FORM 20−F

NICE SYSTEMS LTD − NICE

Filed: June 29, 2005 (period: December 31, 2004)

Registration of securities of foreign private issuers pursuant to section 12(b) or (g)

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As filed with the United States Securities and Exchange Commission on June 29, 2005

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20−F

Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended December 31, 2004

Commission file number 0−27466

NICE−SYSTEMS LTD.

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

Israel
(Jurisdiction of incorporation or organization)

8 Hapnina Street, P.O. Box 690, Ra'anana 43107, 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
None	**None**

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

American Depositary Shares, each representing one Ordinary Share, par value one New Israeli Shekel per share

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report: **18,160,535 Ordinary Shares, par value NIS 1.00 Per Share**

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

Yes ☒ No ☐

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

Item 17 ☐ Item 18 ☒

PRELIMINARY NOTE

This annual report contains historical information and forward−looking statements within the meaning of The Private Securities Litigation Reform Act of 1995 with respect to NICE's business, financial condition and results of operations. The words "anticipate," "believe," "estimate," "expect," "intend," "may," "plan," "project" and "should" and similar expressions, as they relate to NICE or its management, are intended to identify forward−looking statements. Such statements reflect the current views and assumptions of NICE with respect to future events and are subject to risks and uncertainties. Many factors could cause the actual results, performance or achievements of NICE to be materially different from any future results, performance or achievements that may be expressed or implied by such forward−looking statements, including, among others, changes in general economic and business conditions, changes in currency exchange rates and interest rates, difficulties or delays in absorbing and integrating acquired operations, products, technologies and personnel, changes in business strategy and various other factors, both referenced and not referenced in this annual report. These risks are more fully described under Item 3, "Key Information – Risk Factors" of this annual report. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated, expected, intended, planned or projected. NICE does not intend or assume any obligation to update these forward−looking statements.

In this annual report, all references to "NICE," "we," "us" or "our" are to NICE Systems Ltd., a company organized under the laws of the State of Israel, and its wholly owned subsidiaries, NICE Systems Inc., NICE Systems GmbH, NICE Systems Canada Ltd., NICE CTI Systems UK Ltd., STS Software Systems (1993) Ltd., NiceEye BV, NICE Systems S.A.R.L., NICE APAC Ltd., NiceEye Ltd., Racal Recorders, Ltd. NICE Interactive Solutions India Private Ltd., Nice Systems Latin America, Inc. and Nice Japan Ltd.

In this annual report, unless otherwise specified or unless the context otherwise requires, all references to "$" or "dollars" are to U.S. dollars and all references to "NIS" are to New Israeli Shekels. Except as otherwise indicated, the financial statements of and information regarding NICE are presented in U.S. dollars.

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PART I

Item 1. <u>Identity of Directors, Senior Management and Advisers</u>.

Not Applicable.

Item 2. <u>Offer Statistics and Expected Timetable</u>.

Not Applicable.

Item 3. <u>Key Information</u>.

Selected Financial Data

The following selected consolidated financial data as of December 31, 2003 and 2004 and for the years ended December 31, 2002, 2003 and 2004 have been derived from our audited consolidated financial statements. These financial statements have been prepared in accordance with generally accepted accounting principles in the United States, or U.S. GAAP, and audited by Kost, Forer, Gabbay & Kasierer, a member of Ernst & Young Global. The consolidated selected financial data as of December 31, 2000, 2001 and 2002 and for the years ended December 31, 2000 and 2001 has been derived from other consolidated financial statements not included in this annual report and have also been prepared in accordance with U.S. GAAP and audited by Kost, Forer, Gabbay & Kasierer, a member of Ernst & Young Global. The selected consolidated financial data set forth below should be read in conjunction with and are qualified by reference to Item 5, “Operating and Financial Review and Prospects” and the consolidated financial statements and notes thereto and other financial information included elsewhere in this annual report.

On March 31, 2004, we sold the net assets of our COMINT/DF military−related business to ELTA Systems Ltd (“ELTA”) for $4 million in cash. The net assets sold include the intellectual property, fixed assets, inventory, and contracts related to the COMINT/DF product line which includes high performance spectral surveillance and direction finding systems that detect, identify, locate, monitor and record transmission sources. The COMINT/DF business is therefore treated as a discontinued operation in our financial statements.

In 2002, 2003 and 2004, the COMINT/DF business generated revenues of approximately $7.2 million, $6.5 million and $0.8 million, respectively, and net income of approximately $1.4 million, $1.5 million and $3.2 million (including gain on disposition), respectively.

	Year Ended December 31,				
	2000	2001	2002	2003	2004
	(in thousands of U.S. dollars, except per share data)				
OPERATING DATA:					
Revenues					
Products	N/A	$ 99,395	$ 127,896	$ 168,055	$ 182,616
Services	N/A	14,474	27,445	56,203	70,027
Total revenues	144,479	113,869	155,341	224,258	252,643
Cost of revenues					
Products	N/A	47,781	55,453	64,231	64,432
Services	N/A	19,446	26,054	42,084	49,876
Total cost of revenues	69,438	67,227	81,507	106,315	114,308
Gross profit	75,041	46,642	73,834	117,943	138,335
Operating expenses:					
Research and development, net	19,002	18,843	17,122	22,833	24,866
Selling and marketing	34,048	33,719	38,743	53,701	62,172
General and administrative	27,900	26,788	23,806	29,840	31,269
Other special charges	7,646	17,862	29,092	7,082	—
Total operating expenses	88,596	97,212	108,763	113,456	118,307
Operating income (loss)	(13,555)	(50,570)	(34,929)	4,487	20,028
Financial income, net	6,188	4,254	3,992	2,034	3,556
Other income (expenses), net	53	(4,846)	(4,065)	292	54
Income (loss) before taxes on income	(7,314)	(51,162)	(35,002)	6,813	23,638
Taxes on income	273	198	350	1,205	2,319
Net income (loss) from continuing operations	(7,587)	(51,360)	(35,352)	5,608	21,319
Net income (loss) from discontinuing operations	2,268	4,565	1,370	1,483	3,236
Net income (loss)	$ (5,319)	$ (46,795)	$ (33,982)	$ 7,091	$ 24,555
Basic earnings (loss) per share:					
Continuing operations	$ (0.62)	$ (3.94)	$ (2.56)	$ 0.35	$ 1.22
Discontinued operations	0.19	0.35	0.10	0.09	0.18
Net earnings (loss)	$ (0.43)	$ (3.59)	$ (2.46)	$ 0.44	$ 1.40
Weighted average number of shares used in computing basic earnings (loss) per share (in thousands)	12,317	13,047	13,795	16,038	17,497
Diluted earnings (loss) per share:					
Continuing operations	$ (0.62)	$ (3.94)	$ (2.56)	$ 0.33	$ 1.14
Discontinued operations	0.19	0.35	0.10	0.09	0.17
Net earnings (loss)	$ (0.43)	$ (3.59)	$ (2.46)	$ 0.42	$ 1.31
Weighted average number of shares used in computing diluted earnings (loss) per share (in thousands)	12,317	13,047	13,795	16,781	18,703

	At December 31,				
	2000	2001	2002	2003	2004
BALANCE SHEET DATA:					
Working capital	$ 117,837	$ 70,572	$ 79,583	$ 56,174	$ 51,428
Total assets	251,489	210,012	236,288	249,415	298,319
Total debt	—	—	24	—	—
Shareholders’ equity	208,577	167,018	154,536	176,831	222,871

Exchange Rate Information

The following table shows, for each of the months indicated, the high and low exchange rates between New Israeli Shekels and U.S. dollars, expressed as shekels per U.S. dollar and based upon the daily representative rate of exchange as reported by the Bank of Israel:

Month	High	Low
May 2005	NIS 4.416	NIS 4.348
April 2005	4.395	4.360
March 2005	4.379	4.299
February 2005	4.392	4.357
January 2005	4.414	4.352
December 2004	4.374	4.308

The following table shows, for periods indicated, the average exchange rate between New Israeli Shekels and U.S. dollars, expressed as shekels per U.S. dollar, calculated based on the average of the exchange rates on the last day of each month during the relevant period as reported by the Bank of Israel:

Year	Average
2004	NIS 4.483
2003	4.512
2002	4.736
2001.	4.220
2000.	4.068

On June 27, 2005, the exchange rate was 4.541 NIS per U.S. dollar as reported by the Bank of Israel.

The effect of exchange rate fluctuations on our business and operations is discussed in Item 5, “Operating and Financial Review and Prospects.”

Capitalization and Indebtedness

Not applicable.

Reasons for the Offer and Use of Proceeds

Not applicable.

Risk Factors

General Business Risks Relating to Our Business Portfolio and Structure

The markets in which we operate are characterized by rapid technological changes and frequent new products and service introductions. We may not be able to keep up with these rapid technological and other changes.

We are operating in several markets, each characterized by rapidly changing technology and evolving industry standards. The introduction of products embodying new technology and the emergence of new industry standards can render existing products obsolete and unmarketable and can exert price pressures on existing products. We anticipate that a number of existing and potential competitors will be introducing new and enhanced products that could adversely affect the competitive position of our products. Our most significant market is the market for voice recording platforms and related enhanced applications (or Voice Platforms and Applications). Voice Platforms and Applications are utilized by entities operating in the contact center, trading floor, public safety and air traffic control segments to capture, store, retrieve and analyze recorded data. The market for our Voice Platforms and Applications is, in particular, characterized by a group of highly competitive vendors that are introducing rapidly changing competitive offerings around evolving industry standards.

Our ability to anticipate changes in technology and industry standards and to successfully develop and introduce new, enhanced and competitive products, on a timely basis, in all the markets where we operate, will be a critical factor in our ability to grow and be competitive. As a result, we expect to continue to make significant expenditures on research and development, particularly with respect to new software applications, which are continuously required in all our business areas. The convergence of voice and data networks and wired and wireless communications could require substantial modification and customization of our current products and business models, as well as the introduction of new products. Further, customer acceptance of these new technologies may be slower than we anticipate. We cannot assure you that the market or demand for our products will grow as rapidly as we expect, or if at all, that we will successfully develop new products or introduce new applications for existing products, that such new products and applications will achieve market acceptance or that the introduction of new products or technological developments by others will not render our products obsolete. In addition, our products must readily integrate with major third party security, telephone, front−office and back−office systems. Any changes to these third party systems could require us to redesign our products, and any such redesign might not be possible on a timely basis or achieve market acceptance. Our inability to develop products that are competitive in technology and price and responsive to customer needs could have a material adverse effect on our business, financial condition and results of operations.

Our business could be materially adversely affected as a result of the risks associated with acquisitions and investments. In particular, we may not succeed in making additional acquisitions or be effective in integrating such acquisitions.

As part of our growth strategy, we have made a number of acquisitions and have made minority investments in complementary businesses, products or technologies. We frequently evaluate the tactical or strategic opportunity available related to complementary businesses, products or technologies. The process of integrating an acquired company's business into our operations and/or of investing in new technologies, may result in unforeseen operating difficulties and large expenditures and may absorb significant management attention that would otherwise be available for the ongoing development of our business. Other risks commonly encountered with acquisitions include the effect of the acquisition on our financial and strategic position and reputation, the failure of the acquired business to further our strategies, the inability to successfully integrate or commercialize acquired technologies or otherwise realize anticipated synergies or economies of scale on a timely basis and the potential impairment of acquired assets. Moreover, there can be no assurance that the anticipated benefits of any acquisition or investment will be realized. Future acquisitions or investments contemplated and/or consummated could result in potentially dilutive issuances of equity securities, the incurrence of debt and contingent liabilities, and amortization expenses related to intangible assets, any of which could have a material adverse effect on our operating results and financial condition. There can be no assurance that we will be successful in making additional acquisitions or effective in integrating such acquisitions into our existing business. In addition, if we consummate one or more significant acquisitions in which the consideration consists, in whole or in part, of ordinary shares or American Depositary Shares (ADSs), representing our ordinary shares, shareholders would suffer dilution of their interests in us. We have also invested in companies which can still be considered in the start−up or development stages. These investments are inherently risky as the market for the technologies or products they have under development are typically in the early stages and may never materialize. We could lose our entire initial investment in these companies.

We have expanded into new markets and may not be able to manage our expansion and anticipated growth effectively.

We have established a sales and service infrastructure in India by recruiting sales and service personnel in order to bring about further growth in revenue in the Asia Pacific market. Also, since 2002 we have been expanding our presence in Europe (mainly in the United Kingdom) and in the Middle East and Africa (the EMEA region) through organic growth and through our acquisition of Thales Contact Solutions (or TCS). The growth in our business in the EMEA region is still in its early stage, and in particular, we are just beginning to develop our digital video business in the EMEA region. We expect continued growth, particularly in connection with the enhancement and expansion of our operations in the EMEA region, as well as in the Asia Pacific region. We may establish additional operations within these regions where growth opportunities are projected to warrant the investment. However, we cannot assure you that our revenues will increase as a result of this expansion or that we will be able to recover the expenses we incurred in effecting the expansion. Our failure to effectively manage our expansion of our sales, marketing, service and support organizations could have a negative impact on our business. To accommodate our global expansion, we are continuously implementing new or expanded business systems, procedures and controls. There can be no assurance that the implementation of such systems, procedures, controls and other internal systems can be completed successfully.

We depend upon outsourcers for the manufacture of our key products. The failure of our product manufacturers to meet our quality or delivery requirements would likely have a material adverse effect on our business, results of operations and financial condition.

In 2002, we entered into a manufacturing agreement with Flextronics Israel Ltd., a subsidiary of Flextronics, a global electronics manufacturing services company. Under this agreement, Flextronics provides us with a comprehensive manufacturing solution that covers all aspects of the manufacture of our products from order receipt to product shipment, including purchasing, manufacturing, testing, configuration, and delivery services. This agreement covered all our products. In addition, in connection with the acquisition of TCS, we entered into a contract manufacturing agreement with Instem Technologies Ltd, a UK company, pursuant to which Instem manufactures all ex−TCS products. Similarly, in connection with the acquisition of Dictaphone’s Communications Recordings Systems division (or CRS), we assumed a contract manufacturing agreement with Dictaphone’s EMS division pursuant to which EMS manufactures all ex−CRS products. As a result of these arrangements, we are now fully dependent on Flextronics, Instem and EMS to process orders and manufacture our products. Consequently, the manufacturing process of our products is not in our control.

We may from time to time experience delivery delays due to the inability of Flextronics, Instem and EMS to consistently meet our quality or delivery requirements and we may experience production interruptions if any of Flextronics, Instem or EMS is for any reason unable to continue the production of our products. Should we have on−going performance issues with our contract manufacturers, the process to move from one contractor to another is a lengthy and costly process that could affect our ability to execute customer shipment requirements and/or might negatively affect revenue and/or costs. If these manufacturers or any other manufacturer were to cancel contracts or commitments with us or fail to meet the quality or delivery requirements needed to satisfy customer orders for our products, we could lose time−sensitive customer orders and have significantly decreased quarterly revenues and earnings, which would have a material adverse effect on our business, results of operations and financial condition.

If we lose our key suppliers, our business may suffer.

Certain components and subassemblies that are used in the manufacture of our existing products are purchased from a single or a limited number of suppliers. In the event that any of these suppliers are unable to meet our requirements in a timely manner, we may experience an interruption in production until an alternative source of supply can be obtained. Any disruption, or any other interruption of a supplier's ability to provide components to us, could result in delays in making product shipments, which could have a material adverse effect on our business, financial condition and results of operations. In addition, some of our major suppliers use proprietary technology and software code that could require significant redesign of our products in the case of a change in vendor. Further, as suppliers discontinue their products, or modify them in manners incompatible with our current use, or use manufacturing processes and tools that could not be easily migrated to other vendors, we could have significant delays in product availability, which would have a significant adverse impact on our results of operations and financial condition.   Although we generally maintain an inventory for some of our components and subassemblies to limit the potential for an interruption and we believe that we can obtain alternative sources of supply in the event our suppliers are unable to meet our requirements in a timely manner, we cannot assure you that our inventory and alternative sources of supply would be sufficient to avoid a material interruption or delay in production and in availability of spare parts.

If we lose our key personnel or cannot recruit additional personnel, our business may suffer.

If our growth continues, we will be required to hire and integrate new employees. Recruiting and retaining qualified engineers and computer programmers to perform research and development and to commercialize our products, as well as qualified personnel to market and sell those products, are critical to our success. As of December 31, 2004, approximately 25% of our employees were devoted to research and product development and 26% were devoted to marketing and sales.   There can be no assurance that we will be able to successfully recruit and integrate new employees. Competition for highly skilled employees may again become high in the technology industry. We may also experience personnel changes as a result of our move from multimedia recording equipment towards business performance solutions. An inability to attract and retain highly qualified employees may have an adverse effect on our ability to develop new products and enhancements for existing products and to successfully market such products, all of which would likely have a material adverse effect on our results of operations and financial position. Our success also depends, to a significant extent, upon the continued service of a number of key management, sales, marketing and development employees, the loss of whom could materially adversely affect our business, financial condition and results of operations.

Operating internationally exposes us to additional and unpredictable risks.

We sell our products throughout the world and intend to continue to increase our penetration of international markets. In 2000, 2001, 2002, 2003 and 2004, approximately 97%, 98%, 98%, 99% and 99%, respectively, of our total sales were derived from sales to customers outside of Israel, and approximately 55%, 48%, 52%, 50% and 44%, respectively, of our total sales were made to customers in North America. A number of risks are inherent in international transactions. Our future results could be materially adversely affected by a variety of factors including changes in exchange rates, general economic conditions, regulatory requirements, tax structures or changes in tax laws, and longer payment cycles in the countries in our geographic areas of operations. International sales and operations may be limited or disrupted by the imposition of governmental controls and regulations, export license requirements, political instability, trade restrictions, changes in tariffs and difficulties in managing international operations. We cannot assure you that one or more of these factors will not have a material adverse effect on our international operations and, consequently, on our business, financial condition and results of operations.

Inadequate intellectual property protections could prevent us from enforcing or defending our intellectual property and we may be subject to liability in the event our products infringe on the proprietary rights of third parties and we are not successful in defending such claims.

Our success is dependent, to a significant extent, upon our proprietary technology. We currently own 20 patents (including 11 in the United States) to protect our technology and we have over 100 applications pending in the United States and other countries. We currently rely on a combination of patent, trade secret, copyright and trademark law, together with non−disclosure and non−competition agreements, as well as third party licenses to establish and protect the technology used in our systems. However, we cannot assure you that such measures will be adequate to protect our proprietary technology, that competitors will not develop products with features based upon, or otherwise similar to our systems, or that third party licenses will be available to us or that we will prevail in any proceeding instituted by us in order to enjoin competitors from selling similar products. Although we believe that our products do not infringe upon the proprietary rights of third parties, we cannot assure you that one or more third parties will not make a contrary claim or that we will be successful in defending such claim.

From time to time, we receive “cease and desist” letters alleging patent infringements. No formal claims or other actions have been filed with respect to such alleged infringements, except for claims filed by Dictaphone (which have since been settled and dismissed) and Witness Systems (described under “—Legal Proceedings” in Item 8 below). We believe that none of these allegations has merit. We cannot assure you, however, that we will be successful in defending against the claims that have been asserted or any other claims that may be asserted. We also cannot assure you that such claims will not have a material adverse effect on our business, financial condition, or operations. Defending infringement claims or other claims could involve substantial costs and diversion of management resources. In addition, to the extent we are not successful in defending such claims, we may be subject to injunctions with respect to the use or sale of certain of our products or to liabilities for damages and may be required to obtain licenses which may not be available on reasonable terms.

We face potential product liability claims against us.

Our products focus specifically on organizations’ business−critical operations. We may be subject to claims that our products are defective or that some function or malfunction of our products caused or contributed to property, bodily or consequential damages. We minimize this risk by incorporating provisions into our distribution and standard sales agreements that are designed to limit our exposure to potential claims of liability. We carry product liability insurance in the amount of $20,000,000 per occurrence and $20,000,000 overall per annum. No assurance can be given that all claims will be covered either by the contractual provisions limiting liability or by the insurance, or that the amount of any individual claim or all claims will be covered by the insurance or that the amount of any individual claim or all claims in the aggregate will not exceed policy coverage limits. A significant liability claim against us could have a material adverse effect on our results of operations and financial position.

We face risks relating to government contracts.

We sell our products to, among other customers, governments and governmental entities. These sales are subject to special risks, such as delays in funding, termination of contracts or sub−contracts at the convenience of the government, termination, reduction or modification of contracts or sub−contracts in the event of changes in the government's policies or as a result of budgetary constraints, and increased or unexpected costs resulting in losses or reduced profits under fixed price contracts. Although to date we have not experienced any material problems in our performance of government contracts, or in the receipt of payments in full under such contracts, we cannot assure you that we will not experience problems in the future.

The markets in which we operate are highly competitive and we may be unable to compete successfully.

The market for our products and related services, in general, is highly competitive. Additionally, some of our principal competitors such as Witness Systems, Inc. and Verint Systems, Inc. may have significantly greater resources and larger customer bases than do we. We have seen evidence of deep price reductions by our competitors and expect to continue to see such behavior in the future, which, if we are required to match such discounting, will adversely affect our gross margins and results of operations. To date, we have been able to manage our product design and component costs. However, there can be no assurance that we will be able to continue to achieve reductions in component and product design costs. Further, the relative and varying rates of increases or decreases in product price and cost could have a material adverse impact on our earnings.

We are expanding the scope of our Voice Platforms and Applications to Enterprise Performance Management solutions, with a focus on analytic software solutions that are based on voice and data content analysis. The market for such content analysis applications is still in its early phases. Successful positioning of our products is a critical factor in our ability to maintain growth. Furthermore, new potential entrants from the traditional enterprise business intelligence and business analytics sector may decide to develop recording and content analysis capabilities and compete with us in this emerging opportunity. As a result, we expect to continue to make significant expenditures on marketing. We cannot ensure that the market awareness or demand for our new products will grow as rapidly as we expect, or if at all, that we will successfully develop new products or introduce new applications for existing products, that such new products and applications will achieve market acceptance or that the introduction of new products or technological developments by others will not adversely impact the demand for our products.

The recent expansion of Voice over Internet Protocol (or VoIP) into contact centers and trading floors may allow one or more of our competitors to take a leadership position with respect to this new technology. Strategic partners may change their vendor preference as a result or may develop embedded VoIP recording as part of the VoIP switch or networking infrastructure. We cannot assure you that our products or existing partnerships will ensure sustainable leadership.

With respect to the market for digital video products and applications (or Video Platforms and Applications), our Video Platforms and Applications are utilized by entities in the CCTV security, gaming and retail industries to capture, store and analyze digital video and related data. The market for our Video Platforms and Applications is highly competitive and includes products offering a broad range of features and capacities. We compete with a number of large, established manufacturers of video recording systems and distributors of similar products, as well as new emerging competitors. The price per channel of digital recording systems has decreased throughout the market in recent years, primarily due to competitive pressures. We cannot assure you that the price per channel of digital recording systems will not continue to decrease or that our gross profit will not decrease as a result.

With respect to the public safety part of our business, our ability to succeed depends on our ability to develop an effective network of distributors to the mid−low segment of the public safety market, while facing pricing pressures and low barriers to entry. We face significant competition from other well−established competitors, including CVDS Inc., VoicePrint Inc. and others. Prices have decreased throughout the market in recent years, primarily due to competitive pressures. We cannot assure you that prices will not continue to decrease or that our gross profit will not decrease as a result. We believe that our ability to sell and distribute our Voice Platforms and Applications in the public safety market depends on the success of our marketing, distribution and product development initiatives. We cannot assure you that we will be successful in these initiatives.

Continuing adverse conditions in the information technology sector may lead to a decreased demand for our Voice Platforms and Applications and may harm our business, financial condition and results of operations.

Our operating results may be materially adversely affected as a result of recent unfavorable economic conditions and reduced information technology spending, particularly in the product segments in which we compete. In particular, many enterprises, telecommunications carriers and service providers have reduced spending in connection with contact centers, and many financial institutions have reduced spending related to trading floors. These trends may adversely affect the growth of sales of new applications. If these industry−wide conditions persist, they may have a material adverse impact on our business, financial condition and results of operations.

We depend on certain key strategic partners for sales of our products. If our relationship with these partners is for any reason impaired, our business and results of operations will likely suffer.

We have agreements in place with many distributors, dealers and resellers to market and sell our products and services in addition to our direct sales force. We derive a significant percentage of our revenues from one or more of our channel partners. Our financial results could be materially adversely affected if our contracts with channel partners were terminated, if our relationship with channel partners were to deteriorate or if the financial condition of our channel partners were to weaken. Our top channel partner accounted for approximately 23%, 20% and 19% of our revenues in 2002, 2003 and 2004, respectively. Our competitors' ability to penetrate these strategic relationships, particularly our relationship with Avaya Inc., our largest global distribution partner and one of the leading global providers of enterprise business communication platforms in voice, e−business and data, may result in a significant reduction of sales through that partner.

In addition, as our market opportunities change, we may have increased reliance on particular channel partners, which may negatively impact gross margins. There can be no assurance that we will be successful in maintaining or expanding these channels. If we are not successful, we may lose sales opportunities, customers and market share. In addition, there can be no assurance that our channel partners will not develop or market products or services in competition with us in the future.

We depend on the success of the NiceLog system and related products.

We are dependent on the success of the NiceLog system and related products to maintain profitability. In 2002, 2003 and 2004, approximately 82%, 75% and 78%, respectively, of our revenues were generated from sales of NiceLog systems and related products and we anticipate that such products will continue to account for a significant portion of our sales in the next several years. A significant decline in sales of NiceLog systems and related products, or a significant decrease in the profit margin on such products, could have a material adverse effect on our business, financial condition or results of operations.

We may be unable to develop strategic alliances and marketing partnerships for the global distribution of our Video Platforms and Applications, which may limit our ability to successfully market and sell these products.

We believe that developing marketing partnerships and strategic alliances is an important factor in our success in marketing our Video Platforms and Applications and in penetrating new markets for such products. However, unlike our Voice Platforms and Applications, we have only recently started to develop a number of strategic alliances for the marketing and distribution of our Video Platforms and Applications. We cannot assure you that we will be able to develop such partnerships or strategic alliances on terms that are favorable to us, if at all. Failure to develop such arrangements that are satisfactory to us may limit our ability to successfully market and sell our Video Platforms and Applications and may have a negative impact on our business and results of operations.

We may be unable to commercialize new video content analysis applications.

We are currently in the process of developing and commercializing new video content analysis applications that will enable real−time detection of security threats. The market for such video content analysis applications is still in an early phase. In addition, because this is a new opportunity for changing security procedures and represents a transition to proactive security management, we are not able to predict the pace at which security organizations will adopt this technology, if at all. Successful positioning of our products is a critical factor in our ability to maintain growth. New potential entrants to the market may decide to develop video content analysis capabilities and compete with us in this emerging opportunity. As a result, we expect to continue to make significant expenditures on marketing. We cannot assure you that a market for these products will develop as rapidly as we expect or at all, that we will successfully develop new products or introduce new applications for existing products, that new products or applications will meet market expectations and needs, that we will be successful in penetrating these markets and in marketing our products or that the introduction of new products or technological developments by others will not adversely impact the demand for our video content analysis applications.

If the pace of spending by the U.S. Department of Homeland Security is slower than anticipated, our security business will likely be adversely affected, perhaps materially.

The market for our security solutions in CCTV continuous recording, public safety and law enforcement is highly dependent on the spending cycle and spending scope of the United States Department of Homeland Security, as well as local, state and municipal governments and security organizations in international markets. We cannot be sure that the spending cycle will materialize and that we will be positioned to benefit from the potential opportunities.

Risks Relating to Israel

Our business may be impacted by inflation and NIS exchange rate fluctuations.

Exchange rate fluctuations between the United States dollar and the NIS may negatively affect our earnings. A substantial majority of our revenues and a substantial portion of our expenses are denominated in U.S. dollars. However, a significant portion of the expenses associated with our Israeli operations, including personnel and facilities related expenses, are incurred in NIS. Consequently, inflation in Israel will have the effect of increasing the dollar cost of our operations in Israel, unless it is offset on a timely basis by a devaluation of the NIS relative to the U.S. dollar. We cannot predict any future trends in the rate of inflation in Israel or the rate of devaluation of the NIS against the U.S. dollar. If the U.S. dollar cost of our operations in Israel increases, our dollar−measured results of operations will be adversely affected.

We are subject to the political, economic and military conditions in Israel.

Our headquarters, research and development and main manufacturing facilities are located in the State of Israel, and we are directly affected by the political, economic and military conditions to which Israel is subject. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors. A state of hostility, varying in degree and intensity, has led to security and economic problems for Israel. Since October 2000, there has been a high level of violence between Israel and the Palestinians, which has affected Israel's relationship with several Arab countries. Any armed conflicts or political instability in the region could negatively affect local business conditions and harm our results of operations. We cannot predict the effect on the region of the increase in the degree of violence between Israel and the Palestinians. Furthermore, several countries restrict doing business with Israel and Israeli companies, and additional companies may restrict doing business with Israel and Israeli companies as a result of an increase in hostilities. Our products are heavily dependent upon components imported from, and most of our sales are made to, countries outside of Israel. Accordingly, our operations could be materially adversely affected if trade between Israel and its present trading partners were interrupted or curtailed.

Some of our officers and employees are currently obligated to perform annual military reserve duty. Additionally, in the event of a military conflict, including the ongoing conflict with the Palestinians, these persons could be required to serve in the military for extended periods of time. We cannot assess the full impact of these requirements on our workforce or business and we cannot predict the effect on us of any expansion or reduction of these obligations.

Service and enforcement of legal process on us and our directors and officers may be difficult to obtain.

Service of process upon our directors and officers, most of whom reside outside the United States, may be difficult to obtain within the United States. Furthermore, since the majority of our assets and most of our directors and officers are located outside the United States, any judgment obtained in the United States against us or these individuals or entities may not be collectible within the United States.

There is doubt as to the enforceability of civil liabilities under the Securities Act of 1933 and the Securities Exchange Act of 1934 in original actions instituted in Israel. However, subject to certain time limitations and other conditions, Israeli courts may enforce final judgments of United States courts for liquidated amounts in civil matters, including judgments based upon the civil liability provisions of those Acts.

We depend on the availability of government grants and tax benefits.

We derive and expect to continue to derive significant benefits from various programs and laws in Israel including tax benefits relating to our "Approved Enterprise" programs and certain grants from the Office of the Chief Scientist of the Ministry of Industry, Trade and Labor, or OCS, for research and development. To be eligible for these grants, programs and tax benefits, we must continue to meet certain conditions, including making certain specified investments in fixed assets and conducting the research, development and manufacturing of products developed with such OCS grants in Israel (unless a special approval has been granted for performing manufacturing activities outside Israel). From time to time, the Israeli Government has discussed reducing or eliminating the availability of these grants, programs and benefits and there can be no assurance that the Israeli Government's support of grants, programs and benefits will continue. Pursuant to an amendment to Israeli regulations, income from two of our "Approved Enterprises" is exempt from income tax for only two years. Following this two−year period, the "Approved Enterprise" will be subject to corporate tax at a reduced rate of 10−25% (based on the percentage of foreign ownership in each taxable year) for the following eight years. Income from the other two "Approved Enterprises" is tax exempt for four years. Following this four−year period, the "Approved Enterprises" are subject to corporate tax at a reduced rate of 10−25% (based on the percentage of foreign ownership in each taxable year) for the following six years. If grants, programs and benefits available to us or the laws under which they were granted are eliminated or their scope is reduced, or if we fail to meet the conditions of existing grants, programs or benefits and are required to refund grants or tax benefits already received (together with interest and certain inflation adjustments), our business, financial condition and results of operations could be materially adversely affected.

We may be required to pay stamp duty on agreements executed by us on or after June 1, 2003. This would increase our taxes.

The Israeli Stamp Duty on Documents Law, 1961 (the "Stamp Duty Law"), provides that most documents signed by Israeli companies are subject to a stamp duty, generally at a rate of between 0.4% and 1% of the value of the subject matter of such document. De facto, it has been common practice in Israel not to pay such stamp duty unless a document is filed with a governmental authority or with the courts. As a result of an amendment to the Stamp Duty Law that came into effect on June 1, 2003, the Israeli tax authorities have approached many companies in Israel (including us) and requested the disclosure of all agreements signed by such companies after June 1, 2003 with the aim of collecting stamp duty on such agreements. The legitimacy of the aforementioned amendment to the Stamp Duty Law and of said actions by the Israeli tax authorities are currently under review by the Israeli High Court of Justice. Based on advice from our Israeli counsel, we believe that we may only be required to pay stamp duty on documents signed on or after August 2004. However, we cannot give any assurance that the tax authorities or the courts will accept such view. Although at this stage it is not yet possible to evaluate the effect, if any, on us of the amendment to the Stamp Duty Law, the same could materially adversely affect our results of operations in the future.

In January 2005, an order was signed in accordance with which the said requirement to pay stamp duty is cancelled with effect from January 1, 2008.

Risks Related to our Ordinary Shares and ADSs

Our share price is volatile and may decline.

Numerous factors, some of which are beyond our control, may cause the market price of our ordinary shares or our ADSs, each of which represents one ordinary share, to fluctuate significantly. These factors include, among other things, announcements of technological innovations, development of or disputes concerning our intellectual property rights, customer orders or new products by us or our competitors, currency exchange rate fluctuations, earnings releases by us or our competitors, market conditions in the industry and the general state of the securities markets, with particular emphasis on the technology and Israeli sectors of the securities markets.

Our operating results in one or more future periods may fluctuate significantly and may cause our share price to be volatile.

The sales cycle for our products and services is variable, typically ranging between a few weeks to several months from initial contact with the potential client to the signing of a contract. Frequently, sales orders accumulate towards the latter part of a given quarter. Looking forward, given the lead time required by our contract manufacturer, if a large portion of sales orders are received late in the quarter, we may not be able to deliver products within the quarter and thus such sales will be deferred to a future quarter. There can be no assurance that such deferrals will result in sales in the near term, or at all. Thus, delays in executing client orders may affect our revenue and cause our operating results to vary widely. Additionally, as a high percentage of our expenses, particularly employee compensation, is relatively fixed, a variation in the level of sales, especially at or near the end of any quarter, may have a material adverse impact on our quarterly operating results.

In addition, our quarterly operating results may be subject to significant fluctuations due to other factors, including the timing and size of orders and shipments to customers, variations in distribution channels, mix of products, new product introductions, competitive pressures and general economic conditions. It is difficult to predict the exact mix of products for any period between hardware, software and services as well as within the product category between audio platforms and related applications, digital video and communications intelligence. Because a significant portion of our overhead consists of fixed costs, our quarterly results may be adversely impacted if sales fall below management’s expectations. In addition, the period of time from order to delivery of our Audio and Video Platforms and Applications is short, and therefore our backlog for such products is currently, and is expected to continue to be, small and substantially unrelated to the level of sales in subsequent periods. As a result, our results of operations for any quarter may not necessarily be indicative of results for any future period. Due to all of the foregoing factors, in some future quarters our sales or operating results may be below our forecasts and the expectations of public market analysts or investors. In such event, the market price of our ordinary shares and ADSs would likely be materially adversely affected.

Item 4. Information on the Company.

History and Development of the Company

Our legal and commercial name is NICE−Systems Ltd. We are a company limited by shares organized under the laws of the State of Israel. We were originally incorporated as NICE Neptun Intelligent Computer Engineering Ltd. on September 28, 1986 and renamed NICE−Systems Ltd. on October 14, 1991. Our principal executive offices are located at 8 Hapnina Street, P.O. Box 690, Ra'anana 43107, Israel and the telephone number at that location is +972−9−775−3030. Our agent for service in the United States is our subsidiary, NICE Systems Inc., 301 Route 17 North, Rutherford, New Jersey 07070.

Business Overview

NICE offers solutions that consist of multimedia capture, multimedia content analysis and applications. These solutions enable our customers to extract insight from unstructured interactions by capturing the interactions and analyzing the content, thereby enabling improved business decisions or improved security operations. We offer our solutions as products or system solutions to various vertical markets in two major sectors: 1) the Enterprise Interaction sector; and 2) the Public Safety and Security sector.

1) Enterprise Interaction Solutions

Markets

The overall market for products that enable users to extract insight from interactions through digital voice recording, contact center management products and performance management products has experienced steady growth in recent years as a result of the increase in the use of telephones to obtain information, to initiate business and consumer contacts, to provide services such as banking and insurance, and to sell products through contact centers.

Users of our enterprise interaction solutions include financial institutions, such as brokerage and trading houses; contact centers within the enterprise, such as telemarketing, customer service, telebanking and teleinsurance facilities and other departments in the enterprise that can benefit from analyzing customer interactions, such as marketing, operations and legal.

Financial Institutions. Financial institutions conduct a substantial portion of their business over the telephone and are increasingly relying upon their ability to record, store and retrieve voice data of transactions in a timely, reliable and efficient manner. Brokers and dealers record and store recordings of transactions to provide back−up and verification of such transactions and to guard against risks posed by lost or misinterpreted voice communications or fraud. Our customers in the financial institutions market include ABN AMRO Bank, American Express, Bank of America, Barclays, CIBC Oppenheimer, Citibank, Deutsche Bank, Dresdner Bank, First Chicago NBD, JP Morgan Chase, Goldman Sachs, Lehman Brothers, Morgan Stanley, Sydney Futures Exchange and Tokyo Mitsubishi Bank.

Contact Centers. Many enterprises are increasingly using dedicated contact centers as their main contact point with their customers. These contact centers are processing and managing high volumes of incoming and outgoing customer interactions. Contact centers have been used extensively in such fields as financial services (banking, credit cards, insurance, investments), telecommunications, retail, health care and travel services. Typically, the contact center is the primary “hub” within an organization for placing or receiving a large volume of customer interactions. Customer service representatives are talking with customers about issues such as reservations, product information, account information, and problem resolution. As the importance of the contact center increases and more functions and capabilities have been combined, a parallel industry has emerged. This industry creates and supports the systems, software and services that are designed to make these enterprises and the contact center activities within the enterprises efficient, effective and well matched to the broader corporate mission of the enterprise. Also, it is increasingly expected that the contact center be the “eyes and ears” of the enterprise in the market and a prime source of information for the various enterprise departments, such as marketing, sales, legal, finance and operations. The global contact center market is using voice recording solutions and related applications to enable storage of the details of telephone orders and other transactions, supervision of contact center operators and campaigns, and evaluation of salespersons’ efficiency, customer service and training. It is also increasingly being used to extract insight from the recorded interactions to solve business issues and increase the overall enterprise performance. Users of the NICE Perform, NiceUniverse and NiceLog system in this market include AllSec, American Express, Blue Cross Blue Shield, Citibank, DHL, Federal Express, Ford Credit, Home Depot, IBM, Liberty Mutual, National Bank of Canada, Nextel, Nokia, PRC, Spectramind, Telecom New Zealand, Time Warner, Vodafone, Wipro, WPS and Wynn Resorts.

Sales and Marketing; Strategic Relationships

We market, distribute and service our Enterprise Interaction Solutions worldwide, through leading suppliers of complementary products, such as Avaya, independent dealers that predominantly specialize in the voice recording market and contact center and enterprise applications, as well as through our own sales and technical support force in the United States, Canada, Germany, the United Kingdom, France, Spain, Hong Kong, Japan, Singapore, India and Israel. Most of the sales made by our sales force are made to our distributors, who then install the systems and provide day−to−day support to end−users.

In the Financial Trading segment, we have established marketing, sales and support arrangements with leading suppliers of complementary products. These companies market and distribute our products to their customers either as stand−alone systems or as integrated components of their own systems, as follows:

- An OEM agreement with IPC Information Systems, Inc. IPC, a leading provider of integrated communications solutions to the financial services community, has embedded a NiceLog platform customized for IPC into IPC's Alliance MX product line and sells this product as an integral part of the IPC product.
- An OEM agreement with Etrali S.A., a telecom integrator serving the financial community. Etrali is a European leader of dealer−board systems for trading rooms. Etrali and NICE have closely integrated our products for dealing rooms, which are distributed globally by Etrali S.A.
- A marketing and developer support agreement with BT Syntegra, British Telecom's selling and integration company in the trading floor segment.

In the Contact Center segment, we have entered into global distribution agreements as well as alliances and development programs for integration and ensuring compatibility of products with leading vendors, as follows:

- A global partnership with Avaya Inc. Avaya is the leading global provider of enterprise business communication platforms in voice, e−business and data. Avaya and its business partners (or sales partners or dealers) are co−selling our enterprise interaction solutions to their customers globally.
- A marketing and technical collaboration with Dimension Data, IBM, Philips and Siemens.
- An OEM and developer support agreement with Alcatel.
- An alliance program with Aspect Telecommunications to ensure the compatibility of our contact center product line with Aspect's automatic call distribution systems and to promote this integration through Aspect's marketing materials.
- Technical collaboration and development programs with Cisco, Concerto, Ericsson, Genesys, Mitel, NEC, Nortel, Philips and Rockwell.
- Product integrations with Siebel Systems and Amdocs (Clarify Inc.) in the CRM Space. These integrations with leading CRM providers enable customers to capture and enhance their customers' entire experience in the contact center from start to finish and to more tightly integrate the functionality delivered by our products into their business environment.

Products

Our enterprise interaction solutions include recording, monitoring, quality management and business performance management solutions which are designed to capture interactions, analyze them and take action based on this analysis to drive the enterprise performance. They also protect businesses and customers against risks posed by lost or misinterpreted voice or data transmissions and capture and improve contact center agent performance and the customers' experience.

Interaction capture units (known as voice recorders or loggers) are systems that capture and record large volumes of voice data transmitted over multiple telephone or other communication lines and allow users to retrieve and playback specific communication data. Traditional voice recorders were based on analog reel−to−reel technology, which limited an organization's ability to store and retrieve data efficiently, and which could not interface with digital computer and telecommunication networks. In the early 1990s, analog reel−to−reel recorders began to be replaced with analog VHS−based products and, more recently, by digital products, including those based on magnetic disk, optical disk or digital audio tapes (or DAT). Organizations' growing needs to record, process and store large amounts of voice data resulted in the introduction of digitally−based voice recording systems characterized by increased performance and improved system economics. Digital multi−channel recording systems enable simultaneous recording and logging of a large number of channels, while enabling a large number of users to process voice data simultaneously. Digital systems' advantages over traditional analog systems include the immediate random access to recorded data, open connectivity and compact size of both the recording unit and storing and archiving media. Advanced, industry−standard, digital voice recording systems employing computer telephony integration (or CTI) technologies allow for integration of the recording and retrieval functions with organizations' computer and telecommunications networks, thereby delivering maximum business benefits, increased user efficiency, and wider access for larger numbers of users. The demand for sophisticated CTI digital voice recording systems is increasing as a result of the increased demand for digital recording systems, particularly in the contact center market and the conversion by the large installed base of analog systems to digital technology, specifically in the financial institutions, public safety and air traffic control markets.

Today's business is characterized by increasing reliance upon interactions conducted via telephony and web−based communications. These means of communication are becoming an important and strategic dimension of business across a broad spectrum of markets. In these business environments, a great deal of information lies hidden within the ever−growing quantities of unstructured multimedia interactions. This information can provide decision makers throughout the enterprise with insights into their marketplace and customer base, and direct access to key business scenarios. Many of these capabilities are not available with traditional transactional−based analytics tools. They are of great value to organizations constantly searching for better ways to understand their market dynamics and customer intent, while operating within the limitations of traditional surveying and data analysis techniques and growing regulatory requirements.

NICE Perform is our flagship enterprise product. It is an integrated suite of solutions that offers innovative ways for organizations to generate insight from interactions to enhance performance. NICE Perform combines multiple data sources in a fully integrated architecture with a centralized data warehouse, allowing interoperability of all the data sources to address a variety of business issues with a high level of accuracy. The data sources include word spotting, emotion detection, talk pattern analysis, customer surveys, CTI analysis, application activities and business data. With a set of advanced engines, NICE Perform provides multi−dimensional analytics of these data sources. State−of−the−art visualization techniques enable analysts and executives to quickly and easily identify trends, deviations and situations requiring immediate action. All these capabilities are implemented in an advanced application suite that is underpinned by a new series of powerful high density capture and archiving platforms that provide cost−effective reliable processing of multimedia interactions in a format optimized for multi−dimensional analytics.

While providing critical statistical data, NICE Perform goes beyond the scope of transactional analytics to help decision makers understand customer intent and market dynamics, identify current and future trends early enough for proactive management of challenges, opportunities and changes, and enhance corporate governance throughout the enterprise. For example, marketing executives can more effectively track marketing campaigns, analyze causes of success or failure, and quickly adapt to changing market conditions. Finance and legal executives can ensure that company policies are adhered to in all phone conversations across the organization, thereby avoiding costly legal action by spotting and correcting irregularities before they become problems.

NICE Perform also contains all of the contact center quality management capabilities of NiceUniverse described below. In addition, NICE Perform includes advanced online coaching capabilities. These enable supervisors to coach the contact center agents in order to improve their skills and to empower those agents and cover immediate knowledge dispersal matters as needed by the different departments, such as marketing or order administration.

NiceUniverse, introduced in February 1998, is a comprehensive quality management solution used to evaluate agent performance and to raise the level of customer service in contact centers through advanced voice and desktop screen recording technologies. The NiceUniverse system provides objective evaluation tools and helps identify training requirements for contact center agents, including real−time monitoring for instant access to live customer interactions and enhanced reporting and administration features. NiceUniverse uses a CTI that integrates with automatic call distributions (or ACDs). This enables NiceUniverse to monitor and record agent sessions (voice and screen) on a user−defined schedule and store them in compressed digital format. Sessions are later retrieved by the reviewers from their network PCs or thin clients, and agent performance is graded using customized on−screen templates. From these templates and other data, NiceUniverse generates detailed reports, statistics and graphs to help identify training requirements and set relevant benchmarks for contact center agents.

NiceLog, our digital voice recording system, is a computer telephony integrated multi−channel voice recording and retrieval system. NiceLog is an open architecture system based on PC architecture and advanced audio compression technology that performs continuous, reliable recordings of up to thousands of analog and digital telephone lines, as well as radio channels, and enables simultaneous access by multiple users. NiceLog can be used either as a stand−alone unit or as part of a highly expandable and scaleable system comprised of several seamlessly integrated units. Each NiceLog unit can simultaneously record, monitor, archive and playback. The NiceLog System includes client and web applications that enable users to access the system, these applications communicated with the voice servers using the TCP/IP communication protocol and can run on Windows 98/Me, Windows NT, Windows 2000 and Windows XP operating systems. The system can connect to telecommunication interfaces such as T1, E1, ISDN and analog trunks as well as other more specialized interfaces. The modular design of the NiceLog system makes it a powerful voice management tool that can be expanded to satisfy customers' needs by integrating it with additional NiceLog units on the same local area network, or LAN.

Our patented VoIP Capture Unit builds on our NiceLog technology to provide a complete solution to audio storage in Voice over Internet protocol (VoIP) telephony environments. The VoIP Capture Unit provides an IP−recording platform with a wide range of scaleable recording solutions that supports the leading telephony vendors. Our VoIP Capture Units are fully integrated with the NICE product portfolio, making all our applications available for use over VoIP. NICE VoIP Loggers can serve alongside other logger types in a mixed VoIP/non−VoIP environment with the same familiar application software; users are unaware of the voice capture method being used.

NICE VoIP Capture Units can use both packet sniffing and active recording methods for recording VoIP sessions. NICE VoIP active recording solutions integrate with leading vendors such as Avaya, offering centralized recording of distributed environments and other benefits.

NiceLog's central storage option, NICE Storage Center, can integrate with various enterprise storage networks (SAN, NAS or DAS) for long term or medium term voice storage. Central storage sites can hold the entire voice recording from all the organization's different sites thus reducing management costs and redundancy. The retrieval process for voice on the central site is fully automatic.

NiceCall Focus II is a voice recording system that records up to 32 input channels and provides up to 66,000 hours of on−line voice storage capacity (using NICE's ACA compression) and supports wide range of archiving devices for long−term storage options. NiceCall Focus II offers a wide range of connectivity to PABX and Radio systems and is built on the successful legacy of NiceCall Focus which was introduced in 2001. NiceCall Focus II provides organizations that have a relatively small number of input channels, such as public safety agencies, with a competitively priced yet technologically advanced digital recording product that offers many of the connectivity and processing features of NiceLog. NiceCall Focus II is being targeted primarily at public safety facilities, including 911 emergency centers and utilities, as well as small bank branches, financial trading sites, and contact centers.

2) Public Safety and Security Solutions

Markets

The overall market for public safety and security solutions is comprised of voice platforms and applications, digital video platforms and applications, and lawful interception products. The market has experienced steady growth over the last few years driven by continued governmental response to the dangers of terrorism, public disturbance and general heightened awareness of the need for enhanced security within enterprises.

a) Voice Platforms and Applications

Users of our voice platforms and applications include public safety and transportation agencies, such as police, fire and ambulance departments, air traffic control centers and intelligence agencies.

Public Safety and Emergency Services. These organizations include police, fire, ambulance, coastguard, mountain rescue and other similar public and private bodies that respond to calls for assistance from the public. In most cases, local, state or federal law requires that all communications traffic be recorded in order that evidence can be provided in courts of law, and in order that the public safety body can verify that it is following prescribed processes and meeting performance standards. Our customers in the public safety market include: Chicago Police Department, Indiana State Police, Los Angeles Police Department, New Jersey State Police, New York Police Department, Seattle Fire Department, U.S. Department of Defense, Hampshire Police – U.K. and Hertfordshire Police – U.K.

Public Transport Agencies. These organizations include rail, bus and mass transit metro systems. They use large−scale, distributed, fixed and mobile communications networks in order to provide command and control capabilities between the mobile units and one or more control rooms. In the event of an incident, they are required to be able to produce recordings of all associated communications traffic. Many of these organizations are implementing the latest generation of digital trunked radio systems according to one of the several international standards, such as TETRA, Tetrapol or APCO25, and the recording system is required to interface to these radio systems in order to capture and identify all radio traffic. Our customers in the public transportation market include authorities like Singapore Mass Transit Authority and Railtrack – U.K.

Air Traffic Control (or ATC). The ATC market is a traditional user of voice recording systems due to mandatory requirements for the recording of voice communications and radio transmissions. ATC centers are evaluating the need to upgrade their voice communications recording and archiving systems by installing digital voice loggers. NiceLog was selected by the FAA as the voice recording system to be installed in over 800 ATC centers in the United States. NiceLog and Wordnet have also been selected by ICAO and other ATC authorities in Austria, Canada, China, Croatia, Cyprus, Hong Kong, Hungary, Iceland, Israel, Japan, Kazakhstan, the Maldive Islands, the Netherlands, Norway, Poland, Romania, Switzerland and Turkey.

Intelligence Agencies. Law enforcement and intelligence agencies collect large amounts of information in various media for analysis and evaluation, although only a small portion of that information is valuable. Intelligence agencies require sophisticated multi media recording systems that enable the recording, retrieval and processing of the information gathered for purposes of analysis and evaluation. Users who have installed NiceLog or Wordnet systems, either as stand alone systems or in combination with other systems, include intelligence agencies in more than twenty countries.

b) Digital Video Platforms and Applications

The market for digital video platforms, which provide continuous video surveillance and recording for security protection purposes, is currently unfolding as closed circuit television, or CCTV, applications shift from traditional analog recorders to digital recorders. Users of our digital video recording systems include correctional facilities, banks, telecommunication data−center hosting centers, retail stores, casinos, transportation companies and city centers.

Customers for our products include the Atlanta Hartsfield International Airport, Bally's casino in Atlantic City, Bank of England, Casino Cosmopol in Sweden, Chase Manhattan, Dallas Fort Worth International Airport, Dell Computer Corporation, European Space Agency, the Helsinki Railway Station − Finland, the Metropolitan Nashville Airport Authority, Toronto Pearson International Airport, and correctional facilities in Brooklyn, New York, and Rush City, Minnesota.

c) Lawful Interception

The market comprised of law enforcement agencies, internal security and intelligence organizations is undergoing rapid changes. In parallel to the growth in the number and severity of threats, new telecommunications services and applications are utilized by public agencies, which need sophisticated solutions to intercept and analyze the intelligence information collected by these services and applications.

Additionally, governments are adopting new legislation and regulating new standards in order to assist the organizations that deal with intelligence. According to these legislations and regulations, telecom service providers are required to install systems that will enable the interception of certain communications and deliver them in real time to the monitoring agencies.

__Sales and Marketing; Strategic Relationships__

In the public safety market, we distribute our products worldwide through a network of over 100 national and local independent dealers and distributors that also provide installation and maintenance services.

- A marketing agreement with Motorola Inc. for the co−marketing and resale of our range of products for the public safety market in North American and international markets. This relationship includes the appointment of NICE as the only authorized Dimetra Application Partner for Motorola's trunked radio solutions.

- We also market and sell systems through major regional or global partners, such as Alcatel, BT, Damovo, Marconi, Nokia and Siemens.

In the ATC market, we have been awarded contracts for installation of NiceLog systems on the basis of bids submitted to ATC authorities by Denro Systems, Inc. (part of Northrup Grumman, Inc.) and others that incorporated NiceLog as the voice recording system as part of their proposal. Pursuant to an agreement dated August 1995 between the FAA and Denro, NiceLog was selected as the voice recording system to be installed in various ATC centers in the United States. We provide NiceLog cards (including software) to Denro and Denro assembles and installs them.

We have a dedicated sales organization for the NiceVision digital video recording system. We use a network of dealers and security systems integrators for the sale, installation and support of our solutions. In North America we work through key partners such as Anixter, Diebold and Siemens Building Technologies. In EMEA we work with system integrators, such as Siemens, Surveillance Group and Thales Security. Recently, we have also agreed on a collaboration with IBM and Cisco in the area of digital video surveillance.

We have a dedicated sales and marketing organization for the NiceTrack system for lawful interception. We market the system worldwide through our direct sales force and through distributors.

__Products__

a) Voice Platforms and Applications

Through the acquisition of TCS, NICE provides first responders and air traffic control organizations with a full range of recording features for voice, radio and trunked radio, including on−line access to hundreds of hours of recording for a quick response time, a choice of different types of archiving media, and a dubbing capability to edit calls on−line for courtroom presentations. The system enables the organizations to re−construct scenarios, investigate and improve performance. Our products are currently being used in a significant number of air traffic control facilities, including FAA and NAV Canada, as well as large police departments, transportation companies and emergency services command and control centers.

The underlying voice recording platforms used in the public safety marketplace are similar to the products described above. Their primary use is to record and replay voice conversations and associated data in order to be able to reconstruct and analyze incidents that have occurred. However, there are some significant technical differences owing to the need in many cases to capture not only voice traffic coming into and out of the public service command and control center, e.g., a 911 center, but also the radio traffic that is occurring between the command and control center and the field personnel. Hence the technical interfaces and architecture of the products are often different from those required for commercial environments.

The other major difference is that there may be the need to replay and analyze multiple conversations that occurred in connection with an event in order to fully analyze it. For example, it may be necessary to replay, in synchronism, many different radio channels, together with the radio dispatch conversations, together with the telephone conversations from multiple callers.

Our offering to the public safety market ranges in size and complexity from small, single−site single−recorder systems to large, multi−site, multi−recorder systems integrated with trunked radio and computer−aided dispatch systems. Below is a description of the ex−TCS product lines that are primarily offered to the public safety market.

Mirra is a small recording system that is particularly suited to simple recording applications in which it can record up to 32 channels of voice traffic from a wide variety of analogue and digital interfaces. Mirra has been designed to be simple to install, operate and maintain and has been sold to many local, city and state public safety organizations that have a single site operation. Digitized voice and associated data are stored onto DVD disks that provide a robust and long−term archive medium. Mirra's design avoids using an internal hard disk for the operating system and consequently it starts−up very rapidly and avoids the maintenance liabilities associated with hard disks.

