Allot Communications Ltd.
Form 20-F
March 27, 2014

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

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FORM 20-F

(Mark One)

- o REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934
- x REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934
- o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
- o 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……

For the transition period from _____ to _____

Commission File Number 001-33129

ALLOT COMMUNICATIONS LTD.
(Exact Name of Registrant as specified in its charter)

ISRAEL
(Jurisdiction of incorporation or organization)

22 Hanagar Street
Neve Ne'eman Industrial Zone B
Hod-Hasharon 4501317
Israel
(Address of principal executive offices)

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

Title of each class	Name of each exchange on which registered
Ordinary Shares, par value NIS 0.10 per share	Nasdaq Global Select Market

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

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

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of December 31, 2013: 32,877,118 ordinary shares, NIS 0.10 par value per share

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

Yes o No x

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 o No x

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

Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (section 229.405 of this chapter), and (2) has been subject to such filing requirements for the past 90 days:

Yes x No o

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 (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

U.S. GAAP x	International Financial Reporting Standards as issued by the International Accounting Standards Board o	Other o

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

Item 17 o Item 18 o

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 o No x

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PRELIMINARY NOTES

Terms

As used herein, and unless the context suggests otherwise, the terms “Allot,” “Company,” “we,” “us” or “ours” refer to Al Communications Ltd.

Forward-Looking Statements

In addition to historical facts, this annual report on Form 20-F contains forward-looking statements within the meaning of Section 27A of the U.S. Securities Act of 1933, as amended (the “Securities Act”), Section 21E of the U.S. Securities Exchange Act of 1934, as amended (the “Exchange Act”) and the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. We have based these forward-looking statements on our current expectations and projections about future events. These statements include but are not limited to:

- statements regarding projections of capital expenditures;
- statements regarding competitive pressures;
- statements regarding expected revenue growth;
- statements regarding the expected growth demand for video caching and optimization;
- statements regarding trends in mobile networks, including the development of a digital lifestyle, over-the-top applications, the need to manage mobile network traffic and cloud computing, among others;
- statements regarding our ability to develop technologies to meet our customer demands and expand our product and service offerings;
- statements regarding the acceptance and growth of our value-added services by our customers;
- statements regarding the expected growth in the use of particular broadband applications;
- statements as to our ability to meet anticipated cash needs based on our current business plan;
- statements as to the impact of the rate of inflation and the political and security situation on our business;
- statements regarding the price and market liquidity of our ordinary shares;
- statements as to our ability to retain our current suppliers and subcontractors; and
- statements regarding our future performance, sales, gross margins, expenses (including stock-based compensation expenses) and cost of revenues.

These statements may be found in the sections of this annual report on Form 20-F entitled “ITEM 3: Key Information—Risk Factors,” “ITEM 4: Information on Allot,” “ITEM 5: Operating and Financial Review and Prospects,” “ITEM 10: Additional Information—Taxation—United States Federal Income Taxation—Passive Foreign Investment Company Considerations” and elsewhere in this annual report, including the section of this annual report entitled “ITEM 4: Information on Allot—Business Overview—Overview” and “ITEM 4: Information on Allot—Business Overview—Indu

Background," which contain information obtained from independent industry sources. Actual results could differ materially from those anticipated in these forward-looking statements due to various factors, including all the risks discussed in "ITEM 3: Key Information—Risk Factors" and elsewhere in this annual report.

In addition, statements that use the terms "may," "believe," "expect," "plan," "intend," "estimate," "anticipate" "predict," "po similar expressions are intended to identify forward-looking statements. All forward-looking statements in this annual report reflect our current views about future events and are based on assumptions and are subject to risks and uncertainties that could cause our actual results to differ materially from future results expressed or implied by the forward-looking statements. Many of these factors are beyond our ability to control or predict. You should not put undue reliance on any forward-looking statements. Unless we are required to do so under U.S. federal securities laws or other applicable laws, we do not intend to update or revise any forward-looking statements.

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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

You should read the following selected consolidated financial data in conjunction with "ITEM 5: Operating and Financial Review and Prospects" and our consolidated financial statements and the related notes included elsewhere in this annual report on Form 20-F. The consolidated statements of operations data for the years ended December 31, 2011, 2012 and 2013 the consolidated balance sheet data as of December 31, 2012 and 2013 are derived from our audited consolidated financial statements included in "ITEM 18: Financial Statements," which have been prepared in accordance with generally accepted accounting principles in the United States. The consolidated statements of operations for the years ended December 31, 2009 and 2010 and the consolidated balance sheet data as of December 31, 2009, 2010 and 2011 have been derived from our audited consolidated financial statements which are not included in this annual report.

	Year ended December 31,				
	2009	2010	2011	2012	2013
	(in thousands of U.S. dollars, except per share and share data)				
Consolidated Statements of Operations:					
Revenues:					
Products	$29,641	$40,852	$56,810	$77,127	$66,318
Services	12,110	16,120	20,943	27,625	30,227
Total revenues	41,751	56,972	77,753	104,752	96,545
Cost of revenues(2):					
Products	10,094	14,015	19,540	26,857	20,572
Services	1,741	1,970	2,635	4,180	6,246
Expenses related to the settlement of the Office of the Chief Scientist grants(1)	-	-	-	15,886	-
Total cost of revenues	11,835	15,985	22,175	46,923	26,818
Gross profit	29,916	40,987	55,578	57,829	69,727
Operating expenses:					
Research and development, gross	11,705	14,038	16,896	24,915	28,073
Less royalty-bearing grant participation	2,440	2,774	3,674	2,855	1,051
Research and development, net(2)	9,265	11,264	13,222	22,060	27,022
Sales and marketing(2)	20,408	22,021	26,543	34,127	39,817
General and administrative(2)	5,541	5,473	7,474	10,664	9,952
Total operating expenses	35,214	38,758	47,239	66,851	76,791
Operating income (loss)	(5,298)	2,229	8,339	(9,022)	(7,064)
Financing income (expenses), net	(2,311)	(7,907)	415	1,358	727
	(7,609)	(5,678)	8,754	(7,664)	(6,337)

Income (loss) before income tax expenses (benefit)					
Income tax expenses (benefit)	63	84	(55)	(926)	120
Net income (loss)	$(7,672)	$(5,762)	$8,809	$(6,738)	$(6,457)
Basic net earnings (loss) per share	$(0.35)	$(0.25)	$0.35	$(0.21)	$(0.20)
Diluted net earnings (loss) per share	$(0.35)	$(0.25)	$0.33	$(0.21)	$(0.20)
Weighted average number of shares used in computing basic net earnings (loss) per share	22,185,702	22,831,014	25,047,771	31,959,921	32,680,766
Weighted average number of shares used in computing diluted net earnings (loss) per share	22,185,702	22,831,014	27,071,872	31,959,921	32,680,766

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(1) Represents the full balance of the contingent liability related to grants received, which was paid in 2013.

(2) Includes stock-based compensation expense related to options granted to employees and others as follows:

	Year ended December 31,				
	2009	2010	2011	2012	2013
	(in thousands of U.S. dollars)				
Cost of revenues	$104	$95	$103	$222	$368
Research and development expenses, net	357	352	442	1,186	1,666
Sales and marketing expenses	775	851	1,001	2,060	3,106
General and administrative expenses	1,062	692	710	1,349	2,591
Total	$2,298	$1,990	$2,256	$4,817	$7,731

	At December 31,				
	2009	2010	2011	2012	2013
	(in thousands of U.S. dollars)				
Consolidated balance sheet data:					
Cash and cash equivalents	$36,470	$42,858	$116,682	$50,026	$42,813
Short-term deposits and restricted deposits	2,324	1,060	25,138	78,188	38,000
Marketable securities	14,490	15,531	17,580	14,841	40,798
Working capital	38,179	59,841	158,937	131,598	139,934
Total assets	82,943	95,187	197,058	221,791	199,257
Total liabilities	22,531	30,199	34,489	52,670	29,330
Accumulated deficit	(63,694)	(69,456)	(60,647)	(67,385)	(73,842)
Share capital	492	527	720	761	774
Total shareholders' equity	60,412	64,988	162,569	169,121	169,927

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for Offer and Use of Proceeds

Not applicable.

D. Risk Factors

Investing in our ordinary shares involves a high degree of risk. You should consider carefully the risks described below, together with the financial and other information contained in this annual report, before deciding to invest in our ordinary shares. If any of the following risks actually occurs, our business, financial condition and results of operations would suffer. In this case, the trading price of our ordinary shares would likely decline and you might lose all or part of your investment. The risks described below are not the only ones we face. Additional risks that we currently do not know about or that we currently believe to be immaterial may also impair our business operations.

Risks Relating to Our Business

We have a history of losses and may not be able to achieve or maintain profitability in the future.

In 2013, we had a net loss of $6.5 million. We have had a history of net losses in all prior fiscal years since our inception, other than in 2006 and 2011. Our net losses in 2013 were a result of an increase in the company's costs due to the last two acquisitions and due to the decrease in the company's revenues. Our net losses in 2012 were a result of expenses related to the settlement of approximately $15.9 million in grants from Office of the Chief Scientist of the Ministry of Economy (formerly the Ministry of Industry, Trade and Labor), or the Office of the Chief Scientist. Our net losses in 2010 were caused or exacerbated by losses resulting from our realized losses and impairment charges related to auction-rate securities, which we have subsequently sold. We can provide no assurance that we will be able to achieve or maintain profitability, and we may incur losses in the future if we do not generate sufficient revenues.

We may be unable to compete effectively with other companies in our market who offer, or may in the future offer, competing technologies.

We compete in a rapidly evolving and highly competitive sector of the networking technology market, with large incumbent companies having significant market share and established relationships with service providers. We face significant competition from router and switch infrastructure companies, such as Cisco Systems, Inc., Telefonaktiebolager LM Erricson and Huawei Technologies Co., Ltd., which integrate functionalities into their platforms addressing some of the problems that our products address. Our competitors have also identified the potential market opportunity offered by the largest service providers, referred to as Tier 1 operators, and we therefore face intense competition in this portion of our market. Our principal competitors in the field of standalone intelligent policy enforcement and traffic management products enabled by DPI technology are Sandvine Inc. and Procera Networks, Inc. We also face competition from companies that offer partial or alternative solutions addressing limited aspects of the challenges facing broadband providers, such as network monitoring or security.

Our competitors may announce new products, services or enhancements that better meet the needs of customers or changing industry requirements, or may offer alternative methods to achieve customer objectives. One of our direct competitors, Cisco Systems, is substantially larger than we are and has significantly greater financial, sales and marketing, technical, manufacturing and other resources. As the mobile DPI market has grown, new competitors have entered and may continue to enter the market. The entry of new competitors into our market (for example F5 Networks) and acquisitions of our existing competitors by companies with significant resources and established relationships with our potential customers could result in increased competition and harm to our business. Increased competition may cause price reductions, reduced gross margins and loss of market share, any of which could have a material adverse effect on our business, financial condition or result of operations.

We depend on one or more significant customers and the loss of any such significant customer could harm our results of operations.

The loss of any significant customer or a significant decrease in business from any such customer could harm our results of operations and financial condition. In addition, revenues from individual customers may fluctuate from time to time based on the timing and the terms under which further orders are received and the duration of the delivery and implementation of such orders. We derived 15% and 14% of our total revenues in 2011 and 2012, respectively, from one global Tier 1 mobile operator group. In 2013, we derived 45% of our total revenues from three Tier 1 mobile and fixed operators. The revenues derived from each of these three operators were higher than 10% from our total revenues.

Industry consolidation may lead to increased competition and may harm our operating results.

Our market may be subject to industry consolidation, as companies attempt to maintain or strengthen their positions in an evolving industry, are unable to continue their operations or are acquired. For example, some of our current and potential competitors have made, or have been reported as considering making, acquisitions or have announced new strategic alliances designed to position them with the ability to provide many of the same services that we provide, to both the service provider and enterprise markets. We believe that industry consolidation may result in stronger competitors that are better able to compete as sole-source vendors for customers. This could lead to more variability in our operating results and could have a material adverse effect on our financial condition or results of operations.

Demand for our products may be impacted by government regulation of the telecommunications industry.

Service providers are subject to government regulation in a number of jurisdictions in which we sell our products. There are several proposals in the United States, Europe and elsewhere for regulating service providers' ability to prioritize applications in their networks. Advocates for regulating this industry claim that collecting premium fees from certain "preferred" applications would distort the market for Internet applications in favor of larger and better-funded content providers. They also claim that this would impact end-users who already purchased broadband access only to experience response times that differ based on content provider. Opponents believe that content providers who support bandwidth-intensive applications should be required to pay service providers a premium in order to support further network investments. In August 2008, the United States Federal Communications Commission (the "FCC") issued a ruling prohibiting Comcast, the second-largest broadband provider in the United States, from delaying certain peer-to-peer traffic on its network. Comcast filed an appeal of the ruling in September 2008. In April 2010, a federal appeals court ruled that under current law the FCC had limited power over Web traffic. In December 2010, the FCC adopted rules which would give it regulatory power over Internet service providers in order to prevent them from blocking or unreasonably discriminating against Web content, services or applications. In 2011, Verizon and other broadband companies challenged the FCC's rules in the United States Court of Appeals for the District of Columbia Circuit. In January 2014, the United States Court of Appeals for the District of Columbia Circuit overturned the FCC's anti-blocking and anti-discrimination rules, saying the agency overreached in barring

broadband providers from slowing or blocking selected Web traffic. Despite this decision, demand from service providers for the traffic management and subscriber management features of our products could be adversely affected if regulations prohibit or limit service providers from managing traffic on their networks. A decrease in demand for these features could adversely impact sales of our products and could have a material adverse effect on our business, financial condition or result of operations.

Demand for our value-added products, such as video caching and optimization and parental control, may be lower than anticipated.

Our value-added products offer customers additional tools to increase the efficiency of their networks or help them derive additional revenues from their end customers. With our acquisition of Ortiva Wireless Inc. ("Ortiva") and Oversi Networks Ltd. ("Oversi") in 2012, we enhanced our value-added products by introducing video caching products and optimization products, among other value-added products. The industry and market for such services is still developing. We cannot provide any assurance that demand for such products will continue or grow, or that we will be able to generate revenues from such sales at the levels we anticipate or at all. Any inability to sell or maintain our value-added products may lead to commercial disputes with our customers and to lengthy implementation processes and increased spending on technical solutions, all of which may negatively impact our results of operations.

Our revenues and business will be harmed if we do not keep pace with changes in broadband applications and with advances in technology, including through significant investment.

We will need to invest heavily in the continued development of our technology in order to keep pace with rapid changes in applications and increased broadband network speeds and with our competitors' efforts to advance their technology. Our ability to develop and deliver effective product offerings depends on many factors, including identifying our customers' needs, technical implementation of new services and integration of our value-added products with our customers' existing network infrastructure. While we will continue to introduce innovative value-added products, we cannot provide any assurance that any new products we introduce will achieve the same degree of success that we have with our existing products. Designers of broadband applications that our products identify and manage are using increasingly sophisticated methods to avoid detection and management by network operators. Even if our products successfully identify a particular application, it is sometimes necessary to distinguish between different types of traffic belonging to a single application. Accordingly, we face significant challenges in ensuring that we identify new applications and new versions of current applications as they are introduced without impacting network performance, especially as networks become faster. This challenge is increased as we seek to expand sales of our products in new geographic territories because the applications vary from country to country and region to region. Our business and revenues will be adversely affected if we fail to address our customers' needs in particular geographic markets or if we fail to develop enhancements to our products in order to keep pace with advances in technology.

The network equipment market is subject to rapid technological progress and to compete, we need to achieve widespread market acceptance.

The network equipment market is characterized by rapid technological progress, frequent new product introductions, changes in customer requirements and evolving industry standards. To compete, we need to achieve widespread market acceptance. Developments in routers and routing software could also significantly reduce demand for and sales of our products and could cause our products to become obsolete, which may result in inventory write downs. Alternative technologies could achieve widespread market acceptance and displace the technology on which we have based our product architecture. We can give no assurance that our technological approach will achieve broad market acceptance or that other technology or devices will not supplant our technology and products.

We need to increase the functionality of our products and offer additional features and value-added products in order to maintain or increase our profitability.

The market in which we operate is highly competitive and unless we continue to enhance the functionality of our products and add additional features, our competitiveness may be harmed and the average sale prices for our products may decrease. Decreases in sale prices generally result from the introduction by competitors of competing products and from the commoditization and increasing popularity of DPI technology. To counter this trend, we endeavor to enhance our products by offering higher system speeds, additional features and value-added products such as additional security, video functions, and support for additional applications and enhanced reporting tools. We may also need to reduce our per unit manufacturing costs at a rate equal to or greater than the rate at which selling prices decline. If we are unable to reduce costs or offer increased functionally and features, our profitability may be adversely affected.

Sales of our products to large service providers can involve a lengthy sales cycle, which may impact the timing of our revenues and result in us expending significant resources without making any sales.

Our sales cycles to large service providers, including carriers, mobile operators and cable operators, are generally lengthy because these end-customers consider our products to be capital equipment and undertake significant testing to assess the performance of our products within their networks. Furthermore, many of our product and service arrangements with our customers provide that the final acceptance of a product or service may be specified by the customer. In such instances, we do not recognize the revenue until all acceptance criteria have been met. As a result, we often invest significant time from initial contact with a large service provider until it decides to incorporate our products in its network, and we may not be able to recognize the revenue from a customer until all acceptance criteria have been satisfied. We may also expend significant resources in attempting to persuade large service providers to incorporate our products into their networks without success. Even after deciding to purchase our products, the initial network deployment of our products by a large service provider may last up to one year. We have also experienced longer sales cycles as a result of the global economic downturn and uncertainty, particularly in Europe. If a competitor succeeds in convincing a large service provider to adopt that competitor's product, it may be difficult for us to displace the competitor because of the cost, time, effort and perceived risk to network stability involved in changing solutions. As a result, we may incur significant expenses without generating any sales, which could adversely affect our profitability.

The complexity and scope of the solutions and services we provide to larger service providers is increasing. Larger projects entail greater operational risk and an increased chance of failure.

The complexity and scope of the solutions and services we provide to larger service providers is increasing. The larger and more complex such projects are, the greater the operational risks associated with them. These risks include failure to fully integrate our products into the service provider's network or with third-party products, our dependence on subcontractors and partners and on effective cooperation with third-party vendors for the successful and timely completion of such projects. If we encounter any of these risks, we may incur higher costs in order to complete the project and may be subject to contractual penalties resulting in lower profitability. In addition, the project may demand more of our management's time than was originally planned, and our reputation may be adversely impacted.

We depend on third parties to market, sell, install and provide initial technical support for our products for a material portion of our business.

We depend on third-party channel partners, such as distributors, resellers, OEMs and system integrators, to market and sell a material portion of our products to end-customers. In 2013, approximately 40% of our revenues were derived from channel partners. Our channel partners are also responsible for installing our products and providing

initial customer support for them. As a result, we depend on the ability of our channel partners to successfully market and sell our products to these end-customers. We also depend on our ability to maintain our relationships with existing channel partners and to develop relationships with new channel partners in key markets. We cannot assure you that our channel partners will market our products effectively, receive and fulfill customer orders for our products on a timely basis or continue to devote the resources necessary to provide us with effective sales, marketing and technical support. In addition, any failure by our channel partners to provide adequate initial support to end-customers could result in customer dissatisfaction with us or our products, which could result in a loss of customers, harm our reputation and delay or limit market acceptance of our products. Our products are complex and it takes time for a new channel partner to gain experience in the operation and installation of these products. Therefore, it may take a period of time before a new channel partner can successfully market, sell and support our products if an existing channel partner ceases to sell our products. Additionally, our agreements with channel partners are generally not exclusive and our channel partners may market and sell products that compete with our products. Our agreements with our distributors and resellers are usually for an initial one-year term and following the expiration of this term, can be terminated by either party. We can give no assurance that these agreements will remain in effect and any termination of one or more of the agreements may adversely affect our profitability and results of operations.

We are subject to certain regulatory regimes that may affect the way that we conduct business internationally, and our failure to comply with applicable laws and regulations could adversely affect our reputation and result in penalties and increased costs.

We are subject to a complex system of laws and regulations related to international trade, including economic sanctions and export control laws and regulations. It is our policy not to make direct or indirect prohibited sales of our products, including into countries sanctioned under laws to which we are subject, and to contractually limit the territories into which our channel partners may sell our products. Nevertheless, several years ago one of our channel partners sold certain of our products (designed for the enterprise market) outside of its contractually designated territory, including into a sanctioned country, and we subsequently determined that our contract management protocol for authorizing channel partner sales was not adequately followed in that instance.

We are also subject to the U.S. Foreign Corrupt Practices Act, or FCPA, and may be subject to similar worldwide anti-bribery laws that generally prohibit companies and their intermediaries from making improper payments to government officials for the purpose of obtaining or retaining business. Some of the countries in which we operate have experienced governmental corruption to some degree and, in certain circumstances, strict compliance with anti-bribery laws may conflict with local customs and practices.

Despite our compliance and training programs, we cannot be certain that our procedures will be sufficient to ensure consistent compliance with all applicable international trade and anti-corruption laws, or that our employees or channel partners will strictly follow all policies and requirements to which we subject them. Any alleged or actual violations of these laws may subject us to government scrutiny, investigation, debarment, and civil and criminal penalties, which may have an adverse effect on our results of operations, financial condition and reputation.

We are dependent on our traffic management systems and network management application suites for the substantial majority of our revenues.

In the past three years, we increased sales of our Service Gateway platforms and our network management application suite. However, sales of our NetEnforcer traffic management system and NetXplorer network management system continued to account for a significant portion of our revenues in 2012 and 2013. While we currently expect that these systems will continue to account for a considerable portion of our revenues in the immediate future, the growth rate of sales from these systems has declined from 29% in 2012 to 25% in 2013. If we are unable to increase these sales our business will suffer. In addition, service providers may choose embedded or integrated solutions using routers and switches from larger networking vendors over a standalone solutions we offer. Any factor adversely affecting our ability to sell, or the pricing of or demand for, our NetEnforcer traffic management system and NetXplorer network management system would severely harm our ability to generate revenues and could have a material adverse effect on our business.

We integrate various third-party solutions into our products and may integrate or offer additional third-party solutions in the future. If we lose the right to use such solutions, our sales could be disrupted and we would have to spend additional capital to replace such components.

We integrate various third-party solutions into our products and may integrate or offer additional third-party solutions in the future. Sales of our products could be disrupted if such third-party solutions were either no longer available to us or no longer offered to us on commercially reasonable terms. In either case, we would be required to spend additional capital to either redesign our products to function with alternate third-party solutions or develop substitute components ourselves. We might, as a result, be forced to limit the features available in our current or future product offerings, which could have a material adverse effect on our business.

Our products are highly technical and any undetected software or hardware errors in our products could have a material adverse effect on our operating results.

Our products are complex and are incorporated into broadband networks, which are a major source of revenue for service providers and support critical applications for subscribers and enterprises. Due to the highly technical nature of our products and variations among customers' network environments, we may not detect product defects until our products have been fully deployed in our customers' networks. Regardless of whether warranty coverage exists for a product, we may be required to dedicate significant technical resources to repair any defects. If we encounter significant product problems, we could experience, among other things, loss of major customers, cancellation of product orders, increased costs, delay in recognizing revenues and damage to our reputation. We could also face claims for product liability, tort or breach of warranty. Defending a lawsuit, regardless of its merit, is costly and may divert management's attention. In addition, if our business liability insurance is inadequate or future coverage is unavailable on acceptable terms or at all, our financial condition could be harmed.

Demand for our products depends in part on the rate of adoption of bandwidth-intensive broadband applications, such as Internet video and online video gaming applications, and the impact multiple applications may have on network speed.

Our products are used by service providers and enterprises to monitor and manage bandwidth-intensive applications that cause congestion in broadband networks and impact the quality of experience of users. Demand for our products is driven particularly by growth in applications, which are highly sensitive to network delays and therefore require efficient network management, such as Voice over IP (VoIP), Internet video and television and online video gaming applications. If the rapid growth in the adoption of VoIP and in the popularity of Internet video and online video gaming applications does not continue, the demand for our products may be adversely impacted.

We currently depend on a single subcontractor to manufacture and provide hardware warranty support for our Service Gateway platforms, NetEnforcer traffic management systems and Video Optimization platforms. If this subcontractor experiences delays, disruptions, quality control problems or a loss in capacity, it could materially and adversely affect our operating results.

We currently depend on a single subcontractor, Flextronics (Israel) Ltd., a subsidiary of Flextronics, a global electronics manufacturing services company, to manufacture, assemble, test, package and provide hardware warranty support for our Service Gateway platforms, NetEnforcer traffic management systems and Video Optimization platforms. In addition, our agreement with Flextronics (Israel) requires it to procure and store key components for our products at its facilities. If Flextronics (Israel) experiences delays, disruptions or quality control problems in manufacturing our products, or if we fail to effectively manage our relationship with Flextronics (Israel), product shipments may be delayed and our ability to deliver products to customers could be materially and adversely affected. Flextronics (Israel) may terminate our agreement at any time during the term upon 180-days prior notice. We expect

that it would take approximately six months to transition the manufacturing of our products to an alternate manufacturer and our inventory of completed products may not be sufficient for us to continue delivering products to our customers on a timely basis during any such transition period. Therefore, the loss of Flextronics (Israel) could adversely affect our sales and operating results and harm our reputation.

Certain hardware components for our products come from single or limited sources and we could lose sales if these sources fail to satisfy our supply requirements.

We obtain certain hardware components used in our products from single or limited sources. Although these are off-the-shelf items, because our systems have been designed to incorporate these specific components, any change to these components due to an interruption in supply or our inability to obtain such components on a timely basis would require engineering changes to our products before substitute components could be incorporated. Such changes could be costly and result in lost sales particularly to the central processing unit for our Service Gateway platforms, our NetEnforcer AC-6000, AC-1400, AC-3000, AC-500 and the video optimization platforms VDC. The agreements with our suppliers do not contain any minimum supply commitments. If we or our contract manufacturer fail to obtain components in sufficient quantities when required, our business could be harmed. Our suppliers also sell products to our competitors and may enter into exclusive arrangements with our competitors, stop selling their products or components to us at commercially reasonable prices or refuse to sell their products or components to us at any price. Our inability to obtain sufficient quantities of single-source or limited-sourced components or to develop alternative sources for components or products would harm our ability to maintain and expand our business.

We may expand our business or enhance our technology through acquisitions that could result in diversion of resources and extra expenses. This could disrupt our business and adversely affect our financial condition.

Part of our strategy is to selectively pursue partnerships and acquisitions. In 2008, we acquired the business of Esphion, a developer of video optimization and protection solutions for telecommunications operators and internet service providers, which increased the scope of our product offerings. In 2012, we acquired Ortiva, a developer of solutions for mobile and Internet networks, and Oversi, a developer of products and systems for caching Internet content. The negotiation of acquisitions, investments or joint ventures, as well as the integration of acquired or jointly developed businesses or technologies, could divert our management's time and resources. As of the end of 2012, we consolidated the operations of Ortiva and Oversi with ours, and they no longer operate on a standalone basis. Acquired businesses, technologies or joint ventures may not be successfully integrated with our products and operations and we may not realize the intended benefits of these acquisitions. We may also incur future losses from any acquisition, investment or joint venture. In addition, acquisitions could result in:

- substantial cash expenditures;
- potentially dilutive issuances of equity securities;
- the incurrence of debt and contingent liabilities;
- a decrease in our profit margins; and
- amortization of intangibles and potential impairment of goodwill.

If acquisitions disrupt our operations or result in significant expenditures or liabilities, our business, operating results or financial conditions may suffer.

If we fail to attract and retain skilled employees, we may not be able to timely develop, sell or support our products.

Our success depends, in large part, on the continued contribution of our research and development, sales and marketing and managerial personnel. If our business continues to grow, we will need to hire additional qualified research and development, sales and marketing and managerial personnel to succeed. The process of hiring, training and successfully integrating qualified personnel into our operation is a lengthy and expensive one. The market for qualified personnel is very competitive because of the limited number of people available with the necessary technical skills, sales skills and understanding of our products and technology. This is particularly true in Israel, where competition for qualified personnel is intense. Our failure to hire and retain qualified personnel could cause our revenues to decline and impair our ability to meet our research and development and sales objectives.

We may not be able to enforce employees' covenants not to compete under the current laws of some jurisdictions in which we operate and therefore may be unable to prevent our competitors from benefiting from the expertise of some of our former employees.

It is our practice to have our employees sign appropriate non-compete agreements when permitted under applicable law. These agreements prohibit our employees who cease working for us from competing directly with us or working for our competitors for a limited period of time. The enforceability of non-compete clauses in certain jurisdictions in which we operate may be limited. Under the current laws of some jurisdictions in which we operate, we may be unable to enforce these agreements and it may thereby be difficult for us to restrict our competitors from gaining the expertise our former employees gained while working for us.

If we are unable to successfully protect the intellectual property embodied in our technology, our business could be harmed significantly.

Know-how relating to networking protocols, building carrier-grade systems and identifying applications is an important aspect of our intellectual property. To protect our know-how, we customarily require our employees, distributors, resellers, software testers and contractors to execute confidentiality agreements or agree to confidentiality undertakings when their relationship with us begins. Typically, our employment contracts also include the following clauses: assignment of intellectual property rights for all inventions developed by employees and non-disclosure of all confidential information. We cannot provide any assurance that the terms of these agreements are being observed and will be observed in the future. Because our product designs and software are stored electronically and thus are highly portable, we attempt to reduce the portability of our designs and software by physically protecting our servers through the use of closed networks, which prevent external access to our servers. We cannot be certain, however, that such protection will adequately deter individuals or groups from wrongfully accessing our technology. Monitoring unauthorized use of intellectual property is difficult and some foreign laws do not protect proprietary rights to the same extent as the laws of the United States. We cannot be certain that the steps we have taken to protect our proprietary information will be sufficient. In addition, to protect our intellectual property, we may become involved in litigation, which could result in substantial expenses, divert the attention of management, cause significant delays, materially disrupt the conduct of our business or adversely affect our revenue, financial condition and results of operations.

As of December 31, 2013, we had a limited patent portfolio. We had seven issued U.S. patents and several pending patent applications. While we plan to protect our intellectual property with, among other things, patent protection, there can be no assurance that:

- current or future U.S. or foreign patents applications will be approved;
-

our issued patents will protect our intellectual property and not be held invalid or unenforceable if challenged by third-parties;

- we will succeed in protecting our technology adequately in all key jurisdictions in which we or our competitors operate;

- the patents of others will not have an adverse effect on our ability to do business; or

- others will not independently develop similar or competing products or methods or design around any patents that may be issued to us.

The failure to obtain patents, inability to obtain patents with claims of a scope necessary to cover our technology or the invalidation of our patents may weaken our competitive position and may adversely affect our revenues.

We may be subject to claims of intellectual property infringement by third parties that, regardless of merit, could result in litigation and our business, operating results or financial condition could be materially adversely affected.

There can be no assurance that we will not receive communications from third parties asserting that our products and other intellectual property infringe, or may infringe their proprietary rights. We are not currently subject to any proceedings for infringement of patents or other intellectual property rights and are not aware of any parties that intend to pursue such claims against us. Any such claim, regardless of merit, could result in litigation, which could result in substantial expenses, divert the attention of management, cause significant delays and materially disrupt the conduct of our business. As a consequence of such claims, we could be required to pay substantial damage awards, develop non-infringing technology, enter into royalty-bearing licensing agreements, stop selling our products or re-brand our products. If it appears necessary, we may seek to license intellectual property that we are alleged to infringe. Such licensing agreements may not be available on terms acceptable to us or at all. Litigation is inherently uncertain and any adverse decision could result in a loss of our proprietary rights, subject us to significant liabilities, require us to seek licenses from others and otherwise negatively affect our business. In the event of a successful claim of infringement against us and our failure or inability to develop non-infringing technology or license the infringed or similar technology, our business, operating results or financial condition could be materially adversely affected.

We use certain “open source” software tools that may be subject to intellectual property infringement claims, the assertion of which could impair our product development plans, interfere with our ability to support our clients or require us to pay licensing fees.

Certain of our products contain open source code, and we may use more open source code in the future. Open source code is code that is covered by a license agreement that permits the user to liberally copy, modify and distribute the software without cost, provided that users and modifiers abide by certain licensing requirements. The original developers of the open source code provide no warranties on such code. As a result of our use of open source software, we could be subject to suits by parties claiming ownership of what we believe to be open source code, and we may incur expenses in defending claims that we did not abide by the open source code license. If we are not successful in defending against such claims, we may be subject to monetary damages or be required to remove the open source code from our products. Such events could disrupt our operations and the sales of our products, which would negatively impact our revenues and cash flow. In addition, under certain conditions, the use of open source code to create derivative code may obligate us to make the resulting derivative code available to others at no cost. If we are required to publicly disclose the source code for such derivative products or to license our derivative products that use an open source license, our previously proprietary software products would be available to others, including our customers and competitors without charge. We monitor our use of such open source code to avoid subjecting our products to conditions that we do not intend. The use of such open source code, however, may ultimately subject some of our products to unintended conditions so that we are required to take remedial action that may divert resources away from our development efforts.

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Unfavorable global economic conditions could have a material adverse effect on our business, financial condition or operating results.

The 2008 and 2009 crisis in the financial and credit markets in the United States, Europe and Asia led to a global economic slowdown that is ongoing, with economies in those territories continuing to show significant weakness and there is continuing economic uncertainty. If the economies of any part of the world remain uncertain or further deteriorate, many enterprises, telecommunication carriers and service providers may significantly reduce or postpone capital investments. This could result in reductions in the sales of our products or services, longer sales cycles, slower adoption of new technologies and increased price competition. As a result of the most recent downturn in the European economies, we have experienced longer sales cycles than in the past.

We continuously monitor market trends and intend to take such steps as we deem appropriate to adjust our operations. Because a substantial portion of our operating expenses consist of salaries, we may not be able to reduce our operating expenses in line with any reduction in revenues or may elect not to do so for business reasons. We will need to continue to generate increased revenues and manage our costs to maintain profitability. Although a certain recovery has occurred in the U.S. economy, if global economic and market conditions do not improve, or continue to remain uncertain, this may increase our inventories, decrease our revenues, result in additional pressure on the price of our products, prolong payment terms or increase the risk of our incurrence of bad debts. Such circumstances would have a material adverse effect on our results of operations and cash flow from operations.

Our international operations expose us to the risk of fluctuations in currency exchange rates.

Our revenues are generated primarily in U.S. dollars and a major portion of our expenses are denominated in U.S. dollars. As a result, we consider the U.S. dollar to be our functional currency. Other significant portions of our expenses are denominated in shekels and to a lesser extent in Euros and other currencies. Our shekel-denominated expenses consist principally of salaries and related personnel expenses. We anticipate that a material portion of our expenses will continue to be denominated in shekels. In 2013, the shekel continued to fluctuate against the U.S. dollar, and appreciated by approximately 7% against the U.S. dollar. If the U.S. dollar weakens against the shekel or other currencies we are exposed to, there will be a negative impact on our results of operations. We use derivative financial instruments, such as foreign exchange forward contracts, to mitigate the risk of changes in foreign exchange rates on balance sheet accounts and forecast cash flows. We may not purchase derivative instruments adequately to insulate ourselves from foreign currency exchange risks. The volatility in the foreign currency markets may make hedging our foreign currency exposures challenging. In addition, because a portion of our revenue is not earned in U.S. dollars, fluctuations in exchange rates between the U.S. dollar and the currencies in which such revenue is earned may have a material adverse effect on our results of operations and financial condition. If we wish to maintain the U.S. dollar-denominated value of our products in non-U.S. markets, devaluation in the local currencies of our customers relative to the U.S. dollar could cause our customers to cancel or decrease orders or default on payment.

Compliance with new regulations regarding the use of conflict minerals may disrupt our operations, result in additional cost and expense and could result in other significant adverse effects.

In August 2012, under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, the U.S. Securities and Exchange Commission (the “SEC”) adopted new requirements for companies that use certain minerals and derivative metals (referred to as "conflict minerals" regardless of their actual country of origin) in their products. Metals, such as tantalum, tin, gold and tungsten may be present in our products as component parts. We will be required to implement procedures to investigate whether any conflict minerals that are used in our products originated from the Democratic Republic of the Congo or adjoining countries and, if we determine that we are subject to the new disclosure rules, make the required disclosures with the SEC no later than by May 31, 2014. There will be costs associated with these investigations, and the implementation of these rules could adversely affect the sourcing, supply

and pricing of the raw materials used in our products. Also, we may face potential reputational challenges if we are unable to sufficiently verify the origins of all conflict minerals used in our component parts or if we are unable to replace any conflict minerals sourced from the Democratic Republic of the Congo or adjoining countries with acceptable alternatives. We may also encounter challenges to satisfy customers that require that all of the components of our products be certified as conflict-free. If we are not able to meet customer requirements, customers may choose an alternative service provider. These changes could also have an adverse impact in our ability to market our products.

Risks Related to Our Ordinary Shares

The share price of our ordinary shares has been and may continue to be volatile.

Our quarterly financial performance is likely to vary in the future, and may not meet our expectations or the expectations of analysts or investors, which may lead to additional volatility in our share price. The market price of our ordinary shares may be volatile and could fluctuate substantially due to many factors, including, but not limited to:

- announcements or introductions of technological innovations, new products, product enhancements or pricing policies by us or our competitors;
- winning or losing contracts with service providers;
- disputes or other developments with respect to our or our competitors' intellectual property rights;
- announcements of strategic partnerships, joint ventures or other agreements by us or our competitors;
- recruitment or departure of key personnel;
- regulatory developments in the markets in which we sell our products;
- our sale of ordinary shares or other securities in the future;
- changes in the estimation of the future size and growth of our markets; or
- market conditions in our industry, the industries of our customers and the economy as a whole.

Share price fluctuations may be exaggerated if the trading volume of our ordinary shares is too low. The lack of a trading market may result in the loss of research coverage by securities analysts. Moreover, we cannot assure you that any securities analysts will initiate or maintain research coverage of our company and our ordinary shares. If our future quarterly operating results are below the expectations of securities analysts or investors, the price of our ordinary shares would likely decline. Securities class action litigation has often been brought against companies following periods of volatility.

