Report (Form 20-F) for the year ended December 31, 2006.

Yours Truly,

June 26, 2007
Tel-Aviv, Israel

/s/ Kost Forer Gabbay & Kasierer
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

CERTIFICATIONS

I, Ron Al Dor, certify that:

1. I have reviewed this annual report on Form 20-F of Sapiens International Corporation N.V.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the company and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Dated: June 28, 2007

By: /s/ Ron Al Dor

President and Chief Executive Officer
(Principal Executive Officer)

I, Elior Brin, certify that:

1. I have reviewed this annual report on Form 20-F of Sapiens International Corporation N.V.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the company and have:
 - (a) Designed such disclosure controls and procedures or caused such disclosure controls and procedures designed under our supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (c) Disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Dated: June 28, 2007

By: /s/ Elior Brin

Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report on Form 20-F of Sapiens International Corporation N.V. (the "Company") for the period ended December 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Ron Al Dor, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: June 28, 2007

By: /s/ Ron Al Dor

President and Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to Sapiens International Corporation N.V. and will be retained by Sapiens International Corporation N.V. and furnished to the Securities and Exchange Commission or its staff upon request.

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report on Form 20-F of Sapiens International Corporation N.V. (the "Company") for the period ended December 31, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Elijior Brin, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: June 28, 2007

By: /s/ Elijior Brin

Executive Vice President and Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Sapiens International Corporation N.V. and will be retained by Sapiens International Corporation N.V. and furnished to the Securities and Exchange Commission or its staff upon request.