Tienna is a large recorder that is designed to form part of a "Renaissance" solution. Renaissance solutions are used when the customer has a complex requirement typically involving multiple recorders, multiple sites and dual−redundant components in order to provide very high performance and resilience. Tienna can provide up to 480 channels per unit and multiple units can be interconnected to form a system of many thousands of ports. Tienna is unique in that it provides dynamic channel allocation between the active ports on the recorder and a greater number of channels on the networks to which it is connected. This provides a more efficient use of the system's resources than a permanent 1:1 connection of channels to ports. Tienna contains internal hard disks for short−term storage but relies upon the Renaissance Centralized Mass Storage Unit (or CMSU) for all medium and long−term storage and for archiving onto tapes.

Renaissance solutions can incorporate combinations of Wordnet and Tienna recorders, as well as the CMSU, calls database and replay server. These components operate together in a networked configuration to provide a complete recording solution and can be fully duplicated in order to provide very high levels of redundancy and reliability. Since March 2005, Wordnet is no longer generally available for sales, and we offer NiceLog as a replacement to the Wordnet customers and partners.

b) Digital Video Platforms and Applications

Our NiceVision product line consists of the NiceVision Pro, NiceVision Harmony, NiceVision Alto and NiceVision NVSAT. NiceVision is a state−of−the−art digital video and audio recording system that provides continuous CCTV, recording, archiving, and debriefing capabilities that meet the needs of today's demanding security environment, including central banks, Fortune 500 companies, transportation facilities, prisons, and casinos.

The NiceVision Pro is a premium solution designed for high−end applications requiring high−frame rate and/or a large number of cameras in a campus environment. Typical environments for the NiceVision Pro are airports, casinos and ground transportation facilities. The NiceVision Pro accommodates 96 video channels in one single box and can handle storage devices in the range of tera−bytes. These devices are of two types: disk based on−line storage (internal drives or external RAIDs) and tape−based off−line juke box devices.

The NiceVision Harmony is a mid−range digital video recording solution designated for sites accommodating a large number of cameras yet requiring a variety of frame rates per channel, spanning from single frames per second to full frame rate, when required. Typical environments for the NiceVision Harmony are retail shops, certain bank facilities and corporate buildings. The NiceVision Harmony caters for 64 video channels with a preset frame rate shared between groups of channels. The NiceVision Harmony can also support large storage devices like the NiceVision Pro.

The NiceVision Alto is a mid range product that can support eight to 32 video channels using variable frame rates and resolutions. Typical environments for the NiceVision Alto are distributed sites that require high image quality and adjustable level of service to meet different networking channels. The NiceVision Alto runs content analytics to support smart monitoring.

The NiceVision NVSAT is a small scale unit that supports four to eight video channels. It is designed for distributed architectures, where it serves as a smart Codec providing high image quality, level of service and content analytics.

c) Lawful Interception

The NiceTrack product line provides law enforcement agencies, internal security services and intelligence organizations with end−to−end solutions for the interception, delivery, monitoring, collection and advanced analysis of telecommunication interactions. In order to create a full perspective of threats, NiceTrack products handle both telephony and Internet data on the same platform. The working environment provides intelligence analysts with a broad intelligence perspective to ensure that crucial information is always delivered to decision makers and operational staff in real−time. NiceTrack also features an open architecture design that offers government agencies the flexibility they need to build an effective intelligence platform customized and localized to suit specific operational requirements and methodologies.

NiceTrack, as a lawful interception solution, is fully compliant with the international standards defined by ETSI (under various European legislations) and TIA (under the CALEA legislation).

Dictaphone Acquisition

We completed the acquisition of Dictaphone’s Communications Recordings Systems division (or CRS) on June 1, 2005. CRS is a leading provider of recording, liability and quality management systems for first responders, critical facilities, contact centers and financial trading floors.

CRS’s major products are marketed under the Freedom® trademark. The products include:

- Freedom Enterprise, which combines state−of−the−art recording technology for full−time or selective recording with advanced tools for optimizing contact center performance in virtually any telephony environment: circuit−switched telephony, VoIP and hybrid environments.

- Freedom FT, which provides high−level fault−tolerant recording, with a design that eliminates single points of failure and ensures that recordings are captured and accessible when required.

- Freedom rDT, which works with the Motorola or M/A−COM trunked radio system to record radio communications dynamically and capture trunked radio data. It is a solution aimed at the 9−1−1 first responder market.

CRS operated in most of our existing markets, including contact centers, first responders and financial markets. Most of CRS’s activity has been in the first responder sector, while we have had a stronger position in the contact center and financial market sectors. Most of the division’s operations are concentrated in the United States, with some activity in Europe. At the time of the acquisition by us, CRS had approximately 8,000 customers, including the City of Miami, Comcast, Credit Suisse, Verizon and the U.S. Army.

We intend to continue to support the range of CRS Freedom products for up to five years, and while we will not actively seek to expand the sales of these solutions, we are prepared to meet any market demand for them. At the same time, we will continue to develop our range of solutions for the various market sectors, taking into consideration the requirements of the CRS customer base.

Discontinued Operation − COMINT/DF

On March 31, 2004, we sold the net assets of our COMINT/DF military−related business to ELTA Systems Ltd (“ELTA”) for $4 million in cash. The net assets sold include the intellectual property, fixed assets, inventory, and contracts related to the COMINT/DF product line which includes high performance spectral surveillance and direction finding systems that detect, identify, locate, monitor and record transmission sources. The COMINT/DF business is therefore treated as a discontinued operation in our financial statements.

In 2002, 2003 and 2004, the COMINT/DF business generated revenues of approximately $7.2 million, $6.5 million and $0.8 million, respectively, and net income of approximately $1.4 million, $1.5 million and $3.2 million (including gain on disposition), respectively.

Manufacturing and Source of Supplies

Our products are built in accordance with industry standard infrastructure and are PC compatible. The hardware elements in our products are based primarily on standard commercial off−the−shelf components and utilize proprietary in−house developed circuit cards and algorithms and digital processing techniques and software. In the fourth quarter of 2002, we started selling “software only” solutions for use on standard servers.

Prior to the first quarter of 2002, our manufacturing operations consisted primarily of final assembly and testing of components and subassemblies. We manufactured our products in our facility in Ra’anana, Israel and our special NiceLog systems in our facilities in Ra’anana and Sunnyvale, California.

During the first quarter of 2002, however, we began implementation of a contract manufacturing agreement with Flextronics Israel Ltd., a subsidiary of a global electronics manufacturing services (or EMS) company. Under this agreement, Flextronics provides us with a turnkey manufacturing solution including order receipt purchasing, manufacturing, testing and configuration. This agreement covers all of our product lines, including our voice recording family of products, our video product lines, our upgrade lines and our spare parts and RMA. We believe this outsourcing agreement provides us with a number of cost advantages due to Flextronic’s large−scale purchasing power, and greater supply chain flexibility. We completed the transfer to Flextronics of the production for all our products during the second half of 2002.

Some of the components we use have a single approved manufacturer while others have two or more options for purchasing. In addition, for some of the components and subassemblies we maintain an inventory to limit the potential for interruption. We also carry out relationships directly with some of the more significant manufacturers of our components. Although certain components and subassemblies we use in our existing products are purchased from a limited number of suppliers, we believe that we can obtain alternative sources of supply in the event that such suppliers are unable to meet our requirements in a timely manner.

We also have a contract manufacturing agreement with Instem Technologies Ltd, a U.K. company, entered into by TCS prior to its acquisition by NICE. Under this agreement Instem is the manufacturer of all ex−TCS products. This manufacturing facility is located in the United Kingdom. We also have a contract manufacturing agreement with Dictaphone’s EMS division entered into by us simultaneously with the acquisition of CRS. Under this agreement EMS is the manufacturer of all ex−CRS products. This manufacturing facility is located in the United States.

Quality control is conducted at various stages at our manufacturing outsourcers' facilities and at their subcontractors' facilities. We generate reports to monitor our operations, including statistical reports that track the performance of our products from production to installation. This comprehensive data allows us to trace failure and to perform corrective actions accordingly.

We have qualified for and received the ISO−9001:2000 quality standard for all of our products.

Service and Support

We have focused on building a strong service and support organization for all our systems and have focused on rendering the various regions in which we operate to be as self sufficient as possible. Our dealers, as well as other telecommunications companies that market our products, are primarily responsible for supporting the day−to−day requirements of the end−users, while we provide technical support to such dealers and partners. In order to support our direct customers and partners, we established three regional support centers, the largest of which is in Denver, Colorado, to support our U.S. customers and partners, as well as one in Hong Kong to support APAC customers, dealers and partners, and one in the U.K. to support EMEA customers, dealers and partners. We maintain at our headquarters a staff of highly skilled customer service engineers that offer support to our dealers or partners that offer direct support to our customers. These service engineers, as well as additional service engineers located in our offices in the United States, EMEA and APAC, provide first class field services and support worldwide. We maintain regular training sessions for our dealers and installation support as well.

Following our acquisition of TCS in November 2002, we have increased our revenues from services while successfully integrating the ex−TCS services group. We now have a consolidated support group delivering services to both NICE and ex−TCS business partners and customers.

Our systems are generally sold with a warranty for repairs of hardware and software defects and malfunctions, the term of which is usually one year after shipment. Longer warranty periods are applicable to sales in certain international and government markets. Extended warranty and service coverage is provided in certain instances and is usually made available to customers through our distributors on a contractual basis for an additional charge. Our customers may purchase a renewable maintenance agreement from our dealers or directly from us. The maintenance agreements generally provide for maintenance, upgrades of standard system software and on−site repair or replacement.

For our telecommunications monitoring systems, we provide first and second tier service and support either directly using our support organization or indirectly through local companies working closely with the law enforcement agencies.

Research and Development

We believe that the development of new products and the enhancement of existing products are essential to our future success. Therefore, we intend to continue to devote substantial resources to research and new product development, and to continuously improve our systems and design processes in order to reduce the cost of our products. Our research and development efforts have been financed through our internal funds and programs sponsored through the Government of Israel. We believe our research and development effort has been an important factor in establishing and maintaining our competitive position. Gross expenditures on research and development in 2002, 2003 and 2004 were approximately $23.4 million, $26.4 million and $27.5 million, respectively, of which approximately $1.6 million, $1.3 million and $1.3 million, respectively, were derived from third−party funding, and $4.6 million, $2.3 million and $1.3 million, respectively, were capitalized software development costs.

In 2004, we were qualified to participate in six programs funded by the Office of the Chief Scientist, or OCS, of the Israeli Ministry of Industry, Trade and Labor to develop generic technology relevant to the development of our products. We are eligible to receive grants constituting between 20% and 66% of certain research and development expenses relating to these programs. As opposed to the standard type of OCS grants (described below), the grants under these programs are not required to be repaid. However, the restrictions of the Research and Development Law described below apply to these programs. In 2002, 2003 and 2004, we received a total of $1.4 million, $1.4 million and $0.8 million, respectively, and we anticipate receiving approximately $1.0 million in 2005, from these programs.

We are eligible to receive grants from the OCS under its “standard” program, constituting up to 50% of certain research and development expenses, for the research and development of approved technology. Under the terms of this program, we would be required to pay a royalty of 3% to 5% of the net sales of products incorporating technology developed in, and related services resulting from, a project funded by the OCS. The royalties are required to be paid beginning with the commencement of sales of such products and ending when 100% to 150% of the grant is repaid in New Israeli Shekels, or NIS, linked to the U.S. dollar plus LIBOR interest. In 2002, 2003 and 2004, we received no grants and incurred no royalty obligations under this program, and we have no further royalty obligations to the OCS.

The Research and Development Law generally requires that the product developed under an OCS−funded program be manufactured in Israel. However, upon the approval of the OCS, some of the manufacturing volume may be performed outside of Israel, provided that the grant recipient pays royalties at an increased rate, which may be substantial, and the aggregate repayment amount is increased to 120%, 150% or 300% of the grant, depending on the portion of the total manufacturing volume that is performed outside of Israel. Effective April 1, 2003, the Research and Development Law also allows for the approval of grants in cases in which the applicant declares that part of the manufacturing will be performed outside of Israel or by non−Israeli residents and the research committee is convinced that doing so is essential for the execution of the program. This declaration will be a significant factor in the determination of the Office of the Chief Scientist whether to approve a program and the amount and other terms of benefits to be granted. For example, the increased royalty rate and repayment amount will be required in such cases.

The Research and Development Law also provides that know−how developed under an approved research and development program may not be transferred to third parties in Israel without the approval of the Office of the Chief Scientist. Such approval is not required for the sale or export of any products resulting from such research or development. The Research and Development Law further provides that the know−how developed under an approved research and development program may not be transferred to any third parties outside Israel.

The Research and Development Law imposes reporting requirements with respect to certain changes in the ownership of a grant recipient. The law requires the grant recipient and its controlling shareholders and interested parties to notify the Office of the Chief Scientist of any change in control of the recipient or a change in the holdings of the means of control of the recipient that results in a non−Israeli becoming an interested party directly in the recipient and requires the new interested party to undertake to the Office of the Chief Scientist to comply with the Research and Development Law. In addition, the rules of the Office of the Chief Scientist may require prior approval of the Office of the Chief Scientist or additional information or representations in respect of certain of such events. For this purpose, “control” is defined as the ability to direct the activities of a company other than any ability arising solely from serving as an officer or director of the company. A person is presumed to have control if such person holds 50% or more of the means of control of a company. “Means of control” refers to voting rights or the right to appoint directors or the chief executive officer. An “interested party” of a company includes a holder of 5% or more of its outstanding share capital or voting rights, its chief executive officer and directors, someone who has the right to appoint its chief executive officer or at least one director, and a company with respect to which any of the foregoing interested parties owns 25% or more of the outstanding share capital or voting rights or has the right to appoint 25% or more of the directors. Accordingly, any non−Israeli who acquires 5% or more of our ordinary shares or ADSs will be required to notify the Office of the Chief Scientist that it has become an interested party and to sign an undertaking to comply with the Research and Development Law.

The funds available for Office of the Chief Scientist grants out of the annual budget of the State of Israel were reduced in recent years, and the Israeli authorities have indicated in the past that the government may further reduce or abolish Office of the Chief Scientist grants in the future. Even if these grants are maintained, we cannot presently predict what would be the amounts of future grants, if any, that we might receive.

In June 2005, an amendment to the Research and Development Law came into effect, which is intended to make it more compatible with the global business environment by, among other things, relaxing restrictions on the transfer of manufacturing rights outside Israel and on the transfer of OCS−funded know−how outside of Israel. The amendment permits the OCS to approve the transfer of manufacturing rights outside Israel in exchange for an import of different manufacturing into Israel as a substitute, in lieu of the increased royalties. The amendment further permits, under certain circumstances and subject to the OCS’s prior approval, the transfer of OCS−funded know−how outside Israel, in the following cases: (a) the subject company pays to the OCS a portion of the sale price paid in consideration for such funded know−how; (b) the subject company receives know−how from a third party in exchange for its funded know−how; or (c) such transfer of funded know−how arises in connection with certain types of cooperation in research and development activities.

Intellectual Property

We currently rely on a combination of trade secret, patent, copyright and trademark law, together with non−disclosure and non−compete agreements, to establish and/or protect the technology used in our systems. We hold the following eleven issued U.S. patents:

- No. 5,861,959 titled “Facsimile Long Term Storage and Retrieval System”
- No. 5,937,029 titled “Data Logging System Employing M[N + 1] Redundancy”
- No. 6,122,665 titled “Communication Management System”
- No. 6,046,824 titled “CIF – Facsimile Long Term Storage and Retrieval System”
- No. 6,330,025 titled “Digital Video Logging System”
- No. 6,542,602 titled “Telephone Call Monitoring System”
- No. 5,353,168 titled “Recording and Reproduction System using Time Division Multiplexing”
- No. 6,871,229 titled “Storing on a Computer Network−Based Telephone Session Performed Through a Computer Network”
- No. 6,865,604 titled “Extracting a Computer Network−Based Telephone Session Performed Through a Computer Network”
- No. 6,888,004 titled “Restoring a Portion of a Communication Session Transmitted Over a Computer Network”
- No. 6,856,343 titled “Digital Video Logging System”

We currently have nine other patents issued in additional countries and over 100 patent applications pending in the United States and other countries. We believe that the improvement of existing products, and the development of new products are important in establishing and maintaining a competitive advantage. We believe that the value of our products is dependent upon our proprietary software and hardware continuing to be “trade secrets” or subject to copyright or patent protection. We generally enter into non−disclosure and non−compete agreements with our employees and subcontractors. However, there can be no assurance that such measures will protect our technology, or that others will not develop a similar technology or use technology in products competitive with those offered by us. Although we believe that our products do not infringe upon the proprietary rights of third parties, there can be no assurance that one or more third parties will not make a contrary claim or that we will be successful in defending such claim.

From time to time, we receive “cease and desist” letters claiming patent infringements. However, no formal claims or other actions have been filed with respect to such alleged infringement, except for claims filed by Dictaphone (which have since been settled and dismissed) and Witness Systems. We believe that none of these has merit. We cannot assure you, however, that we will be successful in defending such claims, if asserted, or that infringement claims or other claims, if asserted, will not have a material adverse effect on our business, financial condition and results of operations. Defending infringement claims or other claims could involve substantial costs and diversion of management resources. In addition, to the extent we are not successful in defending such claims, we may be subject to injunctions with respect to the use or sale of certain of our products or to liabilities for damages and may be required to obtain licenses which may not be available on reasonable terms.

We own the following trademarks in different countries: 360^0 View™, Agent@home™, Executive Connect®, Executive Insight®, Experience Your Customer®, Freedom®, Investigator®, Lasting Loyalty™, Listen Learn Lead®, Mirra®, Universe®, My Universe™, NICE®, NiceAdvantage®, NICE Analyzer™, NiceCall™, NiceCall Focus™, NiceCLS™, NiceCMS™, NICE Feedback™, NiceFix™, NiceGuard™, NICE Learning™, NICE Link™, NiceLog®, NICE Playback Organizer™, Renaissance®, ScreenSense™, NiceScreen™, NiceSoft®, NICE Storage Center™, NiceTrack™, NiceUniverse®, NiceUniverse LIVE™, NiceVision®, NiceVision Harmony™, NiceVision Mobile™, NiceVision Pro™, NiceVision Virtual™, NiceVision® NVSAT™, NiceVision® Alto™, NiceWatch™, Secure Your Vision™, Scenario Replay™, Tienna®, Wordnet®, NICE Perform™, NICE Inform™, TRUNKNET® and Last Message Replay™. Applications to register certain of these marks have been filed in certain countries, including Australia, Brazil, the European Union, Germany, Great Britain, Israel, Japan, Mexico, Argentina and the United States. Some of such applications have matured to registrations.

Regulation

The export of certain defense products from Israel, such as our NiceTrack products, requires a permit from the Defense Sales and Exports branch of the Israeli Ministry of Defense, or SIBAT. In 2004, only a small portion of our sales were subject to such permit requirements. To date, we have encountered no difficulties in obtaining such permits. However, the Ministry of Defense notifies us from time to time not to conduct business with specific countries that are undergoing political unrest, violating human rights or exhibiting hostility toward Israel. We may be unable to obtain permits for our defense products we could otherwise sell in particular countries in the future.

Competition

The market for our enterprise interaction solutions is highly competitive and includes numerous products offering a broad range of features and capacities. As the market is still developing, we anticipate that a number of our existing and potential competitors will be introducing new and enhanced products. Some of our competitors in the digital voice recording and quality management for contact center agent monitoring businesses include Autonomy (formerly e−talk), Verint Systems Inc. (formerly Comverse Infosys), a subsidiary of Comverse Technology Inc., and Witness Systems Inc.

We believe that competition in the sale of our enterprise interaction solutions is based on a number of factors, including system performance and reliability, the ability to integrate with a variety of other computer and communications systems, marketing and distribution capacity, price and service and support. We believe that the wide range of features provided by the NiceLog system and related applications, their wide connectivity and compatibility with telephone and computer networks and their ease of use create a competitive advantage to the NiceLog and such related applications compared to other similar systems currently being offered on the market.

There are several small competitors who have products that compete with our video platform and applications. Our main competitors in this market are Dallmeier, Fast, Pelco, Verint Systems, and Visionwave.

In the public safety market, there are a number of competitors providing solutions, including ASC Telecom, AudioSoft, CVDS, Cybertech, Mercom, Voiceprint and Weston Digital.

There are a number of competitors in the telecommunications monitoring market, having products competing with our NiceTrack system, the major ones being Raytheon Company, Siemens and Verint Systems Inc. We believe that our solution offers innovations that provide law enforcement agencies the tools and capabilities they require to meet the challenges of today’s advanced telecommunications world, as well as being price competitive.

Organizational Structure

The following is a list of all of our significant subsidiaries, including the name, country of incorporation or residence, and the proportion of our ownership interest in each.

Name of Subsidiary	Country of Incorporation or Residence	Percentage of Ownership Interest
NICE Systems, Inc.	United States	100 %
NICE Systems GmbH	Germany	100 %
NICE Systems Canada Ltd.	Canada	100 %
NICE CTI Systems UK Ltd.	United Kingdom	100 %
STS Software Systems (1993) Ltd.*	Israel	100 %
NICE APAC Ltd.	Hong Kong	100 %
NiceEye BV*	Netherlands	100 %
NiceEye Ltd.*	Israel	100 %
Nice Systems S.A.R.L.	France	100 %
Racal Recorders Ltd.	United Kingdom	100 %
Nice Interactive Solutions India Private Ltd.	India	100 %
Nice Japan Ltd.	Japan	100 %
Nice Systems Latin America, Inc.	United States	100 %

* Inactive

Property, Plants and Equipment

Our executive offices and engineering, research and development operations are located in Ra'anana, Israel, where we occupy approximately 126,000 square feet of space, pursuant to a lease expiring in 2008. This lease may be terminated by us at any time from the year 2006, subject to certain conditions. The annual rent and maintenance fee for the facility is approximately $2.7 million linked to the changes in the U.S. consumer price index. We have various offices and other facilities in North America and in several other countries, as described below.

Our North American facilities consist of:

- Our North American headquarters in Rutherford, New Jersey, which occupy approximately 25,000 square feet, with a monthly rental of approximately $66,000. We also have a warehouse facility in Lyndhurst, New Jersey, which occupies approximately 6,000 square feet, with a monthly rental of approximately $7,000;
- Our office in San Diego, California, which occupies approximately 6,250 square feet, with a monthly rental of approximately $17,500 (subleased in its entirety to a third party);
- Our office in Chicago, Illinois, which occupies approximately 1,000 square feet, with a monthly rental of approximately $3,000;
- Our office in Denver, Colorado, which occupies approximately 30,775 square feet, with a monthly rental of approximately $58,000;
- Our office in Las Vegas, Nevada, which occupies approximately 3,000 square feet, with a monthly rental of approximately $8,000 (subleased in its entirety to a third party); and
- Our office in New York, New York, which occupies approximately 4,300 square feet, with a monthly rental of approximately $10,000.

Our international facilities consist of:

- Our office in Frankfurt, Germany, which occupies approximately 2,850 square feet, with a monthly rental of approximately $4,500;
- Our office in London, UK which occupies approximately 1,430 square feet, with a monthly rental of approximately $21,000;
- Our office in Southampton, UK which occupies approximately 34,249 square feet, with a monthly rental of approximately $66,000;
- Our office in Dublin, Ireland, which occupies approximately 750 square feet, with a monthly rental of approximately $2,200;
- Our office in Paris, France which occupies approximately 1,916 square feet, with a monthly rental of approximately $5,700;

- Our office in Hong Kong, which occupies approximately 4,810 square feet, with a monthly rental of approximately $11,426;

- Our office in Tokyo, which occupies approximately 1,485 square feet, with a monthly rental of approximately $6,428; and

- Our office in Bangalore, which occupies approximately 1,047 square feet, with a monthly rental of approximately $687.

We believe that our existing facilities are adequate to meet our current and foreseeable needs.

Item 5. Operating and Financial Review and Prospects.

We may from time to time make written or oral forward−looking statements, including in filings with the United States Securities and Exchange Commission ("SEC"), in reports to shareholders and in press releases and investor webcasts. You can identify these forward−looking statements by use of words such as "strategy", "expects", "continues", "plans", "anticipates", "believes", "may", "estimates", "intends", "projects", "goals", "targets", and other words of similar meaning. You can also identify them by the fact that they do not relate strictly to historical or current facts.

We cannot assure you that any forward−looking statement will be realized, although we believe we have been prudent in our plans and assumptions. Achievement of future results is subject to risks, uncertainties and inaccurate assumptions. Should known or unknown risks or uncertainties materialize, or should underlying assumptions prove inaccurate, actual results could vary materially from those anticipated, estimated or projected. Investors should bear this in mind as they consider forward−looking statements and whether to invest or remain invested in NICE Systems Ltd.'s securities. The forward−looking statements relate to, among other things: operating results; anticipated cash flows; gross margins; adequacy of resources to fund operations; our ability to maintain our average selling prices despite the aggressive marketing and pricing strategies of our competitors; our ability to maintain and develop profitable relationships with our key distribution partners, one of which constitutes 19% of our revenues; the financial strength of our key distribution partners; and the market's acceptance of our technologies, products and solutions.

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, we are identifying important factors that, individually or in the aggregate, could cause actual results and outcomes to differ materially from those contained in any forward−looking statements made by us; any such statement is qualified by reference to the following cautionary statements. Please read the section below entitled "Factors That May Affect Future Results" to review conditions that we believe could cause actual results to differ materially from those contemplated by the forward−looking statements. You should understand that it is not possible to predict or identify all risk factors. Consequently, you should not consider the following to be a complete discussion of all potential risks or uncertainties. Readers are cautioned not to place undue reliance on these forward−looking statements, which reflect our view only as of the date of this annual report. Except as required by law, we undertake no obligation to update these forward−looking statements to reflect future events or circumstances or the occurrence of unanticipated events.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the related notes and other financial information included elsewhere in this annual report.

Overview

We develop, market and support integrated, scalable multimedia digital recording platforms, enhanced software applications and related professional services. These solutions capture and analyze unstructured (non−transaction) data, and convert it into actionable knowledge for business and security performance management applications. Our solutions capture multiple forms of interaction, including voice, fax, email, web chat, radio, and video transmissions over wireline, wireless, packet telephony, terrestrial trunk radio and data networks. The markets from which we currently derive the majority of our revenues and expect to continue to do so in the future are highly competitive.

Our products are based on two types of recording platforms − audio and video − and are used primarily in contact centers, trading floors, public safety organizations, transportation, corporate security, gaming and correctional facilities as well as various government and intelligence agencies.

Our development efforts for our recording platforms are aimed at addressing several trends we see developing in the industry. The trend towards the proliferation of voice over IP−based networks is leading to a greater requirement for VoIP recording capabilities in financial trading, contact centers and public safety environments. The continued trend towards replacing analog video recording with digital video recording is leading to the need for network applications in the video recording area.

We also see the continuation of a trend towards requirements for multimedia recording capabilities, particularly in contact centers (voice, fax, email, chat screen) and public safety (voice, radio, video, data) markets. We are beginning to see this same trend developing in the financial trading sector, and we expect some Homeland Security initiatives in areas such as border control, critical infrastructure security, first responder communications and lawful interception to require multimedia capture platforms as well.

Our software applications enable our customers to capture, store, retrieve and analyze unstructured data (multimedia interactions) and combine them with data from other systems to create actionable knowledge that can be distributed via reports and alerts to all relevant parties to improve performance.

There is growing demand from our customers for software applications that will leverage the wealth of unstructured data captured by the recording platform to improve overall performance. In turn, as these enhanced software applications are being added, customers are considering our systems “mission critical”. We see an opportunity for applications that analyze the content of unstructured interactions in contact centers for quality monitoring and contact center management as well as for enterprise−wide process improvement and business performance management. We see a trend towards more software applications in the financial trading environment for compliance monitoring and dispute management to improve business performance. We see similar trends happening in digital video recording. We expect video content analysis applications to become increasingly important to building, campus, city center, and infrastructure perimeter security, loss prevention in casinos, retail and warehousing, as well as various homeland security applications to enable proactive security management.

We expect to see an increase in the demand for VoIP recording products, networked video security solutions, and multimedia recording solutions as well as an increase in the proportion of software from quality monitoring and multimedia interaction analytics applications in our product revenue mix and a gradual increase in the amount of professional services and maintenance revenues.

Our products are sold primarily through a global network of distributors, system integrators and strategic partners; a portion of product sales and most services are sold directly to end−users. One distributor accounted for approximately 19%, 20% and 23% of revenues in 2004, 2003 and 2002, respectively.

Acquisitions

The acquisitions we have made were accounted for as purchases, and, accordingly, the purchase price for each acquisition was allocated to the assets acquired and liabilities assumed based on their respective fair values. The results of operations related to each acquisition are included in our consolidated statement of operations from the date of acquisition. The following are details for each of these acquisitions:

- On June 1, 2005, we consummated an agreement to acquire the assets and assume certain liabilities of Dictaphone’s Communications Recording Systems business for approximately $38.5 million. Dictaphone’s CRS business is a leading provider of liability and quality management systems for first responders, critical facilities, contact centers and financial trading floors.

  Among the assets we acquired in the transaction are all of Dictaphone’s rights to receive any damage award or other economic benefit with respect to a violation of any of the rights related to the intellectual property of Dictaphone’s CRS business arising prior to the closing of the transaction.

- In November 2002, we consummated an agreement to acquire certain assets and liabilities of Thales Contact Solutions (or TCS), a developer of customer−facing technology for public safety, financial trading and customer contact centers, based in the United Kingdom. TCS was a unit of Thales Group, one of Europe’s premier electronics companies. In connection with the acquisition, we paid an initial $29.9

million in cash and issued 2,187,500 ordinary shares to Thales Group at a fair market value of $18.1 million calculated at the date of closing. As of June 2, 2005, Thales Group holds approximately 4.6% of our outstanding shares. In June 2005, Mr. Timothy Robinson, one of the two Thales executives who were elected to our Board of Directors in November 2002, resigned from our Board. The acquisition agreement required one nominee of Thales to resign upon the sale of more than half of the shares issued to Thales in the acquisition.

In the fourth quarter of 2002, we recorded a current liability of $2.8 million and a long−term liability of $13.5 million reflecting obligations under a long−term contract we assumed in the TCS acquisition. In the second quarter of 2003 we completed negotiations to terminate this contract as of November 2004 and to amend the terms in the interim. Under the terms of the amended contract, the cost to the Company was $5.2 million less than the amount provided at the acquisition date and consequently, TCS acquisition goodwill was reduced by this amount.

Under the terms of the agreement, the cash portion of the purchase price was subject to downward adjustment based on the value of net assets at closing and the full year 2002 sales of TCS. Based on our calculation of the actual value of net assets acquired and 2002 sales of TCS, we reduced the cash portion of the purchase price as of December 31, 2002 by $12.8 million. This amount was presented on our balance sheet as a Related Party Receivable as of December 31, 2002. Thus, the adjusted purchase price paid, including $4.5 million of capitalized acquisition costs, was recorded as $39.7 million. Of the $12.8 million adjustment referred to above, Thales paid us $6.6 million in March 2003.

Thales disputed our calculation of the net asset value at closing and the matter was submitted in September 2003 to binding arbitration by an Independent Accountant, in accordance with the terms of the acquisition agreement. The Independent Accountant determined a higher net asset value at closing than our calculation of the actual value of net assets acquired in the amount of $2.2 million. This additional amount was recorded as additional goodwill in the fourth quarter of 2003. The remaining Related Party Receivable as at December 31, 2003 of $ 4.0 million was paid in January 2004.

Also under the terms of the agreement, contingent cash payments of up to $10.0 million in 2003, $7.5 million in 2004, and $7.5 million in 2005 would be due if certain financial performance criteria are met as part of a three−year earn−out provision related to the sale of a particular product in 2002 through 2004. The relevant criteria for 2002 through 2004 were not met and therefore no contingent payments will be made under the agreement.

Under the terms of the agreement, the cash portion of the purchase price was subject to adjustment mechanisms and indemnities related to the assets sold to us. On September 8, 2004, we notified Thales of claims in respect of such price adjustment mechanisms, mainly relating to uncollected receivables and inventory. NICE and

Thales signed a settlement agreement in respect of such claims on February 24, 2005, according to which Thales paid us a total indemnity amount of $2.6 million.

- In April 2000, we acquired all of the outstanding capital stock of Centerpoint Solutions Inc. (CPS) for $3.0 million in cash and the issuance of 200,000 ADSs of NICE of which 50,000 were deemed target shares contingent upon the achievement of certain objectives, which were not met. CPS was a developer of internet−based applications for statistical monitoring, digital recording and automatic customer surveys for contact centers.

  In November 2002, we entered into a settlement agreement with Doug Chapiewski, the sole shareholder of CPS, in respect of allegations made against NICE and NICE−Centerpoint Solutions, Inc. of misrepresentation, breach of contract and securities fraud in connection with the acquisition of CPS. The terms of the settlement agreement, which included 50,000 shares, resulted in a charge to Other Expense, Net of $3.5 million. In December 2003, we received $300,000 from our insurers in respect of the settlement.

Other Developments

- We sold the net assets of our COMINT/DF military−related business to ELTA Systems Ltd ("ELTA") for $4.0 million on March 31, 2004. The net assets sold include the intellectual property, fixed assets, inventory, and contracts related to the COMINT/DF product line which includes high performance spectral surveillance and direction finding systems that detect, identify, locate, monitor and record transmission sources. The COMINT/DF business is therefore treated as a discontinued operation in our financial statements. In 2002, 2003 and 2004, the COMINT/DF business generated revenues of approximately $7.2 million, $6.5 million and $0.8 million, respectively, and net income of approximately $1.4 million, $1.5 million and $3.2 million (including gain on disposition), respectively.

Off−Balance Sheet Transactions

We have not engaged in nor been a party to off−balance sheet transactions.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with generally accepted accounting principles in the United States ("US GAAP"). Our significant accounting principles are presented within Note 2 to our Consolidated Financial Statements. While all the accounting policies impact the financial statements, certain policies may be viewed to be critical. These policies are those that are most important to the portrayal of our financial condition and results of operations. Actual results could differ from those estimates discussed below.

Management believes that the significant accounting policies which affect its more significant judgments and estimates used in the preparation of the consolidated financial statements and are the most critical to aid in fully understanding and evaluating our reported results include the following:

- Revenue recognition
- Allowance for doubtful accounts
- Inventory valuation
- Impairment of long−lived assets
- Deferred income taxes
- Contingencies

Revenue Recognition. We derive our revenue primarily from two sources: product revenues, which include hardware and software sales, and service revenues, which include, support and maintenance, installation, consulting and training revenue. Revenue related to sales of our products is generally recognized when persuasive evidence of an agreement exists; the product has been delivered and title and risk of loss have passed to the buyer; the sales price is fixed or determinable; no further obligations exist; and collectibility is probable. Sales agreements with specific acceptance terms are not recognized as revenue until the customer has confirmed that the product or service has been accepted.

Revenues from maintenance and professional services are recognized ratably over the contract period or as services are performed.

For arrangements with multiple elements, we allocate revenue to each component of the arrangement using the residual value method based on Vendor Specific Objective Evidence (“VSOE”) of the undelivered elements. This means that we defer the arrangement fee equivalent to the fair value of the undelivered elements until these elements are delivered. Our VSOE used to allocate the sales price to maintenance is based on the renewal percentage.

To assess the probability of collection for revenue recognition, we have an established credit policy that determines, by way of mathematical formulae based on the customers’ financial statements and payment history, the level of open account that is deemed probably collectible for each customer. These credit limits are reviewed and revised periodically on the basis of new customer financial statement information and payment performance.

We record a provision for estimated sales returns and allowances on product sales in the same period as the related revenues are recorded. We base these estimates on the historical sales returns ratio and other known factors. Actual returns could be different from our estimates and current provisions for sales returns and allowances may need to be increased.

Allowance for Doubtful Accounts. We evaluate the collectibility of our accounts receivable based on a combination of factors. 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. For all other customers, we recognize allowances for doubtful accounts based on the length of time the receivables are past due. Insured balances are not reserved. If the financial condition of one of our significant customers or our customers in general should deteriorate, our revenue growth may be limited and additional allowances may be required.

Inventory valuation. At each balance sheet date, we evaluate our inventory balance for excess quantities and obsolescence. This evaluation includes analyses of sales levels by product line and projections of future demand.   In addition, we write off inventories that are considered obsolete. Remaining inventory balances are adjusted to the lower of cost or market value. If future demand or market conditions are less favorable than our projections, additional inventory write−downs may be required and would be reflected in cost of sales in the period the revision is made.

During 2002 we completed the outsourcing of the manufacture of our audio and video product platforms. Under this arrangement, we take ownership of inventories at the conclusion of the manufacturing process, such inventories representing finished goods or spare parts.   As we largely manufacture to order, we do not tend to accumulate finished goods. We are, however, liable to purchase above a certain level, which is based on a historical level of orders to the contract manufacturer, excess raw material and subassembly inventories from the contract manufacturer deemed obsolete or slow−moving. We monitor the levels of the contract manufacturer's relevant inventories periodically and, if required, will write−off such deemed excess or obsolete inventory.

Impairment of long−lived assets. Our long−lived assets include property and equipment, investment in affiliates, goodwill and other intangible assets. The fair value of the investment in affiliates is dependent upon the performance of the companies in which we have invested. In assessing potential impairment of these investments, we consider this factor as well as the forecast financial performance of the investees and other pertinent information. We record an investment impairment charge when we believe that the investment has experienced a decline in value that is other than temporary. During 2002, we recognized $229,000 of impairment losses related to our investment in affiliates. As of December 31, 2004, the carrying value of the Company's investments in affiliates was $1.2 million.

In assessing the recoverability of our property and equipment, goodwill and other intangible assets, we must make assumptions regarding the estimated future cash flows and other factors to determine the fair value of the respective assets. If these estimates or their related assumptions change in the future, we may be required to record impairment charges for these assets.

In June 2001, the Financial Accounting Standards Board issued SFAS No. 142 "Goodwill and Other Intangible Assets". SFAS No. 142 addresses the initial recognition and measurement of intangible assets acquired in a business combination and the accounting for goodwill and other intangible assets subsequent to their acquisition. SFAS No. 142 provides that intangible assets with finite useful lives will be amortized and that goodwill and intangible assets with indefinite lives will not be amortized, but rather will be tested at least annually for impairment. We adopted SFAS No. 142 beginning January 1, 2002. Upon adoption of SFAS No. 142, we discontinued the amortization of recorded goodwill, which was approximately $3.4 million on an annual basis at that time. We performed an impairment test of our goodwill as of January 1, 2002 under the transitional provisions of SFAS No. 142; our test did not indicate an impairment of goodwill. We confirmed that we have only one reporting unit (the Company) to which we allocated all recorded goodwill, as well as all assets and liabilities.

By October 1, 2002, our stock price had declined significantly from January 1, 2002, at which point our market capitalization, based on our stock price, was below book value. The price of our ADSs on January 2, 2002 was $17.04 per ADS and declined to $8.47 per ADS on October 1, 2002. We determined the fair value of the Company based on relative market multiples for comparable businesses and a discounted cash flow model. This evaluation indicated that an impairment might exist. We then performed Step 2 under SFAS No. 142 in which an amount of the impairment loss, if any, must be measured. Four categories of intangible assets were identified as being separable from goodwill in accordance with SFAS No. 141 **"**Business Combinations**."** These included: trade names; an in−place distribution network; technology based intangible assets and maintenance contracts. In valuing the NICE trade name a relief from royalty method was used. Under this method, the value of a trade name reflects the savings realized by owning the trade name. The value of the intangible asset under the relief from royalty method is dependent upon the following factors: the selected royalty rate, the revenues expected to be generated from the underlying intellectual property, the discount rate and the expected life of the intellectual property. The value of our distribution network was determined through the use of the cost approach. Using this method, the value of the distribution network is estimated as the after−tax direct costs that a potential acquirer would avoid spending in recreating a similar functional distribution network. The value of the intangible asset under the cost method is dependent upon the estimated direct cost of establishing a new distributor relationship. Qualifying technology−based intangible assets consist of current and core technology and technologies that were under development at the valuation date. The current and core technology was valued using a derivation of the income approach, namely the excess earnings method. This method is used to analyze the earnings contribution of an intangible asset. Under this method, the excess earnings that an intangible asset generates are calculated over the intangible asset's expected life and discounted to the present to calculate the fair value of the intangible asset. Excess earnings are defined as the residual earnings after providing for appropriate returns on the other identified contributing assets. The value under the excess earnings method is dependent upon the following factors: the expected revenues generated by the intangible asset, the expected after−tax earnings on those revenues, the charges (or returns) required on other contributing assets and the discount rate. Our maintenance contracts, which are intangible assets under the contractual−legal criterion of SFAS No. 141, were valued using the excess earnings method. In determining the applicable discount rate to be used to estimate the fair value of our net assets, we calculated a market−derived rate based on the estimated weighted average cost of capital for the Company. In determining the cost of equity for the Company, we used a standard methodology based on the capital asset pricing model and analyzed selected guideline companies, industry data and factors specific to NICE. We expect to use a similar decision process in the future.

Following these analyses, we compared the carrying amount of goodwill to the implied fair value of the goodwill and determined that an impairment loss existed. A non−cash charge totaling $28.3 million was recorded in the fourth quarter of 2002 to write down goodwill to its fair value under the caption "Goodwill impairment". The valuation of long−lived assets requires significant estimates and assumptions. These estimates contain management's best estimates, using appropriate and customary assumptions and projections at the time. If different estimates or projections were used, it is reasonably possible that our analysis would have generated materially different results.

In the fourth quarter of 2004, we performed our annual test on the remaining goodwill per SFAS No. 142 requirements applying the same methodologies as those used in the prior year. No additional impairment was found to exist.

We will continue to perform an impairment test at least annually and on an interim basis should circumstances indicate that an impairment loss may exist. The outcome of such testing may lead to the recognition of an impairment loss.

Deferred income taxes. We record income taxes using the asset and liability approach. Deferred income tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax bases, and net operating loss and tax credit carryforwards. Our financial statements contain fully reserved tax assets which have arisen as a result of net operating losses, primarily incurred in 2001 and 2002, as well as other temporary differences between book and tax accounting. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We have considered future taxable income, prudent and feasible tax planning strategies and other available evidence in determining the need for a valuation allowance. We evaluate all of these factors to determine whether it is more likely than not that some portion or all of the deferred income tax assets will not be realized. As a result of uncertainty of realization of losses in future periods, we have continued to record a full valuation allowance, which was approximately $9.4 million as at December 31, 2004. The establishment and amount of the valuation allowance requires significant estimates and judgment and can materially affect our results of operations. If the realization of deferred tax assets in the future is considered more likely than not, an adjustment to the deferred tax assets would increase net income in the period such determination was made.

Our effective tax rate may vary from period to period based on changes in estimated taxable income or loss, changes to the valuation allowance, changes to state or foreign tax laws, future expansion into geographic areas with varying country, state and local income tax rates, deductibility of certain costs and expenses by jurisdiction and as a result of acquisitions, divestitures and reorganizations.

Contingencies. From time to time, we are 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 be charged to earnings, is made after careful and 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, such as a change in settlement strategy. A change in the required reserves would affect our earnings in the period the change is made.

Results of Operations

The following table sets forth selected consolidated income statement data for NICE for each of the three years ended December 31, 2004, 2003 and 2002 expressed as a percentage of total revenues. Figures may not add due to rounding.

	2002	2003	2004
Revenues			
Products	82.3%	74.9%	72.3%
Services	17.7	25.1	27.7
	100.0	100.0	100.0
Cost of revenues			
Products*	43.4	38.2	35.3
Services*	94.9	74.9	71.2
	52.5	47.4	45.2
Gross Profit	47.5	52.6	54.8
Operating expenses			
Research and development, net	11.0	10.2	9.8
Selling and marketing	24.9	23.9	24.7
General and administrative	15.3	13.3	12.4
Restructuring and other	(0.1)	0.8	0.0
In−process research and development	0.8	0.0	0.0
Legal settlement	0.0	2.3	0.0
Amortization of acquired intangibles	0.0	0.0	
Goodwill − impairment and other	18.0	0.0	0.0
Total operating expenses	70.0	50.6	46.9
Operating income (loss)	(22.5)	2.0	7.9
Financial income, net	2.6	0.9	1.4
Other income (expenses), net	(2.6)	0.1	0.0
Income (loss) before taxes	(22.5)	3.0	9.3
Taxes on income	0.2	0.5	0.9
Net income (loss) from continuing operations	(22.8)	2.5	8.4
Net income (loss) from discontinued operations	0.9	0.7	1.3
Net income (loss)	(21.9)	3.2	9.7

* percent of related revenue

YEARS ENDED DECEMBER 31, 2004 and 2003

REVENUES

Our total revenues rose approximately 13% to $252.6 million in 2004 from $224.3 million in 2003. Enterprise Interaction Solutions revenues were $194.1 million in 2004, an increase of 13% from the prior year, and revenues from sales to the public safety and security market were $58.5 million, an increase of 11% from the prior year. We believe that our growth in revenues was due principally to market share gains in these markets and market growth.

	Years Ended December 31,		$	%
	2003	2004	Change	Change
Product Revenues	$ 168.1	$ 182.6	14.5	8.6%
Service Revenues	56.2	70.0	13.8	24.6
Total Revenues	**$ 224.3**	**$ 252.6**	**28.3**	**12.6%**

The increase in product revenues was due primarily to higher sales of our audio recording platforms and applications to contact centers/trading floors and public safety institutions. There can be no assurance that we will continue to experience market share gains, or that our new products will be broadly accepted, or that given weak fiscal spending, we will continue to report growth in our platform and related software applications.

The increase in services revenues was generated by an increasing portion of our installed base engaging us for maintenance services and higher installation and training revenues related mainly to the increase in product sales to the enterprise market. Service revenues represented 28% of total revenues compared with approximately 25% in 2003. Although we typically generate lower profit margins on services than on products, our strategy is to continue to grow our global services business, which we believe increases the competitiveness of our product offerings, and thus expect services to represent a growing portion of total revenues in the future. Our long−term target is for services to represent approximately 30% of total revenues.

Revenues in 2004 in the Americas, which includes the United States, Canada and Latin and South America, rose 3% to $121.6 million from $118.6 million in 2003. The increase was largely attributable to higher post−contract support. Sales to Europe, Middle East and Africa (“EMEA”) rose 26% to $93.2 million in 2004 from $73.8 million in 2003. The increase was due mainly to higher sales to the enterprise market and post−contract support. Sales to Asia−Pacific (“APAC”) increased 19% to $37.8 million in 2004 from $31.8 million in 2003 due mainly to higher sales to the enterprise market in the region.

COST OF REVENUES:

	Years Ended December 31, 2003	2004	$ Change	% Change
Cost of Product Revenues	$ 64.2	$ 64.4	0.2	0.3%
Cost of Service Revenues	42.1	49.9	7.8	18.5
Total Cost of Revenues	**$ 106.3**	**$ 114.3**	**8.0**	**7.5%**

The slight increase in cost of product revenues was due mainly to the higher sales volume. The increase in cost of services revenue was due principally to higher labor, subcontractor and material costs associated with the growth in product installations and maintenance contracts.

GROSS PROFIT

	Years Ended December 31, 2003	2004	$ Change	% Change
Gross Profit on Product Revenues	$ 103.9	$ 118.2	14.3	13.8%
as a percentage of product revenues	*61.8%*	*64.7%*		
Gross Profit on Service Revenues	14.1	20.1	6.0	42.6
as a percentage of service revenues	*25.1%*	*28.8%*		
Total Gross Profit	**$ 117.9**	**$ 138.3**	**20.4**	**17.3%**
as a percentage of total revenues	*52.6%*	*54.8%*		

The improvement in gross profit on product revenues was due primarily to the higher sales volume, product cost reductions and a higher proportion of software in the product mix. The improvement in gross profit margin on services revenue reflects improved staff utilization and efficiencies. On a forward−looking basis, we expect our gross margins to increase gradually to the extent that we are successful in realizing the benefit of a growing proportion of software applications in our product revenue mix, higher volume and improved efficiencies in our global service operations.

EXPENSES

	Years Ended December 31, 2003	2004	$ Change	% Change
Research and development, net	$ 22.8	$ 24.9	2.1	9.2
Selling and marketing	53.7	62.2	8.5	15.8
General and administrative	29.8	31.3	1.5	5.0

Research and Development, Net. Research and development expense, before capitalization of software development costs and grants, increased to $27.5 million in 2004 from $26.4 million in 2003 and represented 10.9% and 11.8% of revenues in 2004 and 2003, respectively. The increase in gross outlays was due mainly to the increase of R&D labor costs.

Software development costs capitalized were $1.3 million in 2004 compared with $2.3 million in 2003. Amortization of capitalized software development costs, included in cost of product revenues, was $4.1 million and $5.7 million in 2004 and 2003, respectively.

Selling and Marketing Expenses. The increase in selling and marketing expenses was due primarily to an increase in our corporate and regional sales and marketing efforts and higher sales commissions resulting mainly from the increase in sales. Selling and marketing expenses represented 24.6% of total revenues in 2004 compared with 23.9% in 2003. We expect that we will continue to leverage our global sales and distribution infrastructure and will increase our corporate and regional marketing efforts in the future.

General and Administrative Expenses. The increase in general and administrative expenses in 2004 was due principally to increase in labor costs and depreciation expenses. General and administrative expenses represented 12.4% of total revenues in 2004 compared with 13.3% in 2003. On a forward−looking basis, general and administrative expenses, while increasing on an absolute dollar basis, are expected to decline as a percentage of total revenues.

OTHER SPECIAL CHARGES:

	Years Ended December 31,		
	2003	**2004**	**$ Change**
Restructuring	$ 1.9	0.0	(1.9)
Legal Settlement	5.2	0.0	(5.2)
	$ 7.1	**0.0**	**(7.1)**

Restructuring. In December 2002 we adopted a restructuring plan, which involved the phased reduction of approximately 75 of our 1,077 staff members and consolidation of certain offices. Some of the involuntary reductions were effected in December 2002 and, in accordance with SFAS No. 146, a liability of $282,000 was recorded as of December 31, 2002 related to those terminations. This liability was utilized as of June 30, 2003. The remaining reductions in force and facility closures were implemented during 2003. We included in our results for 2003 costs of approximately $1.9 million, which related primarily to involuntary terminations and facility closures.

Legal Settlement. In June 2000, Dictaphone Corporation, one of our competitors, filed a patent infringement claim relating to certain technology embedded in some of our products. The claim was for damages for past infringement and enjoinment of any continued infringement of Dictaphone patents. In the fourth quarter of 2003, we reached a settlement with Dictaphone in which both parties agreed to dismiss all claims and counterclaims connected with the aforementioned patent infringement claim. The terms of the settlement call for us to pay Dictaphone $10 million of which approximately $4.8 million was paid by our insurance carrier in December 2003 and the balance was paid by us, except for the final installment in the amount of $333,335. This amount is required to be paid by us by June 30, 2005, subject to certain events which could result in a reduced payment by us. As a result, a charge of approximately $5.2 million was recorded in the last quarter of 2003. The companies also agreed to grant each other a worldwide, royalty−free, perpetual license to certain of their patents including the disputed patents. The companies further agreed to enter into enforcement proceedings with respect to both companies' patent portfolios and to share any proceeds from these actions. As a result of our acquisition of the CRS division of Dictaphone on June 1, 2005, the agreement with respect to patents was terminated since we acquired the relevant patents.

FINANCIAL AND OTHER INCOME

	Years Ended December 31, 2003	2004	$ Change	% Change
Financial income	$ 2.0	$ 3.6	1.4	70.0%
Other income (expense)	0.3	0.1	(0.2)	−66.7

Financial Income, Net. The increase in financial income, net reflects a higher average cash balance and higher prevailing average interest rates in 2004 compared with 2003.

Other Income (Expense), Net. Other income, net was $0.1 million in 2004 compared with $0.3 million in 2003. In 2003, we recorded $0.3 million of income reflecting amounts received from our insurance carrier in respect of the Chapiewski settlement. In 2004, other income represented a capital gain recognized upon the disposal of fixed assets.

Taxes on Income. In 2004, we recorded a provision for income taxes of $2.3 million compared with $1.2 million in 2003. The increase was primarily related to operating profits recorded at certain distribution subsidiaries.

Net Income (Loss) from Continuing Operations. Net income from continuing operations was $21.3 million in 2004 compared with $5.6 million in 2003. The increase in 2004 resulted primarily from the increase in revenues and gross margin.

Net Income from Discontinued Operations. As discussed above under "Other Developments", on March 31, 2004 we sold the assets of our COMINT/DF military−related business to ELTA for $4 million in cash. Net income from this discontinued operation was approximately $3.2 million (including gain on disposition) and $1.5 million for 2004 and 2003, respectively.

YEARS ENDED DECEMBER 31, 2003 and 2002

REVENUES

Total revenues from the enterprise market were $171.4 million in 2003, an increase of 41% from the prior year. Total revenues from the public safety and security market were $52.8 million, an increase of 60% from the prior year. We believe that our growth in revenue was due principally to market share gains in the enterprise and public safety and security markets following the acquisition of TCS in November 2002, and continued penetration of our digital video platform in the security market.

	Years Ended December 31, 2002		Years Ended December 31, 2003		$ Change		% Change
Product Revenues	$	127.9	$	168.1	$	40.2	31.4%
Service Revenues		27.4		56.2		28.8	105.1
Total Revenues	**$**	**155.3**	**$**	**224.3**	**$**	**69.0**	**44.4%**

The increase in product revenues was due primarily to higher sales of our audio recording platforms and applications to enterprise and public safety markets related mainly to the inclusion for a full year of the operations of TCS and market share gains.

The increase in services revenues reflects an increasing portion of our installed base engaging us for maintenance services and higher installation and training revenues related mainly to the increase in product sales to enterprise market.

Revenues in 2003 in the Americas rose 36% to $118.6 million from $86.9 million in 2002. The increase was largely attributable to higher sales of enterprise solution and post−contract support. Sales to EMEA rose 55% to $73.8 million in 2003 from $47.7 million in 2002. The increase was due mainly to the inclusion for a full year of the operations of TCS and favorable currency movements. Sales to APAC increased 54% to $31.8 million in 2003 from $20.7 million in 2002 due mainly to higher sales to the enterprise market in Japan, Australia/New Zealand and India.

COST OF REVENUES:

	Years Ended December 31, 2002		Years Ended December 31, 2003		$ Change		% Change
Cost of Product Revenues	$	55.5	$	64.2	$	8.7	15.7%
Cost of Service Revenues		26.1		42.1		16.0	61.3
Total Cost of Revenues	**$**	**81.5**	**$**	**106.3**	**$**	**24.8**	**30.4%**

The increase in cost of product revenues in 2003 was due mainly to higher sales volume. The increase in cost of services revenue was due principally to higher labor, subcontractor and material costs associated with the inclusion of TCS activities for a full year and with the growth in product installations and maintenance contracts.

GROSS PROFIT

	Years Ended December 31, 2002	2003	$ Change	% Change
Gross Profit on Product Revenues	$ 72.4	$ 103.9	$ 31.5	43.5%
as a percentage of product revenues	*56.6%*	*61.8%*		
Gross Profit on Service Revenues	1.4	14.1	12.7	100.0+
as a percentage of service revenues	*5.1%*	*25.1%*		
Total Gross Profit	**$ 73.8**	**$ 117.9**	**$ 44.1**	**59.8%**
as a percentage of total revenues	*47.5%*	*52.6%*		

The improvement in gross profit on product revenues was due primarily to the higher sales volume, product cost reductions and a higher proportion of software in the product mix. Gross profit margin on services revenue was 25% in 2003 compared with 5% in 2002 reflecting improved staff utilization and efficiencies.

EXPENSES

	Years Ended December 31, 2002	2003	$ Change	% Change
Research and development, net	$ 17.1	$ 22.8	$ 5.7	33.3%
Selling and marketing	38.7	53.7	15.0	38.8
General and administrative	23.8	29.8	6.0	25.2

Research and Development, Net. Research and development expense, before capitalization of software development costs and grants, increased to $26.4 million in 2003 from $23.4 million in 2002 and represented 11.8% and 15.0% of revenues in 2003 and 2002, respectively. The increase in gross outlays was due mainly to the inclusion for a full year of acquired TCS R&D activities and of the impact of the appreciation of the New Israel Shekel to the US dollar on R&D labor costs, as approximately 80% of our R&D staff is based in Israel.