Our shareholders do not have the same protections afforded to shareholders of a U.S. company because we have elected to use certain exemptions available to foreign private issuers from certain NASDAQ corporate governance requirements.

As a foreign private issuer, we are permitted under NASDAQ Marketplace Rule 5615(a)(3) to follow Israeli corporate governance practices instead of the NASDAQ Stock Market requirements that apply to U.S. companies. As a condition to following Israeli corporate governance practices, we must disclose which requirements we are not following and describe the equivalent Israeli law requirement. We must also provide NASDAQ with a letter from our Israeli outside counsel, certifying that our corporate governance practices are not prohibited by Israeli law. As a result of these exemptions, our shareholders do not have the same protections as are afforded to shareholders of a U.S. company. We may also in the future choose to follow Israeli law and practices in lieu of other requirements of NASDAQ Rule 5600.

Our U.S. shareholders may suffer adverse tax consequences if we are characterized as a passive foreign investment company.

We relied on the market capitalization method to determine the fair market value of our assets for the taxable year ended December 31, 2013. Based on certain estimates of our gross income and gross assets, the nature of our business and the anticipated amount of goodwill (which is determined in large part by the price of our stock), we believe that we were not a PFIC for our taxable year ended December 31, 2013 and do not expect to become a PFIC for our taxable year ending December 31, 2014. A non-U.S. company will generally be characterized as a PFIC for any taxable year in which 75% or more of its gross income is passive income or in which 50% or more of the average value of its gross assets produce passive income or are held for the production of passive income.

If we are characterized as a PFIC, our U.S. shareholders may suffer adverse tax consequences, including having gains realized on the sale of our ordinary shares treated as ordinary income, rather than capital gains income, and having potentially punitive interest charges apply to the proceeds of share sales. Similar rules apply to distributions that are "excess distributions."

The tests for determining PFIC status are applied annually and it is difficult to make accurate predictions of our future income, assets, activities and market capitalization, including fluctuations in the price of our ordinary shares, which are relevant to this determination. Accordingly, there can be no assurance that we will not become a PFIC in 2014 or in subsequent years.

If the price of our ordinary shares declines, we may be more vulnerable to an unsolicited or hostile acquisition bid.

We do not have a controlling shareholder. Notwithstanding provisions of our articles of association and Israeli law, a decline in the price of our ordinary shares may result in us becoming subject to an unsolicited or hostile acquisition bid. In the event that such a bid is publicly disclosed, it may result in increased speculation regarding our company and volatility in our share price even if our board of directors decides not to pursue a transaction. If our board of directors does pursue a transaction, there can be no assurance that it will be consummated successfully or that the price paid will represent a premium above the original price paid for our shares by all of our shareholders.

Risks Relating to our Location in Israel

Conditions in Israel could adversely affect our business.

We are incorporated under Israeli law and our principal offices, research and development division and manufacturing facilities are located in Israel. Accordingly, political, economic and military conditions in Israel directly affect our business. Since the State of Israel was established in 1948, a number of armed conflicts have occurred between Israel and its Arab neighbors. Although Israel has entered into various agreements with Egypt, Jordan and the Palestinian Authority, there has been an increase in unrest and terrorist activity, which began in September 2000 and continued with varying levels of severity into 2013. An armed conflict between Israel and Hamas in the Gaza Strip occurred in November 2012 and is ongoing. These conflicts involved missile strikes against civilian targets in various parts of Israel including most recently, central Israel, and negatively affected business conditions in Israel. Any armed conflicts, terrorist activities or political instability in the region may limit materially our ability to obtain raw materials from these countries or sell our products to companies in these countries. Any hostilities involving Israel or the interruption or curtailment of trade between Israel and its present trading partners, or significant downturn in the economic or financial condition of Israel, could adversely affect our operations and product development and manufacturing, cause our revenues to decrease and adversely affect the share price of publicly traded companies having operations in Israel, such as us.

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Our operations may be disrupted by the obligations of personnel to perform military service.

As of December 31, 2013, we employed 430 people, of whom 302 were based in Israel. Some of our employees in Israel are obligated to perform annual military reserve duty in the Israel Defense Forces, depending on their age and position in the army. Additionally, they may be called to active reserve duty at any time under emergency circumstances for extended periods of time. Our operations could be disrupted by the absence of one or more of our executive officers or key employees for a significant period due to military service and any significant disruption in our operations could harm our business. The full impact on our workforce or business if some of our executive officers and employees are called upon to perform military service, especially in times of national emergency, is difficult to predict. Additionally, the absence of a significant number of employees at our manufacturing subcontractor, Flextronix, as a result of military service obligations may disrupt their operations and could have a material adverse effect on our ability to timely deliver products to customers may be materially adversely affected.

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

Our investment program in equipment at our facility in Hod-Hasharon, Israel, has been granted approved enterprise status and we are therefore eligible for tax benefits under the Israeli Law for the Encouragement of Capital Investments, 1959, referred to as the Investments Law. We expect to utilize these tax benefits after we utilize our net operating loss carry forwards. As of December 31, 2013, our net operating loss carry forwards for Israeli tax purposes amounted to approximately $40 million (including losses related to our acquisition of Oversi, the operations of which were merged with ours in 2012). To remain eligible for these tax benefits, we must continue to meet certain conditions stipulated in the Investments Law and its regulations and the criteria set forth in the specific certificate of approval, including, among other conditions, that the approved enterprise be operated over a seven-year period and that at least 30% of our investment in fixed assets of the approved enterprise be funded by additional paid-up ordinary share capital. If we do not meet these requirements, the tax benefits would be canceled and we could be required to refund any tax benefits and investment grants that we received in the past. Further, in the future these tax benefits may be reduced or discontinued. If these tax benefits are cancelled, our Israeli taxable income would be subject to regular Israeli corporate tax rates. The standard corporate tax rate for Israeli companies in 2012 and in 2013 was 25% of their taxable income, and will increase to 26.5% in 2014 and going forward.

Effective January 1, 2011, the Investment Law was amended. Under the amended Investment Law, the criteria for receiving tax benefits were revised. Under the transition provisions of the new legislation, a company may decide to irrevocably implement the new amendment while waiving benefits provided under the current law or to remain subject to the current law. In the future, we may not be eligible to receive additional tax benefits under this law. Our Company did not file a request to apply the new benefits under the 2011 Amendment. We intend to apply for benefits under the 2011 Amendment beginning in 2016. The termination or reduction of these tax benefits would increase our tax liability, which would reduce our profits. Additionally, if we increase our activities outside of Israel through acquisitions, for example, our expanded activities might not be eligible for inclusion in future Israeli tax benefit programs. Finally, in the event of a distribution of a dividend from the abovementioned tax-exempt income, in addition to withholding tax at the following rates: (i) Israeli resident corporation – 0%, (ii) Israeli resident individual – 15% in 2013 and 20% as of 2014 (iii) non-Israeli resident - 15% in 2013 and 20% as of 2014 subject to a reduced tax rate under the provisions of an applicable double tax treaty., we will be subject to tax at the corporate tax rate applicable to our Approved Enterprise's and Beneficiary Enterprise's income on the amount distributed in accordance with the effective corporate tax rate which would have been applied had we not enjoyed the exemption. See "ITEM 10: Additional Information—Taxation—Israeli Tax Considerations and Government Programs."

No assurance can be given that we will be eligible to receive additional tax benefits under the Investments Law in the future. The termination or reduction of these tax benefits would increase our tax liability in the future, which would reduce our profits or increase our losses. Additionally, if we increase our activities outside of Israel, for example, by future acquisitions, our increased activities may not be eligible for inclusion in Israeli tax benefit programs.

The government grants we have received for research and development expenditures require us to satisfy specified conditions and restrict our ability to manufacture products and transfer technologies outside of Israel. If we fail to comply with these conditions or such restrictions, we may be required to refund grants previously received together with interest and penalties and may be subject to criminal charges.

We have received grants from the Office of the Chief Scientist for the financing of a portion of our research and development expenditures in Israel, pursuant to the provisions of The Encouragement of Industrial Research and Development Law, 1984, referred to as the Research and Development Law. In the future we may not receive grants or we may receive significantly smaller grants from the Office of the Chief Scientist, and our failure to receive grants in the future could adversely affect our profitability.

In 2011 and 2012, we received and accrued from the Office of the Chief Scientist royalty-bearing grants totaling $3.7 million and $2.9 million, representing 21.7% and 11.5%, respectively, of our gross research and development expenditures in these periods. In December 2012, we agreed to prepay approximately $15.9 million of contingent royalties to the Office of the Chief Scientist, and thereby eliminated all future royalty obligations related to grants received through 2012. We recorded this prepayment as a liability in 2012 and paid it on August 2013.

In 2013 we received and accrued non-royalty-bearing grants totaling $1.1 million from the Office of the Chief Scientist, representing 3.7% of our gross research and development expenditures during the year. In 2013 we qualified to participate in two non-royalty-bearing research and development programs funded by the Office of the Chief Scientist to develop generic technology relevant to the development of our products. Such programs are approved pursuant to special provisions of the Research and Development Law. We were eligible to receive grants constituting between 40% and 55% of certain research and development expenses relating to these programs. One of the programs are members of programs approved for companies with large Research and Development activities and another members of a "Magnet" consortiums. Although the grants under these programs are not required to be repaid by way of royalties, the restrictions of the Research and Development Law described below apply to these programs.

The provisions of the Research and Development Law and the terms of the Office of the Chief Scientist grants prohibit us from transferring manufacturing products which we originally planned to manufacture in Israel outside of Israel if they incorporate technologies funded by the Office of the Chief Scientist, and from transferring intellectual property rights in technologies developed using these grants, without special approvals from the Office of the Chief Scientist.

Even if we receive approval to manufacture our products outside of Israel, we may be required to pay an increased total amount of royalties, which may be up to 300% of the grant amount plus interest, depending on the manufacturing volume that is performed outside of Israel. This restriction may impair our ability to outsource manufacturing or engage in similar arrangements for those products or technologies. Know-how developed under an approved research and development program may not be transferred to any third-parties, except in certain circumstances and subject to prior approval. Similarly, even if we receive approval to transfer intellectual property rights in technologies developed using these grants, we may be required to repay a multiple of the original grants to the Office of the Chief Scientist In addition, if we fail to comply with any of the conditions and restrictions imposed by the Research and Development Law or by the specific terms under which we received the grants, we may be required to refund any grants previously received together with interest and penalties, and may be subject to criminal charges.

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It may be difficult to enforce a U.S. judgment against us, our officers and directors in Israel or the United States, or to assert U.S. securities laws claims in Israel or serve process on our officers and directors.

We are incorporated in Israel. The majority of our executive officers and directors are not residents of the United States, and the majority of our assets and the assets of these persons are located outside the United States. Therefore, it may be difficult for an investor, or any other person or entity, to enforce a U.S. court judgment based upon the civil liability provisions of the U.S. federal securities laws against us or any of these persons in a U.S. or Israeli court, or to effect service of process upon these persons in the United States. Additionally, it may be difficult for an investor, or any other person or entity, to assert U.S. securities law claims in original actions instituted in Israel. Israeli courts may refuse to hear a claim based on a violation of U.S. securities laws on the grounds that Israel is not the most appropriate forum in which to bring such a claim. Even if an Israeli court agrees to hear a claim, it may determine that Israeli law and not U.S. law is applicable to the claim. If U.S. law is found to be applicable, the content of applicable U.S. law must be proved as a fact which can be a time-consuming and costly process. Certain matters of procedure will also be governed by Israeli law. There is little binding case law in Israel addressing the matters described above.

Provisions of Israeli law and our articles of association may delay, prevent or make undesirable an acquisition of all or a significant portion of our shares or assets.

Our articles of association contain certain provisions that may delay or prevent a change of control, including a classified board of directors. In addition, Israeli corporate law regulates acquisitions of shares through tender offers and mergers, requires special approvals for transactions involving significant shareholders and regulates other matters that may be relevant to these types of transactions. These provisions of Israeli law could delay or prevent a change in control and may make it more difficult for third-parties to acquire us, even if doing so would be beneficial to our shareholders, and may limit the price that investors may be willing to pay for our ordinary shares in the future. Furthermore, Israeli tax considerations may make potential transactions undesirable to us or to some of our shareholders. See “ITEM 10: Additional Information—Memorandum and Articles of Association—Acquisitions under Israeli Law” and “—Anti-Takeover Measures.”

ITEM 4: Information on Allot

A. History and Development of Allot

Our History

Our legal and commercial name is Allot Communications Ltd. We are a company limited by shares organized under the laws of the State of Israel. Our principal executive offices are located at 22 Hanagar Street, Neve Ne’eman Industrial Zone B, Hod-Hasharon 4501317, Israel, and our telephone number is +972 (9) 761-9200. We have irrevocably appointed Allot Communications Inc. as our agent to receive service of process in any action against us in any United States federal or state court. The address of Allot Communications Inc. is 300 TradeCenter, Suite 4680, Woburn, MA 01801-7422.

We were incorporated on November 12, 1996 as “Ariadne Ltd.” and commenced operations in 1997. In September 1997, we changed our name to “Allot Communications Ltd.” In November 2006, we listed our shares on NASDAQ. In 2007, we introduced our Service Gateway platform that enables broadband providers to build efficient, secure, manageable and profitable intelligent networks that are optimized to deliver Internet-based content and services. In January 2008, we completed the acquisition of the business of Esphion Limited, a developer of network protection solutions for carriers and internet service providers. In November 2010, we listed our shares on the Tel Aviv Stock Exchange, or TASE, and began applying the reporting reliefs afforded under the Israeli Securities Law to companies whose securities are dually listed on NASDAQ and the TASE, In May 2012, we acquired the business of Ortiva

Wireless Inc., a developer of video optimization solutions for mobile and Internet networks. In September 2012, we acquired the business of Oversi Networks Ltd., a developer of products and systems for caching Internet content.

We had capital expenditures of $2.7 million in 2013, $3.8 million in 2012 and $2.9 million in 2011. We have financed our capital expenditures with cash generated from operations and through net proceeds from sales of our equity securities and investing activities.

Our capital expenditures during 2011, 2012 and 2013 consisted primarily of investments in lab equipment for research and development.

B. Business Overview

Overview

We are a leading global provider of intelligent broadband solutions, focused on developing mobile, fixed and enterprise networks to support the "digital lifestyle." The digital lifestyle describes the way people rely on broadband connectivity, Internet-connected devices and Internet applications in their everyday lives – at work, at home and at play. Our solutions, which are based on our deep packet inspection (DPI) technology, identify and leverage the business intelligence in data networks, empowering network operators to shape users' digital lifestyle experiences and to capitalize on the network traffic they generate.

We have a global and diverse end-customer base composed of mobile and fixed broadband service providers, cable operators, private networks, data centers, governments and enterprises, such as financial and educational institutions. Our scalable, carrier-grade solutions integrate capabilities that allow our customers to optimize the delivery and performance of over-the-top applications and services, monetize network utilization through value-added product deployment, real-time metering and application-aware charging models and personalize the user experience through service tiering and differentiation.

Through our combination of innovative technology, proven know-how and collaborative approach to industry standards and partnerships with broadband service providers and enterprises, we deliver broadband solutions that equip our customers with the capabilities to elevate their role in the digital lifestyle ecosystem and to expand into new business opportunities. We offer our customers proprietary technologies that are seamlessly woven into carrier-class products and solutions. In addition, we have developed significant industry know-how and expertise through our experience designing and implementing use cases with our diverse customer base. Beginning from the proposal stage of a new project through the testing, acceptance and implementation of our products, we collaborate closely with our customers and other industry participants to create innovative solutions to create the digital lifestyle ecosystems our customers require.

Industry Background

The rapid proliferation of broadband networks in recent years has been largely driven by demand from users for faster and more reliable access to the Internet and by the proliferation in the number and complexity of broadband applications, as well as the proliferation of mobile smartphones, tablets and other Internet-connected devices.

Rising Network Operational Costs Due to the Rapid Adoption of Broadband Applications

Advances in broadband access (such as the introduction of long-term evolution, or LTE, technology) combined with the advanced data capabilities of end-user devices (such as smartphones and tablets) have promoted a growing number of applications and content delivered over broadband networks. The vast majority of these applications run over-the-top (OTT) of the network, which means they are not originated, controlled or charged by the network operator. The use of OTT applications, such as streaming video, peer-to-peer (P2P), Voice over IP (VoIP), social networks, interactive gaming and online content, requires large and increasing amounts of bandwidth. Moreover, many of these applications are highly sensitive to network delays caused by congestion. In response to these challenges, service providers have been forced to invest heavily in network infrastructure upgrades and customer support services in order to maintain the quality of experience for subscribers.

Rising Data Traffic in Mobile Networks

The mobile data market continues to grow rapidly, fueled by the proliferation of smartphones and tablets, mobile-enabled laptops that use mobile modems or tethered smartphones to connect to the Internet. On average, the data traffic generated by an Internet user with a smartphone is multiple times that of an Internet user without a smartphone.

The cost of increasing the bandwidth in mobile networks is significantly higher than that in wireline networks. As a result, mobile operators are experiencing economic and infrastructure challenges in meeting the rising tide of data traffic over their networks. In addition, as capacity increases in mobile networks, smartphone users are likely to have increased expectations with respect to speed and performance.

It is becoming increasingly apparent that unmanaged 3G and 4G/LTE mobile networks, will not be able to cope with the rising tide of data traffic, without implementing intelligent bandwidth management solutions. Moreover, network providers may need to develop new pricing models if they are not able to monetize the OTT traffic carried by their networks.

Service Providers Demand the Ability to Offer Services that Can Be Monetized at Different Rates

Some service providers still offer flat-rate broadband access, regardless of the type of applications and data used by subscribers. These operators provide the same level of service to all subscribers and do not guarantee access quality, regardless of a subscriber's willingness to pay for premium services and network performance. However, with the increasing amount of data used, the flat-rate pricing model may not be profitable, especially for mobile broadband operators, unless they can charge subscribers high rates. As a result, both mobile and fixed operators have begun to offer service plans based on gigabytes of data used. However, this pricing model is also subject to competition from other service providers offering lower rates, contributing to downward pricing pressure and high subscriber turnover rates.

To address these issues and increase the average revenue per user (ARPU), a significantly increased number of service providers have begun to offer premium, differentiated services, such as improved quality for VoIP and Internet video, off-peak usage incentives and parental control over access to content, among others. By offering such tiered services and charging subscribers according to the value of these services, as well as based on the gigabyte usage, service providers can capitalize on the revenue opportunities enabled by OTT Internet applications. To offer premium services and to guarantee high-quality delivery of content and user experience, service providers need enhanced visibility into and control of network traffic, including visibility into the type of applications used on the network and levels of traffic generated by different subscribers.

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The Challenge of Elevating the Role of Fixed and Mobile Broadband Networks

In the evolving digital lifestyle, consumers recognize the importance of the devices they use to access the Internet and choose the Internet content and services they use based on quality. However, the network that connects them to the Internet is not as “visible”, and is therefore not as highly valued, even though it plays a critical role in the service chain. In order to generate revenue through various pricing models and encourage consumers and content providers to seek higher quality network services, service providers are seeking to elevate the role of network connectivity and services. To do so, service providers must be able to identify and leverage the business intelligence in their data networks and capitalize on the network traffic that they generate.

The ability to identify, distinguish and prioritize different applications plays a major role in intelligent management of network resources and service delivery, allowing service providers to optimize bandwidth utilization and reduce operational costs, while maintaining high quality of service for tiered and premium services. Application designers are employing increasingly sophisticated methods to avoid detection by network operators who desire to manage network use. Traditional network infrastructure devices, such as routers and switches, do not generally have sufficient computing resources or the required algorithms to distinguish between different and rapidly evolving applications.

Enterprise Demand for Visibility and Delivery of Mission-Critical Applications and Services in the Cloud

The proliferation of network applications, bring your own device (BYOD) and cloud computing presents significant challenges for enterprises that operate data centers, wide-area networks, virtual private networks (VPN) and Internet connectivity for organizations of all sizes. Enterprises depend on network infrastructure to ensure the delivery of business-critical applications to an increasingly mobile and often global workforce, and as such, face may of the same issues as service providers. At the same time, Internet access has introduced a wide variety of recreational and non-business applications to enterprise networks, resulting in network congestion and negatively impacting employee productivity. As a result, there is an increasing need for enterprises to be able to monitor and control the traffic on their business networks.

Network Security Threats

As reliance on the Internet has grown, service providers and subscribers have become increasingly vulnerable to a wide range of security threats, including denial of service (DOS) attacks, spambots and malware. These attacks are designed to flood the network with traffic that consumes all the available bandwidth and hinder the ability to provide high quality broadband access to subscribers or to prevent enterprises from using mission-critical applications. These threats also compromise network and data integrity. We believe service providers and enterprises must protect against such attacks by detecting and neutralizing malicious traffic at very early stages before such threats can compromise network integrity and services.

Integrated Solutions

Our integrated broadband solutions allow mobile, fixed and enterprise operators to elevate their role in the digital lifestyle ecosystem and expand into new business opportunities. Our solutions enable our customers to increase revenues by monetizing network usage through value-added products, value-based charging and revenue-sharing models, reduce costs by optimizing the delivery and performance of OTT content and cloud computing services and improve customer loyalty by personalizing operator offerings with various choices of service tiers and digital lifestyle options.

Our Integrated Solutions include:

- Analytics solutions deliver accurate and meaningful network business intelligence to drive capacity planning, congestion management, service planning and marketing decisions.

- Traffic Management solutions prioritize existing network capacity, control congestion and optimize service delivery. Dynamic Quality of Service (QoS) enforcement enables effective traffic management strategies that minimize infrastructure and operating costs.

- Video Caching and Optimization solutions improve the quality and efficiency of OTT video delivery. New revenue opportunities are created through service packages designed especially for video consumers and revenue-sharing possibilities with content providers.

- Policy Control and Charging solutions drive personalized service plans and pay-for-use pricing models based on real-time consumption of bandwidth and OTT applications. We provide a single point of integration with provisioning and pricing systems.

- Service Enablement solutions facilitate a wide variety of cost-saving and revenue-generating use cases to create personalized customer experiences demanded by today's sophisticated consumers.

Allot's Products (Our Platforms)

The Allot Service Gateway and Allot NetEnforcer platforms are based on leading technology and high performance, designed for in-line deployment in a wide range of networks. Within each platform, our Dynamic Actionable Recognition Technology (DART) engine employs multiple deep packet inspection and analytical methods to identify network traffic by subscriber, application, device and network topology. Our technology is able to identify more OTT applications than any other solution on the market with frequent and custom updates to our extensive signature library. These granular elements may be mapped directly into dynamic traffic management, charging and service enablement policies.

High-Performance Platforms

- Allot Service Gateway integrates network intelligence, policy enforcement and revenue-generating services in a scalable, carrier-class platform designed for fixed, mobile (3G/4G/LTE) and converged broadband networks. The Allot Service Gateway accurately identifies subscriber traffic in real time at speeds up to 160 gigabits per second (Gbps), optimizes bandwidth utilization based on usage, enforces QoS policy, and steers traffic to digital lifestyle services deployed within or outside the platform. As the focal point for service enablement, The Allot Service Gateway allows service providers to reduce operating costs and drive new revenue by delivering the personalized service and quality of experience that the digital lifestyle demands.

- Allot NetEnforcer bandwidth management devices monitor and manage network traffic per application and per subscriber, enabling intelligent optimization of broadband and wide area network (WAN) services. With full duplex speeds ranging from 10 megabits per second (Mbps) to 8 Gbps, these devices provide essential visibility policy enforcement and traffic steering to added-value services in a wide range of service provider and enterprise networks.

Digital Lifestyle Services

Our growing portfolio of digital lifestyle services operate seamlessly with our in-line platforms and centralized management system, providing new business opportunities for service providers and enterprises.

Subscriber Management Platform

The Allot Subscriber Management Platform (SMP) drives the centralized creation, provisioning and pricing of subscriber services, including tiered and usage-based data plans, which we believe are key to personalizing digital lifestyle offerings and maximizing average revenue per user. The Allot SMP allows subscriber traffic to be managed across converged access networks and when offloading to Wi-Fi hotspots. Modular licensing provides flexible and scalable management for any number of subscribers.

- Allot TierManager: Provides and manages differentiated services and tiered service plans that are tailored to subscriber preferences.

- Allot QuotaManager: Provides and manages usage allowances and caps, with real-time metering of service consumption and dynamic enforcement of quota limits and overage policy.

- Allot ChargeSmart: Enables real-time, pay-for-use pricing, based on a user's consumption of data and applications. It also integrates seamlessly in 3G and 4G mobile networks and implements the pricing model via standard telecommunication interfaces, such as Diameter Gx, Sd, Gy and Gz.

Analytics Services

Our analytics solutions analyze traffic data to drive smart business decisions.

- Allot ClearSee Analytics: is a business intelligence application that helps network operators turn big data into valuable insight for the decision-makers in their organization. Its self-service approach allows network operators to synthesize and analyze large varieties and volumes of data with extreme efficiency. Tools include built-in dashboards for mining Network, Application, Subscriber, Device, and Quality of Experience data, plus Self-Service data mining for modeling fresh perspectives and gaining deeper understanding of network usage and subscriber behavior.

- Allot ClearSee Data Source extracts a rich variety of raw traffic statistics from operator networks, enriches it with data from operator business systems, and loads it into a cutting-edge data warehouse where it is transformed into modeled data objects that are meaningful to telco operators and easy to manipulate using the Allot ClearSee Analytics application This valuable source data may also be exported to external analytics tools and other business applications.

Video Solutions

Our media caching and video optimization platforms enable operators to capitalize on the increasing volume of OTT video traffic.

- Allot MediaSwift E: Comprehensive caching and content delivery system for OTT video, P2P and other applications. Relieves network congestion caused by videos and improves quality of experience for users.

- Allot VideoClass: Optimizes OTT video content and delivery to ensure efficient utilization of mobile radio access network (RAN) resources and consistently high quality video to enhance viewer experience.

Security Solutions

Our security solutions protect network customers, network service integrity and brand reputation.

- Allot WebSafe Personal: Opt-in security services that allow ISP subscribers to define and enforce safe-browsing limits (Parental Control) and to prevent incoming malware from infecting their devices (Anti-Malware). Services are enforced at the network level, requiring no device involvement or battery consumption.

- Allot WebSafe: URL filtering service that blocks blacklisted content and enables access control to objectionable content on the Internet.

- Allot ServiceProtector: Attack detection and mitigation services that protect commercial networks against Denial of Service (DoS/DDoS) attacks, Zero Day attacks, worms, zombie and spambot behavior.

Centralized Management

The Allot NetXplorer is the management umbrella for our devices, platforms and solutions, providing a central access point for network-wide monitoring, reporting, analytics, troubleshooting, accounting and QoS policy provisioning. Its user-friendly interface provides our customers with a comprehensive overview of the application, user, device and network topology traffic, while its wide variety of reports provide accessible, detailed analyses of granular traffic data.

- NetXplorer Analytics and Reporting: Real-time reporting provides 30-second accuracy for timely troubleshooting and resolution of customer care issues, while historical traffic statistics facilitate analyses of usage trends and user behavior.

- NetXplorer Data Collector: Provides distributed data collection and storage at different points in the network in order to support growing and large-scale deployments with large volumes of network traffic.

- NetAccounting Server: Aggregates network-wide usage statistics and exports the data to external accounting systems in standard formats.

- NetPolicy Provisioner: Provides a virtual “bandwidth management device” for self-monitoring and self-provisioning by a networks operator’s VPN, ISP and managed services customers

Customers

We have a global, diversified end-customer base consisting primarily of mobile and fixed service providers, cable operators, private networks, data centers, governments and enterprises. We derive a significant and growing portion of our revenue from direct sales to large mobile and fixed-line service providers. We generate the remainder of our revenue through a select and well-developed network of channel partners, generally consisting of distributors, resellers, original equipment manufacturers (“OEMs”) and system integrators. In 2013, we derived 23% of our revenues from Europe, 22% from the United States, 31% from Asia and Oceania, 19% from the Middle East and Africa and 5% from the Americas (excluding the United States).

Channel Partners

We market and sell our products to end-customers both by direct sales and through channel partners, which include distributors, resellers, OEMs and system integrators. A significant portion of our sales occur through our channel partners. In 2013, approximately 40% of our revenues were derived from channel partners. Our channel partners generally purchase our products from us upon receiving orders from end-customers and are responsible for installing and providing initial customer support for our products. Our channel partners are located around the world and address most major markets. Our channel partners target a range of end-users, including carriers, alternative carriers, cable operators, private networks, data centers and enterprises in a wide range of industries, including government, financial institutions and education. Our agreements with channel partners that are distributors or resellers are generally non-exclusive, for an initial term of one year and automatically renew for successive one-year terms unless terminated. After the first year, such agreements may typically be terminated by either party upon ninety days prior

notice.

We offer support to our channel partners. This support includes the generation of leads through marketing events, seminars and web-based leads and incentive programs as well as technical and sales training.

Sales and Marketing

Our product sales and deployment cycle varies based on the intended use by the end-customer. The sales cycle for initial network deployment may generally last between twelve and eighteen months for large and medium service providers, six to twelve months for small service providers, and one to six months for enterprises. Follow-on orders and additional deployment of our products usually require shorter cycles. Large and medium service providers generally take longer to plan the integration of our solutions into their existing networks and to set goals for the implementation of the technology.

We focus our marketing efforts on product positioning, increasing brand awareness, communicating product advantages and generating qualified leads for our sales organization. We rely on a variety of marketing communications channels, including our website, trade shows, industry research and professional publications, the press and special events to gain wider market exposure.

We have organized our worldwide sales efforts into the following three territories: North and South America; Europe, the Middle East and Africa; and Asia and Oceania. We have regional offices in the United States, Israel, France, United Kingdom, Singapore, Japan, New Zealand and China, and a regional presence in Germany, Italy, Spain, Mexico, Brazil, India, Hong Kong, South Korea, South Africa and Australia.

As of December 31, 2013, our sales and marketing staff, including product management and business development functions, consisted of 82 employees.

Service and Technical Support

We believe our technical support and professional services capabilities are a key element of our sales strategy. Our technical staff assists in presales activities and advises channel partners on the integration of our solutions into end-customer networks. Our basic warranty extended to end-customers (directly or through our channel partners) is three months for software and twelve months for hardware. Generally, end-customers are also offered a choice of one year or three-year customer support programs when they purchase our products. These customer support programs can be renewed at the end of their terms. Our end-customer support plans generally offer the following features:

- unlimited 24/7 access to Allot’s support organization, via phone, emails and online support system;
- expedited replacement units in the event of a warranty claim;
- software updates and upgrades offering new features and addressing new and changing network applications; and
- periodic updates of solution documentation and technical information.

Our support plans are designed to maximize network up-time and minimize operating costs. Our customers, including channel partners and their end-customers, are entitled to take advantage of our around-the-clock technical support which we provide through our four help desks, primarily located in France, Israel, Singapore and the United States. We also offer our customers 24-hour access to an external web-based technical knowledge base, which provides technical support information and, in the case of our channel partners, enables them to support their customers independently and obtain follow up and support from us.

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The expenditures associated with the technical support staff are allocated in our statements of operations between sale and marketing expenses and cost of goods sold, based on the roles of and tasks performed by personnel.

As of December 31, 2013, our technical staff consisted of 117 employees.

Research and Development

Our research and development activities take place primarily in Israel. As of December 31, 2013, 172 of our employees were engaged primarily in research and development. We devote a significant amount of our resources towards research and development to introduce and continuously enhance products to support our growth strategy. We have assembled a core team of experienced engineers, many of whom are leaders in their particular field or discipline and have technical degrees from top universities and experience working for leading Israeli networking companies. These engineers are involved in advancing our core technologies, as well as in applying these core technologies to our product development activities. Our research and development efforts have benefited from royalty-bearing grants from the Office of the Chief Scientist. The State of Israel does not own any proprietary rights in technology developed with the Office of the Chief Scientist funding and there is no restriction related to the Office of the Chief Scientist on the export of products manufactured using technology developed with Office of the Chief Scientist funding (other limitations on export apply under applicable law). For a description of restrictions on the transfer of the technology and with respect to manufacturing rights, please see "ITEM 3: Key Information—Risk Factors—The government grants we have received for research and development expenditures require us to satisfy specified conditions and restrict our ability to manufacture products and transfer technologies outside of Israel. If we fail to comply with these conditions or such restrictions, we may be required to refund grants previously received together with interest and penalties and may be subject to criminal charges."

Manufacturing

We subcontract the manufacture and repair of our Service Gateway platforms and our NetEnforcer traffic management systems to Flextronics (Israel) Ltd., a subsidiary of Flextronics, a global electronics manufacturing services company. This strategy enables us to reduce our fixed costs, focus on our core research and development competencies and provide flexibility in meeting market demand. Flextronics (Israel) is contractually obligated to provide us with manufacturing services based on agreed specifications, including manufacturing, assembling, testing, packaging and procuring the raw materials for our devices. We are not required to provide any minimum orders. Our agreement with Flextronics (Israel) is automatically renewed annually for additional one-year terms. Flextronics (Israel) may terminate our agreement with them at any time during the term upon 180 days prior notice. We retain the right to procure independently any of the components used in our products. Flextronics (Israel) has a U.S. affiliate to which it can, with the prior consent of the Office of the Chief Scientist, transfer manufacturing of our products if necessary, in which event we may be required to pay increased royalties to the Office of the Chief Scientist. We expect that it would take approximately six months to transition manufacturing of our products to an alternate manufacturer.

We design and develop internally a number of the key components for our products, including printed circuit boards and software. Some of the hardware components of our products are obtained from single or limited sources. Since our products have been designed to incorporate these specific components, any change in these components due to an interruption in supply or our inability to obtain such components on a timely basis would require engineering changes to our products before we could incorporate substitute components. In particular, we purchase the central processing unit for our Service Gateway platforms and for our NetEnforcer products from NetLogic Microsystems, Inc. (now part of Broadcom Corporation). We carry approximately three to six months of inventory of key components. We also work closely with our suppliers to monitor the end-of-life of the product cycle for integral components, and believe that in the event that they announce end of life, we will be able to increase our inventory to allow enough time for

replacing such components. The agreements with our suppliers do not contain any minimum purchase or supply commitments. Product testing and quality assurance is performed by our contract manufacturer using tests and automated testing equipment and according to controlled test documentation we specify. We also use inspection testing and statistical process controls to assure the quality and reliability of our products.

Competition

We compete in a rapidly evolving and highly competitive sector of the networking technology market. We face significant competition from router and switch infrastructure companies, such as Cisco Systems, Inc., Telefonaktiebolager LM Erricson and Huawei Technologies Co., Ltd. that integrate functionalities into their platforms addressing some of the problems that our products address. Our competitors have also identified the potential market opportunity offered by the largest service providers, referred to as Tier 1 operators, and we therefore expect intense competition in this portion of our market in the future. Our principal competitors in the field of DPI technology are Sandvine Inc. and Procera Networks, Inc. We also face competition from companies that offer partial or alternative solutions addressing limited aspects of the challenges facing broadband providers, such as network monitoring or security. We compete on the basis of product performance, such as speed and number of applications identified, ease of use and installation, and customer support. Price is also an important, although not the principal, basis on which we compete. See “ITEM 3: Key Information—Risk Factors—We may be unable to compete effectively with other companies in our market who offer, or may in the future offer, competing technologies.”

Intellectual Property

Our intellectual property rights are very important to our business. We believe that the complexity of our products and the know-how incorporated in them makes it difficult to copy them or replicate their features. We rely on a combination of confidentiality and other protective clauses in our agreements, copyright and trade secrets to protect our know-how. We also restrict access to our servers physically and through closed networks since our product designs and software are stored electronically and thus are highly portable.

We customarily require our employees, customers, distributors, resellers, software testers, technology partners and contractors to execute confidentiality agreements or agree to confidentiality undertakings when their relationship with us begins. Typically, our employment contracts also include the following clauses: assignment of intellectual property rights for all inventions developed by employees, non-disclosure of all confidential information, and non-compete clauses, which generally restrict the employee for six months following termination of employment. The enforceability of non-compete clauses in certain jurisdictions in which we operate may be limited. See “ITEM 3: Key Information—Risk Factors—We may not be able to enforce employees’ covenants not to compete under the current laws of some jurisdictions in which we operate and therefore may be unable to prevent our competitors from benefiting from the expertise of some of our former employees.” Because our product designs and software are stored electronically and thus are highly portable, we attempt to reduce the portability of our designs and software by physically protecting our servers through the use of closed networks, which prevent external access to our servers.

The communications equipment industry is characterized by constant product changes resulting from new technological developments, performance improvements and lower hardware costs. We believe that our future growth depends to a large extent on our ability to be an innovator in the development and application of hardware and software technology. As we develop the next generation products, we intend to pursue patent protection for our core technologies in the telecommunications segment. We plan to seek patent protection in our largest markets and our competitors’ markets, for example in the United States and Europe. As we continue to move into markets, such as Japan, Korea and China, we will evaluate how best to protect our technologies in those markets. We intend to vigorously prosecute and defend the rights of our intellectual property.

As of December 31, 2013, we had two U.S. patents and four pending patent applications in the United States. We expect to formalize our evaluation process for determining which inventions to protect by patents or other means. We cannot be certain that patents will be issued as a result of the patent applications we have filed.

We have obtained a U.S. trademark registration for one of our key marks that we use to identify our products or services: “NetEnforcer.”

Government Regulation

See “ITEM 5: Overview—Government Grants” for a description of grants received from the Office of the Chief Scientist of the Ministry of Economy.