Software development costs capitalized were $2.3 million in 2003 compared with $4.6 million in 2002. Net research and development expense increased 33% in 2003 to $22.8 million from $17.1 million in 2002. Amortization of capitalized software development costs, included in cost of product revenues, was $5.7 million and $4.3 million in 2003 and 2002, respectively.

Selling and Marketing Expenses. The increase in selling and marketing expenses was due primarily to the inclusion for a full year of the activities of TCS and higher sales commissions resulting mainly from the increase in sales.

General and Administrative Expenses. The increase in general and administrative expenses in 2003 was due principally to the inclusion of TCS administrative costs for a full year, higher corporate insurance premiums and the impact of the appreciation of the New Israel Shekel to the US dollar on labor and facility costs only partly offset by lower additions to doubtful debt reserves.

OTHER SPECIAL CHARGES:

	Years Ended December 31, 2002	Years Ended December 31, 2003	$ Change
Restructuring	$ (0.1)	$ 1.9	$ 2.0
In−process research and development	1.3	0.0	(1.3)
Goodwill − Impairment and other	27.9	0.0	(27.9)
Legal Settlement	0.0	5.2	5.2
	$ 29.1	**$ 7.1**	**$ (22.0)**

Restructuring. As described above, in December 2002 we adopted a restructuring plan which involved the phased reduction of approximately 75 of our 1,077 staff members and consolidation of certain offices. Some of the involuntary reductions were effected in December 2002 and, in accordance with SFAS No. 146, a liability of $282,000 was recorded as of December 31, 2002 related to those terminations. This liability was utilized as of June 30, 2003. The remaining reductions in force and facility closures were implemented during 2003. We included in our results for 2003 costs of approximately $1.9 million, which related primarily to involuntary terminations and facility closures. Restructuring related charges for 2002 of $0.1 million consisted of the $282,000 expense noted above offset by a reduction of $400,000 to the accrual remaining from the 2001 restructuring plan.

In−process Research and Development. In 2002, in connection with the acquisition of TCS and in accordance with SFAS No. 2 "Accounting for Research and Development Costs", a portion of the purchase price, $1.3 million, was allocated to purchased in−process research and development. As part of the process of analyzing this acquisition, we made a decision to buy three technologies that had not yet been commercialized rather than develop those technologies internally. In doing so, we considered our internal research resource allocation and our progress on comparable technology, if any. At the date of the acquisition, technological feasibility had not yet been established for the in−process research and development projects and they had no alternative future use. Accordingly, the fair value allocated to these technologies, which was based on an analysis of the discounted excess earnings that the intangible assets generate over their expected lives, was immediately expensed at acquisition.

Goodwill Impairment and Other. During the fourth quarter of 2002 we performed our annual impairment test of acquired intangible assets as prescribed by SFAS No. 142. Our stock price had declined significantly from January 1, 2002, at which point our market capitalization, based on our stock price, was below book value. We determined the fair value of the Company based on relative market multiples for comparable businesses and a discounted cash flow model. This evaluation indicated that an impairment loss might exist. We then performed Step 2 under SFAS No. 142 and compared the carrying amount of goodwill to the implied fair value of the goodwill and determined that an impairment loss existed. A non−cash charge totaling $28.3 million was recorded in the fourth quarter of 2002 to write down the goodwill recorded primarily in the acquisitions of SCI, CPS and STS to its fair value.

In the fourth quarter of 2003, we performed our annual test on the remaining goodwill per SFAS No. 142 requirements applying the same methodologies as those used in the prior year. No additional impairment was found to exist. As of December 31, 2003, we had $32.1 million of non−amortizable goodwill and other intangible assets.

Legal Settlement. As described above, in June 2000, Dictaphone Corporation, one of our competitors, filed a patent infringement claim relating to certain technology embedded in some of our products. The claim was for damages for past infringement and enjoinment of any continued infringement of Dictaphone patents. In the fourth quarter of 2003, we reached a settlement with Dictaphone in which both parties agreed to dismiss all claims and counterclaims connected with the aforementioned patent infringement claim. The terms of the settlement call for us to pay Dictaphone $10 million of which approximately $4.8 million was paid by our insurance carrier in December 2003 and the balance was paid by us, except for the final installment in the amount of $333,335. This amount is required to be paid by us by June 30, 2005, subject to certain events which could result in a reduced payment by us. As a result, a charge of approximately $5.2 million was recorded in the last quarter of 2003. The companies also agreed to grant each other a worldwide, royalty−free, perpetual license to certain of their patents including the disputed patents. The companies further agreed to enter into enforcement proceedings with respect to both companies' patent portfolios and to share any proceeds from these actions. As a result of our acquisition of the CRS division of Dictaphone on June 1, 2005, the agreement with respect to patents was terminated since we acquired the relevant patents.

FINANCIAL AND OTHER INCOME

	Years Ended December 31,		$	%
	2002	2003	Change	Change
Financial income	$ 4.0	$ 2.0	$ (2.0)	(50.0)%
Other income (expense)	(4.1)	0.3	4.4	107.3

Financial Income, Net. The decrease in financial income, net reflects lower prevailing average interest rates and lower net foreign exchange gains realized in 2003 compared with 2002.

Other Income (Expense), Net. In 2002, we recorded expenses of $3.5 million related to the settlement of claims by Douglas Chapiewski, the former sole shareholder of CPS, $335,000 representing the cost of moving our North American headquarters to a different facility, and $229,000 to write−off our long−term investment in Espro Ltd. In 2003, we recorded $300,000 of income reflecting amounts received from our insurance carrier in respect of the Chapiewski settlement.

Taxes on Income. In 2003, we recorded a provision for income taxes of $1.2 million compared with $0.4 million in 2002. The increase was primarily related to changes in the tax law in Israel in 2003 and operating profits recorded at certain distribution subsidiaries.

Net Income (Loss) from Continuing Operations. Net income from continuing operations was $5.6 million in 2003 compared with a net loss of $35.4 million in 2002. The increase in

2003 resulted primarily from the increase in revenues and gross margin, and the inclusion of $7.1 million of other special charges in 2003 compared with $29.1 million in 2002.

Net Income from Discontinued Operations. As discussed above under “Other Developments”, on March 31, 2004 we sold the assets of our COMINT/DF military−related business to ELTA for $4 million in cash. Net income from this discontinued operation was approximately $1.5 million and $1.4 million for 2003 and 2002, respectively.

Liquidity and Capital Resources

We have historically financed our operations through cash generated from operations and sales of equity securities. Generally, we invest our excess cash in instruments that are highly liquid, investment grade securities. At December 31, 2004, we had approximately $165.9 million of cash and cash equivalents and short and long−term investments compared with $107.3 million at December 31, 2003 and $68.6 million at December 31, 2002. The increase in 2004 was due to higher net income in 2004 and the proceeds from the issuance of shares upon the exercise of stock options and under our employee share purchase plan. The increase in 2003 from 2002 was due mainly to net income versus net loss in 2002.

Cash provided by operating activities of continuing operations was $44.3 million and $36.9 million in 2004 and 2003, respectively, compared with $16.7 million in 2002. The improvement in 2004 compared with 2003 was primarily attributable to higher net operating income. The improvement in 2003 compared with 2002 was primarily attributable to our moving from a net operating loss to a net operating income position. Also contributing to the increase in cash provided by operating activities was our continued improvement in accounts receivable day’s sales outstanding (or DSO) to 67 days at December 31, 2004 compared to 74 days at December 31, 2003 and 112 days at December 31, 2002. This improvement was primarily attributable to the implementation of process change improvements and our credit policy. We expect to see our DSO levels remain between 70 and 80 days as we continue to place particular focus on managing our working capital, particularly the level of accounts receivable day’s sales outstanding. In connection with the TCS acquisition, we recorded a current liability of $2.8 million and a long−term liability of $13.5 million in 2002 reflecting obligations under a long−term contract assumed by NICE. We reached agreement to terminate this contract in 2003 and amend the terms in the interim. Under the terms of the amended contract, the cost to us is $5.2 million less than the amount provided at the November 2002 acquisition date.

Net cash used in investing activities from continuing operations was $72.3 million and $39.8 million in 2004 and 2003, respectively, compared with $28.2 million in 2002. The increases in 2004 and 2003 are mainly due to investments in marketable securities. Capital expenditures were $6.7 million in 2004, $5.5 million in 2003, and $5.3 million in 2002. Capital expenditures in 2003 and 2004 included investment in back−office IT systems, equipment for research and development and testing purposes, and general computer equipment. In 2002 capital expenditures related primarily to investment in additional modules for our global ERP system including the implementation of the order management and financial systems modules at TCS’

Southampton facility following the acquisition, and equipment for research and development and demonstration purposes. As of December 31, 2004, we had no material commitment for capital expenditures.

Net cash provided by financing activities was $19.9 million, $12.1 million and $2.1 million in 2004, 2003 and 2002 respectively, almost entirely as a result of net proceeds from the issuance of shares upon the exercise of stock options and under our employee share purchase plan. As of December 31, 2004, we had authorized credit lines from banks in the amount of $139 million. When utilized, the credit lines will be denominated in dollars and will bear interest at the rate of up to LIBOR + 1.5 % per year. An amount of $116 million out of the total credit lines is secured by our marketable securities. There are no financial covenants associated with these credit lines. As of December 31, 2004, $5.8 million of the $139 million referred to above was used for bank guarantees.

We believe that based on our current operating forecast, the combination of existing working capital, expected cash flows from operations and available credit lines will be sufficient to finance our ongoing operations for the next twelve months. This belief takes into consideration the steps we have taken to limit certain customer−related risks through insuring a significant portion of our accounts receivable and achieving ISO 9000−2001 certification to help ensure the quality of our products and services, which in turn lowers our exposure to certain commercial risks. Depending upon our future growth, the success of our business initiatives and acquisition opportunities, and our transition towards an enterprise software business model, we will consider from time to time various financing alternatives and may seek to raise additional capital to finance our strategic efforts through debt or equity financing, the sale of non−strategic assets or entry into strategic arrangements.

Set forth below are our contractual obligations and other commercial commitments over the medium term as of December 31, 2004 ($ in thousands):

Contractual Obligations	Total	Payments Due by Period Less than 1 year	1−3 years	3−5 years	More than 5 years
Long−Term Debt					
Capital Lease Obligations					
Operating Leases	15,381	5,842	8,929	610	
Unconditional Purchase Obligations	4,654	2,887	1,623	144	
Other Long−Term Obligations					
Total Contractual Cash Obligations	20,035	8,729	10,552	754	

Other Commercial Commitments	Total Amounts Committed	Amount of Commitment Expiration Per Period Less than 1 year	1−3 years	3−5 years	More than 5 years
Lines of Credit					
Standby Letters of Credit					
Guarantees – continuing operations	2,254	859	343		1,052
Guarantees – discontinued operation	3,463	3,463			
Standby Repurchase Obligations					
Other Commercial Commitments					
Total Commercial Commitments	5,717	4,322	343		1,052

Qualitative and Quantitative Disclosure About Market Risk

Market risks relating to our operations result primarily from weak economic conditions in the markets in which we sell our products and changes in interest rates and exchange rates. To manage the volatility related to the latter exposure, we may enter into various derivative transactions. Our objective is to reduce, where it is deemed appropriate to do so, fluctuations in earnings and cash flows associated with changes in currency exchange rates. It is our policy and practice to use derivative financial instruments only to manage exposures. We do not use financial instruments for trading purposes and are not a party to any leveraged derivative.

Foreign Currency Risk*.* We conduct our business primarily in US dollars but also in the currencies of the United Kingdom, Canada, the European Union, Israel as well as other currencies. Thus, we are exposed to foreign exchange movements, primarily in UK, European and Israel currencies. We monitor foreign currency exposure and, from time to time, may enter into various derivative transactions to preserve the value of sales transactions and commitments.

Interest Rate Risk**.** We invest in investment−grade US corporate bonds and dollar deposits with FDIC−insured US banks. At least 80% of our securities investments are in corporate and US government agency bonds. Since these investments carry fixed interest rates and since our policy and practice is to hold these investments to maturity, interest income over the holding period is not sensitive to changes in interest rates. Up to 20% of our investment portfolio may be invested in investment grade Callable Range Accrual Notes whose principal is guaranteed. As of December 31, 2004, 10% of our investment portfolio consisted of such Notes. The Notes are subject to interest rate, liquidity and price risks. Since our policy is to hold these investments to maturity or until called, the interest income from these notes will not be effected by changes in their market value or to liquidity risk. However, a significant increase in prevailing interest rates may effect whether or not interest income is received for a particular period. As of December 31 2004, 10% of our investment portfolio is invested in auction rate securities. Since our policy is to hold these auction rate securities until their interest reset date, we face potential capital loss if interest in the market rises dramatically during the holding period (up to 28 days).

Recently Issued or Adopted Accounting Pronouncements

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued Statement No. 123 (revised 2004), “Share−Based Payment” (“Statement 123R”), which is a revision of FASB Statement No. 123, “Accounting for Stock−Based Compensation” (“Statement 123”). Generally, the approach in Statement 123R is similar to the approach described in Statement 123. However, Statements 123 permitted, but not required, share−based payments to employees to be recognized based on their fair values while Statement 123R requires all share−based payments to employees to be recognized based on their fair values. Statement 123R also revises, clarifies and expands guidance in several areas, including measuring fair value, classifying an award as equity or as a liability and attributing compensation cost to reporting periods. The new Standard will be effective with respect to us in the first fiscal year beginning after June 15, 2005. The adoption of Statement 123R will have a significant effect on our results of operations.

In November 2004, the FASB issued Statement of Financial Accounting Standard No. 151, “Inventory Costs, an Amendment of ARB No. 43, Chapter 4.” (“SFAS 151”). SFAS 151 amends Accounting Research Bulletin (“ARB”) No. 43, Chapter 4, to clarify that abnormal amounts of idle facility expense, freight handling costs and wasted materials (spoilage) should be recognized as current−period charges. In addition, SFAS 151 requires that the allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. We do not expect that the adoption of SFAS 151 will have a material effect on our financial position or results of operations.

Factors That May Affect Future Results

We operate globally in a dynamic and changing environment that involves numerous risks and uncertainties. The following section lists some, but not all, of those risks and uncertainties that could cause actual results and outcomes to differ materially from those contained in any forward−looking statement made by us or on our behalf. Other risks and uncertainties that could affect actual results and outcomes are described in Item 3 of this Report under "Risk Factors."

New Accounting Pronouncements Require Us to Change the Way in Which We Account for Employee Stock Options. Commencing with fiscal year 2006, we will be required by applicable accounting principles to record as expenses all share−based payments to employees based on their fair values. This will result in increased expenses in our statement of operations and a consequent reduction of our net income and earnings per share.

The Overall Economic Environment Continues to be Weak. We are subject to the effects of general global economic and market conditions. Our operating results have been adversely affected as a result of unfavorable economic conditions and reduced information technology spending, particularly in the product segments in which we compete. During 2002 and 2003, and continuing through 2004, there was an increase in demand for our type of products as customers allocated resources to enhance their recording and analysis capabilities for compliance and risk management and for security. However, customer purchase decisions may be significantly affected by a variety of factors including trends in spending for information technology and enterprise software, market competition, and the viability or announcement of alternative technologies. If economic conditions continue to be weak, demand for our products could decrease resulting in lower revenues, profits and cash flows.

Our Business Strategy Continues to Evolve. Historically we have supplied the hardware and some software for implementing multimedia recording solutions. Our shift towards providing professional support services and an enterprise software business model has required and will continue to require substantial change, potentially resulting in some disruption to our business. These changes may include changes in management and technical personnel; expanded or differing competition resulting from entering the enterprise software market; increased need to expand our distribution network to include system integrators which could impact revenues and gross margins, and, as our applications are sold either to our installed base or to new customers together with our recording platforms, the rate of adoption of our software applications by the market.

We May Experience Difficulty Managing Changes in Our Business. The changes in our business may place a significant strain on our operational and financial resources. We may experience substantial disruption from changes and could incur significant expenses and write−offs. Failing to carefully manage expense and inventory levels consistent with product demand and to carefully manage accounts receivable to limit credit risk, could materially adversely affect our results of operations.

Our Service Revenues are Dependent on Our Installed Base of Customers. We derive a significant portion of our revenues from services, which include maintenance, project management, support and training. As a result, if we lose a major customer or if a support contract is delayed or cancelled, our revenues would be adversely affected. In addition, customers who have accounted for significant services revenues in the past may not generate revenues in future periods. Our failure to obtain new customers or additional orders from existing customers could also materially affect our results of operations.

Risks Associated with Our Distribution Channels May Materially Adversely Affect Our Financial Results. We have agreements in place with many distributors, dealers and resellers to market and sell our products and services in addition to our direct sales force. We derive a significant percentage of our revenues from one of our distributor channels and new channels may, in the future, account for a significant percentage of our revenues. Our top channel partner accounted for approximately 19%, 20% and 23% of our revenues in 2004, 2003 and 2002, respectively. Our financial results could be materially adversely affected if our contracts with channel partners were terminated, if our relationship with channel partners were to deteriorate or if the financial condition of our channel partners were to weaken. In addition, as our market opportunities change, we may have increased reliance on particular channel partners, which may negatively impact gross margins. There can be no assurance that we will be successful in maintaining or expanding these channels. If we are not successful, we may lose sales opportunities, customers and market share. In addition, some of our channel partners are suppliers of telecommunication infrastructure equipment. There can be no assurance that our channel partners will not develop or market VoIP, software applications and storage products and services in competition with us in the future.

Our Uneven Sales Patterns Could Significantly Impact Our Quarterly Revenues and Earnings. The sales cycle for our products and services is variable, typically ranging between a few weeks to several months from initial contact with the potential client to the signing of a contract. Frequently, sales orders accumulate towards the latter part of a given quarter. Looking forward, given the lead−time required by our contract manufacturer, if a large portion of sales orders are received late in the quarter, we may not be able to deliver products within the quarter and thus such sales will be deferred to a future quarter. There can be no assurance that such deferrals will result in sales in the near term, or at all. Thus, delays in executing client orders may affect our revenue and cause our operating results to vary widely. Additionally, as a high percentage of our expenses, particularly employee compensation, is relatively fixed, a variation in the level of sales, especially at or near the end of any quarter, may have a material adverse impact on our quarterly operating results.

Competitive Pricing and Difficulty Managing Product Costs Could Materially Adversely Affect Our Revenues and Earnings. The market for our products and related services, in general, is highly competitive. Additionally, some of our principal competitors such as Witness Systems, Inc. and Verint Systems, Inc. may have significantly greater resources and larger customer bases than do we. We have seen evidence of deep price reductions by our competitors and expect to continue to see such behavior in the future, which, if we are required to match such discounting, will adversely affect our gross margins and results of operations. To date, we have been able to manage our product design and component costs. However, there can be no assurance that we will be able to continue to achieve reductions in component and product design costs. Further, the relative and varying rates of increases or decreases in product price and cost could have a material adverse impact on our earnings.

Our Gross Margins are Highly Dependent upon Our Product Mix. It is difficult to predict the exact mix of products for any period between hardware, software and services as well as within the product category between audio platforms and related applications and digital video. As each of our product types and services have different gross margins, changes in the mix of products in a period will have an impact, and perhaps a material impact, on our gross profit and net income in that period.

If Our Suppliers Are Not Able to Meet Our Requirements, We Could Have Decreased Revenues and Earnings:

- In 2002, we migrated the manufacturing of all of our key products to a contract manufacturer. The TCS product line is also manufactured by a third party. We may experience delivery delays due the inability of the outsourcers to consistently meet our quality or delivery requirements. If these suppliers or any other supplier were to cancel contracts or commitments with us or fail to meet the quality or delivery requirements needed to satisfy customer orders for our products, we could lose time−sensitive customer orders and have significantly decreased quarterly revenues and earnings, which would have a material adverse effect on our business, results of operations and financial condition.

- Should we have on−going performance issues with our contract manufacturers, the process to move from one contractor to another is a lengthy and costly process that could affect our ability to execute customer shipment requirements and /or might negatively affect revenue and/or costs.

We depend on certain critical components in the production of our products and parts. Some of these components are obtained only from a single supplier and only in limited quantities. In addition, some of our major suppliers use proprietary technology and software code that could require significant redesign of our products in the case of a change in vendor. Further, as suppliers discontinue their products, or modify them in manners incompatible with our current use, or use manufacturing processes and tools that could not be easily migrated to other vendors, we could have significant delays in product or spare parts availability, which would have a significant adverse impact on our results of operations and financial condition.

Undetected Problems in Our Products Could Directly Impair our Financial Results. If flaws in design, production, assembly or testing of our products (by us or our suppliers) were to occur, we could experience a rate of failure in our products that would result in substantial repair, replacement or service costs and potential liability and damage to our reputation. There can be no assurance that our efforts to monitor, develop, modify and implement appropriate test and manufacturing processes for our products will be sufficient to permit us to avoid a rate of failure in our products that results in substantial delays in shipment, significant repair or replacement costs or potential damage to our reputation, any of which could have a material adverse effect on our business, results of operations and financial condition.

We May Experience Difficulty Managing Operational Expansion. We have recently established a sales and service infrastructure in India by recruiting sales and service personnel in order to bring about further growth in revenue in the Asia Pacific market and have expanded our professional services group to include business consultants. We may establish additional operations where growth opportunities are projected to warrant the investment. However, we cannot assure you that our revenues will increase as a result of this expansion or that we will be able to recover the expenses we incurred in effecting the expansion. Our failure to effectively manage our expansion of our sales, marketing, service and support organizations could have a negative impact on our business. To accommodate our global expansion, we are continuously implementing new or expanded business systems, procedures and controls. There can be no assurance that the implementation of such systems, procedures, controls and other internal systems can be completed successfully.

Changes in Foreign Conditions Could Materially Adversely Affect our Financial Results. Approximately half of our revenues are derived from sales outside the United States. Accordingly, our future results could be materially adversely affected by a variety of factors including changes in exchange rates, general economic conditions, regulatory requirements, tax structures or changes in tax laws, and longer payment cycles in the countries in our geographic areas of operations.

Our Business Could Be Materially Adversely Affected as a Result of the Risks Associated with Acquisitions and Investments. As part of our growth strategy, we have made a number of acquisitions and have made minority investments in complementary businesses, products or technologies. We frequently evaluate the tactical or strategic opportunity available related to complementary businesses, products or technologies. The process of integrating an acquired company's business into our operations and/or of investing in new technologies, may result in unforeseen operating difficulties and large expenditures and may absorb significant management attention that would otherwise be available for the ongoing development of our business. Other risks commonly encountered with acquisitions include the effect of the acquisition on our financial and strategic position and reputation; the failure of the acquired business to further our strategies, the inability to successfully integrate or commercialize acquired technologies or otherwise realize anticipated synergies or economies of scale on a timely basis and the potential impairment of acquired assets. Moreover, there can be no assurance that the anticipated benefits of any acquisition or investment will be realized. Future acquisitions or investments contemplated and/or consummated could result in potentially dilutive issuances of equity securities, the incurrence of debt and contingent liabilities, and amortization expenses related to intangible assets, any of which could have a material adverse effect on our operating results and financial condition. There can be no assurance that we will be successful in making additional acquisitions or effective in integrating such acquisitions into our existing business. In addition, if we consummate one or more significant acquisitions in which the consideration consists, in whole or in part, of ordinary shares or American Depositary Shares (ADSs), representing our ordinary shares, shareholders would suffer dilution of their interests in us. We have also invested in companies, which can still be considered in the start−up or development stages. These investments are inherently risky as the market for the technologies or products they have under development are typically in the early stages and may never materialize. We could lose our entire initial investment in these companies.

We May Be Unable to Keep Pace with Rapid Industry, Technological and Market Changes. The market for our products and services is subject to rapid technological change and new product introductions. Current competitors and/or new market entrants may develop new, proprietary products with features that could adversely affect the competitive position of our products. We may not successfully anticipate market demand for new products or services, or introduce them in a timely manner. The convergence of voice and data networks, and wired and wireless communications could require substantial modification and customization of our current products and business models, as well as the introduction of new products. Further, customer acceptance of these new technologies may be slower than we anticipate. We may not be able to compete effectively in these markets. In addition, our products must readily integrate with major third party security, telephone, front−office and back−office systems. Any changes to these third party systems could require us to redesign our products, and any such redesign might not be possible on a timely basis or achieve market acceptance. Additional factors that may cause actual results to differ materially from our expectations include industry specific factors; our ability to continuously develop, introduce and deliver commercially viable products, solutions and technologies, and the market's rate of acceptance of the solutions we offer and our ability to keep pace with market and technology changes and to compete successfully.

If Our Advanced Compliance Recording Solutions Fail to Record Our Customers' Interactions, We May be Subject to Liability and Our Reputation May be Harmed. Many of our customers use our solutions to record and to store recordings of commercial interactions. These recordings are used to provide back−up and verification of transactions and to guard against risks posed by lost or misinterpreted voice communications. These customers rely on our solutions to record, store and retrieve voice data in a timely, reliable and efficient manner. If our solutions fail to record our customer's interactions or our customers are unable to retrieve stored recordings when necessary, we may be subject to liability and our reputation may be harmed. Although we attempt to limit any potential exposure through quality assurance programs, insurance and contractual terms, we cannot assure you that we will eliminate or successfully limit our liability for any failure of our recording and storage solutions.

If We are Unable to Maintain the Security of Our Systems, Our Business, Financial Condition and Operating Results Could be Harmed. The occurrence of or perception of occurrence of security breaches in the operation of our business or by third parties using our products could harm our business, financial condition and operating results. Some of our customers use our products to compile and analyze highly sensitive or confidential information. We may come into contact with such information or data when we perform service or maintenance functions for our customers. While we have internal policies and procedures for employees in connection with performing these functions, the perception or fact that any of our employees has improperly handled sensitive information of a customer or a customer's customer could negatively impact our business. If, in handling this information we fail to comply with our privacy policies or privacy and security laws, we could incur civil liability to government agencies, customers and individuals whose privacy was compromised. If personal information is received or used from sources outside the US, we could be subject to civil, administrative or criminal liability under the laws of other countries. In addition, third parties may attempt to breach our security or inappropriately use our products through computer viruses, electronic break−ins and other disruptions. If successful, confidential information, including passwords, financial information, or other personal information may be improperly obtained and we may be subject to lawsuits and other liability. Any internal or external security breaches could harm our reputation and even the perception of security risks, whether or not valid, could inhibit market acceptance of our products.

Changes in Regulations Could Materially Adversely Affect Us. Our business, results of operations and financial condition could be materially adversely affected if laws, regulations or standards relating to our products or us are newly implemented or changed.

Changes in Israeli Government Benefit Programs Could Materially Adversely Affect Us. We derive and expect to continue to derive significant benefits from various programs and laws in Israel including tax benefits relating to our "Approved Enterprise" programs and certain grants from the Office of the Chief Scientist, or OCS, for research and development. To be eligible for these grants, programs and tax benefits, we must continue to meet certain conditions, including making certain specified investments in fixed assets and conducting the research, development and manufacturing of products developed with such OCS grants in Israel (unless a special approval has been granted for performing manufacturing outside Israel). Pursuant to an amendment to Israeli regulations, income from two of our "Approved Enterprises" is exempt from income tax for only two years. Following this two−year period, the "Approved Enterprise" will be subject to corporate tax at a reduced rate of 10−25% (based on the percentage of foreign ownership in each taxable year) for the following eight years. Income from the other two "Approved Enterprises" is tax exempt for four years. Following this four−year period, the "Approved Enterprises" are subject to corporate tax at a reduced rate of 10−25% (based on the percentage of foreign ownership in each taxable year) for the following six years. On April 1, 2005, an amendment to the applicable law regarding "Approved Enterprise" programs came into force. Pursuant to the amendment, a company's facility will be granted the status of "Approved Enterprise" only if it is proven to be an industrial facility (as defined in such law) that contributes to the economic independence of the Israeli economy and is a competitive facility that contributes to the Israeli gross domestic product. The amendment incorporates certain changes to both the criteria and procedure for obtaining “Approved Enterprise” status for an investment program, and changes to the tax benefits afforded in certain circumstances to “Approved Enterprises” under such law. The amendment will apply to Approved Enterprise programs in which the year of commencement of benefits under the law is 2004 or later, unless such programs received approval from the applicable government authority prior to December 31, 2004 in which case the provisions of the amendment will not apply. If grants, programs and benefits available to us or the laws under which they were granted are eliminated or their scope is further reduced, or if we fail to meet the conditions of existing grants, programs or benefits and are required to refund grants or tax benefits already received (together with interest and certain inflation adjustments) or fail to receive approval for future Approved Enterprises, our business, financial condition and results of operations could be materially adversely affected.

We May Have Exposure to Additional Income Tax Liabilities. As a global corporation, we are subject to income taxes both in Israel and various foreign jurisdictions. Our domestic and international tax liabilities are subject to the allocation of revenues and expenses in different jurisdictions and the timing of recognizing revenues and expenses. Additionally, the amount of income taxes paid is subject to our interpretation of applicable laws in the jurisdictions in which we file. From time to time, we are subject to income tax audits. While we believe we comply with all applicable income tax laws, there can be no assurance that a governing tax authority will not have a different interpretation of the law and assess us with additional taxes. Should we be assessed additional taxes, there could be a material adverse affect on our results of operations and financial condition.

Item 6. Directors, Senior Management and Employees.

Directors and Senior Management

The following table sets forth, as of June 27, 2005, the name, age and position of each of our directors and executive officers:

Name	Age	Position
Ron Gutler(2)(4)	47	Chairman of the Board of Directors
Joseph Atsmon(2)	56	Vice−Chairman of the Board of Directors
Rimon Ben−Shaoul(4)	59	Director
Yoseph Dauber(1)(4)	69	Director
Dan Falk(1)(2)(3)(4)	60	Director
John Hughes	53	Director
David Kostman	40	Director
Dr. Leora Meridor(1)(2)(3)	57	Director

Name	Age	Position
Haim Shani	48	Director and Chief Executive Officer
Dr. Shlomo Shamir	57	President
Ran Oz	38	Corporate Vice President and Chief Financial Officer
Koby Huberman	47	Corporate Vice President, Strategic Alliances & Business Development
Yechiam Cohen	48	Corporate Vice President, General Counsel and Corporate Secretary
Zvi Baum	49	Corporate Vice President, General Manager Product Division
Yoav Zaltzman	47	President, Intelligence Solutions
Doron Eidelman	49	Corporate Executive Vice President, President NiceVision
Jim Park	48	Corporate Vice President & General Manager Public Safety
Eran Gorev	40	President and Chief Executive Officer, NICE Systems Inc.
Eran Porat	42	Corporate Vice President, Finance

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(1) Member of the Internal Audit Committee.
(2) Member of the Audit Committee.
(3) Outside Director. See "— Outside Directors."
(4) Member of the Compensation Committee

Set forth below is a biographical summary of each of the above−named directors and executive officers of NICE.

Ron Gutler has been a director of NICE since May 2001 and chairman of the board since May 2002. Mr. Gutler is currently the chairman of G.J.E 121 Promoting Investment Ltd., a real estate investment company. Between 2000 and 2002, he managed the Blue Border Horizon Fund, a global macro fund. Mr. Gutler is a former Managing Director and a Partner of Bankers Trust Company (currently part of Deutche Bank). Between 1987 and 1999, he filled various positions with Bankers Trust. Mr. Gutler headed the Trading and Sales Activities in Asia, South America and Emerging Europe. He also established and headed the Israeli office of Bankers Trust. Mr. Gutler holds a Bachelor's degree in economics and international relations and a Master's degree in Business Administration, cum laude, both from the Hebrew University, Jerusalem.

Joseph Atsmon has been a director of NICE since September 2001 and Vice−Chairman of the Board since May 2002. Mr. Atsmon currently serves as a Director of Ceragon Networks and of Radvision Ltd. From 1995 until 2000, Mr. Atsmon served as Chief Executive Officer of Teledata Communications Ltd., a public company acquired by ADC Telecommunications Inc. in 1998. Mr. Atsmon had a twenty−year career with Tadiran Ltd. In his last role at Tadiran Ltd., Mr. Atsmon served as Corporate VP for business development. Prior to that, he served as President of various military communications divisions. Mr. Atsmon received a B.Sc. in Electrical Engineering, suma cum laude, from the Technion, Israel Institute of Technology.

Rimon Ben−Shaoul has been a director of NICE since September 2001. Mr. Ben−Shaoul currently serves as co−Chairman, President, and CEO of Koonras Technologies Ltd., which he joined on February 1, 2001. Koonras Technologies Ltd. is a technology investment company controlled by Poalim Investments Ltd., a large Israeli holding company. Mr. Ben−Shaoul also serves as Chairman of Nipson Digital Printing Systems PLC and Dor Chemicals Ltd. and as a director of MIND C.T.I. Ltd., BVR Systems Ltd. and several private companies. In addition, he is the President and CEO of Polar Communications Ltd., which manages media and communication investments. Between 1997 and February 1, 2001, Mr. Ben−Shaoul was the President and CEO of Clal Industries and Investments Ltd., one of the largest holding companies in Israel with substantial holdings in the high tech industry. During that time, Mr. Ben−Shaoul also served as Chairman of the Board of Directors of Clal Electronics Industries Ltd., Scitex Corporation Ltd., and various other companies within the Clal Group. Mr. Ben−Shaoul also served as a director of ECI Telecom Ltd., Fundtech Ltd., Creo Products, Inc., Nova Measuring Instruments Ltd., and other public and private companies. From 1985 to 1997, Mr. Ben−Shaoul was President and CEO of Clal Insurance Company Ltd. and a director of the company and its various subsidiaries. Mr. Ben−Shaoul holds a bachelor's degree in economics and a master's degree in business administration, both from Tel−Aviv University**.**

Yoseph Dauber has been a director of NICE since April 2002. Until June 2002 Mr. Dauber was deputy chairman of the board of Management and joint Managing Director of Bank Hapoalim and was responsible for the commercial division of the bank. During the years 1994−1996 and until 6/ 2002 Mr. Dauber served as Chairman of Poalim American Express and of the Isracard Group. He now serves as a member of the Board of Bank Hapoalim. Mr. Dauber holds a Bachelor's degree in Economics and Statistics from the Hebrew University of Jerusalem.

Dan Falk has been a director of NICE since January 2002. Mr. Falk serves as a member of the boards of directors of Orbotech Systems Ltd., Attunity Ltd., Orad Hi Tech Systems Ltd., Netafim Ltd., Plastopil Ltd., Visionix Ltd., ClickSoftware Technologies Ltd., Dmatek Ltd., Jacada Ltd. and Poalim Ventures 1 Ltd., all of which are Israeli companies, and Ormat Technology Inc. In 1999 and 2000, Mr. Falk was President and Chief Operating Officer of Sapiens International Corporation N.V. From 1985 to 1999, Mr. Falk served in various positions in Orbotech Systems Ltd., the last of which were Chief Financial Officer and Executive Vice President. From 1973 to 1985, he served in several executive positions in the Israel Discount Bank. Mr. Falk holds a Bachelor's degree in Economics and Political Science and a Master's degree in Business Administration from the Hebrew University, Jerusalem. As described above, Mr. Falk serves on the board of directors of a number of companies, both public and private and qualifies as an Outside Director of NICE under Israeli law. See "— Outside Directors."

John Hughes has been a director of NICE since November 2, 2002. Mr. Hughes is currently Chairman of Intec Telecom Systems plc and Executive Chairman of Parity Group plc. From December 2000 to July 2004, he held senior executive positions at Thales Group, most recently as Executive Vice President and CEO of all civil activities for the Group. During the years 1997 until 2000, he held positions with Lucent Technologies, and was President of its GMS/UMTS division and in the years 1991 through 1997, Mr. Hughes served as Director of Convex Global Field operations within the Hewlett Packard Company. Prior to that, Mr. Hughes held various positions with UK and US companies. Mr. Hughes holds a bachelor of science degree in Electrical and Electronic Engineering from the University of Hertfordshire.

David Kostman has been a director of NICE since January 2000. Mr. Kostman is currently the Chief Executive Officer of Delta Galil USA Inc., a subsidiary of Delta Galil Industries Ltd., a Nasdaq−listed apparel manufacturer. From April 2003 until April 2005, he was Chief Operating Officer of Delta Galil USA. Until May, 2002 he was the Chief Operating Officer of VerticalNet, Inc., a Nasdaq listed software company, which he joined in June 2000. Prior thereto, Mr. Kostman was a Managing Director in the Investment Banking Division of Lehman Brothers Inc., which he joined in 1994. Mr. Kostman holds a bachelor’s degree in law from Tel−Aviv University and a master’s degree in business administration from INSEAD, France.

Leora (Rubin) Meridor has been a director of NICE since January 2002. Since 2001, Dr. Meridor has been the Chairwoman of the Board of Bezeq International and Walla Telecommunication and between 2001 and 2004 Dr. Meridor served as Chairwoman of the Board of Poalim Capital Markets. From 1996 to 2000, Dr. Meridor served as Senior Vice President, Head of the Credit and Risk Management Division of the First International Bank of Israel. Between 1983 and 1996, Dr. Meridor held various positions in the Bank of Israel, the last of which was Head of the Research Department. Dr. Meridor has held various teaching positions with the Hebrew University and holds a B.Sc. degree in mathematics and physics, a M.Sc. degree in Mathematics and a Ph.D in Economics from the Hebrew University, Jerusalem. Dr. Meridor serves on the boards of directors of Teva Pharmaceutical Industries Ltd., Isrotel Ltd. and G.J.E. 121 Promoting Investment Ltd. She qualifies as an Outside Director of NICE under Israeli law. See “— Outside Directors.”

Haim Shani has served as a director and Chief Executive Officer of NICE since January 2001. He also served as President of NICE from January 2001 to April 2005. Mr. Shani came to NICE from Applied Materials (Israel), where he served as General Manager in its Israeli office from 1998 to 2000, heading up the Process Diagnostic and Control (PDC) business group formed following the acquisition by Applied Materials of Opal Ltd. and Orbot Instruments, Ltd. Prior to joining Applied Materials, Mr. Shani held various management positions at Orbotech Ltd. From 1995 to 1998, he served as Corporate Vice President of Marketing and Business Development, from 1993 to 1995, he served as President of Orbotech’s subsidiary in Asia Pacific, based in Hong Kong and from 1992 to 1993, he served as President of Orbotech Europe, based in Brussels. From 1982 to 1992, Mr. Shani held various management positions at Scitex Corporation and IBM Israel. Mr. Shani holds a bachelor’s degree in industrial and management engineering from the Technion – Israel Institute of Technology and a master's degree in business administration from INSEAD, France.

Dr. Shlomo Shamir has served as the President of NICE since April 2005. From April 2001 to April 2005, he served as President and Chief Executive Officer of NICE Systems Inc., NICE's wholly owned subsidiary and corporate headquarters in North America. From 2000 to April 2001, Dr. Shamir served as President and CEO of CreoScitex America, Inc. From 1997 to 2000, Dr. Shamir served as President and CEO of Scitex America Corp. and from 1994 to 1997, he served as its Corporate Vice President of Operations. Prior to 1994, Dr. Shamir served in the IDF where he attained the rank of Brigadier General. Dr. Shamir built and led the planning division in the IDF headquarters and served as Israel's military attaché to Germany. He holds a bachelor's degree in physics from the Technion – Israel Institute of Technology and master's and doctor of philosophy degrees in engineering and economic systems from Stanford University.

Ran Oz has served as Corporate Vice President and Chief Financial Officer of NICE since September 2004. Mr. Oz came to NICE from Ceragon Networks, an international fixed wireless company, where he was Chief Financial Officer from 2001 to 2004. Prior thereto he worked for six years with Jacada, an international software company, where he held a variety of positions in finance and operations − most recently as general manager of the parent company and corporate CFO. Mr. Oz holds a bachelor's degree in accounting and economics and a master's degree in business administration and economics from Hebrew University in Jerusalem. He is also a licensed CPA.

Koby Huberman has served as Corporate Vice President, Business Development of NICE since January 2000, and is currently Corporate Vice President, Strategic Alliances & Business Development. From 1998 to January 2000, Mr. Huberman served as Vice President of Marketing for the Enterprise Internetworking Systems Group of Lucent Technologies Ltd. and, from 1995 to 1998, he was Vice President of Global Marketing and Business Development for Lannet Data Communications Ltd., which was acquired by Lucent in 1998. Prior thereto, Mr. Huberman was the Managing Director of ServiceSoft Europe, a pan−European leading vendor of artificial intelligence and knowledge−based software for call center and customer service applications. Mr. Huberman holds a bachelor's degree in economics and business administration from the Leon Recanati Business School of Tel−Aviv University.

Yechiam Cohen has served as Corporate Vice President, General Counsel and Corporate Secretary of NICE since April 2005. Prior to joining NICE, he served for eight years as General Counsel of Amdocs, a leading provider of billing and CRM software solutions to the telecommunications industry. Before joining Amdocs, Mr. Cohen was a partner in the Tel Aviv law firm of Dan Cohen, Spigelman & Company. From 1987 to 1990, he was an associate with the New York law firm of Dornbush, Mensch, Mandelstam and Schaeffer. Mr. Cohen served as a law clerk to Justice Beijski of the Supreme Court of Israel in Jerusalem. He graduated in 1984 from the Hebrew University School of Law and is admitted to practice law in Israel and New York.

Zvi Baum is currently Corporate Vice President & General Manager Product Division. He previously served as Director of Product Management in the CEM Division of NICE and since May 2003 was in the position of Corporate VP of Marketing. Before joining NICE, Mr. Baum served as the Managing Director of Call Vision Israel Ltd., a company that specialized in the development of advanced web−based quality monitoring solutions for call centers. Prior to that, he served as the VP of International Sales and Marketing at STS Software Systems, which developed recording solutions and was acquired by NICE at the end of 1999. Between 1987 and 1998, Mr. Baum worked for a number of American and European companies in several areas, including technical management, marketing and channel management. Mr. Baum holds a bachelor's degree in Engineering from the Technion – Israel Institute of Technology and a Mater's degree in Computer Science and an MBA, both from the University of California in Los Angeles (UCLA).

Yoav Zaltzman is currently President, Intelligence Solutions. Mr. Zaltzman previously served as Corporate Vice President & General Manager Intelligence Solutions Division and since May 2001 was in the position of Corporate Vice President, Business Operations of NICE. Prior to joining NICE, Mr. Zaltzman served as Senior Director of Sales for Applied Materials Israel since 1997. From 1994 to 1997, Mr. Zaltzman served as General Manager of Orbot Instruments in Europe, based in Brussels, which was acquired by Applied Materials in 1997. From 1987 to 1992, Mr. Zaltzman held various sales and marketing positions for Oracle in Israel. Mr. Zaltzman holds a bachelor's degree in Computer Sciences and a master's degree in business administration, both from Tel Aviv University.

Doron Eidelman serves as Corporate Executive Vice President, President NiceVision since May 2002. Previously, he was COO of AudioCodes, a telecommunications company. From 1992 to 2001, Mr. Eidelman was Executive Vice President and President of the Display Division of Orbotech and from 1987 to 1992, he held various positions in Optrotech, the last of which was Vice President. Mr. Eidelman served in an elite intelligence unit in the IDF and was awarded the prestigious Israel Defense Award .He holds a bachelor's degree in electronic engineering from the Technion−Israel Institute of Technology and a master's degree in electronic engineering from the University of Tel Aviv.

Jim Park is currently Corporate Vice President & General Manager Public Safety. Mr. Park previously served as the President of NICE Systems CTI UK Ltd, NICE's wholly owned subsidiary and corporate headquarters in EMEA. Mr. Park was previously CEO of Thales Contact Solutions (previously Racal Recorders) which was acquired, by NICE, in Nov 2002. Prior to joining Racal, in 1998, Mr. Park held various senior management positions at Mitel Telecom. From 1996 to 1998 he served as General Manager for Mitel's EMEA switching business, from 1994 to 1996 he was VP of business development, from 1991 to 1994 he was director of Marketing and from 1982 to 1991 he held various sales management roles, in Europe, the Middle East and Africa. Mr. Park's early career was spent in various engineering roles with Siemens UK (1979 to 1982) and British Telecom (1974 to 1979), who sponsored him through college.

Eran Gorev has been the President and Chief Executive Officer of NICE Systems Inc. since March 2005. From 2002 to 2004, Mr. Gorev was President of the North America − Major Clients division at Amdocs. From 2000 to 2002, Mr. Gorev served as Corporate Vice President and Head of Worldwide Sales at Amdocs. Prior thereto, Mr. Gorev held various marketing and sales management positions in the Information Technology industry. Mr. Gorev earned an L.LB degree from Tel−Aviv University and a joint MBA degree from the Kellogg School of Management, Northwestern University, and the Recanati School of Business Administration, Tel−Aviv University.

Eran Porat has been the Corporate Vice President Finance of NICE since 2005. From March 2000 to 2005, he served as Corporate Controller of NICE. From 1997 to February 2000, Mr. Porat served as Corporate Controller of Technomatics Technologies Ltd. From 1996 to 1997, he served as Corporate Controller of Nechushtan Elevators Ltd. Mr. Porat is a CPA and holds a bachelor's degree in economics and accounting from the University of Tel−Aviv.

Compensation

The aggregate compensation paid to or accrued on behalf of all our directors and executive officers as a group (24 persons) during 2004 consisted of approximately $4.1 million in salary, fees, bonus, commissions and directors' fees and approximately $0.1 million in amounts set aside or accrued for to provide pension, retirement or similar benefits, but excluding amounts we expended for automobiles made available to our officers, expenses (including business travel, professional and business association dues and expenses) reimbursed to our officers and other fringe benefits commonly reimbursed or paid by companies in Israel.

During 2004, our officers and directors received, in the aggregate, options to purchase up to 208,000 ordinary shares under our 2003 Stock Option Plan. These options have an average exercise price of $23.31 and will expire six years after the date the options were granted.

Compensation and reimbursement for Outside Directors (as described below) is statutorily determined pursuant to the Israeli Companies Law, 5759–1999, or the Companies Law. The statutory rates for Outside Directors is approximately NIS 46,000 per annum and approximately NIS 1,800 per meeting. Compensation and reimbursement of all other directors who do not serve as officers are the same as the statutory rates paid to Outside Directors except for the chairman of the Board who receives 150% of the annual amount and an additional monthly fee of approximately $4,000 and the vice chairman of the Board who receives 137.5% of the annual amount.

Board Practices

Our articles of association provide that the number of directors serving on the board shall be not less than three but shall not exceed thirteen. Our directors, other than outside directors, are elected at the annual shareholders meeting to serve until the next annual meeting or until their earlier death, resignation, bankruptcy, incapacity or removal by an extraordinary resolution of the general shareholders meeting. Directors may be re−elected at each annual shareholders meeting. The board may appoint additional directors (whether to fill a vacancy or create new directorships) to serve until the next annual shareholders meeting, provided, however, that the board shall have no obligation to fill any vacancy unless the number of directors is less than three.

The board may, subject to the provisions of the Companies Law, appoint a committee of the board and delegate to such committee all or any of the powers of the board as it deems appropriate. Notwithstanding the foregoing, the board may, at any time, amend, restate or cancel the delegation of any of its powers to any of its committees. The board has appointed an internal audit committee, as required under the Companies Law, that has three members, an audit committee that currently has four members and a compensation committee that has three members.

Outside Directors

Under the Companies Law, companies incorporated under the laws of Israel whose shares have been offered to the public in or outside of Israel are required to appoint at least two “outside” directors.

To qualify as an outside director, an individual or his or her relative, partner, employer or any entity under his or her control, may not have as of the date of appointment as an outside director, and may not have had during the previous two years, any affiliation with the company, with any entity controlling the company on the date of the appointment or with any entity that is a controlling shareholder, on the date of the appointment or during the previous two years, is the company or an entity controlling the company. In general, the term “affiliation” includes:

- an employment relationship;
- a business or professional relationship maintained on a regular basis;
- control; and
- service as an office holder.

No person may serve as an outside director if the person’s position or other activities create, or may create, a conflict of interest with the person’s responsibilities as an outside director or may otherwise interfere with the person’s ability to serve as an outside director.

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

- the majority of shares voted at the meeting shall include at least one−third of the shares of non−controlling shareholders present at the meeting and voting on the matter (without taking into account the votes of the abstaining shareholders); or
- the total number of shares of non−controlling shareholders voted against the election of the outside directors does not exceed one percent of the aggregate voting rights in the company.

The term of an outside director will be three years and may be extended for an additional term of three years. Each committee of a company's board of directors which is empowered to exercise any of the board's powers is required to include at least one outside director.

Our outside directors were elected for a second term at our Annual General Meeting held on October 19, 2004. An outside director is entitled to compensation as provided in regulations adopted under the Companies Law and is otherwise prohibited from receiving any other compensation, directly or indirectly, from the company.

Independent Directors

Under the rules of the Nasdaq Stock Market, a majority of our directors are required to be "independent" as defined in Nasdaq's rules. Except for Mr. Shani, all of our directors are independent.

The Nasdaq rules require that director nominees be selected or recommended for the board's selection either by a nominations committee composed solely of independent directors or by a majority of independent directors. Our director nominees are selected by a majority of independent directors, and we anticipate that our board will adopt a board resolution formalizing that process prior to July 31, 2005, the effective date of this rule.

Audit Committee

The Nasdaq rules also require that the audit committee of a listed company must be composed of at least three directors, each of whom is (i) independent; (ii) does not receive any compensation (except for board fees) from the company; (iii) is not an affiliated person of the company or any subsidiary; and (iv) has not participated in the preparation of the company's (or a current subsidiary's) financial statements during the past three years. All of the current members of our audit committee (presently comprised of Ron Gutler (Chairman), Dan Falk, Leora Meridor, and Joseph Atsmon) meet the Nasdaq standards described above.

Our audit committee has adopted a charter specifying the committee's purpose and outlining its duties and responsibilities which include, among other things: (i) appointing, retaining and compensating the company's independent auditor, subject to shareholder approval, and (ii) pre−approving all services of the independent auditor. The audit committee must review and approve all related party transactions.

We believe we currently meet the applicable Nasdaq requirements and we intend to continue to take all actions as may be necessary for us to maintain our compliance with applicable Nasdaq requirements.

Internal Audit Committee

The Companies Law requires public companies to appoint an internal audit committee. The role of the internal audit committee under the Companies Law is to examine flaws in the management of the company's business in consultation with the internal auditors and the independent accountants, and to propose remedial measures to the board. The internal audit committee also reviews interested party transactions for approval as required by law. Under the Companies Law, an internal audit committee must consist of at least three directors, including all of the outside directors. The chairman of the board of directors, any director employed by or otherwise providing services to the company on a regular basis, and a controlling shareholder or any relative of a controlling shareholder, may not be a member of the internal audit committee. All of the current members of our internal audit committee (presently comprised of Leora Meridor, Dan Falk and Joseph Dauber) meet these qualifications.

Internal Auditor

Under the Companies Law, the board of directors must appoint an internal auditor, proposed by the internal audit committee. The role of the internal auditor is to examine, among other matters, whether the company's activities comply with the law and orderly business procedure. Under the Companies Law, the internal auditor may be an employee of the company but may not be an interested party or office holder, or a relative of any interested party or office holder, and may not be a member of the company's independent accounting firm or its representative. We have appointed an internal auditor in accordance with the requirements of the Companies Law.

Compensation Committee

The compensation committee is responsible for making recommendations to the board with respect to all director and officer compensation issues including the grant of stock options. The current members of our compensation committee are Messrs. Falk (Chairman), Ben Shaoul, Dauber, and Gutler.

Employees

At December 31, 2004, we had approximately 1072 employees worldwide, which represented an increase of 5.7% from year−end 2003.

The following table sets forth the number of our full−time employees at the end of each of the last three fiscal years as well as the main category of activity and geographic location of such employees:

	At December 31,		
Category of Activity	**2002**	**2003**	**2004**
Operations	66	55	54
Customer Support	266	299	317
Sales & Marketing	285	270	291
Research & Development	253	256	279
General & Administrative	152	134	131
Total	1,022	1,014	1072
Geographic Location			
Israel	498	478	532
North America	332	333	340
Europe	230	180	160
Asia Pacific	16	23	40
Total	1,022	1,014	1,072

We also utilize temporary employees in various activities. On average, we employed approximately 54 such temporary employees and 128 contractor employees (not included in the numbers set forth above) during 2004.

Our future success will depend in part upon our ability to attract and retain highly skilled and qualified personnel. Although competition for such personnel in Israel is generally intense, we believe that adequate personnel resources are currently available in Israel to meet our requirements.

We are not a party to any collective bargaining agreement with our employees or with any labor organization. However, we are subject to certain labor related statutes, and to certain provisions of collective bargaining agreements between the Histadrut (General Federation of Labor in Israel) and the Coordinating Bureau of Economic Organizations (including the Industrialists' Association of Israel) that are applicable to our Israeli employees by order of the Israeli Ministry of Labor and Welfare. These statutes and provisions principally concern the length of the work day and the work week, minimum wages for workers, contributions to a pension fund, insurance for work−related accidents, determination of severance pay and other conditions of employment. Furthermore, pursuant to such provisions, the wages of most of our employees are automatically adjusted based on changes in the Israeli consumer price index, or CPI. The amount and frequency of these adjustments are modified from time to time.

Israeli law generally requires the payment by employers of severance pay upon the death of an employee, his retirement or upon termination of employment by the employer without due cause. We currently fund our ongoing severance obligations by making monthly payments to approved severance funds or insurance policies. Please see Note 2(s) to our consolidated financial statements. In addition, according to the National Insurance Law, Israeli employers and employees are required to pay predetermined sums to the National Insurance Institute, an organization similar to the United States Social Security Administration. These contributions entitle the employees to benefits in periods of unemployment, work injury, maternity leave, disability, reserve military service and bankruptcy or winding−up of the employer. Since January 1, 1995, such amount also includes payments for national health insurance. The payments to the National Insurance Institute are equal to approximately 16.25% of an employee's wages (up to a certain cap as determined from time to time by law), of which the employee contributes approximately 66% and the employer contributes approximately 34%.

Employment Agreements

We have employment agreements with our officers. Pursuant to these employment agreements, each party may terminate the employment for no cause by giving a 30, 60 or 90 day prior written notice (six months in the case of certain senior employees). In addition, we may terminate such agreement for cause with no prior notice. The agreements generally include non−compete and non−disclosure provisions, although the enforceability of non−compete provisions under Israeli law is very limited.

Share Ownership

As of June 7, 2005, our directors and executive officers beneficially owned an aggregate of 805,397 ordinary shares, or approximately 4.1% of our outstanding ordinary shares, which amount includes options to purchase 773,701 ordinary shares that were vested on such date or that were scheduled to vest within the following 60 days. The options have an average exercise price of $35.13 per share and expire between 2005 and 2010. As of June 7, 2005, our chief executive officer, Mr. Haim Shani, beneficially owned 294,952 ordinary shares, or approximately 1.5% of our outstanding ordinary shares, which includes options to purchase 294,508 ordinary shares that were vested on such date or that were scheduled to vest within the following 60 days, and 444 ordinary shares owned by him. Of the 294,508 options, 250,000 options have an exercise price of $55.5 per share and expire on October 22, 2006. The remaining 44,508 options have exercises prices ranging from $10.95 per share to $23.4 per share, and expire between May 2007 and December 2009. No other individual director or executive officer beneficially owns 1% or more of our outstanding ordinary shares.

The following is a description of each of our option plans, including the amount of options currently outstanding and the weighted average exercise price.

1995 Stock Option Plan

In 1995, we adopted the NICE−Systems Ltd. 1995 Stock Option Plan, or 1995 Plan, to attract, motivate and retain talented employees by rewarding performance and encouraging behavior that will improve our profitability. Under the 1995 Plan, our employees and officers may be granted options to acquire our ordinary shares. The options to acquire ordinary shares are granted at an exercise price of not less than the fair market value of the ordinary shares on the date of the grant, subject to certain exceptions which may be determined by our board of directors. We have registered, through the filing of registration statements on Form S−8 with SEC under the Securities Act of 1933, 6,000,000 ADSs for issuance under the 1995 Plan.