C. Organizational Structure

As of December 31, 2013, we held directly and indirectly the percentage indicated of the outstanding capital stock of the following subsidiaries:

Company	Jurisdiction of Incorporation	Percentage Ownership
Allot Communications Inc.	United States	100%
Allot Communications Europe SARL	France	100%
Allot Communications (Asia Pacific) Pte. Limited	Singapore	100%
Allot Communications (UK) Limited	United Kingdom	100%
Allot Communications Japan K.K.	Japan	100%
Allot Communications (New Zealand) Limited	New Zealand	100%
Oversi Networks Ltd.	Israel	100%
Allot Communications (Hong Kong) Ltd	Hong Kong	100%
Allot Communications Africa (PTY) Ltd	South Africa	100%
Allot Communications India Private Ltd	India	100%

D. Property, Plants and Equipment

Our principal administrative and research and development activities are located in approximately 72,000 square foot (6,700 square meter) facilities in Hod-Hasharon, Israel. The leases for our facilities vary in dates and terms, with the main facility’s lease commencing in July 2006 and expiring in June 2018.

We also lease a 5,862 square foot (545 square meter) facility in Woburn, Massachusetts, for the purposes of our U.S. sales and marketing operations pursuant to a lease that expires in August 2019 and a 15,119 square foot (1,400 square meter) facility in San Diego, California for the purposes of our U.S research and development activities, which expires in April 2018. We lease other smaller facilities for the purpose of our development, sales and marketing and support

activities in France, the United Kingdom, Italy, Germany, Singapore, Spain, China, Japan and New Zealand.

ITEM 4A: Unresolved Staff Comments

Not applicable.

ITEM 5: Operating and Financial Review and Prospects

A. Operating Results

Overview

We are a leading provider of intelligent Internet Protocol ("IP") service optimization, monetization and personalization solutions for mobile, fixed and wireless broadband service providers and enterprises. Our portfolio of hardware platforms and software applications uses our proprietary deep packet inspection ("DPI") technology, which we refer to as Dynamic Actionable Recognition Technology, or DART, to transform broadband connections or pipes into smart networks that can manage data traffic efficiently and rapidly deploy value-added products. End-customers use our solutions to create sophisticated policies to monitor network applications, enforce quality of service policies that guarantee mission-critical application performance, mitigate security risks and leverage network infrastructure investments. Demand from users for faster and more reliable access to the Internet, an increase in the number and complexity of broadband applications, and growth in mobile data-enhanced smartphones have resulted in the rapid proliferation of broadband access networks in recent years. Our carrier-class products are used by service providers to offer subscriber-based and application-based tiered services that enable them to optimize their service offerings, reduce churn rates and increase ARPU.

We market and sell our products through a variety of channels, including direct sales and through our channel partners, which include distributors, resellers, OEMs and system integrators. End customers of our products include carriers, mobile operators, cable operators, wireless, wireline and satellite Internet service providers, educational institutions, governments and enterprises. The resulting intelligent, content-aware broadband networks enable our customers to accurately monitor and manage IP traffic per application, subscriber, network topology and device.

In 2013, the primary drivers of our growth were the mobile and fixed markets, which were highlighted by our ongoing relationship with a global Tier 1 mobile and fixed operators groups. Revenues from these customers in 2013 accounted for 45% of our total revenues.

Acquisition of Ortiva and Oversi

In 2012, we acquired the business of Ortiva Wireless Inc. ("Ortiva"), a developer of solutions for mobile and Internet networks and Oversi Networks Ltd. ("Oversi"), a developer of products and systems for caching Internet content. See note 1(b) to our consolidated financial statements for further information.

Revenues

We generate revenues from two sources: (1) sales of our network traffic management systems and our network management application solutions and platforms, and (2) maintenance and support services, including installation and training. We generally provide maintenance and support services pursuant to a one- or three-year maintenance and support program, which may be purchased by customers at the time of product purchase or on a renewal basis.

We recognize revenues from product sales when persuasive evidence of an agreement exists, delivery of the product has occurred, no significant obligations with respect to implementation remain, the fee is fixed or determinable and collection is probable. We typically grant a one-year hardware and three-month software warranty on all of our products, or one-year hardware and software extended warranty to customers which purchase annual maintenance and support. We record a provision for warranty at the time the product's revenue is recognized. We estimate the liability of possible warranty claims based on our historical experience. Warranty claims have to date been immaterial to our results of operations. Maintenance and support revenues are recognized on a straight-line basis over the term of the applicable maintenance and support agreement. See "—Critical Accounting Policies and Estimates—Revenue Recognition" below.

Customer concentration. We derived 14% and 15% of our total revenues in 2012 and 2011, respectively, from one global Tier 1 mobile operator group. In 2013, we derived 45% of our total revenues from three Tier 1 mobile and fixed operators.

Geographical breakdown. The following table sets forth the geographic breakdown of our revenues by percentage for the periods indicated:

	Year Ended December 31,		
	2011	2012	2013
United States	12 %	24 %	22 %
Europe	50	38	23
Asia and Oceania	26	21	31
Middle East and Africa	3	10	19
Americas (excluding United States)	9	7	5
Total	100 %	100 %	100 %

Cost of revenues and gross margins

Our products' cost of revenues consists primarily of costs of materials, manufacturing services and overhead, warehousing, product testing and royalties paid primarily to the Office of the Chief Scientist (until the end of 2012; when the obligation to royalties to OCS ended due to the repayment to OCS). Our services' cost of revenues consists primarily of salaries and related personnel costs for our customer support staff as well as the royalty payments mentioned above. We expect cost of revenues to increase as a result of an increase in our product and service revenues, an increase in sales of our higher end products, primarily our Service Gateway platforms, to large customers that we expect will require additional personnel hiring and other operational expenditures related to such sales. Such increases may be partially offset by increased sales of our network management application suites as their related cost of revenues is generally lower. In addition, we are no longer obligated to make royalty payments to the Office of the Chief Scientist, as we reached a settlement with them in December 2012. The balance of the liability related to the grants received from the Office of Chief Scientist was approximately $15.9 million, which was recorded as cost of revenues for the year ended December 31, 2012. In 2013 our gross margin increased as a result of the elimination of royalty payments to the Office of the Chief Scientist with respect to grants received through 2012.

Operating expenses

Research and development. Our research and development expenses consist primarily of salaries and related personnel costs, costs for subcontractor services, depreciation, rent and costs of materials consumed in connection with the design and development of our products. We expense all of our research and development costs as they are incurred. Our net research and development expenses are comprised of gross research and development expenses offset by financing through royalty-bearing grants from the Office of the Chief Scientist. Such participation grants are

recognized at the time at which we are entitled to such grants on the basis of the costs incurred and included as a deduction of research and development expenses (see "—Government Grants" below). We believe that significant investment in research and development, including hiring high quality research and development personnel, is essential to our future success and expect that in future periods our research and development expenses will increase on an absolute basis.

Sales and marketing. Our sales and marketing expenses consist primarily of salaries and related personnel costs, travel expenses, costs associated with promotional activities such as public relations, conventions and exhibitions, rental expenses, depreciation and commissions paid to third parties. We intend to continue expanding our activities in the service provider market, and therefore we expect that sales and marketing expenses will increase on an absolute basis in the future as we hire additional sales, marketing and presale support personnel to continue to promote our brand, establish new marketing channels and expand our presence worldwide.

General and administrative. Our general and administrative expenses consist of salaries and related personnel costs, rental expenses, costs for professional services and depreciation. We expect these expenses to increase on an absolute basis as we hire additional personnel and incur additional costs related to the growth of our business as we increase our global presence. General and administrative expenses also include costs associated with corporate governance, tax and regulatory compliance, compliance with the rules implemented by the SEC, NASDAQ and the Tel-Aviv Stock Exchange ("TASE") and premiums for our director and officer liability insurance.

Financial income (expenses), net

Financial income (expenses), net consists primarily of interest earned on our cash balances and other financial investments, foreign currency exchange gains or losses, gains or losses resulting from the sale of marketable securities and bank fees.

In 2013, we had $0.7 million financial income, net compared to $1.4 million financial income, net in 2012. The change is primarily attributed to a decrease in our interest income which derived from lower interest rates received for our short-term bank deposits during 2013 and from the increase in the amortization of our marketable securities' premium during 2013.

In addition, financial and other income (expenses), net, may fluctuate due to foreign currency exchange gains or losses, as well as interest rate changes. See "—Factors Affecting Our Performance."

Approved Enterprise

Our facilities in Hod-Hasharon, Israel have been granted Approved Enterprise status under the Encouragement of Capital Investments Law, 1959 and enjoy certain tax benefits under this program. We expect to utilize these tax benefits after we utilize our net operating loss carry forwards. As of December 31, 2013, our net operating loss carry forwards for Israeli tax purposes totaled approximately $40 million, which includes losses related to our acquisition of Oversi. As a result of our acquisition of Oversi, we offset operating losses in Israel against taxable income annually with a limitation of up to 20% of the total accumulated loss but no more than 50% of our taxable income. Income derived from other sources, other than through our "Approved Enterprise" status, during the benefit period will be subject to the regular corporate tax rate.

Government Grants

Our research and development efforts have been financed, in part, through grants from the Office of the Chief Scientist under our approved plans in accordance with the Research and Development Law. Through December 31, 2012, we had received approval for and recorded in our books grants totaling $30.8 million from the Office of the Chief Scientist, including $4.1 million attributed to NetReality products. Because the NetReality products were discontinued and will no longer be sold, the $4.1 million was cancelled, and we are not obligated to repay this amount. Under Israeli law and the approved plans, royalties on the revenues derived from sales of all of our products are payable to the Israeli government, generally at the rate of 3.0% during the first three years and 3.5% beginning in the fourth year, up to the amount of the received grants as adjusted for fluctuation in the U.S. dollar/shekel exchange rate.

The amounts received after January 1, 1999 bear interest at the twelve-month LIBOR as at the beginning of the year in which a grant is approved. Our obligation to pay these royalties is contingent upon actual sales of our products and no payment is required if no sales are made. In December 2012, we recorded a liability of $15.9 million due to a settlement with the Office of the Chief Scientist, representing the full balance of the contingent liability related to grants received. This settlement was paid in 2013. Upon making this payment, we have eliminated all royalty obligations related to our anticipated revenues and did not incur the expense associated with future interest payments related to such obligations.

Factors Affecting Our Performance

Our business, financial position and results of operations, as well as the period-to-period comparability of our financial results, are significantly affected by a number of factors, some of which are beyond our control, including:

Customer concentration. We derived 45% of our total revenues in 2013 from three global Tier 1 mobile and fixed operator groups. While we have some visibility into the likely scope of the customers' projects, our relationships are conducted solely on a purchase order basis and we do not have any commitment for future purchase orders from these customers. The loss of any of such significant customers could harm our results of operations and financial condition.

Size of end-customers and sales cycles. We have a global, diversified end-customer base consisting primarily of service providers and enterprises. The deployment of our products by small and midsize enterprises and service providers can be completed relatively quickly with a limited number of NetEnforcer and/or Service Gateway systems compared to the number required by large service providers. In 2013, we have increased the portion of our sales to large service providers. Large service providers take longer to plan the integration of our solutions into their existing networks and to set goals for the implementation of the technology. Sales to large service providers are therefore more complicated as they involve a relatively larger number of network elements and solutions, as well as NetEnforcer and/or Service Gateway systems. We are seeking to achieve further significant customer wins in the large service provider market that would positively impact our future performance. The longer sales cycles associated with the increased sales to large service providers of our platforms may increase the unpredictability of the timing of our sales and may cause our quarterly and annual operating results to fluctuate if a significant customer delays its purchasing decision and/or defers an order. Furthermore, longer sales cycles may result in delays from the time we increase our operating expenses and make investments in inventory to the time that we generate revenue from related product sales.

Average selling prices. Our performance is affected by the selling prices of our products. We price our products based on several factors, including manufacturing costs, the stage of the product's life cycle, competition, technical complexity of the product, discounts given to channel partners in certain territories, customization and other special considerations in connection with larger projects. We typically are able to charge the highest price for a product when it is first introduced to the market. We expect that the average selling prices for our products will decrease over the product's life cycle as our competitors introduce new products and DPI technology becomes more standardized. In order to maintain or increase our current prices, we expect that we will need to enhance the functionality of our existing products by offering higher system speeds, additional value-added products and features, such as additional security functions, supporting additional applications and providing enhanced reporting tools. We also from time to time introduce enhanced products, typically higher-end models that include new architecture and design and new capabilities. Such enhanced products typically increase our average selling price. To further offset such declines, we sell maintenance and support programs for our products, and as our customer base and number of field installations grow, our related service revenues are expected to increase.

Cost of revenues and cost reductions. Our cost of revenues as a percentage of total revenues was 28.5% for 2011, 44.8% for 2012 (29.6% excluding the impact of the $15.9 million expenses related to settlement of Office of Chief Scientist grants) and 27.8% for 2013. Our products use off-the-shelf components and typically the prices of such components decline over time. However, the introduction and sale of new or enhanced products and services may result in an increase in our cost of revenues. We make a continuous effort to identify cheaper components of comparable performance and quality. We also seek improvements in engineering and manufacturing efficiency that will reduce costs. Our products incorporate features that require the payment of royalties to third parties. In addition, new products usually have higher costs during the initial introduction period. We generally expect such costs to decline as the product matures and sales volume increases. The introduction of new products may also involve a significant decrease in demand for older products. Such a decrease may result in a devaluation or write-off of such older products and their respective components. In 2013, we recorded a write-off of $ 0.7 million of inventory to our cost of revenues for products and components. The growth of our customer base is usually coupled with increased service revenues primarily resulting from increased maintenance and support. In addition, the growth of our installed base with large service providers may result in increased demand for professional services, such as training and installation services. An increase in demand for such services may require us to hire additional personnel and incur other expenditures. However, these additional expenses, handled efficiently, may be utilized to further support the growth of our customer base and increase service revenues.

Currency exposure. A majority of our revenues and a substantial portion of our expenses are denominated in the U.S. dollar. However, a significant portion of the expenses associated with our global operations, including personnel and facilities-related expenses, are incurred in currencies other than the U.S. dollar. This is the case primarily in Israel and to a lesser extent in other countries in Europe and Asia. Consequently, a decrease in the value of the U.S. dollar relative to local currencies will increase the dollar cost of our operations in these countries. A relative decrease in the value of the U.S. dollar would be partially offset to the extent that we generate revenues in such currencies. In order to partially mitigate this exposure we have decided in the past and may decide from time to time in the future to enter into hedging transactions. We may discontinue hedging activities at any time. As such decisions involve substantial judgment and assessments primarily regarding future trends in foreign exchange markets, which are very volatile, as well as our future level and timing of cash flows of these currencies, we cannot provide any assurance that such hedging transactions will not affect our results of operations when they are realized. See Note 5 to our consolidated financial statements included elsewhere in this annual report for further information.

Interest rate exposure. We have a significant amount of cash that is currently invested primarily in interest bearing vehicles, such as bank time deposits and available for sale marketable securities. These investments expose us to risks associated with interest rate fluctuations.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles, or U.S. GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. These estimates and judgments are subject to an inherent degree of uncertainty and actual results may differ. Our significant accounting policies are more fully described in Note 2 to our consolidated financial statements included elsewhere in this annual report. Certain of our accounting policies are particularly important to the portrayal of our financial position and results of operations. In applying these critical accounting policies, our management uses its judgment to determine the appropriate assumptions to be used in making certain estimates. Those estimates are based on our historical experience, the terms of existing contracts, our observance of trends in our industry, information provided by our customers and information available from other outside sources, as appropriate. With respect to our policies on revenue recognition and warranty costs, our historical experience is based principally on our operations since we commenced selling our products in

1998. Our estimates are primarily guided by observing the following critical accounting policies:

- Revenue recognition;

- Provision for returns;
- Warranty costs;
- Allowance for doubtful accounts;
- Accounting for stock-based compensation;
- Inventories;
- Marketable securities;
- Impairment of goodwill and long lived assets;
- Income taxes; and
- Contingencies.

Because each of the accounting policies listed above requires the exercise of certain judgments and the use of estimates, actual results may differ from our estimations and as a result would increase or decrease our future revenues and net income.

Revenue recognition. We generate revenues mainly from selling its products along with related maintenance and support services. At times, these arrangements may also include professional services, such as installation services or training. The Company generally sells its products through resellers, distributors, OEMs and system integrators, all of whom are considered end-users.

Revenues from product sales are recognized when persuasive evidence of an agreement exists, title and risk of loss have transferred to the customer, no significant performance obligations remain, payment for products is not contingent upon performance of installation or service obligations, the fee is fixed or determinable and collectability is probable. In instances where final acceptance of the product or service is specified by the customer, we do not recognize the revenue until all acceptance criteria have been met.

Maintenance and support related revenues included in multiple element arrangements are deferred and recognized on a straight-line basis over the term of the applicable maintenance and support agreement. Other services are recognized upon the completion of installation or when the service is provided. In instances where the services provided in a multiple element arrangement are considered essential to the functionality of the product and payment of the product is contingent upon performance of the services, the sales of the products and services would be considered one unit of accounting. Deferred revenues are classified as short and long term based on their contractual term and recognized as revenues at the time the respective elements are provided.

Revenues arrangements with multiple deliverables are allocated using the relative selling price method. The Company determines the best estimated selling price (“BESP”) in multiple elements arrangements as follows:

For the products the Company determine the “BESP” based on management’s estimated selling price (“ESP”) by reviewing historical transactions and considering multiple other factors, including but not limited to, pricing practices including discounting, and competition.

As of January 1, 2011, the Company changed its pricing policy in respect of the sale of maintenance and support in new, multiple element arrangements. For the maintenance and support under the new pricing policy, the Company determined the ESP for the year ended December 31, 2011 in multiple-element arrangements based on reviewing historical transactions, and considering several other external and internal factors including, but not limited to, pricing practices including discounting and competition.

For the years ended December 31, 2013 and December 31, 2012, for maintenance and support, the Company determined the selling price based on VSOE of the price charged based on standalone sales (renewals) of such elements using a consistent percentage of the Company's product price lists in the same territories.

Deferred revenues are classified as short- and long-term based on their contractual term and recognized as revenues at the time the respective elements are provided.

We provide a provision for product returns and stock rotation based on its experience with historical sales returns, stock rotations and other known factors. Such provisions amounted to $0.89 million and $0.79 million as of December 31, 2013 and 2012, respectively.

Warranty costs. We typically grant a one-year hardware and three months software warranty on all of our products, or one-year hardware and software extended warranty to customers which purchase annual maintenance and support, and record a provision for warranty at the time the product's revenue is recognized. We estimate the liability of possible warranty claims based on our historical experience. We estimate the costs that may be incurred under our warranty arrangements and record a liability in the amount of such costs at the time product revenue is recognized. We periodically assess the adequacy of the recorded warranty liabilities and adjust the amounts as necessary.

Allowance for doubtful accounts. We evaluate the collectability of our accounts receivable on a specific basis. We estimate this allowance based on our judgment as to our ability to collect outstanding receivables. We primarily base this judgment on an analysis of significant outstanding invoices, the age of the receivables, our historical collection experience and current economic trends. In circumstances where we are aware of a specific customer's inability to meet its financial obligations to us, we record a specific allowance against amounts due to reduce the net recognized receivable to the amount we reasonably believe will be collected.

Accounting for stock-based compensation. We account for stock-based compensation in accordance with Accounting Standards Codification No. 718, "Compensation - Stock Compensation" ("ASC No. 718") that requires companies to estimate the fair value of equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as an expense over the requisite service periods in our consolidated statement of operations. We recognize compensation expense for the value of its awards granted based on the straight-line method over the requisite service period of each of the awards, net of estimated forfeitures. ASC No. 718 requires forfeitures to be estimated at the time of the grant and revised in subsequent periods if actual forfeitures differ from those estimates.

In connection with the grant of options, we recorded total stock-based compensation expense of $2.3 million in 2011, $4.8 million in 2012 and $7.7 million in 2013. In 2013, $0.3 million, $1.7 million, $3.1 million and $2.6 million of our stock-based compensation expense resulted from cost of revenue, research and development expenses, net, sales and marketing expenses and general and administrative expenses, respectively, based on the department in which the recipient of the option grant was employed. As of December 31, 2013, we had an aggregate of $15.8 million of deferred unrecognized stock-based compensation remaining to be recognized over a weighted average vesting period of 2.13 years. Inventories are stated at the lower of cost or market value. Inventory write-offs are provided to cover risks arising from slow-moving items, technological obsolescence, excess inventory and discontinued products. Inventory write-off provision as of December 31, 2013, 2012 and 2011 totaled $1.8 million, $1.4 million and $1.7 million respectively.

Marketable securities. We account for our investments in marketable securities using Accounting Standards Codification No. 320, "Investments – Debt and Equity Securities" ("ASC No. 320").

We determine the appropriate classification of marketable securities at the time of purchase and evaluate such designation as of each balance sheet date. We classify all of our investments in marketable securities as available for sale. Available for sale securities are carried at fair value, with unrealized gains and losses reported in "accumulated other comprehensive income (loss)" in shareholders' equity. Realized gains and losses on sales of investments are included in earnings and are derived using the specific identification method for determining the cost of securities. The amortized cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization together with interest and dividends on securities are included in financial income, net, if any.

As of December 31, 2013, we held available for sale marketable securities of $40.8 million. As of December 31, 2013, the unrealized loss recorded to other comprehensive income was $0.02 million.

Impairment of goodwill and long lived assets. Goodwill represents the excess of the purchase price over the fair value of net assets of purchased businesses. Under Accounting Standards Codification No. 350, "Intangibles-Goodwill and Other" ("ASC No. 350"), goodwill and intangible assets deemed to have indefinite lives are tested for impairment annually, or more often if there are indicators of impairment present.

We perform an annual impairment analysis of goodwill at December 31 of each year, or more often as applicable. We operate in one operating segment, and this segment comprises only reporting unit. The provisions of ASC No. 350 require that a two-step impairment test be performed on goodwill at the level of the reporting units. In the first step, we compare the fair value of each reporting unit to its carrying value. If the fair value exceeds the carrying value of the net assets, goodwill is considered not impaired, and no further testing is required to be performed. If the carrying value of the net assets exceeds the fair value, then we must perform the second step of the impairment test in order to determine the implied fair value of goodwill. If the carrying value of goodwill exceeds its implied fair value, then we would record an impairment loss equal to the difference.

We believe that our business activity and management structure meet the criterion of being a single reporting unit for accounting purposes. We performed an annual impairment analysis as of December 31, 2013 and determined that the carrying value of the reporting unit was less than the fair value of the reporting unit. Fair value is determined using market capitalization. During the years ended 2011, 2012 and 2013, no impairment losses were recorded.

Property and equipment and intangible assets subject to amortization are reviewed for impairment in accordance with ASC No. 360, "Accounting for the Impairment or Disposal of Long-Lived Assets," 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. As of December 31, 2013, no impairment losses have been identified.

Intangible assets acquired in a business combination are recorded at fair value at the date of the acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets that are not considered to have an indefinite useful life are amortized over their estimated useful lives. Some of the acquired intangible assets are amortized over their estimated useful lives in proportion to the economic benefits realized. This accounting policy results in accelerated amortization of such customer relationships and backlog as compared to the straight-line method. All other intangible assets are amortized over their estimated useful lives on a straight-line basis.

During 2011, 2012 and 2013, no impairment losses were recorded.

Income taxes. We account for income taxes in accordance with Accounting Standards Codification No. 740, "Income Taxes" ("ASC No. 740"). ASC No. 740 prescribes the use of the liability method, whereby deferred tax asset and liability account balances are determined based on differences between 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. We provide a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value if it is more likely than not that some portion or all of the deferred tax assets will not be realized.

In Israel, we have accumulated operating loss carry forwards of approximately $40.0 million and capital losses of approximately $27.3 million for tax purposes as of December 31, 2013, which may be carried forward and offset against taxable capital gains in the future for an indefinite period. In the United States, the accumulated losses for U.S. federal income tax return purposes were approximately $5.0 million as of December 31, 2013, which expire between 2024 and 2032. In France, we had approximately $4.4 million in net operating loss carry forwards as of December 31, 2013, which may be carried forward and offset against taxable capital gains in the future for an indefinite period. We believe that because of our history of losses, and uncertainty with respect to future taxable income, it is more likely than not that some of the deferred tax assets regarding the loss carry forwards will not be utilized in the foreseeable future, and therefore, a valuation allowance was provided to reduce deferred tax assets to their realizable value. The valuation allowance for the year ended December 31, 2013 was $12.7 million.

ASC No. 740 contains a two-step approach to recognizing and measuring a liability for uncertain tax positions. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. We recognize interest and penalties related to unrecognized tax benefits in our provision for income tax.

Contingencies. From time to time, we are a defendant or plaintiff in various legal actions, which arise in the normal course of business. We are required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of reserves required for these contingencies, if any, which would impact our results of operations, is made after considered analysis of each individual action together with our legal advisors. The required reserves may change in the future due to new developments in each matter or changes in circumstances and estimations. A change in the required reserves would impact our results of operations in the period the change is made.

Results of Operations

The following table sets forth our statements of operations as a percentage of revenues for the periods indicated:

	Year Ended December 31,		
	2011	2012	2013
Revenues:			
Products	73.1 %	73.6 %	68.7 %
Services	26.9	26.4	31.3
Total revenues	100.0	100.0	100.0
Cost of revenues:			
Products	25.1	25.6	21.3
Services	3.4	4.0	6.5
Total cost of revenues	28.5	44.8	27.8
Gross profit	71.5	55.2	72.2
Operating expenses:			
Research and development, net	17.1	21.1	28.0
Sales and marketing	34.1	32.5	41.2
General and administrative	9.6	10.2	10.3
Total operating expenses	60.8	63.8	79.5
Operating profit (loss)	10.7	(8.6)	(7.3)
Financing income (expenses), net	0.5	(1.3)	0.8
Profit (loss) before income tax expense (benefit)	11.2	(7.3)	(6.6)
Income tax (expense) benefit	0.1	0.9	(0.1)
Net profit (loss)	11.3 %	(6.4)%	(6.7)%

Year Ended December 31, 2013 Compared to Year Ended December 31, 2012

Revenues

Products. Product revenues decreased by $10.8 million, or 14.0%, to $66.3 million in 2013 from $77.1 million in 2012.The decrease is derived by the fact that, a portion of our sales are made to customers in countries in Europe, which have been impacted by the economic downturn and led our customers to minimize their investments in Capital Expenditure activities in 2013 and, to a lesser degree in 2012 and 2011. Sales of our high-end products, primarily the Allot Service Gateway platforms and value added products increase in 2013 (such as Allot Service Protector and Allot Proactive Analytics).

Services. Services revenues increased by $2.6 million, or 9.4%, to $30.2 million in 2013 from $27.6 million in 2012. The increase in service revenues is primarily attributable to an increase in our installed base in 2013 and also the growth of our professional services activities.

Product revenues comprised 68.7% of our total revenues in 2013, a decrease of 4.9% compared to 2012 while services revenues' portion of total revenues increased by the same percentage.

During 2013, revenues in Europe decreased by $17.9 million, or 45.1%, compared to 2012. Revenues in the Americas (excluding the United States) decreased by $2.6 million, or 32.7%, in 2013 compared to 2012, and revenues in Asia and Oceania increased by $8.0 million, or 36.2%, in 2013 compared to 2012. Revenues in the Middle East and Africa increased by $7.6 million, or 72.4%, compared to 2012. Revenues in the United States decreased by $3.3 million, or 13.5%, compared to 2012.

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Cost of revenues and gross margin

Products. Cost of product revenues decreased by $6.3 million, or 23.4%, to $20.6 million in 2013 from $26.9 million in 2012. Product gross margin, increased to 69.0% in 2013 from 65.2% in 2012.The main reason is the contribution of the settlement reached with the Office of Chief Scientist in December 31, 2012. The Company paid to the Office of Chief Scientist an amount of $15.9 million liability outstanding in 2013 which eliminated recurring royalty obligations related to revenues recorded.

Excluding the non-recurring payment to the Office of Chief Scientist in 2012, the decrease in cost of revenues is consistent with the decrease in product revenues.

Services. Cost of service revenues increased by $2.1 million, or 49.4%, to $6.3 million in 2013 from $4.2 million in 2012. This increase is consistent with the increase of service revenues.

Total gross margin, increased to 72.2% in 2013 from 70.4% in 2012, excluding the impact of the settlement.

Operating expenses

Research and development. Gross research and development expenses increased by $3.2 million, or 12.9%, to $28.1 million in 2013 from $24.9 million in 2012. This increase is primarily attributable to an increase in salaries and labor costs which principally resulted from an increase in the average yearly head count derived mainly from the acquisitions of Ortiva and Oversi. This increase along with the increase in other overhead expenses amounted to $2.7 million. In addition, stock-based compensation increased by $0.5 million.

Research and development expenses, net of received and accrued grants from the Office of the Chief Scientist, increased by $4.9 million, or 22.5%, to $27.0 million in 2013 from $22.1 million in 2012. Grants received from the Office of the Chief Scientist totaled $1.1 million in 2013 compared to $2.9 million in 2012. The decrease in grants received is due the fact that from 2013, the Company is qualified to participate in an approved program with the OCS for companies with large research and development activities and certain threshold of revenues. Under this program the Company is eligible to receive non-bearing royalty grants that do not require repayments. The grants are smaller than the royalty bearing grants the company received in previous years.

Sales and marketing. Sales and marketing expenses increased by $5.7 million, or 16.7%, to $39.8 million in 2013 from $34.1 million in 2012. This increase is primarily attributable to increased salaries and related expenses of approximately $4.7 million due to increase in average yearly head count from the acquisitions of Ortiva and Oversi. Stock-based compensation increased by $1.5 million, commission expenses, travel and other expenses decreased by $0.5 million.

Sales and marketing expenses, as a percentage of total revenues increased to 41.2% in 2013 from 32.6% in 2012.

General and administrative. General and administrative expenses decreased by $0.7 million, or 6.7%, to $10.0 million in 2013 from $10.7 million in 2012. This decrease is attributable to a decrease in acquisitions activity related expenses of approximately $3.1 million. These expenses were higher in 2012 as a result of non-recurring legal and finance expenses related to acquisition activities during 2012. Labor costs increased by approximately $0.7 million due to increase in the average yearly head count. Stock-based compensation increased by approximately $1.2 million. Travel and other overhead expenses increased by $0.5 million.

General and administrative expenses as a percentage of revenues increased to 10.3% in 2013 from 10.2% 2012.

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Financial income (expenses), net. In 2013, we had $0.7 million financial income, net compared to $1.4 million financial income, net in 2012. The change is primarily attributed to a decrease in our interest income derived from lower interest rates received for short-term bank deposits during 2013 and from the increase in the amortization of the premium for our marketable securities during 2013.

Income tax expense (benefit). Income tax expense in 2013 was $0.1 million, compared to income tax benefit of $1.0 million in 2012. The change is primarily due to the fact that the company recorded deferred tax assets for the first time in 2012 related to our net operating losses expected to be utilized in the foreseeable future.

Year Ended December 31, 2012 Compared to Year Ended December 31, 2011

Revenues

Products. Product revenues increased by $20.3 million, or 35.8%, to $77.1million in 2012 from $56.8 million in 2011. The increase is primarily attributable to increased sales of our high-end products, primarily the Service Gateway platforms and value added products (such as Service Protector and MediaSwift), driven by orders placed by Tier 1 operator group and leading operators in North America, Latin America, Africa and East Asia. Video optimization and caching products sales, driven from the acquisitions of Ortiva and Oversi contributed to the increased sales in the second half of 2012.

Services. Services revenues increased by $6.7 million, or 31.9%, to $27.6 million in 2012 from $20.9 million in 2011. The increase in service revenues is primarily attributable to an increase in our installed base in 2012 and services revenues related to video optimization and caching products, driven from the acquisitions.

Product revenues comprised 73.6% of our total revenues in 2012, an increase of 0.6% compared to 2011 while services revenues' portion of total revenues decreased by the same percentage.

During 2012, revenues in Europe increased by $1.2 million, or 3.2%, compared to 2011. Revenues in the Americas (excluding the United States) increased by $1.0 million, or 13.9%, in 2012 compared to 2011, and revenues in Asia and Oceania increased by $1.7 million, or 8.4%, in 2012 compared to 2011. Revenues in the Middle East and Africa increased by $7.8 million, or 288.9%, compared to 2011. Revenues in the United States increased by $15.2 million, or 160.2%, compared to 2011, which was primarily attributable to orders placed by a leading operator.

Cost of revenues and gross margin

Products. Cost of product revenues increased by $7.3 million, or 37.4%, to $26.9 million in 2012 from $19.5 million in 2011. In December 31, 2012 we recorded a liability related to settlement of the Office of Chief Scientist grants of approximately $15.9 million to be paid in 2013. Excluding the non-recurring payment to the Office of Chief Scientist, the increase in cost of revenues is consistent with the increase in product revenues. Product gross margin, decreased to 65.2% in 2012 from 65.6% in 2011.

Services. Cost of service revenues increased by $1.5 million, or 58.6 %, to $4.2 million in 2012 from $2.6 million in 2011. This increase is primarily attributable to higher support personnel expenses associated with deployment of our products with large service providers. In 2012, services gross margin decreased to 84.9% from 87.4% in 2011.

Total gross margin, excluding the impact of the settlement, decreased to 70.4% in 2012 from 71.4% in 2011.

Operating expenses

Research and development. Gross research and development expenses increased by $8.0 million, or 47.5%, to $24.9 million in 2012 from $16.9 million in 2011. This increase is primarily attributable to an increase in salaries and labor costs of approximately $5.4 million, which principally resulted from an increase in head count derived mainly from the acquisition of Ortiva and Oversi, which have significant research and development departments. In addition, other overhead expenses increased by $1.0 million, costs of contractors increased by $0.8 million and stock-based compensation increased by $0.8 million and depreciation.

Research and development expenses, net of received and accrued grants from the Office of the Chief Scientist, increased by $8.8 million, or 66.8%, to $22.1 million in 2012 from $13.2 million in 2011. Grants received from the Office of the Chief Scientist totaled $2.9 million in 2012 compared to $3.7 million in 2011. The decrease in grants received is attributable to a decrease in the approved grants from the Office of the Chief Scientist due to the settlement reached with them. We did not receive grants from the Office of Chief Scientist during the fourth quarter of 2012, and accordingly did not record accrued grants for this period. Research and development expenses, net, as a percentage of revenues increased to 21.1% in 2012 from 17.0% in 2011.

Sales and marketing. Sales and marketing expenses increased by $7.6 million, or 28.6%, to $34.1 million in 2012 from $26.5 million in 2011. This increase is primarily attributable to increased salaries and related expenses of approximately $5.3 million due to increased head count from the acquisitions of Ortiva and Oversi and new recruitments of sales and pre sales personnel. Stock-based compensation increased by $1.0 million, commission expense increased by $0.8 million, and travel and other expenses increased by $0.5 million.

Sales and marketing expenses, as a percentage of total revenues decreased to 32.6% in 2012 from 34.1% in 2011.

General and administrative. General and administrative expenses increased by $3.2 million, or 42.7%, to $10.7 million in 2012 from $7.5 million in 2011. This increase is attributable to increased professional services of approximately $1.0 million resulted from non-recurring legal and finance expenses related to acquisition activity. Wage expenses increased by approximately $1.0 million due to increased head count. Stock-based compensation increase approximately $0.6 million. Travel and other overhead expenses increased by $0.6 million.

General and administrative expenses as a percentage of revenues increased to 10.2% in 2012 from 9.6% 2011.

Financial expenses (income), net. Financial and other income, net in 2012 was $1.4 million income compared to $0.4 million in 2011. The decrease is primarily attributable to the decrease in interest income received from investments in short-term bank deposits as a result of the cash received from our offering of ordinary shares in November 2011.

Income tax benefit. Income tax benefit in 2012 was $1.0 million, compared to income tax benefit of $0.1 million in 2011. The change is primarily due to an increase in deferred tax assets related to our net operating losses expected to be utilized in the future.

B. Liquidity and Capital Resources

As of December 31, 2013, we had $42.8 million in cash and cash equivalents, $40.8 million available for sale marketable securities and $38.0 million short-term deposits. As of December 31, 2013, our working capital, which we calculate by subtracting our current liabilities from our current assets, was $133.9 million.

Based on our current business plan, we believe that our existing cash balances, will be sufficient to meet our anticipated cash needs for working capital and capital expenditures for at least the next twelve months. If our estimates of revenues, expense or capital or liquidity requirements change or are inaccurate and are insufficient to satisfy our liquidity requirements, we may seek to sell additional equity or arrange additional debt financing. In addition, we may seek to sell additional equity or arrange debt financing to give us financial flexibility to pursue attractive acquisitions or investment opportunities that may arise in the future.

Operating activities.

Net cash we used in operating activities in 2013 was $19.2 million. Net cash used in operating activities consisted of a net loss of $6.5 million, a decrease of $15.9 million in liability related to settlement of the Office of Chief Scientist grants, depreciation and amortization of intangible assets of $6.3 million, $7.7 million of stock-based compensation expense, an increase of $3.8 million in inventory, a decrease of $2.1 million in employees and payroll accruals, a decrease of $3.3 million in trade receivables, a decrease of $2.8 million in deferred revenues attributed to sales which revenue recognition criteria were met while cash was collected in the previous years and a decrease of $1.6 million in trade payables.

During 2012, we generated $8.7 million in cash and cash equivalents from operating activities. Net cash provided by operating activities consisted of a net loss of $6.7 million, an increase of $15.9 million in liability related to settlement of the Office of Chief Scientist grants, depreciation and amortization of intangible assets of $5.1 million, $4.8 million of stock-based compensation expense, a decrease of $3.2 million in inventory and an increase of $2.4 million in employees and payroll accruals. This was partially offset by an increase of $8.1 million in trade receivables, a decrease of $7.1 million in deferred revenues attributed to sales which revenue recognition criteria were met while cash was collected in the previous years and a decrease of $1.3 million in trade payables.

Investing activities.

Net cash provided by investing activities in 2013 was $11.1 million, primarily attributable to the redemption of short-term bank deposits of $40.0 million, an investment in available-for sale marketable securities of $32.8 million and the purchase of property and equipment of $2.7 million and an increase due to redemption of marketable securities of $6.5 million.

Net cash used in investing activities in 2012 was $79.3 million, primarily attributable to the investment in short-term bank deposits of $54.0 million, cost of acquiring Ortiva and Oversi of $24.9 million, an investment in available-for sale marketable securities of $8.2 million and the purchase of property and equipment of $3.8 million. The above changes were partially offset by redemption of marketable securities of $10.7 million.

We expect that our capital expenditures will total approximately $3.0 million in 2014. We anticipate that these capital expenditures will be primarily related to further investments in lab equipment for research and development, as well as customer support and demo units.

Financing activities.

Net cash provided by financing activities in 2013 was $0.9 million, which was attributable to issuance of share capital through the exercise of stock options of $0.9 million.

Net cash provided by financing activities in 2012 was $4.0 million, which was attributable to issuance of share capital through the exercise of stock options of $5.9 million partially offset by a $2.0 million redemption of bank loan in connection with our acquisition of Oversi.

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C. Research and Development, Patents and Licenses

Our research and development efforts have benefited from royalty-bearing grants from the Office of the Chief Scientist. The government grants we have received for research and development expenditures restrict our ability to manufacture products and transfer technologies outside of Israel and require us to satisfy specified conditions. If we fail to comply with such restrictions or these conditions, we may be required to refund grants previously received together with interest and penalties, and may be subject to criminal charges.

In 2013 we were qualified to participate in two research and development program funded by the Office of the Chief Scientist to develop generic technology relevant to the development of our products. Such programs are approved pursuant to the Research and Development Law, and the regulations promulgated thereunder. One of the programs is for companies with large research and development activities and the other is for members of a "Magnet" consortium. We were eligible to receive non-royalty-bearing grants constituting between 40% and 55% of certain research and development expenses relating to these programs. Although the grants under these programs are not required to be repaid by way of royalties, the restrictions under the Research and Development Law described above apply to these programs.

Total research and development expenses, before royalty bearing grants, were approximately $16.9 million, $24.9 million and $28.1 million in the years ended December 31, 2011, 2012 and 2013, respectively. Royalty bearing grants amounted to $3.7 million and $2.9 million in 2011 and 2012 respectively and non-bearing royalty grants amounted to $1.1 million in 2013.

D. Trend Information

See “ITEM 5: Operating and Financial Review and Prospects” above.

E. Off-Balance Sheet Arrangements

We are not a party to any material off-balance sheet arrangements. In addition, we have no unconsolidated special purpose financing or partnership entities that are likely to create material contingent obligations.

F. Contractual Obligations

The following table of our material contractual and other obligations known to us as of December 31, 2013, summarizes the aggregate effect that these obligations are expected to have on our cash flows in the periods indicated.

		Payments due by period			
Contractual Obligations	Total	Less than 1 year	1– 3 years	3-5 years	Over 5 years
		(in thousands of U.S. dollars)			
Operating leases — offices(1)	$8,742	$2,447	$5,389	$906	$-
Operating leases — vehicles	799	461	338	-	-
Purchase obligations	1,166	934	116	116	-
Accrued severance pay(2)	282	-	-	-	282
Total	$10,989	$3,842	$5,843	$1,022	$282

(1) Consists primarily of an operating lease for our facilities in Hod Hasharon, Israel, as well as operating leases for facilities leased by our subsidiaries.

(2)

Severance pay relates to accrued severance obligations to our Israeli employees as required under Israeli labor law. These obligations are payable only upon termination, retirement or death of the respective employee and there is no obligation if the employee voluntarily resigns. Of this amount, $28,000 is unfunded.

ITEM 6: Directors, Senior Management and Employees

A. Directors and Senior Management

Our directors and executive officers, their ages and positions as of March 6, 2014 are as follows:

Name	Age	Position
Directors		
Shraga Katz	61	Chairman of the Board
Rami Hadar	50	Director, Chief Executive Officer and President
Itzhak Danziger	65	Director
Nurit Benjamini(1)(2)(3)	47	Director
Steven D. Levy(1)(2)	57	Director
Dov Baharav(1)(2)	63	Director
Yigal Jacoby	53	Director
Executive Officers		
Nachum Falek	42	Chief Financial Officer
Amir Hochbaum	54	Vice President — Research and Development
Anat Shenig	44	Vice President — Human Resources
Andrei Elefant	40	Vice President — Product Management and Marketing
Gary Drutin	52	Vice President — International Sales
Itamar Rosen	49	Vice President — Legal Affairs, General Counsel and Company Secretary
Jay Klein	50	Vice President — Chief Technology Officer
Lior Moyal	42	Vice President — Business Development
Pini Gvili	48	Vice President — Operations
Ramy Moriah	58	Vice President — Customer Care and Information Technology
Vin Costello	57	Vice President and General Manager — The Americas

(1) Member of our compensation and nomination committee.
(2) Member of our audit committee.
(3) Lead independent director.

Directors

Shraga Katz has served as our chairman of the board of directors since 2008. Mr. Katz is a Venture Partner of Magma Venture Partners, a leading venture capital firm specializing in early-stage investments in communication, semiconductors, internet and media. Mr. Katz has over 30 years of experience in the technology sector and has specialized for over 20 years in the communications industry. In 1996, Mr. Katz founded Ceragon Networks Ltd. (NASDAQ: CRNT), a global provider of high capacity wireless networking solutions for mobile and fixed operators

and private networks, and served as its President and Chief Executive Officer until mid-2005. Prior to founding Ceragon, Mr. Katz served in the Israeli Defense Forces for 17 years. Mr. Katz was head of the Electronic Research and Development Department of the Israeli Ministry of Defense. Mr. Katz serves as director on the Board of GreenSQL and Corephotonics. Mr. Katz holds a B.Sc. from the Technion — Israel Institute of Technology and an M.B.A. from Tel Aviv University.

Rami Hadar has served as our Chief Executive Officer and President since 2006 and is a member of our board of directors. Prior to joining us, Mr. Hadar founded CTP Systems, a developer of cordless telephony systems in 1989 and served as Chief Executive Officer until its acquisition by DSP Communications in 1995. Mr. Hadar continued with DSP Communication's executive management team for two years, and thereafter, in 1999, the company was acquired by Intel. In 1997, Mr. Hadar co-founded Ensemble Communications, a pioneer in the broadband wireless space and the WiMax standard, where he served as Executive Vice President of Sales and Marketing until 2002. Mr. Hadar also served as Chief Executive Officer of Native Networks from 2002 to 2005, which was successfully sold and integrated to Alcatel. Mr. Hadar holds a B.Sc. in Electrical Engineering from Technion — Israel Institute of Technology.

Itzhak Danziger has served as a director since 2011. Prior to his appointment as a director, Mr. Danziger served as an observer to our Board since 2010. Itzhak Danziger serves as chairman of the board of Galil Software, an Israeli software services company, and as a director of Jinni Media, a privately held technology company. From 1985 to 2007, Mr. Danziger held various executive positions at Comverse, a technology companies group that develops and markets telecommunications systems, including as president of Comverse Technology Group, as president of Comverse Network Systems and as chairman of Comverse subsidiary - Starhome. Prior to joining Comverse, Mr. Danziger held various R&D and management positions in Tadiran Telecom Division, which was later acquired by ECI Telecom. Further, Mr. Danziger serves as a director in Israel Venture Network, a venture philanthropy NGO, in Avney Rosha, the Israel Institute for School Leadership, and in other non-governmental organizations. Mr. Danziger was also a member of the National Task Force for the Advancement of Education in Israel (Dovrat Committee) and was chairman of two of its subcommittees. Mr. Danziger holds B.Sc. cum laude and M.Sc. in electrical engineering from the Technion - Israel Institute of Technology and M.A. cum laude in philosophy and digital culture from Tel Aviv University.

Nurit Benjamini has served as an outside director since 2007 and serves as the lead independent director on our board. Ms. Benjamini serves as the Chief Financial Officer of Wixpress Ltd., an internet company that offers web technology that enables online users to create HTML5 websites regardless of technical skill or previous knowledge, since May 2011. Previously, from 2007 to 2011, Ms. Benjamini has served as the Chief Financial Officer of CopperGate Communications Ltd., a leading fabless semiconductor company in home entertainment networking, that was acquired by Sigma Designs Inc. (NASDAQ:SIGM) in November 2009. Prior to her position with CopperGate Communications Ltd., Ms. Benjamini served as the Chief Financial Officer of Compugen Ltd. (NASDAQ: CGEN) from 2000 to 2007. Prior to her position with Compugen Ltd., from 1998 to 2000, Ms. Benjamini served as the Chief Financial Officer of Phone-Or Ltd. Between 1993 and 1998, Ms. Benjamini served as the Chief Financial Officer of Aladdin Knowledge Systems Ltd. (formerly NASDAQ: ALDN). Ms. Benjamini serves as an outside director of BiolineRX Ltd., a member of its compensation committee, and as a chairman of its audit committee. Ms. Benjamini holds a B.A. in Economics and Business and an M.B.A. in Finance, both from Bar Ilan University, Israel.

Steven D. Levy has served as an outside director since 2007. Mr. Levy served as a Managing Director and Global Head of Communications Technology Research at Lehman Brothers from 1998 to 2005. Before joining Lehman Brothers, Mr. Levy was a Director of Telecommunications Research at Salomon Brothers from 1997 to 1998, Managing Director and Head of the Communications Research Team at Oppenheimer & Co. from 1994 to 1997 and a senior communications analyst at Hambrecht & Quist from 1986 to 1994. Mr. Levy has served as a director of PCTEL, a broadband wireless technology company since January 2006 and of privately held GENBAND Inc., a U.S. provider of telecommunications equipment, since August 2007. Mr. Levy holds a B.Sc. in Materials Engineering and an M.B.A., both from the Rensselaer Polytechnic Institute.

Yigal Jacoby co-founded our company in 1996 and served as our CEO until 2006 and as a Chairman of our board of directors until 2008. Prior to co-founding Allot, Mr. Jacoby founded Armon Networking, a manufacturer of network management solutions in 1992, and managed it until it was acquired by Bay Networks, where he served as the General Manager of its Network Management Division. From 1985 to 1992, Mr. Jacoby held various engineering and

marketing management positions at Tekelec, a manufacturer of Telecommunication monitoring and diagnostic equipment. Currently, Mr. Jacoby is an active investor and director of several Israeli start-up companies, including Chairman at LiveU Ltd., a provider of live cellular video transmission solutions and Chairman at Appforma Ltd., a provider of SMB marketing platforms. Mr. Jacoby has a B.A., cum laude, in Computer Science from Technion — Israel Institute of Technology and an M.Sc. in Computer Science from University of Southern California.

Dov Baharav joined our board of directors in 2013. He has served as a member of Mellanox's Board of Directors since November 2010. Mr. Baharav was previously the chairman of the Board of Directors of Israel Aerospace Industries Ltd., a world leader in defense and civil aerospace technology, with revenue over 3.5 Billion dollars, of which 82% is exported. In addition, Mr. Baharav was also previously President and Chief Executive Officer and a member of the board of directors of Amdocs Management Limited, where he transformed the company through vertical and horizontal expansion, various acquisitions, and corporate restructuring. Beginning in 1991 when he joined Amdocs, Mr. Baharav served as Vice President and then President of Amdocs' principal US subsidiary, Amdocs, Inc. Four years later, he served as Chief Financial Officer of Amdocs Management, and in July 2002, was appointed President and Chief Executive Officer. He was instrumental in transitioning the company back to a state of growth with annual revenues more than doubling over a span of a few years following his appointment. Prior to 1991, Mr. Baharav served as Chief Operating Officer of Optrotech Ltd., a publicly held company that develops, manufactures and markets electro-optical devices. Mr. Baharav is actively involved with the College of Management Academic Studies in Rishon Lezion, Israel. He is also a member of the board of directors at SeamBI, a company specializing in dynamic product placement. Mr. Baharav holds a Bachelor of Science in Physics and Accounting, as well as an MBA from Tel Aviv University.

Executive Officers

Nachum Falek has served as Chief Financial Officer since 2010. Prior to joining Allot, Mr. Falek served from 2003 as the CFO of AudioCodes (NASDAQ: AUDC), a leading provider of Voice over IP (VoIP) technologies and Voice Network products. From 2000 to 2003, Mr. Falek was the Director of Finance of AudioCodes. Earlier in his career, Mr. Falek served as a Controller at ScanVec-Amiable Ltd., and as a Manager at Ernst & Young Israel. Mr. Falek is a Certified Public Accountant (CPA) and holds a B.A. in Accounting and Economics from Haifa University and a M.B.A. from Tel Aviv University.

Amir Hochbaum has served as our Vice President — Research and Development since 2008. Before joining Allot, Mr. Hochbaum served as the Chief Operating Officer of Axerra Networks. From 2005 to 2007, Mr. Hochbaum was Senior Vice President, Research, Development and Operations of Vyyo Israel (NASDAQ: VYYO) where he also served as a member of Vyyo's executive management team. Prior to Vyyo, between 1994 and 2005, Mr. Hochbaum held a succession of management positions at Avaya (formerly Lucent, Madge and Lannet) including Managing Director and Vice President of R&D. Between 1984 and 1994, Mr. Hochbaum held a succession of management positions at ServiceSoft, including management of engineering, product development, product management and customer service . Mr. Hochbaum holds a B.S. in Mathematics and Computer Science and an M.S. in Computer Science from the Hebrew University of Jerusalem.

Gary Drutin joined our company in 2012 and serves as our Vice President — International Sales. Mr. Drutin oversees the international development, implementation and management of direct and channel sales in EMEA and Asia-Pacific markets. Before joining Allot, Mr. Drutin served as the business development director of the microWave LOB at Broadcom (after the Provigent acquisition) from 2011 to 2012. Prior to the acquisition he was Senior VP worldwide Sales at Provigent from 2010 to 2011. From 2004 to 2010 he was VP Global Sales at AudioCodes Ltd. From 1997 to 2004, he served as Country Manager and General Manager for Cisco Israel, Cyprus and Malta. From 1990 to 1997, he served in sales management roles at Digital Equipment Corporation Israel. Mr. Drutin holds an M.B.A from Tel-Aviv University in Information Systems and Marketing and a B.Sc. degree in Computer Engineering from the Technion — Israel Institute of Technology.

Itamar Rosen joined our company in 2012 and has served as our Vice President — Legal Affairs, General Counsel and Company Secretary. Prior to joining Allot, Mr. Rosen served as Vice President Legal Affairs and General Counsel of AudioCodes Ltd. between 2000 and 2012, and in various positions at four different major law firms in England and Israel prior to that. Mr. Rosen is a qualified arbitrator and admitted to practice as a lawyer in New York, England and Wales and Israel. Mr. Rosen received a LL.B (Hons.) degree from University of Essex in 1989 (England), an M.B.A from the Open Business School in 1995 (England) and a LL.M, magna cum laude from Tel-Aviv University as part of an executive program in collaboration with University of California Berkeley in 2005.

Anat Shenig joined our company in 2000 and has served as our Vice President — Human Resources since 2007. Ms. Shenig is responsible for human resources recruiting, welfare policy and employees' training. Prior to joining us, Ms. Shenig served as Human Resource Manager for Davidoff insurance company and as an organizational consultant for Aman Consulting. Ms. Shenig holds bachelor degrees in Psychology and Economics from Tel Aviv University and an M.B.A. in organizational behavior from Tel Aviv University.

Andrei Elefant joined our company in 2000 and has served as our Vice President — Product Management since 2007. Mr. Elefant assumed responsibility over our marketing activities in 2008. Mr. Elefant is responsible for product management, product marketing and strategic project management. Prior to joining us, Mr. Elefant served as officer in the Israeli air force. Mr. Elefant holds a B.Sc. in Mechanical Engineering from the Technion — Israel Institute of Technology and an M.B.A. from Tel-Aviv University.

Jay Klein joined our company in 2006 and has served as our Vice President — Chief Technology Officer since 2007. Mr. Klein is responsible for driving our technology strategy, expanding our core algorithmic competence and driving intellectual property development, industry standards involvement and academic cooperation. Prior to joining us, between 2004 and 2006, Mr. Klein served as VP at DSPG (VoIP and multimedia silicon solutions) where he was responsible for strategic technology acquisitions. Between 1997 and 2003, Mr. Klein was Co-Founder and CTO of Ensemble Communications, a wireless access systems manufacturer and was one of the founders and creators of WiMAX and IEEE 802.16. Prior to that, between 1993 and 1997, he served as CTO and VP of R&D at CPT Systems, a cellular systems manufacturer, which was acquired by DSP Communications and later by Intel. Mr. Klein holds a B.Sc. in Electrical and Electronic Engineering from Tel-Aviv University.

Lior Moyal has served as Vice President Business Development since 2009. Mr. Moyal is responsible for driving the company's global business development strategy including developing partnerships with global system integrators, creating alliances with value added network and subscriber services partners, and recruiting and managing worldwide OEM partners. Prior to joining us, from 2008 to 2009, Mr. Moyal was VP of Business Development of AudioCodes (NASDAQ: AUDC). Previously, from 2005 to 2007, Mr. Moyal was AudioCodes' VP of Marketing. Before that, from 2004 to 2005, Mr. Moyal was VP of Business Development at BridgeWave Communications. Prior to that, Mr. Moyal held variety of management positions in Orckit (NASDAQ: ORCT), including VP of Product Management and VP of Business Development. Mr. Moyal holds a B.Sc. in Physics from the Hebrew University of Jerusalem and an M.B.A. from Tel Aviv University.

Pini Gvili has served as our Vice President — Operations since 2006. Prior to joining us, from 2004 to 2006, he served as Vice President Operations for Celerica, a start-up company specializing in solutions for cellular network optimization. From 2001 to 2004, Mr. Gvili was the Vice President — Operations and IT at Terayon Communication Systems, and from 1998 to 2000, held the position of Manager of Integration and Final Testing at Telegate. Mr. Gvili was also a hardware/software engineer at Comverse/Efrat, a world leader of voice mail and digital recording systems, from 1994 to 1997. Mr. Gvili has a B.Sc. in Computer Science from Champlain University and was awarded a practical electronics degree from ORT Technical College.

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Ramy Moriah has served as our Vice President — Customer Care & IT since 2005. Prior to joining us, Mr. Moriah was a founding member of Daisy System's Design Center in Israel, in 1984. From 1991 to 1994, Mr. Moriah held the position of Manager of Software Development at Orbot Instruments, a world leader of Automatic Optical Inspection manufacturer for the VLSI Chip Industry. Mr. Moriah was also the acting General Manager at ACA, 3D CAD/solid modeling software for architecture from 1995 to 1997, and served there as Vice President — Research and Development from 1995 to 1997. Mr. Moriah holds a B.Sc., cum laude , in Computer Engineering from the Technion — Israel Institute of Technology and an M.Sc. in Management and Information Systems from the Tel Aviv University School of Business Administration.

Vin Costello has served as our Vice President and General Manager — The Americas since 2006. Mr. Costello began his career with NYNEX and rapidly rose through the ranks achieving the title of Vice President, Business Network Solutions and Vice President Global Sales. Mr. Costello founded and headed NYNEX Network Integration and upon the merger with Bell Atlantic, was named President and CEO of Bell Atlantic Network Integration. Mr. Costello departed Verizon for an optical networking start-up where he served as VP of Sales and assisted Corvis Corporation, in their successful initial public offering. Mr. Costello was subsequently named VP and General Manager of the Managed Storage Division after Corvis purchased Broadwing and reinvented itself as a service provider. Mr. Costello holds a B.Sc. in Computer Applications and Information Systems as well as Business Management (double major) from New York University and earned a M.Sc. in Telecommunications and Computing Management from Polytechnic University.

B. Compensation of Officers and Directors

The aggregate compensation paid to or accrued on behalf of our directors and executive officers as a group during 2013 consisted of approximately $3.5 million in salary, fees, bonus, commissions and directors' fees and approximately $0.4 in amounts set aside or accrued to provide pension, retirement or similar benefits, but excluding amounts we expended for automobiles made available to our officers, expenses, including dues for professional and business associations, business travel and other expenses, and other benefits commonly reimbursed or paid by companies in Israel.

In 2013, we paid the chairman of the board of directors, Mr. Shraga Katz, an annual fee of NIS 279,000 (approximately $80,000). Mr. Katz is also entitled to customary benefits for a senior executive officer at an Israeli company. In 2013, we paid each of our directors, Itzhak Danziger and Yigal Jacoby, an annual fee of NIS 45,000 (approximately $12,900) and a per meeting attendance fee of NIS 3,750 (approximately $1,100), linked to the Israeli consumer price index. During such time, we paid each of our outside directors, Nurit Benjamini, Steven Levy and Dov Baharav, fees as permitted by the Israeli Companies Law (the "Companies Law"). In 2013, we paid each of our directors (except for Shraga Katz and Rami Hadar) a per meeting attendance fee of NIS 3,750 (approximately $1,100) for any meeting he or she attended in person, NIS 2,250 (approximately $650) for any meeting he or she attended by conference call or similar means, and NIS 1,875 (approximately $550) for any written resolution of the Board executed by such director. Our directors are also typically granted upon election an agreed amount of options and upon reelection options to purchase 30,000 of our ordinary shares, which vest in equal installments on a quarterly basis over a period of three years.

In 2013, we paid our President and Chief Executive Officer, Mr. Rami Hadar, an annual salary of NIS 1,003,000 (approximately $288,000) and a bonus of NIS 401,000 (approximately $115,000) in connection with his performance in 2012.

During 2013, our officers and directors received, in the aggregate, options to purchase 263,334 ordinary shares under our equity based compensation plan. These options have a weighted average exercise price of approximately $12.68 and the options will expire ten years after the date the options were granted.

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Compensation Policy

Under the Companies Law, we are required to adopt a compensation policy, recommended by the compensation and nominating committee and approved by the Board of Directors and the shareholders, in that order. The shareholder approval requires a majority of the votes cast by shareholders, excluding any controlling shareholder and those who have a personal interest in the matter. In general, all directors and executive officers' terms of compensation – including fixed remuneration, bonuses, equity compensation, retirement or termination payments, indemnification, liability insurance and the grant of an exemption from liability – must comply with the compensation policy.

In addition, the compensation terms of directors, the chief executive officer, and any employee or service provider who is considered a controlling shareholder must be approved separately by the compensation and nominating committee, the Board of Directors and the shareholders of the Company (by the same majority noted above), in that order. The compensation terms of other executive officers require the approval of the compensation and nominating committee and the Board of Directors.

Our compensation policy was approved by our compensation and nominating committee and by our Board of Directors, and subsequently approved by our shareholders in August 2013, and will be in effect for a period of three years following approval. The following is a summary of our Compensation Policy and is qualified by reference to the full text thereof, a copy of which was attached to our Proxy Statement for our 2013 Annual Meeting of Shareholders.

Objectives: To attract, motivate and retain highly experienced personnel who will provide leadership for Allot's success and enhance shareholder value, and to provide for each executive officer an opportunity to advance in a growing organization.

Compensation instruments: Includes base salary; limited personal benefits and perquisites; cash bonuses; equity-based awards; and retirement and termination arrangements.

Ratio between fixed and variable compensation: Allot aims to balance the mix of fixed compensation (such as base salary) and variable compensation (such as performance based cash bonuses and equity-based awards) pursuant to the ranges set forth in the Compensation Policy in order, among other things, to tie the compensation of each executive officer to Allot's financial and strategic achievements and enhance the alignment between the executive officer's interests and the long-term interests of Allot and its shareholders.

Internal compensation ratio: Allot will target a ratio between overall compensation of the executive officers and the average and median salary of the other employees of Allot, as set forth in the Compensation Policy, to ensure that levels of executive compensation will not have a negative impact on work relations in Allot.

Base salary, benefits and perquisites: The Compensation Policy provides guidelines and criteria for determining base salary, benefits and perquisites for executive officers.

Cash bonuses: Allot's policy is to allow annual cash bonuses, which may be awarded to executive officers pursuant to the guidelines and criteria, including caps on maximum payouts, set forth in the Compensation Policy.

"Clawback": In the event of an accounting restatement, Allot shall be entitled to recover from current executive officers bonus compensation in the amount of the excess over what would have been paid under the accounting restatement, with a three-year look-back.

Equity-based awards: Allot's policy is to provide equity-based awards in the form of stock options, restricted stock units and other forms of equity, which may be awarded to executive officers pursuant to the guidelines and criteria, including minimum vesting period, set forth in the Compensation Policy.

Retirement and termination: The Compensation Policy provides guidelines and criteria for determining retirement and termination arrangements of executive officers, including limitations thereon.

Exculpation, indemnification and insurance: The Compensation Policy provides guidelines and criteria for providing directors and executive officers with exculpation, indemnification and insurance.

Directors: The Compensation Policy provides guidelines for the compensation of our directors in accordance with applicable regulations promulgated under the Companies Law, and for equity-based awards that may be granted to directors pursuant to the guidelines and criteria, including minimum vesting period, set forth in the Compensation Policy.

Applicability: The Compensation Policy applies to all compensation agreements and arrangements approved after the date on which the Compensation Policy is approved by the shareholders.

Review: The compensation and nominating committee and the Board of Directors of Allot reviews the adequacy of the Compensation Policy from time to time, as required by the Companies Law.

C. Board Practices

Corporate Governance Practices

As a foreign private issuer, we are permitted under NASDAQ Marketplace Rule 5615(a)(3) to follow Israeli corporate governance practices instead of the NASDAQ Stock Market requirements applicable to the U.S. issuers, provided we disclose which requirements we are not following and describe the equivalent Israeli requirement. See "ITEM 16G: Corporate Governance Requirements" for a discussion of those ways in which our corporate governance practices differ from those required by NASDAQ for domestic companies.

Board of Directors

Terms of Directors

Our articles of association provide that we may have not less than five directors and up to nine directors.

Under our articles of association, our directors (other than the outside directors, whose appointment is required under the Companies Law; see "—Outside Directors") are divided into three classes. Each class of directors consists, as nearly as possible, of one-third of the total number of directors constituting the entire board of directors (other than the outside directors). At each annual general meeting of our shareholders, the election or re-election of directors following the expiration of the term of office of that class of directors is for a term of office that expires on the third annual general meeting following such election or re-election, such that each year the term of office of only one class of directors will expire.

Shraga Katz, who is a Class I director and our Chairman of the board of directors, will hold office until our annual meeting of shareholders to be held in 2016. Our Class II director, Itzhak Danziger, will hold office until our annual meeting of shareholders to be held in 2014. Our Class III directors, Yigal Jacoby and Rami Hadar, will hold office until our annual meeting of shareholders to be held in 2015. The directors (other than the outside directors) are elected by a vote of the holders of a majority of the voting power present and voting at the meeting. Each director will hold office until the annual general meeting of our shareholders for the year in which his or her term expires and until his or her successor is duly elected and qualified, unless the tenure of such director expires earlier pursuant to the Companies Law or unless he or she resigns or is removed from office.

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Under the Companies Law, a director (including an outside director) must declare in writing that he or she has the required skills and the ability to dedicate the time required to serve as a director in addition to other statutory requirements. A director who ceases to meet the statutory requirements for his or her appointment must immediately notify us of the same and his or her office will become vacated upon such notice.

Under our articles of association the approval of a special majority of the holders of at least 75% of the voting rights present and voting at a general meeting is generally required to remove any of our directors (other than the outside directors) from office. The holders of a majority of the voting power present and voting at a meeting may elect directors in their stead or fill any vacancy, however created, in our board of directors. In addition, vacancies on our board of directors, other than a vacancy in the office of an outside director, may be filled by a vote of a simple majority of the directors then in office. A director so chosen or appointed will hold office until the next annual general meeting of our shareholders, unless earlier removed by the vote of a majority of the directors then in office prior to such annual meeting. See "—Outside Directors" for a description of the procedure for election of outside directors.

Outside Directors

Qualifications of Outside Directors

The Companies Law requires companies incorporated under the laws of the State of Israel with shares listed on a stock exchange, including the NASDAQ Global Market, to appoint at least two outside directors. Our outside directors are Ms. Benjamini, Mr. Levy and Mr. Baharav. Ms. Benjamini also serves as the lead independent director.

Outside directors are required to meet standards of independence and qualifications set forth in the Companies Law and related regulations. Among other independence qualifications, a person may not serve as an outside director if he is a relative of a controlling shareholder of a company, or if he or his affiliate (as defined in the Companies Law) has an employment, business or professional relationship or other affiliation (as defined in the Companies Law) with us.

In addition, the Companies Law requires every outside director appointed to the board of directors of an Israeli company to qualify as a "financial and accounting expert" or as "professionally competent," as such terms are defined in the applicable regulations under the Companies Law, and at least one outside director must qualify as a "financial and accounting expert." If at least one of our directors meets the independence requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and the standards of the NASDAQ Stock Market rules for membership on the audit committee and also has financial and accounting expertise as defined in the Companies Law, then the other outside directors are only required to meet the professional qualifications requirement. Under applicable regulations, a director with financial and accounting expertise is a director who, through his or her education, professional experience and skill, has a high level of proficiency in and understanding of business accounting matters and financial statements. He or she must be able to thoroughly comprehend the financial statements of the company and initiate debate regarding the manner in which financial information is presented.

Election of Outside Directors

Outside directors are elected by a majority vote at a shareholders' meeting, provided that either:

- the majority of shares voted at the meeting, including at least a majority of the shares of non-controlling shareholder(s) and shareholders who do not have a personal interest in the election of the outside director (other than a personal interest that does not result from the shareholder's relationship with a controlling shareholder), voted at the meeting, excluding abstentions, vote in favor of the election of the outside director; or

- the total number of shares of non-controlling shareholders and shareholders who do not have a personal interest in the election of the outside director (excluding a personal interest that does not result from the shareholder's relationship with a controlling shareholder) voted against the election of the outside director does not exceed two percent of the aggregate voting rights in the company.

The initial term of an outside director is three years, and he or she may be reelected to up to two additional terms of three years each at a shareholders' meeting, subject to the voting threshold set forth above. Thereafter, an outside director may be reelected for additional periods of up to three years each, only if the company's audit committee and board of directors confirm that, in light of the outside director's expertise and special contribution to the work of the board of directors and its committees, the reelection for such additional period is beneficial to the company. Outside directors may be removed by the same voting threshold as is required for their election, or by a court, and only if the outside directors cease to meet the statutory qualifications for their appointment or if they violate their duty of loyalty to the company. The tenure of outside directors, like all directors, may also be terminated by a court under limited circumstances. If the vacancy of an outside director position causes the company to have fewer than two outside directors, a company's board of directors is required under the Companies Law to call a special general meeting of the company's shareholders as soon as possible to appoint a new outside director. Each committee of a company's board of directors which is authorized to exercise the board of directors' authorities is required to include at least one outside director, except for the audit committee and the compensation committee, which are required to include all outside directors.

An outside director is entitled to compensation and reimbursement of expenses as provided in regulations promulgated under the Companies Law, and is otherwise prohibited from receiving any other compensation, directly or indirectly, in connection with services provided as an outside director, other than indemnification, exculpation and insurance as permitted pursuant to the Companies Law.

NASDAQ Requirements

Under the NASDAQ Stock Market rules, a majority of directors must meet the independence requirements specified in those rules. Our board of directors consists of seven members, four of whom are independent under the NASDAQ Stock Market rules. Specifically, our board has determined that Ms. Nurit Benjamini, Mr. Dov Baharav, Mr. Yigal Jacoby and Mr. Steven Levy meet the independence standards of the NASDAQ Stock Market rules. In reaching this conclusion, the board determined that none of these directors have a relationship that would preclude a finding of independence and that the other relationships that these directors have with us do not impair their independence. As stated above under "– Corporate Governance Practices,". See "ITEM 16G. Corporate Governance" for additional information.

Audit Committee

Companies Law Requirements

Under the Companies Law, the board of directors of any public company must appoint an audit committee comprised of at least three directors, including all of the outside directors. The following persons may not be appointed as members of the audit committee:

- the chairperson of the board of directors;

- a controlling shareholder or a relative of a controlling shareholder (as defined in the Companies Law); or

- any director who is engaged by, or provides services on a regular basis to the company, the company's controlling shareholder or an entity controlled by a controlling shareholder or any director who generally relies on a controlling shareholder for his or her livelihood.

The Companies Law requires the majority of the audit committee members to be independent directors (as defined in the Companies Law), and the chairman of the audit committee is required to be an outside director. Any person disqualified from serving as a member of the audit committee may not be present at the audit committee meetings, unless the chairperson of the audit committee has determined that this person is required to be present for a particular matter. The Companies Law provides for certain other exclusions to this provision.

NASDAQ Requirements

Under the NASDAQ Stock Market rules, companies are required to maintain an audit committee consisting of at least three independent directors, all of whom are financially literate and one of whom has accounting or related financial management expertise. Our audit committee members are required to meet additional independence standards, including minimum standards set forth in rules of the SEC and adopted by the NASDAQ Stock Market.

Approval of Transactions with Related Parties

The approval of the audit committee is required to effect specified actions and transactions with office holders and controlling shareholders. The term "office holder" means a general manager, chief business manager, deputy general manager, vice general manager, or any other person assuming the responsibilities of any of the foregoing positions, without regard to such person's title, as well as any director or manager directly subordinate to the general manager. The term "controlling shareholder" means a shareholder with the ability to direct the activities of the company, other than by virtue of being an office holder. A shareholder is presumed to be a controlling shareholder if the shareholder holds 50% or more of the voting rights in a company or has the right to appoint the majority of the directors of the company or its general manager. For the purpose of approving transactions with controlling shareholders, the term also includes any shareholder that holds 25% or more of the voting rights of the company, if the company has no shareholder that owns more than 50% of its voting rights. For purposes of determining the holding percentage stated above, two or more shareholders who have a personal interest in a transaction that is brought for the company's approval are deemed as joint holders. The audit committee may not approve an action or a transaction with a controlling shareholder or with an office holder unless all the requirements of the Companies Law regarding the structure of the committee and the persons entitled to be present at meetings are met at the time of approval.

Audit Committee Role

Our board of directors has adopted an audit committee charter setting forth the responsibilities of the audit committee consistent with the rules of the SEC and the NASDAQ Global Market, which include:

- retaining and terminating the company's independent auditors, subject to shareholder ratification;

- pre-approval of audit and non-audit services provided by the independent auditors; and

- approval of transactions with office holders and controlling shareholders, as described above, and other related-party transactions.

Additionally, under the Companies Law, the audit committee is responsible for: (a) identifying deficiencies in the management of a company's business and making recommendations to the board of directors as to how to correct them; (b) reviewing and deciding whether to approve certain related party transactions and certain transactions involving conflicts of interest; (c) deciding whether certain actions involving conflicts of interest are material actions and whether certain related party transactions are extraordinary transactions; (d) reviewing the internal auditor's work program; (e) examining the company's internal control structure and processes, the performance of the internal auditor and whether the internal auditor has the tools and resources required to perform his or her duties; and (f) examining the independent auditor's scope of work as well as the independent auditor's fees, and providing the corporate body responsible for determining the independent auditor's fees with its recommendations. In addition the audit committee is also be responsible for implementing procedures concerning employee complaints on improprieties in the administration of the company's business and the protection to be provided to such employees. Furthermore, in accordance with regulations promulgated under the Companies Law, the audit committee discusses the draft financial statements and presents to the board its recommendations with respect to the draft financial statements. The audit committee charter states that in fulfilling this role the committee is entitled to rely on interviews and consultations with our management, our internal auditor and our independent auditor, and is not obligated to conduct any independent investigation or verification.

Our audit committee consists of Ms. Nurit Benjamini, Mr. Steven Levy and Mr. Dov Baharav. The financial experts on the audit committee pursuant to the definition of the SEC are all members of the audit committee.

Compensation and Nominating Committee

Under the Companies Law, the compensation committee of a public company must consist of at least three directors who satisfy certain independence qualifications, including the additional independence requirements of the NASDAQ Stock Market rules applicable to the members of compensation committees, and the chairman of the compensation committee is required to be an outside director. We have established a compensation and nominating committee which currently consists of Ms. Nurit Benjamini, Mr. Steven Levy, and Mr. Dov Baharav. The chairperson is Mr. Levy. This committee oversees matters related to our compensation policy and practices. Our board of directors has adopted a compensation and nominating committee charter setting forth the responsibilities of the committee consistent with the Companies Law and the NASDAQ Stock Market rules, which include:

- approving, and recommending to the board of directors and the shareholders for their approval, the compensation of our Chief Executive Officer and other executive officers;
- granting options to our employees and the employees of our subsidiaries;
- recommending candidates for nomination as members of our board of directors; and
- developing and recommending to the board corporate governance guidelines and a code of business ethics and conduct in accordance with applicable laws.

The compensation committee is also authorized to retain and terminate compensation consultants, legal counsel or other advisors to the committee and to approve the engagement of any such consultant, counsel or advisor, to the extent it deems necessary or appropriate after specifically analyzing the independence of any such consultant retained by the committee.

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On specified criteria, to review modifications to the compensation policy from time to time, to review its implementation and to approve the actual compensation terms of office holders prior to approval by the board of directors.

Internal Auditor

Under the Companies Law, the board of directors of a public company must appoint an internal auditor nominated by the audit committee. The role of the internal auditor is, among other things, to examine whether a company's actions comply with applicable law and orderly business procedure. The internal auditor may be an employee of the company but not an interested party (as defined in the Companies Law), an office holder of the company, or a relative of an interested party or an office holder, among other restrictions. The firm of Deloitte Brightman Almagor Zohar is the internal auditor of the Company.

Exculpation, Insurance and Indemnification of Office Holders

Under the Companies Law, a company may not exculpate an office holder from liability for a breach of the duty of loyalty. However, a company may provide certain indemnification rights as detailed below and obtain insurance for an act performed in breach of the duty of loyalty of an office holder provided that the office holder acted in good faith, the act or its approval does not harm the company, and the office holder discloses the nature of his or her personal interest in the act and all material facts and documents a reasonable time before discussion of the approval. Our articles of association, in accordance with Israeli law, allow us to exculpate an office holder, in advance, from liability to us, in whole or in part, for damages caused to us as a result of a breach of duty of care. We may not exculpate a director for liability arising out of a prohibited dividend or distribution to shareholders or prohibited purchase of its securities.