Under the terms of the 1995 Plan, 25% of each stock option granted becomes exercisable on each of the first, second, third and fourth anniversaries of the date of grant so long as the grantee is, subject to certain exceptions, employed by us at the date the stock option becomes exercisable. As of February 15, 2000, our board of directors adopted a resolution amending the exercise terms of the 1995 Plan whereby 25% of the stock options granted become exercisable on the first anniversary of the date of grant and 6.25% becomes exercisable once every quarter during the subsequent three years. Stock options expire six years after the date of grant. Stock options are non−transferable except upon the death of the grantee. When applicable, the options are held by, and registered in the name of, a trustee for a period of two years after the date of grant in accordance with Section 102 of the Israeli Income Tax Ordinance.

Pursuant to a tax reform effectuated in Israeli in 2003 (the “Tax Reform”) and in order to comply with the provisions of Section 102 of the Income Tax Ordinance [New Version], 5721−1961 (the “Ordinance”) following the Tax Reform, on February 11, 2003 our board of directors adopted an addendum to our share option plan with respect to options granted as of January 1, 2003 to grantees who are residents of Israel (the “Addendum”). The Addendum does not add to nor modify our share option plan in respect of grantees that are not residents of Israel. On December 19, 2003 the board of directors resolved to elect the “Capital Gains Route” (as defined in Section 102(b)(2) of the Ordinance) for the grant of options to Israeli grantees. Generally, subject to the fulfillment of the provisions of Section 102 of the Ordinance, under the Capital Gains Route gains realized from the sale of shares issued upon exercise of options shall generally be taxed at a rate of only 25% and not at the marginal income tax rate applicable to the grantee (up to 49%). In general, according to the Addendum and pursuant to the election of the Capital Gains Route by our board of directors, all options granted to Israeli grantees, shares issued upon exercise of such options and any bonus shares issued with respect to such shares, shall be held in trust for the benefit of the grantee and registered in the name of a trustee appointed by the Company and approved by the Israeli tax authorities. Such options and shares will, subject to the provisions of Section 102 of the Ordinance and any regulations, rules or orders promulgated thereunder, be held in trust for a period of two years from the end of the tax year in which the options are granted and shall not be released from the trust prior to the payment of the grantee’s tax liabilities. In the event the requirements of Section 102 for the allocation of options according to the Capital Gains Route are not met – the applicable marginal income tax rates shall apply.

The Addendum, the trustee and the Company's election of the "Capital Gains Route" were approved by the Israeli tax authorities.

The 1995 Plan is generally administered by our board of directors, which determines the grantees under the 1995 Plan and the number of options to be granted. As of June 7, 2005, options to purchase 1,641,131 ordinary shares were outstanding under the 1995 Plan at a weighted average exercise price of $41.85.

1997 Executive Share Option Plan

In 1996, we adopted the NICE−Systems Ltd. 1997 Executive Share Option Plan, or 1997 Plan, to provide an incentive to our officers and to our directors who are also officers by enabling them to share in the future growth of our business. We have registered, through the filing of registration statements on Form S−8 with SEC under the Securities Act, 2,000,000 ADSs for issuance under the 1997 Plan.

Under the terms of the 1997 Plan, stock options will be exercisable during a 60−day period ending four years after grant. Notwithstanding the foregoing, if our year−end earnings per share shall reach certain defined targets, 40% of such stock options shall become exercisable; if earnings per share shall reach certain higher defined targets, an additional 30% of such stock options shall become exercisable; and if earnings per share shall reach certain higher defined targets, an additional 30% of such stock options shall become exercisable, provided that with respect to all of the above−referenced periods, our operating profit shall not be less than 10% of revenues and earnings per share shall exclude any non−recurring expenses related to mergers and acquisitions. Notwithstanding the foregoing, none of the stock options shall be exercisable before the expiration of two years from the date of issuance. When applicable, the options are held by, and registered in the name of, a trustee for a period of two years after the date of grant in accordance with Section 102 of the Israeli Income Tax Ordinance.

The 1997 Plan is generally administered by our board of directors, which determines the grantees under the 1997 Plan and the number of options to be granted. As of June 7, 2005, there were no outstanding options to purchase ordinary shares under the 1997 Plan. All of the outstanding options under this plan have expired.

2001 Stock Option Plan

In 2001, we adopted the NICE−Systems Ltd. 2001 Stock Option Plan, or 2001 Plan, for the purpose of providing an incentive to certain employees, directors, officers and consultants in order to further the advancement our business. The options to acquire our ordinary shares are granted at an exercise price equal to the closing price of our ADSs as quoted on the Nasdaq National Market on the most recent date prior to the date of the resolution of our board of directors to grant the option for which the price was quoted. We have registered, through the filing of a registration statement on Form S−8 with SEC under the Securities Act, 4,000,000 ADSs for issuance under the 2001 Plan.

Under the terms of the 2001 Plan, one−third of the stock options granted became exercisable ten months after the date of grant and the remaining two−thirds will become exercisable on the first and second anniversaries of the first date of exercise so long as the grantee is, subject to certain exceptions, employed by us at the date the stock option becomes exercisable. The third portion of the options granted under this plan may be exercised at the end of the second anniversary of the first date of exercise if we meet a pre−tax profit target of 20%, as determined by our board of directors in its discretion. Unless otherwise determined by our board of directors as of the date of grant, stock options expire six years after the date of grant. Stock options are non−transferable except upon the death of the grantee. When applicable, the options are held by, and registered in the name of, a trustee for a period of two years after the date of grant in accordance with Section 102 of the Israeli Income Tax Ordinance.

The 2001 Plan is generally administered by our board of directors which determines the grantees under the 2001 Plan and the number of options to be granted. As of June 7, 2005, options to purchase 491,672 ordinary shares were outstanding under the 2001 Plan at a weighted average exercise price of $12.1.

2003 Stock Option Plan

In December 2003, we adopted the NICE−Systems Ltd. 2003 Employee Stock Option Plan, or 2003 Plan, to attract, motivate and retain talented employees by rewarding performance and encouraging behavior that will improve our profitability. Under the 2003 Plan, our employees, officers and directors may be granted options to acquire our ordinary shares. The options to acquire ordinary shares are granted at an exercise price of not less than the fair market value of the ordinary shares on the date of the grant, subject to certain exceptions which may be determined by our board of directors. We have registered, through the filing of registration statements on Form S−8 with SEC under the Securities Act of 1933, 2,000,000 ADSs for issuance under the 2003 Plan.

Under the terms of the 2003 Plan, 25% of the stock options granted become exercisable on the first anniversary of the date of grant and 6.25% becomes exercisable once every quarter during the subsequent three years. Stock options expire six years after the date of grant. Stock options are non−transferable except upon the death of the grantee.

Pursuant to the Tax Reform and in order to comply with the provisions of Section 102 of the Ordinance, on January 5, 2004 our board of directors adopted an addendum to our share option plan with respect to options granted as of December 2, 2003 to grantees who are residents of Israel (the “Addendum”). The Addendum does not add to nor modify our share option plan in respect of grantees that are not residents of Israel. On December 19, 2003 the board of directors resolved to elect the “Capital Gains Route” (as defined in Section 102(b)(2) of the Ordinance) for the grant of options to Israeli grantees, which is described above under “1995 Stock Option Plan”.

The 2003 Plan is generally administered by our board of directors, which determines the grantees under the 2003 Plan and the number of options to be granted. As of June 7, 2005, options to purchase 2,004,375 ordinary shares were outstanding under the 2003 Plan at a weighted average exercise price of $24.84.

1999 Amended and Restated Employee Stock Purchase Plan

In 1999, we adopted the NICE−Systems Ltd. 1999 Employee Stock Purchase Plan, or ESPP, in order to provide an incentive to our employees and the employees of our subsidiaries by providing them with an opportunity to purchase our ordinary shares through accumulated payroll deductions, and thereby enable such persons to share in the future growth of our business. We amended the ESPP in December 2003. We have registered, through the filing of a registration statement on Form S−8 with SEC under the Securities Act, 2,250,000 ADSs for issuance under the ESPP.

Under the terms of the ESPP, eligible employees (generally, all our employees and the employees of our eligible subsidiaries who are not directors or controlling shareholders) may, on January 1 and July 1 of each year in which the ESPP is in effect, elect to become participants in the ESPP for that six−month period by filing an agreement with us arranging for payroll deductions of between 2% and 10% of such employee's compensation for the relevant period. An employee's election to purchase ordinary shares under the ESPP is subject to his or her right to withdraw from the ESPP prior to exercise, six months after the offering date. The election price under the ESPP is 85% of the lowest price of our ordinary shares as quoted on the Nasdaq National Market on the commencement date of each offering period or on the semi−annual purchase date.

Item 7. Major Shareholders and Related Party Transactions.

Major Shareholders

The following table sets forth certain information with respect to the beneficial ownership of our ordinary shares as of June 11, 2005 with respect to each person known to us to be the beneficial owner of 5% or more of our outstanding ordinary shares. None of our major shareholders has any different voting rights than any other shareholder.

	Shares Beneficially Owned	
Name and Address	**Number**	**Percent(1)**
Bank Hapoalim Funds 65 Yehuda Halevi Street Tel Aviv 65227, Israel (2)	1,191,911	6.3%

(1) Based upon 18,938,992 ordinary shares issued and outstanding on June 11, 2005.

(2) Based upon the information contained in a report filed with the Tel Aviv Stock Exchange on June 11, 2005 by Bank Hapoalim pursuant to Israeli law with respect to the aggregate holdings of various of its affiliated mutual

funds and provident funds. The method used to compute holdings under Israeli law does not necessarily bear the same result as the method used to compute beneficial ownership under SEC rules and regulations.

As of June 16, 2005, we had 80 ADS holders of record in the United States, holding approximately 55.1% of our outstanding ordinary shares, as reported by The Bank of New York, the depositary for our ADSs.

As of June 9, 2005, Bank Leumi holds 875,174, or 4.6%, of our ordinary shares. This information is based upon a report provided to us by Bank Leumi pursuant to Israeli law with respect to the aggregate holdings of various of its affiliated mutual funds and provident funds. As of March 31, 2004, Bank Leumi reported that it held 1,271,000, or 7.3%, of our ordinary shares. The method used to compute holdings under Israeli law does not necessarily bear the same result as the method used to compute beneficial ownership under SEC rules and regulations.

Between April 28, 2004 and June 2, 2005, Thales S.A. sold 762,025 ordinary shares. Consequently, Thales SA now holds less than 5% of our ordinary shares. This information is based upon the information contained in an amendment to Schedule 13D filed with the SEC on June 3, 2005 by Thales SA.

To our knowledge, we are not directly or indirectly owned or controlled by another corporation or by any foreign government and there are no arrangements that might result in a change in control of our company.

Related Party Transactions

None.

Registration Rights Agreement

In November 2002, we consummated an agreement to acquire certain assets and liabilities of Thales Contact Solutions (or TCS), a developer of customer−facing technology for public safety, financial trading and customer contact centers, based in the United Kingdom. TCS was a unit of Thales Group, one of Europe’s premier electronics companies. In connection with the acquisition, we issued 2,187,500 ordinary shares to the Thales Group. In November 2, 2002, we entered into a Registration Rights Agreement with Thales SA relating to the 2,187,500 ordinary shares issued to the Thales Group. Pursuant to the agreement, we filed under the Securities Act of 1933 a registration statement covering the offer and sale of the ordinary shares, which was declared effective on January 9, 2004. For a discussion of the TCS acquisition, please see “Item 5, Operating and Financial Review.”

Interests of Experts and Counsel

Not applicable.

Item 8. Financial Information.

Consolidated Statements and Other Financial Information.

See Item 18, “Financial Statements”.

Legal Proceedings

We are not involved in any legal proceedings that we believe, individually or in the aggregate, will have a material adverse effect on our business, financial condition or results of operation, except as noted below.

CipherActive Lawsuit

On October 19, 2004, CipherActive filed an action against us in the District Court of Tel Aviv. In this lawsuit, CipherActive claims that under a development agreement with us, it is entitled to receive license fees in respect of certain software that it allegedly developed for us and which has been embedded in one of our products. CipherActive claims that it is entitled to license fees in an amount of $600,000, in addition to the amount of $100,000 already paid to CipherActive by us in respect of such license fees. In our statement of defense we claim that the software developed by CipherActive under the agreement has not been successful in the market, is no longer embedded in our product and, therefore, CipherActive is not entitled to any additional license fees.

Witness Patent Infringement Lawsuits

On July 20, 2004, STS Software System Ltd., a wholly owned subsidiary of ours, filed a lawsuit against Witness Systems, Inc. in the United States District Court for Southern District of New York claiming that Witness Systems is infringing our U.S. patent entitled “Communication Management System for Computer Network−Based Telephones”. The action was subsequently transferred to the Northern District of Georgia. In this lawsuit, we claim that Witness Systems infringes our VoIP patent by marketing and selling products that incorporate methods of detecting, monitoring and recording information – all fully protected by our patent. We are seeking an injunction to prevent Witness Systems from making, using, or offering to sell or selling any product in the United States which infringes this patent. The case is currently in the preliminary stages of discovery.

On August 30, 2004, Witness Systems filed a lawsuit in the United States District Court for the Northern District of Georgia against Nice Systems, Inc., a wholly owned subsidiary of ours, alleging infringement of two U.S. patent numbers entitled “Method and Apparatus for Simultaneously Monitoring Computer User Screen and Telephone Activity from a Remote

Location.” On February 24, 2005, Witness Systems filed a similar action in the Northern District of Georgia against Nice Systems Ltd. alleging infringement of the same two patents. The two actions were consolidated in March 2005. Witness Systems is seeking unspecified damages and injunctive relief. We have denied infringing either of these patents and are vigorously defending the actions.

The 2001 Securities Actions

On February 8, 2001, the trading price of our securities dropped, following our announcements that, among other things, we would be restating our revenue for fiscal year 1999 and the first three quarters of 2000 and that we were revising downward our revenue estimates for the final quarter of 2000. Thereafter, various plaintiffs filed in the United States District Court for the District of New Jersey fourteen putative class action securities lawsuits against us and several of our present or former officers and directors. The first of these actions was commenced on February 13, 2001. All of the actions were allocated to the Newark vicinage of the District of New Jersey, and all were assigned to the Hon. Joseph A. Greenaway, Jr., U.S.D.J.

The complaint in each action alleged that we and the individual defendants violated Section 10(b) of the Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b−5 promulgated thereunder. The plaintiffs also attempted to state a “control person” claim against several of the individual defendants under Section 20(a) of the Exchange Act, 15 U.S.C. § 78t(a). While there were differences among the fourteen complaints, the plaintiffs essentially contended that we and the individual defendants misrepresented to investors, either affirmatively or through omissions, our financial results and the value of our securities. The plaintiffs sought damages in an unspecified amount. The plaintiffs in each such action sought to represent a class of investors in our securities throughout a specified period, approximately from February 2000 to February 2001.

On April 11, 2001, we and several of the individual defendants successfully moved to consolidate the various actions under the caption “*In re: Nice Systems Ltd. Securities Litigation*,” Master File No. 01−CV−00737 (JAG), and to establish a schedule for the filing by plaintiffs of an amended consolidated complaint and our and the individual defendants’ response to such complaint.

By Order dated May 21, 2001, a group of plaintiffs were appointed “Lead Plaintiffs” pursuant to the Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u−4(a)(3)(B). On August 20, 2001, the Lead Plaintiffs filed and served a Consolidated Amended Class Action Complaint, purporting to bring their securities claims on behalf of a class of persons who purchased our ADSs between November 3, 1999, and February 7, 2001. On October 22, 2001, we and the individual defendants moved to dismiss the consolidated complaint in its entirety, for failure to state a claim upon which relief could be granted, for failure to plead fraud with the requisite particularity, and on grounds of *forum non conveniens* in favor of proceedings in Israel. Briefing on that motion was completed on December 27, 2001.

Before that motion was decided by the Court, the parties to the litigation entered into a settlement of the claim, without any admission of liability or wrongdoing on our part, in the amount of ten million dollars, including attorneys' fees. We received the funds for this settlement through our directors and officers insurance policy.

Because the action was brought as a class action, the settlement was subject to court approval. By Order dated April 7, 2003, the settlement was approved by the United States District Court for the District of New Jersey, over the objections of two shareholders. On April 30, 2003, one of those shareholders, James J. Hayes, appealed from that Order to the United Stated Court of Appeals for the Third Circuit. Objector Hayes also later appealed from the District Court's subsequent refusal to reconsider its decision approving the settlement.

In a single opinion dated February 9, 2004, the Court of Appeals for the Third Circuit rejected both appeals of Objector Hayes, by affirming the decision of the District Court approving the settlement and its subsequent refusal to reconsider that determination.

On February 23, 2004, Objector Hayes petitioned the Court of Appeals for the Third Circuit to reconsider its February 9 decision. That Petition was denied by the Third Circuit on March 17, 2004.

On June 7, 2004, Objector Hayes filed with the Supreme Court of the United States a Petition for a Writ of Certiorari, asking the Supreme Court to review the determinations of the Court of Appeals for the Third Circuit. The Supreme Court denied that Petition on October 4, 2004.

On November 29, 2004, Objector Hayes filed before the Supreme Court a Petition for Rehearing. That Petition was denied on January 10, 2005.

Evesham School District Investigation

The U.S. Consumer Product Safety Commission has brought to our attention and provided us an opportunity to comment on an alleged incident of a fire allegedly involving a NICE product used in a school building in the Evesham New Jersey School District. We have retained special counsel and engineering consultants and are investigating this matter. We believe that, based on the facts known at present, it is not expected this matter will result in any regulatory action.

Dividends

Since our initial public offering on Nasdaq in 1996, we have not declared or paid dividends on our ordinary shares. We intend to retain our earnings for future growth and therefore do not anticipate paying any cash dividends in the foreseeable future.

Significant Changes

Please see the descriptions of significant changes that occurred in 2005 under the subheadings "—Dictaphone Acquisition", "—TCS Acquisition" and "—Sale of Comint/DF Business to Elta" below under the heading "Additional Information—Material Contracts".

Item 9. The Offer and Listing.

Trading in the ADSs

Our American Depositary Shares, or ADSs, have been quoted on The Nasdaq National Market under the symbol "NICEV" from our initial public offering in January 1996 until April 7, 1999, and thereafter under the symbol "NICE." Prior to that time, there was no public market for our ordinary shares in the United States. Each ADS represents one ordinary share. The following table sets forth, for the periods indicated, the high and low last reported closing prices for our ADSs.

	ADSs	
	High	**Low**
Annual		
2000	$ 99.00	$ 17.50
2001	27.75	8.88
2002	17.04	6.70
2003	25.35	8.34
2004	31.39	17.88
Quarterly 2003		
First Quarter	$ 11.13	$ 8.34
Second Quarter	15.19	11.10
Third Quarter	19.640	14.20
Fourth Quarter	25.35	19.01
Quarterly 2004		
First Quarter	$ 29.88	$ 22.56
Second Quarter	25.75	21.16
Third Quarter	23.38	17.88
Fourth Quarter	31.39	21.04

	ADSs	
	High	Low
Monthly		
December 2004	$ 31.39	$ 27.27
January 2005	31.52	29.66
February 2005	34.28	30.35
March 2005	35.03	32.22
April 2005	37.08	30.57
May 2005	39.85	35.98

On June 27, 2005, the last reported sale price of our ADSs was $38.1 per ADS.

The Bank of New York is the depositary for our ADSs. Its address is 101 Barclay Street, New York, New York 10286.

Trading in the Ordinary Shares

Our ordinary shares have been listed on the Tel−Aviv Stock Exchange, or TASE, since 1991. Our ordinary shares are not listed on any other stock exchange and have not been publicly traded outside Israel (other than through ADSs as noted above). The table below sets forth the high and low last reported prices of our ordinary shares (in NIS and dollars) on the TASE. The translation into dollars is based on the daily representative rate of exchange published by the Bank of Israel.

	Ordinary Shares			
	High		Low	
	NIS	$	NIS	$
Annual				
2000	388.00	95.10	79.50	19.49
2001	97.90	23.68	39.19	9.27
2002	75.50	16.81	32.02	6.63
2003	113.30	25.04	37.96	8.01
2004	137.70	31.10	79.51	17.52
Quarterly 2003				
First Quarter	52.80	11.12	37.96	8.01
Second Quarter	67.40	15.56	51.70	11.28
Third Quarter	90.20	20.25	62.70	14.15
Fourth Quarter	113.30	25.04	84.80	19.17

	Ordinary Shares			
	High		Low	
	NIS	$	NIS	$
Quarterly 2004				
First Quarter	137.70	31.10	100.80	22.36
Second Quarter	117.90	25.99	97.56	21.43
Third Quarter	107.10	23.90	79.51	17.52
Fourth Quarter	131.90	30.40	92.79	20.74
Monthly				
December 2004	131.90	30.40	117.40	27.03
January 2005	139.50	31.72	130.40	29.56
February 2005	148.40	34.01	135.00	30.85
March 2005	151.30	34.90	142.00	32.60
April 2005	160.30	36.56	135.40	30.96
May 2005	172.60	39.42	155.90	35.68

As of June 27, 2005, the last reported price of our ordinary shares on the TASE was NIS 170.60 (or $37.57) per share.

Item 10. Additional Information.

Memorandum and Articles of Association

Organization and Register

We are a company limited by shares organized in the State of Israel under the Israeli Companies Law. We are registered with the Registrar of Companies of the State of Israel and have been assigned company number 52−0036872.

Objects and Purposes

Our objects and purposes include a wide variety of business purposes, including all kinds of research, development, manufacture, distribution, service and maintenance of products in all fields of technology and engineering and to engage in any other kind of business or commercial activity. Our objects and purposes are set forth in detail in Section 2 of our memorandum of association.

In our annual general meeting of shareholders held on December 24, 2002, we adopted amended and restated articles of association of the Company.

Directors

Our articles of association provide that the number of directors serving on the board shall be not less than three but shall not exceed thirteen. Our directors, other than outside directors, are elected at the annual shareholders meeting to serve until the next annual meeting or until their earlier death, resignation, bankruptcy, incapacity or removal by resolution of the general shareholders meeting. Directors may be re−elected at each annual shareholders meeting. The board may appoint additional directors (whether to fill a vacancy or create new directorship) to serve until the next annual shareholders meeting, provided, however, that the board shall have no obligation to fill any vacancy unless the number of directors is less than three. Our officers serve at the discretion of the board.

The board of directors may meet and adjourn its meetings according to the Company's needs but at least once every three months. A meeting of the board may be called at the request of each director. The quorum required for a meeting of the board consists of a majority of directors. The adoption of a resolution by the board requires approval by a simple majority of the directors present at a meeting in which such resolution is proposed. In lieu of a board meeting, a resolution may be adopted if all of the directors lawfully entitled to vote thereon consent in writing.

Subject to the Companies law, the board may appoint a committee of the board and delegate to such committee all or any of the powers of the board, as it deems appropriate. Under the Companies Law the board of directors must appoint an internal audit committee, comprised of at least three directors and including both of the external directors. The function of the internal audit committee is to review irregularities in the management of the Company's business and recommend remedial measures. The committee is also required, under the Companies Law to approve certain related party transactions. Notwithstanding the foregoing, the board may, at any time, amend, restate or cancel the delegation of any of its powers to any of its committees. The board has appointed an internal audit committee which has three members, an audit committee which currently has four members and a compensation committee which has four members.

Fiduciary Duties of Officers

The Companies Law codifies the fiduciary duties that "office holders," including directors and executive officers, owe to a company. An office holder's fiduciary duties consist of a duty of care and a duty of loyalty. The duty of loyalty includes avoiding any conflict of interest between the office holder's position in the company and his personal affairs, avoiding any competition with the company, avoiding exploiting any business opportunity of the company in order to receive personal advantage for himself or others, and revealing to the company any information or documents relating to the company's affairs which the office holder has received due to his position as an office holder.

Approval of Certain Transactions

Under the Companies Law, all arrangements as to compensation of office holders who are not directors, or controlling parties, require approval of the board of directors. Arrangements regarding the compensation of directors also require internal audit committee and shareholder approval.

The Companies Law requires that an office holder of the company promptly disclose any personal interest that he or she may have and all related material information known to him or her, in connection with any existing or proposed transaction by the company. In addition, if the transaction is an extraordinary transaction as defined under Israeli law, the office holder must also disclose any personal interest held by the office holder's spouse, siblings, parents, grandparents, descendants, spouse's descendants and the spouses of any of the foregoing. In addition, the office holder must also disclose any interest held by any corporation in which the office holder is a 5% or greater shareholder, director or general manager or in which he or she has the right to appoint at least one director or the general manager. An extraordinary transaction is defined as a transaction other than in the ordinary course of business, otherwise than on market terms, or that is likely to have a material impact on the company's profitability, assets or liabilities.

In the case of a transaction which is not an extraordinary transaction, after the office holder complies with the above disclosure requirement, only board approval is required unless the articles of association of the company provide otherwise. The transaction must not be adverse to the company's interest. Furthermore, if the transaction is an extraordinary transaction, then, in addition to any approval stipulated by the articles of association, it also must be approved by the company's audit committee and then by the board of directors, and, under certain circumstances, by a meeting of the shareholders of the company. An office holder who has a personal interest in an extraordinary transaction that is considered at a meeting of the board of directors or the audit committee may not be present at the deliberations or vote on this matter. If a majority of the directors has a personal interest in an extraordinary transaction with the Company, shareholder approval of the transaction is required.

The Companies Law applies the same disclosure requirements to a controlling shareholder of a public company, which includes a shareholder that holds 25% or more of the voting rights if no other shareholder owns more than 50% of the voting rights in the company. Extraordinary transactions with a controlling shareholder or in which a controlling shareholder has a personal interest, and the terms of compensation of a controlling shareholder who is an office holder, require the approval of the audit committee, the board of directors and the shareholders of the company by simple majority, provided that either such majority vote must include at least one−third of the shareholders who have no personal interest in the transaction and are present at the meeting (without taking into account the votes of the abstaining shareholders), or that the total shareholdings of those who have no personal interest in the transaction who vote against the transaction represent no more than one percent of the voting rights in the company.

In addition, under the Companies Law, a private placement of securities requires approval by the board of directors and the shareholders of the company if it will cause a person to become a controlling shareholder or if:

- the securities issued amount to twenty percent or more of the company's outstanding voting rights before the issuance;
- some or all of the consideration is other than cash or listed securities or the transaction is not on market terms; and
- the transaction will increase the relative holdings of a shareholder that holds five percent or more of the company's outstanding share capital or voting rights or that will cause any person to become, as a result of the issuance, a holder of more than five percent of the company's outstanding share capital or voting rights.

According to the Company's Articles of Association certain resolutions, such as resolutions regarding mergers, and windings up, require approval of the holders of 75% of the shares represented at the meeting and voting thereon.

Duties of Shareholders

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

- any amendment to the articles of association;
- an increase of the company's authorized share capital;
- a merger; or
- approval of interested party transactions which require shareholder approval.

In addition, any controlling shareholder, any shareholder who knows that it possesses power to determine the outcome of a shareholder vote and any shareholder who, pursuant to the provisions of a company's articles of association, has the power to appoint or prevent the appointment of an office holder in the company, is under a duty to act with fairness towards the company. The Companies Law does not describe the substance of this duty but provides that a breach of his duty is tantamount to a breach of fiduciary duty of an officer of the Company.

Exemption, Insurance and Indemnification of Directors and Officers

Exemption of Office Holders

Under the Companies Law, an Israeli company may not exempt an office holder from liability for breach of his duty of loyalty, but may exempt in advance an office holder from liability to the company, in whole or in part, for a breach of his duty of care (except in connection with distributions), provided the articles of association of the company allow it to do so. Our articles of association do not allow us to do so.

Office Holder Insurance

Our Articles of Association provide that, subject to the provisions of the Companies Law, we may enter into a contract for the insurance of the liability of any of our office holders with respect to:

- a breach of his duty of care to us or to another person,
- a breach of his fiduciary duty to us, provided that the office holder acted in good faith and had reasonable grounds to assume that his act would not prejudice our interests, or
- a financial liability imposed upon him in favor of another person concerning an act performed by him in his capacity as an office holder.

Indemnification of Office Holders

Our Articles of Association provide that we may indemnify an office holder against:

- a financial liability imposed on him in favor of another person by any judgment, including a settlement or an arbitrator's award approved by a court concerning an act performed in his capacity as an office holder, and
- reasonable litigation expenses, including attorneys' fees, expended by the office holder or charged to him by a court, in proceedings instituted against him by or on our behalf or by another person, or in a criminal charge from which he was acquitted, or a criminal charge in which he was convicted for a criminal offense that does not require proof of intent, in each case relating to an act performed in his capacity as an office holder.

The Companies Law was recently amended to also permit indemnification of reasonable litigation expenses, including attorneys' fees, expended by the office holder as a result of an investigation or proceeding instituted against him by a competent authority, provided that such investigation or proceeding concluded without the filing of an indictment against him and either (A) concluded without the imposition of any financial liability in lieu of criminal proceedings or

(B) concluded with the imposition of a financial liability in lieu of criminal proceedings but relates to a criminal offense that does not require proof of criminal intent. We intend to amend or Articles of Association accordingly.

Our Articles of Association also include provisions:

- authorizing us to grant an undertaking to indemnify an office holder, provided that the undertaking is limited to types of events which our board of directors deems to be foreseeable at the time of the undertaking and limited to an amount determined by our board of directors to be reasonable under the circumstances and provided that the total amount of indemnification for all persons we have agreed to indemnify in such circumstances does not exceed, in the aggregate twenty−five percent (25%) of our shareholders' equity at the time of the actual indemnification; and

- authorizing us to retroactively indemnify an office holder.

The recent amendment to the Companies Law imposes similar conditions only on undertakings to indemnify an office holder for financial liabilities imposed by judgments but not for litigation expenses. Such an undertaking would be permitted if it is limited to events that our board of directors believes are foreseeable in light of our actual operations at the time of providing the undertaking and to a sum or criterion that our board of directors determines to be reasonable under the circumstances. We intend to amend or Articles of Association accordingly.

We have undertaken to indemnify our directors and officers pursuant to applicable law and intend to amend such undertakings in accordance with the recent amendment to the Companies Law. We have obtained directors and officers liability insurance for the benefit of our office holders.

Limitations on Exemption, Insurance and Indemnification

The Companies Law provides that a company may not exempt or indemnify an office holder, or enter into an insurance contract, which would provide coverage for any monetary liability incurred as a result of any of the following:

- a breach by the office holder of his duty of loyalty unless, with respect to insurance coverage, the office holder acted in good faith and had a reasonable basis to believe that the act would not prejudice the company;

- a breach by the office holder of his duty of care if the breach was done intentionally or recklessly;

- any act or omission done with the intent to derive an illegal personal benefit; or

- any fine levied against the office holder.

Required Approvals

In addition, under the Companies Law, any exemption of, indemnification of, or procurement of insurance coverage for, our office holders must be approved by our audit committee and our board of directors and, if the beneficiary is a director, by our shareholders.

Rights of Ordinary Shares

Our Ordinary Shares confer upon our shareholders the right to receive notices of, and to attend, shareholder meetings, the right to one vote per Ordinary Share at all shareholders' meetings for all purposes, and to share equally, on a per share basis, in such dividends as may be declared by our Board of Directors; and upon liquidation or dissolution, the right to participate in the distribution of any surplus assets of the Company legally available for distribution to shareholders after payment of all debts and other liabilities of the Company. All Ordinary Shares rank pari passu in all respects with each other. Our Board of Directors may, from time to time, make such calls as it may think fit upon a shareholder in respect of any sum unpaid in respect of shares held by such shareholder which is not payable at a fixed time, and each shareholder shall pay the amount of every call so made upon him (and of each installment thereof if the same is payable in installments).

Meetings of Shareholders

An annual general meeting of our shareholders shall be held once in every calendar year at such time and at such place either within or without the State of Israel as may be determined by our Board of Directors.

Our Board of Directors may, whenever it thinks fit, convene a special general meeting at such time and place, within or without the State of Israel, as may be determined by the Board of Directors. Special general meetings may also be convened upon requisition in accordance with the Companies Law.

Mergers and Acquisitions

A merger of the Company shall require the approval of the holders of a majority of seventy five percent (75%) of the voting power represented at the annual or special general meeting in person or by proxy or by written ballot, as shall be permitted, and voting thereon in accordance with the provisions of the Companies Law. Upon the request of a creditor of either party of the proposed merger, the court may delay or prevent the merger if it concludes that there exists a reasonable concern that as a result of the merger, the surviving company will be unable to satisfy the obligations of any of the parties to the merger. In addition, a merger may not be completed unless at least (i) 50 days have passed from the time that the requisite proposal for the merger has been filed by each party with the Israeli Registrar of Companies and (ii) 30 days have passed since the merger was approved by the shareholders of each party.

The Companies Law also provides that an acquisition of shares of a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 25% or greater shareholder of the company and there is no existing 25% or greater shareholder in the company. An acquisition of shares of a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 45% or greater shareholder of the company and there is no existing 45% or greater shareholder in the company. These requirements do not apply if the acquisition (i) occurs in the context of a private placement by the company that received shareholder approval, (ii) was from a 25% shareholder of the company and resulted in the acquirer becoming a 25% shareholder of the company or (iii) was from a 45% shareholder of the company and resulted in the acquirer becoming a 45% shareholder of the company. The tender offer must be extended to all shareholders, but the offerer is not required to purchase more than 5% of the company's outstanding shares, regardless of how many shares are tendered by shareholders. The tender offer may be consummated only if (i) at least 5% of the company's outstanding shares will be acquired by the offerer and (ii) the number of shares tendered in the offer exceeds the number of shares whose holders objected to the offer.

If as a result of an acquisition of shares the acquirer will hold more than 90% of a company's outstanding shares, the acquisition must be made by means of a tender offer for all of the outstanding shares. If as a result of a full the tender offer the acquirer would own more than 95% of the outstanding shares, then all the shares that the acquirer offered to purchase will be transferred to it. The law provides for appraisal rights if any shareholder files a request in court within three months following the consummation of a full tender offer. If as a result of a full tender offer the acquirer would own 95% or less of the outstanding shares, then the acquirer may not acquire shares that will cause his shareholding to exceed 90% of the outstanding shares.

Material Contracts

Settlement Agreement with Dictaphone

In June 2000, Dictaphone Corporation, one of our competitors, filed a patent infringement claim relating to certain technology embedded in some of our products. The claim was for damages for past infringement and enjoinment of any continued infringement of Dictaphone patents. On December 11, 2003, we agreed with Dictaphone to dismiss all claims and counterclaims in connection with Dictaphone's patent infringement claim against us. Under the terms of the settlement we are required to pay Dictaphone $10 million, of which approximately $4.8 million was paid by our insurance carrier in December 2003 and the balance was paid by us, except for the final installment in the amount of $333,335. This amount is required to be paid by us by June 30, 2005, subject to certain events which could result in a reduced payment by us. Each of the companies will grant the other a worldwide, royalty−free, perpetual license to certain of their respective patents including the disputed patents. The two companies further agreed to enter into enforcement proceedings with respect to both companies' patent portfolios and to share any proceeds from these actions.

Dictaphone Acquisition

On June 1, 2005, we consummated an agreement to acquire the assets and assume certain liabilities of Dictaphone's Communications Recording Systems (CRS™) business for approximately $38.5 million. Dictaphone's CRS business is a leading provider of liability and quality management systems for first responders, critical facilities, contact centers and financial trading floors.

Among the assets we acquired in the transaction is all of Dictaphone's rights to receive any damage award or other economic benefit with respect to a violation of any of the rights related to the intellectual property of Dictaphone's CRS business arising prior to the closing of the transaction.

TCS Acquisition

In November 2002, we consummated an agreement to acquire certain assets and liabilities of Thales Contact Solutions (or TCS), a developer of customer−facing technology for public safety, financial trading and customer contact centers, based in the United Kingdom. TCS was a unit of Thales Group, one of Europe's premier electronics companies. In connection with the acquisition, we paid an initial $29.9 million in cash and issued 2,187,500 ordinary shares to Thales Group at a fair market value of $18.1 million calculated at the date of closing. As of June 2, 2005, Thales Group holds approximately 4.6% of our outstanding shares. In June 2005, Mr. Timothy Robinson, one of the two Thales executives who were elected to our Board of Directors in November 2002, resigned from our Board. The acquisition agreement requires one nominee of Thales to resign upon the sale of more than half of the shares issued to Thales in the acquisition.

In the fourth quarter of 2002, we recorded a current liability of $2.8 million and a long−term liability of $13.5 million reflecting obligations under a long−term contract we assumed in the TCS acquisition. In the second quarter of 2003 we completed negotiations to terminate this contract as of November 2004 and to amend the terms in the interim. Under the terms of the amended contract, the cost to the Company was $5.2 million less than the amount provided at the acquisition date and consequently, TCS acquisition goodwill was reduced by this amount.

Under the terms of the agreement, the cash portion of the purchase price was subject to downward adjustment based on the value of net assets at closing and the full year 2002 sales of TCS. Based on our calculation of the actual value of net assets acquired and 2002 sales of TCS, we reduced the cash portion of the purchase price as of December 31, 2002 by $12.8 million. This amount was presented on our balance sheet as a Related Party Receivable as of December 31, 2002. Thus, the adjusted purchase price paid, including $4.5 million of capitalized acquisition costs, was recorded as $39.7 million. Of the $12.8 million adjustment referred to above, Thales paid us $6.6 million in March 2003.

Thales disputed our calculation of the net asset value at closing and the matter was submitted in September 2003 to binding arbitration by an Independent Accountant, in accordance with the terms of the acquisition agreement. The Independent Accountant determined a higher net asset value at closing than our calculation of the actual value of net assets acquired in the amount of $2.2 million. This additional amount was recorded as additional goodwill in the fourth quarter of 2003. The remaining Related Party Receivable as at December 31, 2003 of $4.0 million was paid in January 2004**.**

Also under the terms of the agreement, contingent cash payments of up to $10 million in 2003, $7.5 million in 2004, and $7.5 million in 2005 would be due if certain financial performance criteria are met as part of a three−year earn−out provision related to the sale of a particular product in 2002 through 2004. The relevant criteria were not met and, therefore, no contingent payments will be made under the agreement.

Under the terms of the agreement, the cash portion of the purchase price was subject to adjustment mechanisms and indemnities related to the assets sold to us. On September 8, 2004, we notified Thales of claims in respect of such price adjustment mechanisms, mainly relating to uncollected receivables and inventory. NICE and Thales signed a settlement agreement in respect of such claims on February 24, 2005, according to which Thales paid us a total indemnity amount of $2.6 million.

Sale of Comint/DF Business to Elta

On March 31, 2004, we sold the net assets of our COMINT/DF military−related business to ELTA Systems Ltd (“ELTA”) for $4 million in cash. The net assets sold include the intellectual property, fixed assets, inventory, and contracts related to the COMINT/DF product line which includes high performance spectral surveillance and direction finding systems that detect, identify, locate, monitor and record transmission sources. The COMINT/DF business is therefore treated as a discontinued operation in our financial statements.

In 2002, 2003 and 2004, the COMINT/DF business generated revenues of approximately $7.2 million, $6.5 million and $0.8 million, respectively, and net income of approximately $1.4 million, $1.5 million and $3.2 million (including gain on disposition), respectively.

Exchange Controls

Holders of ADSs are able to convert dividends and liquidation distributions into freely repatriable non−Israeli currencies at the rate of exchange prevailing at the time of repatriation, pursuant to regulations issued under the Currency Control Law, 5738–1978, provided that Israeli income tax has been withheld by us with respect to amounts that are being repatriated to the extent applicable or an exemption has been obtained.

Our ADSs may be freely held and traded pursuant to the General Permit and the Currency Control Law. The ownership or voting of ADSs by non−residents of Israel, except with respect to citizens of countries that are in a state of war with Israel, are not restricted in any way by the our memorandum of association or articles of association or by the laws of the State of Israel.

Taxation

The following is a discussion of Israeli and United States tax consequences material to our shareholders. The discussion is not intended, and should not be construed, as legal or professional tax advice and does not exhaust all possible tax considerations.

Holders of our ADSs should consult their own tax advisors as to the United States, Israeli or other tax consequences of the purchase, ownership and disposition of our ADSs, including, in particular, the effect of any foreign, state or local taxes.

Israeli Tax Considerations

The following is a summary of the principal tax laws applicable to companies in Israel, with special reference to their effect on us. The following contains a discussion of the material Israeli tax consequences to purchasers of our ordinary shares or ADSs. To the extent that the discussion is based on new tax legislation which has not been subject to judicial or administrative interpretation, we cannot assure you that the views expressed in the discussion will be accepted by the appropriate tax authorities or the courts. The discussion is not intended, and should not be construed, as legal or professional tax advice and is not exhaustive of all possible tax considerations. For a discussion of certain Israeli government programs benefiting various Israeli businesses, including us, please see "Item 5, Operating and Financial Review and Prospects."

General Corporate Tax Structure

Generally, Israeli companies are subject to corporate tax on taxable income at the rate of 35% for the 2004 tax year, 34% for the 2005 tax year, 32% for the 2006 tax year and 30% for the 2007 tax year and thereafter, and are subject to capital gains tax at a rate of 25% for capital gains (other than gains deriving from the sale of listed securities) derived after January 1, 2003. However, the effective tax rate payable by a company that derives income from an Approved Enterprise may be considerably less. See "Item 5, Operating and Financial Review and Prospects" for a discussion regarding our Approved Enterprise programs.

The Israeli Ministry of Finance recently published a memorandum proposing an amendment to the Israeli Tax Ordinance [New Version], 1961 ("Tax Ordinance"), under which the corporate tax rate will be gradually reduced to 25%, as follows: 31% for the 2006 tax year; 29% for the 2007 tax year; 27% for the 2008 tax year; 26% for the 2009 tax year; and 25% for the 2010 tax year and thereafter. In order to enact such proposal as legislation, it must be approved by the Israeli parliament and published. Because we cannot predict whether, and to what extent, such proposal will eventually be enacted into law, we face uncertainties as to the potential consequences of such proposal.

Stamp Duty

The Israeli Stamp Duty on Documents Law, 1961 (the "Stamp Duty Law"), provides that any document (or part thereof) that is signed in Israel or that is signed outside of Israel and refers to an asset or other thing in Israel or to an action that is executed or will be executed in Israel, is subject to a stamp duty, generally at a rate of between 0.4% and 1% of the value of the subject matter of such document. De facto, it has been common practice in Israel not to pay such stamp duty unless a document is filed with a governmental authority. An amendment to the Stamp Duty Law that came into effect on June 1, 2003, determines, among other things, that stamp duty on most agreements shall be paid by the parties that signed such agreement, jointly or severally, or by the party that undertook under such agreement to pay the stamp duty. As a result of the aforementioned amendment to the Stamp Duty Law, the Israeli tax authorities have approached many companies in Israel and requested disclosure of all agreements signed by such companies after June 1, 2003, with the aim of collecting stamp duty on such agreements. The legitimacy of the aforementioned amendment to the Stamp Duty Law and of said actions by the Israeli tax authorities are currently under review by the Israeli High Court of Justice.

Based on advice from our Israeli counsel, we believe that we may only be required to pay stamp duty on documents signed on or after August 2004. However, we cannot give any assurance that the tax authorities or the courts will accept such view. Although at this stage it is not yet possible to evaluate the effect, if any, on us of the amendment to the Stamp Duty Law, the same could materially adversely affect our results of operations in the future.

In January 2005, an order was signed in accordance with which the said requirement to pay stamp duty is cancelled with effect from January 1, 2008. Furthermore, pursuant to such order, as of January 1, 2005, stamp duty is no longer chargeable on, among others, loan agreements.

Tax Benefits and Grants for Research and Development

Israeli tax law allows, under specified conditions, a tax deduction for expenditures, including capital expenditures, for the year in which they are incurred. These expenses must relate to scientific research and development projects and must be approved by the relevant Israeli government ministry, determined by the field of research, and the research and development must be for the promotion of the company and carried out by or on behalf of the company seeking such deduction. However, the amount of such deductible expenses shall be reduced by the sum of any funds received through government grants for the finance of such scientific research and development projects. Expenditures not so approved are deductible over a three−year period.

Tax Benefits Under the Law for the Encouragement of Industry (Taxes), 1969

Under the Law for the Encouragement of Industry (Taxes), 1969 (the "Industry Encouragement Law"), Industrial Companies (as defined below) are entitled to the following tax benefits, among others:

- deductions over an eight−year period for purchases of know−how and patents;
- deductions over a three−year period of expenses involved with the issuance and listing of shares on the Tel Aviv Stock Exchange or, on or after January 1, 2003, on a recognized stock market outside of Israel;
- the right to elect, under specified conditions, to file a consolidated tax return with other related Israeli Industrial Companies; and
- accelerated depreciation rates on equipment and buildings.

Eligibility for benefits under the Industry Encouragement Law is not subject to receipt of prior approval from any governmental authority. Under the Industry Encouragement Law, an "Industrial Company" is defined as a company resident in Israel, at least 90% of the income of which, in any tax year, determined in Israeli currency, exclusive of income from government loans, capital gains, interest and dividends, is derived from an "Industrial Enterprise" owned by it. An "Industrial Enterprise" is defined as an enterprise whose major activity in a given tax year is industrial production activity. We believe that we currently qualify as an Industrial Company within the definition of the Industry Encouragement Law. No assurance can be given that we 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, represents an attempt to overcome the problems presented to a traditional tax system by an economy undergoing rapid inflation. The Inflationary Adjustments Law is highly complex. The features that are material to us can be described as follows:

- When the value of a company's equity, as calculated under the Inflationary Adjustments Law, exceeds the depreciated cost of Fixed Assets (as defined in the Inflationary Adjustments Law), a deduction from taxable income is permitted equal to the product of the excess multiplied by the applicable annual rate of inflation. The maximum deduction permitted in any single tax year is 70% of taxable income, with the unused portion permitted to be carried forward, linked to the increase in the consumer price index.
- If the depreciated cost of Fixed Assets exceeds a company's equity, then the product of such excess multiplied by the applicable annual rate of inflation is added to taxable income.
- Subject to certain limitations, depreciation deductions on Fixed Assets and losses carried forward are adjusted for inflation based on the increase in the consumer price index.

- Taxable gains on certain listed securities (which are currently taxed at a reduced tax rate with respect to individuals) are taxable at the Corporate Tax rate in certain circumstances.

However, the Minister of Finance may, with the approval of the Knesset Finance Committee, determine by order, during a certain fiscal year (or until February 28th of the following year) in which the rate of increase of the price index would not exceed or shall not have exceeded, as applicable, 3%, that all or some of the provisions of this Law shall not apply to such fiscal year, or, that the rate of increase of the price index relating to such fiscal year shall be deemed to be 0%, and to make the adjustments required to be made as a result of such determination.

The Tax Ordinance and regulations promulgated thereunder allow “Foreign−Invested Companies,” which maintain their accounts in U.S. dollars in compliance with the regulations published by the Israeli Minister of Finance, to base their tax returns on their operating results as reflected in the dollar financials statements or to adjust their tax returns based on exchange rate changes rather than changes in the Israeli consumer price index, in lieu of the principles set forth by the Inflationary Adjustments Law. For these purposes, a Foreign−Invested Company is a company, more than 25% of whose share capital, in terms of rights to profits, voting and appointment of directors, and of whose combined share and loan capital is held by persons who are not residents of Israel. A company that elects to measure its results for tax purposes based on the dollar exchange rate cannot change that election for a period of three years following the election. We believe that we qualify as a Foreign Investment Company within the meaning of the Inflationary Adjustments Law. For the time being we have elected to measure our results for tax purposes based on the U.S. dollar exchange rate.

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 unless 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 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, capital gains tax is imposed on Israeli resident individuals at a rate of 15% on real gains derived on or after January 1, 2003, from the sale of shares in, among others, (i) Israeli companies publicly traded on Nasdaq or on a recognized stock market in a country that has a treaty for the preventions of double taxation with Israel, or (ii) companies dually traded on both the Tel Aviv Stock Exchange and Nasdaq or a recognized stock market outside of Israel (such as NICE). This tax rate is contingent upon the shareholders not claiming a deduction for financing expenses in connection with such shares (in which case the gain will generally be taxed at a rate of 25%), and does not apply to: (i) the sale of shares by dealers in securities; (ii) the sale of shares by shareholders that report in accordance with the Income Tax Law (Inflationary Adjustments), 1985, referred to as the Inflationary Adjustments Law (that will generally be taxed at Corporate Tax rates for corporations and at marginal tax rates for individuals); or (iii) 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). The tax basis of shares acquired prior to January 1, 2003, will be 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.

According to the aforementioned memorandum proposing an amendment of the Tax Ordinance, it is proposed to reduce the aforementioned tax rate, commencing on January 1, 2006, to 20% for individuals, excluding with respect to a shareholder holding more than 10% of the outstanding share capital of the company who shall continue to be subject to a 25% tax rate.

Non−Israeli residents are generally exempt from Israeli capital gains tax on any gains derived from the sale of shares publicly traded on the TASE provided such gains did not derive from a permanent establishment of such shareholders in Israel, and 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 market outside of Israel, provided such shareholders did not acquire their shares prior to the issuer’s initial public offering and that the gains did not derive from a permanent establishment of such shareholders in Israel and that such shareholders are not subject to the Inflationary Adjustment Law. 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.

Taxation of Non−Residents

Individuals who are non−residents of Israel are subject to income tax on income derived or accrued from sources in Israel. Dividend distributions, other than bonus shares (share dividends) or stock dividends, are subject to a 25% withholding tax (15% in the case of dividends distributed from taxable income derived from an Approved Enterprise), unless a different rate is provided in a treaty between Israel and the shareholder’s country of residence. The withheld tax is the final tax in Israel on dividends paid to non−residents. See “—U.S.−Israel Tax Treaty.”

The aforementioned memorandum proposing an amendment of the Tax Ordinance, proposes to reduce the tax rate applicable to distributions of dividends to a rate of 20% for individuals, excluding a shareholder holding more than 10% of the outstanding share capital of the distributing company who shall continue to be subject to a 25% tax rate on such distributions.

A non−resident of Israel who has dividend income derived from or accrued in Israel, from which tax was withheld at source, is generally exempt from the duty to file tax returns in Israel in respect of such income, provided such income was not derived from a business conducted in Israel by the taxpayer.

Residents of the United States generally will have withholding tax in Israel deducted at source. They may be entitled to a credit or deduction for United States federal income tax purposes in the amount of the taxes withheld, subject to detailed rules contained in United States tax legislation.

U.S.−Israel Tax Treaty

Pursuant to the U.S.−Israel Tax Treaty, which became effective as of January 1, 1995, the sale, exchange or disposition of ADSs by a person who qualifies as a resident of the United States within the meaning of, and who is entitled to claim the benefits afforded to such resident by, the U.S.−Israel Tax Treaty ("Treaty U.S. Resident") will generally not be subject to the Israeli capital gains tax unless such Treaty 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 the capital gains from such sale, exchange or disposition can be allocated to a permanent establishment of such Treaty U.S. Resident in Israel. A sale, exchange or disposition of ADSs by a Treaty U.S. Resident who holds, directly or indirectly, shares representing 10% or more of the voting power of NICE at any time during such preceding 12−month period would be subject to such Israeli tax, to the extent applicable; however, under the U.S.−Israel Tax Treaty, the gain would be treated as foreign source income for United States foreign tax credit purposes and such Treaty U.S. Resident would be permitted to claim a credit for such taxes against the United States income tax imposed on such sale, exchange or disposition, subject to the limitations under the United States federal income tax laws applicable to foreign tax credits.

Under the U.S.−Israel Treaty, the maximum Israeli withholding tax on dividends paid by us is 25%. Dividends of an Israeli company derived from income of an Approved Enterprise are subject to a 15% withholding tax under Israeli law. The U.S.−Israel Tax Treaty further provides for a 12.5% Israeli dividend withholding tax on dividends paid by an Israeli company to a United States corporation owning at least 10% or more of such Israeli company's issued voting power for, in general, the part of the tax year which precedes the date of payment of the dividend and the entire preceding tax year, provided such United States corporation meets certain limitations concerning the amount of its dividend and interest income. The lower 12.5% rate applies only to dividends from income not derived from an Approved Enterprise in the applicable period and does not apply if the company has certain amounts (25%) of passive income. See "—Capital Gains and Income Taxes Applicable to Non−Israeli Shareholders."

U.S. Federal Income Tax Considerations

The following is a summary of certain material U.S. Federal income tax consequences that apply to U.S. Holders who hold ADSs as capital assets. This summary is based on U.S. Federal income tax laws, regulations, rulings and decisions in effect as of the date of this annual report, all of which are subject to change at any time, possibly with retroactive effect. This summary does not address all tax considerations that may be relevant with respect to an investment in ADSs. This summary does not account for the specific circumstances of any particular investor such as

- broker−dealers;
- financial institutions;
- certain insurance companies;
- investors liable for alternative minimum tax;
- tax−exempt organizations;
- investors that actually or constructively own 10 percent or more of our voting shares;
- investors holding ADSs as part of a straddle or a hedging or conversion transaction; and
- investors that are treated as partnerships or other pass through entities for U.S. federal income tax purposes.

This summary does not address the effect of any U.S. Federal taxation other than U.S. Federal income taxation. In addition, this summary does not include any discussion of state, local or foreign taxation.

You are urged to consult your tax advisors regarding the foreign and United States Federal, state and local tax considerations of an investment in ADSs.

For purposes of this summary, a U.S. Holder is:

- an individual who is a citizen or, for U.S. Federal income tax purposes, a resident of the United States;
- a corporation or other entity taxable as a corporation created or organized in or under the laws of the United States or any political subdivision thereof;
- an estate whose income is subject to U.S. Federal income tax regardless of its source; or
- a trust if:

(a) a court within the United States is able to exercise primary supervision over administration of the trust; and

(b) one or more United States persons have the authority to control all substantial decisions of the trust.

Taxation of Dividends

Subject to the discussion below under “passive foreign investment companies,” the gross amount of any distributions that you receive with respect to ADSs, including the amount of any

Israeli taxes withheld from these distributions, will constitute dividends for U.S. Federal income tax purposes, to the extent of our current and accumulated earnings and profits as determined for U.S. Federal income tax principles. You will be required to include this amount of dividends in gross income as ordinary income on the date such dividend is actually or constructively received. Distributions in excess of our earnings and profits will be treated as a non−taxable return of capital to the extent of your tax basis in the ADSs and, to the extent in excess of your tax basis, will be treated as capital gain. See "—Dispositions of ADSs" below for the discussion on the taxation of capital gains. Dividends generally will not qualify for the dividends−received deduction available to corporations.

Dividends that we pay in NIS, including the amount of any Israeli taxes withheld from these dividends, will be included as income to you in a U.S. dollar amount calculated by reference to the exchange rate in effect on the day such dividends are distributed. If you convert dividends paid in NIS into U.S. Dollars on the day the dividends are distributed, you generally should not be required to recognize foreign currency gain or loss with respect to such conversion. Any gain or loss resulting from a subsequent exchange of such NIS generally will be treated as U.S. source ordinary income or loss.

Subject to certain conditions and limitations, you may elect to claim a credit against your U.S. Federal income tax liability for Israeli tax withheld from dividends received in respect of the ADSs. Dividends generally will be treated as foreign−source passive income or financial services income for United States foreign tax credit purposes. 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. Alternatively, you may elect to claim a U.S. tax deduction, instead of a foreign tax credit, for such Israeli tax, but only for a year in which you elect to do so with respect to all foreign income taxes.

Dispositions of ADSs

If you sell or otherwise dispose of your ADSs, you will recognize gain or loss for U.S. Federal income tax purposes in an amount equal to the difference between the amount realized on the sale or other disposition and your adjusted tax basis in your ADSs. Subject to the discussion below under the heading ''—Passive Foreign Investment Companies,'' such gain or loss generally will be capital gain or loss and will be long−term capital gain or loss if you had held the ADSs for more than one year at the time of the sale or other disposition. Long−term capital gains realized by individual U.S. Holders generally are subject to a lower marginal U.S. federal income tax rate than ordinary income. Under most circumstances, any gain that you recognize on the sale or other disposition of ADSs will be U.S.−source for purposes of the foreign tax credit limitation; and losses recognized will be allocated against U.S. source income.

Passive Foreign Investment Companies

For U.S. Federal income tax purposes, we will be considered a passive foreign investment company, or PFIC, for any taxable year in which either 75% or more of our gross income is passive income, or at least 50% of the average value of all of our assets for the taxable year produce or are held for the production of passive income. For this purpose, passive income includes dividends, interest, royalties, rents, annuities and the excess of gain over losses from the disposition of assets which produce passive income. If we were determined to be a PFIC for U.S. Federal income tax purposes, highly complex rules would apply to U.S. Holders owning ADSs. Accordingly, you are urged to consult your tax advisors regarding the application of such rules.

If we are treated as a PFIC for any taxable year,

- you would be required to allocate income recognized upon receiving certain dividends or gain recognized upon the disposition of ADSs ratably over your holding period for such ADSs,
- the amount allocated to each year during which we are considered a PFIC other than the year of the dividend payment or disposition would be subject to tax at the highest individual or corporate tax rate, as the case may be, and an interest charge would be imposed with respect to the resulting tax liability allocated to each such year,
- gain recognized upon the disposition of ADSs would be taxable as ordinary income and
- you would be required to make an annual return on IRS Form 8621 regarding distributions received with respect to ADSs and any gain realized on your ADSs.

One method to avoid the aforementioned treatment is to make a timely mark−to−market election in respect of your ADSs. If you elect to mark−to−market your ADSs, you will generally include in income any excess of the fair market value of the ADSs at the close of each tax year over your adjusted basis in the ADSs. If the fair market value of the ADSs had depreciated below your adjusted basis at the close of the tax year, you may generally deduct the excess of the adjusted basis of the ADSs over its fair market value at that time. However, such deductions generally would be limited to the net mark−to−market gains, if any, that you included in income with respect to ADSs in prior years. Income recognized and deductions allowed under the mark−to−market provisions, as well as any gain or loss on the disposition of ADSs with respect to which the mark−to−market election is made, is treated as ordinary income or loss.

Based on our income, assets and activities for the year 2004, we believe that we were not a PFIC for that year, nor do we expect to become a PFIC in the foreseeable future. However, there can be no assurances that we will not be treated as a PFIC for that year or any taxable year. If we are or become a PFIC for any taxable year included in your holding period, we generally will remain a PFIC for all subsequent taxable years with respect to your holding of our ADSs.

You are urged to consult your tax advisor regarding the possibility of us being classified as a PFIC and the potential tax consequences arising from the ownership and disposition (directly or indirectly) of an interest in a PFIC.

Backup Withholding and Information Reporting

Payments in respect of ADSs may be subject to information reporting to the U.S. Internal Revenue Service and to U.S. backup withholding tax. Backup withholding will not apply, however, if you furnish a correct taxpayer identification number and make any other required certification or are otherwise exempt from backup withholding. Generally, you will provide such certification on Form W−9 (Request for Taxpayer Identification Number and Certification).

Documents on Display

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

You may read and copy any document we file with the SEC at its public reference facilities at, 450 Fifth Street, N.W., Washington, D.C. 20549 and at the SEC's regional offices at 500 West Madison Street, Suite 1400, Chicago, IL 60661−2511. You may also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549. The SEC also maintains a web site that contains reports, proxy and information statements and other information regarding registrants that file electronically with the SEC. The address of this web site is http://www.sec.gov. Please call the SEC at 1−800−SEC−0330 for further information on the operation of the public reference facilities. In addition, our ADSs are quoted on the Nasdaq Stock Market, so our reports and other information can be inspected at the offices of the National Association of Securities Dealers, Inc. at 1735 K Street, N.W., Washington, D.C. 20006.

Item 11. Quantitative and Qualitative Disclosures About Market Risk.

General

Market risks relating to our operations result primarily from weak economic conditions in the markets in which we sell our products and changes in interest rates and exchange rates. To manage the volatility related to the latter exposure, we may enter into various derivative transactions. Our objective is to reduce, where it is deemed appropriate to do so, fluctuations in earnings and cash flows associated with changes in currency exchange rates. It is our policy and practice to use derivative financial instruments only to manage exposures. We do not use financial instruments for trading purposes and are not a party to any leveraged derivative.

Foreign Currency Risk. We conduct our business primarily in U.S. dollars but also in the currencies of the United Kingdom, Canada, the European Union and Israel as well as other currencies. Thus, we are exposed to foreign exchange movements, primarily in UK, European and Israel currencies. We monitor foreign currency exposure and, from time to time, may enter into various contracts to preserve the value of sales transactions and commitments.

Interest Rate Risk**.** We invest in investment−grade U.S. corporate bonds and dollar deposits with FDIC−insured US banks. At least 80% of our securities investments are in corporate and US government agency bonds. Since these investments carry fixed interest rates and since our policy and practice is to hold these investments to maturity, interest income over the holding period is not sensitive to changes in interest rates. Up to 20% of our investment portfolio may be made in investment grade Callable Range Accrual Notes whose principal is guaranteed. As of December 31, 2004, 10% of our investment portfolio was in such Notes. The Notes are subject to interest rate, liquidity and price risks. Since our policy is to hold these investments to maturity or until called, the interest income from these notes will not be effected by changes in their market value or to liquidity risk. However, a significant increase in prevailing interest rates may effect whether or not interest income is received for a particular period. As of December 31 2004, 10% of our investment portfolio is invested in auction rate securities. Since our policy is to hold these auction rate securities until their interest reset date, we face potential capital loss if interest in the market rises dramatically during the holding period (up to 28 days).

Other risks and uncertainties that could affect actual results and outcomes are described in Item 3 of this Report under "Risk Factors."

Item 12. <u>Description of Securities Other than Equity Securities</u>.

Not Applicable.

PART II

Item 13. **Defaults, Dividend Arrearages and Delinquencies.**

None.

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

None.

Item 15. **Controls and Procedures.**

An evaluation was performed under the supervision and with the participation NICE's management, including its Chief Executive Officer and Chief Financial Officer, of the effectiveness of the NICE's disclosure controls and procedures (as defined in Rules 13a−15(e) and 15d−15(e) under the Securities and Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that these disclosure controls and procedures were effective. There has been no change in NICE's internal control over financial reporting during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the NICE's internal control over financial reporting.

Item 16A. **Audit Committee Financial Expert.**

Our board of directors has determined that Dan Falk meets the definition of an audit committee financial expert, as defined in Item 401 of Regulation S−K.

Item 16B. **Code of Ethics.**

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

Item 16C. Principal Accountant Fees and Services.

Fees Paid to Independent Auditors

Ernst & Young, has served as our independent auditor for the fiscal years ended December 31, 2003 and 2004. Fees billed or expected to be billed by Ernst & Young for professional services for each of the last two fiscal years were as follows:

Services Rendered	2003 Fees	2004 Fees
Audit (1)	$ 557,000	$ 495,000
Audit−related (2)	64,000	54,000
Tax (3)	79,000	207,000
Total	**$ 700,000**	**$ 756,000**

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(1) Audit fees consist of services that would normally be provided in connection with statutory and regulatory filings or engagements, including services that generally only the independent accountant can reasonably provide.

(2) Audit−related fees relate to assurance and associated services that traditionally are performed by the independent auditor, including: accounting consultation and consultation concerning financial accounting, reporting standards and government approvals.

(3) Tax fees relate to tax compliance, planning, advice and transfer price study.

Policies and Procedures

Our Audit Committee has adopted a policy and procedures for the pre−approval of audit and non−audit services rendered by our independent registered public accounting firm, Ernst & Young. The policy generally requires the Audit Committee's approval of the scope of the engagement of our independent auditor or on an individual basis. The policy prohibits retention of the independent auditors to perform the prohibited non−audit functions defined in Section 201 of the Sarbanes−Oxley Act of 2002 or the rules of the SEC, and also considers whether proposed services are compatible with the independence of the public auditors.

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

Not applicable.

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

In 2004, we did not purchase any of our own shares.

PART III

Item 17. Financial Statements.

Not Applicable.

Item 18. Financial Statements.

See pages F−1 through F−39, incorporated herein by reference.

Item 19. Exhibits.

Exhibit No.	Description
1.1	Memorandum of Association of NICE−Systems Ltd. (together with an English translation thereof) (filed as Exhibit 3.1 to NICE−Systems Ltd.'s Registration Statement on Form F−1 (Registration No. 333−99640) filed with the Commission on November 21, 1995, and incorporated herein by reference).
1.2	Articles of Association of NICE−Systems Ltd. approved by the Annual General Meeting of the Company's shareholders held on December 24, 2002 (filed as Exhibit 1.2 to NICE−Systems Ltd.'s Annual Report on Form 20−F filed with the Commission on June 26, 2003, and incorporated herein by reference).
2.1	Form of Share Certificate (filed as Exhibit 4.1 to Amendment No. 1 to NICE−Systems Ltd.'s Registration Statement on Form F−1 (Registration No. 333−99640) filed with the Commission on December 29, 1995, and incorporated herein by reference).
2.2	Form of Deposit Agreement including Form of ADR Certificate (filed as Exhibit A to NICE−Systems Ltd.'s Registration Statement on Form F−6 (Registration No. 333−13518) filed with the Commission on May 17, 2001, and incorporated herein by reference).
4.3	Sales and Purchase Agreement dated July 30, 2002 by and among NICE−Systems Ltd, NICE CTI Systems UK Ltd., NICE Systems SARL, NICE Systems GmbH, NICE Systems, Inc. and Thales SA. (filed as Exhibit 4.3 to NICE−Systems Ltd.'s Annual Report on Form 20−F filed with the Commission on June 26, 2003, and incorporated herein by reference).
4.4	Registration Rights Agreement between NICE−Systems Ltd. and Thales SA. (filed as Exhibit 4.4 to NICE−Systems Ltd.'s Annual Report on Form 20−F filed with the Commission on June 26, 2003, and incorporated herein by reference).
4.5	Manufacturing Outsourcing Agreement between Nice Systems Ltd. dated January 21, 2002 by and among Nice Systems Ltd. and Flextronics Israel Ltd. (filed as Exhibit 4.5 to NICE−Systems Ltd.'s Annual Report on Form 20−F filed with the Commission on June 26, 2003, and incorporated herein by reference).
4.6	Manufacturing Agreement dated November 5,2001 by and among Thales Contact Solutions Ltd. and Instem Technologies Ltd. (filed as Exhibit 4.6 to NICE−Systems Ltd.'s Annual Report on Form 20−F filed with the Commission on June 26, 2003, and incorporated herein by reference).

4.7	Settlement Agreement, dated February 24, 2005, among Thales SA, NICE Systems Ltd., NICE CTI Systems UK Ltd., NICE Systems SARL, NICE Systems GmbH and NICE Systems, Inc.
4.8	Asset Purchase and Sale Agreement, dated as of April 11, 2005, between Dictaphone Corporation and NICE Systems Inc.
4.9	Amendment No. 1, dated as of May 31, 2005, to the Asset Purchase and Sale Agreement, dated as of April 11, 2005, between Dictaphone Corporation and NICE Systems Inc.
8.1	List of significant subsidiaries
10.1	Consent of Kost, Forer, Gabbay & Kasierer, a member of Ernst & Young Global.
12.1	Certification by Haim Shani, the Chief Executive Officer of NICE Systems Ltd., pursuant to Section 302 of the Sarbanes−Oxley Act 2002.
12.2	Certification by Ran Oz, the Chief Financial Officer of NICE Systems Ltd., pursuant to Section 302 of the Sarbanes−Oxley Act of 2002.
13.1	Certification by Haim Shani, the Chief Executive Officer of NICE Systems Ltd., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes−Oxley Act of 2002.
13.2	Certification by Ran Oz, the Chief Financial Officer of NICE Systems Ltd., pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes−Oxley Act of 2002.

NICE SYSTEMS LTD. AND SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2004

IN U.S. DOLLARS

INDEX

Report of Independent Registered Public Accounting Firm

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of

NICE SYSTEMS LTD.

We have audited the accompanying consolidated balance sheets of NICE Systems Ltd. ("the Company") and subsidiaries as of December 31, 2003 and 2004, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above, present fairly, in all material respects, the consolidated financial position of the Company and subsidiaries as of December 31, 2003 and 2004, and the consolidated results of their operations and cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States.

Tel−Aviv, Israel
February 2, 2005

KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

CONSOLIDATED BALANCE SHEETS
U.S. dollars in thousands

	December 31, 2003	December 31, 2004
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 29,859	$ 26,579
Short−term bank deposits	189	175
Marketable securities	17,187	24,348
Trade receivables (net of allowance for doubtful accounts of $2,284 and $2,661 in 2003 and 2004, respectively)	45,973	46,407
Other receivables and prepaid expenses	7,366	7,937
Related party receivables	4,013	—
Inventories	12,634	12,615
Assets of discontinued operation	3,945	652
Total current assets	121,166	118,713
LONG−TERM INVESTMENTS:		
Long−term marketable securities	60,034	114,805
Investment in affiliates	1,200	1,200
Severance pay fund	6,155	7,356
Long−term receivables and prepaid expenses	729	854
Total long−term investments	68,118	124,215
PROPERTY AND EQUIPMENT, NET	18,627	16,981
OTHER INTANGIBLE ASSETS, NET	16,193	12,665
GOODWILL	25,311	25,745
Total assets	$ 249,415	$ 298,319

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

CONSOLIDATED BALANCE SHEETS
U.S. dollars in thousands (except share data)

	December 31, 2003	December 31, 2004
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Trade payables	$ 15,744	$ 11,975
Accrued expenses and other liabilities	47,370	55,302
Liabilities of discontinued operation	1,878	8
Total current liabilities	64,992	67,285
LONG−TERM LIABILITIES:		
Accrued severance pay	6,925	8,163
Other long−term liabilities	667	—
Total long−term liabilities	7,592	8,163
COMMITMENTS AND CONTINGENT LIABILITIES		
SHAREHOLDERS' EQUITY:		
Share capital−		
Ordinary shares of NIS 1 par value:		
Authorized: 50,000,000 shares as of December 31, 2003 and 2004; Issued and outstanding: 16,748,953 and 18,180,260 shares as of December 31, 2003 and 2004, respectively	5,142	5,464
Additional paid−in capital	224,855	244,400
Accumulated other comprehensive income	3,888	5,506
Accumulated deficit	(57,054)	(32,499)
Total shareholders' equity	176,831	222,871
Total liabilities and shareholders' equity	$ 249,415	$ 298,319

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

CONSOLIDATED STATEMENTS OF OPERATIONS
U.S. dollars in thousands (except per share data)

	Year ended December 31,		
	2002	2003	2004
Revenues:			
Products	$ 127,896	$ 168,055	$ 182,616
Services	27,445	56,203	70,027
Total revenues	155,341	224,258	252,643
Cost of revenues:			
Products	55,453	64,231	64,432
Services	26,054	42,084	49,876
Total cost of revenues	81,507	106,315	114,308
Gross profit	73,834	117,943	138,335
Operating expenses:			
Research and development, net	17,122	22,833	24,866
Selling and marketing	38,743	53,701	62,172
General and administrative	23,806	29,840	31,269
Goodwill impairment	28,260	—	—
Restructuring expenses, in−process research and development write−off, settlement of litigation and other	832	7,082	—
Total operating expenses	108,763	113,456	118,307
Operating income (loss)	(34,929)	4,487	20,028
Financial income, net	3,992	2,034	3,556
Other income (expenses), net	(4,065)	292	54
Income (loss) before taxes on income	(35,002)	6,813	23,638
Taxes on income	350	1,205	2,319
Net income (loss) from continuing operations	(35,352)	5,608	21,319
Net income from discontinued operation	1,370	1,483	3,236
Net income (loss)	$ (33,982)	$ 7,091	$ 24,555
Net earnings (loss) per share:			
Basic:			
Continuing operations	$ (2.56)	$ 0.35	$ 1.22
Discontinued operation	0.10	0.09	0.18
	$ (2.46)	$ 0.44	$ 1.40
Diluted:			
Continuing operations	$ (2.56)	$ 0.33	$ 1.14
Discontinued operation	0.10	0.09	0.17
Net earnings (loss)	$ (2.46)	$ 0.42	$ 1.31

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

STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
U.S. dollars in thousands

	Share capital	Additional paid−in capital	Deferred stock compensation	Accumulated other comprehensive income (loss)	Accumulated deficit	Total comprehensive income (loss)	Total shareholders' equity
Balance as of January 1, 2002	$ 4,398	$ 192,845	$ (24)	$ (38)	$ (30,163)		$ 167,018
Issuance of shares of ESPP	28	1,355	—	—	—		1,383
Issuance of shares in respect of the acquisition of CPS	11	458	—	—	—		469
Issuance of shares in respect of the acquisition of TCS	458	17,593	—	—	—		18,051
Issuance of shares in respect of the acquisition of SCI	*) —	29	—	—	—		29
Amortization of deferred stock compensation	—	—	12	—	—		12
Exercise of share options	13	723	—	—	—		736
Comprehensive loss:							
Foreign currency translation adjustments	—	—	—	793	—	$ 793	793
Unrealized gains on derivative instruments, net	—	—	—	27	—	27	27
Net loss	—	—	—	—	(33,982)	(33,982)	(33,982)
Total comprehensive loss						$ (33,162)	
Balance as of December 31, 2002	4,908	213,003	(12)	782	(64,145)		154,536
Issuance of shares of ESPP	49	1,470	—	—	—		1,519
Amortization of deferred stock compensation	—	—	12	—	—		12
Exercise of share options	185	10,382	—	—	—		10,567
Comprehensive income:							
Foreign currency translation adjustments	—	—	—	3,031	—	$ 3,031	3,031
Unrealized gains on derivative instruments, net	—	—	—	75	—	75	75
Net income	—	—	—	—	7,091	7,091	7,091
Total comprehensive income						$ 10,197	
Balance as of December 31, 2003	5,142	224,855	—	3,888	(57,054)		176,831
Issuance of shares of ESPP	31	2,234	—				2,265
Exercise of share options	291	17,311	—				17,602
Comprehensive income:							
Foreign currency translation adjustments	—	—	—	1,617	—	$ 1,617	1,617
Unrealized gains on derivative instruments, net	—	—	—	1	—	1	1
Net income	—	—	—	—	24,555	24,555	24,555
Total comprehensive income						$ 26,173	
Balance as of December 31, 2004	$ 5,464	$ 244,400	$ —	$ 5,506	$ (32,499)		$ 222,871
Accumulated unrealized gains on derivative instruments				$ 65			
Accumulated foreign currency translation adjustments				5,441			
Accumulated other comprehensive income as of December 31, 2004				$ 5,506			

*) Represents an amount lower than $ 1.

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

CONSOLIDATED STATEMENTS OF CASH FLOWS
U.S. dollars in thousands

	Year ended December 31,		
	2002	2003	2004
Cash flows from operating activities:			
Net income (loss)	$ (33,982)	$ 7,091	$ 24,555
Less: net income from discontinued operation	(1,370)	(1,483)	(3,236)
Net income (loss) from continuing operations	(35,352)	5,608	21,319
Adjustments required to reconcile net income (loss) from continuing operations to net cash provided by operating activities from continuing operations:			
Depreciation and amortization	15,248	17,617	13,793
In−process research and development write−off	1,270	—	—
Stock compensation in respect of CPS acquisition	469	—	—
Amortization of deferred stock compensation	12	12	—
Accrued severance pay, net	(399)	124	37
Goodwill impairment	28,260	—	—
Impairment of investment in affiliate	229	—	—
Amortization of premium (accretion of discount) and accrued interest on held−to−maturity marketable securities	915	1,459	1,205
Decrease (increase) in trade receivables	(1,523)	3,901	(585)
Decrease (increase) in other receivables and prepaid expenses	(1,281)	1,208	(549)
Decrease (increase) in inventories	4,025	1,515	(122)
Decrease (increase) in long−term receivables and prepaid expenses	(483)	39	(105)
Increase (decrease) in trade payables	2,895	(104)	(3,761)
Increase in accrued expenses and other liabilities	2,051	4,819	13,043
Increase in long−term liabilities related to legal settlement	—	667	—
Other	315	(5)	(7)
Net cash provided by operating activities from continuing operations	16,651	36,860	44,268
Net cash provided by operating activities from discontinued operation	3,462	1,316	750
Net cash provided by operating activities	20,113	38,176	45,018

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

	Year ended December 31,		
	2002	2003	2004
Cash flows from investing activities:			
Purchase of property and equipment	(5,322)	(5,492)	(6,701)
Proceeds from sale of property and equipment	557	747	89
Purchase of other intangible assets	(610)	—	—
Investment in marketable securities	(16,936)	(72,077)	(122,192)
Proceeds from maturity of marketable securities	29,492	33,997	17,710
Proceeds from sale and call of held−to−maturity marketable securities	820	8,500	41,345
Investment in short−term bank deposits	(150)	(132)	(129)
Proceeds from short−term bank deposits	265	165	149
Payment for the acquisition of certain assets and liabilities of TCS (a)	(31,480)	(316)	—
Decrease in accrued acquisition costs	(214)	(3,008)	(75)
Payment in respect of terminated contract from TCS acquisition	—	(6,518)	(5,249)
Decrease in related party receivables from TCS acquisition	—	6,635	4,013
Capitalization of software development costs	(4,609)	(2,291)	(1,305)
Net cash used in investing activities from continuing operations	(28,187)	(39,790)	(72,345)
Net cash provided by (used in) investing activities from discontinued operation	(117)	(52)	4,136
Net cash used in investing activities	(28,304)	(39,842)	(68,209)
Cash flows from financing activities:			
Proceeds from issuance of shares upon exercise of options and ESPP, net	2,119	12,086	19,867
Short−term bank credit, net	24	(24)	—
Net cash provided by financing activities	2,143	12,062	19,867
Effect of exchange rate changes on cash	73	182	44
Increase (decrease) in cash and cash equivalents	(5,975)	10,578	(3,280)
Cash and cash equivalents at the beginning of the year	25,256	19,281	29,859
Cash and cash equivalents at the end of the year	$ 19,281	$ 29,859	$ 26,579
Supplemental disclosure of cash flows activities:			
Cash paid during the year for:			
Income taxes	$ 445	$ 564	$ 598

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

	Year ended December 31, 2002	2003	2004
(a) Payment for the acquisition of certain assets and liabilities of TCS:			
Fair value of assets acquired and liabilities assumed at the acquisition date:			
Working capital (excluding cash and cash equivalents)	$ 8,347	$ —	
Related party receivables	12,804	—	
Property and equipment	7,616	—	
Other intangible assets	9,320	—	
In−process research and development	1,270	—	
Other long−term liability	(13,500)	—	
Goodwill	26,682	416	
	52,539	416	
Less − amount acquired by issuance of shares	(18,051)	—	
Less − accrued acquisition costs	(3,008)	(100)	
	$ 31,480	$ 316	
Non−cash activities:			
(a) Issuance of additional shares related to settlement of SCI acquisition:			
Goodwill	$ 29		
(b) Adjustments of goodwill in respect of TCS acquisition:			
Related party receivables		$ 2,156	
Accrued expenses and other liabilities		(319)	
Other long−term liability		(5,162)	
		$ (3,325)	
(c) Adjustment of goodwill in respect of discontinued operation sale			$ (250)

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

NOTE 1:− GENERAL

a. General:

NICE Systems Ltd. (“NICE”) and subsidiaries (collectively − “the Company”) develop, market and support integrated, scalable multimedia digital recording platforms, enhanced software applications and related professional services. These solutions capture and analyze unstructured (non−transaction) data and convert it for business and security performance management applications. The Company’s solutions capture multiple forms of interaction, including voice, fax, email, web chat, radio, and video transmissions over wire line, wireless, packet telephony, terrestrial trunk radio and data networks.

The Company’s products are based on two types of recording platforms − audio and video. The Company’s solutions are offered to various vertical markets in two major sectors: (1) the Enterprise Interaction Solutions Sector − contact centers and trading floors and (2) the Public Safety and Security Sector − safety organizations, transportation, corporate security, gaming and correctional facilities and government and intelligence agencies.

The Company’s products are sold primarily through a global network of distributors, system integrators and strategic partners; a portion of product sales and most services are sold directly to end−users.

The Company’s markets are located primarily in North America, EMEA and the Far East.

The Company depends on a limited number of contract manufacturers for producing its products. If any of these manufacturers become unable or unwilling to continue to manufacture or fail to meet the quality or delivery requirements needed to satisfy the Company’s customers, it could result in the loss of sales, which could adversely affect the Company’s results of operations and financial position.

The Company relies upon a number of independent distributors to market, sell and service its products in certain markets. If the Company is unable to effectively manage and maintain relationships with its distributors, or to enter into similar relationships with others, its ability to market and sell its products in these markets will be affected. In addition, a loss of a major distributor, or any event negatively affecting such distributors’ financial condition, could cause a material adverse effect on the Company’s results of operations and financial position.

As for major customer data, see Note 16c.

b. Disposal by sale of the COMINT/DF operation:

In the fourth quarter of 2003, the Company reached a definitive agreement to sell the assets and liabilities of its COMINT/DF military−related business to ELTA Systems Ltd. for $ 4,000 in cash. On March 31, 2004, the Company completed the sale of the COMINT/DF operation. The COMINT/DF business was treated as a discontinued operation in the financial statements.

The Company’s balance sheets at December 31, 2003 and 2004 reflect the assets and liabilities of the COMINT/DF operation, as assets and liabilities of the discontinued operation within current assets and current liabilities.

The carrying amounts of the major classes of assets and liabilities included as part of the discontinued operation are:

	December 31, 2003	December 31, 2004
Trade receivables	$ 2,839	$ 652
Other receivables and prepaid expenses	207	—
Severance pay fund	687	—
Property and equipment, net	212	—
Assets of discontinued operation	$ 3,945	$ 652
Trade payables	$ 66	$ —
Accrued expenses and other liabilities	982	8
Accrued severance pay	830	—
Liabilities of discontinued operation	$ 1,878	$ 8

Summarized selected financial information of the discontinued operation is as follows:

	Year ended December 31, 2002	2003	2004
Revenues	$ 7,164	$ 6,510	$ 816
Net income	$ 1,370	$ 1,483	$ *) 3,236

*) Includes gain from the sale in the amount of $ 3,286.

c. Acquisition of Thales Contact Solutions:

In November 2002, the Company acquired certain assets and assumed certain liabilities of Thales Contact Solutions (“TCS”) for an aggregate consideration of $ 52,539 including the issuance of 2,187,500 American Depositary Shares (“ADSs”) of NICE valued at $ 18,051. TCS is a developer of customer−facing technology for Public Safety, Wholesale Trading and Call Centers, based in the United Kingdom. The acquisition was accounted for by the purchase method and accordingly, the purchase price has been allocated according to the estimated fair value of the assets acquired and liabilities assumed of TCS. The value of the shares issued was determined based on the market price of NICE’s shares on the acquisition date. The results of TCS’s operations have been included in the consolidated financial statements since November 2, 2002 (“the closing date”).

With the acquisition of TCS, the Company significantly expanded its customer base, presence in Europe, and its network of distributors and partners. Additionally, the Company broadened its product offerings and global professional services team.

In the fourth quarter of 2002, the Company recorded a current liability of $ 2,800 and a long−term liability of $ 13,500 reflecting estimation of obligations under a long−term contract assumed by the Company in the TCS acquisition for which no future benefit exists. During the second quarter of 2003, the Company signed an agreement to amend and terminate the above mentioned agreement as of November 2004. The cost to the Company under the termination agreement was $ 5,162 less than the amount provided in respect of the above mentioned agreement at the acquisition date. Consequently, goodwill has been reduced by $ 5,162.

Under the terms of the agreement, the initial cash portion of the purchase price was adjusted downward in 2002 by $ 12,804 in respect of the actual net value of assets acquired and 2002 sales of TCS. Thales disputed the net asset value at closing and in September 2003 the parties submitted the matter to binding arbitration by an independent accountant. In December 2003, an arbitration award was issued, according to which the related party receivables from Thales should be reduced by $ 2,156. The Company recorded the $ 2,156 as addition to goodwill in the fourth quarter of 2003. Due to the arbitration award and additional acquisition costs incurred during 2003, the acquisition cost totaled $ 42,307 as of December 31, 2003.

The following table summarizes the fair values of the assets acquired and liabilities assumed:

Trade receivables	$ 15,808
Other receivables and prepaid expenses	1,448
Inventories	6,776
Property and equipment	7,616
In−process research and development	1,270
Trademarks	1,040
Core technology	1,620
Distribution network	6,160
Maintenance contracts	500
Goodwill	23,773
Total assets acquired	66,011
Trade payables	(1,747)
Accrued expenses and other liabilities	(13,619)
Long−term liability	(8,338)
Total liabilities assumed	(23,704)
Net assets acquired	$ 42,307

Other intangible assets with definite life in the amount of $ 3,160 are amortized using the straight−line method at annual weighted average rate of 29%.

The $ 1,270 assigned to in−process research and development was written off at the acquisition date in accordance with FASB Interpretation (“FIN”) No. 4, “Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method”.

The following represents the unaudited pro−forma condensed results of operations for the year ended December 31, 2002, assuming that the acquisition occurred on January 1, 2002. The pro−forma information is not necessarily indicative of the results of operations, which actually would have occurred if the acquisition had been consummated on January 1, 2002, nor does it purport to represent the results of operations for future periods.

	Year ended December 31, 2002
Revenues	$ 206,838
Net loss	$ (53,821)
Basic and diluted net loss per share	$ (3.45)

The condensed results of operations of TCS are based on the results of operations of TCS for the period from January 1, 2002 to November 2, 2002 (the closing date), which were prepared by TCS's management and were submitted to the Company as part of the acquisition.

d. Acquisition of CenterPoint Solutions Inc.:

In April 2000, the Company acquired all of the outstanding capital stock of CenterPoint Solutions Inc. ("CPS") for a total consideration of $ 12,886 including the issuance of 200,000 ADSs of NICE of which 50,000 were deemed target shares ("the target shares") contingent upon the achievement of certain objectives. The acquisition was accounted for by the purchase method and accordingly, the purchase price has been allocated according to the estimated fair value of the assets acquired and liabilities assumed of CPS.

CPS is a developer of Internet−based applications for statistical monitoring, digital recording and automatic customer surveys for customer contact centers.

On March 19, 2002, Mr. Chapiewski, a former shareholder of CPS, filed an action against the Company by complaint. In this complaint, Mr. Chapiewski alleged that the Company violated Sections 604(3) and 604(4) of the Colorado Securities Act, committed common law fraud and negligent misrepresentation, and breached representations and warranties in the agreement relating to the CPS acquisition, by misrepresenting to Mr. Chapiewski, either affirmatively or through omissions, the Company's financial results and value of securities. Mr. Chapiewski also claimed that NICE Centerpoint breached severance provisions of an employment agreement with him in the amount of $ 80. Mr. Chapiewski sought damages in an unspecified amount. On November 25, 2002, the Company settled the claim with Mr. Chapiewsky, without any admission of liability or wrongdoing on its part, for an amount of $ 3,000 and the release from escrow of the target shares valued at $ 469. The settlement agreement resulted in a one−time charge to other expenses of $ 3,469 in 2002, of which $ 300 was recovered from insurance proceeds in 2003.

**NOTE 2:−	SIGNIFICANT ACCOUNTING POLICIES**

The consolidated financial statements were prepared in accordance with United States Generally Accepted Accounting Principles ("U.S. GAAP").

a. Use of estimates:

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

b. Financial statements in United States dollars:

The currency of the primary economic environment in which the operations of NICE and certain subsidiaries are conducted is the U.S. dollar ("dollar"); thus, the dollar is the functional currency of NICE and certain subsidiaries.

NICE and certain subsidiaries' transactions and balances denominated in dollars are presented at their original amounts. Non−dollar transactions and balances have been remeasured to dollars in accordance with Statement of Financial Accounting Standards ("SFAS") No. 52, "Foreign Currency Translation". All transaction gains and losses from remeasurement of monetary balance sheet items denominated in non−dollar currencies are reflected in the statements of operations as financial income or expenses, as appropriate.

For those subsidiaries whose functional currency has been determined to be their local currency, assets and liabilities are translated at year−end exchange rates and statement of operations items are translated at average exchange rates prevailing during the year. Such translation adjustments are recorded as a separate component of accumulated other comprehensive income (loss) in shareholders' equity.

c. Principles of consolidation:

Intercompany transactions and balances have been eliminated upon consolidation.

d. Cash equivalents:

The Company considers short−term unrestricted highly liquid investments that are readily convertible into cash, purchased with maturities of three months or less to be cash equivalents.

e. Short−term bank deposits:

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

f. Marketable securities:

The Company accounts for investments in debt securities in accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities".

Management determines the appropriate classification of its investments in debt securities at the time of purchase and reevaluates such determinations at each balance sheet date.

Debt securities are classified as held−to−maturity when the Company has the positive intent and ability to hold the securities to maturity and are stated at amortized cost. The cost of held−to−maturity securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization, accretion, decline in value judged to be other than temporary, and interest are included in financial income or expenses, as appropriate.

Interest income resulting from investments in structured notes that are classified as held to maturity is accounted for under the provision of EITF No. 96−12, "Recognition of Interest Income and Balance Sheet Classification of Structured Notes". Under Emerging Issues Task Force ("EITF") No. 96−12, the retrospective interest method is used for recognizing interest income.

Auction rate securities are classified as available−for−sale and accordingly, these securities are stated at fair value. Realized gains and losses on sales of securities, as determined on a specific identification basis, are included in the consolidated statement of operations.

g. Inventories:

Inventories are stated at the lower of cost or market value. The cost of raw materials and work−in−progress is determined by the "average cost" method, and the cost of finished goods on the basis of costs charged by third party manufacturer.

Inventory provisions are provided to cover risks arising from slow−moving items, technological obsolescence, excess inventories, discontinued products and for market prices lower than cost. Inventory provisions for 2002, 2003 and 2004, were $ 1,650, $ 2,368 and $ 2,822, respectively, and have been included in cost of revenues.

h. Investment in affiliates:

The investments in affiliated companies are stated at cost, since the Company does not have the ability to exercise significant influence over operating and financial policies of those investees.

The Company's investment in affiliates is reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the investment may not be recoverable. In 2002, an impairment loss had been identified in the amount of $ 229.

i. Property and equipment, net:

Property and equipment are stated at cost, net of accumulated depreciation.

Depreciation is calculated using the straight−line method over the estimated useful lives of the assets, at the following annual rates:

	%
Computers and peripheral equipment	33
Office furniture and equipment	6 − 15
Motor vehicles	15

Leasehold improvements are amortized by the straight−line method over the term of the lease or the estimated useful life of the improvements, whichever is shorter.

j. Other intangible assets, net:

Intangible assets are amortized over their useful lives using a method of amortization that reflects the pattern in which the economic benefits of the intangible assets are consumed or otherwise used, in accordance with SFAS No. 142, "Goodwill and Other Intangible Assets".

Amortization is calculated using the straight−line method over the estimated useful lives at the following annual rates:

	Weighted average %
Capitalized software development costs (see o)	33
Core technology	28
Trademarks	34
Maintenance contracts	33

In accordance with the requirement of SFAS No. 142, intangible assets deemed to have indefinite lives are no longer amortized after January 1, 2002. The distribution network is deemed to have an indefinite useful life because it is expected to generate cash flows indefinitely. In accordance with SFAS No. 142, the Company evaluates the remaining useful life each year to determine whether events and circumstances continue to support an indefinite useful life. The Company performed annual impairment test in 2004, and did not identify any impairment.

k. Impairment of long−lived assets:

The Company's long−lived assets and certain identifiable intangibles are reviewed for impairment in accordance with SFAS No. 144, "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 the assets to the future undiscounted cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. In 2004, no impairment indicators have been identified.

l. Goodwill:

Goodwill represents the excess of the cost over the fair value of the net assets of businesses acquired. Under SFAS No. 142, goodwill acquired in a business combination consummated on or after July 1, 2001, is not amortized. Goodwill arising from acquisitions prior to July 1, 2001 was amortized until December 31, 2001 on a straight−line basis over 10 years.

SFAS No. 142 requires goodwill to be tested for impairment at least annually or between annual tests in certain circumstances, and written down when impaired, rather than amortized as previous accounting standards required. Goodwill is tested for impairment by comparing the fair value of the reporting unit with its carrying value. Fair value is determined using discounted cash flows and market capitalization. Significant estimates used in the fair value methodologies include estimates of future cash flows, future growth rates and the weighted average cost of capital of the reporting unit. The Company performed annual impairment tests during the fourth quarter of 2002, 2003 and 2004, and recognized impairment losses of $ 28,260, $ 0 and $ 0, respectively.

m. Revenue recognition:

The Company generates revenues from sales of products, which include hardware and software, software licensing, professional services and maintenance.

The Company sells its products indirectly through a global network of distributors, system integrators and strategic partners, all of whom are considered end−users, and through its direct sales force.

Revenues from product sales and software license agreements are recognized when all criteria outlined in Statement Of Position (“SOP”) 97−2, “Software Revenue Recognition” (as amended by SOP 98−9) are met. Revenue from products and license fees is recognized when persuasive evidence of an agreement exists, delivery of the product has occurred, the fee is fixed or determinable, no further obligations exist and collectibility is probable. Sales agreements with specific acceptance terms are not recognized until the customer has confirmed that the product or service has been accepted.

Where software license arrangements involve multiple elements, revenue is allocated to each element based on Vendor Specific Objective Evidence (“VSOE”) of the relative fair values of each element in the arrangement, in accordance with the residual method. The Company’s VSOE used to allocate the sales price to maintenance is based on the renewal percentage. Under the residual method, revenue is recognized for the delivered elements when (1) there is VSOE of the fair values of all the undelivered elements, and (2) all revenue recognition criteria of SOP 97−2, as amended, are satisfied. Under the residual method any discount in the arrangement is allocated to the delivered element.

The Company maintains a provision for product returns in accordance with SFAS No. 48, “Revenue Recognition When Right of Return Exists”. The provision is estimated based on the Company’s past experience and is deducted from revenues. Trade receivables as of December 31, 2003 and 2004, are presented net of provision for product returns in the amounts of $ 2,079 and $ 1,617, respectively.

Revenues from maintenance and professional services are recognized ratably over the contractual period or as services are performed.

Deferred revenue includes advances and payments received from customers, for which revenue has not yet been recognized.

n. Warranty costs:

Provisions for warranty costs are made at the time revenues are recognized, for estimated costs during the warranty period based on the Company’s experience. Provision for warranty as of December 31, 2003 and 2004, amounted to $ 446 and $ 498, respectively. A tabular reconciliation of the changes in the Company’s aggregate product warranty liability was not provided due to immateriality.

o. Research and development costs:

Research and development costs (net of grants and participations) incurred in the process of software production before establishment of technological feasibility, are charged to expenses as incurred. Costs of the production of a product master incurred subsequent to the establishment of technological feasibility are capitalized according to the principles set forth in SFAS No. 86, “Accounting for the Costs of Computer Software to be Sold, Leased or Otherwise Marketed”. Based on the Company’s product development process, technological feasibility is established upon completion of a detailed program design or a working model.

Costs incurred by the Company between completion of the detailed program design or working model and the point at which the product is ready for general release have been capitalized.

Capitalized software development costs are amortized commencing with general product release by the straight−line method over the estimated useful life of the software product.

p. Income taxes:

The Company accounts for income taxes in accordance with SFAS No. 109, “Accounting for Income Taxes”. This statement 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.

q. Government grants:

Non−royalty bearing grants from the Government of Israel for funding research and development projects are recognized at the time the Company is entitled to such grants on the basis of the related costs incurred and recorded as a deduction from research and development costs.

r. Concentrations of credit risk:

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

The Company's cash and cash equivalents and short−term bank deposits are invested in deposits mainly in dollars with major international banks. Such deposits in the United States may be in excess of insured limits and are not insured in other jurisdictions. Management believes that the financial institutions that hold the Company's investments are financially sound and, accordingly, minimal credit risk exists with respect to these investments.

The Company's trade receivables are derived from sales to customers located primarily in North America, EMEA and the Far East. The Company performs ongoing credit evaluations of its customers and obtains letter of credit and bank guarantees for certain receivables. Additionally, the Company insures certain of its receivables with a credit insurance company. An allowance for doubtful accounts is provided with respect to specific debts that the Company has determined to be doubtful of collection and a general provision on the remaining balance, based on the length of time the receivables are past due.

The Company's marketable securities include investment in U.S. corporate debentures, U.S government debentures, structured notes and auction rate securities. Management believes that the portfolio is well diversified, and accordingly, minimal credit risk exists with respect to those marketable securities.

The Company entered into forward contracts and option strategies (together: "derivative instruments") intended to protect against the increase in value of forecasted non−dollar currency cash flows and the increase/decrease in fair value of non−dollar liabilities/assets. The derivative instruments effectively hedge the Company's non−dollar currency exposure (see Note 10).

s. Severance pay:

The Company's liability for severance pay for its Israeli employees is calculated pursuant to Israeli severance pay law based on the most recent monthly salary of the employees multiplied by the number of years of employment as of the balance sheet date. Employees are entitled to one month's salary for each year of employment, or a portion thereof. The Company's liability is fully provided by monthly deposits with insurance policies and severance pay funds and by an accrual.

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

Severance pay expense for 2002, 2003 and 2004, was $ 1,869, $ 2,745 and $ 2,956, respectively.

t. Basic and diluted net earnings (loss) per share:

Basic net earnings (loss) per share are computed based on the weighted average number of Ordinary shares outstanding during each year. Diluted net earnings (loss) per share are computed based on the weighted average number of Ordinary shares outstanding during each year plus dilutive potential equivalent Ordinary shares considered outstanding during the year, in accordance with SFAS No. 128, “Earnings Per Share”.

The weighted average number of shares related to outstanding antidilutive options excluded from the calculations of diluted net earnings (loss) per share was 5,315,170, 1,935,692 and 1,094,775 for the years ended December 31, 2002, 2003 and 2004, respectively.

u. Stock−based compensation:

The Company has elected to follow APB No. 25, “Accounting for Stock Issued to Employees” and FIN No. 44, “Accounting for Certain Transactions Involving Stock Compensation” in accounting for its employee stock option plan. Under APB No. 25, when the exercise price of the Company’s options is less than the market value of the underlying shares on the date of grant, compensation expense is recognized and amortized ratably over the vesting period of the options.

The Company adopted the disclosure provisions of SFAS No. 148, “Accounting for Stock−Based Compensation − Transition and Disclosure”, which amended certain provisions of SFAS No. 123. The Company continues to apply the provisions of APB No. 25, in accounting for stock−based compensation.

Pro forma information regarding net income (loss) and net earnings (loss) per share is required by SFAS No. 123, “Accounting for Stock−Based Compensation”, and has been determined as if the Company had accounted for its employee options under the fair value method prescribed by that statement. The fair value for these options was estimated at the date of grant using the Black−Scholes option pricing model with the following assumptions:

	Year ended December 31,		
	2002	2003	2004
Risk free interest rate	1.7%	1.8%	2.7%
Dividend yield	0%	0%	0%
Volatility factor	0.827	0.545	0.457
Expected life of the options	4.3	3	3

Black−Scholes pricing−model also was used to estimate the fair value of the ESPP compensation; assumptions are not provided due to the immateriality of the ESPP portion.

Pro forma information under SFAS No. 123:

	Year ended December 31,		
	2002	2003	2004
Net income (loss) as reported	$ (33,982)	$ 7,091	$ 24,555
Add: Stock−based compensation expense included in the determination of net income (loss) as reported	12	12	—
Deduct: Stock−based compensation expense determined under fair value method for all awards	(18,467)	(10,350)	(7,182)
Pro forma net income (loss)	$ (52,437)	$ (3,247)	$ 17,373
Basic net earnings (loss) per share as reported	$ (2.46)	$ 0.44	$ 1.40
Diluted net earnings (loss) per share as reported	$ (2.46)	$ 0.42	$ 1.31
Pro forma basic net earnings (loss) per share	$ (3.80)	$ (0.20)	$ 0.99
Pro forma diluted net earnings (loss) per share	$ (3.80)	$ (0.20)	$ 0.93

v. Fair value of financial instruments:

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

The carrying amount reported in the balance sheet for cash and cash equivalents, short−term bank deposits, trade receivables, short−term bank credit and trade payables approximates their fair value due to the short−term maturities of such instruments.

The fair value for marketable securities is based on quoted market prices and does not differ significantly from the carrying amount (see Note 3).

w. Advertising expenses:

Advertising expenses are charged to expense as incurred. Advertising expenses for the years 2002, 2003 and 2004, was $ 1,760, $ 2,077 and $ 2,621, respectively.

x. Derivatives and hedging activities:

SFAS No. 133, “Accounting for Derivative Instruments and Hedging Activities” requires the Company to recognize all of its derivative instruments as either assets or liabilities on the balance sheet at fair value. The accounting for changes in the fair value (i.e., gains or losses) of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship. For those derivative instruments that are designated and qualify as hedging instruments, a company must designate the hedging instrument, based upon the exposure being hedged, as a fair value hedge, cash flow hedge or a hedge of a net investment in a foreign operation.

For derivative instruments that are designated and qualify as a fair value hedge (i.e., hedging the exposure to changes in the fair value of an asset or a liability or an identified portion thereof that is attributable to a particular risk), the gain or loss on the derivative instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the line item associated with the hedged item in earnings during the period of the change in fair values. For derivative instruments that are designated and qualify as a cash flow hedge (i.e., hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of accumulated other comprehensive income and reclassified into earnings in the line item associated with the hedged transaction in the period or periods during which the hedged transaction affects earnings. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item, if any, is recognized in financial income/expense in the period of change.

y. Impact of recently issued accounting standards:

On December 16, 2004, the Financial Accounting Standards Board (FASB) issued Statement No. 123 (revised 2004), “Share−Based Payment” (“Statement 123R”), which is a revision of FASB Statement No. 123, “Accounting for Stock−Based Compensation” (“Statement 123”). Generally, the approach in Statement 123R is similar to the approach described in Statement 123. However, Statements 123 permitted, but not required, share−based payments to employees to be recognized based on their fair values while Statement 123R requires all share−based payments to employees to be recognized based on their fair values. Statement 123R also revises, clarifies and expands guidance in several areas, including measuring fair value, classifying an award as equity or as a liability and attributing compensation cost to reporting periods. The new Standard will be effective for the Company in the first fiscal year beginning after June 15, 2005. The adoption of Statement 123R will have a significant effect on the Company’s results of operations.

In November 2004, the FASB issued SFAS No. 151, “Inventory Costs, an Amendment of ARB No. 43, Chapter 4”. SFAS No. 151 amends Accounting Research Bulletin (“ARB”) No. 43, Chapter 4, to clarify that abnormal amounts of idle facility expense, freight handling costs and wasted materials (spoilage) should be recognized as current−period charges. In addition, SFAS No. 151 requires that the allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. SFAS No. 151 is effective for inventory costs incurred during fiscal years beginning after June 15, 2005. The Company does not expect that the adoption of SFAS No. 151 will have a material effect on its financial position or results of operations.

z. Reclassification:

Certain amounts from prior years have been reclassified to conform to the current year’s presentation. The reclassification had no effect on previously reported net income (loss), shareholders’ equity or cash flows.

NOTE 3:− MARKETABLE SECURITIES

a. The following table summarizes amortized costs, gross unrealized gains and losses and estimated fair values of held−to−maturity marketable securities as of December 31, 2003 and 2004:

	Amortized cost December 31,		Gross unrealized gains December 31,		Gross unrealized losses December 31,		Estimated fair value December 31,	
	2003	2004	2003	2004	2003	2004	2003	2004
U.S. corporate debentures	$ 40,216	$ 37,968	$ 164	$ 1	$ 67	$ 368	$ 40,313	$ 37,601
U.S government debentures	19,505	74,805	24	11	77	560	19,452	74,256
Structured notes	17,500	12,680	—	—	7	—	17,493	12,680
	$ 77,221	$ 125,453	$ 188	$ 12	$ 151	$ 928	$ 77,258	$ 124,537

Information about gross unrealized losses based on the length of time that individual securities have been in a continuous unrealized loss position was not provided due to immateriality.

As of December 31, 2003 and 2004, all the Company’s U.S. corporate debentures, U.S. government debentures and structured notes were classified as held−to−maturity.

In 2002 and 2004, the Company sold debt securities, which were classified as held−to−maturity, due to a rating decrease, in consideration of $ 820 and $ 911, respectively. As a result of the sale, the Company recorded a loss of $ 55 and $ 14, respectively. In 2003, the Company did not sell any securities prior to their maturity and accordingly, did not realize any gains or losses on held−to−maturity securities in that year. During 2003 and 2004, held−to−maturity marketable securities in the amount of $ 8,500 and $ 40,434, respectively, were called by the issuers prior to maturity.

The scheduled maturities of held−to−maturity marketable securities at December 31, 2004 are as follows:

	Amortized cost	Estimated fair value
Held−to−maturity:		
Due within one year	$ 10,648	$ 9,091
Due after one year through five years	109,805	110,446
Due after five years through ten years	5,000	5,000
	$ 125,453	$ 124,537

b. Auction rate securities amounting to $ 13,700 as of December 31, 2004, were classified as available−for−sale marketable securities and were presented as short−term marketable securities.

NOTE 4:− OTHER RECEIVABLES AND PREPAID EXPENSES

	December 31,	
	2003	2004
Government authorities	$ 1,670	$ 1,848
Interest receivable	1,151	994
Prepaid expenses	3,064	4,250
Other	1,481	845
	$ 7,366	$ 7,937

NOTE 5:− INVENTORIES

	December 31,	
	2003	2004
Raw materials	$ 2,574	$ 1,286
Work−in−progress	120	71
Finished goods	9,940	11,258
	$ 12,634	$ 12,615

NOTE 6:− PROPERTY AND EQUIPMENT, NET

	December 31, 2003	December 31, 2004
Cost:		
Computers and peripheral equipment	$ 44,144	$ 50,474
Office furniture and equipment	13,105	13,701
Motor vehicles	134	—
Leasehold improvements	3,658	3,823
	61,041	67,998
Accumulated depreciation:		
Computers and peripheral equipment	35,992	42,454
Office furniture and equipment	4,749	6,501
Motor vehicles	99	—
Leasehold improvements	1,574	2,062
	42,414	51,017
Depreciated cost	$ 18,627	$ 16,981

Depreciation expense totaled $ 9,775, $ 10,547 and $ 8,603 for the years ended December 31, 2002, 2003 and 2004, respectively.

NOTE 7:− OTHER INTANGIBLE ASSETS, NET

a. Other intangible assets

	December 31, 2003	December 31, 2004
Original amounts:		
Capitalized software development costs	$ 22,979	$ 19,355
Core technology	4,419	4,419
Trademarks	1,040	1,040
Maintenance contracts	548	576
	28,986	25,390
Accumulated amortization:		
Capitalized software development costs	15,838	14,980
Core technology	3,078	3,695
Trademarks	408	726
Maintenance contracts	213	416
	19,537	19,817
Amortized cost	9,449	5,573
Distribution network	6,744	7,092
Total other intangible assets	$ 16,193	$ 12,665

b. Amortization expense amounted to $ 5,473, $ 7,070 and $ 5,190 for the years ended December 31, 2002, 2003 and 2004, respectively.

c. Estimated amortization expense for the years ended (excluding amortization of capitalized software development costs):

	December 31,
2005	$ 665
2006	188
2007	188
2008	157
	$ 1,198

NOTE 8:− GOODWILL

The changes in the carrying amount of goodwill for the years ended December 31, 2003 and 2004 are as follows:

Balance as of January 1, 2003	$ 27,417
Adjustments to goodwill	(2,909)
Foreign currency translation adjustments	803
Balance as of December 31, 2003	$ 25,311
Applied against sale of discontinued operation	(250)
Foreign currency translation adjustments	684
Balance as of December 31, 2004	$ 25,745

NOTE 9:− ACCRUED EXPENSES AND OTHER LIABILITIES

	December 31,	
	2003	2004
Employees and payroll accruals	$ 11,580	$ 13,228
Accrued expenses	22,966	19,949
Restructuring accrual	604	256
Deferred revenues	10,054	18,677
Other	2,166	3,192
	$ 47,370	$ 55,302

NOTE 10:− DERIVATIVE INSTRUMENTS

To protect against changes in the value of forecasted foreign currency transactions and balances, the Company has instituted a foreign−currency hedging program. The Company hedges portions of its forecasted cash flows and balances denominated in foreign currencies with forward contracts and option strategies (together: “derivative instruments”).

The Company entered into derivative instrument arrangements to hedge a portion of anticipated New Israeli Shekel ("NIS") payroll payments. These derivative instruments are designated as cash flows hedges, as defined by SFAS No. 133, as amended, and are all highly effective as hedges of these expenses when the salary is recorded. The effective portion of the derivative instruments is included in payroll expenses in the statements of operations.

In addition, the Company entered into derivative instruments to hedge certain trade receivables, trade payable payments, expected payments under fixed price contracts denominated in foreign currency, liabilities to employees and other long−term liability. The purpose of the Company's foreign currency hedging activities is to protect the Company from changes in the foreign currency exchange rate to the dollar.

At December 31, 2004, the Company expects to reclassify $ 65 of net gains on derivative instruments from accumulated other comprehensive income to earnings during the next twelve months.

NOTE 11:− RESTRUCTURING EXPENSES

Following the acquisition of TCS, the Company identified an opportunity to increase flexibility and focus, improve responsiveness and reduce unnecessary overhead. In December 2002, the Company adopted a plan ("the 2002 Plan") to achieve these objectives, which involved the phased reduction of approximately 75 of the initially combined 1,077 staff and consolidation of certain field offices. The Company expects to incur a total cost of $ 2,170 in connection with this plan. The Company elected early adoption of SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". The major components of the 2002 Plan are as follows:

	Employee termination benefits	Facility closure	Loss on disposal of property and equipment	Total restructuring charge
Total amount expected to be incurred	$ 1,544	$ 605	$ 21	$ 2,170
Costs incurred in 2002	$ 282	$ —	$ —	$ 282
Restructuring accrual as of December 31, 2002	282	—	—	282
Costs incurred in 2003	1,262	605	21	1,888
Costs paid in 2003	(1,443)	(139)	(21)	(1,603)
Restructuring accrual as of December 31, 2003	101	466	—	567
Additional restructuring expenses (reversal of over accrued amounts)	(16)	16	—	—
Costs paid in 2004	(85)	(239)	—	(324)
Restructuring accrual as of December 31, 2004	$ —	$ 243	$ —	$ 243
Remaining amount expected to be incurred	$ —	$ —	$ —	$ —

At December 31, 2004, a total amount of $ 256 is included in accrued expenses and other liabilities for the above−mentioned plan and for the 2001 plan together.

NOTE 12:− COMMITMENTS AND CONTINGENT LIABILITIES

a. Lease commitments:

The Company leases office space, office equipment and various motor vehicles under operating leases.

1. The Company’s office space and office equipment are rented under several operating leases.

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

2005	$ 5,842
2006	4,724
2007	2,637
2008	1,568
2009 and thereafter	610
	$ 15,381

Rent expenses for the years ended December 31, 2002, 2003 and 2004 were approximately $ 5,761, $ 6,554 and $ 6,107, respectively.

2. The Company leases its motor vehicles under cancelable operating lease agreements.

The minimum payment under these operating leases, upon cancellation of these lease agreements was $ 768 as of December 31, 2004.

Lease expenses of vehicles for the years ended December 31, 2002, 2003 and 2004 were $ 1,616, $ 2,124 and $ 2,396, respectively.

b. Other commitments:

The Company is obligated under certain agreements with its suppliers to purchase goods and under an agreement with its manufacturing subcontractor to purchase excess inventory. Non cancelable obligations as of December 31, 2004, were approximately as follows:

2005	$ 2,887
2006	1,335
2007	144
2008	144
2009	144
	$ 4,654

c. Legal proceedings:

1. On October 19, 2004, CipherActive filed an action against the Company in the District Court of Tel Aviv, State of Israel. In this lawsuit, CipherActive claimed that under a development agreement with the Company, it is entitled to receive license fees in respect of certain software that it allegedly developed for the Company and which has been embedded in one of the Company's products. CipherActive claimed that it is entitled to license fees in the amount of $ 600, in addition to the amount of $ 100 already paid to CipherActive by the Company in respect of such license fees. In the Company's statement of defense it claimed that the software developed by CipherActive under the agreement has not been successful in the market, is no longer embedded in the Company's product and, therefore, CipherActive is not entitled to any additional license fees.