In accordance with Israeli law, our articles of association allow us to indemnify an office holder in respect of certain liabilities either in advance of an event or following an event. Under Israeli law, an undertaking provided in advance by an Israeli company to indemnify an office holder with respect to a financial liability imposed on him or her in favor of another person pursuant to a judgment, settlement or arbitrator's award approved by a court must be limited to events which in the opinion of the board of directors can be foreseen based on the company's activities when the undertaking to indemnify is given, and to an amount or according to criteria determined by the board of directors as reasonable under the circumstances, and such undertaking must detail the above mentioned events and amount or criteria. Our articles of association allow us to undertake in advance to indemnify an office holder for, among other costs, reasonable litigation expenses, including attorneys' fees, and certain financial liabilities and obligations, subject to certain restrictions pursuant to the Companies Law.

In accordance with Israeli law, our articles of association allow us to insure an office holder against certain liabilities incurred for acts performed as an office holder, including certain breaches of duty of loyalty to the company, a breach of duty of care to the company or to another person and certain financial liabilities and obligations imposed on the office holder.

We may not indemnify or insure an office holder against any of the following:

- a breach of duty of loyalty, except to the extent that the office holder acted in good faith and had a reasonable basis to believe that the act would not prejudice the company;

- a breach of duty of care committed intentionally or recklessly, excluding a breach arising out of the negligent conduct of the office holder;

- an act or omission committed with intent to derive illegal personal benefit; or

- a fine, civil fine, monetary sanction or forfeit levied against the office holder.

Under the Companies Law, exculpation, indemnification and insurance of office holders must be approved by our compensation committee and our board of directors and, in respect of our directors, the chief executive officer, and any employee or service provider who is considered a controlling shareholder, by our shareholders, provided that changes to existing arrangements may be approved by the audit committee if it approves that such changes are immaterial.

As of the date of this annual report, there are no claims for directors' and officers' liability insurance have been filed under our policies and we are not aware of any pending or threatened litigation or proceeding involving any of our directors or officers in which indemnification is sought.

We have entered into agreements with each of our directors and with certain of our office holders exculpating them, to the fullest extent permitted by law, from liability to us for damages caused to us as a result of a breach of duty of care, and undertaking to indemnify them to the fullest extent permitted by law. This indemnification is limited to events determined as foreseeable by the board of directors based on our activities, and to an amount or according to criteria determined by the board of directors as reasonable under the circumstances, and the insurance is subject to our discretion depending on its availability, effectiveness and cost. The current maximum amount set forth in such agreements is the greater of (1) with respect to indemnification in connection with a public offering of our securities, the gross proceeds raised by us and/or any selling shareholder in such public offering, and (2) with respect to all permitted indemnification, including a public offering of our securities, an amount equal to 50% of the our shareholders' equity on a consolidated basis, based on our most recent financial statements made publicly available before the date on which the indemnity payment is made.

In the opinion of the SEC, indemnification of directors and office holders for liabilities arising under the Securities Act is against public policy and therefore unenforceable.

D. Employees

As of December 31, 2013, we had 430 employees of whom 302 were based in Israel, 66 in the United States and the remainder in Europe, Asia and Oceania. The breakdown of our employees by department is as follows:

	December 31,		
Department	2011	2012	2013
Manufacturing and operations	19	18	16
Research and development	117	178	172
Sales, marketing, service and support	153	199	199
Management and administration	35	47	44
Total	324	442	430

Under applicable Israeli law, we and our employees are subject to protective labor provisions such as restrictions on working hours, minimum wages, minimum vacation, sick pay, severance pay and advance notice of termination of employment as well as equal opportunity and anti-discrimination laws. Orders issued by the Israeli Ministry of Economy make certain industry-wide collective bargaining agreements applicable to us. These agreements affect matters such as cost of living adjustments to salaries, length of working hours and week, recuperation, travel expenses, and pension rights. Our employees are not represented by a labor union. We provide our employees with benefits and working conditions which we believe are competitive with benefits and working conditions provided by similar companies in Israel. We have never experienced labor-related work stoppages and believe that our relations with our employees are good.

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E. Share Ownership

Beneficial Ownership of Executive Officers and Directors

The following table sets forth certain information regarding the beneficial ownership of our ordinary shares as of March 6, 2014 by (i) each of our directors and nominees, (ii) each of our executive officers and (iii) all of our executive officers and directors serving as of March 6, 2014, as a group. Unless otherwise stated, the address of each named executive officer and director is c/o Allot Communications Ltd., 22 Hanagar Street, Neve Ne'eman Industrial Zone B, Hod-Hasharon 4501317, Israel.

Name of Beneficial Owner	Number of Shares Beneficially Held(1)	Percent of Class
Directors		
Itzhak Danziger	*	*
Nurit Benjamini	*	*
Rami Hadar	*	*
Shraga Katz	*	*
Steven D. Levy	*	*
Yigal Jacoby	*	*
Dov Baharav	*	*
Executive Officers		
Amir Hochbaum	*	*
Anat Shenig	*	*
Andrei Elefant	*	*
Gary Drutin	*	*
Itamar Rosen	*	*
Jay Klein	*	*
Lior Moyal	*	*
Nachum Falek	*	*
Pini Gvili	*	*
Ramy Moriah	*	*
Vin Costello	*	*
All directors and executive officers as a group (18 persons)	635,242	1.89 %

* Less than one percent of the outstanding ordinary shares.

(1) As used in this table, "beneficial ownership" is determined in accordance with the rules of the SEC and consists of either or both voting or investment power with respect to securities. For purposes of this table, a person is deemed to be the beneficial owner of securities that can be acquired within 60 days from March 6, 2014 through the exercise of any option or warrant. Ordinary shares subject to options or warrants that are currently exercisable or exercisable within 60 days are deemed outstanding for computing the ownership percentage of the person holding such options or warrants, but are not deemed outstanding for the purpose of computing the ownership percentage of any other person. Except as otherwise indicated, the persons named in the table have reported that they have sole voting and sole investment power with respect to all shares of common stock shown as beneficially owned by them. The amounts and percentages are based upon 33,001,100 ordinary shares outstanding as of March 6, 2014 pursuant to Rule 13d-3(d)(1)(i) under the Exchange Act.

Our directors and executive officers hold, in the aggregate, outstanding options exercisable for 1,113,431 ordinary shares, as of March 6, 2014. These options have a weighted average exercise price of $9.84 per share and have expiration dates until 2024.

Share Option Plans

We have adopted four share option plans and, as of March 6, 2014, we had 2,799,950 ordinary shares outstanding and 715,457 remained available for future options or other awards.

Total shares outstanding as of March 6, 2014 totaled 33,001,100. Under our share option plans, as of March 6, 2014 options to purchase 2,799,950 ordinary shares at a weighted average exercise price of $10.76 per share were outstanding of which options to purchase 1,327,802 ordinary shares were vested and exercisable.

We will only grant options or other equity incentive awards under the 2006 Incentive Compensation Plan, although previously-granted options will continue to be governed by our other plans.

2006 Incentive Compensation Plan

The 2006 plan is intended to further our success by increasing the ownership interest of certain of our and our subsidiaries' employees, directors and consultants and to enhance our and our subsidiaries' ability to attract and retain employees, directors and consultants.

The number of ordinary shares that we may issue under the 2006 plan will increase on the first day of each fiscal year during the term of the 2006 plan, in each case in an amount equal to the lesser of (i) 1,000,000 shares, (ii) 3.5% of our outstanding ordinary shares on the last day of the immediately preceding year, or (iii) an amount determined by our board of directors. The number of shares subject to the 2006 plan is also subject to adjustment if particular capital changes affect our share capital. Ordinary shares subject to outstanding awards under the 2006 plan or our 2003 plan or 1997 plans that are subsequently forfeited or terminated for any other reason before being exercised will again be available for grant under the 2006 plan. As of March 6, 2014, options or other awards to purchase 2,796,269 ordinary shares were outstanding under the 2006 plan and 638,190 remained available for future options or other awards.

Israeli participants in the 2006 plan may be granted options and/or restricted stock units subject to Section 102 of the Israeli Income Tax Ordinance. Section 102 of the Israeli Income Tax Ordinance, allows employees, directors and officers, who are not controlling shareholders and are considered Israeli residents to receive favorable tax treatment for compensation in the form of shares or options. Our non-employees service providers and controlling shareholders may only be granted options under another section of the Tax Ordinance, which does not provide for similar tax benefits. Section 102 includes two alternatives for tax treatment involving the issuance of options or shares to a trustee for the benefit of the grantees and also includes an additional alternative for the issuance of options or shares directly to the grantee. The most favorable tax treatment for the grantees is under Section 102(b)(2) of the Tax Ordinance, the issuance to a trustee under the "capital gain track." However, under this track we are not allowed to deduct an expense with respect to the issuance of the options or shares. Any stock options granted under the 2006 plan to participants in the United States will be either "incentive stock options," which may be eligible for special tax treatment under the U.S. Internal Revenue Code of 1986, or options other than incentive stock options (referred to as "nonqualified stock options"), as determined by our compensation and nominating committee and stated in the option agreement.

Our compensation and nominating committee administers the 2006 plan and it selects which of our and our subsidiaries' and affiliates' eligible employees, directors and/or consultants receive options or other awards under the 2006 plan and will determine the terms of the grant, including, exercise prices, method of payment, vesting schedules, acceleration of vesting and the other matters necessary in the administration of the plan.

If we undergo a change of control, as defined in the 2006 plan, subject to any contrary law or rule, or the terms of any award agreement in effect before the change of control, (a) the compensation and nominating committee may, in its discretion, accelerate the vesting, exercisability and payment, as applicable, of outstanding options and other awards;

and (b) the compensation and nominating committee, in its discretion, may adjust outstanding awards by substituting ordinary shares or other securities of any successor or another party to the change of control transaction, or cash out outstanding options and other awards, in any such case, generally based on the consideration received by our shareholders in the transaction.

Allot Communications Ltd. Key Employee Share Incentive Plan (2003)

Our 2003 share option plan provides for the grant of options to our and our affiliates' employees, directors, officers, consultants, advisers and service providers. As of March 6, 2014, there were outstanding options to purchase 3,681 ordinary shares under the plan, all of which were vested and exercisable. We no longer grant options under this plan, and ordinary shares underlying any option granted under this plan that terminates without exercise become available for future issuance under our 2006 plan.

The terms of the 2003 plan are in compliance with Section 102 of the Israeli Income Tax Ordinance, which allows employees, directors and officers, who are not controlling shareholders and are considered Israeli residents to receive favorable tax treatment for compensation in the form of shares or options. Our non-employees service providers and controlling shareholders may only be granted options under another section of the Tax Ordinance, which does not provide for similar tax benefits.

We have elected to issue our options under the capital gain track and, accordingly, all options granted under this plan to Israeli residents have been granted under the capital gain track. Section 102 also provides for an income tax track, under which, among other things, the benefits to the employees would be taxed as ordinary income, we would be allowed to recognize expenses for tax purposes and the minimum holding period for the trustee will be twelve months from the end of the calendar year in which such options are granted, and if granted after January 1, 2006, twelve months after the date of grant. In order to comply with the terms of the capital gain track, all options, as well as the ordinary shares issued upon exercise of these options and other shares received subsequently following any realization of rights with respect to such options, such as stock dividends and stock splits are granted to a trustee and should be held by the trustee for the lesser of thirty months from the date of grant, or two years following the end of the tax year in which the options were granted and if granted after January 1, 2006 only two years after the date of grant. Under this plan, all options, whether or not granted pursuant to said Section 102, the ordinary shares issued upon their exercise and other shares received subsequently following any realization of rights are issued to a trustee.

The plan is administered by our board of directors which has delegated certain responsibilities to our compensation and nomination committee.

In the event of our being acquired by means of merger with or into another entity, in which our outstanding shares are exchanged for securities or other consideration issued, or caused to be issued, by the acquiring company or its subsidiary, or in the event of the sale of all or substantially all of our assets, to the extent it has not been previously exercised, each vested or unvested option will terminate immediately prior to the consummation of such transaction. The plan further provides that, in the event of our consolidation or merger with or into another corporation, the compensation committee may, in its absolute discretion and without obligation, agree that instead of termination: (i) each unexercised option, if possible, will be assumed or an equivalent option will be substituted by our successor corporation or a parent or subsidiary of our successor corporation; or (ii) we will pay to the grantee an amount equivalent to the valuation of the grantee's unexercised options on an as converted basis at that time.

The plans are administered by our compensation and nominating committee.

We no longer grant options under the 2003 plan, and ordinary shares underlying any options granted under the 2009 plan that terminated without exercise became available for issuance under our 2006 plan.

ITEM 7: Major Shareholders and Related Party Transactions

A. Major Shareholders

The following table sets forth certain information regarding the beneficial ownership of our outstanding ordinary shares as of March 6, 2014, by each person who we know beneficially owns 5.0% or more of the outstanding ordinary shares. Each of our shareholders has identical voting rights with respect to its shares. All of the information with respect to beneficial ownership of the ordinary shares is given to the best of our knowledge.

	Ordinary Shares Beneficially Owned(1)	Percentage of Ordinary Shares Beneficially Owned	
FMR LLC (2)	3,250,691	9.9	%
Zohar Zisapel (3)	2,842,378	8.6	%
T. Rowe Price Associates, Inc (4)	2,786,740	8.4	%
Migdal Insurance & Financial holdings Ltd (5)	2,616,542	7.9	%
Psagot Investment Ltd (6)	1,876,791	5.7	%

(1) As used in this table, “beneficial ownership” means the sole or shared power to vote or direct the voting or to dispose or direct the disposition of any security. For purposes of this table, a person is deemed to be the beneficial owner of securities that can be acquired within 60 days from March 6, 2014 through the exercise of any option or warrant. Ordinary shares subject to options or warrants that are currently exercisable or exercisable within 60 days are deemed outstanding for computing the ownership percentage of the person holding such options or warrants, but are not deemed outstanding for computing the ownership percentage of any other person. The amounts and percentages are based upon 33,001,100 ordinary shares outstanding as of March 6, 2014.

(2) Based on a Schedule 13G/A filed on February 14, 2013. Includes 2,920,191 shares beneficially owned by Fidelity Management & Research Company, a wholly-owned subsidiary of FMR LLC, of which Edward C. Johnson 3d and FMR LLC, through its control of Fidelity Management & Research Company, and the funds each has sole dispositive power; Edward C. Johnson 3d and FMR LLC, through its control of Pyramis Global Advisors, LLC , each has sole dispositive power and sole voting power over 11,900 shares; and Edward C. Johnson 3d and FMR LLC, through its control of Pyramis Global Advisors Trust Company each has sole dispositive power and sole voting power over 318,600 shares. The address of the FMR entities is 82 Devonshire St., Boston MA 02109.

(3) Based on a Schedule 13G/A filed on January 13, 2011. Consists of 2,777,487 shares held by Zohar Zisapel and 64,891 shares held by Lomsha Ltd., an Israeli company controlled by Zohar Zisapel. The address of Mr. Zisapel and Lomsha Ltd. is 24 Raoul Wallenberg Street, Tel Aviv 69719, Israel.

(4) Based on a Schedule 13G/A filed on February 13, 2014. Of these shares, T. Rowe Price Associate reported that it held sole voting power over 613,300 and sole dispositive power over 2,786,740 shares. The address of T. Rowe Price Associates Inc is 100 E. Prat Street, Baltimore, Maryland 21202.

(5) Based on a Schedule 13G/A filed on February 13, 2014.Midgal Insurance & Financial Holdings Ltd reported that it held shared voting power and shared dispositive power over these shares. Of these shares, 2,553,131 shares are held for members of the public through, among others, provident funds, mutual funds, pension funds and insurance policies, which are managed by subsidiaries of Midgal Insurance & Financial Holdings Ltd, according to the following segmentation: 1,465,149 shares are held by Profit participating life assurance accounts; 991,940 shares are held by Provident funds and companies that manage provident funds and 96,042 shares are held by

companies for the management of funds for joint investments in trusteeship, each of which subsidiaries operates under independent management and makes independent voting and investment decisions. The address of the reporting person is 4 Efal Street; P.O BOX 3063; Petach Tikva 49512, Israel.

(6) Based on a Schedule 13G filed on February 19, 2014. Psagot Investment House Ltd. reported that it held shared voting power and shared dispositive power over these shares. Consists of 699,295 shares beneficially owned by Psagot Securities Ltd; 327,646 shares beneficially owned by Psagot Provident Funds and Pension Ltd; 34,194 shares beneficially owned by Psagot Mutual Funds Ltd (of this amount, 8,508 shares may also be considered beneficially owned by Psagot Securities Ltd., but are not included in the shares beneficially owned by Psagot Securities Ltd., as indicated above); and 815,656 shares beneficially owned by Psagot Exchange Traded Notes Ltd. The address of the Psagot entities is Psagot Investment House Ltd. – 14 Ahad Ha'am Street, Tel Aviv 65142, Israel.

Significant Changes in the Ownership of Major Shareholders

As of March 6, 2014, FMR LLC was the beneficial owner of 3,250,691, or 9.9%, of our ordinary shares. Its beneficial ownership did not change compared to the amounts reported in our 2012 Annual Report. As of August 31, 2012, FMR LLC was the beneficial owner of 4,032,891, or 12.6%, of our ordinary shares, as reported in FMR LLC's Schedule 13G filed on September 10, 2012.

As of March 6, 2014, Alydar Group was no longer a major shareholder. As of March 8, 2013, Alydar Group was the beneficial owner of 1,708,860, or 5.3%, of our ordinary shares, as reported in our 2012 Annual Report.

As of March 6, 2014, Zohar Zisapel was the beneficial owner of 2,842,378, or 8.6%, of our ordinary shares. Its beneficial ownership did not change since December 31, 2010.

As of March 6, 2014, Turner Investments was no longer a major shareholder. As of March 8, 2013, Turner Investments was the beneficial owner of 1,661,239, or 5.0%, of our ordinary shares, as reported in our 2012 Annual Report.

As of March 6, 2014, T. Rowe Price Associates, Inc. was the beneficial owner of 2,786,740, or 8.4%, of our ordinary shares. As of May 31, 2013, T. Rowe Price Associates, Inc. was the beneficial owner of 3,280,510, or 10.0%, of our ordinary shares as reported in T. Rowe Price Associates, Inc.'s Schedule 13G filed on June 10, 2013.

As of March 6, 2014, Migdal Insurance & Financial Holdings Ltd was the beneficial owner of 2,616,542, or 7.9%, of our ordinary shares. As of April 12, 2013, Migdal Insurance & Financial Holdings Ltd was the beneficial owners of 1,662,268, or 5.1%, of our ordinary shares as reported in Midgal Insurance & Financial Holdings Ltd filed on May 21, 2013.

As of March 6, 2014, Psagot Investment House Ltd was the beneficial owner of 1,876,791, or 5.75% of our ordinary shares. As of April 30, 2013, Psagot investment Ltd was the beneficial owner of 1,785,319, or 5.5%, of our ordinary shares as reported in Psagot Investment House Ltd's Schedule 13G filed on May 13, 2013.

Record Holders

Based on a review of the information provided to us by our transfer agent, as of March 1, 2014, there were 18 record holders of ordinary shares, of which 9 consisted of United States record holders holding approximately 99.40% of our outstanding ordinary shares. The United States record holders included Cede & Co., the nominee of the Depositary Trust Company.

B. Related Party Transactions

Our policy is to enter into transactions with related parties on terms that, on the whole, are no less favorable, than those available from unaffiliated third parties. Based on our experience in the business sectors in which we operate and the terms of our transactions with unaffiliated third parties, we believe that all of the transactions described below met this policy standard at the time they occurred.

Agreements with Directors and Officers

Engagement of Officers. We have entered into employment or consulting agreements with each of our officers, who work for us as employees or as consultants. These agreements all contain provisions standard for a company in our industry regarding noncompetition, confidentiality of information and assignment of inventions. The enforceability of covenants not to compete in Israel may be limited. In connection with the engagement of our officers, we have granted them options pursuant to our 2006 Incentive Compensation Plan.

Exculpation, Indemnification and Insurance. Our articles of association permit us to exculpate, indemnify and insure our office holders, in accordance with the provisions of the Companies Law. We have entered into agreements with each of our directors and certain office holders, exculpating them from a breach of their duty of care to us to the fullest extent permitted by law and undertaking to indemnify them to the fullest extent permitted by law, to the extent that these liabilities are not covered by insurance. See "ITEM 6: Directors, Senior Management and Employees—Board Practices—Exculpation, Insurance and Indemnification of Office Holders."

Agreement with Galil Software

Our director, Itzhak Danziger, is Chairman of the board of directors of Galil Software Ltd. We have engaged Galil Software since 2010 to provide us with certain quality assurance services in the ordinary course of our business. We paid Galil Software approximately $305,000 in 2012, approximately $302,000 in 2013 and approximately $13,000 in 2013 through March 6, 2014.

C. Interests of Experts and CounselNot applicable.

ITEM 8: Financial Information

A. Consolidated Financial Statements and Other Financial Information.

Consolidated Financial Statements

For our audited consolidated financial statements for the year ended December 31, 2012, please see pages F-2 to F-45 of this report.

Export Sales

See "ITEM 5: Operating and Financial Review and Prospects" under the caption "Geographic Breakdown of Revenues" for certain details of export sales for the last three fiscal years.

Legal Proceedings

We may, from time to time in the future be involved in legal proceedings in the ordinary course of business.

Dividends

We have never declared or paid any cash dividends on our ordinary shares and we do not anticipate paying any cash dividends on our ordinary shares in the future. We currently intend to retain all future earnings to finance our operations and to expand our business. Any future determination relating to our dividend policy will be made at the discretion of our board of directors and will depend on a number of factors, including future earnings, capital requirements, financial condition and future prospects and other factors our board of directors may deem relevant.

B. Significant Changes

Since the date of our audited financial statements included elsewhere in this annual report, there have not been any significant changes in our financial position.

ITEM 9: The Offer and Listing

Not applicable, except for Items 9.A.4 and 9.C, which are detailed below.

Stock Price History

Our ordinary shares have been trading on the NASDAQ Global Select Market under the symbol “ALLT” since November 2006. The following table sets forth the high and low sales prices for our ordinary shares as reported by the NASDAQ Global Market, in U.S. dollars, for 2013 and 2013, each quarter in the 2013 and 2012 and the most recent six months prior to the filing of this annual report as reported by the Tel Aviv Stock Exchange (since December 2010), in NIS, for each of the last five years:

	NASDAQ Global Market		Tel Aviv Stock Exchange	
Year	High	Low	High	Low
2010	$ 11.64	$ 4.00	NIS 42.57	NIS 37.20
2011	19.05	9.45	71.22	35.74
2012	28.03	15.55	111.60	58.56
2013	18.28	11.01	68.12	39.2
2014 (through March 6, 2014)	17.06	14.93	62.96	52.01

	NASDAQ Global Market		Tel Aviv Stock Exchange	
2012	High	Low	High	Low
First Quarter	$ 23.25	$ 15.55	NIS 86.17	NIS 58.56
Second Quarter	28.03	21.87	110.00	83.07
Third Quarter	27.82	21.32	111.60	88.58
Fourth Quarter	25.50	17.12	99.72	63.60

	NASDAQ Global Market		Tel Aviv Stock Exchange	
2013	High	Low	High	Low
First Quarter	$ 18.28	$ 11.94	NIS 68.12	NIS 45.19
Second Quarter	13.79	11.01	50.14	39.20
Third Quarter	15.55	12.02	54.86	42.86
Fourth Quarter	15.13	12.63	53.18	45.04

	NASDAQ Global Market		Tel Aviv Stock Exchange	
Most Recent Six Months	High	Low	High	Low
March 2014 (through March 6, 2014)	$ 16.51	$ 16.29	NIS 58.22	NIS 57.13
February 2014	17.13	15.78	60.28	54.54
January 2014	17.06	14.93	62.96	52.01
December 2013	15.13	13.02	53.18	45.89
November 2013	13.77	12.71	48.17	45.08
October 2013	14.35	12.63	50.43	45.04

Markets

Our ordinary shares have been quoted under the symbol “ALLT” on the NASDAQ Stock Market since November 16, 2006 and on the Tel Aviv Stock Exchange since December 21, 2010.

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ITEM 10: Additional Information

A. Share Capital

Not applicable.

B. Memorandum and Articles of Association

Memorandum and Articles of Association Incorporation

We are registered as a public company with the Israeli Registrar of Companies. Our registration number is 51-239477-6.

Objective

Our objectives under our memorandum of association are to engage in the business of computers, hardware and software, including without limitation research and development, marketing, consulting and the selling of knowledge, and any other activity which our board of directors shall determine.

Ordinary Shares

Our authorized share capital consists of 200,000,000 ordinary shares, par value NIS 0.10 per share. As of March 6, 2014, we had 33,001,100 ordinary shares outstanding. All outstanding ordinary shares are validly issued, fully paid and non-assessable. The rights attached to the Ordinary Shares are as follows:

Voting

Holders of our ordinary shares have one vote for each ordinary share held on all matters submitted to a vote of shareholders at a shareholder meeting. Shareholders may vote at shareholder meeting either in person, by proxy or by written ballot. Shareholder voting rights may be affected by the grant of any special voting rights to the holders of a class of shares with preferential rights that may be authorized in the future.

Transfer of Shares

Fully paid ordinary shares are issued in registered form and may be freely transferred under our articles of association unless the transfer is restricted or prohibited by another instrument, Israeli law or the rules of a stock exchange on which the shares are traded.

Election of Directors

Our ordinary shares do not have cumulative voting rights for the election of directors. Rather, under our articles of association our directors are elected by the holders of a simple majority of our ordinary shares at a general shareholder meeting. As a result, the holders of our ordinary shares that represent more than 50% of the voting power represented at a shareholder meeting have the power to elect any or all of our directors whose positions are being filled at that meeting, subject to the special approval requirements for outside directors. See “ITEM 6: Directors, Senior Management and Employees—Board Practices—Outside Directors.”

Dividend and Liquidation Rights

Under the Companies Law, shareholder approval is not required for the declaration of a dividend, unless the company's articles of association provide otherwise. Our articles of association provide that our board of directors may declare and distribute a dividend to be paid to the holders of ordinary shares without shareholder approval in proportion to the paid up capital attributable to the shares that they hold. Dividends may be paid only out of profits legally available for distribution, as defined in the Companies Law, provided that there is no reasonable concern that the payment of a dividend will prevent us from satisfying our existing and foreseeable obligations as they become due. If we do not have profits legally available for distribution, we may seek the approval of the court to distribute a dividend. The court may approve our request if it is convinced that there is no reasonable concern that a payment of a dividend will prevent us from satisfying our existing and foreseeable obligations as they become due.

In the event of our liquidation, after satisfaction of liabilities to creditors, our assets will be distributed to the holders of ordinary shares in proportion to the paid up capital attributable to the shares that they hold. Dividend and liquidation rights may be affected by the grant of preferential dividend or distribution rights to the holders of a class of shares with preferential rights that may be authorized in the future.

Shareholder Meetings

We are required to convene an annual general meeting of our shareholders once every calendar year within a period of not more than 15 months following the preceding annual general meeting. Our board of directors may convene a special general meeting of our shareholders and is required to do so at the request of two directors or one quarter of the members of our board of directors or at the request of one or more holders of 5% or more of our share capital and 1% of our voting power or the holder or holders of 5% or more of our voting power. All shareholder meetings require prior notice of at least 21 days. The chairperson of our board of directors, or any other person appointed by the board of directors, presides over our general meetings. In the absence of the chairperson of the board of directors or such other person, one of the members of the board designated by a majority of the directors presides over the meeting. If no director is designated to preside as chairperson, then the shareholders present will choose one of the shareholders present to be chairperson. Subject to the provisions of the Companies Law and the regulations promulgated thereunder, shareholders entitled to participate and vote at general meetings are the shareholders of record on a date to be decided by the board of directors, which may be between four and 40 days prior to the date of the meeting.

Quorum

The quorum required for a meeting of shareholders consists of at least two shareholders present in person, by proxy or by written ballot, who hold or represent between them at least 25% of our voting power. A meeting adjourned for lack of a quorum generally is adjourned to the same day in the following week at the same time and place or any time and place as the directors designate in a notice to the shareholders. At the reconvened meeting, the required quorum consists of at least two shareholders present, in person, by proxy or by written ballot, who hold or represent between them at least 10% of our voting power, provided that if the meeting was initially called pursuant to a request by our shareholders, then the quorum required must include at least the number of shareholders entitled to call the meeting. See "— Shareholder Meetings."

Resolutions

An ordinary resolution requires approval by the holders of a simple majority of the voting rights represented at the meeting, in person, by proxy or by written ballot, and voting on the resolution.

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Under the Companies Law, unless otherwise provided in the articles of association or applicable law, all resolutions of the shareholders require a simple majority. A resolution for the voluntary winding up of the company requires the approval by holders of at least 75% of the voting rights represented at the meeting, in person, by proxy or by written ballot, and voting on the resolution. Under our articles of association (1) certain shareholders' resolutions require the approval of a special majority of the holders of at least 75% of the voting rights represented at the meeting, in person, by proxy or by written ballot, and voting on the resolution, and (2) certain shareholders' resolutions require the approval of a special majority of the holders of at least two-thirds of the voting securities of the company then outstanding.

Access to Corporate Records

Under the Companies Law, all shareholders generally have the right to review minutes of our general meetings, our shareholder register, including with respect to material shareholders, our articles of association, our financial statements and any document we are required by law to file publicly with the Israeli Companies Registrar. Any shareholder who specifies the purpose of its request may request to review any document in our possession that relates to any action or transaction with a related party which requires shareholder approval under the Companies Law. We may deny a request to review a document if we determine that the request was not made in good faith, that the document contains a commercial secret or a patent or that the document's disclosure may otherwise impair our interests.

Fiduciary duties and approval of specified related party transactions under Israeli law

Fiduciary duties of office holders

The Companies Law imposes a duty of care and a duty of loyalty on all office holders of a company.

The duty of care of an office holder requires an office holder to act with the degree of proficiency with which a reasonable office holder in the same position would have acted under the same circumstances. The duty of care includes, among other things, a duty to use reasonable means, in light of the circumstances, to obtain certain information pertaining to the proposed action before the board of directors.

The duty of loyalty incumbent on an office holder requires him or her to act in good faith and for the benefit of the company, and includes, among other things, the duty to avoid conflicts of interest with the company, to refrain from competing with the company, and to disclose to the company information disclosed to him or her as a result of being an office holder.

We may approve an act specified above which would otherwise constitute a breach of the office holder's duty of loyalty, provided that the office holder acted in good faith, the act or its approval does not harm the company, and the office holder discloses his or her personal interest a sufficient time before the approval of such act. Any such approval is subject to the terms of the Companies Law, setting forth, among other things, the organs of the company entitled to provide such approval, and the methods of obtaining such approval.

Disclosure of personal interests of an office holder and approval of acts and transactions

The Companies Law requires that an office holder promptly disclose to the company any personal interest that he or she may have relating to any existing or proposed transaction by the company (as well as certain information or documents). Once an office holder has disclosed his or her personal interest in a transaction, the approval of the appropriate organ(s) in the company is required in order to effect the transaction. However, a company may approve such a transaction or action only if it is in the best interests of the Company.

Disclosure of personal interests of a controlling shareholder and approval of transactions

Under the Companies Law, a controlling shareholder must also disclose any personal interest it may have in an existing or proposed transaction by the company. Transactions with controlling shareholders that are material, that are not in the ordinary course of business or that are not on market terms require approval by the audit committee, the board of directors and the shareholders of the company, and the Companies Law provides for certain quantitative requirements in respect of the voting of shareholders not having a personal interest in the applicable transaction.

Duties of shareholders

Under the Companies Law, a shareholder has a duty to refrain from abusing its power, to act in good faith and to act in an acceptable manner in exercising its rights and performing its obligations to the company and other shareholders. A shareholder also has a general duty to refrain from acting to the detriment of other shareholders.

In addition, any controlling shareholder or any shareholder having specific power with respect to a company (the power to appoint an office holder, or specific influence over a certain vote) is under a duty to act with fairness towards the company. The Companies Law does not describe the substance of this duty except to state that the remedies generally available upon a breach of contract will also apply in the event of a breach of the duty to act with fairness, taking the shareholder's position in the company into account.

Approval of private placements

Under the Companies Law and the regulations promulgated thereunder, certain private placements of securities may require approval at a general meeting of the shareholders of a company. These include, for example, certain private placements completed in lieu of a special tender offer (See "Memorandum and Articles of Association—Acquisition under Israeli law") or a private placement which qualifies as a related party transaction (See "Corporate governance practices—Fiduciary duties and approval of specified related party transactions under Israeli law").

Acquisitions under Israeli Law

Full Tender Offer. A person wishing to acquire shares of a public Israeli company and who would as a result hold over 90% of the target company's issued and outstanding share capital is required by the Companies Law to make a tender offer for the purchase of all of the issued and outstanding shares of the company. If the shareholders who do not accept the offer hold less than 5% of the issued and outstanding share capital of the company, and more than half of the offerees who do not have a personal interest in the tender offer accept the tender offer, all of the shares that the acquirer offered to purchase will be transferred to the acquirer by operation of law. Notwithstanding the above, if the shareholders who do not accept the offer hold less than 2% of the issued and outstanding share capital of the company or of the applicable class, the offer will nonetheless be accepted. However, a shareholder that had its shares so transferred may, within six months from the date of acceptance of the tender offer, petition the court to determine that the tender offer was for less than fair value and that the fair value should be paid as determined by the court. The bidder may provide in its tender offer that any accepting shareholder may not petition the court for fair value, but such condition will not be valid unless all of the information required under the Companies Law was provided prior to the acceptance date. The description above regarding a full tender offer also applies, with certain limitations, when a full tender offer for the purchase of all of the company's securities is accepted.

Special Tender Offer. The Companies Law provides, subject to certain exceptions, that an acquisition of shares of a public Israeli company must be made by means of a "special tender offer" if, as a result of the acquisition, the purchaser would become a holder of at least 25% of the voting rights in the company. This rule does not apply if there is already another holder of at least 25% of the voting rights in the company. Similarly, the Companies Law provides that an acquisition of shares in a public company must be made by means of a tender offer if, as a result of the acquisition, the purchaser would become a holder of more than 45% of the voting rights in the company, and there is no other shareholder of the company who holds more than 45% of the voting rights in the company. The special tender offer may be consummated subject to certain majority requirements set forth in the Companies Law, and provided further that at least 5% of the voting rights attached to the company's outstanding shares will be acquired by the party making the offer.

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Merger. The Companies Law permits merger transactions between two Israeli companies if approved by each party's board of directors and a certain percentage of each party's shareholders. Following the approval of the board of directors of each of the merging companies, the boards must jointly prepare a merger proposal for submission to the Israeli Registrar of Companies.

Under the Companies Law, if the approval of a general meeting of the shareholders is required, merger transactions may be approved by the holders of a simple majority of our shares present, in person, by proxy or by written ballot, at a general meeting of the shareholders and voting on the transaction. In determining whether the required majority has approved the merger, if shares of the company are held by the other party to the merger, by any person holding at least 25% of the voting rights, or 25% of the means of appointing directors or the general manager of the other party to the merger, then a vote against the merger by holders of the majority of the shares present and voting, excluding shares held by the other party or by such person, or any person or entity acting on behalf of, related to or controlled by either of them, is sufficient to reject the merger transaction. In certain circumstances, a court may still approve the merger upon the request of holders of at least 25% of the voting rights of a company, if the court holds that the merger is fair and reasonable, taking into account the value of the parties to the merger and the consideration offered to the shareholders.

The Companies Law provides for certain requirements and procedures that each of the merging companies is to fulfill. In addition, a merger may not be completed unless at least fifty days have passed from the date that a proposal for approval of the merger was filed with the Israeli Registrar of Companies and thirty days from the date that shareholder approval of both merging companies was obtained.

Anti-Takeover Measures

Undesignated preferred shares. The Companies Law allows us to create and issue shares having rights different from those attached to our ordinary shares, including shares providing certain preferred or additional rights with respect to voting, distributions or other matters and shares having preemptive rights. We do not have any authorized or issued shares other than ordinary shares. In the future, if we do create and issue a class of shares other than ordinary shares, such class of shares, depending on the specific rights that may be attached to them, may delay or prevent a takeover or otherwise prevent our shareholders from realizing a potential premium over the market value of their ordinary shares. The authorization of a new class of shares will require an amendment to our articles of association which requires the prior approval of a simple majority of our shares represented and voted at a general meeting. In addition, we undertook towards the TASE that, as long as our shares are registered for trading with the TASE we will not issue or authorize shares of any class other than the class currently registered with the TASE, unless such issuance is in accordance with certain provisions of the Israeli Securities Law determining that a company registering its shares for trade on the TASE may not have more than one class of shares for a period of one year following registration with the TASE, and following such period the company is permitted to issue preferred shares if the preference of those shares is limited to a preference in the distribution of dividends and the preferred shares have no voting rights.

Supermajority voting. Our articles of association require the approval of the holders of at least two-thirds of our combined voting power to effect certain amendments to our articles of association.

Classified board of directors. Our articles of association provide for a classified board of directors. See "ITEM 6: Directors, Senior Management and Employees—Board Practices—Term of Directors."

Transfer Agent and Registrar

The transfer agent and registrar for our ordinary shares is American Stock Transfer & Trust Company. Its address is 59 Maiden Lane, New York, New York 10038 and its telephone number is (718) 921-8200.

C. Material Contracts

Summaries of the following material contracts and amendments to these contracts are included in this annual report in the places indicated:

Material Contract	Location
Agreement with Flextronics (Israel) Ltd.	"ITEM 4.B: Information on the Company–Business Overview–Manufacturing."

D. Exchange Controls

In 1998, Israeli currency control regulations were liberalized significantly, so that Israeli residents generally may freely deal in foreign currency and foreign assets, and non-residents may freely deal in Israeli currency and Israeli assets. There are currently no Israeli currency control restrictions on remittances of dividends on the ordinary shares or the proceeds from the sale of the shares provided that all taxes were paid or withheld; however, legislation remains in effect pursuant to which currency controls can be imposed by administrative action at any time.

Non-residents of Israel may freely hold and trade our securities. Neither our memorandum of association nor our articles of association nor the laws of the State of Israel restrict in any way the ownership or voting of ordinary shares by non-residents, except that such restrictions may exist with respect to citizens of countries which are in a state of war with Israel. Israeli residents are allowed to purchase our ordinary shares.