2. In July 2004, the Company's wholly owned subsidiary, STS Software Systems Ltd. ("STS"), filed a lawsuit in the U.S. District Court for the Southern District of New York charging Witness Systems, Inc. ("Witness") with infringement of the one of the Company's VoIP patents in the U.S, by marketing and selling products that incorporate methods of detecting, monitoring and recording information − all fully protected by that patent. STS is seeking an injunction against Witness, preventing the sale of any solution which infringes the Company's patent.

   In August 2004, Witness filed a patent infringement action in the Federal Court for the Northern District of Georgia against the Company's wholly owned subsidiary NICE Systems, Inc. Witness subsequently filed an identical action in February 2005 against NICE in the same court. The two actions were consolidated in March 2005. Witness accuses the Company of infringing two U.S patents relating to certain technology used with some of the Company's products. Witness is requesting a permanent injunction against alleged future infringement and damages for past alleged infringement. The Company has responded to Witness' claims and has asserted that the patents are invalid and not infringed. At this stage the Company cannot predict the outcome of the claim, nor can it make any estimate of the amount of damages, if any, for which it will be held responsible in the event of a negative conclusion to the claim.

3. The U.S Consumer Product Safety Commission has brought to the Company's attention and provided it an opportunity to comment on an alleged incident of a fire allegedly involving a NICE product used in a school building in the Evesham New Jersey School District. The Company has retained specialized counsel and engineering consultants and is investigating this matter. The Company believes, as advised by outside counsel, that based on the facts known at present, it is not expected that this matter will result in any regulatory action.

NOTE 13:− CREDIT LINES

As of December 31, 2004, the Company had authorized credit lines from banks in the amount of $ 139,000. When utilized, the credit lines will be denominated in dollars and will bear interest at the rate of up to LIBOR + 1.5 %. An amount of $ 116,000 out of the total credit lines is secured by the Company's marketable securities. There are no financial covenants associated with these credit lines. As of December 31, 2004, $ 5,756 of the $ 139,000 referred to above was used for bank guarantees.

NOTE 14:− TAXES ON INCOME

a. Measurement of taxable income:

Results for tax purposes are measured in real terms, in accordance with the changes in the Israeli Consumer Price Index ("CPI") or changes in the exchange rate of the NIS against the dollar for a "foreign investors" company. NICE has elected to measure its results for tax purposes on the basis of the changes in the exchange rate of NIS against the dollar.

b. Tax benefits under the Israel Law for the Encouragement of Capital Investments, 1959 ("the Law"):

Certain production facilities of NICE have been granted the status of "Approved Enterprise" under the Law, in four separate investment programs.

According to the provisions of the Law, NICE elected the "alternative benefits" and waived government grants in return for a tax exemption.

Income derived from the first and second program was tax−exempt for a period of four years, commencing 1999 and 1997, respectively, and is taxed at the reduced corporate tax rate of 10%−25% (based on the percentage of foreign ownership in each taxable year) for an additional period of six years.

Income derived from the third and fourth programs will be tax−exempt for a period of two years, commencing with the year NICE first earns taxable income, and will be taxed at the reduced corporate tax rate of 10%−25% (based on the percentage of foreign ownership in each taxable year) for an additional period of eight years.

The period of tax benefits detailed above is subject to limits of the earlier of 12 years from the commencement of production or 14 years from receiving the approval.

The entitlement to the above benefits is conditional upon NICE's fulfilling the conditions stipulated by the above Law, regulations published thereunder and the certificates of approval for the specific investments in an "Approved Enterprise". In the event of failure to comply with these conditions, the benefits may be canceled and NICE may be required to refund the amount of the benefits, in whole or in part, including interest. As of December 31, 2004, management believes that NICE is in compliance with all the conditions required by the law.

As of December 31, 2004, approximately $ 18,214 was derived from tax−exempt profits earned by NICE's "Approved Enterprises". NICE has decided not to declare dividends out of such tax−exempt income. Accordingly, no deferred tax liabilities have been provided on income attributable to NICE's "Approved Enterprises". If the net retained tax exempt income is distributed, it would be taxed at the corporate tax rate applicable to such profits as if NICE had not elected the alternative tax benefits (currently − 20% of the gross distributed amount) and an income tax liability would be incurred of approximately $ 4,554 as of December 31, 2004.

Income of NICE from sources other than the "Approved Enterprise" during the period of benefits will be taxable at the regular corporate tax rate.

A recent amendment to the Law, which has been officially published effected as of April 1, 2005 (the "Amendment") has changed certain provisions of the Law. The Amendment enacted changes in the manner in which tax benefits are awarded under the law so that companies no longer require Investment Center approval in order to qualify for tax benefits. The Company's existing Approved Enterprises will generally not be subject to the provisions of the Amendment.

c. Tax benefits under the Israeli Law for the Encouragement of Industry (Taxation), 1969:

NICE is an industrial company under the above law and as such is entitled to certain tax benefits including accelerated depreciation, deduction of public offering expenses in three equal annual installments and amortization of other intangible property rights as a deduction for tax purposes.

d. Reduction in corporate tax rate:

In June 2004, the Israeli Parliament approved an amendment to the Income Tax Ordinance (No. 140 and Temporary Provision), which progressively reduces the regular corporate tax rate from 36% to 35% in 2004, 34% in 2005, 32% in 2006 and to a rate of 30% in 2007.

e. Net operating loss carryforward:

As of December 31, 2004, the Company had carryforward tax losses totaling approximately $ 25,468, most of which can be carried forward and offset against taxable income with expiration dates from 2005 to 2022. Utilization of U.S. net operating losses may be subject to the substantial annual limitation due to the "change in ownership" provisions of the Internal Revenue Code of 1986 and similar state provisions. The annual limitation may result in the expiration of net operating losses before utilization.

f. 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 tax assets are as follows:

	December 31, 2003	December 31, 2004
Net operating loss carryforward	$ 12,478	$ 8,712
Reserves and allowances	709	720
Net deferred tax asset before valuation allowance	13,187	9,432
Valuation allowance	(13,187)	(9,432)
Net deferred tax asset	$ —	$ —

The Company has provided valuation allowances in respect of deferred tax assets resulting from tax loss carry forwards and other reserves and allowances due to uncertainty concerning its realization of these deferred tax assets.

g. Reconciliation between the theoretical tax expenses assuming all income is taxed at the statutory tax rate applicable to income of NICE and the actual tax expense as reported in the consolidated statements of operations is as follows:

	Year ended December 31, 2002	2003	2004
Income (loss) before taxes on income, as reported in the consolidated statements of operations	$ (35,002)	$ 6,813	$ 23,638
Statutory tax rate in Israel	36%	36%	35%
Theoretical income tax expense (benefit)	$ (12,601)	$ 2,453	$ 8,273
Losses and other items for which a valuation allowance was provided	3,218	174	3,055
Non−deductible acquisition−related costs (income)	11,201	(108)	71
Tax exempt interest income	(1,145)	—	—
Utilization of net operating losses for which a valuation allowance was provided	(676)	(2,014)	(9,490)
Non−deductible expenses	407	515	420
Other	(54)	185	(10)
Actual tax expense	$ 350	$ 1,205	$ 2,319

h. Income (loss) before taxes on income is comprised as follows:

	Year ended December 31,		
	2002	2003	2004
Domestic	$ (34,043)	$ 4,345	$ 15,367
Foreign	(959)	2,468	8,271
	$ (35,002)	$ 6,813	$ 23,638

i. The provision for income taxes is comprised as follows:

Current taxes	$ 350	$ 1,205	$ 2,319
Domestic	$ 126	$ 949	$ 1,836
Foreign	224	256	483
	$ 350	$ 1,205	$ 2,319

NOTE 15:− SHAREHOLDERS' EQUITY

a. The Ordinary shares of the Company are traded on the Tel Aviv Stock Exchange and its ADSs are traded on NASDAQ.

b. Share option plans:

In 1995, the Company adopted an employee share option plan ("the 1995 Option Plan"). Under the 1995 option plan, employees and officers of the Company may be granted options to acquire Ordinary shares. The options to acquire Ordinary shares, which may only be determined by the Board of Directors of the Company, are granted at an exercise price, subject to certain exceptions, of not less than the fair market value of the Ordinary shares on the grant date. 8,345,566 options of the 1995 Option Plan were granted.

The options generally vest gradually over a four−year period from the date of grant. As of February 15, 2000, the Board of Directors of the Company adopted a resolution amending the exercise terms for any option granted subsequent to February 15, 2000 under the 1995 Option Plan whereby 25% of the stock options granted become exercisable on the first anniversary of the date of grant and 6.25% become exercisable once every quarter during the subsequent three years. The options expire no later than 6 years from the date of grant.

In 1996, the Company adopted the 1997 Executive Share Option Plan (“the 1997 Option Plan”). Under the terms of the 1997 Option Plan, stock options will be exercisable during a 60−day period ending four years after grant. The plan met the definition of Time Accelerated Restricted Stock Award Options Plan (“TARSAP”). The TARSAP includes an acceleration feature based on the following: if the year−end earnings per share of the Company shall reach certain defined targets, 40% of such stock options shall become exercisable; if earnings per share shall reach certain higher defined targets, an additional 30% of such stock options shall become exercisable; and if earnings per share shall reach certain higher defined targets, an additional 30% of such stock options shall become exercisable, provided that with respect to all of the above−referenced periods, the operating profit of the Company shall not be less than 10% of revenues and earnings per share shall exclude any non−recurring expenses related to mergers and acquisitions. Notwithstanding the foregoing, none of the stock options shall be exercisable before the expiration of two years from the date of issuance. 950,000 options of the 1997 Option Plan were granted. As of December 31, 2004, none of the targets specified under the TARSAP were met and accordingly there was no acceleration of options.

In 2001, the Company adopted the 2001 Stock Option Plan (“the 2001 Option Plan”). The options to acquire Ordinary shares, which may only be determined by the Board of Directors of the Company, are granted at an exercise price, of not less than the fair market value of the Ordinary shares on the grant date. 2,959,750 options of the 2001 Option Plan were granted. Under the terms of the 2001 Option Plan, a one third of the stock options granted became exercisable ten months after the grant date and the remaining two thirds will become exercisable on the first and second anniversaries of the first date of exercise so long as the grantee is, subject to certain exceptions, employed by the Company at the date the stock option becomes exercisable. The third portion of the options may be exercised at the end of the second year following the first date of exercise, if the Company meets a pre−tax profit target of 20% of revenues. Unless otherwise determined by the Company’s Board of Directors as of the date of grant, the stock options expire six years after the date of grant. As of December 31, 2004, none of the targets specified were met and accordingly there was no acceleration of options.

In 2003, the Company adopted the 2003 Stock Option Plan (“the 2003 Option Plan”). Under the 2003 option plan, employees and officers of the Company may be granted options to acquire Ordinary shares. The options to acquire Ordinary shares, which may only be determined by the Board of Directors of the Company, are granted at an exercise price, subject to certain exceptions, of not less than the fair market value of the Ordinary shares on the grant date. 1,368,500 options of the 2003 Option Plan were granted. Unless otherwise determined by the Company’s Board of Directors as of the date of grant, the stock options expire six years after the date of grant.

A summary of the Company's stock options activity and related information for the years ended December 31, 2002, 2003 and 2004, is as follows:

	2002		2003		2004	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at the beginning of the year	6,408,825	$ 29.31	5,965,980	$ 25.74	4,910,389	$ 26.80
Granted	981,000	$ 11.49	390,000	$ 22.55	997,500	$ 21.33
Exercised	(60,830)	$ 12.10	(823,363)	$ 12.83	(1,291,394)	$ 13.63
Forfeited	(1,363,015)	$ 32.87	(622,228)	$ 32.52	(346,178)	$ 40.46
Outstanding at the end of the year	5,965,980	$ 25.74	4,910,389	$ 26.80	4,270,317	$ 28.40
Exercisable at the end of the year	2,373,039	$ 34.46	2,790,417	$ 33.55	2,556,779	$ 34.59

The options outstanding as of December 31, 2004, have been separated into exercise price categories as follows:

Ranges of exercise price	Options outstanding as of December 31, 2004	Weighted average remaining contractual life	Weighted average exercise price	Options exercisable as of December 31, 2004	Weighted average exercise price of options exercisable
$		(Years)	$		$
7.83−11.14	334,325	3.74	9.98	104,105	10.19
12.00−16.81	1,395,531	2.62	12.97	1,177,463	12.81
19.33−28.07	1,453,761	5.07	21.91	188,511	23.09
30.13−40.94	41,000	0.86	39.62	41,000	39.62
48.13−70.88	702,500	1.51	57.36	702,500	57.36
75.63−78.88	343,200	1.16	75.87	343,200	75.87
	4,270,317	3.23	28.40	2,556,779	34.59

Weighted average fair values and weighted average exercise prices of options whose exercise price is equal or higher than the market price of the shares at date of grant are as follows:

	Weighted average fair value of options granted at an exercise price			Weighted average exercise price of options granted at an exercise price		
	Year ended December 31,					
	2002	2003	2004	2002	2003	2004
Equal to fair value at date of grant	$ 8.03	$ 8.36	$ 7.14	$ 12.99	$ 22.55	$ 21.33
Higher than fair value at date of grant	$ 5.19	$ —	$ —	$ 10.51	$ —	$ —

c. Employee Stock Purchase Plan ("ESPP"):

In February 1999, the Company's Board of Directors adopted the Employee Stock Purchase Plan ("the Purchase Plan"). Eligible employees can have up to 10% of their earnings withheld, up to certain maximums, to be used to purchase Ordinary shares. The price of Ordinary shares purchased under the Purchase Plan will be equal to 85% of the lower of the fair market value of the Ordinary shares on the commencement date of each offering period or on the semi−annual purchase date.

During 2002, 2003 and 2004, employees purchased 131,667, 221,184 and 139,913 shares at average prices of $ 10.51, $ 6.86 and $ 16.20 per share, respectively.

d. Dividends:

Dividends, if any, will be paid in NIS. Dividends paid to shareholders outside Israel may be converted to dollars on the basis of the exchange rate prevailing at the date of the conversion. The Company does not intend to pay cash dividends in the foreseeable future.

NOTE 16:− MAJOR CUSTOMER AND GEOGRAPHIC INFORMATION

a. Summary information about geographic areas:

The Company manages its business on a basis of one reportable segment. See Note 1a for a brief description of the Company's business. The following data is presented in accordance with SFAS No. 131, "Disclosure About Segments of an Enterprise and Related Information". Total revenues are attributed to geographic areas based on the location of end customers.

The following table presents total revenues and long−lived assets for the years ended December 31, 2002, 2003 and 2004 and as of December 31, 2002, 2003 and 2004 respectively:

	2002		2003		2004	
	Total revenues	Long−lived assets	Total revenues	Long−lived assets	Total revenues	Long−lived assets
Americas	$ 86,938	$ 10,835	$118,594	$ 9,926	$121,578	$ 10,130
EMEA*)	45,236	18,489	70,926	19,586	89,768	19,372
Far East	20,679	95	31,832	72	37,779	140
Israel	2,488	42,345	2,906	30,547	3,518	25,749
	$155,341	$ 71,764	$224,258	$ 60,131	$252,643	$ 55,391

*) Includes Europe, the Middle East (excluding Israel) and Africa.

b. Market sectors:

Total revenues from external customers divided on the basis of the Company's market sectors are as follows:

	Year ended December 31,		
	2002	2003	2004
Enterprise Interaction Solutions	$ 122,422	$ 171,381	$ 194,111
Public Safety and Security sector	32,919	52,877	58,532
	$ 155,341	$ 224,258	$ 252,643

c. Major customers' data as a percentage of total revenues:

Customer A	23.3%	20.0%	18.8%

NOTE 17:− SELECTED STATEMENTS OF OPERATIONS DATA

a. Research and development, net:

	Year ended December 31,		
	2002	2003	2004
Total costs	$ 23,363	$ 26,384	$ 27,512
Less − grants and participations	(1,632)	(1,260)	(1,341)
Less − capitalization of software development costs	(4,609)	(2,291)	(1,305)
	$ 17,122	$ 22,833	$ 24,866

b. Financial income (expenses), net:

	Year ended December 31,		
	2002	2003	2004
Financial income:			
Interest and amortization/accretion of premium/discount of marketable securities	$ 2,747	$ 1,821	$ 2,349
Interest	551	422	1,427
Foreign currency translation	1,152	405	1,078
	4,450	2,648	4,854
Financial expenses:			
Interest	(15)	(79)	(2)
Foreign currency translation	(95)	(204)	(894)
Other	(348)	(331)	(402)
	(458)	(614)	(1,298)
	$ 3,992	$ 2,034	$ 3,556

c. Restructuring expenses, in−process research and development write−off, settlement of litigation and other:

	Year ended December 31, 2002	2003	2004
Restructuring expenses (income) (Note 11)	$ (118)	$ 1,888	$ —
In−process research and development write−off (Note 1c)	1,270	—	—
Settlement of litigation (*)	—	5,194	
Other	(320)	—	—
	$ 832	$ 7,082	$ —

(*) In the fourth quarter of 2003, the Company reached a settlement agreement with one of its competitors to settle a patent infringement claim filed by the competitor in June 2000. Under the settlement agreement the Company paid to the competitor $ 10,000 (of which approximately $ 4,800 was covered by insurance).

d. Net earnings (loss) per share:

The following table sets forth the computation of basic and diluted net earnings (loss) per share:

1. Numerator:

	Year ended December 31, 2002	2003	2004
Numerator for basic and diluted net earnings (loss) per share −			
Net income (loss) from continuing operations	$ (35,352)	$ 5,608	$ 21,319
Net income from discontinued operation	1,370	1,483	3,236
Net income (loss) available to Ordinary shareholders	$ (33,982)	$ 7,091	$ 24,555

2. Denominator (in thousands):

Denominator for basic net earnings (loss) per share −			
Weighted average number of shares	13,795	16,038	17,497
Effect of dilutive securities:			
Add − Employee stock options	—	731	1,198
Add − ESPP	—	12	8
Denominator for diluted net earnings (loss) per share − adjusted weighted average shares	13,795	16,781	18,703

The effect of the inclusion of the options and warrants in 2002 would be anti−dilutive. Because of the loss in 2002, all potential dilutive securities are anti−dilutive.

NOTE 18:− SUBSEQUENT EVENT (UNAUDITED)

On April 11, 2005, the Company signed a definitive agreement to acquire the assets and assume certain liabilities of Dictaphone’s Communications Recording Systems (“CRS”) business for approximately $ 38,500. Dictaphone’s CRS business is a leading provider of liability and quality management systems for first responders, critical facilities, contact centers and financial trading floors. The closing took place on June 1, 2005.

SIGNATURES

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, 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, in the City of Ra'anana, State of Israel, on the 29th day of June, 2005.

NICE−SYSTEMS LTD.

By: /s/ Haim Shani
Haim Shani
Chief Executive Officer

THIS SETTLEMENT AGREEMENT is made on 24 February 2005

B E T W E E N:

(1) **THALES SA**, a French société anonyme having its registered office at 45 rue de Villiers, Neuilly sur Seine (92200) ("Thales"); and

(2) **NICE SYSTEMS LTD.** an Israeli company having its registered office at 8 Hapnina Street, Ra'anana, 43107 Israel ("Nice"); and

(3) **NICE CTI SYSTEMS UK LIMITED** (a company incorporated in England and Wales with registered number 03403044) whose registered office is at Tollbar House, Tollbar Way, Hedge End, Southampton, Hampshire SO30 2ZP; and

(4) **NICE SYSTEMS SARL**, a French société a responsabilité limitée having its registered office at 110/112 boulevard Jeans Jaures, 92100, Boulogne Billancourt, France; and

(5) **NICE SYSTEMS GMBH** (a German company) whose registered office is at Lyonerstrasse 44−48, Frankfurt 60528, Germany; and

(6) **NICE SYSTEMS INC.** (a company incorporated under the laws of the State of Delaware , USA), whose principal place of business is at 301 Route 17 North, Rutherford, New Jersey 07070; (together "the Subsidiaries").

WHEREAS:

A Thales, Nice and the Subsidiaries signed a Sale and Purchase Agreement on 30 July 2002 in connection with the acquisition by Nice of certain assets and liabilities of Thales Contact Solutions Limited, Thales Contact Solutions S.A. Thales Contact Solutions GmbH and Thales Contact Solutions Inc. (the "SPA").

B The SPA contained various price adjustment mechanisms and indemnities related to the assets sold to Nice.

C On 8 September 2004, Nice notified claims to Thales pursuant to Clause 15 (“Debts and Accounts Receivable”), Clause 16 (“Inventory”), and Clause 18 (“Instem Manufacturing Agreement”) of the SPA (the “Claims”).

D Nice, Thales and the Subsidiaries have agreed the following terms of settlement in respect of the price adjustment mechanisms under the SPA and, in particular, in respect of any and all claims which Nice and the Subsidiaries may have against Thales howsoever and whensoever arising out of Clauses 15, 16 and 18.

IT IS AGREED as follows:

1. In this Settlement Agreement, save where the context otherwise requires:

1.1. words and expressions defined in the SPA shall have the same meanings in this Settlement Agreement;

1.2. words in the singular shall include the plural, and vice versa;

1.3. except if provided differently in this Settlement Agreement a reference to a clause or sub−clause shall be a reference to a clause or sub−clause (as the case may be) of the Settlement Agreement;

1.4. the headings in this Settlement Agreement are for convenience only and shall not affect the interpretation of any provision of this Settlement Agreement;

1.5. references to a “Party” or the “Parties” are to a party or the parties to this Settlement Agreement;

1.6. references to the SPA shall include any amendment thereto entered into between the Parties.

2. SETTLEMENT

2.1. In consideration of:

2.1.1. the payment by Thales to Nice of the sum of USD 2,130,000 (two million one hundred thirty thousand United States dollars); and

2.1.2. the payment by Thales ATM, or failing that by Thales, to Nice of €89,399.40 (eighty nine thousand three hundred ninety nine point forty euros) in respect of an invoice numbered “90201” due by Thales ATM to Nice;

2.1.3. Thales’ agreement that Nice and the Subsidiaries may retain the benefit of the Accounts Receivable and the Inventory and need not account to it by way of reassignment of Accounts Receivable or the return of Unsold Inventory as otherwise required by Clauses 15 and 16 of the SPA respectively or at all,

Nice and the Subsidiaries agree that:

2.1.4. such payments are in full and final settlement of the Claims and (except as provided at clause 2.2) hereby release Thales and its subsidiaries from all and any actual or potential claims or complaints of whatsoever nature, howsoever and whensoever arising, whether known or unknown, that any of them and/or any parent, subsidiary, associated or group company of any of them (and/or their respective employees and/or officers and/or former employees and/or former officers) has or may have against Thales or any of its subsidiaries which have arisen or may arise out of, or which are connected with the price adjustment mechanisms under the SPA and, in particular, in respect of any and all claims which Nice may have against Thales and/or any of its subsidiaries howsoever and whensoever arising out of Clauses 15, 16 and 18 of the SPA; and

2.1.5. such payments are in full and final settlement of all Accounts Receivable and other amounts owed by Thales and its subsidiaries in respect of goods and/or services supplied to any of them by the TCS Group as at or prior to the Completion Date and hereby release Thales and its subsidiaries from all and any actual or potential claims or complaints of whatsoever nature, howsoever and whensoever arising, whether known or unknown, that any of them may have against Thales and/or any of its subsidiaries howsoever and whensoever arising in respect of such supplies, save in respect of the payment required under clause 2.1.2 above.

2.2. Nothing in this Settlement Agreement shall operate to settle, waive, compromise or in anyway prejudice any right of Nice and/or the Subsidiaries with respect to any existing and/or potential claim or claims arising pursuant to the SPA which are not connected with the price adjustment mechanisms and/or Clauses 15, 16 and 18 of the SPA, including, without limitation, claims pursuant to Clauses 3 (Business Properties), 6 (Liabilities to be Assumed), 11 (Indemnities), 14 (Employment), 17 (Warranty Work and Additional Services), 20 (Insurance Claims), 22 (Warranties and Limitation of Liability) and 25 (Pensions), howsoever and whensoever arising.

2.3. This Settlement Agreement may be signed in counterpart copies and Nice agrees to fax a copy of this Settlement Agreement, executed respectively by an officer with the necessary authority to Thales (*fax number: +33 1 57 77 84 77 for the attention of: Olivier MAS*) by 10am London time on February 2005. Thales agrees to fax a copy of this Agreement, executed by an officer with the necessary authority, to Nice (*fax number:+44 8707 22 4042, for the attention of: John MALINS*) by 10am London time on February 2005.

2.4. After Thales and Nice have confirmed receipt of the faxes mentioned above by telephone (*Thales to telephone John MALINS at Nice on +44 8707 22 4042*),

2.4.1. Thales shall pay to Nice the sum at clause 2.1.1 above within five business days of the signature of this Settlement Agreement, and

2.4.2. Thales ATM, or failing that Thales, shall pay to Nice the sum at clause 2.1.2 above, within sixty calendar days of the signature of this Settlement Agreement.

2.5. Nice agrees to forward the original of the Agreement faxed to Thales, to Thales (*for the attention of: Olivier MAS, Thales SA, 45 rue de Villiers – 92200 Neuilly sur Seine*). Thales agrees to forward the original signed Agreement faxed to Nice, to Nice (*for the attention of: Stephen DUNNE, NICE CTI Systems UK Limited, Tollbar House, Tollbar Way, Hedge End, Southampton, Hampshire SO30 2ZP*).

2.6. Thales shall make the payment at clause 2.1.1 to:

Nice Systems Limited

CITIBANK (TEL AVIV)

SWIFT CODE: _CITIILIT

Account Number: 500079029 (through ac. No. 36154271 of Citibank Tel Aviv with Citibank New York (citius33).

2.7. Thales ATM or alternatively Thales shall make the payment at clause 2.1.2 to:

Nice Systems SARL

CITIBANK

SWIFT CODE: CTIFRPP IBAN:FR76 1168 9007 0000 6550 6300 522

Account Number: 655063005−22.

2.8. If payment of any sum due to be paid under this Settlement Agreement is not made by Thales or, as the case may be, Thales ATM, on or before the due date for payment then interest shall accrue on the amount outstanding for the period from the due date to the date of actual payment at the rate of 3% above the base rate of Barclays Bank plc computed on a daily basis until and including the date of payment.

3. CONFIDENTIALITY

3.1. The terms of this Settlement Agreement and all facts and matters relating to its subject−matter (including the nature and details of the claims and events leading up to them, all pleadings, documents, evidence submitted and the negotiations which have led up to this Settlement Agreement) are confidential and the Parties whether by their directors or officers, servants, agents or otherwise, agree to keep the terms of this

Settlement Agreement and all facts and matters relating to its subject−matter (including the nature and details of the claims and events leading up to them, all documents, evidence submitted and the negotiations which have led up to this Settlement Agreement) confidential and agree not to disclose the contents of the Settlement Agreement (or related facts and matters) to any third party other than their professional legal advisers and accountants, save to the extent that such disclosure is required by law or regulation to which a Party is subject or for the purposes of enforcing this Settlement Agreement or is permitted by a prior written agreement of the Parties to this Settlement Agreement such agreement not to be unreasonably withheld.

3.2. For the avoidance of doubt, nothing in this Settlement Agreement shall prevent any Party or any parent, subsidiary, associated or group company of any Party disclosing these terms of settlement in connection with any disposal of a Party and/or any parent, subsidiary, associated or group company of any Party providing that any third party to whom disclosure is made has previously agreed in writing to treat such disclosure as confidential as set out at paragraph 3.1 above.

4. MISCELLANEOUS

4.1 This Settlement Agreement shall be binding on and enure for the benefit of the successors and permitted assigns of the Parties.

4.2 The benefit of this Settlement Agreement may not be assigned by any Party without the prior written consent of the others.

4.3 This Settlement Agreement constitutes the entire agreement between the Parties in relation to the subject matter of this Settlement Agreement. Each Party acknowledges and confirms that in entering into this Settlement Agreement it is not relying upon any statement or representation made by or on behalf of any of the other Parties, whether or not in writing, at any time prior to the execution of this Settlement Agreement, which is not expressly set out herein. Each of the Parties expressly agrees that it will not have any right of action in relation to any statement or representation, whether oral or written, made by or on behalf of any other Party in the course of any negotiations which preceded the execution hereof, unless such statements or representations were made fraudulently. This Settlement Agreement may be varied or modified only by the written agreement of the Parties.

5. SEVERABILITY

If any provision of this Settlement Agreement shall be held to be illegal or unenforceable, whether in whole or in part in relation to any of the Parties to the Settlement Agreement, the validity and enforceability of the remainder of the Settlement Agreement, or its validity or enforceability as against other parties, shall not be affected.

6. COSTS

Each Party will bear its own legal costs arising to date, including any costs arising out of the negotiation and execution of this Settlement Agreement.

7. NOTICES

7.1 A notice, approval, consent or other communication in connection with this Settlement Agreement must:

7.1.1 be in writing;

7.1.2 in the case of Thales be marked for the attention of Mr Olivier MAS and left at the following address:

THALES S.A. 45 rue de Villiers 92200 Neuilly sur Seine ;

7.1.3 in the case of Nice and/or the Subsidiaries be marked for the attention of Mr Stephen DUNNE, and left at the following address:

NICE CTI Systems UK Limited, Tollbar House, Tollbar Way, Hedge End, Southampton, Hampshire SO30 2ZP.

7.2. A notice, approval, consent or other communication shall take effect from the time it is received (or, if earlier, the time it is deemed to be received in accordance with sub−clause 7.3) unless a later time is specified in it.

7.3. A letter is deemed to be received, unless actually received earlier, on the seventh day after posting.

8. GOVERNING LAW, JURISDICTION AND SERVICE OF PROCESS

8.1 This Settlement Agreement shall be governed by and construed in accordance with English law.

8.2. In relation to any disputes arising out of or in connection with this Settlement Agreement, the Parties shall first use all reasonable endeavours to resolve amicably such matters between them. Failing such resolution, such disputes shall be finally settled in the courts of England.

8.3. Each Party agrees that, without preventing any other mode of service, any document in an action may be served on any Party by being delivered to or left for that Party at the address as provided in the paragraph headed “Notices” above.

IN WITNESS of which the Parties have executed this Settlement Agreement on the date first mentioned above

SIGNED on behalf of
THALES−SA

In the presence of:

SIGNED on behalf of
NICE SYSTEMS LTD

In the presence of:

SIGNED on behalf of
NICE CTI SYSTEMS UK LIMITED

In the presence of:

SIGNED on behalf of
NICE SYSTEMS SARL,

In the presence of:

SIGNED on behalf of
NICE SYSTEMS GMBH

In the presence of:

SIGNED on behalf of
NICE SYSTEMS INC.

In the presence of:

Exhibit 4.8

EXECUTION VERSION

ASSET PURCHASE AND SALE AGREEMENT

dated as of April 11, 2005

between

DICTAPHONE CORPORATION

and

NICE SYSTEMS INC.

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ASSET PURCHASE AND SALE AGREEMENT

ASSET PURCHASE AND SALE AGREEMENT, dated April 11, 2005, between Dictaphone Corporation, a Delaware corporation ("Dictaphone"), and Nice Systems Inc., a Delaware corporation (the "Buyer").

RECITALS

A. The Buyer desires to purchase the Purchased Assets, and assume the Assumed Liabilities, from Dictaphone, on the following terms and conditions; and

B. Dictaphone desires to sell the Purchased Assets, and assign the Assumed Liabilities, to the Buyer, on the following terms and conditions.

NOW, THEREFORE, in consideration of the foregoing recitals and the mutual covenants, representations, warranties, conditions and agreements hereinafter expressed, the Parties agree as follows:

ARTICLE 1
DEFINITIONS

The following words shall have the meaning given them in this Article 1:

1.1 "AAA" has the meaning set forth in Section 11.9(c).

1.2 "AAA Rules" has the meaning set forth in Section 11.9(c).

1.3 "Accounts Payable" means those accounts payable of the Business recorded or required to be recorded as such on financial statements of the Business prepared in accordance with U.S. GAAP, and "accounts payable" means all accounts of the Business representing obligations to pay for goods or services received and other liabilities of the type customarily included as payables of a business that arose or arise in the Ordinary Course.

1.4 "Accounts Receivable" means those accounts receivable of the Business recorded or required to be recorded as such on financial statements of the Business prepared in accordance with U.S. GAAP, and "accounts receivable" means all accounts of the Business representing moneys due for goods sold or services rendered, as evidenced by notes, statements, invoices or other written evidence of a present obligation.

1.5 "Accrued Expenses" means those accrued expenses of the Business recorded or required to be recorded as such on financial statements of the Business prepared in accordance with U.S. GAAP, and "accrued expenses" means all liabilities of the Business of the type customarily included as accrued expenses of a business that arose or arise in the Ordinary Course. The types and categories of accrued expenses are listed on Annex 1.5.

1.6 "Affiliate" means, with respect to any Person, any other Person which is controlling, controlled by, or under common control with, directly or indirectly through any Person, the Person referred to, and, if the Person referred to is a natural person, any member of such Person's immediate family. The term "control" (including, with correlative meaning, the terms “controlled by” and “under common control with”), as used with respect to any Person, means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of such Person, whether through the ownership of voting securities, by contract or otherwise.

1.7 “Agreement” means this Asset Purchase and Sale Agreement as executed on the date hereof and as amended or supplemented in accordance with the terms hereof, including the Disclosure Schedule and all other Schedules, Annexes and Exhibits hereto.

1.8 “Assigned Contracts” has the meaning set forth in Section 2.1(d).

1.9 “Assumed Liabilities” has the meaning set forth in Section 2.3.

1.10 “Audited Financial Statements” means the audited balance sheet of the Business as of December 31, 2004, and the related audited statement of operations and statement of cash flows for the year then ended, prepared on a “carved−out” basis in accordance with U.S. GAAP and as otherwise set forth in Section 3.4(b).

1.11 “Auditor” has the meaning in Section 2.5(b)(iv).

1.12 “Auditor’s Consent” has the meaning in Section 6.7(a).

1.13 “Auditor’s Report” has the meaning in Section 3.4(b).

1.14 “Balance Sheet Escrowed Funds” has the meaning in Section 2.5(b)(iii).

1.15 “Benefit Plan” means any employee benefit plan (as defined in Section 3(3) of ERISA) and any other employee benefit plan, program or arrangement.

1.16 “Business” means all global commercial activities relating to the current or the currently planned, design, development, sale, production, marketing and servicing of hardware and software for call logging systems and related replay and surveillance systems and application software, for: (i) call centers and contact centers, with related software applications for quality monitoring, workforce optimization, business performance management and voice content analytics; (ii) command, control, communications and dispatch operations of public safety, first responders, transportation, air−traffic control organizations and other government agencies, with related software applications for dispatch, resource allocation, scenario reconstruction and evidence gathering; and (iii) financial institutions, with related software applications for risk management and compliance, including anti−fraud, anti−money laundering and securities regulation, including Sarbanes−Oxley regulations; as such business has been conducted as of the Closing Date by Dictaphone’s Communications Recording Systems division, including through its channel partners and Dictaphone Affiliates; provided, however, that Business shall not include the business or operations of the Healthcare Solutions Group, Integrated Voice Systems or EMS divisions of Dictaphone.

1.17 “Business Day” means any day which is not a Saturday, Sunday or a legal holiday in the State of Connecticut, United States of America.

1.18 "Business Use" has the meaning set forth in Section 6.11(a).

1.19 "Business Intellectual Property" has the meaning set forth in Section 2.1(c).

1.20 "Buyer" has the meaning set forth in the title of this Agreement.

1.21 "Buyer Maximum Indemnity Amount" has the meaning set forth in Section 9.6.

1.22 "Buyer Affiliates" means (i) NICE CTI Systems UK Limited, organized under the law of the United Kingdom, (ii) NICE Systems sarl, organized under the laws of France, and (iii) NICE Systems GmbH, organized under the laws of Germany, each of which is an Affiliate of Buyer under common control with Buyer.

1.23 "Buyer's FSA" has the meaning set forth in Section 5.2(e).

1.24 "Closing" means the consummation of the transactions contemplated by this Agreement, as provided for in Section 2.6.

1.25 "Closing Date" means the date on which the Closing occurs, which shall be within five (5) Business Days from the satisfaction or waiver of all applicable conditions to Closing set out herein, or such other date as shall be mutually agreed upon by the Parties, after allowing for reasonable time periods for performing certain pre−Closing activities, including the physical inventory count contemplated by Section 2.5(b)(i), the preparation and review of the Estimated Closing Date Balance Sheet and the release of the Encumbrances described in Section 1.83(e).

1.26 "Closing Date Balance Sheet" means the audited balance sheet of the Business as of the Closing Date reflecting the Purchased Assets acquired and the Assumed Liabilities assumed pursuant to this Agreement, as more specifically set forth in Section 2.5(b).

1.27 "Code" means the United States Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

1.28 "Competitive Activities" has the meaning set forth in Section 6.5(a).

1.29 "Contract" means any contract, lease, indenture, mortgage, license, deed of trust, evidence of indebtedness, binding commitment or instrument to which Dictaphone or a Selling Subsidiary (in each case in respect of the Business) is a party or by which it is bound.

1.30 "December 31 Balance Sheet" means the balance sheet of the Business as of December 31, 2004 included in the Audited Financial Statements.

1.31 "Dictaphone" has the meaning set forth in the title of this Agreement.

1.32 "Dictaphone's FSA" has the meaning set forth in Section 5.2(e).

1.33 "Dictaphone Maximum Indemnity Amount" has the meaning set forth in Section 9.6(b).

1.34 "Disclosure Schedule" means the schedule, dated the date hereof and as it may be amended or supplemented from time to time on or prior to Closing, of exceptions to the representation and warranties made, and the listings of information provided, by Dictaphone or the Buyer hereunder.

1.35 "Dictaphone Successor" means any Person who is an investor in, a successor to, or assignee of, Dictaphone or any acquirer of, successor to or assignee of a majority of the businesses or assets of Dictaphone or its Affiliates, in each case, pursuant to an asset acquisition, stock acquisition, merger, stock exchange, consolidation or other business combination, and any Affiliate of such Person (other than Dictaphone or its Affiliates at the time of such investment, succession or assignment).

1.36 "Dispute" has the meaning set forth in Section 11.9(a).

1.37 "Effective Time" means the effective time of the Closing, which shall be deemed to be 11:59 p.m. eastern time on the Closing Date.

1.38 "Employees" means individuals who immediately prior to the Effective Time are employees of Dictaphone or its subsidiaries and who primarily perform services in the Business; "EU Employees" means those Employees based in the European Union and whose contracts of employment are subject to the laws of a member state of the European Union and listed on Annex 1.38(i); "Swiss Employees" means those Employees based in the European Union and whose contracts of employment are subject to the laws of Switzerland and listed on Annex 1.38(ii); "Canadian Employees" means those Employees based in Canada and whose contracts of employment are subject to the laws of Canada and listed on Annex 1.38(iii); "Singapore Employees" means those Employees based in Singapore and whose contracts of employment are subject to the laws of Singapore and listed on Annex 1.38(iv); and "U.S. Employees" means all Employees other than the EU Employees, Swiss Employees, Canadian Employees and Singapore Employees.

1.39 "EMS" means all commercial business, operations or activities anywhere in the world relating to the design, development, sale, manufacture, assembly, marketing, servicing or support of electrical or electronic equipment, including printed circuit board assembly, cable assembly, metal fabrication, machining or finishing, final system builds, or design support, but excluding the present or currently planned design, development, sale, production, marketing, service or support of products or services of the Business (determined without regard to the proviso at the end of Section 1.16).

1.40 "Encumbrances" means mortgages, liens, charges, claims, security interests, easements or other encumbrances.

1.41 "Environmental Law" means any Law relating to pollution or protection of the environment.

1.42 "Environmental Permit" means any permit, approval, consent or other authorization pursuant to any Environmental Law.

1.43 "ERISA" means the Employee Retirement Income Security Act of 1974, as amended.

1.44 "Escrow Agent" means the escrow agent named in the Escrow Agreement.

1.45 "Escrow Agreement" means an agreement, in the form attached hereto as Exhibit E, by and among the Buyer, Dictaphone and the escrow agent named therein.

1.46 "Estimated Closing Date Balance Sheet" means the unaudited balance sheet of the Business as of the Closing Date reflecting the Purchased Assets to be acquired and the Assumed Liabilities to be assumed pursuant to this Agreement, as more specifically set forth in Section 2.5(b).

1.47 "Excluded Assets" has the meaning set forth in Section 2.2.

1.48 "GAAP" means generally accepted accounting principles in the applicable specified jurisdiction (and when not specified, in the United States) as in effect from time to time, and "U.S. GAAP" means generally accepted accounting principles in the United States as in effect from time to time, in each case together with the procedures, practices and methodologies of the relevant Party used in connection therewith, consistently applied. For this purpose, "as in effect from time to time" when used in reference to GAAP or U.S. GAAP as applied (i) to the Audited Financial Statements, shall mean as of the date or for the period covered by the Audited Financial Statements, (ii) to the Closing Date Balance Sheet, shall mean as of the Closing Date, and (iii) to all other references in this Agreement, shall mean as of the date or for the period covered by the financial statement, representation, warranty, covenant or information in respect of which the term GAAP or U.S. GAAP is used.

1.49 "Healthcare Solutions Group" means all commercial business, operations or activities, other than in the call logging market and related replay and surveillance system market, in the healthcare market, anywhere in the world, relating to the design, development, sale, production, marketing or servicing of handheld, PC, networked or enterprise wide digital recording, dictation or transcription systems, dictation workflow management systems, document or records management systems (including archiving, transmitting, receiving, indexing, analyzing or processing of documents or records), voice or data file management systems, natural language processing solutions or speech recognition solutions, including speaker verification, voice recognition, voice−activated command or control or related technologies.

1.50 "Houlihan" has the meaning set forth in Section 3.27.

1.51 "Indemnification Escrowed Funds" has the meaning set forth in Section 2.5(a).

1.52 "Indemnifying Party" has the meaning set forth in Section 9.3.

1.53 "Indemnity Threshold" has the meaning set forth in Section 9.6(a).

1.54 "Injured Party" has the meaning set forth in Section 9.3.

1.55 "Integrated Voice Systems" means all commercial business, operations or activities, other than in the call logging market and related replay and surveillance system market, anywhere in the world relating to the design, development, sale, production, marketing or servicing of handheld, PC, networked or enterprise wide systems for archiving, consolidating, transmitting, receiving or indexing audio files, images, photographs, video or data, or dictation/transcription systems, dictation workflow management systems, document or records management systems (including archiving, transmitting, receiving, indexing, analyzing, digesting or processing of documents or records), voice or data file management systems, natural language processing solutions or speech recognition solutions, speaker verification, voice recognition, voice−activated command or control or related technologies.

1.56 "Intellectual Property" means patents, patent rights, inventions, designs, proprietary processes and formulae, models, know how, trade secrets, trademarks, trade dress, service marks, copyrights, business names, domain names, trade names, service names, logos, designs and registrations, applications, renewals and rights to apply for any of the foregoing, and documentation and media embodying any of the foregoing (including manuals, memoranda and records), and goodwill associated with any of the foregoing, and rights to sue or take any other action with respect to any infringement, misappropriation, dilution or other violation of any rights with respect to any of the foregoing.

1.57 "Interim 2005 Financial Statements" has the meaning set forth in Section 6.7(c).

1.58 "IRS" means the U.S. Internal Revenue Service.

1.59 "Inventory" has the meaning set forth in Section 2.1(b).

1.60 "IP Policy" has the meaning set forth in Section 3.18(k).

1.61 "Key Employees" has the meaning set forth in Section 5.1(d).

1.62 "knowledge" means a Person's actual knowledge (i.e., the conscious awareness of facts or other information), after undertaking a customary and reasonable investigation under the circumstances, including undertaking a reasonable inquiry of those Persons who report directly to them. The words "know," "knowing" and "known" shall be construed accordingly. In the case of Dictaphone, "knowledge" means the actual knowledge of the Persons listed on Annex 1.62(i) (other than those Persons listed on Annex 1.62(i) solely for the purpose of identifying such Persons as Persons who report directly to other Persons listed on Annex 1.62(i)), after undertaking a customary and reasonable investigation under the circumstances, including undertaking a reasonable inquiry of those Persons who report directly to them (other than those Persons specifically listed on Annex 1.62(i) as excluded from the requirement of making such inquiry). In the case of the Buyer, "knowledge" means the actual knowledge of the Persons listed on Annex 1.62(ii), after undertaking a customary and reasonable investigation under the circumstances, including undertaking a reasonable inquiry of those Persons who report directly to them.

1.63 "Law" means a statute, law, ordinance, decree, order, injunction, rule, directive or regulation of any U.S. or non−U.S. government or governmental authority, and includes rules and regulations of any regulatory or self−regulatory authority compliance with which is required by any of the foregoing.

1.64 "Liabilities" means claims, liabilities, obligations, losses, costs, expenses (including reasonable legal, accounting and other expenses), Proceedings, fines, Taxes, deficiencies, assessments, charges, penalties, allegations, demands, damages (including actual, punitive or consequential, foreseen or unforeseen, known or unknown damages), settlements or judgments of any kind or nature whatsoever.

1.65 "Loss" means a Liability, to the extent actually paid or incurred, but net of any proceeds, indemnities or recoveries from insurers or other third parties received by the Injured Party with respect to such Liability.

1.66 "Major Customers" has the meaning set forth in Section 3.24(a).

1.67 "Manufacturing Agreement" means an agreement, in the form attached hereto as Exhibit A, between an Affiliate of the Buyer and Dictaphone relating to the provision of equipment and related items to the Buyer by Dictaphone's EMS division.

1.68 "Material Adverse Effect" means a material adverse effect on the assets, liabilities, business, condition (financial or otherwise) or results of operations or prospects of the Business taken as a whole, but shall not be deemed to include (i) any changes resulting from general economic, regulatory or political conditions, (ii) acts attributable to, omissions by or circumstance affecting the Buyer or any of its Affiliates, (iii) changes in foreign currency exchange rates, (iv) circumstances that affect the industries in which the Business operates generally or (v) any changes resulting from the announcement or pendency of the transactions provided for in this Agreement.

1.69 "Material Contract" has the meaning set forth in Section 3.13(a).

1.70 "Net Adjusted Working Capital Level" means the excess, if any, of (x) the Purchased Assets that are current assets (determined and calculated in accordance with U.S. GAAP), over (y) the sum of (i) total Assumed Liabilities that are current liabilities (determined and calculated in accordance with U.S. GAAP) and (ii) long−term deferred revenues (determined and calculated in accordance with U.S. GAAP).

1.71 "Nice Settlement Agreement" means that certain Settlement Agreement entered into on or about December 11, 2003 by and among Dictaphone, Nice Systems Ltd. and Nice Systems Inc.

1.72 "Non−Compete Period" has the meaning set forth in Section 6.5(a).

1.73 "Notice of Claim" has the meaning set forth in Section 9.3.

1.74 "Omitted IP" has the meaning set forth in Section 6.11(a).

1.75 "Omitted IP License" has the meaning set forth in Section 6.11(a).

1.76 "Ordinary Course" means the ordinary course of commercial operations customarily engaged in by the Business.

1.77 "OSS Agreement" means the Professional Services Agreement, dated as of April 2, 2001, by and between Dictaphone and Omnee Systems and Software Corporation.

1.78 "Other Assets" has the meaning set forth in Section 2.1(k).

1.79 "Other Dictaphone Businesses" means all businesses, operations and activities of Dictaphone and its Affiliates other than the Business, including those businesses of Dictaphone described in the proviso to the definition of "Business".

1.80 "Other Financial Information" has the meaning set forth in Section 3.4(a).

1.81 "Party" means Dictaphone or the Buyer.

1.82 "Permitted Encumbrances" means, collectively, (a) Encumbrances that are disclosed in the Disclosure Schedule, (b) Encumbrances to secure Taxes which are not yet delinquent, (c) Encumbrances in favor of mechanics, material men, laborers, employees and suppliers and similar Encumbrances arising by operation of law, (d) Assumed Liabilities and (e) Encumbrances which shall be released on or prior to the Closing Date.

1.83 "Person" means an individual, a partnership, a corporation, a limited liability company, an association, a joint stock company, a trust, a joint venture, an unincorporated organization, a government or governmental authority (which term includes any department, agency or political subdivision thereof) or other entity.

1.84 "Prepaid Expenses" means those prepaid expenses of the Business recorded or required to be recorded as such on financial statements of the Business prepared in accordance with U.S. GAAP, and "prepaid expenses" means deposits and other prepayments of expenses of the Business and all rights in respect thereof.

1.85 "Proceeding" means any suit, action, proceeding or arbitration or any investigation by a government or governmental authority.

1.86 "Product Backlog" means written orders in the form of a purchase order or contract for products of the Business that have been placed and for which revenues have not yet been recognized, less any cancellations of such orders.

1.87 "Purchase Price" has the meaning set forth in Section 2.5(a).

1.88 "Purchased Assets" has the meaning set forth in Section 2.1.

1.89 "Records" has the meaning set forth in Section 6.2.

1.90 "Related Agreements" means (i) the Manufacturing Agreement, (ii) the Technology License Agreement, (iii) the Trademark License Agreement, (iv) the Transition Services Agreement/Shared Services Agreements, (v) the Escrow Agreement and (vi) the Subsidiary Asset Purchase Agreements.

1.91 "Retained Employees" means all of the Employees who are listed on Annex 1.91 or who are not Transferred U.S. Employees or Transferred Foreign Employees.

1.92 "Retained Liabilities" has the meaning set forth in the first sentence of Section 2.4.

1.93 "Section 6.12 Schedule" has the meaning set forth in Section 6.12.

1.94 "Sellers" means, collectively, Dictaphone and the Selling Subsidiaries.

1.95 "Selling Subsidiaries" means (i) Dictaphone Canada (1995) Inc., a Canadian corporation, (ii) Dictaphone Company Limited, a U.K. company, (iii) Dictaphone Deutschland GmbH, a German company, (iv) Dictaphone Europe AG, a Swiss company, and (v) Dictaphone International Limited, a U.K. company.

1.96 "Singapore Employees" has the meaning set forth in Section 1.38.

1.97 "Straddle Period" means any taxable period that begins prior to and ends after the Effective Time.

1.98 "Subsidiary Asset Purchase Agreements" has the meaning set forth in Section 2.11.

1.99 "Swiss Employees" has the meaning set forth in Section 1.38.

1.100 "Tangible Business Assets" has the meaning set forth in Section 2.1(a).

1.101 "Taxes" means taxes, charges, duties, imposts, fees, levies and other assessments of any kind by any government or governmental authority, including federal, provincial, possession, state, city, county and foreign income, profits, franchise, gross receipts, sales, use, transfer, stamp, occupation, property, capital, windfall profits, customs, ad valorem, value−added and excise taxes, and penalties, additions to tax and interest relating to any of the foregoing.

1.102 "Technology License Agreement" means an agreement, in the form attached hereto as Exhibit B, between the Buyer and Dictaphone pursuant to which the Buyer will license to Dictaphone, subject to Section 6.5, certain Business Intellectual Property.

1.103 "Termination Agreement" means the Settlement Termination and Litigation Transfer Agreement related to the Nice Settlement Agreement in the form of Exhibit H.

1.104 "Third−Party Claim" has the meaning set forth in Section 9.4.

1.105 "Third Party Intellectual Property" means any Intellectual Property to which Dictaphone does not exclusively own the entire right, title and interest.

1.106 "Trademark License Agreement" means an agreement, in the form attached hereto as Exhibit C, between the Buyer and Dictaphone regarding the license by Dictaphone of its trademark "Dictaphone" to the Buyer.

1.107 "Transferred Employees" means all Transferred U.S. Employees and Transferred Non−U.S. Employees.

1.108 "Transferred Non−U.S. Employees" means those EU Employees, Swiss Employees and Canadian Employees whose employment is transferred to, or who accept employment as of the Effective Time by, the Buyer or any of its Affiliates as of the Effective Time under Section 5.6.

1.109 "Transferred U.S. Employees" means those U.S. Employees who accept employment as of the Effective Time with the Buyer or any of its Affiliates under Section 5.1(c).

1.110 "Transition Services/Shared Services Agreements" means the agreements, in the form attached hereto as Exhibit D, between an Affiliate of the Buyer and Dictaphone regarding services to be provided (i) by Dictaphone to the Buyer (or to third parties to which the Buyer may outsource certain assigned maintenance and service contracts), (ii) by Dictaphone for the benefit of customers of the Buyer, as a subcontractor to the Buyer, or (iii) by the Buyer to customers of Dictaphone, as a subcontractor to Dictaphone, or to be shared by the Buyer and Dictaphone.

Whenever required by the context hereof, all terms and pronouns, and any variations thereof, will be deemed to refer to the masculine, feminine or neuter and the singular or plural. When used in this Agreement, the term "including" means "including but not limited to" and the words "asset" and "property" are synonymous.

ARTICLE 2
PURCHASE AND SALE OF THE BUSINESS

2.1 Transfer of Assets. Upon the terms and subject to the conditions of this Agreement and the Related Agreements, at the Closing and as of the Effective Time, Dictaphone shall, and shall cause its Selling Subsidiaries to, sell, assign, transfer and convey to the Buyer or to a Buyer Affiliate, and the Buyer shall, and shall cause the Buyer Affiliates to, purchase, acquire and accept from Dictaphone and the Selling Subsidiaries, all of Sellers' right, title and interest to and in the following assets, properties and rights used or held for use primarily in the Business, whether now in use or currently under development, including such changes therein, additions thereto and deletions therefrom as may occur from the date hereof through the Closing in the Ordinary Course or as otherwise permitted or required pursuant to the terms hereof (the "Purchased Assets"), free and clear of all Encumbrances other than Permitted Encumbrances:

(a) all equipment, machinery, supplies, vehicles, tools, personal computers, workstations, network infrastructure, laboratory equipment, testing equipment and apparatus, mock−ups, demonstration equipment, personal property and other tangible personal property used or held for use primarily in the Business including that listed on Annex 2.1(a), and including any specialized or otherwise non−generic equipment, machinery, tooling and testing equipment used by EMS for the design, development, manufacture, assembly, servicing or support of products of the Business (collectively, the "Tangible Business Assets");

(b) all inventory, including spare parts and finished goods, but not including raw materials and works−in−progress, whether stored at a Business location or stored at a third−party location or other Dictaphone location, used or held for use primarily in the Business, including that listed on Annex 2.1(b) (collectively, the "Inventory") and, for the avoidance of doubt, Inventory shall not include any inventory held by EMS;

(c) all Intellectual Property used or held for use, or currently under development for use, primarily in the Business, including that listed on Annex 2.1(c), and including any designs, proprietary processes and formulae, models, and know how used by EMS for the design, development, manufacture, assembly, servicing or support of products of the Business (collectively, the "Business Intellectual Property");

(d) all Contracts relating primarily to the Business or the other Purchased Assets (collectively, the "Assigned Contracts"), including those listed on Annex 2.1(d), which shall be divided into the following categories on such Annex 2.1(d):

(i) Maintenance Contracts (Annex 2.1(d)(i));

(ii) Product Purchase Contracts (Annex 2.1(d)(ii));

(iii) Dealer, Distributor or Reseller Agreements (Annex 2.1(d)(iii));

(iv) Software OEM Agreements (Annex 2.1(d)(iv));

(v) License Agreements (Annex 2.1(d)(v));

(vi) Professional Development Services Agreements (Annex 2.1(d)(vi));

(vii) Service Provider and Vendor Agreements (Annex 2.1(d)(vii)); and

(viii) Other Assigned Contracts (Annex 2.1(d)(viii));

(e) all Accounts Receivable (excluding Accounts Receivable from the Other Dictaphone Businesses) arising from products or services sold or leased by the Business;

(f) all (i) customer and vendor lists relating primarily to the Business, including all files and documents (including credit information) relating primarily to (1) current or proposed customers and customers who were customers at any time after January 1, 2002 (including business proposals to current and proposed customers and all other documents such as business cards and documents reflecting customer or sales "leads") of the Business and (2) vendors of the Business, and (ii) other business and financial records, data, files, books and documents (whether in hard copy, computer format or any other storage media) and any other Records relating primarily to the Business, in each case subject to the right of Dictaphone (y) to keep and use for itself and transfer to any of its Affiliates or any third party any of the foregoing which does not relate primarily to the Business and (z) to keep and use for itself and transfer to any Affiliates controlled by, or successors to, Dictaphone copies of any of the Purchased Assets described in this Section 2.1(f), subject to Section 6.5;

(g) all advertising, marketing, sales, creative and promotional materials relating primarily to the Business, in each case subject to the right of Dictaphone (i) to keep and use for itself and transfer to any of its Affiliates or any third party any of the foregoing which does not relate primarily to the Business and (ii) to keep and use for itself and transfer to any of its successors for their use, in each case, in accordance with Sections 6.2, 6.4 and 9.3, copies of any of the foregoing which relate primarily to the Business, subject to Section 6.5;

(h) subject to Section 2.2(e), all rights and claims to deposits and prepayments that would be recorded as Prepaid Expenses on financial statements prepared by Dictaphone in accordance with U.S. GAAP which were paid to third−parties and that relate primarily to the Purchased Assets or the Business;

(i) all warranties from third parties and, except as set forth on Annex 2.1(i) and not set forth on the December 31 Balance Sheet or as set forth in Section 2.2(b), refunds from and rights of set off against third−parties, in each case that relate primarily to the Purchased Assets or the Business;

(j) except as provided in Section 2.2(j), all rights to receive any damage award or other economic benefit with respect to infringement, misappropriation, dilution or other violation of any rights related to the Business Intellectual Property arising prior to the Effective Time, including all rights to litigation claims brought pursuant to the Nice Settlement Agreement; and

(k) the assets, rights, properties and interests listed in Annex 2.1(k) (the "Other Assets").