E. Taxation

Israeli Tax Considerations and Government Programs

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 ordinary shares in light of their particular circumstances, or certain types of purchasers of our ordinary 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 ordinary 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 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 ordinary shares.

General Corporate Tax Structure in Israel

Israeli companies are generally subject to corporate tax. In 2013 and 2012, the corporate tax rates were25% of their taxable income. The corporate tax rate for 2014 is 26.5%. However, the effective tax rate payable by a company that derives income from an Approved Enterprise, a Preferred Enterprise or a Beneficiary Enterprise (as discussed below) may be considerably less. Capital gains derived by an Israeli company are generally subject to the prevailing corporate tax rate.

Tax Benefits and Grants for Research and Development

Israeli tax law allows, under certain conditions, a tax deduction for expenditures, including capital expenditures, for the year in which they are incurred. Expenditures are deemed related to scientific research and development projects, if:

- The expenditures are approved by the relevant Israeli government ministry, determined by the field of research;
- The research and development must be for the promotion of the company; and
- The research and development is carried out by or on behalf of the company seeking such tax deduction.

The amount of such deductible expenses is reduced by the sum of any funds received through government grants for the finance of such scientific research and development projects. No deduction under these research and development deduction rules is allowed if such deduction is related to an expense invested in an asset depreciable under the general depreciation rules of the income Tax Ordinance, 1961. Expenditures not so approved are deductible in equal amounts over three years.

From time to time we may apply the Office of the Chief Scientist for approval to allow a tax deduction for all research and development expenses during the year incurred. There can be no assurance that such application will be accepted.

Law for the Encouragement of Industry (Taxes), 1969

The Law for the Encouragement of Industry (Taxes), 1969, generally referred to as the Industry Encouragement Law, provides several tax benefits for industrial companies. We believe that we currently qualify as an “Industrial Company” within the meaning of the Industry Encouragement Law. The Industry Encouragement Law defines “Industrial Company” as a company resident in Israel, of which 90% or more of its income in any tax year, other than of income from defense loans, capital gains, interest and dividend, is derived from an “Industrial Enterprise” owned by it. An “Industrial Enterprise” is defined as an enterprise whose major activity in a given tax year is industrial production activity.

The following corporate tax benefits, among others, are available to Industrial Companies:

- Amortization of the cost of purchased know-how and patents and of rights to use a patent and know-how which are used for the development or advancement of the company, over an eight-year period;
- Under specified conditions, an election to file consolidated tax returns with additional related Israeli Industrial Companies; and
- Expenses related to a public offering in Israel and in recognized stock markets outside Israel, are deductible in equal amounts over three years.

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Under certain tax laws and regulations, an "Industrial Enterprise" may be eligible for special depreciation rates for machinery, equipment and buildings. These rates differ based on various factors, including the date the operations begin and the number of work shifts. An "Industrial Company" owning an approved enterprise may choose between these special depreciation rates and the depreciation rates available to the approved enterprise.

Eligibility for the benefits under the Industry Encouragement Law is not subject to receipt of prior approval from any governmental authority. We can give no assurance that we qualify or will continue to qualify as an "Industrial Company" or that the benefits described above will be available in the future.

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.

According to the Inflationary Adjustments Law, until 2007, the results for tax purposes were adjusted for the changes in the Israeli CPI. In February 2008, the "Knesset," the Israeli parliament, passed an amendment to the Inflationary Adjustments Law, which limits the scope of the law starting 2008 and thereafter. Starting 2008, the results for tax purposes are measured in nominal values, excluding certain adjustments for changes in the Israeli CPI carried out in the period up to December 31, 2007. The amendment to the Inflationary Adjustments Law includes, inter alia, the elimination of the inflationary additions and deductions and the additional deduction for depreciation starting 2008.

Israeli Transfer Pricing Regulations

On November 29, 2006, the Income Tax Regulations (Determination of Market Terms), 2006, promulgated under Section 85A of the Tax Ordinance, came into effect (the "TP Regulations"). Section 85A of the Tax Ordinance and the TP Regulations generally require that all cross-border transactions carried out between related parties be conducted on an arm's length basis and be taxed accordingly. The TP Regulations are not expected to have a material effect on us.

Tax Benefits Under the Law for Encouragement of Capital Investments, 1959

Tax benefits prior the 2005 amendment

The Law for the Encouragement of Capital Investments, 1959, as amended (effective as of April 1, 2005), generally referred to as the Investments Law, provides that a proposed capital investment in eligible facilities may, upon application to the Investment Center of the Ministry of Industry and Commerce of the State of Israel, be designated as an "Approved Enterprise." The Investment Center bases its decision as to whether or not to approve an application, among other things, on the criteria set forth in the Investments Law and regulations, the policy of the Investment Center, and the specific objectives and financial criteria of the applicant. Each certificate of approval for an Approved Enterprise relates to a specific investment program delineated both by its financial scope, including its capital sources, and by its physical characteristics, such as the equipment to be purchased and utilized pursuant to the program.

The Investments Law provides that an approved enterprise is eligible for tax benefits on taxable income derived from its approved enterprise programs. The tax benefits under the Investments 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 within the Approved Enterprise's ordinary course of business. If a company has more than one approval or only a portion of its capital investments are approved, its effective tax rate is the result of a

weighted average of the applicable rates. The tax benefits under the Investments Law are not, generally, available with respect to income derived from products manufactured outside of Israel. In addition, the tax benefits available to an Approved Enterprise are contingent upon the fulfillment of conditions stipulated in the Investments Law and regulations and the criteria set forth in the specific certificate of approval, as described above. In the event that a company does not meet these conditions, it would be required to refund the amount of tax benefits, plus a consumer price index linkage adjustment and interest.

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 Enterprise program in the first five years of using the equipment.

Taxable income of a company derived from an Approved Enterprise is subject to corporate tax at the maximum rate of 25%, rather than the regular corporate tax rate, for the benefit period. This period is ordinarily seven years commencing with the year in which the approved enterprise first generates taxable income after the commencement of production, and is limited to twelve years from commencement of production or fourteen years from the date of approval, whichever is earlier. This time limitation does not apply to the exemption period described below.

Should we derive income from sources other than the Approved Enterprise during the relevant period of benefits, such income will be taxable at the regular corporate tax rates.

Under certain circumstances (as further detailed below), the benefit period may extend to a maximum of ten years from the commencement of the benefit period.

A company may elect to receive an alternative package of benefits. Under the alternative package of benefits, a company's undistributed income derived from the Approved Enterprise will be exempt from corporate tax for a period of between two and ten years from the first year the company derives taxable income under the program, after the commencement of production, depending on the geographic location of the Approved Enterprise within Israel, and such company will be eligible for a reduced tax rate for the remainder of the benefits period. The year's limitation does not apply to the exemption period.

A company that has elected the alternative package of benefits, such as us, that subsequently pays a dividend out of income derived from the approved enterprise(s) during the tax exemption period will be subject to corporate tax in the year the dividend is distributed in respect of the gross amount distributed, at the rate which would have been applicable had the company not elected the alternative package of benefits, (generally 10%-25%, depending on the percentage of the company's ordinary shares held by foreign shareholders). The dividend recipient is subject to withholding tax at the reduced rate of 15% applicable to dividends from approved enterprises, if the dividend is distributed during the tax exemption period or within twelve years thereafter. In the event, however, that the company is qualifies as a foreign investors' company, there is no such time limitation.

As of December 31, 2012, we believe that we are meeting the aforementioned conditions.

Foreign Investor's Company ("FIC")

A company that has an Approved Enterprise program is eligible for further tax benefits if it qualifies as a foreign investors' company. A foreign investors' company is a company of which, among other criteria, more than 25% of its share capital and combined share and loan capital is owned by non-Israeli residents. A company that qualifies as a foreign investors' company and has an approved enterprise program is eligible for tax benefits for a ten-year benefit period. As specified above, depending on the geographic location of the approved enterprise within Israel, income derived from the approved enterprise program may be entitled to the following:

- Extension of the benefit period to up to ten years.

- An additional period of reduced corporate tax liability at rates ranging between 10% and 25%, depending on the level of foreign (that is, non-Israeli) ownership of our shares. Those tax rates and the related levels of foreign investment are as set forth in the following table:

Region A

Rate of Reduced Tax	Reduced Tax Period	Tax Exemption Period	Percent of Foreign Ownership
25	0 years	10 years	0-25%
25	0 years	10 years	25-48.99%
20	0 years	10 years	49-73.99%
15	0 years	10 years	74-89.99%
10	0 years	10 years	90-100%

Region B

Rate of Reduced Tax	Reduced Tax Period	Tax Exemption Period	Percent of Foreign Ownership
25	1 years	6 years	0-25%
25	4 years	6 years	25-48.99%
20	4 years	6 years	49-73.99%
15	4 years	6 years	74-89.99%
10	4 years	6 years	90-100%

Other Regions

Rate of Reduced Tax	Reduced Tax Period	Tax Exemption Period	Percent of Foreign Ownership
25	5 years	2 years	0-25%
25	8 years	2 years	25-48.99%
20	8 years	2 years	49-73.99%
15	8 years	2 years	74-89.99%
10	8 years	2 years	90-100%

The twelve years limitation period for reduced tax rate of 15% on dividend from the approved enterprise will not apply.

Subject to applicable provisions concerning income under the alternative package of benefits, dividends paid by a company are considered to be attributable to income received from the entire company and the company's effective tax rate is the result of a weighted average of the various applicable tax rates, excluding any tax-exempt income. Under the Investments Law, a company that has elected the alternative package of benefits is not obliged to distribute retained profits, and may generally decide from which year's profits to declare dividends.

In 1998, the production facilities of the Company related to its computational technologies were granted the status of an "Approved Enterprise" under the Law. In 2004, an expansion program was granted the status of "Approved Enterprise." According to the provisions of the Law, the Company has elected the alternative package of benefits and has waived Government grants in return for tax benefits.

Tax Benefits under the 2005 Amendment

An amendment to the Investments Law, generally referred as the 2005 Amendment, effective as of April 1, 2005 has significantly changed the provisions of the Investments Law. The amendment includes revisions to the criteria for investments qualified to receive tax benefits as an Approved Enterprise. The 2005 Amendment applies to new investment programs and investment programs commencing after 2004, and does not apply to investment programs approved prior to December 31, 2004, and therefore to benefits included in any certificate of approval that was granted before the 2005 Amendment came into effect, which will remain subject to the provisions of the Investments Law as they were on the date of such approval.

However, a company that was granted benefits according to Section 51 of the Investments Law (prior the 2005 Amendment) will not be allowed to choose new tax year as a "Year of Election," referred to below, under the 2005 Amendment, for a period of two years from the company's previous Commencement Year (referred to below) under the old Investments Law.

The 2005 Amendment simplifies the approval process for the approved enterprise. According to the 2005 Amendment, only approved enterprises receiving cash grants require the approval of the Investment Center.

As a result of the 2005 Amendment, it is no longer necessary for a company to acquire Approved Enterprise status in order to receive the tax benefits previously available under the Alternative Route, and therefore such companies need not apply to the Investment Center for this purpose. Rather, a company may claim the tax benefits offered by the Investments Law directly in its tax returns or by notifying the Israeli Tax Authority within twelve months of the end of that year, provided that its facilities meet the criteria for tax benefits set out by the 2005 Amendment. Such enterprise is referred to as the Benefited Enterprise. Companies are also granted a right to approach the Israeli Tax Authority for a pre-ruling regarding their eligibility for benefits under the 2005 Amendment. The 2005 Amendment includes provisions attempting to ensure that a company will not enjoy both Government grants and tax benefits for the same investment program.

Tax benefits are available under the 2005 Amendment to production facilities (or other eligible facilities), which are generally required to derive more than 25% of their business income from export. In order to receive the tax benefits, the 2005 Amendment states that a company must make an investment in the Benefited Enterprise exceeding a certain percentage or a minimum amount specified in the Investments Law. Such investment may be made over a period of no more than three years ending at the end of the year in which the company requested to have the tax benefits apply to the Benefited Enterprise, or the Year of Election. Where the company requests to have the tax benefits apply to an expansion of existing facilities, then only the expansion will be considered a Benefited Enterprise and the company's effective tax rate will be the result of a weighted average of the applicable rates. In this case, the minimum investment required in order to qualify as a Benefited Enterprise is required to exceed a certain percentage or a minimum amount of the company's production assets at the end of the year before the expansion.

The duration of tax benefits is subject to a limitation of the earlier of seven to ten years from the Commencement Year, or twelve years from the first day of the Year of Election. The Commencement Year is defined as the later of (a) the first tax year in which a company had derived income for tax purposes from the Beneficiary Enterprise or (b) the year in which a company requested to have the tax benefits apply to the Beneficiary Enterprise – Year of Election. The tax benefits granted to a Benefited Enterprise are determined, as applicable to its geographic location within Israel, according to one of the following new tax routes, which may be applicable to us:

- Similar to the currently available alternative route, exemption from corporate tax on undistributed income for a period of two to ten years, depending on the geographic location of the Benefited Enterprise within Israel, and a reduced corporate tax rate of 10% to 25% for the remainder of the benefits period, depending on the level of foreign investment in each year. Benefits may be granted for a term of seven to ten years, depending on the level of foreign investment in the company. If the company pays a dividend out of income derived from the Benefited Enterprise during the tax exemption period, such income will be subject to corporate tax at the applicable rate (10%-25%) in respect of the gross amount of the dividend that we may be distributed. The company is required to withhold tax at the source at a rate of 15% from any dividends distributed from income derived from the Benefited Enterprise; and

- A special tax route, which enables companies owning facilities in certain geographical locations in Israel to pay corporate tax at the rate of 11.5% on income of the Benefited Enterprise. The benefits period is ten years. Upon payment of dividends, the company is required to withhold tax at source at a rate of 15% for Israeli residents and at a rate of 4% for foreign residents.

Generally, a company that is Abundant in Foreign Investment (owned by at least 74% foreign shareholders and has undertaken to invest a minimum sum of $20 million in the Beneficiary Enterprise as defined in the Investments Law) is entitled to an extension of the benefits period by an additional five years, depending on the rate of its income that is derived in foreign currency.

The 2005 Amendment changes the definition of "foreign investment" in the Investments Law so that the definition 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, provided that the company's outstanding and paid-up share capital exceeds NIS 5 million. Such changes to the aforementioned definition will take effect retroactively from 2003.

As a result of the 2005 Amendment, tax-exempt income generated under the provisions of the Investments Law, as amended, will subject us to taxes upon distribution or liquidation and we may be required to record deferred tax liability with respect to such tax-exempt income.

We elected the years of 2006 and 2009 as "year of election" under the Investments Law after the 2005 Amendment.

We expect that a substantial portion of any taxable operating income that we may realize in the future will be derived from our approved enterprise status.

We currently intend to reinvest any income derived from our Approved Enterprise program and not to distribute such income as a dividend. As of December 31, 2012, we did not generate income under the provisions of the Investments Law.

Tax benefits under the 2011 Amendment

As of January 1, 2011 new legislation amending to the Investment Law came into effect (the "2011 Amendment"). The 2011 Amendment introduced a new status of "Preferred Company" and "Preferred Enterprise", replacing the existed status of "Beneficiary Company" and "Beneficiary Enterprise". Similarly to "Beneficiary Company", a Preferred Company is an industrial company owning a Preferred Enterprise which meets certain conditions (including a minimum threshold of 25% export). However, under this new legislation the requirement for a minimum investment in productive assets was cancelled.

Under the 2011 Amendment, a uniform corporate tax rate will apply to all qualifying income of the Preferred Company, as opposed to the former law, which was limited to income from the Approved Enterprises and Beneficiary Enterprise during the benefits period. The uniform corporate tax rate will be 7 % in areas in Israel designated as Development Zone A and 12.5% elsewhere in Israel during 2013, 9% and 16%, respectively, in 2014.

A dividend distributed from income which is attributed to a Preferred Enterprise/Special Preferred Enterprise will be subject to withholding tax at source at the following rates: (i) Israeli resident corporation – 0%, (ii) Israeli resident individual – 15% in 2013 and 20% as of 2014 (iii) non-Israeli resident - 15% in 2013 and 20% as of 2014 subject to a reduced tax rate under the provisions of an applicable double tax treaty.

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The provisions of the 2011 Amendment also provided transitional provisions to address companies already enjoying current benefits. These transitional provisions provide, among other things, that unless an irrevocable request is made to apply the provisions of the Investment Law as amended in 2011 with respect to income to be derived as of January 1, 2011: (i) the terms and benefits included in any certificate of approval that was granted to an Approved Enterprise, which chose to receive grants, before the 2011 Amendment came into effect, will remain subject to the provisions of the Investment Law as in effect on the date of such approval, and subject to certain conditions; (ii) terms and benefits included in any certificate of approval that was granted to an Approved Enterprise, which had participated in an alternative benefits program, before the 2011 Amendment came into effect will remain subject to the provisions of the Investment Law as in effect on the date of such approval, provided that certain conditions are met; and (iii) a Beneficiary Enterprise can elect to continue to benefit from the benefits provided to it before the 2011 Amendment came into effect, provided that certain conditions are met.

Under the transition provisions of the new legislation, a company may decide to irrevocably implement the new law while waiving benefits provided under the current law or to remain subject to the current law. We intend to implement the new legislation in 2016.

Tax benefits under the 2012 Amendment

Special Provisions Relating to Taxation Under Inflationary Conditions

Under the Income Tax (Inflationary Adjustments) Law, 1985 (the “Israeli law”), results for tax purposes are measured in real terms, in accordance with the changes in the Israeli Consumer Price Index ("Israeli CPI"). Accordingly, until 2011, results for tax purposes were measured in terms of earnings in NIS after certain adjustments for increases in the Israeli CPI. Commencing in the taxable year 2003, we have elected to measure our taxable income and file our tax return under the Israeli Income Tax Regulations (Principles Regarding the Management of Books of Account of Foreign Invested Companies and Certain Partnerships and the Determination of Their Taxable Income), 1986. This election is for a three-year period. Accordingly, commencing in the taxable year 2012.

Capital Gains Tax on Sales of Our Ordinary Shares

Israeli law generally imposes a capital gains tax on the sale of any capital assets by residents of Israel, as defined for Israeli tax purposes, and on the sale of assets located in Israel, including shares in Israeli companies, by both residents and non-residents of Israel, unless a specific exemption is available or a tax treaty between Israel and the shareholder’s country of residence provides otherwise. The law distinguishes between real gain and inflationary surplus. The inflationary surplus is a portion of the total capital gain which is equivalent to the increase of the relevant asset’s purchase price which is attributable to the increase in the Israeli consumer price index or, in certain circumstances, a foreign currency exchange rate, between the date of purchase and the date of sale. The real gain is the excess of the total capital gain over the inflationary surplus.

Generally, until the 2006 tax year, capital gains tax was imposed on individuals who are Israeli residents at a rate of 15% on real gains derived on or after January 1, 2003 from the sale of shares in Israeli companies publicly traded on NASDAQ or another recognized stock exchange or regulated market in a country that has a treaty for the prevention of double taxation with Israel. This tax rate was contingent upon the shareholder not claiming a deduction for financing expenses in connection with such shares (in which case the gain was generally taxed at a rate of 25%), and did not apply to: (i) the sale of shares to a relative (as defined in the Israeli Income Tax Ordinance); (ii) the sale of shares by dealers in securities; (iii) the sale of shares by shareholders that report in accordance with the Inflationary Adjustments Law (that were taxed at corporate tax rates for corporations and at marginal tax rates for individuals); or (iv) the sale of shares by shareholders who acquired their shares prior to an initial public offering (that may be subject to a different tax arrangement).

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As of January 1, 2006, the tax rate applicable to capital gains derived from the sale of shares, whether listed on a stock market or not, is 20% for Israeli individuals, unless such shareholder claims a deduction for financing expenses in connection with such shares, in which case the gain is generally taxed at a rate of 25%. Additionally, if such shareholder is considered a "material shareholder" at any time during the 12-month period preceding such sale, i.e., such shareholder holds directly or indirectly, including with others, at least 10% of any means of control in a company, the tax rate is 25%. Israeli companies are subject to the Corporate Tax rate on capital gains derived from the sale of shares, unless such companies were not subject to the Adjustments Law (or certain regulations) at the time of publication of the aforementioned amendment to the Tax Ordinance that came into effect on January 1, 2006, in which case the applicable tax rate is 25%. However, the foregoing tax rates do not apply to: (i) dealers in securities; and (ii) shareholders who acquired their shares prior to an initial public offering (that may be subject to a different tax arrangement).

The tax basis of shares acquired prior to January 1, 2003 is determined in accordance with the average closing share price in the three trading days preceding January 1, 2003. However, a request may be made to the tax authorities to consider the actual adjusted cost of the shares as the tax basis if it is higher than such average price.

Non-Israeli residents are exempt from Israeli capital gains tax on any gains derived from the sale of shares of Israeli companies publicly traded on a recognized stock exchange or regulated market outside of Israel, provided that such capital gains are not derived from a permanent establishment in Israel, the shareholders are not subject to the Adjustments Law, and the shareholders did not acquire their shares prior to an initial public offering. However, non-Israeli corporations will not be entitled to such exemption if an Israeli resident (i) has a controlling interest of 25% or more in such non-Israeli corporation, or (ii) is the beneficiary or is entitled to 25% or more of the revenues or profits of such non-Israeli corporation, whether directly or indirectly.

In some instances where our shareholders may be liable to Israeli tax on the sale of their ordinary shares, the payment of the consideration may be subject to the withholding of Israeli tax at the source.

Pursuant to the Convention between the government of the United States and the government of Israel with respect to taxes on income, as amended (the "U.S.-Israel Tax Treaty"), the sale, exchange or disposition of ordinary shares by a person who (i) holds the ordinary shares as a capital asset, (ii) qualifies as a resident of the United States within the meaning of the U.S.-Israel Tax Treaty and (iii) is entitled to claim the benefits afforded to such person by the U.S.-Israel Tax Treaty, generally, will not be subject to the Israeli capital gains tax. Such exemption will not apply if (i) such U.S. resident holds, directly or indirectly, shares representing 10% or more of our voting power during any part of the 12-month period preceding such sale, exchange or disposition, subject to certain conditions, or (ii) the capital gains from such sale, exchange or disposition can be allocated to a permanent establishment in Israel. In such case, the sale, exchange or disposition of ordinary shares would be subject to Israeli tax, to the extent applicable; however, under the U.S.-Israel Tax Treaty, such U.S. resident would be permitted to claim a credit for such taxes against the U.S. federal income tax imposed with respect to such sale, exchange or disposition, subject to the limitations in U.S. laws applicable to foreign tax credits. The U.S.-Israel Tax Treaty does not relate to U.S. state or local taxes.

United States Federal Income Taxation

The following is a description of the material United States federal income tax consequences of the ownership and disposition of our ordinary shares. This description addresses only the United States federal income tax considerations of holders that hold such ordinary shares as capital assets. This description does not address tax considerations applicable to holders that may be subject to special tax rules, including:

- financial institutions or insurance companies;

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- real estate investment trusts, regulated investment companies or grantor trusts;
- dealers or traders in securities or currencies;
- tax-exempt entities;
- certain former citizens or long-term residents of the United States;
- persons that will hold our shares through a partnership or other pass-through entity;
- persons that received our shares as compensation for the performance of services;
- persons that will hold our shares as part of a "hedging" or "conversion" transaction or as a position in a "straddle" for United States federal income tax purposes;
- persons whose "functional currency" is not the United States dollar; or
- holders that own directly, indirectly or through attribution 10.0% or more of the voting power or value of our shares.

Moreover, this description does not address the United States federal estate and gift or alternative minimum tax consequences of the ownership and disposition of our ordinary shares.

This description is based on the U.S. Internal Revenue Code of 1986, as amended, existing, proposed and temporary United States Treasury Regulations and judicial and administrative interpretations thereof, in each case as in effect and available on the date hereof. All of the foregoing are subject to change, which change could apply retroactively and could affect the tax consequences described below.

For purposes of this description, a "U.S. Holder" is a beneficial owner of our ordinary shares that, for United States federal income tax purposes, is:

- a citizen or resident of the United States;
- corporation, or other entity treated as a corporation for U.S. federal income tax purposes, created or organized in or under the laws of the United States or any state thereof, including the District of Columbia;
- an estate the income of which is subject to United States federal income taxation regardless of its source; or
- a trust if such trust has validly elected to be treated as a United States person for United States federal income tax purposes or if (1) a court within the United States is able to exercise primary supervision over its administration and (2) one or more United States persons have the authority to control all of the substantial decisions of such trust.

A "Non-U.S. Holder" is a beneficial owner of our ordinary shares that is neither a U.S. Holder nor a partnership (or other entity treated as a partnership for United States federal income tax purposes).

If a partnership (or any other entity treated as a partnership for United States federal income tax purposes) holds our ordinary shares, the tax treatment of a partner in such partnership will generally depend on the status of the partner and the activities of the partnership. Such a partner or partnership should consult its tax advisor as to its tax consequences.

You should consult your tax advisor with respect to the United States federal, state, local and foreign tax consequences of owning and disposing of our ordinary shares.

Distributions

Subject to the discussion below under "Passive Foreign Investment Company Considerations," if you are a U.S. Holder, for United States federal income tax purposes, the gross amount of any distribution made to you, with respect to our ordinary shares before reduction of any Israeli taxes withheld therefrom, other than certain distributions, if any, of our ordinary shares distribute pro rata to all our shareholders, will be includible in your income as dividend income to the extent such distribution is paid out of our current or accumulated earnings and profits as determined under United States federal income tax principles. Subject to the discussion below under "Passive Foreign Investment Company Considerations," non-corporate U.S. Holders may qualify for the lower rates of taxation with respect to dividends on ordinary shares applicable to long-term capital gains (that is, gains from the sale of capital assets held for more than one year), provided that certain conditions are met, including certain holding period requirements and the absence of certain risk reduction transactions. However, such dividends will not be eligible for the dividends received deduction generally allowed to corporate U.S. Holders. Subject to the discussion below under "Passive Foreign Investment Company Considerations," to the extent, if any, that the amount of any distribution by us exceeds our current and accumulated earnings and profits as determined under United States federal income tax principles, it will be treated first as a tax-free return of your adjusted tax basis in our ordinary shares and thereafter as capital gain. We do not expect to maintain calculations of our earnings and profits under United States federal income tax principles and, therefore, if you are a U.S. Holder you should expect that the entire amount of any distribution generally will be reported as dividend income to you.

If you are a U.S. Holder, dividends paid to you with respect to your ordinary shares will be treated as foreign source income, which may be relevant in calculating your foreign tax credit limitation. Subject to certain conditions and limitations, Israeli tax withheld on dividends may be deducted from your taxable income or credited against your United States federal income tax liability. The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For this purpose, dividends that we distribute generally should constitute "passive category income," or, in the case of certain U.S. Holders, "general category income." A foreign tax credit for foreign taxes imposed on distributions may be denied when you do not satisfy certain minimum holding period requirements. The rules relating to the determination of the foreign tax credit are complex, and you should consult your personal tax advisors to determine whether and to what extent you would be entitled to this credit.

Subject to the discussion below under "Backup Withholding Tax and Information Reporting Requirements," if you are a Non-U.S. Holder, you generally will not be subject to United States federal income or withholding tax on dividends received by you on your ordinary shares, unless you conduct a trade or business in the United States and such income is effectively connected with that trade or business.

Sales Exchange or other Disposition of Ordinary Shares

Subject to the discussion below under "Passive Foreign Investment Company Considerations," if you are a U.S. Holder, you generally will recognize gain or loss on the sale, exchange or other disposition of our ordinary shares equal to the difference between the amount realized on such sale, exchange or other disposition and your adjusted tax basis in our ordinary shares. Such gain or loss will be capital gain or loss. If you are a non-corporate U.S. Holder, capital gain

from the sale, exchange or other disposition of ordinary shares is eligible for the preferential rate of taxation applicable to long-term capital gains if your holding period for such ordinary shares exceeds one year (that is, such gain is long-term capital gain). Gain or loss, if any, recognized by you generally will be treated as United States source income or loss for United States foreign tax credit purposes. The deductibility of capital losses for U.S. federal income tax purposes is subject to limitations.

Subject to the discussion below under “Backup Withholding Tax and Information Reporting Requirements,” if you are a Non-U.S. Holder, you generally will not be subject to United States federal income or withholding tax on any gain realized on the sale or exchange of our ordinary shares unless:

- such gain is effectively connected with your conduct of a trade or business in the United States; or
- you are an individual and have been present in the United States for 183 days or more in the taxable year of such sale or exchange and certain other conditions are met.

Passive Foreign Investment Company Considerations

A non-U.S. corporation will be classified as a “passive foreign investment company,” or a PFIC, for United States federal income tax purposes in any taxable year in which, after applying certain look-through rules, either:

- at least 75 percent of its gross income is "passive income"; or
- at least 50 percent of the average value of its gross assets (based on the quarterly value of such gross assets) is attributable to assets that produce “passive income” or are held for the production of passive income.

Passive income for this purpose generally includes dividends, interest, royalties, rents, gains from commodities and securities transactions and the excess of gains over losses from the disposition of assets which produce passive income.

PFIC status is an annual determination that is based on tests which are factual in nature and our status for any year will depend on our income, assets and activities for such year. Therefore there can be no assurance that we will not be considered a PFIC for any taxable year. Although we did not use the market capitalization method to value our assets in 2009 as noted in our prior Form 20-Fs, we are relying on the market capitalization method to determine the fair market value of our assets for the taxable year ended December 31, 2012. Based on certain estimates of our gross income and gross assets, the nature of our business and the anticipated amount of goodwill (which is determined in large part by the market price of our stock), we believe that we were not a PFIC for our taxable year ended December 31, 2012. There can be no certainty, however, that the IRS will agree with our position. If we were a PFIC, and you are a U.S. Holder, as further described below, you generally would be subject to ordinary income tax rates, imputed interest charges and other disadvantageous tax treatment (including the denial of the taxation of such dividends at the lower rates applicable to long-term capital gains, as discussed above under “—Distributions”) with respect to any gain from the sale, exchange or other disposition of, and certain distributions with respect to, your ordinary shares. We are not providing any U.S. tax opinion to any U.S. Holder concerning our status as a PFIC for 2012, or any other tax year. A U.S. Holder should consult his, her or its own tax advisor with respect to the potential application of the PFIC rules in his, her or its particular circumstances.

Because the market price of our ordinary shares is likely to fluctuate and the market price of the shares of technology companies has been especially volatile, and because that market price may affect the determination of whether we will be considered a PFIC, we cannot assure you that we will not be considered a PFIC for any taxable year.

Under the PFIC rules, unless a U.S. Holder makes one of the elections described in the next paragraphs, a special tax regime will apply to both (a) any "excess distribution" by us (generally, the U.S. Holder's ratable portion of distributions in any year which are greater than 125% of the average annual distribution received by such U.S. Holder in the shorter of the three preceding years or the U.S. Holder's holding period) and (b) any gain realized on the sale or other disposition of the ordinary shares. Under this regime, any excess distribution and realized gain will be treated as ordinary income and will be subject to tax as if (a) the excess distribution or gain had been realized ratably over the U.S. Holder's holding period, (b) the amount deemed realized had been subject to tax in each year of that holding period, and (c) the interest charge generally applicable to underpayments of tax had been imposed on the taxes deemed to have been payable in those years. In addition, dividend distributions made to you will not qualify for the lower rates of taxation applicable to long term capital gains discussed above under "Distributions."

Certain elections are available to U.S. Holders of shares that may serve to alleviate some of the adverse tax consequences of PFIC status. If we agreed to provide the necessary information, you could avoid the interest charge imposed by the PFIC rules by making a qualified electing fund, or a QEF election, which election may be made retroactively under certain circumstances, in which case you generally would be required to include in income on a current basis your pro rata share of our ordinary earnings as ordinary income and your pro rata share of our net capital gains as long-term capital gain. We do not expect to provide to U.S. Holders the information needed to report income and gain pursuant to a QEF election, and we make no undertaking to provide such information in the event that we are a PFIC.

Under an alternative tax regime, you may also avoid certain adverse tax consequences relating to PFIC status discussed above by making a mark-to-market election with respect to our ordinary shares annually, provided that the shares are "marketable." Shares will be marketable if they are regularly traded on certain U.S. stock exchanges (including NASDAQ) or on certain non-U.S. stock exchanges. For these purposes, the shares will generally be considered regularly traded during any calendar year during which they are traded, other than in negligible quantities, on at least fifteen days during each calendar quarter.

If you choose to make a mark-to-market election, you would recognize as ordinary income or loss each year an amount equal to the difference as of the close of the taxable year between the fair market value of the PFIC shares and your adjusted tax basis in the PFIC shares. Losses would be allowed only to the extent of net mark-to-market gain previously included by you under the election for prior taxable years. If the mark-to-market election were made, then the PFIC rules set forth above relating to excess distributions and realized gains would not apply for periods covered by the election. If you make a mark-to-market election after the beginning of your holding period of our ordinary shares, you would be subject to interest charges with respect to the inclusion of ordinary income attributable to the period before the effective date of such election.

Under certain circumstances, ordinary shares owned by a Non-U.S. Holder may be attributed to a U.S. person owning an interest, directly or indirectly, in the Non-U.S. Holder. In this event, distributions and other transactions in respect of such ordinary shares may be treated as excess distributions with respect to such U.S. person, and a QEF election may be made by such U.S. person with respect to its indirect interest in us, subject to the discussion in the preceding paragraphs.

We may invest in stock of non-U.S. corporations that are PFICs. In such a case, provided that we are classified as a PFIC, a U.S. Holder would be treated as owning its pro rata share of the stock of the PFIC owned by us. Such a U.S. Holder would be subject to the rules generally applicable to shareholders of PFICs discussed above with respect to distributions received by us from such a PFIC and dispositions by us of the stock of such a PFIC (even though the U.S. Holder may not have received the proceeds of such distribution or disposition). Assuming we receive the necessary information from the PFIC in which we own stock, certain U.S. Holders may make the QEF election discussed above with respect to the stock of the PFIC owned by us, with the consequences discussed above. However,

no assurance can be given that we will be able to provide U.S. Holders with such information. A. U.S. Holder generally would not be able to make the mark-to-market election described above with respect to the stock of any PFIC owned by us.

If we were a PFIC, a holder of ordinary shares that is a U.S. Holder must file United States Internal Revenue Service Form 8621 for each tax year in which the U.S. Holder owns the ordinary shares.

You should consult your own tax advisor regarding our potential status as a PFIC and the tax consequences and filing requirements that would arise if we were treated as a PFIC.

Foreign Asset Reporting

Certain U.S. Holders who are individuals (and certain specified entities) are required to report information relating to an interest in ordinary shares, subject to certain exceptions (including an exception for securities held in certain accounts maintained by financial institutions). U.S. Holders are encouraged to consult their own tax advisers regarding the effect of this reporting requirement on their ownership and disposition of ordinary shares.

3.8% Medicare Tax on "Net Investment Income"

Certain U.S. Holders who are individuals, estates or trusts are required to pay an additional 3.8% tax on, among other things, dividends and capital gains from the sale or other disposition of ordinary shares. U.S. Holders are encouraged to consult their own tax advisers regarding the effect of this additional tax on their ownership and disposition of ordinary shares.

Backup Withholding Tax and Information Reporting Requirements

United States backup withholding tax and information reporting requirements generally apply to certain payments to certain non-corporate holders of stock. Information reporting generally will apply to payments of dividends on, and to proceeds from the sale or redemption of, ordinary shares made within the United States, or by a United States payor or United States middleman, to a holder of ordinary shares, other than an exempt recipient (including a corporation, a payee that is not a United States person that provides an appropriate certification and certain other persons). A payor will be required to withhold backup withholding tax from any payments of dividends on, or the proceeds from the sale or redemption of, ordinary shares within the United States, or by a United States payor or United States middleman, to a holder, other than an exempt recipient, if such holder fails to furnish its correct taxpayer identification number or otherwise fails to comply with, or establish an exemption from, such backup withholding tax requirements. The backup withholding tax rate currently is 28.0%.

Any amounts withheld under the backup withholding rules will be allowed as a refund or credit against the beneficial owner's United States federal income tax liability, if any, provided that the required information is furnished to the IRS.

The above description is not intended to constitute a complete analysis of all tax consequences relating to ownership and disposition of our ordinary shares. You should consult your tax advisor concerning the tax consequences of your particular situation.

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, and file periodic reports and other information with the SEC through its electronic data gathering, analysis and retrieval (EDGAR) system. Our securities filings, including this annual report and the exhibits thereto, are available for inspection and copying at the public reference facilities of the SEC located at Room 1580, 100 F Street, N.E., Washington, D.C. 20549. You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Washington, DC 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The Commission also maintains a website at http://www.sec.gov from which certain filings may be accessed. As of November 2010, our filings are also available at the TASE's website at http://maya.tase.co.il and at the Israeli Securities Authority's website at http://www.magna.isa.gov.il.

As a foreign private issuer, we are exempt from the rules under the Exchange Act relating to the furnishing and content of proxy statements, and our officers, directors and principal shareholders will be exempt from the reporting and short-swing profit recovery provisions contained in Section 16 of the Exchange Act. In addition, we are not required under the Exchange Act to file periodic reports and financial statements with the SEC as frequently or as promptly as United States companies whose securities are registered under the Exchange Act.

I. Subsidiary Information

Not applicable.

ITEM 11: Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss related to changes in market prices, including interest rates and foreign exchange rates, of financial instruments that may adversely impact our consolidated financial position, results of operations or cash flows.

Risk of Interest Rate Fluctuation

We do not have any long-term borrowings. We have a significant amount of cash that is currently invested primarily in interest bearing investment such as bank time deposits, money market funds, U.S. government treasury bills and available for sale marketable securities. These investments expose us to the changes in interest rates. If interest rates further decline, our results of operations may be adversely affected due to lower interest income from these investments. The primary objective of our investment activities is to preserve principal while maximizing the income that we receive from our investments without significantly increasing risk and loss. Our investments are exposed to market risk due to fluctuation in interest rates, which may affect our interest income and the fair market value of our investments. We manage this exposure by performing ongoing evaluations of our investments. Due to the short and medium-term maturities nature of our investments to date, their carrying value approximates the fair value. We generally hold investments to maturity in order to limit our exposure to interest rate fluctuations.