2.2 Excluded Assets. Notwithstanding any provision in this Agreement to the contrary, only those assets, rights, interests and properties which are expressly identified as Purchased Assets in Section 2.1 are to be sold, assigned, transferred or conveyed to the Buyer or the Buyer Affiliates hereunder and all other assets, rights, interests and properties of Sellers are specifically excluded from the transactions contemplated by this Agreement, including the following (collectively, the "Excluded Assets"):

(a) all cash on hand, cash on deposit and cash equivalents, including bank deposits, investments in "money market" funds and commercial paper funds, certificates of deposit, Treasury Bills and other marketable securities and all accrued interest thereon;

(b) all refunds, and all rights or claims to refunds, of any Taxes with respect to the Purchased Assets or the Business relating to any date or period prior to or through the Effective Time and all interest thereon (regardless of whether any such refund or interest is received prior to or after the Effective Time), including all refunds of Taxes and interest thereon received by, or credited against Tax liability of, the Buyer or any Affiliate of the Buyer attributable to Taxes paid by Dictaphone or an Affiliate thereof for periods or portions thereof ending on or prior to the Effective Time;

(c) all real property owned by or leased to Dictaphone, including related buildings and fixtures;

(d) all intracompany and intercompany receivables of the Business;

(e) (i) all current and prior insurance policies, (ii) all reimbursements for, or other benefits associated with, prepaid insurance and (iii) all rights and claims to deposits and prepayments that would be recorded as Prepaid Expenses on financial statements prepared by Dictaphone in accordance with U.S. GAAP for which the Buyer will not receive the benefit after the Effective Time and (iv) insurance proceeds with respect to events occurring prior to the Effective Time;

(f) all assets of any Benefit Plan of Dictaphone;

(g) all ownership rights of Dictaphone in respect of Intellectual Property to be licensed to Buyer pursuant to the Trademark License Agreement;

(h) subject to Section 2.1(j), all rights, claims or causes of action that Dictaphone may have against any Person arising from or related to the ownership or use of the Purchased Assets or the operation of the Business before the Effective Time;

(i) all raw materials and works−in−progress, whether stored at a Business location or stored at a third−party location or other Dictaphone location, used or held for use by EMS;

(j) all rights under the escrow agreement executed in connection with the Nice Settlement Agreement and any remaining payments to be made by the Buyer to Dictaphone under the Nice Settlement Agreement; and

(k) the assets, rights, interests and properties listed on Annex 2.2.

2.3 Assumed Liabilities. On the Closing Date, the Buyer shall hereby, and shall cause its Buyer Affiliates to, assume and thereafter discharge when and as due the following debts, liabilities and obligations of Dictaphone and the Selling Subsidiaries, but only to the extent arising out of or pertaining to the Business or the Purchased Assets (collectively, the “Assumed Liabilities”):

(a) all liabilities that would constitute accounts payable and amounts that would constitute accrued expenses (but not including any accrued expenses relating to Employees or Taxes) that remain unpaid as of the Effective Time, but only to the extent reflected in the Estimated Closing Date Balance Sheet, as and to the extent modified by the Closing Date Balance Sheet;

(b) all lawsuits commenced and claims made after the Effective Time to the extent resulting from the conduct of the Business or the Purchased Assets after the Effective Time, including lawsuits and claims relating to any alleged Intellectual Property infringement;

(c) all Liabilities for Taxes to the extent set forth in Section 2.8(a);

(d) all Liabilities to suppliers for materials and services relating to the Business ordered in the Ordinary Course prior to the Effective Time, but scheduled to be delivered or provided thereafter, and all liabilities to customers under purchase orders for products of the Business which have not yet been shipped prior to the Effective Time;

(e) except as provided in Section 2.4(i), all Liabilities under the Assigned Contracts, including time and materials relationships, (including, subject to Section 2.4(i), with respect to maintenance, repair and warranty claims arising in the Ordinary Course);

(f) all Liabilities with respect to products or services of the Business sold after the Effective Time and all Liabilities arising out of, or otherwise caused by, acts or omissions of the Buyer or its Affiliates after the Effective Time;

(g) all Liabilities in respect of ordinary course trade letters of credit, bid bonds and performance bonds set forth on Annex 2.3(g) and those permitted to be entered into under Section 6.1(e) between the date hereof and the Closing Date;

(h) all Liabilities related to the Transferred Employees with respect to periods after the Effective Time, except as otherwise provided in this Agreement;

(i) all Liabilities for which the Buyer or a Local Buyer (as defined in Annex 5.6) is responsible under Article 5, including Annex 5.6;

(j) all Liabilities asserted against Dictaphone and its Affiliates in connection with the litigation transferred pursuant to the Termination Agreement; and

(k) except as provided in clauses (b) through (i) of Section 2.4, all other Liabilities arising in the Ordinary Course before or after the Effective Time relating to the Purchased Assets or the Business.

2.4 Retained Liabilities. Notwithstanding any provision in this Agreement to the contrary, Dictaphone shall, and shall cause its Affiliates to, retain and be responsible for its and their respective Liabilities other than the Assumed Liabilities (the "Retained Liabilities"), which Retained Liabilities include the following:

(a) except as provided in Section 2.3(j), all Liabilities resulting from all lawsuits pending as of the Effective Time to the extent resulting from the conduct of the Business by Dictaphone and its Affiliates prior to the Effective Time, or otherwise relating to the operation of the Business prior to the Effective Time, including any contingency legal fee relating to Business Intellectual Property;

(b) all Liabilities for Taxes imposed by any Federal, state or local government or other Taxing authority in the United States or in any other jurisdiction for any period through the Effective Time;

(c) all intracompany and intercompany payables of the Business (including corporate overhead charges, except to the extent set forth on Annex 2.4(c));

(d) except as provided in Article 5, including Annex 5.6, all Liabilities related to the Benefit Plans and other employment−related matters concerning Employees;

(e) except as provided in Section 2.3 (and subject to clause (i) of this Section 2.4), all Liabilities arising other than in the Ordinary Course prior to the Effective Time relating to the Purchased Assets or the Business;

(f) all Liabilities arising prior to the Effective Time and relating to compensation, benefits or severance payments or expenses with respect to the Employees and all Liabilities arising under WARN, whether arising before or after the Effective Time, as a consequence of any Employee layoff by, or separation from, Dictaphone;

(g) except as provided in Section 2.3, all Liabilities arising prior to or after the Effective Time to the extent such Liabilities arise from acts or omissions prior to the Effective Time and are not related to, or do not arise out of, the operation of the Business by the Buyer and its Affiliates or the ownership or use of the Purchased Assets by the Buyer and its Affiliates;

(h) all Liabilities to third parties for accounting, audit, tax, legal and other professional services incurred in connection with the preparation, negotiation and execution of this Agreement and the Related Agreements;

(i) notwithstanding anything contained in Section 2.3 or this Section 2.4 to the contrary, all Liabilities to third parties (including governmental authorities) with respect to claims for violation of Laws (including environmental Laws) arising out of the operation of the Business prior to the Effective Time, and all Liabilities to third parties (including governmental authorities) with respect to claims for personal injury, property damage or business interruption (in each case, other than Liabilities in the Ordinary Course with respect to maintenance, repair or warranty claims) regarding products or services of the Business to the extent that such Liabilities arise from acts or omissions prior to the Effective Time; provided, however, that, while Dictaphone shall have initial responsibility for addressing any such claims, the Buyer and its Affiliates shall use commercially reasonable efforts to, as promptly as practicable, provide to Dictaphone and its Affiliates (or to such third party at Dictaphone's request) all maintenance, repair and other product support services, including new replacement and, if then existing, upgraded products (including newer product model(s)) that Dictaphone may request to seek to resolve or mitigate such Liabilities, subject to Buyer's available resources with respect to discontinued products or services; and

(j) all Liabilities arising from or related to the Excluded Assets or the Other Dictaphone Businesses.

The Buyer agrees to, and to cause its Affiliates to, provide the services and products as described in Section 2.4(i) and Dictaphone agrees to reimburse the Buyer (promptly upon presentation of appropriate supporting documentation) at (y) cost with respect to products manufactured by EMS and (z) with respect to services, the lesser of (A) fifty percent (50%) of list price or (B) prices no less favorable than those generally made available to most−favored customers of the Business at that time.

2.5 Consideration.

(a) Purchase Price. In consideration for Dictaphone's and the Selling Subsidiaries' sale, assignment, transfer, conveyance and delivery of the Purchased Assets to the Buyer and the Buyer Affiliates, the Buyer shall:

(i) pay to Dictaphone on behalf of Dictaphone and the Selling Subsidiaries a purchase price of U.S. Thirty−Eight Million Four Hundred Ten Thousand Dollars (US$38,410,000.00) (the "Purchase Price"), of which (x) U.S. Thirty−Five Million Four Hundred Ten Thousand Dollars (US$35,410,000.00) shall be paid directly to Dictaphone, and (y) U.S. Three Million Dollars (US$3,000,000.00) shall be deposited in escrow (with any accrued interest earned thereon, the "Indemnification Escrowed Funds") in accordance with Section 2.7 and the terms and conditions of the Escrow Agreement, as security for the indemnification obligations of Dictaphone set forth in Article 9; provided, however, that the Purchase Price is subject to adjustment pursuant to Section 2.5(b); and provided further, however, that all amounts payable under this Section 2.5 are stated exclusive of any value added or similar sales tax which shall be payable in addition; and

(ii) assume, duly perform and discharge, or cause the Buyer Affiliates to assume, duly perform and discharge, when due all of the outstanding obligations of Dictaphone and its Affiliates under the Assumed Liabilities in accordance with Section 2.3.

(b) Certain Adjustments. Without limiting the Buyer's rights under Article 9, without duplication, the Purchase Price shall be subject to adjustment, to the extent that Net Adjusted Working Capital Level as of the Closing Date is less than $0.00, in accordance with the provisions of this Section 2.5(b) as follows:

(i) At least five (5) Business Days prior to Closing, Dictaphone shall prepare and deliver to the Buyer (i) a balance sheet of the Business setting forth the Purchased Assets and Assumed Liabilities as of the then−projected Closing Date (the "Estimated Closing Date Balance Sheet"), and (ii) a calculation of Net Adjusted Working Capital Level as of the then−projected Closing Date. The Estimated Closing Date Balance Sheet shall (i) be derived from the books and records of the Business, (ii) fairly present, in all material respects, the Purchased Assets to be acquired and the Assumed Liabilities to be assumed pursuant to this Agreement, and (iii) be prepared in accordance with U.S. GAAP. Notwithstanding the foregoing, in no event shall the Estimated Closing Date Balance Sheet attribute any value to, include any asset or liabilities created by, or otherwise reflect (x) the OSS Payment or any other payments made by or on behalf of Dictaphone in connection with the amendment to the OSS Agreement or (y) the transactions contemplated thereby. To the extent that any Prepaid Expense of the Business relating to services provided by Dictaphone or any Account Receivable owing to

Dictaphone is to be terminated or forgiven as of the Closing, such Prepaid Expense or Account Receivable shall be recorded on the Estimated Closing Date Balance Sheet as $0.00 and any related proceeds shall be retained by Dictaphone. The Estimated Closing Date Balance Sheet shall be prepared by Dictaphone, and reviewed by the Buyer. Representatives of the Buyer and Dictaphone shall jointly conduct a physical count of the Inventory and Tangible Business Assets as of the Closing Date pursuant to procedures reasonably designed to minimize disruption of the Business and cost to the Parties.

(ii) Subject to Section 2.5(b)(iv), the Purchase Price payable at Closing shall be decreased on a dollar−for−dollar basis by an amount equal to the amount by which the Net Adjusted Working Capital Level as set forth on the Estimated Closing Date Balance Sheet is less than $0.00.

(iii) In the event that the Buyer promptly, but in any event prior to any scheduled Closing Date, notifies Dictaphone that the Buyer in good faith disputes the Estimated Closing Date Balance Sheet, the Buyer and Dictaphone shall use their commercially reasonable efforts for a period of five (5) Business Days (or such longer period as they may mutually agree) to resolve any disagreements with respect to the Estimated Closing Date Balance Sheet, and any scheduled Closing Date shall be deferred up to ten (10) days to accommodate such attempted resolution. If the Buyer and Dictaphone resolve such disagreements and agree on an Estimated Closing Date Balance Sheet, such agreed upon Estimated Closing Date Balance Sheet shall be final and binding and references to the Estimated Closing Date Balance Sheet shall thereafter mean such agreed upon Estimated Closing Date Balance Sheet. If, at the end of such period, the Buyer and Dictaphone are unable to resolve their disagreements with respect to the Estimated Closing Date Balance Sheet, (x) the amount in dispute shall be deposited in escrow by the Buyer (the "Balance Sheet Escrowed Funds") if such amount equals or exceeds Two Hundred Fifty Thousand U.S. Dollars ($250,000), but only to the extent that, if the Buyer's good faith claims in the dispute were upheld, the Net Adjusted Working Capital Level as of the Closing would be less than zero and would result in a reduction of the Purchase Price of at least Two Hundred Fifty Thousand U.S. Dollars ($250,000) and (y) the Estimated Closing Date Balance Sheet prepared by Dictaphone shall be used to calculate the Purchase Price payable at Closing (and references to the Estimated Closing Date Balance Sheet shall thereafter mean the Estimated Closing Date Balance Sheet prepared by Dictaphone), but without limiting any Party's rights under Section 2.5(b)(iv). The Balance Sheet Escrowed Funds shall be released in accordance with Section 2.5(b)(v) and the terms and provisions of the Escrow Agreement.

(iv) As soon as practicable (but in no event later than sixty (60) days) following the Closing Date, Dictaphone shall prepare and deliver to the Buyer (i) a balance sheet of the Business reflecting the Purchased Assets actually acquired and Assumed Liabilities actually assumed as of the Closing (the "Closing Date Balance Sheet") and (ii) a calculation of the Net Adjusted Working Capital Level as of the Closing. The Closing Date Balance Sheet shall (i) be derived from the books and records of the Business, (ii) fairly present, in all material respects, the Purchased Assets actually acquired and the Assumed Liabilities actually assumed pursuant to this Agreement and (iii) be prepared in accordance with U.S. GAAP. Notwithstanding the foregoing, in no event shall the Closing Date Balance Sheet attribute any value to, include any asset or liabilities created by, or otherwise reflect (x) the OSS Payment or any other payments made to OSS by or on behalf of Dictaphone in connection with the amendment to the OSS Agreement or (y) the transactions contemplated thereby. For the purpose of preparing the Closing Date Balance Sheet and calculating Net Adjusted Working Capital Level as of the Closing, the Buyer shall provide Dictaphone and its accountants with reasonable access to (i) all the underlying documentation and records necessary for Dictaphone and its auditors to prepare the Closing Date Balance Sheet and calculation of Net Adjusted Working Capital Level as of the Closing and all other records of the Buyer and its Affiliates reasonably related to the preparation of the Closing Date Balance Sheet and the calculation of Net Adjusted Working Capital Level as of the Closing and (ii) the employees of the Buyer and its Affiliates. The Buyer may dispute any element of the Closing Date Balance Sheet or the calculation of Net Adjusted Working Capital Level as of the Closing by notifying Dictaphone of such disagreement in writing, setting forth in detail the particulars of such disagreement, within sixty (60) calendar days after the Buyer's receipt of the Closing Date Balance Sheet and the calculation of Net Adjusted Working Capital Level as of the Closing from Dictaphone. In the event that the Buyer does not provide such a notice of disagreement within such sixty (60) calendar day period, the Buyer shall be deemed to have accepted Dictaphone's Closing Date Balance Sheet and calculation of Net Adjusted Working Capital Level as of the Closing, which shall be final, binding and conclusive for all purposes hereunder. In the event any such notice of disagreement is timely provided, the Buyer and Dictaphone shall use their commercially reasonable efforts for a period of thirty (30) calendar days (or such longer period as they may mutually agree) to resolve any disagreements with respect to the Closing Date Balance Sheet and the calculation of Net Adjusted Working Capital Level as of the Closing. If, at the end of such period, they are unable to resolve such disagreements, then such dispute shall be referred to an independent accounting firm of recognized national standing mutually selected by the Buyer and Dictaphone (the "Auditor") which shall resolve any remaining disagreements. The Auditor shall determine as promptly as practicable, but in any event within thirty (30) calendar days of the date on which such dispute is referred to the Auditor, based solely on the written submissions forwarded by the Buyer and Dictaphone, whether and to what extent (if any) the Closing Date Balance Sheet and the calculation of Net Adjusted Working Capital Level as of the Closing require adjustment. The fees and expenses of the Auditor shall be paid one−half by the Buyer and one−half by Dictaphone. The determination of the Auditor shall be final, conclusive and binding on the Parties. The final Closing Date Balance Sheet and the final calculation of the Net Adjusted Working Capital Level as of the Closing shall be deemed to be an annex to this Agreement (the "Net Adjusted Working Capital Level Annex").

(v) If, as a result of the procedure set forth in Section 2.5(b)(iv), the final Net Adjusted Working Capital Level as of the Closing is determined to be:

(A) Less than the Net Adjusted Working Capital Level determined on the basis of the Estimated Closing Date Balance Sheet, then the difference (up to but not greater than the amount by which the final Net Adjusted Working Capital Level determined in accordance with Section 2.5(b)(iv) is less than zero) between the final Net Adjusted Working Capital Level determined in accordance with Section 2.5(b)(iv) and the Net Adjusted Working Capital Level determined on the basis of the Estimated Closing Date Balance Sheet shall be paid by Dictaphone to the Buyer (1) first, from the Balance Sheet Escrowed Funds and (2) if the Balance Sheet Escrowed Funds are insufficient to pay in full any amounts due to the Buyer from Dictaphone under this Section 2.5(b)(v)(A), then from Dictaphone's other assets;

provided, however, that any Balance Sheet Escrowed Funds remaining after payment to the Buyer under this Section 2.5(b)(iv)(A) shall be released to Dictaphone; or

(B) Equal to or greater than the Net Adjusted Working Capital Level determined on the basis of the Estimated Closing Date Balance Sheet, then the difference (up to but not greater than the amount by which the Net Adjusted Working Capital Level determined on the basis of the Estimated Closing Date Balance Sheet is less than zero) between the final Net Adjusted Working Capital Level determined in accordance with Section 2.5(b)(iv) and the Net Adjusted Working Capital Level determined on the basis of the Estimated Closing Dated Balance Sheet shall be paid by Buyer to Dictaphone in the following manner: (1) first, all Balance Sheet Escrowed Funds shall be released to Dictaphone and (2) if the Balance Sheet Escrowed Funds are insufficient to pay in full any amounts due to Dictaphone from the Buyer under this Section 2.5(b)(v)(B), then from the Buyer's other assets.

The Parties agree that the amount described in the parenthetical clause in Section 2.5(b)(v)(B) can not be less than the Balance Sheet Escrowed Funds. Not later than the tenth (10th) day following the final determination of the Net Adjusted Working Capital Level Annex in accordance with Section 2.5(b)(iv), the Buyer and Dictaphone shall jointly instruct the Escrow Agent to release the Balance Sheet Escrowed Funds from escrow in accordance with this Section 2.5(b)(v) and the terms and conditions of the Escrow Agreement.

2.6 Closing. The Closing shall take place at 9:00 a.m. on the Closing Date at the offices of Kelley Drye & Warren LLP at 101 Park Avenue, New York, N.Y., or at such other place as the Parties may agree in writing. At the Closing, Dictaphone shall deliver or cause its Affiliates to deliver to the Buyer or the Buyer Affiliates, as applicable, the documents and other items identified in Article 7, and the Buyer shall deliver or cause its Affiliates to deliver to Dictaphone, the Selling Subsidiaries and the Escrow Agent, as applicable, (a) by wire transfer of immediately available funds, in accordance with Section 2.5(a)(i) and the wire transfer instructions provided by Dictaphone prior to the Closing, the Purchase Price and (b) the documents and other items identified in Article 8.

2.7 Escrow.

(a) Creation of Escrow. On the Closing Date, the Buyer shall deposit or cause to be deposited the Indemnification Escrowed Funds and, if applicable, the Balance Sheet Escrowed Funds with the Escrow Agent in a separate account, and such Indemnification Escrowed Funds and Balance Sheet Escrowed Funds shall be held by the Escrow Agent in accordance with the terms and conditions of the Escrow Agreement as security for the indemnification obligations of Dictaphone to the Buyer set forth in Article 9 and pending determination of the final Net Adjusted Working Capital Level as of the Closing pursuant to Section 2.5(b).

(b) Set−Off. Pursuant to the terms and conditions of the Escrow Agreement and subject to Article 9, the Buyer shall have the right to set off, in whole or in part, any Losses arising out of a breach of any representation, warranty, agreement or covenant in this Agreement or any Related Agreement by Dictaphone from the Indemnification Escrowed Funds to the extent that the Buyer is entitled to indemnification under Article 9.

(c) Release of Indemnification Escrowed Funds. Fifty percent (50%) of the Indemnification Escrowed Funds then held in escrow less the amount of any claims for Losses pursuant to a Notice of Claim under Section 9.3 delivered by the Buyer to Dictaphone prior to the twelve (12) month anniversary of the Closing Date shall be released to Dictaphone on the twelve (12) month anniversary of the Closing Date. The remaining Indemnification Escrowed Funds then held in escrow less the amount of any claims for Losses pursuant to a Notice of Claim under Section 9.3 delivered by the Buyer to Dictaphone prior to the twenty−one (21) month anniversary of the Closing Date shall be released to Dictaphone on the twenty−one (21) month anniversary of the Closing Date. Any Indemnification Escrowed Funds remaining in escrow after the twenty−one (21) month anniversary of the Closing Date will be released from escrow in accordance with the terms and provisions of the Escrow Agreement.

(d) Release of Balance Sheet Escrowed Funds. The Balance Sheet Escrowed Funds shall be released to the Buyer or Dictaphone in accordance with the terms and provisions of the Escrow Agreement and Section 2.5(b)(v).

2.8 Taxes.

(a) All sales, use, value−added, gross receipts, registration, stamp duty and other similar transfer Taxes, if any, together with all recording or filing fees, notarial fees and other similar costs of Closing, that may be imposed upon, or payable, collectible or incurred in connection with, the transfer and sale of the Purchased Assets as contemplated by the terms of this Agreement shall be borne one−half by the Buyer or a Buyer Affiliate and one−half by Dictaphone or a Selling Subsidiary. The Party responsible for paying any such Taxes shall collect from the other Party an amount equal to fifty percent (50%) of any such Taxes it is required to withhold or pay and, to the extent that a Party receives a refund of any such Taxes, it shall reimburse the other Party for fifty percent (50%) of such refund received.

(b) Each Party shall and shall cause its Affiliates to, upon request, use its reasonable efforts to provide or obtain from any Taxing authority or other Person any certificate or other document necessary to mitigate, reduce or eliminate any Taxes described in Section 2.8(a).

(c) The Buyer shall prepare and timely file or caused to be prepared and timely filed all Tax returns for all Taxes that are not based on income or receipts (e.g., property Taxes) relating solely to the Purchased Assets or the Business for a Straddle Period. Such Tax returns shall be prepared in a manner consistent with practices followed in prior years with respect to similar Tax returns, except for changes required by applicable Law. The Buyer shall pay or cause to be paid all Taxes reflected on such Tax returns; provided, that Dictaphone shall deliver or cause to be delivered to the Buyer Dictaphone’s portion of such Taxes that relates to the portion of such Straddle Period ending on the Closing Date no later than five (5) Business Days prior to the date on which the Buyer proposes to pay or cause to be paid such Taxes. For purposes of this Section 2.8(c), the portion of any such Tax allocated to Dictaphone shall be the amount of such Tax for the entire Taxable period multiplied by a fraction, the numerator of which is the number of days in the taxable period ending on the Closing Date and the denominator of which is the number of days in the entire taxable period. Any credits relating to a Straddle Period shall be taken into account as though the relevant Taxable period ended on the Closing Date.

(d) The Buyer and Dictaphone shall furnish or cause to be furnished to each other, upon request, as promptly as practicable, such information (including reasonable access to books and records) and assistance as is reasonably necessary for the filing of any Tax return, the conduct of any Tax audit, and the prosecution or defense of any Proceeding relating to any Tax matter. Any Tax audit or other Tax Proceeding shall be deemed to be a Third−Party Claim subject to the procedures set forth in Section 9.4.

2.9 Allocation of Purchase Price. The Buyer and Dictaphone shall mutually agree to the allocation of the Purchase Price (as it may be adjusted pursuant to Section 2.5(b)) among Dictaphone and the Selling Subsidiaries, among the Buyer and the Buyer Affiliates and among the Purchased Assets in accordance with applicable Laws, including Code Sections 338 and 1060, within 90 days after the Closing Date. The Parties hereby agree to file IRS Form 8594 and file or cause to be filed all Tax returns and information reports in a manner consistent with such allocation and shall use their reasonable best efforts to sustain such allocation in any subsequent Tax audit or Tax dispute.

2.10 Completion of Transfers.

(a) The entire beneficial interest in and to, and the risk of loss with respect to, the Purchased Assets and the Assumed Liabilities, shall, regardless of when legal title thereto or responsibility therefor shall be transferred to or assumed by the Buyer, pass to the Buyer at the Closing as of the Effective Time. In the event that legal title in or to any of the Purchased Assets or legal responsibility for any of the Assumed Liabilities is not transferred or assumed at the Closing, Dictaphone and its Affiliates shall hold such Purchased Assets or Assumed Liabilities as nominee for the Buyer and its Affiliates until completion of such transfer or assumption.

(b) In the event that legal title in or to any of the Purchased Assets or legal responsibility for any of the Assumed Liabilities to be sold, assigned, transferred, conveyed or assumed pursuant to this Agreement, or any claim, right or benefit arising thereunder or resulting therefrom, cannot be sold, assigned, transferred, conveyed or assumed hereunder as of the Closing Date because any waiting or notice period required in connection therewith has not expired or any consents, authorizations or approvals required therefor have not been obtained or waived, then the legal title in or to such Purchased Assets or the legal responsibility for such Assumed Liabilities shall not be sold, assigned, transferred, conveyed or assumed unless and until such waiting or notice period shall have expired or been waived or until such consent, authorization or approval shall have been obtained or waived. In such event, Dictaphone shall, at its expense, and the Buyer shall, at its expense, use commercially reasonable efforts to cooperate in obtaining such consents, authorizations, approvals or waivers as soon as practicable. Subject to Section 7.2, the failure of Dictaphone to obtain any required consents, authorizations, approval or waivers shall not affect the Buyer's obligations to close under this Agreement or to pay, or cause to be paid, the Purchase Price. Nothing in this Agreement shall be construed as an attempt to assign to the Buyer or its Affiliates any legal title or responsibility which, as a matter of Law or by the terms of any legally binding Contract to which Dictaphone or its Affiliates is subject, is not assignable without the consent of any other Person, unless such consent shall have been given or waived.

(c) Pending the assignments, conveyances, transfers and assumptions referred to in Section 2.10(b), (A) Dictaphone shall (i) hold any such non−assigned, non−conveyed, non−transferred or non−assumed Purchased Assets or Assumed Liabilities for the benefit and at the risk of the Buyer, (ii) cooperate with the Buyer in any lawful and reasonable arrangements designed to provide the benefits and burdens of ownership thereof and responsibility therefor to the Buyer and (iii) indemnify and hold the Buyer harmless from and against any and all Losses rising solely from the failure to assign, convey, transfer or assume such Purchased Assets or Assumed Liabilities or to obtain any such consent, authorization or approval as has not been obtained or waived and (B) Buyer shall perform or cause the Buyer Affiliates to perform under any such non−assigned, non−conveyed, non−transferred or non−assumed Purchased Assets or Assumed Liabilities as if such non−assigned, non−conveyed, non−transferred or non−assumed Purchased Asset or Assumed Liability had been assigned, conveyed, transferred or assumed to or by Buyer or a Buyer Affiliate, including providing services under any warranty and recognizing, and not taking any action inconsistent with, any license granted under any such Purchased Asset or Assumed Liability.

(d) All of the costs and expenses associated with the assignment to the Buyer, and the recordation by it, of the Business Intellectual Property shall be paid one−half by the Buyer and one−half by Dictaphone.

2.11 Subsidiary Asset Purchase Agreements. At or prior to the Closing, Dictaphone shall cause each of the Selling Subsidiaries to enter into a separate transfer of assets and assumption of liabilities agreement with the applicable Buyer Affiliate, and the Buyer shall cause each such Buyer Affiliate to enter into such separate agreement with the applicable Selling Subsidiary, each such agreement to be substantially in the form of Exhibit F, with such modifications as are necessary or appropriate as a result of (a) differences in the businesses and Purchased Assets and Assumed Liabilities of each Selling Subsidiary, (b) differences in local law or customs which may require changes in order to maintain substantially the same legal meaning and effect under local law and custom as provided for with respect to the comparable provisions of this Agreement, and (c) the parties' respective tax considerations to the extent that they are not inconsistent with the comparable provisions of this Agreement (such agreements are, collectively, the "Subsidiary Asset Purchase Agreements"). Each Subsidiary Asset Purchase Agreement shall be subject to this Agreement and shall be construed so as to be consistent with each other and this Agreement and so as not to create duplicative rights and liabilities (although they may create additional rights and liabilities); provided, however, that, in the event of a conflict or inconsistency between this Agreement and such Subsidiary Asset Purchase Agreement as to any matter other than one mandatorily governed by laws or orders of the applicable jurisdiction of the Selling Subsidiary whose assets and liabilities are subject to such Subsidiary Asset Purchase Agreement, this Agreement shall govern and, in the event of a conflict or inconsistency as to any matter mandatorily so governed, such Subsidiary Asset Purchase Agreement shall govern. The Parties agree to use commercially reasonable efforts to limit the number and scope of Subsidiary Asset Purchase Agreements to those required by local legal requirements and their respective tax considerations.

ARTICLE 3
REPRESENTATIONS AND WARRANTIES OF DICTAPHONE

Dictaphone hereby makes the following representations and warranties, each of which is true and correct on the date hereof and shall survive the Closing Date and the transactions contemplated hereby to the extent set forth herein.

3.1 Existence and Power; Consents.

(a) Each Seller has the corporate, partnership, limited liability company or other organizational power and authority, as applicable, to execute and deliver this Agreement and any Related Agreement to which it is a party, to perform its obligations hereunder and thereunder, and to consummate the transactions contemplated hereby and thereby. Each Seller has the requisite corporate, partnership, limited liability company or other organizational power and authority, as applicable, to transfer the Purchased Assets owned by such Seller, to assign the Assumed Liabilities of such Seller and to consummate the transactions contemplated hereby.

(b) Each Seller is validly existing and in good standing under the laws of its jurisdiction of formation (to the extent such concept is recognized in such jurisdiction) and each jurisdiction in which the nature of its business makes such qualification necessary, except where the failure to be so qualified and in good standing would not have a Material Adverse Effect. Dictaphone is qualified to transact business as a foreign corporation in Florida.

(c) No Seller is a party to, subject to or bound by any Encumbrance or Law which would (i) be breached or violated in any material respect by the execution or delivery by such Seller of this Agreement (to the extent it is a party hereto) or a Related Agreement to which it is a party or the performance by any Seller of the transactions contemplated by this Agreement or a Related Agreement (to the extent it is a party hereto) or (ii) prevent the carrying out of the transactions contemplated hereby (to the extent it is a party hereto). Except as set forth in Disclosure Schedule Section 3.1(c), no permit, consent, waiver, approval or authorization of, or declaration to or filing or registration with, any governmental or regulatory authority or any lender, lessor, distributor, customer, supplier, licensor or other third−party is required in connection with the execution, delivery or performance of this Agreement by any Seller or any of the Related Agreements to which such Seller is a party or the consummation by the Sellers of the transactions contemplated hereby (to the extent it is a party hereto) and thereby (to the extent it is a party hereto), except for any such permits, consents, waivers, approvals, authorizations, declarations, filings or registrations the failure of which to obtain would not, individually or in the aggregate, have a Material Adverse Effect. The transactions contemplated hereby will not result in the creation of any Encumbrance against the Purchased Assets.

(d) The Sellers have the power and authority to own, lease and use their respective assets in connection with the Business.

3.2 Valid and Enforceable Agreement; Authorization. This Agreement and the Related Agreements have been duly executed and delivered by the Sellers party thereto and constitute legal, valid and binding obligations of the Sellers, enforceable against the Sellers in accordance with their terms, except that such enforcement may be subject to (a) bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting or relating to enforcement of creditors' rights generally and (b) general principles of equity. The execution and delivery of this Agreement and the Related Agreements and the consummation of the transactions contemplated hereby and thereby have been duly authorized, approved and ratified by all necessary corporate action (including stockholder approval to the extent required by law or contract) on the part of the Sellers party thereto.

3.3 Ownership. Except for the Permitted Encumbrances, the Sellers together have good title to and are the sole and exclusive owner of all right, title and interest in and to all of the Purchased Assets, free and clear of all Encumbrances. At Closing, the Buyer and the Buyer Affiliates together will acquire all right, title and interest in and to all of the Purchased Assets, free and clear of all Encumbrances, other than Permitted Encumbrances and any Encumbrances created by acts or omissions of the Buyer and its Affiliates. Except as set forth in Disclosure Schedule Section 3.3, none of the Purchased Assets is in the possession of Persons other than a Seller or held by Dictaphone or its Affiliates on consignment.

3.4 Financial Statements; Other Financial Information.

(a) Other Financial Information. Disclosure Schedule Section 3.4(a) set forth, in each case as of, or for, the twelve (12) months ended December 31, 2004: (i) the aggregate dollar amount of product revenue of the Business (calculated in accordance with U.S. GAAP); (ii) the aggregate dollar amount of Product Backlog of the Business calculated in a manner consistent with past practices and (iii) the aggregate dollar amount of Net Adjusted Working Capital Level of the Business (collectively, the "Other Financial Information"). The Other Financial Information (y) was derived from the books and records of the Business and (z) is true and correct in all material respects.

(b) Audited Financial Statements. The Audited Financial Statements to be delivered prior to the Closing pursuant to Section 6.7 (i) will be derived from the books and records of the Business, (ii) will fairly present, in all material respects, the financial position and results of operations of the Business at the dates and for the periods indicated in accordance with U.S. GAAP and the applicable requirements of Rule 3−05 of Regulation S−X, except as described in Disclosure Schedule Section 3.4(b) and (iii) will be accompanied by (x) an unqualified report thereon by an independent auditor (which shall be one of the four largest independent auditing firms in the United States) (the "Auditor's Report"). The balance sheets included in the Audited Financial Statements will not include any material assets or liabilities that do not constitute a part of the Business as currently conducted by Dictaphone, the Purchased Assets or the Assumed Liabilities. The statements of profit and loss included in the Audited Financial Statements will not reflect the operations of any Person or business that does not constitute a part of the Business as currently conducted by Dictaphone.

(c) Estimated Closing Date Balance Sheet. The Estimated Closing Date Balance Sheet to be delivered prior to the Closing pursuant to Section 2.5(b) will (i) be derived from the books and records of the Business and (ii) fairly present, in all material respects, the financial position of the Business as of the Closing Date in accordance with U.S. GAAP. The Estimated Closing Date Balance Sheet will not include any material assets or liabilities that do not constitute a part of the Business as currently conducted by Dictaphone, the Purchased Assets or the Assumed Liabilities, recognizing that the Estimated Closing Date Balance Sheet will be an estimated financial statement.

(d) Warranties. Except as listed in Disclosure Schedule Section 3.4(d), there are no material unresolved warranty and support claims (including any pending claims) related to products or services of the Business (other than deferred revenues).

3.5 Absence of Certain Developments. Except as set forth in Disclosure Schedule Section 3.5, since September 30, 2004, neither the Business nor the Sellers in respect of the Business have:

(a) suffered any event, circumstance or condition having a Material Adverse Effect;

(b) incurred any obligation or liability, whether due or to become due, or entered into any other transaction except in the Ordinary Course and except for liabilities and transactions that have not, individually or in the aggregate, had a Material Adverse Effect;

(c) suffered any material adverse change in its relationship with any of the suppliers, customers, distributors, lessors, licensors, licensees or other third−parties which are material to the Business;

(d) increased the rate or terms of compensation or benefits payable to or to become payable by it to any management or other key employee earning over $75,000 per year or increased the rate or terms of any bonus or Benefit Plan covering any such employee, except in each case increases occurring in the Ordinary Course in accordance with its customary practice (including normal periodic performance reviews and related compensation and benefits increases) or made any material changes in policies of employment;

(e) received any notice of termination of any contract, lease or other agreement or suffered any damage, destruction or loss which, individually or in the aggregate, has had or is reasonably likely to have a Material Adverse Effect;

(f) transferred or granted any rights or licenses under, or entered into any settlement regarding the breach or infringement of, any Business Intellectual Property, or modified any existing rights with respect thereto;

(g) received any written notice by any customer or supplier material to the Business of an intention to discontinue or change the terms of its relationship;

(h) made any material change in its accounting methods or practices, policies or principles, or made any new tax elections or changes in existing tax elections with respect to the Business inconsistent with past practice;

(i) instituted, settled or agreed to settle any material litigation, action or proceeding before any court or governmental body relating to the Business or the Purchased Assets;

(j) made any material changes in policies or practices relating to selling practices, returns, discounts or other terms of sale;

(k) waived any claims or rights of material value to the Business other than in the Ordinary Course;

(l) sold, leased, licensed or otherwise disposed of any of the Purchased Assets, other than in the Ordinary Course;

(m) amended or terminated any Material Contract to which it is or was a party, other than in the Ordinary Course;

(n) mortgaged, pledged or otherwise subjected to an Encumbrance any property, business or assets, tangible or intangible, used or held for use primarily in the Business, except Permitted Encumbrances or Encumbrances that will be released prior to the Closing Date; or

(o) committed pursuant to a legally binding agreement to do any of the things set forth in clauses (b) through (n) above.

3.6 Taxes. Except as set forth in Disclosure Schedule Section 3.6:

(a) All material Tax returns required to be filed with respect to the Purchased Assets or the Business have been properly filed in a timely manner (taking into account all extensions of due dates) and are true, correct and complete in all material respects.

(b) All Taxes (other than Retained Liabilities) due with respect to the Business or the Purchased Assets for all periods through the Effective Time have been or will be timely paid in full.

(c) There are no deficiencies for any Taxes (including penalties and interest) in respect of the Purchased Assets or the Business. To the knowledge of Dictaphone, no audit of any Tax return with respect to the Business is currently pending or threatened. No claim has ever been made by any governmental authority in a jurisdiction where Dictaphone does not file Tax returns that it is or may be subject to taxation by that jurisdiction.

(d) Dictaphone has not waived any statute of limitations with respect to Taxes or agreed to any extension of time with respect to a Tax assessment or deficiency that in either case, would have a Material Adverse Effect.

3.7 Insurance.

(a) Disclosure Schedule Section 3.7(a) lists and describes the following information with respect to each material insurance policy (including policies providing property, casualty, liability and workers' compensation coverage, and bond and surety arrangements) with respect to which Dictaphone, in respect of the Business, is a party, a named insured, or otherwise the beneficiary of coverage:

(i) The name, address and telephone number of the agent;

(ii) The names of the insurer, the policyholder and each covered insured;

(iii) The policy number and the period of coverage;

(iv) The scope (including an indication of whether the coverage is on a claims made, occurrence or other basis) and amount (including a description of how deductibles and ceilings are calculated and operate) of coverage; and

(v) A description of any retroactive premium adjustments or other material loss−sharing arrangements.

(b) With respect to each such insurance policy: (i) the policy is legal, valid, binding, enforceable, and in full force and effect in all material respects; (ii) neither Dictaphone, in respect of the Business, nor, to Dictaphone's knowledge, any other party to the policy is in material breach or default (including with respect to the payment of premiums or the giving of notices), and no event has occurred that, with notice or the lapse of time, would constitute such a material breach or default, or permit termination, modification or acceleration, under the policy; and (iii) no party to the policy has repudiated any material provision thereof. Disclosure Schedule Section 3.7(b) describes any material self−insurance arrangements affecting the Business.

3.8 Litigation. Except as set forth in Disclosure Schedule Section 3.8, there are no material actions, suits or proceedings pending or, to Dictaphone's knowledge, threatened against Dictaphone or the other Sellers in respect of the Business. Neither Dictaphone nor the other Sellers in respect of the Business are subject to any adverse order, judgment, writ, injunction or decree of any court or governmental or regulatory authority or body (excluding any such matters of general applicability or applicable to entities situated similarly to Dictaphone or the Business rather than to them specifically).

3.9 Product Liability Claims. Except as set forth in Disclosure Schedule Section 3.9, neither Dictaphone nor the other Sellers in respect of the Business has received notice of any unresolved claim of personal injury, death, or property or economic damages, or any unresolved claim for injunctive relief in connection with any product or service manufactured, sold or provided by Dictaphone or the other Sellers (in respect of or as part of the Business).

3.10 Inventory and Accounts Receivable.

(a) Inventory.

(i) The inventory of the Business consists of supplies, manufactured and purchased parts, and finished goods, all of which (i) is merchantable, in good condition, fit for use in the future operations of the Business as currently operated and of a quality that is usable or saleable in the Ordinary Course, (ii) is adequate for the present needs of the Business and (iii) none of which is obsolete, damaged or defective, in the case of each clause (i), (ii) and (iii) above, except (x) to the extent of, but only of, any reserve for inventory or other write−down as adjusted for the passage of time and conduct of the Business in the Ordinary Course in accordance with U.S. GAAP or (y) as set forth on Disclosure Schedule Section 3.10(a). All inventory of the Business conforms in all material respects with applicable specifications and warranties, and has been produced in material compliance with applicable quality control procedures. All inventory of the Business has been manufactured in accordance with applicable law in effect at the time of such manufacture, other than such noncompliance, if any, which would not, individually or in the aggregate, have a Material Adverse Effect. The amount and mix of items in the inventory is in all material respects consistent with past practices.

(ii) The Inventory reflected on the Estimated Closing Date Balance Sheet will consist of supplies, manufactured and purchased parts, and finished goods, all of which (i) will be merchantable, in good condition, fit for use in the future operations of the Business as currently operated and of a quality that will be usable or saleable in the Ordinary Course, (ii) will be adequate for the needs of the Business (as presently conducted by Dictaphone) as of the Closing Date and (iii) none of which will be obsolete, damaged or defective, in the case of clause (i), (ii) and (iii) above, except (x) to the extent of, but only of, any reserve for inventory or other write−down as adjusted for the passage of time and conduct of the Business in the Ordinary Course in accordance with U.S. GAAP, subject to adjustment by the Closing Date Balance Sheet, or (y) as set forth on Disclosure Schedule Section 3.10(a). All Inventory reflected on the Estimated Closing Date Balance Sheet will conform in all material respects with applicable specifications and warranties, and will have been produced in material compliance with applicable quality control procedures. All Inventory reflected on the Estimated Closing Date Balance Sheet will have been manufactured in accordance with applicable law in effect at the time of such manufacture, other than such noncompliance, if any, which would not, individually or in the aggregate, have a Material Adverse Effect. The amount and mix of items in the Inventory reflected on the Estimated Closing Date Balance Sheet will be consistent in all material respects with past practices.

(b) Accounts Receivable.

(i) All notes and accounts receivable of the Business are valid receivables subject to no setoffs or counterclaims and are current and collectible in the Ordinary Course without resort to litigation, in each case, except (x) to the extent of, but only of, any reserve for doubtful accounts and bad debts or other write−down as adjusted for the passage of time and conduct of the Business in the Ordinary Course in accordance with U.S. GAAP or (y) the other matters as set forth on Disclosure Schedule Section 3.10(b).

(ii) All Accounts Receivable reflected on the Estimated Closing Date Balance Sheet will be valid receivables subject to no setoffs or counterclaims and will be current and collectible in the Ordinary Course without resort to litigation, in each case, except (x) to the extent of, but only of, any reserve for doubtful accounts and bad debts or other write−down as adjusted for the passage of time and conduct of the Business in the Ordinary Course in accordance with U.S. GAAP, subject to adjustment by the Closing Date Balance Sheet, or (y) as set forth on Disclosure Schedule Section 3.10(b). All orders which are included in Accounts Receivable on the Estimated Closing Date Balance Sheet will not, to the knowledge of Dictaphone, as of the Closing Date, be subject to valid return (except for products returned in the Ordinary Course).

3.11 Condition of Personal Property. Except as set forth in Disclosure Schedule Section 3.11, all of the Tangible Business Assets which are material to the conduct of the Business are in good condition and repair (ordinary wear and tear excepted) and are suitable for the purposes used in the Business.

3.12 Property; Title. On the Closing Date, the Purchased Assets, and the assets utilized in performing transition and manufacturing services pursuant to the Transition Services/Shared Services Agreement and Manufacturing Agreement, will constitute all property, tangible and intangible, (a) used by the Sellers to transact the Business as presently conducted and as currently proposed to be conducted by Sellers (absent the transactions contemplated hereby) in the Ordinary Course, or (b) necessary to operate the Business in the Ordinary Course, except, in each case, (i) for the Excluded Assets and (ii) where the absence thereof does not have a Material Adverse Effect. On the Closing Date, the assets identified in Section vi of Annex 2.1(a) and Section vi of Annex 2.1(c) constitute all of the Purchased Assets necessary to perform the Services (as defined in the Manufacturing Agreement) under the Manufacturing Agreement, except that such Purchased Assets expressly exclude any generic, commercially−available equipment identified in Section 5 of Annex 2.2.

3.13 Contracts.

(a) Disclosure Schedule Section 3.13(a) sets forth a list of all Contracts as of the date hereof that:

(i) involve payments by a Seller to another party having a value in excess of $25,000 in any 12−month period and which may not be cancelled with less than thirty (30) days' prior written notice;

(ii) involve joint ventures;

(iii) involve distribution or reseller arrangements;

(iv) are with any current employee or consultant;

(v) are with any labor union or association representing any employee;

(vi) are leases with respect to personal property having lease payments in excess of $25,000 in any twelve (12) month period;

(vii) are customer sales, service, maintenance or license agreements or other end user agreements under which payments exceeding $25,000 were made in the prior fiscal year;

(viii) grant a Seller the right to use Intellectual Property of third−parties in the Business under which payments exceeding $25,000 in the aggregate were or will be made in the prior, current or any single future fiscal year, but not including licenses or agreements relating to "shrink wrap" software or other software used to support the infrastructure or enterprise operations of the Business;

(ix) limit or otherwise restrict a Seller, the Business or any successor to a Seller as operator of the Business in the manner or scope (including geographic or technological scope) of the design, development, marketing, sale, production or service of systems and products of the Business; and

(x) any other material Contract of a Seller with respect to the Business entered into other than in the Ordinary Course.

Each contract described in Section 3.13 is referred to as a "Material Contract."

(b) Except as set forth in Disclosure Schedule Section 3.13(b), each Material Contract is a legal, valid and binding obligation of the Seller party thereto, enforceable against such Seller party thereto and, to Dictaphone's knowledge, is in full force and effect, is a legal, valid and binding obligation of the other parties thereto and is enforceable against the other parties thereto. No Seller party to any Material Contract has taken any action to terminate, repudiate or disclaim such Material Contract and, to the knowledge of Dictaphone, after the Closing Date, the Material Contracts will continue to be in full force and effect, be legal, valid and binding obligations of the other parties thereto and enforceable against the other parties thereto following delivery of any consents, waivers or approvals contemplated hereby. For purposes of this Section 3.13(b), the enforceability of any Material Contract is subject to applicable bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and similar laws affecting creditor's rights generally and subject to principles of equity.

(c) To Dictaphone's knowledge, no Seller nor other party thereto is in default under any Material Contract, other than such defaults, if any, which would not, individually or in the aggregate, have a Material Adverse Effect.

(d) No Seller has received any written notice of any intention to terminate, repudiate or disclaim any Material Contract from any other party thereto.

3.14 Licenses and Permits. Except as set forth in Disclosure Schedule Section 3.14, each Seller has all governmental permits, licenses and authorizations necessary for the conduct of the Business as presently conducted by it and as currently proposed to be conducted by it in the Ordinary Course, except where the absence thereof does not have a Material Adverse Effect, and all such permits, licenses and authorizations are valid and in full force and effect in all material respects. Each Seller is in compliance in all material respects with such permits, licenses and authorizations. No such permit, license or authorization has been, or to Dictaphone's knowledge is threatened to be, revoked, canceled, suspended or materially adversely modified.

3.15 Undisclosed Liabilities. Except as set forth in Disclosure Schedule Section 3.15, the Business has no material known Liabilities except for (i) Liabilities set forth on the December 31 Balance Sheet and (ii) Liabilities that have arisen subsequent to the date of the December 31 Balance Sheet in the Ordinary Course.

3.16 Compliance with Laws. Except as set forth in Disclosure Schedule Section 3.16, each Seller in respect of the Business is in compliance in all material respects with all applicable Laws currently in effect (including the Foreign Corrupt Practices Act), and no Seller has received any notice, report or other information alleging any material conflict, violation, breach or default of such Laws.

3.17 Environmental Matters. Except as set forth in Disclosure Schedule Section 3.17:

(a) Each Seller in respect of the Business is in compliance in all material respects with all Environmental Laws. There is no civil, criminal or administrative action, suit, investigation or proceeding pending or, to Dictaphone's knowledge, threatened against any Seller in respect of the Business relating to or arising from any Environmental Laws which is reasonably expected to have a Material Adverse Effect.

(b) No Seller in respect of the Business has not received any written notice, report or other information regarding any actual or alleged material violation of, or liability under, Environmental Laws relating to it or its past or current operations or facilities except such notices, reports or other information that have been complied with and resolved. Neither Dictaphone in respect of the Business nor any of its predecessors or Affiliates in respect of the Business has treated, stored, disposed of, arranged for or permitted the disposal of, transported, handled, or released any substance, including any hazardous materials, or owned or operated the Business or any owned or leased real property in a manner that has given or will give rise to any material liability under any Environmental Law. The off−site treatment, storage or disposal (or arrangement for off−site disposal) of hazardous materials, substances or wastes by the Sellers (in relation to the Business), including any such materials, substances or wastes produced or generated in connection with operations upon any owned or leased real property, has not given and will not give rise to any material liability under any Environmental Law.

3.18 Intellectual Property.

(a) Annex 2.1(c) sets forth the Business Intellectual Property which will be transferred by the Sellers to the Buyer at the Closing, including (i) all Business Intellectual Property comprising issued patents and patent applications (including all provisional, continuation, continuation−in−part, divisional and foreign applications) and trademarks, service marks, trade names, fictitious names, service marks and copyright registrations owned by or assigned or licensed exclusively to the Sellers and (ii) the jurisdictions in which each item of such Business Intellectual Property has been issued or registered or in which any such application for such issuance or registration has been filed. The Business Intellectual Property that will be transferred by the Sellers to the Buyer at the Closing constitutes all of the Intellectual Property necessary to operate the Business in the Ordinary Course as the Business is operated as of the date of this Agreement.

(b) Except as set forth in Disclosure Schedule Section 3.18(b), no material claims by any Person contesting the validity or ownership of any of the Business Intellectual Property or the other Intellectual Property listed on Annex 2.1(c) are pending or, to Dictaphone's knowledge, threatened.

(c) Except as set forth in Disclosure Schedule Section 3.18(c), no claims have been filed by the Sellers asserting that any Person is infringing upon, misappropriating or otherwise violating the Business Intellectual Property listed on Annex 2.1(c).

(d) Except as set forth in Disclosure Schedule Section 3.18(d), Dictaphone has provided to the Buyer true and complete copies of all material contracts, licenses, sublicenses and other agreements to which any Seller is a party under which it is authorized to use any Third Party Intellectual Property related to the Business, including any Third Party Intellectual Property related to the Business that is or is intended to be used by it in the Business, or otherwise in connection with any product or service currently in use, marketed or under development for the Business.

(e) Except as set forth in Disclosure Schedule Section 3.18(e), no Seller is a party to any oral license, sublicense or other agreement related to the Business Intellectual Property which, if reduced to written form, would be required to be listed and provided under any other section of this Agreement.

(f) Except as set forth in Disclosure Schedule 3.18(f), the Business Intellectual Property listed in Annex 2.1(c) has been properly filed, applied for, registered and/or maintained, as applicable, and, to the knowledge of Dictaphone, is in good standing and enforceable under applicable laws and regulations, and no renewal, fee payment, filing of an affidavit of continuing use, or any other action is or will be required to be taken with respect to any such application, registration, or issued patent within twelve (12) months after the date of this Agreement in order to maintain its validity and enforceability.

(g) Except as set forth in Disclosure Schedule Sections 3.8 or 3.18(g), no material action, suit, proceeding or other investigation with respect to Intellectual Property to be conveyed or licensed under this Agreement or otherwise relating to the Business is pending or, to Dictaphone's knowledge, threatened. Dictaphone has made available to the Buyer true, correct and complete copies of all suits, actions or proceedings or written notices listed in Disclosure Schedule Section 3.18 (g).

(h) Neither the development, manufacturing, marketing, licensing or sale of any of its current products of the Business or the performance by any Seller of any of its services of the Business, nor the conduct of the Business as presently conducted, infringes, violates or misappropriates any Third Party Intellectual Property in any material respect.

(i) Except as set forth in Disclosure Schedule Section 3.18(i), to the knowledge of Dictaphone, none of the Business Intellectual Property is being infringed by activities, products or services of, or is being misappropriated by, any Third Party in any material respect.

(j) Except as set forth in Disclosure Schedule Section 3.18(j), the execution and delivery of this Agreement, the consummation of the transactions contemplated by this Agreement and the compliance by any Seller with the provisions of this Agreement do not and will not conflict with, or result in any material violation of, or material default (with or without notice or lapse of time or both) under, or give rise to, any material right, license or encumbrance relating to any Intellectual Property to be conveyed or licensed under this Agreement, and do not and will not result in any material right of termination, cancellation or acceleration of any such Intellectual Property right or obligation set forth in any agreement to which any Seller is a party or any material loss or encumbrance (other than Permitted Encumbrances) of any such Intellectual Property or benefit related thereto, and do not and will not result in the creation of any Lien in or upon any such Intellectual Property, or otherwise limit or restrict the Buyer's ability to conduct the Business as currently conducted or as currently proposed to be conducted by Dictaphone.