Foreign Currency Exchange Risk

Our foreign currency exposures give rise to market risk associated with exchange rate movements of the U.S. dollar, our functional and reporting currency, mainly against the shekel. In 2012, we derived our revenues primarily in

U.S. dollars and a portion in Euros and other currencies. Although a substantial part of our expenses were denominated in U.S. dollars, a significant portion of our expenses were denominated in shekels and to a lesser extent in Euros and other currencies. Our shekel-denominated expenses consist principally of salaries and related personnel expenses. We monitor foreign currency exposure and, from time to time, may use various instruments to preserve the value of sales transactions and commitments; however, this cannot assure our protection against risks of currency fluctuations. For more information regarding foreign currency related risks, see “ITEM 3: Key Information—Risk Factors—Our international operations expose us to the risk of fluctuations in currency exchange rates.”

We use currency forward contracts together with currency options primarily to hedge payments in NIS. These transactions constitute a future cash flow hedge. As of December 31, 2013, we had outstanding forward contracts in the amount of $1.7 million. These transactions were for a period of up to twelve months. As of December 31, 2013, the fair value of the above mentioned foreign currency derivative contracts was $0.3 million.

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 Proceed

A. Material Modifications to the Rights of Security Holders

None.

E. Use of Proceeds

The effective date of the registration statement (file no. 333-138313) for our initial public offering of ordinary shares, par value NIS 0.10, was November 15, 2006. The offering commenced on November 15, 2006 and terminated after the sale of all the securities registered. Lehman Brothers Inc. acted as the sole book-running manager for the offering, Deutsche Bank Securities Inc. acted as co-lead manager and, CIBC World Markets Corp. and RBC Capital Markets Corporation acted as co-managers. We registered 6,500,000 ordinary shares in the offering. We sold 6,500,000 ordinary shares at an aggregate offering price of $78 million at a price per share of $12.00. Under the terms of the offering, we incurred aggregate underwriting discounts of $5.5 million. We also incurred expenses of $2 million in connection with the offering. The net proceeds that we received as a result of the offering were $70.5 million.

From the effective date of the registration statement and until December 31, 2013, the net proceeds had been invested in cash equivalents, marketable securities, capital expenditure and other corporate purposes. None of the net proceeds of the offering was paid directly or indirectly to any director, officer, general partner of ours or to their associates, persons owning ten percent or more of any class of our equity securities, or to any of our affiliates.

We conducted a subsequent public offering of our ordinary shares on November 15, 2011 raising net proceeds of $85 million.

ITEM 15: Controls and Procedures

(a) Disclosure Controls and Procedures. Our management, including our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of December 31,2013. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2013, our disclosures controls and procedures were effective at the reasonable assurance level.

(b) Management's Annual Report on Internal Control over Financial Reporting. Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets;

- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and

- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2013. In making this assessment, our management used the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Our management has concluded, based on its assessment, that our internal control over financial reporting was effective as of December 31, 2013 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external reporting purposes in accordance with generally accepted accounting principles.

Our independent auditors, Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global, have issued an audit report on the effectiveness of our internal control over financial reporting. The report is included with our consolidated financial statements included elsewhere in this annual report.

(c) Changes in Internal Control over Financial Reporting. During the period covered by this report, no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) have occurred that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 16: [Reserved]

ITEM 16A: Audit Committee Financial Expert

The board of directors has determined that Nurit Benjamini is an "audit committee financial expert" as defined under the U.S. federal securities laws and is independent under the rules of the NASDAQ Stock Market.

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ITEM 16B: Code of Ethics

We have adopted a code of ethics applicable to our Chief Executive Officer, Chief Financial Officer, controller and persons performing similar functions. This code has been posted on our website, www.allot.com. Waivers of our code of ethics may only be granted by the board of directors. Any amendments to this code or any waiver that is granted, and the basis for granting the waiver, will be publicly communicated as appropriate. We granted no waivers under our Code of Ethics in 2013.

ITEM 16C: Principal Accountant Fees and Services

Fees paid to the Auditors

The following table sets forth, for each of the years indicated, the fees expensed by our independent registered public accounting firm.

	Year ended December, 31,	
	2012	2013
	(in thousands of U.S. dollars)	
Audit Fees(1)	$285	$275
Audit-Related Fees(2)	105	25
Tax Fees(3)	73	83
All Other Fees(4)	41	15
Total	$504	$398

(1) "Audit fees" include fees for services performed by our independent public accounting firm in connection with our annual audit for 2012 and 2013, certain procedures regarding our quarterly financial results submitted on Form 6-K, the filing of our Form F-3, fees related to public offering, and consultation concerning financial accounting and reporting standards.

(2) "Audit-Related fees" relate to assurance and associated services that are traditionally performed by the independent auditor, including: accounting consultation and consultation concerning financial accounting, reporting standards and due diligence investigations.

(3) "Tax fees" include fees for professional services rendered by our independent registered public accounting firm for tax compliance, transfer pricing and tax advice on actual or contemplated transactions.

(4) "Other fees" include fees for services rendered by our independent registered public accounting firm with respect to government incentives and other matters.

Audit Committee's Pre-Approval Policies and Procedures

Our audit committee pre-approved all audit and non-audit services provided to us and to our subsidiaries during the periods listed above.

ITEM 16D: Exemptions from the Listing Standards for Audit Committees

Not applicable.

ITEM 16E: Purchase of Equity Securities by the Company and Affiliated Purchasers

Not applicable.

ITEM 16F: Change in Registrant's Certifying Accountant

None.

ITEM 16G: Corporate Governance

As a foreign private issuer, we are permitted under NASDAQ Marketplace Rule 5615(a)(3) to follow Israeli corporate governance practices instead of the NASDAQ Stock Market requirements, provided we disclose which requirements we are not following and describe the equivalent Israeli requirement. We must also provide NASDAQ with a letter from outside counsel in our home country, Israel, certifying that our corporate governance practices are not prohibited by Israeli law.

We rely on this "foreign private issuer exemption" with respect to the following items:

- We follow the requirements of Israeli law with respect to the quorum requirement for meetings of our shareholders, which are different from the requirements of Rule 5620(c). Under our articles of association, the quorum required for an ordinary meeting of shareholders consists of at least two shareholders present in person, by proxy or by written ballot, who hold or represent between them at least 25% of the voting power of our shares, instead of 33 1/3% of the issued share capital provided by under the NASDAQ Global Market requirements. This quorum requirement is based on the default requirement set forth in the Companies Law. We submitted a letter from our outside counsel in connection with this item prior to our initial public offering in November 2006.

- We do not seek shareholder approval for equity compensation plans in accordance with the requirements of the Companies Law, which does not fully reflect the requirements of Rule 5635(c). Under Israeli law, we may amend our 2006 Incentive Compensation Plan by the approval of our board of directors, and without shareholder approval as is generally required under Rule 5635(c). Under Israeli law, the adoption and amendment of equity compensation plans, including changes to the reserved shares, do not require shareholder approval. We submitted a letter from our outside counsel in connection with this item in June 2008.

We are subject to additional Israeli corporate governance requirements applicable to companies incorporated in Israel whose securities are listed for trading on a stock exchange outside of Israel.

We may in the future provide NASDAQ with an additional letter or letters notifying NASDAQ that we are following our home country practices, consistent with the Companies Law and practices, in lieu of other requirements of Rule 5600.

ITEM 16H: Mine Safety Disclosure

Not applicable.

PART III

ITEM 17: Financial Statements

Not applicable.

ITEM 18: Financial Statements

See Financial Statements included at the end of this report.

ITEM 19: Exhibits

See exhibit index incorporated herein by reference.

SIGNATURES

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

Allot Communications Ltd.

By: /s/ Rami Hadar
Rami Hadar
Chief Executive Officer and
President

Dated: March 26, 2014

ANNUAL REPORT ON FORM 20-F

INDEX OF EXHIBITS

Number	Description
1.1	Articles of Association of the Registrant
1.2	Certificate of Name Change (1)
2.1	Specimen share certificate (1)
4.1	Non-Stabilized Lease Agreement, dated February 13, 2006, by and among, Aderet Hod Hasharon Ltd., Miritz, Inc., Leah and Israel Ruben Assets Ltd., Tamar and Moshe Cohen Assets Ltd., Drish Assets Ltd., S. L. A. A. Assets and Consulting Ltd., Iris Katz Ltd., Y. A. Groder Investments Ltd., Ginotel Hod Hasharon 2000 Ltd. and Allot Communications Ltd. (1)
4.2	Key Employees of Subsidiaries and Consultants Share Incentive Plan (1997) (1)
4.3	Key Employees Share Incentive Plan (1997) (1)
4.4	Key Employees Share Incentive Plan (2003) (1)
4.5	2006 Incentive Compensation Plan(2)
4.6	Manufacturing Agreement, dated July 19, 2007, by and between Flextronics (Israel) Ltd. and the Registrant* (3)
4.7	Amendment No. 1, dated September 1, 2012, to the Manufacturing Agreement, dated July 19, 2007, by and between Flextronics (Israel) Ltd. and the Registrant*(4)
8.1	List of Subsidiaries of the Registrant
11.1	Code of Ethics (5)
12.1	Certification of Principal Executive Officer required by Rule 13a-14(a) and Rule 15d-14(a) (Section 302 Certifications)
12.2	Certification of Principal Financial Officer required by Rule 13a-14(a) and Rule 15d-14(a) (Section 302 Certifications)
13.1	Certification of Principal Executive Officer and Principal Financial Officer required by Rule 13a-14(b) and Rule 15d-14(b) (Section 906 Certifications) (6)
14.1	Consent of Kost Forer Gabbay & Kasierer
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.PRE	XBRL Taxonomy Presentation Linkbase Document
101.CAL	XBRL Taxonomy Calculation Linkbase Document
101.LAB	XBRL Taxonomy Label Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document

(1) Previously filed with the Securities and Exchange Commission on October 31, 2006 pursuant to a registration statement on Form F-1 (File No. 333-138313) and incorporated by reference herein.

(2) Previously filed with the Securities and Exchange Commission on March 21, 2013 as Exhibit 4.5 to Form 20-F for the year ended December 31, 2012 and incorporated by reference herein.

(3) Previously filed with the Securities and Exchange Commission on June 27, 2008 as Exhibit 4.11 to Form 20-F for the year ended December 31, 2007 and incorporated by reference herein.

(4) Previously filed with the Securities and Exchange Commission on March 21, 2013 as Exhibit 4.7 to Form 20-F for the year ended December 31, 2012 and incorporated by reference herein.

(5) Previously filed with the Securities and Exchange Commission on June 28, 2007 as Exhibit 4 to Form 20-F for the year ended December 31, 2006 and incorporated by reference herein.

(6) Furnished herewith.

* Portions of this exhibit were omitted and have been filed separately with the Secretary of the Securities and Exchange Commission pursuant to the Registrant's application requesting confidential treatment under Rule 24b-2 of the Exchange Act.

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2013

U.S. DOLLARS IN THOUSANDS

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2013

U.S. DOLLARS IN THOUSANDS

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

ALLOT COMMUNICATIONS LTD.

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

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company at December 31, 2013 and 2012, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 26, 2014 expressed an unqualified opinion thereon.

Tel Aviv, Israel
March 26, 2014

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

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Directors of

ALLOT COMMUNICATIONS LTD.

We have audited Allot Communications Ltd. ("the Company") and its subsidiaries internal control over financial reporting as of December 31, 2013, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Company's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

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

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

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Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. 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.

In our opinion, the Company and its subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company and its subsidiaries as of December 31, 2013 and 2012, and the related consolidated statements of comprehensive income, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2013 and our report dated March 26, 2014 expressed an unqualified opinion thereon.

Tel Aviv, Israel
March 26, 2014

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

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands

	December 31,	
	2013	2012
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$42,813	$50,026
Restricted cash and deposits	-	146
Short-term bank deposits	38,000	78,042
Available-for-sale marketable securities	40,798	14,841
Trade receivables (net of allowance for doubtful accounts of $ 441 and $ 280 at December 31, 2013 and 2012 respectively)	16,908	20,236
Other receivables and prepaid expenses	8,218	6,815
Inventories	13,798	9,963
Total current assets	160,535	180,069
NON-CURRENT ASSETS:		
Severance pay fund	254	213
Deferred taxes	1,602	1,525
Other assets	771	239
Total non-current assets	2,627	1,977
PROPERTY AND EQUIPMENT, NET	5,874	6,609
INTANGIBLE ASSETS, NET	9,407	12,322
GOODWILL	20,814	20,814
Total assets	$199,257	$221,791

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

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED BALANCE SHEETS

U.S. dollars in thousands, except share and per share data

	December 31,	
	2013	2012
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Trade payables	$3,191	$4,809
Employees and payroll accruals	6,129	8,182
Deferred revenues	12,504	13,829
Liability related to settlement of OCS grants (See note 11a)	-	15,886
Other payables and accrued expenses	4,777	5,765
Total current liabilities	26,601	48,471
LONG-TERM LIABILITIES:		
Deferred revenues	2,447	3,945
Accrued severance pay	282	254
Total long-term liabilities	2,729	4,199
COMMITMENTS AND CONTINGENT LIABILITIES		
SHAREHOLDERS' EQUITY:		
Share capital -		
Ordinary shares of NIS 0.1 par value - Authorized: 200,000,000 shares at December 31, 2013 and 2012; Issued and outstanding: 32,877,118 and 32,547,151 shares at December 31, 2013 and 2012, respectively	774	761
Additional paid-in capital	242,629	233,985
Accumulated other comprehensive income	366	1,760
Accumulated deficit	(73,842)	(67,385)
Total shareholders' equity	169,927	169,121
Total liabilities and shareholders' equity	$199,257	$221,791

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

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

U.S. dollars in thousands, except share and per share data

	Year ended December 31,		
	2013	2012	2011
Revenues:			
Products	$ 66,318	$ 77,127	$ 56,810
Services	30,227	27,625	20,943
Total revenues	96,545	104,752	77,753
Cost of revenues:			
Products	20,572	26,857	19,540
Services	6,246	4,180	2,635
Expenses related to settlement of OCS grants (See note 11a)	-	15,886	-
Total cost of revenues	26,818	46,923	22,175
Gross profit	69,727	57,829	55,578
Operating expenses:			
Research and development (net of grant participations of $ 1,051, $ 2,855 and $ 3,674 for the years ended December 31, 2013, 2012 and 2011, respectively)	27,022	22,060	13,222
Sales and marketing	39,817	34,127	26,543
General and administrative	9,952	10,664	7,474
Total operating expenses	76,791	66,851	47,239
Operating income (loss)	(7,064)	(9,022)	8,339
Financial income, net	(727)	(1,358)	(415)
Income (loss) before income tax expenses (benefit)	(6,337)	(7,664)	8,754
Income tax expenses (benefit)	120	(926)	(55)
Net income (loss)	$ (6,457)	$ (6,738)	$ 8,809
Unrealized gain (loss) on available-for-sale marketable securities	(20)	15	68
Unrealized gain (loss) on foreign currency cash flow hedges transactions	(1,374)	2,555	(1,312)
Total comprehensive income (loss)	$ (7,851)	$ (4,168)	$ 7,565
Net earnings (loss) per share:			
Basic	$ (0.20)	$ (0.21)	$ 0.35
Diluted	$ (0.20)	$ (0.21)	$ 0.33

Weighted average number of shares used in per share computations of net earnings (loss):			
Basic	32,680,766	31,959,921	25,047,771
Diluted	32,680,766	31,959,921	27,071,872

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

ALLOT COMMUNICATIONS LTD.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share data

	Ordinary shares		Additional paid-in capital	Accumulated other comprehensive income (loss)	Accumulated deficit	Total shareholders' equity
	Outstanding shares	Amount				
Balance at January 1, 2011	23,806,313	$527	$133,483	$ 434	$ (69,456)	$ 64,988
Issuance of shares related to secondary offering, net of issuance costs (*)	6,325,000	169	84,753	-	-	84,922
Exercise of stock options	818,921	24	2,814	-	-	2,838
Stock-based compensation	-	-	2,256	-	-	2,256
Other comprehensive loss	-	-	-	(1,244)	-	(1,244)
Net income	-	-	-	-	8,809	8,809
Balance at December 31, 2011	30,950,234	$720	$223,306	$ (810)	$ (60,647)	$ 162,569
Exercise of stock options	1,596,917	41	5,862	-	-	5,903
Stock-based compensation	-	-	4,817	-	-	4,817
Other comprehensive gain	-	-	-	2,570	-	2,570
Net loss	-	-	-	-	(6,738)	(6,738)
Balance at December 31, 2012	32,547,151	$761	$233,985	$ 1,760	$ (67,385)	$ 169,121

(*) $ 252 of issuance costs.

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

ALLOT COMMUNICATIONS LTD.

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

U.S. dollars in thousands, except share data

	Ordinary shares		Additional paid-in capital	Accumulated other comprehensive income (loss)	Accumulated deficit	Total shareholders' equity
	Outstanding shares	Amount				
Balance at December 31, 2012	32,547,151	$761	$233,985	$ 1,760	$ (67,385)	$ 169,121
Exercise of stock options	329,967	13	913	-	-	926
Stock-based compensation	-	-	7,731	-	-	7,731
Other comprehensive loss	-	-	-	(1,394)	-	(1,394)
Net loss	-	-	-	-	(6,457)	(6,457)
Balance at December 31, 2013	32,877,118	$774	$242,629	$ 366	$ (73,842)	$ 169,927

Accumulated other comprehensive income (loss):

	Year ended December 31,		
	2013	2012	2011
Accumulated unrealized gain on available-for-sale marketable securities	$ 41	$ 61	$ 45
Accumulated unrealized gain (loss) on foreign currency cash flows hedge transactions	325	1,699	(855)
Accumulated other comprehensive income (loss) (see note 2u)	$ 366	$ 1,760	$ (810)

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

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2013	2012	2011
Cash flows from operating activities:			
Net income (loss)	$(6,457)	$(6,738)	$8,809
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Depreciation and amortization	6,338	5,067	2,878
Stock-based compensation	7,731	4,817	2,256
Capital loss	18	20	7
Decrease (increase) in accrued severance pay, net	(13)	-	12
Decrease (increase) in other assets	(532)	6	98
Decrease in accrued interest and amortization of premium on marketable securities	366	212	151
Decrease (increase) in trade receivables	3,328	(8,139)	(1,187)
Decrease (increase) in other receivables and prepaid expenses	(2,749)	1,159	(970)
Decrease (increase) in inventories, net	(3,835)	3,233	329
Increase in long-term deferred taxes, net	(77)	(931)	(227)
Decrease in trade payables	(1,618)	(1,287)	(2,456)
Increase (decrease) in employees and payroll accruals	(2,053)	2,392	(748)
Increase (decrease) in deferred revenues	(2,823)	(7,089)	7,423
Increase (decrease) in other payables and accrued expenses	(988)	84	(1,178)
Liability related to settlement of OCS grants (See Note 11a)	(15,886)	15,886	-
Net cash provided by (used in) operating activities	(19,250)	8,692	15,197
Cash flows from investing activities:			
Decrease (increase) in restricted cash and deposits	146	913	(78)
Investments in short-term bank deposits	-	(54,042)	(24,000)
Proceeds of short-term bank deposits	40,042	-	-
Purchase of property and equipment	(2,706)	(3,820)	(2,953)
Proceeds from sale of property and equipment	-	-	30
Investment in available-for sale marketable securities	(32,805)	(8,194)	(4,735)
Proceeds from sales of available-for-sale marketable securities	2,597	750	803
Proceeds from maturity of available-for-sale marketable securities	3,864	9,986	1,800
Payments (and loan issued) for subsidiaries acquired, net of cash (see schedule A below)	-	(24,892)	-
Net cash provided by (used in) investing activities	11,138	(79,299)	(29,133)

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

ALLOT COMMUNICATIONS LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2013	2012	2011
Cash flows from financing activities:			
Issuance of shares related to secondary offering, net	-	-	84,922
Proceeds from exercise of stock options	899	5,903	2,838
Repayment of bank loan	-	(1,952)	-
Net cash provided by financing activities	899	3,951	87,760
Increase (decrease) in cash and cash equivalents	(7,213)	(66,656)	73,824
Cash and cash equivalents at the beginning of the year	50,026	116,682	42,858
Cash and cash equivalents at the end of the year	$ 42,813	$ 50,026	$ 116,682
Supplementary cash flow information:			
Cash paid (received) during the year for:			
Taxes	$ (9)	$ (48)	$ 100
Schedule A- Acquisitions of subsidiaries (see also Note 1b):			
Estimated net fair value of assets acquired and liabilities assumed at the date of acquisition was as follows:			
Working capital, net (excluding cash and cash equivalents)	$ -	$ (4,501)	$ -
Equipment and other assets	-	597	-
Intangible assets		14,025	
Goodwill	-	17,663	-
Deferred tax assets, net	-	409	-
Long-term liabilities	-	(1,952)	-
Total Consideration	$ -	$ 26,241	$ -
Non cash - Contingent Consideration (See also note 1b)	$ -	(1,349)	$ -
Payments (and loan issued) for subsidiaries acquired, net of cash	$ -	$ 24,892	$ -
Schedule B –non cash activities during the year for:			
Proceeds from exercise of stock options	$27	$-	$-

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

ALLOT COMMUNICATIONS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL

a. Allot Communications Ltd. (the "Company") was incorporated in November 1996 under the laws of the State of Israel. The Company is engaged in developing, selling and marketing intelligent IP service optimization solutions for mobile, DSL and wireless broadband carriers, cable operator service providers, and enterprises. The Company's portfolio of hardware platforms and software applications utilizes advanced deep packet inspection technology to transform broadband pipes into smart networks that can rapidly and efficiently manage data over mobile and wireline networks and deploy value added Internet services. The Company's products consist of the Service Gateway and NetEnforcer traffic management systems, the NetXplorer and Subscribe Management Platform application management suites and value added services such as the Service Protector network protection solution, the MediaSwift video caching solution and the WebSafe network service.

The Company's Ordinary Shares are listed in the NASDAQ Global Select Market under the symbol "ALLT" from its initial public offering in November 2006. Since November, 2010, the Company's Ordinary Shares have been listed for trading in the Tel Aviv Stock Exchange as well. In November 2011, the Company completed a secondary public offering for a total amount of approximately $85,000 at an average price per share of $13.47.

The Company holds eight wholly-owned subsidiaries (the Company together with said subsidiaries shall collectively be referred to as "Allot"): Allot Communications Inc. in Woburn, Massachusetts, United-States (the "U.S. subsidiary"), which was incorporated in 1997 under the laws of the State of California, Allot Communication Europe SARL in Sophia, France (the "European subsidiary"), which was incorporated in 1998 under the laws of France, Allot Communications Japan K.K. in Tokyo, Japan (the "Japanese subsidiary"), which was incorporated in 2004 under the laws of Japan, Allot Communication (UK) Limited (the "UK subsidiary"), which was incorporated in 2006 under the laws of England and Wales, Allot Communications (Asia Pacific) Pte. Ltd. ("the Singaporean subsidiary"), which was incorporated in 2006 under the laws of Singapore, Allot Communications (New Zealand) Limited. (the "NZ subsidiary"), which was incorporated in 2007 under the laws of New Zealand, Allot India Private Limited. (the "Indian subsidiary"), which was incorporated in 2012 under the laws of India and started it's activity in 2013 and Allot Communication Africa (PTY) Ltd. (the "African subsidiary"), which was incorporated in 2013 under the laws of South Africa.

The U.S. subsidiary commenced operations in 1997. It is engaged in the sale, marketing and technical support and research and development services in the Americas of products manufactured and imported by the Company. The European, Japanese, UK, Singaporean, Indian and African subsidiaries are engaged in marketing and technical support services of the Company's products in Europe, Japan, UK and Asia Pacific, respectively. The NZ subsidiary commenced its operations in 2008 and is engaged in the research and development activities related to the Service Protector and technical support services for this product.

ALLOT COMMUNICATIONS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL (CONT.)

b. Acquisitions:

1. On May 15, 2012 (the "Ortiva acquisition date"), the Company entered into a share purchase agreement (the "Ortiva SPA") with the shareholders of Ortiva Wireless Inc. ("Ortiva") a private, California-based company that develops video optimization solutions for mobile and internet networks. The Company paid $ 10,816 in cash as consideration for all the shares of Ortiva.

The acquisition was accounted for using the purchase method of accounting in accordance with ASC No. 805, “Business Combinations” ("ASC No. 805"). Accordingly, the purchase price was allocated according to the estimated fair values of the assets acquired and liabilities assumed and the excess of the purchase price over the net tangible and identified intangible assets was assigned to goodwill. The fair value of intangible assets was determined by management with the assistance of a third party valuation.

The results of Ortiva's operations have been included in the Company’s consolidated financial statements since the Ortiva acquisition date. Revenues recognized from the Ortiva acquisition date to December 31, 2012 were $ 3,404.

On December 31, 2012 Ortiva was merged into the U.S. subsidiary.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date:

	Fair value
Current assets	$ 1,967
Equipment	459
Deferred revenues	(1,803)
Current and non-current liabilities	(3,949)
Deferred tax assets, net	409
Technology	3,899
Backlog	910
Goodwill	8,924
Net assets acquired	$ 10,816

Technology includes Ortiva’s internally developed proprietary technologies and platforms for video optimization. The technology is being amortized over the estimated useful life of 9.6 years using the straight line method.

Backlog from customer orders is amortized over the estimated useful life of 1.6 years.

ALLOT COMMUNICATIONS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL (CONT.)

2. On September 4, 2012, (the "Oversi acquisition date") the Company entered into a share purchase agreement (the "Oversi SPA") with the shareholders of Oversi Networks Ltd ("Oversi"), a private, Israeli-based company that develops and sells products and systems for caching Internet content.

   The total consideration for the acquisition was $ 17,349, which consisted of $ 16,000 in cash and contingent consideration estimated at fair value of $ 1,349 at the Oversi acquisition date.

   Pursuant to the Oversi SPA, the Company had a contingent liability to pay additional consideration if Oversi reaches a certain threshold of bookings for the year ended December 31, 2012. As of December 31, 2012, the fair value of the contingent consideration was determined to be $ 1,088 and was presented in other payables and accrued expenses. During 2013, the fair value of the contingent consideration was estimated to $ 0 as the booking threshold was not achieved. The changes in fair value of the contingent consideration were recorded in general and administrative expenses.

   The acquisition of Oversi was accounted for using the purchase method of accounting in accordance with ASC No. 805. Accordingly, the purchase price has been allocated according to the estimated fair value of the assets acquired and liabilities assumed. The excess of the purchase price over the net tangible and identified intangible assets was assigned to goodwill. The fair value of the intangible assets and the contingent consideration was determined by management with the assistance of a third party valuation.

   The results of Oversi's operations have been included in the Company consolidated financial statements since September 4, 2012. Revenues recognized from the Oversi acquisition date to December 31, 2012 were $ 1,954.

   On December 31, 2012, Oversi was merged into the Company.

   The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date:

	Fair value
Current assets	$ 4,182
Equipment and other assets	138
Deferred revenues	(936)
Other current liabilities	(2,038)
Bank loan	(1,952)
Technology	6,826
Backlog	1,491
Customer relationships	899
Goodwill	8,739
Net assets acquired	$ 17,349

U.S. dollars in thousands, except share and per share data

NOTE 1: GENERAL (CONT.)

Technology includes rich-media caching and content delivery solutions for peer to peer, Internet video and other media applications. The technology is amortized over the estimated useful life of 6.3 years using the straight line method.

Backlog from customer orders is amortized over the estimated useful life of 1.4 years.

Customer relationships is derived from customer contracts and related customer relationships with existing customers. Customer relationships is amortized based on the accelerated method over the estimated useful life of 4.3 years.

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:

The preparation of the consolidated financial statements in conformity with U.S. GAAP requires management to make estimates, judgments and assumptions. The Company's management believes that the estimates, judgments and assumptions used are reasonable based upon information available at the time they are made. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

U.S. dollars in thousands, except share and per share data

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

b. Financial statements in U.S. dollars:

The majority of the revenues of the Company and its subsidiaries are generated in U.S. dollars ("dollar") or linked to the dollar. In addition, a major portion of the Company's and certain of its subsidiaries' costs are incurred or determined in dollars. The Company's management believes that the dollar is the currency of the primary economic environment in which the Company and its subsidiaries operate. Thus, the functional and reporting currency of the Company and its subsidiaries is the dollar.

Accordingly, monetary accounts maintained in currencies other than the dollar are remeasured into U.S. dollars in accordance with Accounting Standards Codification No. 830, "Foreign Currency Matters" ("ASC No. 830"). All transactions gains and losses from the remeasurement of monetary balance sheet items are reflected in the statements of operations as financial income or expenses as appropriate.

c. Principles of consolidation:

The consolidated financial statements include the accounts of the Company and its subsidiaries. Intercompany balances and transactions have been eliminated upon consolidation.

d. Cash and cash equivalents:

The Company considers all unrestricted highly liquid investments which are readily convertible into cash, with maturity of three months or less at the date of acquisition, to be cash equivalents.

e. Restricted cash and deposits:

The restricted cash and deposits are held in favor of financial institutions in respect of fulfillments of forward contract and operating obligations.

f. Short-term bank deposits:

Short-term bank deposits are deposits with maturities of more than three months but less than one year. The deposits are in dollars, New Israeli Shekels ("NIS") and Euros, and bear interest at annual weighted average rate of 0.51% and 1.1% at December 31, 2013 and 2012 respectively.

U.S. dollars in thousands, except share and per share data

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

g. Marketable securities:

The Company accounts for investments in Marketable securities in accordance with ASC 320, "Investments - Debt and Equity Securities". Management determines the appropriate classification of its investments in debt securities at the time of purchase and re-evaluates such determinations at each balance sheet date.

Marketable securities classified as "available-for-sale" are carried at fair value, based on quoted market prices. Unrealized gains and losses are reported in a separate component of shareholders' equity in accumulated other comprehensive income (loss). Gains and losses are recognized when realized, on a specific identification basis, in the Company's consolidated statements of comprehensive income.

The Company's securities are reviewed for impairment in accordance with ASC 320-10-65. If such assets are considered to be impaired, the impairment charge is recognized in earnings when a decline in the fair value of its investments below the cost basis is judged to be Other-Than-Temporary Impairment (OTTI). Factors considered in making such a determination include the duration and severity of the impairment, the reason for the decline in value, the potential recovery period and the Company's intent to sell, including whether it is more likely than not that the Company will be required to sell the investment before recovery of cost basis. Based on the above factors, the Company concluded that unrealized losses on its available-for-sale securities, for the years ended 2013, 2012 and 2011, were not OTTI.

h. Inventories:

Inventories are stated at the lower of cost or market value. Inventory write-offs are provided to cover risks arising from slow-moving items, technological obsolescence, excess inventory and discontinued products. Inventory write-off as of December 31, 2013, 2012 and 2011 totaled $ 1,835, $ 1,385 and $ 1,714, respectively.

Cost is determined as follows:

Raw materials and Finished goods – weighted average cost method

i. Property and equipment:

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is calculated by the straight-line method over the estimated useful lives of the assets at the following annual rates:

	%
Lab equipment	25 - 33
Computers and peripheral equipment	15 - 33
Office furniture	6 - 15

Leasehold improvements	By the shorter of term of the lease or the useful life of the asset

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

j. Goodwill impairment:

Goodwill represents the excess of the purchase price over the fair value of net assets of purchased businesses. Under Accounting Standards Codification No. 350, "Intangibles-Goodwill and Other" ("ASC No. 350"), goodwill is not amortized, but rather subject to an annual impairment test, or more often if there are indicators of impairment present. In accordance with ASC No. 350 the Company performs an annual impairment test at December 31 each year. The first step, identifying a potential impairment, compares the fair value of the reporting unit with its carrying amount. If the carrying amount exceeds its fair value, the second step would need to be performed; otherwise, no further step is required. The second step, measuring the impairment loss, compares the implied fair value of the goodwill with the carrying amount of the goodwill. Any excess of the goodwill carrying amount over the applied fair value is recognized as an impairment loss, and the carrying value of goodwill is written down to fair value.

The Company operates in a single reportable unit. The Company has performed an annual impairment analysis as of December 31, 2013 and determined that the carrying value of the reporting unit was less than the fair value of the reporting unit. Fair value is determined using market capitalization. During years 2013, 2012 and 2011 no impairment losses were recorded.

k. Impairment of long lived assets and intangible assets subject to amortization:

Property and equipment and intangible assets subject to amortization are reviewed for impairment in accordance with ASC No. 360, "Accounting for the Impairment or Disposal of Long-Lived Assets," 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.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

Intangible assets acquired in a business combination are recorded at fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets that are not considered to have an indefinite useful life are amortized over their estimated useful lives. Some of the acquired intangible assets are amortized over their estimated useful lives in proportion to the economic benefits realized. This accounting policy results in accelerated amortization of such customer relationships as compared to the straight-line method. All other intangible assets are amortized over their estimated useful lives on a straight-line basis.

During 2011, 2012 and 2013, no impairment losses were recorded.

l. Revenue recognition:

The Company generates revenues mainly from selling its products along with related maintenance and support services. At times, these arrangements may also include professional services, such as installation services or training. The Company generally sells its products through resellers, distributors, OEMs and system integrators, all of whom are considered end-users.

Revenues from product sales are recognized when persuasive evidence of an agreement exists, title and risk of loss have transferred, no significant performance obligations remain, product payment is not contingent upon performance of installation or service obligations, the fee is fixed or determinable and collectability is probable. In instances where final acceptance of the product or service is specified by the customer, revenue recognition is deferred until all acceptance criteria have been met.

Maintenance and support related revenues included in multiple element arrangements are deferred and recognized on a straight-line basis over the term of the applicable maintenance and support agreement. Other services are recognized upon the completion of installation or when the service is provided. In instances where the services provided in a multiple element arrangement are considered essential to the functionality of the product and payment of the product is contingent upon performance of the services, the sales of the products and services would be considered one unit of accounting.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

In October 2009, the FASB issued ASU 2009-14, "Certain Arrangements That Include Software Elements, (amendments to ASC Topic 985, Software)" (ASU 2009-14). Tangible products containing software components and non-software components that function together to deliver the tangible product's essential functionality is no longer within the scope of the software revenue guidance in Subtopic 985-605 of the Codification. Accordingly, the Company was considered outside the scope of Subtopic 985-605. For 2011 and future periods, pursuant to the guidance of ASU 2009-13, "Multiple-Deliverable Revenue Arrangements, (amendments to ASC Topic 605, Revenue Recognition)" (ASU 2009-13) and ASU 2009-14, when a sales arrangement contains multiple elements, such as products and services, the Company allocates revenues to each element based on a selling price hierarchy. The selling price for a deliverable is based on VSOE if available, third party evidence ("TPE") if VSOE is not available, or estimated selling price ("ESP") if neither VSOE nor TPE is available. In multiple element arrangements, revenues are allocated to each separate unit of accounting for each of the deliverables using the relative selling prices of each of the deliverables in the arrangement based on the aforementioned selling price hierarchy.

Revenues arrangements with multiple deliverables are allocated using the relative selling price method. The Company determines the best estimated selling price ("BESP") in multiple elements arrangements as follows:

For the products the Company determine the "BESP" – it is based on management ESP by reviewing historical transactions and considering multiple other factors, including but not limited to, pricing practices including discounting, and competition.

As of January 1, 2011, the Company changed its pricing policy in respect of the sale of maintenance and support in new, multiple element arrangements. For the maintenance and support under the new pricing policy, the Company determined the ESP for the year ended December 31, 2011 in multiple-element arrangements based on reviewing historical transactions, and considering several other external and internal factors including, but not limited to, pricing practices including discounting and competition.

For the year ended December 31, 2013 and 2012, for maintenance and support, the Company determined the selling price based on VSOE of the price charged based on standalone sales (renewals) of such elements using a consistent percentage of the Company's product price lists in the same territories.

Deferred revenues are classified as short and long term based on their contractual term and recognized as revenues at the time the respective elements are provided

U.S. dollars in thousands, except share and per share data

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

The Company records a provision for estimated product returns and stock rotation based on its experience with historical product returns, stock rotations and other known factors. Such provisions amounted to $ 892 and $ 785 as of December 31, 2013 and 2012, respectively.

m. Advertising expenses:

Advertising expenses are charged to the statement of operations, as incurred. Advertising expenses for the years ended December 31, 2013, 2012 and 2011 amounted to $ 973, $ 1,002 and $ 885, respectively.

n. Research and development costs:

Accounting Standards Codification No. 985-20, 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 the completion of a working model. The Company does not incur material costs between the completion of a working model and the point at which the products are ready for general release. Therefore, research and development costs are charged to the consolidated statement of operations as incurred.

o. Severance pay:

The liability in Israel for substantially all of the Company`s employees in respect of severance pay liability is calculated in accordance with Section 14 of the Severance Pay Law -1963 (herein- "Section 14"). Section 14 states that Company's contributions for severance pay shall be in line of severance compensation and upon release of the policy to the employee, no additional obligations shall be conducted between the parties regarding the matter of severance pay and no additional payments shall be made by the Company to the employee.

Furthermore, the related obligation and amounts deposited on behalf of such obligation under Section 14, are not stated on the balance sheet, because pursuant to current ruling, they are legally released from obligation to employees once the deposits have been paid.

There are a limited number of employees in Israel, for whom the Company is liable for severance pay. The Company's liability for severance pay for its Israeli employees was calculated pursuant to Section 14, based on the most recent monthly salary of its Israeli employees multiplied by the number of years of employment as of the balance sheet date for such employees.

ALLOT COMMUNICATIONS LTD.

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 liability was partly provided by monthly deposits with severance pay funds and insurance policies and the remainder by an accrual.

Severance expense for the years ended December 31, 2013, 2012 and 2011, amounted to $ 2,139, $ 1,486 and $ 1,280, respectively.

p. Accounting for stock-based compensation:

The Company accounts for stock based compensation in accordance with Accounting Standards Codification No. 718, "Compensation - Stock Compensation" ("ASC No. 718") that requires companies to estimate the fair value of equity-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as an expense over the requisite service periods in the Company's consolidated statement of operations.

ASC No. 718 requires forfeitures to be estimated at the time of the grant and revised in subsequent periods if actual forfeitures differ from those estimates.

The following table sets forth the total stock-based compensation expense resulting from stock options granted to employees included in the consolidated statements of operations, for the years ended December 31, 2013, 2012 and 2011:

	Year ended December 31,		
	2013	2012	2011
Cost of revenues	$ 368	$ 222	$ 103
Research and development	1,666	1,186	442
Sales and marketing	3,106	2,060	1,001
General and administrative	2,591	1,349	710
Total stock-based compensation expense	$ 7,731	$ 4,817	$ 2,256

The Company selected the binomial option pricing model as the most appropriate fair value method for its stock-based compensation awards with the following assumptions for the years ended December 31, 2013, 2012 and 2011:

	Year ended December 31,		
	2013	2012	2011
Suboptimal exercise multiple	3	2.5-3.5	2.5-3.5
Risk free interest rate	0.1%-2.77%	0.15%-1.39%	0.11%-5.46%
Volatility	53%-63 %	51%-66 %	50%-53 %
Dividend yield	0 %	0 %	0 %

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

The expected annual post-vesting and pre-vesting forfeiture rates affects the number of exercisable options. Based on the Company's historical experience, the annual post-vesting and pre-vesting forfeiture rates are 0%-5.7%.

The computations of expected volatility and suboptimal exercise multiple are based on the average of the Company's realized historical stock price volatility based on market capitalization and type of technology platform. The computation of the suboptimal exercise multiple and the forfeiture rates are based on the grantees expected exercise prior and post vesting termination behavior. The interest rate for period within the contractual life of the award is based on the U.S. Treasury Bills yield curve in effect at the time of grant. The Company currently has no plans to distribute dividends and intends to retain future earnings to finance the development of its business.

The expected life of the stock options represents the weighted-average period the stock options are expected to remain outstanding and is a derived output of the binomial model. The expected life of the stock options is impacted by all of the underlying assumptions used in the Company's model.

q. Concentration of credit risks:

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, marketable securities, short-term bank deposits, trade receivables and derivative instruments.

The majority of cash and cash equivalents, marketable securities, restricted cash and short-term deposits of the Company are invested in dollar deposits in major U.S. and Israeli banks. Such deposits in the United States may be in excess of insured limits and are not insured in other jurisdictions. Generally, the cash and cash equivalents and short-term bank deposits may be redeemed upon demand, and therefore, bear minimal risk.

The Company's trade receivables are primarily derived from sales to customers located mainly in the United States, as well as in EMEA, APAC and Latin America. Concentration of credit risk with respect to trade receivables is limited by credit limits, ongoing credit evaluation and account monitoring procedures. The Company performs ongoing credit evaluations of its customers and establishes an allowance for doubtful accounts on a specific basis. Allowance for doubtful accounts amounted to $ 441 and $ 280 as of December 31, 2013 and 2012, respectively.

The Company has no significant off balance sheet concentrations of credit risk, except for hedging arrangements to cover the currency exposure on identified cash flow items (see also Note 2w).

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

r. Grants from the OCS:

Participation grants from the Office of the Chief Scientist of the Ministry of Industry, Trade and Labor in Israel ("OCS") for research and development activity are recognized at the time the Company is entitled to such grants on the basis of the costs incurred and included as a deduction of research and development costs. Research and development grants recognized amounted to $ 1,051, $ 2,855 and $ 3,674 in 2013, 2012 and 2011, respectively.

s. Income taxes:

The Company accounts for income taxes in accordance with Accounting Standards Codification No. 740, "Income Taxes" ("ASC No. 740"). ASC No. 740 prescribes the use of the liability method, whereby deferred tax asset and liability account balances are determined based on differences between 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 provides a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value if it is more likely than not that some portion or all of the deferred tax assets will not be realized.

ASC No. 740 contains a two-step approach to recognizing and measuring a liability for uncertain tax positions. The first step is to evaluate the tax position taken or expected to be taken in a tax return by determining if the weight of available evidence indicates that it is more likely than not that, on an evaluation of the technical merits, the tax position will be sustained on audit, including resolution of any related appeals or litigation processes. The second step is to measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement.

t. Basic and diluted net income/loss per share:

Basic net income per share is computed based on the weighted average number of Ordinary Shares outstanding during each year. Diluted net income per share is computed based on the weighted average number of Ordinary Shares outstanding during each year, plus dilutive potential Ordinary Shares considered outstanding during the year, in accordance with FASB ASC 260 "Earnings Per Share".

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

For the years ended December 31, 2013 and 2012, all outstanding options and warrants have been excluded from the calculation of the diluted loss per share since their effect was anti-dilutive. For the year ended December 31, 2011, 577,750 outstanding options and warrants have been excluded from the calculation of the diluted net income per share since their effect was anti-dilutive. See Note 16.

u. Comprehensive income (loss):

The Company accounts for comprehensive income (loss) in accordance with Accounting Standards Codification No. 220, "Comprehensive Income" ("ASC No. 220"). This statement establishes standards for the reporting and display of comprehensive income (loss) and its components in a full set of general purpose financial statements. Comprehensive income (loss) generally represents all changes in shareholders' equity during the period except those resulting from investments by, or distributions to shareholders. The Company determined that its items of comprehensive income (loss) relate to unrealized gains and losses on hedging derivative instruments and unrealized gains and losses on available-for-sale marketable securities.

In May 2011, the FASB issued guidance that changed the requirement for presenting "Comprehensive Income" in the consolidated financial statements. The update requires an entity to present the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011 and should be applied retrospectively. The Company adopted this new guidance on January 1, 2012 and elected to present the comprehensive income in Consolidated Statement of Comprehensive Income.

In February 2013, the FASB issued Accounting Standards Update ("ASU") 2013-02, which requires entities to present information about significant items reclassified out of accumulated other comprehensive income (loss) by component either on the face of the statement where net income is presented or as a separate disclosure in the notes to the financial statements.

ALLOT COMMUNICATIONS LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands, except share and per share data

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

The following table shows the components and the effects on net income of amounts reclassified from Accumulated other comprehensive income as of December 31, 2013:

	Year ended December 31, 2013		
	Unrealized gains (losses) on marketable securities	Unrealized gains (losses) on cash flow hedges	Total
Balance as of December 31, 2012	$ 61	$ 1,699	$ 1,760
Changes in other comprehensive income (loss) before reclassifications	(5)	1,636	1,631
Amounts reclassified from accumulated other comprehensive income to :			
Cost of revenues	-	(184)	(184)
Operating expenses	-	(2,826)	(2,826)
Financial income, net	(15)	-	(15)
Net current-period other comprehensive loss	(20)	(1,374)	(1,394)
Balance as of December 31, 2013	$ 41	$ 325	$ 366

v. Fair value of financial instruments:

The Company measures its cash and cash equivalents, marketable securities, derivative instruments, restricted cash and deposits, short-term bank deposits, trade receivables, other receivables, trade payables and other payables at fair value.

Fair value is an exit price, representing the amount that would be received if the Company were to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or a liability. The Company uses a three-tier value hierarchy, which prioritizes the inputs used in the valuation methodologies in measuring fair value:

Level 1 - Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

The following table shows the components of Accumulated other comprehensive income, net of taxes, as of December 31, 2013:

Level 2 - Include other inputs that are directly or indirectly observable in the marketplace, other than quoted prices included in Level 1, such as quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets with insufficient volume or infrequent transactions, or other inputs that are observable (model-derived valuations in which significant inputs are observable), or can be derived principally from or corroborated by observable market data; and

Level 3 - Unobservable inputs which are supported by little or no market activity.

The Company categorized each of its fair value measurements in one of those three levels of hierarchy. The fair value hierarchy also requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

w. Derivatives and hedging:

The Company accounts for derivatives and hedging based on Accounting Standards Codification No. 815, "Derivatives and Hedging" ("ASC No. 815").

The Company accounts for its derivative instruments as either assets or liabilities and carries them at fair value. Derivative instruments that are not designated and qualified as hedging instruments must be adjusted to fair value through earnings.

For derivative instruments that hedge the exposure to variability in expected future cash flows that are designated as cash flow hedges, the effective portion of the gain or loss on the derivative instrument is reported as a component of accumulated other comprehensive income (loss) in shareholders' equity and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of the gain or loss on the derivative instrument is recognized in current earnings. To apply hedge accounting treatment, cash flow hedges must be highly effective in offsetting changes to expected future cash flows on hedged transactions. (See Note 5).

x. Business combinations:

The Company accounts for business combinations in accordance with ASC No. 805. ASC No. 805 requires recognition of assets acquired, liabilities assumed, and any non-controlling interest at the acquisition date, measured at their fair values as of that date. Any excess of the fair value of net assets acquired over the purchase price is recorder as goodwill, any subsequent changes in estimated contingencies are to be recorded in earnings. In addition, changes in valuation allowance related to acquired deferred tax assets and acquired income tax positions are to be recognized in earnings.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 2: SIGNIFICANT ACCOUNTING POLICIES (CONT.)

y. Warranty costs:

The Company generally provides a three months software warranty and a one year hardware warranty for all of its products. A provision is recorded for estimated warranty costs at the time revenues are recognized based on the Company's experience. Warranty expenses for the years ended December 31, 2011, 2012 and 2013 were immaterial.

NOTE 3: AVAILABLE-FOR-SALE MARKETABLE SECURITIES

The following is a summary of available-for-sale marketable securities:

	December 31, 2013				December 31, 2012			
	Amortized cost	Gross unrealized gain	Gross unrealized loss	Fair value	Amortized cost	Gross unrealized gain	Gross unrealized loss	Fair value
Available-for-sale - matures within one year:								
Governmental debentures	$-	$ -	$ -	$-	$200	$ 1	$ -	$201
Corporate debentures	3,921	7	-	3,928	3,701	12	-	3,713
	3,921	7	-	3,928	3,901	13	-	3,914
Available-for-sale - matures after one year through three years:								
Governmental debentures	1,673	4	(1)	1,676	933	4	(4)	933
Corporate debentures	35,163	77	(46)	35,194	9,946	48	-	9,994
	36,836	81	(47)	36,870	10,879	52	(4)	10,927
	$40,757	$ 88	$ (47)	$40,798	$14,780	$ 65	$ (4)	$14,841

All investments with unrealized loss as of December 31, 2013 are with continuous unrealized losses for less than 12 months.

NOTE 4: FAIR VALUE MEASUREMENTS

In accordance with ASC No. 820, the Company measures its cash equivalents, marketable securities and foreign currency derivative instruments at fair value. Cash equivalents and available for sale marketable securities are classified within Level 1 or Level 2. This is because these assets are valued using quoted market prices or alternative

pricing sources and models utilizing market observable inputs.

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NOTE 4: FAIR VALUE MEASUREMENTS (CONT.)

The Company's financial assets measured at fair value on a recurring basis, including accrued interest components, consisted of the following types of instruments as of December 31, 2013 and 2012, respectively:

	As of December 31, 2013 Fair value measurements using input type			
	Level 1	Level 2	Level 3	Total
Available-for-sale marketable securities	$ -	$ 40,798	$ -	$ 40,798
Foreign currency derivative contracts	-	264	-	264
Total financial assets	$ -	$ 41,062	$ -	$ 41,062

	As of December 31, 2012 Fair value measurements using input type			
	Level 1	Level 2	Level 3	Total
Available-for-sale marketable securities	$ -	$ 14,841	$ -	$ 14,841
Foreign currency derivative contracts	-	1,624	-	1,624
Total financial assets	$ -	$ 16,465	$ -	$ 16,465

NOTE 5: DERIVATIVE INSTRUMENTS

The Company enters into hedge transactions with a major financial institution, using derivative instruments, primarily forward contracts and options to purchase and sell foreign currencies, in order to reduce the net currency exposure associated with anticipated expenses (primarily salaries and related expenses) in currencies other than U.S. dollar, and forecasted revenues denominated in Euro. The net losses (income) recognized in "Financial income, net" during the years ended December 31, 2013, 2012 and 2011 were $ 181, $ (231) and $ 230, respectively.

The Company currently hedges such future exposures for a maximum period of one year. However, the Company may choose not to hedge certain foreign currency exchange exposures for a variety of reasons, including but not limited to immateriality, accounting considerations and the prohibitive economic cost of hedging particular exposures. There can be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in foreign currency exchange rates.

U.S. dollars in thousands, except share and per share data

NOTE 5: DERIVATIVE INSTRUMENTS (CONT.)

The Company records all derivatives on the consolidated balance sheets at fair value in accordance with ASC No. 820 at Level 2. The effective portions of cash flow hedges are recorded in other comprehensive income until the hedged item is recognized in earnings. The ineffective portions of cash flow hedges are adjusted to fair value through earnings in financial other income or expense. The Company does not enter into derivative transactions for trading purposes.

The Company had a net unrealized gain (loss) associated with cash flow hedges of $ 325 and $ 1,699 recorded in other comprehensive income (loss) as of December 31, 2013 and 2012, respectively.

As of December 31, 2013 and 2012, the Company had outstanding forward contracts in the amount of $ 14,904 and $ 33,938, respectively.

The fair value of the outstanding foreign exchange contracts recorded by the Company on its consolidated balance sheets as of December 31, 2013 and 2012, as an asset is as follows:

Foreign exchange forward and options contracts	Balance sheet	December 31, 2013	December 31, 2012
Fair value of foreign exchange forward contracts, net	Other receivables and prepaid expenses	325	1,699
Total derivatives designated as hedging instrument		$ 325	$ 1,699
Total derivatives not designated as hedging instruments, net	Other payables and accrued expenses	$ (61)	$ (75)

Gain or loss on the derivative instruments, which partially offset the foreign currency impact from the underlying exposures, reclassified from other comprehensive income to operating expenses for the years ended December 31, 2013 and 2012 were $ 3,010 and $ 748, respectively.

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NOTE 5: DERIVATIVE INSTRUMENTS (CONT.)

Non-designated hedges:

The Company also uses foreign currency forward contracts to mitigate variability in gains and losses generated from the re-measurement of certain monetary assets and liabilities denominated in foreign currencies. These derivatives do not qualify for special hedge accounting treatment. These derivatives are carried at fair value with changes recorded in financial income (expense), net. Changes in the fair value of these derivatives are largely offset by re-measurement of the underlying assets and liabilities. Cash flows from such derivatives are classified as operating activities. The derivatives have maturities of approximately twelve months.

NOTE 6: OTHER RECEIVABLES AND PREPAID EXPENSES

	December 31,	
	2013	2012
Prepaid expenses	$ 5,815	$ 2,772
Government authorities	1,540	1,284
Short-term lease deposits	282	211
Foreign currency derivative contracts	325	1,702
Grants receivable from the OCS	94	224
Others	162	622
	$ 8,218	$ 6,815

NOTE 7: INVENTORIES

	December 31,	
	2013	2012
Raw materials	$ 3,693	$ 2,371
Finished products	10,105	7,592
	$ 13,798	$ 9,963

As of December 31, 2013 and 2012, the finished products line item above includes deferral of the cost of goods sold for which revenue was not yet recognized in the amount of approximately $ 3,436 and $ 1,200, respectively.

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NOTE 8: PROPERTY AND EQUIPMENT, NET

	December 31,	
	2013	2012
Cost:		
Lab equipment	$ 9,967	$ 8,134
Computers and peripheral equipment	17,405	16,910
Office furniture and equipment	675	606
Leasehold improvements	674	703
	28,721	26,353
Accumulated depreciation:		
Lab equipment	6,676	5,093
Computers and peripheral equipment	15,293	13,770
Office furniture and equipment	398	358
Leasehold improvements	480	523
	22,847	19,744
Depreciated cost	$ 5,874	$ 6,609

Depreciation expense for the years ended December 31, 2013, 2012 and 2011 was $ 3,423, $ 3,120 and $ 2,754, respectively.

NOTE 9: INTANGIBLE ASSETS, NET

a. The following table shows the Company's intangible assets for the periods presented:

		December 31,	
	Weighted average remaining useful life	2013	2012
Original Cost:			
Technology	6.1	$ 10,725	$ 11,451
Backlog	1.0	1,491	2,401
Customer relationships	2.5	899	899
		$ 13,115	$ 14,751
Accumulated amortization:			

Technology	6.1	$ 2,103	$ 1,217
Backlog	1.0	1,330	1,168
Customer relationships	2.5	275	44
		$ 3,708	$ 2,429
Amortized cost		$ 9,407	$ 12,322

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 9: INTANGIBLE ASSETS, NET (CONT.)

b. Amortization expense for the years ended December 31, 2013, 2012 and 2011 was $ 2,915, $ 1,947 and $ 124, respectively.

c. Estimated amortization expense for the years ending:

Year ending December 31,	
2014	$ 1,912
2015	1,718
2016	1,621
2017	1,489
Thereafter	2,667
Total	$ 9,407

NOTE 10: OTHER PAYABLES AND ACCRUED EXPENSES

	December 31,	
	2013	2012
Accrued expenses	$ 3,806	$ 3,887
Foreign currency derivative contracts	61	78
Contingent consideration payable	-	1,088
Accrual taxes	824	409
Others	86	303
	$ 4,777	$ 5,765

NOTE 11: COMMITMENTS AND CONTINGENT LIABILITIES

a. Royalties:

The Company receives research and development grants from the OCS. Until the end of 2012, the Company was participating in programs sponsored by the Israeli Government for the support of research and development activities. As part of this program the Company is obligated to pay royalties to the OCS, amounting to 3.5% of the sales of the sponsored products, up to 100% of the grants received, linked to the U.S. dollar and for grants received after January 1, 1999 also bearing interest at the rate of LIBOR. The obligation to pay these royalties is contingent upon actual sales of products of the Company and in the absence of such sales no payment is required.

U.S. dollars in thousands, except share and per share data

NOTE 11: COMMITMENTS AND CONTINGENT LIABILITIES (CONT.)

During December 2012, the Company recorded a liability for the early payment of $ 15,886 due to settlement with the Israeli Office of Chief Scientist (OCS), representing the full balance of the contingent liability related to grants received (including interest), which was fully paid during 2013. Upon making this payment, the Company eliminated all future royalty obligations related to its anticipated revenues. These expenses were included in the cost of revenues in the consolidated statement of operations.

For the years ended December 31, 2013, 2012 and 2011, the royalties expense paid and accrued, as part of the Company's cost of revenues, was $ 250, $ 17,703 and $ 2,746 respectively.

From 2013, the Company is qualified to participate in an approved program with the OCS for companies with large research and development activities and certain threshold of revenues. Under this program the Company is eligible to receive grants that do not require repayments.

b. Lease commitments:

In March 2013, the Company signed an agreement to rent offices for an average period of five years, starting July 2013. The total rental expenses are approximately $ 155 per month.

The U.S. subsidiary has an operating lease for office facilities in Woburn, Massachusetts and in San Diego, California, the lease expires on August 31, 2019 and on April 30, 2018 respectively. The Company's subsidiaries maintain smaller offices in South Africa, China, Singapore, Japan, New Zealand, UK and various locations in Europe.

In addition, the Company has operating lease agreements for its motor vehicles, which terminate in 2014 through 2016.

Operating leases (offices and motor vehicles) expense for the years ended December 31, 2013, 2012 and 2011 was $ 3,273, $ 2,345 and $ 2,415, respectively.

As of December 31, 2013, the aggregate future minimum lease obligations (offices and motor vehicles) under non-cancelable operating leases agreements were as follows:

Year ending December 31,	
2014	$ 2,908
2015	2,156
2016	1,836
2017	1,736
Thereafter	905
Total	$ 9,541

U.S. dollars in thousands, except share and per share data

NOTE 11: COMMITMENTS AND CONTINGENT LIABILITIES (CONT.)

c. Major subcontractor:

The Company currently depends on one subcontractor to manufacture and provide hardware, warranty and support for its traffic management systems. If the subcontractor experiences delays, disruptions, quality control problems or a loss in capacity, shipments of products may be delayed and the Company's ability to deliver products could be materially adversely affected. Certain hardware components for the Company's products come from single or limited sources, and the Company could lose sales if these sources fail to satisfy its supply requirements. In the event that the Company terminates its business connection with the subcontractor, it will have to compensate the subcontractor for certain inventory costs, as specified in the agreement with the subcontractor.

d. Purchase commitments:

At December 31, 2013, the Company had approximately $ 1,167 off-balance non-cancelable purchase commitments with its suppliers.

NOTE 12: SHAREHOLDERS' EQUITY

a. Company's shares:

As of December 31, 2013, the Company's authorized share capital consists of NIS 20,000,000 divided into 200,000,000 Ordinary Shares, par value NIS 0.1 per share. Ordinary Shares confer on their holders the right to receive notice to participate and vote in general meetings of the Company, the right to a share in the excess of assets upon liquidation of the Company, and the right to receive dividends, if declared.

b. Stock option plan:

A summary of the Company's stock option activity, pertaining to its option plans for employees and related information is as follows:

	Year ended December 31,					
	2013		2012		2011	
	Number of shares upon exercise	Weighted average exercise price	Number of shares upon exercise	Weighted average exercise price	Number of shares upon exercise	Weighted average exercise price
Outstanding at beginning of year	2,709,910	$ 11.03	3,164,090	$ 5.90	3,427,870	$ 3.81
Granted	764,224	$ 11.52	1,301,455	$ 8.11	649,000	$ 14.31
Forfeited	(254,956)	$ 11.63	(158,718)	$ 12.15	(93,859)	$ 8.57
Exercised	(329,967)	$ 2.85	(1,596,917)	$ 3.72	(818,921)	$ 3.46
Outstanding at end of year	2,889,211	$ 11.96	2,709,910	$ 11.03	3,164,090	$ 5.90
Exercisable at end of year	1,364,620	$ 10.38	819,869	$ 6.62	1,592,432	$ 3.66
Vested and Expected to Vest	2,117,348	$ 11.65	1,686,435	$ 9.86	2,324,031	$ 4.80

U.S. dollars in thousands, except share and per share data

NOTE 12: SHAREHOLDERS' EQUITY (CONT.)

The aggregate intrinsic value represents the total intrinsic value (the difference between the Company's closing stock price on the last trading day of the fiscal year 2013 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, 2013. This amount may change based on the fair market value of the Company's stock. The total intrinsic value of options outstanding at December 31, 2013, was $ 14,261. The total intrinsic value of exercisable options at December 31, 2013 was approximately $ 8,321. The total intrinsic value of options vested and expected to vest at December 31, 2013 was approximately $ 10,993.

The total intrinsic value of options exercised during the year ended December 31, 2013 was approximately $ 76,922. The number of options vested during the year ended December 31, 2013 was 874,802. The weighted-average remaining contractual life of the outstanding options as of December 31, 2013 is 8.27 years. The weighted-average remaining contractual life of exercisable options as of December 31, 2013 is 6.92 years.

As of December 31, 2013, $ 15,770 unrecognized compensation cost related to stock options is expected to be recognized over a weighted average vesting period of 2.13 years.

The options outstanding as of December 31, 2013, have been classified by exercise price, as follows:

Exercise price	Shares upon exercise of options outstanding as of December 31, 2013	Weighted average remaining contractual life Years	Shares upon exercise of options exercisable as of December 31, 2013
$ 23.31-27.58	456,969	8.57	153,876
$ 16.82-17.07	317,410	7.96	148,099
$ 11.32-15.43	1,024,648	8.43	323,948
$ 5.25-9.25	256,401	6.63	221,876
$ 0-4.95	833,783	8.54	516,821
	2,889,211		1,364,620

U.S. dollars in thousands, except share and per share data

NOTE 12: SHAREHOLDERS' EQUITY (CONT.)

The Company has two option plans under which outstanding options as of December 31, 2013, are as follows: (i) under the 2003 option plan, the outstanding options are exercisable for 4,681 Ordinary shares, and (ii) under the 2006 option plan, the outstanding options are exercisable for 2,884,530 Ordinary shares.

Under the terms of the above option plans, options may be granted to employees, officers, directors and various service providers of the Company and its subsidiaries. The options generally become exercisable quarterly over a four-year period, commencing one year after date of the grant, subject to the continued employment of the employee. The options generally expire no later than ten years from the date of the grant. The exercise price of the options at the date of grant under the plans may not be less than the nominal value of the shares into which such options are exercised, any options, which are forfeited or cancelled before expiration, become available for future grants. As of December 31, 2013, 442,881 Ordinary shares are available for future issuance under the option plans.

In 2013, and 2012 the Company granted 75,099 and 436,455 options respectively to Israeli employees with an exercise price in the range of $ 0 - $ 0.03, which was lower than the trading price of the Company's Ordinary Shares quoted on the NASDAQ Global Select Market on the date of the grants.

In addition to granting stock options, the Company granted in 2008 RSUs under the 2006 option plan. RSUs vest over a four year period subject to the continued employment of the employee. RSUs that are cancelled or forfeited become available for future grants.

NOTE 13: TAXES ON INCOME

a. Corporate tax rates:

The Israeli corporate tax rate was 24% in 2011 and 25% in 2012 and 2013.

On July 30, 2013, the Israeli Parliament passed a law, which, among other things, was designated to increase the tax levy for years 2013 and 2014 (the "New Law"). The New Law increases the Israeli corporate tax rate from 25% to 26.5%. However, the effective tax rate payable by a company that derives income from an Approved Enterprise, a Preferred Enterprise or a Beneficiary Enterprise (as discussed below) may be considerably less. Capital gains derived by an Israeli company are generally subject to the prevailing corporate tax rate.

b. Foreign Exchange Regulations:

Commencing in taxable year 2013, the Company has elected to measure its taxable income and file its tax return under the Israeli Income Foreign Tax Regulations. Under the Foreign Exchange Regulations, an Israeli company must calculate its tax liability in U.S. Dollars according to certain orders. The tax liability, as calculated in U.S. Dollars is translated into NIS according to the exchange rate as of December 31st of each year.

NOTE 13: TAXES ON INCOME (CONT.)

c. Tax benefits under Israel's law for the Encouragement of Capital Investments, 1959 ("the Law"):

In 1998, the production facilities of the Company related to its computational technologies were granted the status of an "Approved Enterprise" under the Law. In 2004, expansion program was granted the status of "Approved Enterprise". According to the provisions of the Law, the Company has elected the alternative package of benefits and has waived Government grants in return for tax benefits.

According to the provisions of the Law, the Company's income is tax-exempt for a period of two years commencing with the year it first earns taxable income, and subject to corporate taxes at the reduced rate of 10% to 25%, for an additional period of five to eight years depending upon the level of foreign ownership of the Company. As of December 31, 2013 the benefit period of tax benefit has not yet commenced, since the Company has not yet utilized all its carry forward losses.

The period of tax benefits, detailed above, is limited to the earlier of 12 years from the commencement of production, or 14 years from the approval date.

The Law was significantly amended effective April 1, 2005 ("the Amendment"). The Amendment includes revisions to the criteria for investments qualified to receive tax benefits as a Beneficiary Enterprise and among other things, simplifies the approval process. The Amendment applies to new investment programs. Therefore, investment programs commencing after December 31, 2004, do not affect the approved programs of the Company.

In addition, the Law provides that terms and benefits included in any letter of approval already granted will remain subject to the provisions of the Law as they were on the date of such approval. Therefore, the Company's existing Approved Enterprise will generally not be subject to the provisions of the Amendment. The Company elected 2006 and 2009 as "year of election" under the Amendment.

The entitlement to the above benefits is contingent upon the fulfillment of the conditions stipulated in the Law, regulations published there under and the criteria set forth in the specific letters of approval. In the event of failure to comply with these conditions, the benefits may be canceled and the Company may be required to refund the amount of the benefits, in whole or in part, including interest and linked to changes in the Israeli CPI. As of December 31, 2013, management believes that the Company is meeting the aforementioned conditions.

NOTE 13: TAXES ON INCOME (CONT.)

If the Company pays a dividend out of income derived from the Approved and Beneficiary Enterprise during the tax exemption period, it will be subject to corporate tax in respect of the gross amount distributed, including any taxes thereon, at the rate which would have been applicable had it not enjoyed the alternative benefits, generally 10%-25%, depending on the percentage of the Company's Ordinary shares held by foreign shareholders. The dividend recipient is subject to withholding tax at the rate of 15% applicable to dividends from approved enterprises, if the dividend is distributed during the tax exemption period or within twelve years thereafter. The Company currently has no plans to distribute dividends and intends to retain future earnings to finance the development of its business.

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

As of January 1, 2011 new legislation amending to the Investment Law came into effect (the "2011 Amendment"). The 2011 Amendment introduced a new status of "Preferred Company" and "Preferred Enterprise", replacing the existed status of "Beneficiary Company" and "Beneficiary Enterprise". Similarly to "Beneficiary Company", a Preferred Company is an industrial company owning a Preferred Enterprise which meets certain conditions (including a minimum threshold of 25% export). However, under this new legislation the requirement for a minimum investment in productive assets was cancelled.

Under the 2011 Amendment, a uniform corporate tax rate will apply to all qualifying income of the Preferred Company, as opposed to the former law, which was limited to income from the Approved Enterprises and Beneficiary Enterprise during the benefits period. The uniform corporate tax rate will be 7 % in areas in Israel designated as Development Zone A and 12.5% elsewhere in Israel during 2013, 9% in development Zone A and 16% elsewhere in Israel, respectively, in 2014.

A dividend distributed from income which is attributed to a Preferred Enterprise/Special Preferred Enterprise will be subject to withholding tax at source at the following rates: (i) Israeli resident corporation – 0%, (ii) Israeli resident individual – 15% in 2013 and 20% as of 2014 (iii) non-Israeli resident - 15% in 2013 and 20% as of 2014 subject to a reduced tax rate under the provisions of an applicable double tax treaty.

Under the transition provisions of the new legislation, the Company may decide to irrevocably implement the new law while waiving benefits provided under the current law or to remain subject to the current law. The Company intends to implement the new law in 2016.

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NOTE 13: TAXES ON INCOME (CONT.)

e. Tax benefits under the law for the Encouragement of Industry (Taxes), 1969 (the "Encouragement Law"):

The Encouragement Law, provides several tax benefits for industrial companies. An industrial company is defined as a company resident in Israel, at least 90% of the income of which in a given tax year exclusive of income from specified 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.

Management believes that the Company is currently qualified as an "industrial company" under the Encouragement Law and as such, enjoys tax benefits, including: (1) deduction of purchase of know-how and patents and/or right to use a patent over an eight-year period; (2) the right to elect, under specified conditions, to file a consolidated tax return with additional related Israeli industrial companies and an industrial holding company; (3) accelerated depreciation rates on equipment and buildings; and (4) expenses related to a public offering on the Tel-Aviv Stock Exchange and on recognized stock markets outside of Israel, are deductible in equal amounts over three years.

Eligibility for benefits under the Encouragement Law is not subject to receipt of prior approval from any Governmental authority. No assurance can be given that the Israeli tax authorities will agree that the Company qualifies, or, if the Company qualifies, then the Company will continue to qualify as an industrial company or that the benefits described above will be available to the Company in the future.

f. Pre-tax income (loss) is comprised as follows:

	Year ended December 31,		
	2013	2012	2011
Domestic	$ (6,556)	$ (2,372)	$ 9,737
Foreign	219	(5,292)	(983)
	$ (6,337)	$ (7,664)	$ 8,754

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NOTE 13: TAXES ON INCOME (CONT.)

g. A reconciliation of the theoretical tax expenses (benefit), assuming all income is taxed at the statutory tax rate applicable to the income of the Company and the actual tax expenses (benefit) is as follows:

	Year ended December 31,		
	2013	2012	2011
Income (loss) before taxes on income	$ (6,337)	$ (7,664)	$ 8,754
Theoretical tax expense (benefit) computed at the Israeli statutory tax rate (25%, 25% and 24% for the years 2013, 2012 and 2011, respectively)	$ (1,584)	$ (1,916)	$ 2,101
Creation (Utilization) of valuation allowance	931	(1,554)	(4,328)
Increase (decrease) in losses and temporary differences due to change in Israeli corporate " and Approved Enterprise" tax	3,056	(7,073)	5,419
Increase (decrease) in valuation allowance related to losses and temporary differences due to change in Israeli corporate " and Approved Enterprise" tax	(3,056)	7,073	(5,419)
Taxes with respect to prior years	-	2	(84)
Impairment (recording) of withholding tax asset	-	-	221
Increase in deferred tax assets related to losses and temporary differences due to changes in tax rates and different basis of measurement	(594)		
Non-deductible expenses and other	(223)	1,699	(27)
Non-deductible share-based compensation expenses	1,590	833	541
Exchange rate differences	-	10	1,521
Actual tax expenses (benefit)	$ 120	$ (926)	$ (55)

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NOTE 13: TAXES ON INCOME (CONT.)

h. Income tax expense (tax benefit) is comprised as follows:

	Year ended December 31,		
	2013	2012	2011
Current taxes (benefit)	$ 408	$ (2)	$ 31
Deferred taxes benefit	(288)	(926)	(223)
Taxes in respect of previous years	-	2	(84)
Impairment (recording) of withholding tax asset	-	-	221
	$ 120	$ (926)	$ (55)

i. Net operating losses carry forward:

The Company has accumulated losses for tax purposes as of December 31, 2013, in the amount of approximately $ 39,800, which may be carried forward and offset against taxable income in the future for an indefinite period. In light of the merger between the Company and Oversi as of December 31, 2012, the net operating losses may be offset against taxable income annually with limitation of up to 20% of the total accumulated losses but no more than 50% of the Company's taxable income. In addition, the Company has accumulated capital losses for tax purposes as of December 31, 2013, in the amount of approximately $ 27,300, which may be carried forward and offset against taxable capital gains in the future for an indefinite period, but are limited as stated above. Management currently believes that since the Company has a history of losses, and uncertainty with respect to future taxable income, it is more likely than not that some of the deferred tax assets regarding the loss carry forwards will not be utilized in the foreseeable future. Thus, a valuation allowance was provided to reduce deferred tax assets to their realizable value.

The U.S. subsidiary has accumulated losses for U.S. federal income tax return purposes of approximately $ 4,977. The federal accumulated losses for tax purposes expire between 2024 and 2032. The state accumulated losses for tax purposes begin to expire in 2014. An amount of $ 1,519 of the net operating loss carry-forwards relates to excess tax deductions from stock options.

Such losses are subject to limitations of Internal Revenue Code, Section 382, which in general provides that utilization of net operating losses is subject to an annual limitation if an ownership change results from transactions increasing the ownership of certain shareholders or public groups in the stock of a corporation by more than 50 percentage points over a three-year period. The annual limitations may result in the expiration of losses before utilization.

The European subsidiary is subject to French income taxes and has a net operating loss carry forward amounting as of December 31, 2013 to approximately $ 4,400, which may be carried forward and offset against taxable gains in the future for an indefinite period.

ALLOT COMMUNICATIONS LTD.

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NOTE 13: TAXES ON INCOME (CONT.)

j. 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's deferred income taxes are as follows:

	December 31,	
	2013	2012
Deferred tax assets:		
Operating and capital loss carryforwards	$ 14,567	$ 11,264
Reserves and allowances	785	215
Deferred tax asset before valuation allowance	15,352	11,479
Valuation allowance	(12,736)	(8,749)
Net deferred tax asset	2,616	2,730
Deferred tax liability	(609)	(1,006)
Net deferred tax asset	$ 2,007	$ 1,724

k. As of December 31, 2013 and 2012, the provision in respect of ASC 740 was immaterial. The Company accrues interest and penalties related to the provision in income taxes in its statement of operations. Such interest and penalties were immaterial for all reported periods.

The Company conducts business globally and, as a result, the Company or one or more of its subsidiaries file income tax returns in the U.S. federal jurisdiction and various states and foreign jurisdictions. In the normal course of business, the Company is subject to examination by taxing authorities throughout the world, including such major jurisdictions as Israel, France, and the United States. With few exceptions, the Company is no longer subject to Israeli final tax assessment through the year 2008 and the European and U.S. subsidiaries have final tax assessments through 2009.

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NOTE 14: GEOGRAPHIC INFORMATION

Allot operates in a single reportable segment. Revenues are based on the location of the Company's channel partners which are considered as end customers, as well as direct customers of the Company:

	Year ended December 31,		
	2013	2012	2011
Europe	$ 21,753	$ 39,655	$ 38,409
Asia and Oceania	29,909	21,953	20,195
United States of America	21,350	24,674	9,484
Middle East and Africa	18,210	10,565	2,723
Americas (excluding United States of America)	5,323	7,905	6,942
	$ 96,545	$ 104,752	$ 77,753

The following are the company’s major customers:

	Year ended December 31,		
	2013	2012	2011
Customer A	17 %	14 %	15 %
Customer B	17 %	-	-
Customer C	11 %	-	-
	45 %	14 %	15 %

The following presents total long-lived assets as of December 31, 2013 and 2012:

	December 31,	
	2013	2012
Long-lived assets:		
Israel	$ 27,747	$ 26,976
United States of America	10,514	14,380
Other	207	153
	$ 38,468	$ 41,509

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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NOTE 15: FINANCIAL EXPENSES (INCOME), NET

	Year ended December 31,		
	2013	2012	2011
Financial income:			
Interest income	$ (1,358)	$ (1,746)	$ (661)
Financial expenses:			
Exchange rate differences and other	47	176	95
Amortization/accretion of premium/discount on marketable securities , net	584	212	151
	$ (727)	$ (1,358)	$ (415)

NOTE 16: EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted net earnings (loss) per share:

	Year ended December 31,		
	2013	2012	2011
Numerator:			
Net income (loss)	$ (6,457)	$ (6,738)	$ 8,809
Denominator:			
Weighted average number of shares outstanding used in computing basic net earnings per share	32,680,766	31,959,921	25,047,771
Dilutive effect: stock options	-	-	2,024,101
Total weighted average number of shares used in computing diluted net earnings per share	32,680,766	31,959,921	27,071,872
Basic net earnings (loss) per share	$ (0.20)	$ (0.21)	$ 0.35
Diluted net earnings (loss) per share	$ (0.20)	$ (0.21)	$ 0.33