(k) Dictaphone has provided to the Buyer a copy of its policy regarding the protection of its trade secrets and confidential information and regarding the assignment to it of all Intellectual Property rights arising from services provided to it by its personnel (the "IP Policy"). Dictaphone has used commercially reasonable efforts to safeguard and maintain the secrecy and confidentiality of the Business Intellectual Property, and to obtain rights in and to any such Intellectual Property generated by its personnel. To the knowledge of Dictaphone, none of the current officers, employees or consultants of the Sellers currently claim or have claimed any material ownership interest in any of the Business Intellectual Property as a result of that Person having been involved in the development of any such Intellectual Property while employed by or providing consulting services to it, or otherwise. To the knowledge of Dictaphone, there has been no material violation of its IP Policy or any confidentiality or assignment of Intellectual Property agreement relating to the Business Intellectual Property.

(l) To the knowledge of Dictaphone, none of the source code related to any products or services related to the Business provided by the Sellers, nor any other of the trade secrets of the Sellers related to the Business, has been published or disclosed, except pursuant to a non−disclosure agreement that is in the standard form used by the Sellers requiring the parties receiving such information to keep it confidential.

(m) Disclosure Schedule Section 3.18(m) lists all worldwide opposition or cancellation proceedings pending or, to the knowledge of Dictaphone, threatened relating to a trademark registration or trademark application listed on Annex 2.1(c). Except for those pending or threatened opposition or cancellation proceedings so listed, to the knowledge of Dictaphone, no trademark office worldwide has put forth a substantive objection to a Dictaphone trademark application that should prevent registration of a pending trademark application.

(n) Dictaphone expects all pending copyright applications worldwide to receive registration and, to the knowledge of Dictaphone, no third party has objected or threatened to object to registration of a Dictaphone copyright.

(o) To the knowledge of Dictaphone, no issued patent or patent application to be conveyed or licensed under this Agreement has been declared or adjudicated invalid, null or void, or its subject matter declared unpatentable or finally rejected as unpatentable, in any judicial or administrative proceeding, nor has any foreign patent or application corresponding in whole or in part to the patent been declared invalid, null or void, or its subject matter declared unpatentable or finally rejected as unpatentable in any judicial or administrative proceeding.

(p) Dictaphone has no knowledge of any prior material art or other material facts which would jeopardize the validity or enforceability of any patent, trademark, or copyright to be conveyed or licensed under this Agreement.

(q) Dictaphone has duly recorded all assignments and transfers affecting title to any patent, trademark or copyright related to the Business to be conveyed or licensed under this Agreement in the U.S. Patent and Trademark Office or appropriate foreign patent office or other governmental agency and, to the knowledge of Dictaphone, Dictaphone is the sole owner of such patents, trademarks and copyrights free of any lien or encumbrance (other than Permitted Encumbrances).

(r) To the knowledge of Dictaphone, except as listed in Disclosure Schedule Section 3.18(r), no licenses or rights related to the Business have been granted to any third party to distribute or copy any of Dictaphone's source code for, or to use any of its source code to create Derivative Works (as defined by US copyright law) related to the Business from, any products embodying any Business Intellectual Property to be conveyed hereunder.

(s) No federal, state, local or other government funding or university or college facilities were used in the development of the Business Intellectual Property or products to be conveyed hereunder.

3.19 Employee Matters. Except as set forth in Disclosure Schedule Section 3.19, (i) no Seller in respect of the Business is delinquent in payments to any of the Employees for any wages or other compensation for any services performed by them or amounts required to be reimbursed to such Employees, (ii) subject to Article 5, including Annex 5.6(a), upon termination of the employment of any Transferred Employees, the Buyer will not by reason of any action taken or not taken by the Sellers prior to the Closing be liable to any of such Employees for severance pay or any other payments and (iii) to Dictaphone's knowledge, no management or Key Employee engaged primarily in the operations of the Business and earning a base salary over $75,000 per year intends to terminate his or her employment with the Sellers.

3.20 Employee Benefits. Disclosure Schedule Section 3.20 lists each Benefit Plan that a Seller maintains, or to which it contributes, in respect of the Business.

(a) To Dictaphone's knowledge, each such Benefit Plan (and each related trust, insurance contract or fund) has been maintained, funded and administered in accordance with the terms thereof and complies in form and in operation in all respects with the applicable requirements of ERISA and the Code, except where the failure to so comply would not have a Material Adverse Effect.

(b) All contributions (including all employer contributions and employee salary reduction contributions) that are due have been made to each such Benefit Plan that is an "employee pension benefit plan" (as defined in Section 3(2) of ERISA). All premiums or other payments that are due have been paid with respect to each such Benefit Plan that is an "employee welfare benefit plan" (as defined in Section 3(1) of ERISA).

(c) Each such Benefit Plan that is intended to meet the requirements of a "qualified plan" under Code Section 401(a) has received a determination letter from the IRS to the effect that it meets the requirements of Code Section 401(a).

(d) With respect to each Benefit Plan that Dictaphone, in respect of the Business, maintains or has maintained, or to which it contributes or has been required to contribute, during the prior six (6) years:

(i) No action, suit, proceeding, hearing or investigation with respect to the administration or the investment of the assets of any such Benefit Plan (other than routine claims for benefits) is pending, except where the action, suit, proceeding, hearing or investigation would not have a Material Adverse Effect.

(ii) As of the last day of the most recent prior plan year, the market value of assets under each Benefit Plan that is an "employee pension benefit plan" equaled or exceeded the present value of liabilities thereunder (determined in accordance with then current funding assumptions).

(iii) Dictaphone, in respect of the Business, has not incurred any Liability to the Pension Benefit Guaranty Corporation (other than premium payments thereto) or otherwise under Title IV of ERISA (including any withdrawal liability) with respect to any such Benefit Plan that is an "employee pension benefit plan."

3.21 No Guarantees. None of the Liabilities of the Business or of any Seller incurred in connection with the operation of the Business is guaranteed by or subject to a similar contingent obligation of any other Person. Except for ordinary course trade activities with respect to the sale and servicing of products, no Seller with respect to the Business has guaranteed or become subject to a similar contingent obligation in respect of the obligations or Liabilities of any other Person. Except for trade letters of credit and other ordinary course trade activities, there are no outstanding letters of credit, surety bonds or similar instruments of Dictaphone or any of its Affiliates in connection with the Business or the Purchased Assets.

3.22 Certain Business Relationships with the Business. Neither Dictaphone nor any of its stockholders, officers, directors or employees, including any Affiliates thereof, (i) have been involved in any material business arrangement or relationship with the Business within the past twelve (12) months or (ii) own any material asset, tangible or intangible, that is used or held for use in the Business except through the Sellers.

3.23 Disclosure. The representations and warranties contained in Article 3 do not contain any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements and information contained therein not misleading.

3.24 Customers and Suppliers.

(a) Disclosure Schedule Section 3.24(a) lists the 25 largest customers (the "Major Customers") of the Business based on revenues (on a consolidated basis) for the 2004 fiscal year and sets forth opposite the name of each such Major Customer the percentage of revenues of the Business (on a consolidated basis) attributable to each such Major Customer. No

Seller has received any written notice that any such Major Customer has (i) ceased, or will cease, to use the products or services of the Business, (ii) substantially reduced or will substantially reduce, the use of products or services of the Business or (iii) has sought, or is seeking, to reduce the price it will pay for products or services of the Business (other than due to announcements of the transactions contemplated by this Agreement) or that any such Major Customer will not purchase products or services of the Business from the Buyer at any time after the Closing Date on terms and conditions similar to those used in its current purchases from the Business. Disclosure Schedule Section 3.24(a) sets forth as of February 28, 2005 any account or note receivable past ninety (90) days due from any Major Customer.

(b) Since the date of the December 31 Balance Sheet, to the knowledge of Dictaphone, no Seller has received any written or oral notice that there has been any material adverse change in the price of software development services, software products, hardware, raw materials, supplies, merchandise or other goods or services provided by any material supplier of or licensor to the Business or that any such supplier will not sell or license software development services, software products, hardware, raw materials, supplies, merchandise or other goods or services for use in the Business to the Buyer at any time after the Closing Date on terms and conditions similar to those used in its current sales or licenses to the Business.

(c) Except has listed in Disclosure Schedule Section 3.24(c), no Seller is a party to any exclusive distribution agreement or obligation, non−compete agreements, or other agreements which limit the scope of its sales and marketing activities in any geographic area or industry sector in respect of the Business.

3.25 Product Backlog. As of March 31, 2005, the aggregate Product Backlog was Nine Million One Hundred Thousand U.S. Dollars (U.S.$9,100,000). Disclosure Schedule Section 3.25 sets forth, for each order included in Product Backlog, the customer name, product/service description and dollar amount of the revenue associated with such order and the date such order was received. Except as set forth on Disclosure Schedule Section 3.25, all such Product Backlog has been determined on a basis consistent with the Business's historical practices.

3.26 Absence of Certain Business Practices. No Seller nor, to Dictaphone's knowledge, any officer, director, employee, agent or Affiliate of Dictaphone, or any other person acting on their behalf, has, directly or indirectly, within the past five (5) years given or agreed to give any gift or similar benefit to any customer, supplier, governmental employee or other person who is or may be in a position to help or hinder the Business in violation of any Law (i) which subjected or would have subjected any Seller to any damage or penalty in any civil, criminal or governmental litigation or proceeding, (ii) which if not given in the past, would have had a Material Adverse Effect or (iii) which if not continued in the future, would have a Material Adverse Effect or would subject any Seller to suit or penalty in any private or governmental litigation or proceeding.

3.27 Brokers, Finders. Other than Houlihan Lokey Howard & Zukin ("Houlihan"), whose fee may be paid by Dictaphone, no finder, broker, agent or other intermediary acting on behalf of Dictaphone is entitled to a commission, fee or other compensation in connection with the negotiation or consummation of this Agreement or any of the transactions contemplated hereby.

3.28 Amendment to OSS Agreement. Attached hereto as Exhibit G is a true and correct copy of the amendment to the OSS Agreement. The amendment to the OSS Agreement has been duly executed and delivered by Dictaphone and Omnee Systems Software Corporation, and the sole condition to its effectiveness and valid and effective assignment to Buyer are (a) the payment of $1,000,000 by Dictaphone to OSS (the "OSS Payment"), and (b) the Closing.

3.29 No Other Representations or Warranties. Except for the representations and warranties contained in this Article 3, neither Dictaphone, nor any other Person, makes any other express or implied representation or warranty on behalf of Dictaphone or any Affiliate of Dictaphone with respect to the Business, the Purchased Assets, the Assumed Liabilities or otherwise with respect to the subject matter of this Agreement or the Related Agreements.

ARTICLE 4
REPRESENTATIONS AND WARRANTIES OF THE BUYER

The Buyer hereby makes the following representations and warranties to Dictaphone, each of which is true and correct on the date hereof and shall survive the Closing Date and the transactions contemplated hereby to the extent set forth herein.

4.1 Existence and Power.

(a) The Buyer and each Buyer Affiliate has the corporate, partnership, limited liability company or other organizational power and authority, as applicable, to execute and deliver this Agreement and each Related Agreement to which it is a party, to perform its obligations hereunder and thereunder, and to consummate the transactions contemplated hereby and thereby.

(b) The Buyer and each Buyer Affiliate is validly existing and in good standing under the laws of its jurisdiction of formation (to the extent such concept is recognized in such jurisdiction) and each jurisdiction in which the nature of its business makes such qualification necessary, except where the failure to be so qualified and in good standing would not have a material adverse effect on the Buyer or the Buyer Affiliates.

(c) Neither the Buyer nor any Buyer Affiliate is a party to, subject to or bound by any contract, Encumbrance or Law which would (i) be breached or violated or the Buyer's or any Subsidiary's obligations thereunder accelerated or increased (whether or not with notice or lapse of time or both) by the execution or delivery by the Buyer or any Buyer Affiliate of this Agreement (to the extent it is a party hereto) or any Related Agreement to which it is a party or the performance by the Buyer or any Buyer Affiliate of the transactions contemplated hereby (to the extent it is a party hereto) or thereby (to the extent it is a party thereto) or (ii) prevent the carrying out of the transactions contemplated by this Agreement (to the extent it is a party hereto) or by the Related Agreements (to the extent it is a party thereto). Except as provided for in Disclosure Schedule Section 4.1, no permit, consent, waiver, approval or authorization of, or declaration to or filing or registration with, any governmental or regulatory authority or third−party is required in connection with the execution, delivery or performance of this Agreement or any of the Related Agreements by the Buyer or any Buyer Affiliate or the consummation by the Buyer or any Buyer Affiliate of the transactions contemplated by this Agreement (to the extent it is a party hereto) or any Related Agreement to which it is a party, except for any such permits, consents, waivers, approvals, authorizations, declarations, filings or registrations the failure of which to obtain would not have a material adverse effect on the Buyer or upon the consummation of the transactions contemplated by this Agreement or by the Related Agreements.

4.2 Valid and Enforceable Agreement; Authorization. This Agreement and the Related Agreements have been duly executed and delivered by the Buyer and the Buyer Affiliates party thereto and constitute legal, valid and binding obligations of the Buyer and the Buyer Affiliates party thereto, enforceable against the Buyer and the Buyer Affiliates in accordance with their terms, except that such enforcement may be subject to (i) bankruptcy, insolvency, reorganization, moratorium or other similar laws affecting or relating to enforcement of creditors' rights generally and (ii) general principles of equity. The execution and delivery of this Agreement and the consummation of the transactions contemplated hereby have been duly authorized, approved and ratified by all necessary action on the part of the Buyer and the Buyer Affiliates.

4.3 Brokers, Finders. The Buyer shall pay all commissions, fees or other compensation incurred by any finder, broker, agent or other intermediary retained by the Buyer and acting on behalf of the Buyer in connection with the negotiation or consummation of this Agreement or any of the transactions contemplated hereby.

4.4 Litigation. There are no actions, suits, proceedings, orders or investigations pending or, to the Buyer's knowledge, threatened against the Buyer or any of the Buyer Affiliates, at law or in equity, which if adversely determined would have a material adverse effect on the Buyer's or any Buyer Affiliate's performance under this Agreement or any Related Agreement to which it is a party or the consummation of the transactions contemplated hereby or thereby. There are no injunctions, decrees or unsatisfied judgments outstanding against or related to the Buyer or any Buyer Affiliate which could interfere with the Buyer's or any Buyer Affiliate's ability to consummate the transactions contemplated by this Agreement.

4.5 Funds. The Buyer has, and at all times will have, sufficient funds on hand or available pursuant to unconditional commitments to pay the Purchase Price and any Adjustment.

4.6 Amendment to OSS Agreement. The Buyer acknowledges that (a) a true and complete copy of the amendment to the OSS Agreement has been attached by Dictaphone as Exhibit G to this Agreement, (b) the terms and provisions of the amendment to the OSS Agreement attached hereto as Exhibit G are in form and substance satisfactory to the Buyer and (c) no condition to effectiveness of the amendment to the OSS Agreement and its valid and effective assignment to Buyer remains unsatisfied other than the (a) the OSS Payment, and (b) Closing.

4.7 No Other Representations or Warranties. Except for the representations and warranties contained in this Article 4, neither the Buyer, nor any other Person, makes any other express or implied representation or warranty on behalf of the Buyer. By entering into this Agreement, the Buyer acknowledges that it has not relied on, and is not relying on, projections, predictions, forecasts or similar forward−looking statements which were made or prepared by or on behalf of Dictaphone or its Affiliates.

ARTICLE 5
EMPLOYEES

5.1 Access to Employees; Offers of Employment to U.S. Employees.

(a) Offers to U.S. Employees. From and after the date of this Agreement, Dictaphone shall make the General Manager and Vice Presidents of the Business available to Buyer, for the purpose of evaluating U.S. Employees and assisting Buyer in deciding to which U.S. Employees the Buyer and/or a Buyer Affiliate shall make offers of employment. The General Manager, Vice Presidents and Key Employees of the Business shall cooperate with the Buyer to provide the Buyer with reasonable access to the U.S. Employees for the purpose of the Buyer or a Buyer Affiliate interviewing, evaluating and extending offers to certain U.S. Employees; provided, however, that normal conduct of the Business shall not be unreasonably disrupted thereby. The Buyer shall make or cause a Buyer Affiliate to make an offer of employment to those U.S. Employees, other than the Retained Employees, it wishes to hire and shall provide Dictaphone with a list of all such U.S. Employees to whom it has extended offers within twenty (20) Business Days of the date hereof, but in no event later than ten (10) Business Days prior to Closing. The number of U.S. Employees of the Business to whom the Buyer shall make offers within twenty (20) Business Days hereof shall not be less than one hundred fifty (150) U.S. Employees. If any such offers of employment are rejected by any U.S. Employees, the Buyer agrees to extend, or cause a Buyer Affiliate to extend, additional offers of employment in lieu of such original offers of employment to other U.S. Employees who are not Retained Employees and to whom offers of employment have not yet been made, provided, however, that the Buyer and the Buyer Affiliates may, but shall not be required, to extend additional offers (x) to U.S. Employees who are not qualified for the positions with respect to which offers have been made to other U.S. Employees and rejected or (y) to the extent that the aggregate number at any time of offers which have been accepted plus offers which have been extended but neither accepted nor rejected exceeds one hundred fifty (150). The Buyer and the Buyer Affiliates shall extend all such offers of employment to U.S. Employees in good faith and in collaboration with Dictaphone and shall keep Dictaphone and its Vice President of Human Resources informed of all material developments relating to the terms, acceptance, negotiation or rejection of such offers. No Seller shall make any offers to U.S. Employees, who are not Retained Employees, for them to remain in the employ of any Seller after the Closing Date, which offers compete with the Buyer's or any Buyer Affiliate's offers of employment to such Employees. No Seller shall make any offers to employ or engage or otherwise solicit (at any stage) any EU Employee, Swiss Employee or Canadian Employee, in each case, who are not Retained Employees, for them to remain in or transfer to the employ or engagement of any Seller after the Closing Date.

(b) Terms of Offers. The offers of employment referred to in Section 5.1(a) shall be conditioned and effective upon the Effective Time (or, for any U.S. Employee on a leave of absence when offered employment by the Buyer or a Buyer Affiliate, the offer of the Buyer or a Buyer Affiliate may specify that the initial date of employment under such offer shall be effective upon the date of the U.S. Employee's return from the leave of absence). Such offers of employment shall be on terms and conditions to be decided by the Buyer in its sole discretion, provided only that as to each U.S. Employee such terms and conditions may be either (i) comparable with the terms and conditions of such offeree's employment with Dictaphone or a Selling Subsidiary in effect as of the date of this Agreement or (ii) consistent with the customary employment practices of the Buyer or a Buyer Affiliate as of the Effective Time for those of its employees having similar levels of responsibility as such offeree. The Buyer shall provide to Dictaphone, prior to extending any offer of employment to any U.S. Employee and within twenty (20) Business Days after the date hereof, but in no event later than twenty (20) Business Days prior to Closing or with reasonable promptness after extending an offer, the terms and conditions of any offers of employment to any U.S. Employee and shall extend any such offers of employment in consultation with Dictaphone, in a manner that minimizes interruption to the Business and Dictaphone's other businesses and in a manner that encourages U.S. Employees to accept such offers of employment from the Buyer or a Buyer Affiliate. An agreement by the Buyer and Dictaphone as to what constitutes "terms and conditions that are comparable with the terms and conditions of each such U.S. Employee's employment with Dictaphone or a Selling Subsidiary in effect as of the date of this Agreement" for purposes of this Section 5.1(c) shall be set forth in a separate letter agreement between Buyer and Dictaphone, shall be entered into by the Parties within ten (10) Business Days of the date of this Agreement and shall be incorporated by reference in this Section 5.1(c).

(c) Transferred Employees. Those U.S. Employees who accept employment as of the Effective Time with the Buyer or any of its Affiliates are referred to as "Transferred U.S. Employees." Receipt by the Buyer or a Buyer Affiliate of acceptances of employment by less than one hundred thirteen (113) U.S. Employees as of the Effective Time shall constitute the failure of the condition to Closing set forth in Section 7.5; provided, however, that it shall not constitute a failure of such condition to Closing unless all U.S. Employees (except for up to five (5) U.S. Employees) have been offered employment by the Buyer within thirty (30) Business Days after the date of this Agreement on terms and conditions that are comparable with the terms and conditions of each such U.S. Employee's employment with Dictaphone or a Selling Subsidiary in effect as of the date of this Agreement; and provided further, however, that the Buyer shall promptly notify Dictaphone of the receipt by the Buyer or any Buyer Affiliate of any acceptances of employment by any U.S. Employee.

(d) Required Transferred Employees. The Parties acknowledge that, on or prior to the date hereof, the Buyer or a Buyer Affiliate has entered into definitive employment agreements with those U.S. Employees listed on Annex 5.1(d), on terms reasonably satisfactory to the Buyer, which agreements shall become effective upon the Closing and, accordingly, that any condition to Closing in respect thereof has been satisfied. The U.S. Employees listed on Annex 5.1(d) are collectively referred to herein as the "Key Employees."

(e) U.S. Severance. To the extent that the payment of severance benefits or government−required termination liabilities to any Transferred U.S. Employee is required as a result of the consummation of the transactions contemplated by this Agreement and the concurrent transfers of employment, such severance benefits and government−required termination liabilities shall be the sole responsibility of Dictaphone.

(f) Benefits Service, Waiting Periods and Thresholds. The Buyer shall have sole discretion with respect to establishing all rights of Transferred Employees under its Benefit Plans, including credit for service accrued, waiting periods, deductibles and similar thresholds, subject to any Transfer Regulations (as defined at Annex 5.6(a)) applicable to the EU Employees and the Swiss Employees.

5.2 Post−Closing Employment and Employee Benefits.

(a) Transfer of Employment. Effective as of the Effective Time, in accordance with the principles set forth in Sections 5.1(a) and 5.6, the Buyer shall hire each Transferred Employee. In addition, following the Effective Time, the Buyer shall maintain employee benefit plans, programs, policies and arrangements for Transferred Employees (other than the features of any plans or arrangements based on employer equity securities) that are reasonably comparable, in the aggregate, with respect to those Benefit Plans that the Buyer has in effect for its similarly situated employees, subject to any Transfer Regulations (as defined at Annex 5.6(a) applicable to the EU Employees and the Swiss Employees.

(b) Dictaphone U.S. Retirement Benefits.

(i) Dictaphone shall, effective as of the Effective Time, cease benefit accruals for each Transferred U.S. Employee in any tax−qualified and nonqualified defined benefit pension plans maintained by Dictaphone in which such individual is then participating. Dictaphone shall remain solely liable for only those benefits accrued and vested under such pension plans on or prior to the Effective Time.

(ii) Dictaphone shall, effective as of the Effective Time, cease the accrual of additional contributions in respect of each Transferred U.S. Employee to all tax−qualified and nonqualified defined contribution plans maintained by Dictaphone in which such individual is then participating.

(c) U.S. Welfare Benefits.

(i) Dictaphone shall be responsible in accordance with its applicable welfare plans in effect prior to the Effective Time for all medical and dental claims for expenses incurred prior to the Effective Time by Transferred U.S. Employees and their spouses and dependents. Reimbursement for medical and dental expenses associated with such claims shall be determined in accordance with the terms of Dictaphone's medical and dental programs as in effect immediately prior to the Effective Time. The Buyer shall be responsible for all medical and dental claims for expenses incurred on and after the Effective Time by Transferred U.S. Employees and their spouses and dependents pursuant to and in accordance with the terms of plans maintained by the Buyer and in which Transferred U.S. Employees and their spouses and dependents become enrolled following the Effective Time and in accordance with the Buyer's plans and practices for its current employees.

(ii) The Buyer shall be responsible for all other insurance and disability benefit coverage claims of Transferred U.S. Employees and their beneficiaries for claims incurred by such Transferred U.S. Employees on and after the Effective Time under group life, travel, disability accident, and accidental death and dismemberment insurance policies or programs of the Buyer in which Transferred U.S. Employees become enrolled. Dictaphone shall be responsible for claims incurred under policies or programs of Dictaphone by Transferred U.S. Employees prior to the Effective Time. Dictaphone shall also remain responsible for any claims incurred under policies or programs of Dictaphone by Employees who are not Transferred U.S. Employees, whether incurred prior to or after the Effective Time, and Buyer shall have no responsibility or liability for any such claims.

(iii) For purposes of this Section 5.2, the following claims and liabilities shall be deemed to be incurred as follows: (A) life, accidental death and dismemberment and business travel accident insurance benefits, upon the death or accident giving rise to such benefits; (B) hospital−provided health, dental, prescription drug or other benefits that become payable with respect to any hospital confinement shall be allocated between Dictaphone and the Buyer in proportion to the number of days of such hospital confinement that occur before and after the Effective Time; and (C) non−hospital−provided health, dental or prescription drug benefits, upon provision of the related services, materials or supplies.

(d) 401(k) Plan. Transferred U.S. Employees shall be eligible to authorize a direct rollover of their account balances in the Dictaphone 401(k) Plan, including plan loans, to the defined contribution plan maintained by the Buyer, to the extent permitted by the terms and conditions of the defined contribution plan maintained by the Buyer and subject to the Buyer's receipt as of the Closing Date of a copy of an up−to−date favorable determination letter issued by the IRS with respect to the Dictaphone 401(k) Plan (so long as it is favorable).

(e) Flexible Spending Accounts. The Buyer shall cover Transferred U.S. Employees who have elected to participate in Dictaphone's Flexible Spending Account ("Dictaphone's FSA") under the Buyer's Flexible Spending Account ("Buyer's FSA") at the same level of coverage provided under Dictaphone's FSA, but solely to the extent currently offered to Buyer's U.S. employees. Transferred U.S. Employees shall be treated as if their participation in Buyer's FSA had been continuous from the beginning of Dictaphone's plan year in which the Effective Time falls and their existing salary reduction elections shall be taken into account for the remainder of the Buyer's plan year in which the Effective Time falls as if made under the Buyer's FSA. The Buyer's FSA shall provide reimbursement for eligible expenses incurred by Transferred U.S. Employees at any time during Dictaphone's plan year in which the Effective Time falls (including, to the extent permissible under applicable law and the terms of Buyer's FSA, claims incurred before the Effective Time), up to the amount of such Transferred U.S. Employees' elections and reduced by amounts previously reimbursed by Dictaphone's FSA. As soon as administratively feasible after the end of the calendar year in which the Effective Time occurs, the Buyer and Dictaphone shall reconcile the FSA account balances of Transferred U.S. Employees under the Buyer's and Dictaphone's respective FSAs for such calendar year and shall make payment to one another so that they share, based on the portion of the plan year each employed the Transferred U.S. Employees who participated in the FSA, the amount of any net loss or net surplus resulting from the aggregate claims paid from the flexible spending accounts of the Transferred U.S. Employees under the Buyer's FSA and Dictaphone's FSA, after giving effect to the aggregate amount of the contributions received by the Buyer and Dictaphone from such Transferred U.S. Employees under the Buyer's and Dictaphone's FSA, respectively. Within fifteen (15) Business Days after the Closing Date, Dictaphone shall provide to Buyer a detailed summary of the amounts of employee contributions to, and all claims filed and paid under, Dictaphone's FSA between January 1, 2005 and the day before the Closing Date.

(f) U.S. Workers' Compensation. The Buyer's workers' compensation program shall be responsible for all claims for workers' compensation benefits which are incurred after the Effective Time by participating Transferred U.S. Employees. Subject to Section 5.6, Dictaphone shall remain responsible for all claims for such benefits that are incurred prior to the Effective Time by Employees, regardless of when such claims are submitted.

(g) Responsibilities Under WARN. Dictaphone shall be responsible for providing or discharging any and all notifications, benefits and liabilities to U.S. Employees and governmental authorities required by the Worker Adjustment and Retraining Notification Act ("WARN") or by any other applicable Law in the United States relating to plant closings or employee separations or severance pay that are required to be provided as a result of the consummation of the transactions contemplated by this Agreement, regardless of whether such separations or layoffs occur prior to or after the Closing Date.

5.3 U.S. Employees Vacation Pay. No later than sixteen (16) calendar days after the end of the Dictaphone employee payroll period in which the Closing occurs, Dictaphone shall make a cash payment to each Transferred U.S. Employee who, as of the Effective Time, has any accrued but unused vacation time pursuant to the vacation policy applicable to each such Transferred U.S. Employee immediately prior to the Effective Time. The Buyer shall assume no liability whatsoever for any such pre−Effective Time accrued vacation.

5.4 Transfer of U.S. Employee Withholding. Dictaphone and the Buyer agree to comply with the alternate procedure described in Section 5 of Revenue Procedure 2004−53. With respect to wages paid after the Closing Date by the Buyer to the Transferred U.S. Employees, the Buyer shall, in accordance with Revenue Procedure 2004−53, assume all responsibility for preparing and filing: Form W−2, Wage and Tax Statements; Form W−3, Transmittal of Income and Tax Statements; Form 941, Employer's Quarterly Federal Tax Returns; Form W−4, Employee's Withholding Allowance Certificates; and Form W−5, Earned Income Credit Advance Payment Certificates. Dictaphone and the Buyer shall cooperate in good faith to the extent necessary to permit each of them to comply with the alternate procedure.

5.5 Transfer of U.S. Unemployment Insurance Rate and Base. Dictaphone shall execute such documents as are necessary in order to transfer and assign to the Buyer all state unemployment insurance wage bases and experience and tax rates in respect of the Business with regard to the calendar year that includes the Closing Date.

5.6 Non−U.S. Employees.

(a) EU Employees and Swiss Employees. Annex 5.6(a) sets forth the provisions in relation to any and all EU Employees and Swiss Employees. In the event of any conflict between the provisions of Sections 5.1 through 5.5 and the provisions of Annex 5.6(a), the provisions of Annex 5.6(a) shall prevail.

(b) Canadian Employees. Unless otherwise specifically provided herein, the Canadian Employees will be subject to the same terms and provisions as the U.S. Employees; provided, however, that the Buyer shall only be required to make or cause a Buyer Affiliate to make an offer of employment to one Canadian Employee, other than a Retained Employee, within twenty (20) Business Days hereof. To the extent that the payment of severance benefits or government−required termination liabilities to any Canadian Employee is required as a result of the consummation of the transactions contemplated by this Agreement and any concurrent or deemed transfers of employment, such severance benefits and government−required termination liabilities shall be the sole responsibility of Dictaphone.

(c) Singapore Employees. The Buyer shall not be required to make or cause a Buyer Affiliate to make an offer of employment to any Singapore Employee. To the extent that the payment of compensation, severance benefits or government−required termination liabilities to any Singapore Employee is required as a result of the consummation of the transactions contemplated by this Agreement and any deemed transfers of employment, such severance benefits and government−required termination liabilities shall be the sole responsibility of Dictaphone.

(d) Compliance. The Buyer will and will cause each of the Buyer Affiliates to extend offers of employment to EU Employees, Swiss Employees and Canadian Employees on a basis which will not violate non−discrimination laws applicable to the Buyer or the relevant Buyer Affiliates, as the case may be.

5.7 Non−Solicitation. From the date of this Agreement through the end of the twelve (12) month period commencing with the Effective Time:

(a) neither Dictaphone nor any of its Affiliates shall directly or indirectly, endeavor to entice away, make any offer of employment or engagement to, or otherwise solicit the employment or engagement of, any Employee other than a Retained Employee, without the prior written consent of the Buyer, provided that such restriction shall terminate upon the Closing as to any Employee who is not a Transferred Employee;

(b) Dictaphone shall not solicit the employment of any Transferred Employee without the prior written consent of the Buyer; and

(c) neither the Buyer nor any of its Affiliates shall directly or indirectly, endeavor to entice away, make any offer of employment or engagement to, or otherwise solicit the employment or engagement, in connection with the Business, of any Retained Employee without the prior written consent of Dictaphone.

For the purposes set forth in this Section 5.7, general advertising which is not specifically directed at any Transferred Employee shall not be considered solicitation.

ARTICLE 6
ADDITIONAL COVENANTS OF THE PARTIES

6.1 Conduct of Business Until Closing. Except as otherwise provided in this Agreement or as the Buyer may otherwise consent to or approve in writing on and after the date hereof and prior to the Closing Date (which consent shall not be unreasonably withheld) Dictaphone shall, and shall cause the Selling Subsidiaries to, in respect of the Business:

(a) not enter into any discussions or effect any transactions relating to the disposition of any material part of the Purchased Assets, other than products or services in the Ordinary Course; provided, however, that, for purposes of this Section 6.1(a), transactions with respect to the sale of any product of the Business the price of which is greater than Two Hundred Thousand U.S. Dollars ($200,000) and the product margin of which is below forty percent (40%), customer rights to replace products of the Business with products of Buyer either prior to or after installation or other non−standard rights of customers of the Business, including the right to receive free multiple−year maintenance, shall be deemed not in the Ordinary Course;

(b) (i) conduct its business, operations, activities and practices in all material respects in the Ordinary Course and consistent with past practice, (ii) use commercially reasonable efforts to preserve its current business organization and existing business relationships in all material respects, and (iii) maintain its property in substantially the condition as currently existing, normal wear and tear excepted;

(c) not enter into, terminate or amend in any material respect any Material Contract (except to the extent necessary to obtain the consents for assignment and transfer contemplated by this Agreement);

(d) not sell, license or transfer any Business Intellectual Property other than as part of a sale of products or services in the Ordinary Course;

(e) not issue any letters of credit in excess of $50,000, individually or in the aggregate;

(f) not make any new tax elections or change any existing tax elections with respect to the Business;

(g) not enter into any new, or vary or revoke the terms of any existing, contract, agreement, plan, program or arrangement with any EU Employee or Swiss Employee or any trade union or other body collectively representing any EU Employee or Swiss Employee, or make any offer of employment or engagement in the Business to any person who would, upon acceptance thereof, be an EU Employee, a Swiss Employee or an Employee otherwise based outside the United States; and

(h) not enter into any agreement (conditional or otherwise) to do any of the foregoing.

For purposes of this Section 6.1, consent or approval in writing of the Buyer shall be evidenced only by a written consent or approval signed by the Buyer's President.

6.2 Books and Records. From and after the Closing, the Buyer shall provide Dictaphone and its representatives with reasonable access, during normal business hours, to all books and records of the Business, including accounting and Tax records, sales and purchase documents, notes, memoranda, and any other electronic or written data ("Records") pertaining or relating to the period prior to the Effective Time as is reasonably necessary for (a) financial reporting, Tax and accounting matters, and the preparation and filing of any returns, reports or forms, (b) defending any claim or assessment against Dictaphone or its Affiliates, (c) asserting any claims which Dictaphone or its Affiliates may have or (d) complying with any Law or governmental or judicial order. To the extent deemed necessary by Dictaphone and its Affiliates with respect to their other business operations, Dictaphone and its Affiliates may retain copies of such Records prior to providing the originals to the Buyer or, as soon as practicable after Closing, the Buyer shall provide to Dictaphone and its Affiliates copies of all or any portion of such Records as requested by Dictaphone and its Affiliates. Unless otherwise consented to in writing by Dictaphone, the Buyer shall not, for a period of seven (7) years following the date hereof or such longer period as retention thereof is required by applicable Law, destroy, alter or otherwise dispose of (or allow the destruction, alteration or disposal of) any of the Records without first offering (which offer shall remain open for at least ninety (90) days) to surrender to Dictaphone such Records.

6.3 Confidentiality.

(a) In lieu of the terms, provisions and covenants of (x) the Confidentiality Agreement dated July 12, 2004 between the Buyer and Houlihan (with Dictaphone being a third party beneficiary) and (y) the Confidential Non−Disclosure Agreement dated January 1, 2004 between the Buyer and Dictaphone, which Confidentiality Agreement and Confidential Non−Disclosure Agreement and Dictaphone's rights thereunder are hereby terminated, the Buyer acknowledges that, in the course of its investigations of the Business, the Buyer and its representatives have and will become aware of confidential information and documents of Dictaphone and its Affiliates, the Business and the Other Dictaphone Businesses, and that its use of such confidential information and documents, or communication of such information to third parties, could be detrimental to Dictaphone and its Affiliates, the Business and the Other Dictaphone Businesses. The Buyer covenants that (1) prior to the Closing (including after termination of this Agreement without the Closing having taken place), all information and documents concerning Dictaphone and its Affiliates, the Business and the Other Dictaphone Businesses received or reviewed by the Buyer, its Affiliates or its representatives in connection with this Agreement, any Related Agreement or the transactions contemplated hereby and (2) following the Closing, all such information and documents to the extent related to any of the Excluded Assets, the Retained Liabilities or the Other Dictaphone Businesses shall be maintained in confidence and shall not be disclosed or used by the Buyer, its Affiliates or its representatives without Dictaphone's prior written consent, unless such information is (i) otherwise publicly available, (ii) required to be disclosed pursuant to judicial order or applicable Law, (iii) required to be disclosed by the rules of a securities exchange on which the securities of the Buyer or a controlling Affiliate of the Buyer may from time to time be listed or (iv) disclosed to any Person that proposes to finance, in whole or in part, the purchase of the Purchased Assets or the operations of the Buyer or of its controlling Affiliates, solely for the purpose of permitting such Person to evaluate the advisability of providing such financing. In the event that the Buyer or any of its Affiliates or representatives becomes legally compelled to disclose any information or documents referred to in this Section 6.3(a), the Buyer shall provide Dictaphone with prompt written notice before such disclosure, sufficient to enable Dictaphone, at its expense, either to seek a protective order or other appropriate remedy preventing or limiting such disclosure or to waive compliance with the provisions of this Section 6.3(a) or both. The Buyer shall cause its Affiliates and representatives to comply with this Section 6.3(a) and shall be responsible for any breach thereof by them.

(b) Following the Closing, Dictaphone shall and shall cause its Affiliates and representatives to maintain in confidence any information it or they may have or receive in relation to the Business or in connection with the Related Agreements, other than with respect to the Excluded Assets, the Retained Liabilities and the Other Dictaphone Businesses, and not disclose or use such information without the Buyer's prior written consent, unless such information is (i) otherwise publicly available, (ii) required to be disclosed pursuant to judicial order or applicable Law or (iii) required to be disclosed by the rules of a securities exchange on which the securities of Dictaphone or a controlling Affiliate of Dictaphone may be from time to time listed. In the event that Dictaphone or its Affiliates and representatives become legally compelled to disclose any information or documents referred to in this Section 6.3(b), Dictaphone shall, to the extent reasonably practicable, provide the Buyer with prompt written notice before such disclosure, sufficient to enable the Buyer, at its expense, either to seek a protective order or other appropriate remedy preventing or prohibiting such disclosure or to waive compliance with the provisions of this Section 6.3(b) or both.

(c) Until after the Effective Time, no press release or other public statement concerning the negotiation, execution and delivery of this Agreement or the transactions contemplated hereby shall be issued or made without the prior approval of both Dictaphone and the Buyer (which approval shall not be unreasonably withheld), except to the extent necessary or advisable to comply with accounting rules, rules of the Securities and Exchange Commission or the National Association of Securities Dealers, Inc., or other disclosure obligations imposed by Law.

6.4 Filings; Further Assurances and Cooperation.

(a) Prior to the Closing, the Parties shall proceed expeditiously and in good faith to make such filings and take such other actions as may be reasonably necessary to satisfy the conditions to Closing set forth in Sections 7.2 and 8.2, if any. The Parties also acknowledge and agree that they have each independently concluded on the basis of the information available to each Party that no filings with respect to the transactions contemplated hereby are required to be made pursuant to the Hart−Scott−Rodino Antitrust Improvements Act of 1976, as amended, the competition or antitrust laws of the jurisdictions listed on Disclosure Schedule Section 6.4(a), or Section 5021 of the Omnibus Trade and Competitiveness Act of 1988, as amended by Section 721 of the Defense Production Act of 1950. The Buyer acknowledges that it has independently concluded that no filings with respect to the transactions contemplated hereby are required to be made by either Party pursuant to Israeli Laws, and Dictaphone acknowledges that it is not relying on the Buyer's independent conclusion as it relates to any filing obligations of Dictaphone under Israeli Laws.

(b) In connection with each Party's obligations under Section 6.4(a), each Party agrees to (i) cooperate and collaborate with the other Party in preparing and filing any submission to be made to any governmental authority and in responding to any comments, requests for information or inquires therefrom, (ii) notify promptly the other Party of any comments, requests or inquiries made by a governmental authority, (iii) provide copies of all written submissions to and communications with or from any governmental authority to the other Party and (iv) permit the other Party and its advisors to participate in discussions, and attend meetings, with any governmental authority.

(c) On or after the Closing Date, the Parties shall, on request, cooperate with one another by furnishing any additional information, executing and delivering any additional documents and instruments, including contract assignments, and doing any and all such other things as may be reasonably required by the Parties or their counsel to consummate or otherwise implement the transactions contemplated by this Agreement. In connection with the Assumed Liabilities and the Retained Liabilities, each of the Parties shall, and shall cause their Affiliates and employees to, aid, cooperate with and assist the other Party in its defense thereof by, among other things, providing such other Party with full access to pertinent records at such times as such other Party may reasonably request.

6.5 Covenant Not to Compete.

(a) For the period beginning on the Closing Date and ending on the fifth (5^{th}) anniversary thereof (the "Non−Compete Period"), neither Dictaphone nor an Affiliate of Dictaphone shall engage, directly or indirectly, in any business or activity which competes directly or indirectly with the Business ("Competitive Activities"); provided, however, that this covenant shall not be deemed to have been breached as a result of the ownership by Dictaphone or an Affiliate of Dictaphone of: (i) less than an aggregate of 5% of any class of stock of a Person engaged, directly or indirectly, in Competitive Activities; or (ii) a Person which engages, directly or indirectly, in Competitive Activities if such Competitive Activities account for less than Five Million Dollars ($5,000,000) or less than 5% of such Person's consolidated annual revenues (or, if the Competitive Activities of a Person described in this clause (a) account for 5% or more, but in any event no more than 20%, of such Person's consolidated annual revenues and such Person is acquired after the date hereof, within one (1) year following the consummation of such acquisition by Dictaphone or one or more of its Affiliates, Competitive Activities account for less than 5% of such Person's consolidated annual revenues).

(b) Without limiting the remedies otherwise available, the Parties agree that damages at law would be an insufficient remedy in the event of breach of this Section 6.5 and that the injured party should be entitled to injunctive relief or other equitable remedies in the event of any such breach.

(c) If any of the provisions of this Section 6.5 are held to be unenforceable in any jurisdiction, then, as to such jurisdiction, such provision shall be ineffective to the extent of its unenforceability in such jurisdiction, without affecting the remaining provisions of this Section 6.5 in such jurisdiction or affecting in any other jurisdiction the validity or enforceability of such provision or of this Section 6.5.

(d) Notwithstanding any provision of this Agreement to the contrary, neither this Section 6.5 nor Section 5.7 will apply to a Dictaphone Successor's businesses, operations or activities (i) existing as of the date such Person becomes a Dictaphone Successor, (ii) acquired after the date such Person becomes a Dictaphone Successor or (iii) developed or expanded any time after such Person becomes a Dictaphone Successor to the extent that such developments or expansions are not derived from the businesses, operations or activities of Dictaphone and its Affiliates as of the time such Person becomes a Dictaphone Successor; provided, however, that, in the case of each of clauses (i), (ii) and (iii) above, such Dictaphone Successor does not use the assets or exercise any of the rights licensed under Section 2.1 of the Manufacturing Agreement, Section 2 of the Technology License Agreement or Section 2.8 of the Services Agreement in competition with the Business as currently conducted or as currently proposed to be conducted by Dictaphone. The foregoing proviso shall be in addition to and not in limitation of the restrictions on use of those assets and rights licensed to Dictaphone under the Manufacturing Agreement, Technology License Agreement and the Services Agreement. At the Buyer's request, a senior executive officer of each of Dictaphone and a Dictaphone Successor, if any, shall certify in writing to the Buyer that Dictaphone and the Dictaphone Successor, as applicable, are in compliance with the terms and provisions of this Section 6.5; provided, however, that neither Dictaphone nor a Dictaphone Successor are required to provide to the Buyer such certification more often than once within any nine (9) month period.

6.6 Notice of Developments. Dictaphone may elect at any time prior to the Closing to notify the Buyer of any development or other information occurring after the date hereof in the Ordinary Course which renders any representation, warranty or statement contained in this Agreement or any Disclosure Schedule or Annex inaccurate or incomplete at any time prior to the Closing, including any such development or information which first becomes known to Dictaphone after the date hereof. The written notice pursuant to this Section 6.6 shall be deemed to have amended the Disclosure Schedules or Annexes, to have qualified the representations and warranties contained in this Agreement, and to have cured any misrepresentation or breach of warranty that otherwise might have existed hereunder by reason of the development or information.

6.7 Delivery of Audited Financial Statements, Closing Date Balance Sheet and Interim 2005 Financial Statements.

(a) Not less than five (5) Business Days prior to the Closing Date, Dictaphone, at its own expense, shall have prepared and delivered to the Buyer (i) the Audited Financial Statements, which Audited Financial Statements shall conform to the representations and warranties with respect thereto set forth in Section 3.4(b) and (ii) the Auditor's Report thereon. After the Closing Date, Dictaphone shall, upon request, cooperate with the Buyer in obtaining, at any time or from time to time (with respect to no more than six (6) separate filings with the United States Securities and Exchange Commission) until December 31, 2006, from the independent auditor that prepared the Audited Report a letter from such independent auditor consenting to the use of the Auditor's Report in future filings by the Buyer with the U.S. Securities and Exchange Commission and Israeli Securities Authority (the "Auditor's Consent"). The Buyer shall be responsible for all fees and disbursements billed by the auditor for its services in providing any Auditor's Consent.

(b) Dictaphone shall deliver the Estimated Closing Date Balance Sheet and Closing Date Balance Sheet as specified in Section 2.5(b).

(c) Within sixty (60) calendar days of the Closing Date, Dictaphone, at its own expense, shall have prepare and deliver to the Buyer unaudited financial statements relating to the Business, prepared in accordance with U.S. GAAP and the applicable requirements of Rule 3−05 of Regulation S−X, consisting of the adjusted balance sheet of the Business as of the end of the fiscal quarter ending immediately prior to the Closing Date and the related adjusted statement of operations and statement of cash flows for each of the three−month periods then ended (the "Interim 2005 Financial Statements").

(d) The Interim 2005 Financial Statements (a) will be derived from the books and records of the Business and (b) will fairly present, in all material respects, the financial position and results of operations of the Business at the dates and for the periods indicated in accordance with U.S. GAAP and the applicable requirements of Rule 3−05 of Regulation S−X, except as described in Disclosure Schedule Section 3.4(a). The balance sheets included in the Interim 2005 Financial Statements will not include any material assets or liabilities not intended to constitute a part of the Business or the Purchased Assets after giving effect to the transactions contemplated hereby. The statements of profit and loss included in the Interim 2005 Financial Statements will not reflect the operations of any Person or business not intended to constitute a part of the Business after giving effect to the transactions contemplated hereby.

6.8 Commencement of Transition Planning and Services; Execution and Delivery of Transition Services Agreement. From and after the execution of this Agreement and through the Closing Date, Dictaphone shall, on request, cooperate with the Buyer to plan and establish the framework for prompt and effective transition at the Effective Time of management information systems and other information, documentation and control systems relating to the Business in a manner consistent with Buyer's effective operation of the Business, effective use by Buyer of all Purchased Assets and the objectives of the Transition Services/Shared Services Agreements. The parties are simultaneously herewith executing and delivering to each other a copy of the form of Transition Services Agreement attached hereto as part of Exhibit D, with the intent and agreement that the provisions of the Transition Services Agreement shall be implemented from and after the date of this Agreement, except to the extent specified in the Transition Services Agreement as being effective only upon the Closing Date. Each Party shall bear its own expenses in connection with any transition planning services under this Section 6.8.

6.9 Renegotiation of Certain Contracts; Assignment of Certain Rights. From and after the execution of this Agreement and through the Closing Date, Dictaphone and the Buyer shall use commercially reasonable efforts to obtain consent to assignment of each of the Contracts or other commercial understandings listed on Annex 6.9(a) and to amend each of such Contracts or other commercial understandings on the terms described therein or otherwise mutually agreed by the Parties. Neither Party is required to incur any material expenses in connection with assigning or amending any of such Contracts pursuant to this Section 6.9. The Parties acknowledge that a consent to assignment of each of the Contracts listed on Annex 6.9(b) has been obtained, in each case in a form acceptable to each Party and, accordingly, that any condition to Closing in respect thereof has been satisfied.

6.10 Certain Patents. Without limiting Buyer's rights and remedies under Section 6.5, Dictaphone agrees that for the period beginning on the Closing Date and ending on the third (3rd) anniversary thereof, Dictaphone shall not, and shall not permit any Affiliate or successor in interest, to grant to Voice Print International, Inc., Mercom Systems, Inc., ASC Incorporated, E−Talk, Witness Systems, Inc., Verint Systems, Inc. or their respective known Affiliates a license or any other rights, anywhere in the world, to make, have made, use or sell products in competition with the Business embodying any invention described in and claimed in the patents or patent applications listed on Annex 6.10 or any patent foreign or domestic claiming priority therefrom.

6.11 Omitted IP. Without limiting Buyer's rights and remedies under Section 6.5:

(a) In order to address the possibility that Dictaphone may retain rights to Intellectual Property actually used in or covering the Business as of the Closing Date, which rights are not being transferred, assigned or licensed to the Buyer pursuant to this Agreement (the "Omitted IP"), Dictaphone hereby grants to the Buyer, effective from and after, and conditional upon the consummation of, the Closing, a license to all Omitted IP solely for use in the operation of the Business as presently conducted and as currently proposed to be conducted by Dictaphone absent the transactions contemplated by this Agreement ("Business Use"), such license being a perpetual, worldwide, irrevocable, royalty−free license; provided, however, that, subject to the remainder of this Section 6.11(a), the foregoing license shall be exclusive solely for Business Use, even as to Dictaphone, during the period commencing on the Closing Date and ending on the fifth (5th) anniversary of the Closing Date, and non−exclusive thereafter (the "Omitted IP License"). Notwithstanding the foregoing, neither Dictaphone nor any Dictaphone Affiliate or their respective successors shall be in breach or violation of the exclusivity granted by the preceding sentence, and shall have no liability, as a result of any act or omission committed prior to Dictaphone's (or any successor's) receipt of notice from the Buyer or Dictaphone's (or any successor's) otherwise gaining actual knowledge that Intellectual Property retained by Dictaphone is Omitted IP.

(b) Dictaphone further agrees that Dictaphone, its Affiliates or any successor in interest (i) shall not file a claim, lawsuit or other action against the Buyer or any Affiliate of the Buyer alleging that the Buyer or an Affiliate of the Buyer, in exercising the rights expressly granted by the Omitted IP License, is infringing or otherwise violating any rights in any Omitted IP and (ii) effective as of the Closing Date, unconditionally release Buyer and its Affiliates from any and all claims of infringement arising from any such Omitted IP for acts in the conduct of the Business that occurred prior to the granting of a license under this Section, including any and all claims which are known or unknown, absolute or contingent, direct or indirect, in contract, tort or otherwise.

(c) The license contemplated by this Section 6.11 is intended to be, and shall at all times be construed by the parties as being, within the scope of the provisions of Section 365(n) of the U.S. Bankruptcy Code.

(d) Any dispute arising under this Section 6.11 shall be resolved in accordance with the procedures established by Section 11.9 of this Agreement.

6.12 Accounts Receivable Collections Assistance. Commencing from the date hereof, Dictaphone shall promptly forward to the Buyer copies of any communications or other information received by Dictaphone in respect of any Accounts Receivable or Accounts Payable related to the Business. Any amounts received by Dictaphone in respect of any Accounts Receivable related to the Business shall be held in trust for the Buyer. No later than thirty (30) calendar days following the end of each calendar month in which Dictaphone has received amounts in respect of Accounts Receivable related to the Business, Dictaphone shall provide to the Buyer a schedule setting forth such amounts (the "Section 6.12 Schedule") and remit such amounts to the Buyer. Dictaphone shall, as promptly as practicable, forward to the Buyer any telephone calls, orders, notices, requests, inquiries and other communications relating to the Business that Dictaphone may receive following the Closing. Dictaphone shall provide the Buyer with reasonable access to (i) all the underlying documentation and records used by Dictaphone and its auditors in preparing the Section 6.12 Schedule and all other records of the Sellers reasonably related to the preparation of the Section 6.12 Schedule, (ii) the employees of the Sellers who assisted in preparation of the Section 6.12 Schedule and (iii) the work papers of Dictaphone's accountants or auditor related to their review of the Section 6.12 Schedule.

6.13 Accounts Payable and Accrued Expenses. Buyer and Dictaphone will establish mutually acceptable procedures for the review and verification of accounts payable and accrued expenses presented to Buyer by Dictaphone for payment by Buyer as bona fide accounts payable and accrued expenses of the Business, including review of whether and to what extent allocation to the Business of third−party invoices addressed to Dictaphone is appropriate, which procedures established mutually by the Parties shall be set forth on Annex 6.13. In the absence of such agreed−upon procedures, Dictaphone acknowledges that Buyer shall be required to discharge when due accounts payable and accrued expenses only to the extent evidenced by an open invoice or other appropriate documentation either reasonably satisfactory to Buyer or consistent with generally accepted auditing standards in the United States. For the avoidance of doubt, the Parties acknowledge that any such agreed−upon procedures or any payment by Buyer shall by itself not be determinative as to the appropriate carrying value of the Assumed Liabilities on the Closing Date Balance Sheet, which value shall be determined in accordance with the provisions of Section 2.5(b).

6.14 Insurance Coverage. Dictaphone (a) represents and warrants that it has maintained since December 1, 2003 and will maintain through the Closing Date occurrence based product liability insurance in the amount of not less than $5 million with respect to products of the Business sold by Dictaphone prior to the Closing Date, and (b) agrees to maintain a claims made errors and omissions tail policy for a period of thirty six (36) months after the Closing Date in the amount of $5 million with respect to services of the Business provided by Dictaphone prior to the Closing Date; provided, however, that the premiums, fees and expenses incurred by Dictaphone in connection with this Section 6.14 with respect to the tail policy insurance covering services of the Business will be paid fifty percent (50%) by the Buyer, on the one hand, and fifty percent (50%) by Dictaphone, on the other hand. In addition to the Buyer's obligations under the last sentence of Section 2.4, the Buyer agrees to use commercially reasonable efforts to cooperate with Dictaphone to minimize the amount of any losses for which a claim may be made under the insurance coverage obtained and maintained under this Section 6.14, including providing replacement products manufactured by EMS at cost and other products and services at the lesser of (y) fifty percent (50%) of list price or (z) prices no less favorable than those generally made available to most−favored customers of the Business at that time.

6.15 Bulk Sales Laws. The Buyer and Dictaphone agree, on behalf of themselves and their respective Affiliates, to waive compliance with the requirements of any bulk sales or transfer laws or similar laws of any jurisdiction which may be applicable to the transactions contemplated by this Agreement and the Subsidiary Asset Purchase Agreements.

ARTICLE 7
CONDITIONS PRECEDENT TO OBLIGATIONS OF THE BUYER

The obligation of the Buyer to proceed with the Closing shall be subject to the satisfaction, on or prior to the Closing Date, of each of the following conditions precedent, any of which may be waived in whole or in part by the Buyer:

7.1 Accuracy of Representations and Warranties and Performance of Obligations. All representations and warranties made by Dictaphone in this Agreement shall be true and correct in all material respects, except for those representations and warranties that are qualified as to materiality which shall be true and correct in all respects, on and as of the Closing Date with the same effect as if such representations and warranties had been made on and as of the Closing Date, except to the extent that any such representation or warranty by its terms relates to an earlier date and except to the extent of any change permitted by the terms of this Agreement (excluding the delivery of a notice by Dictaphone pursuant to Section 6.6) or consented to by the Buyer. Dictaphone shall have performed or complied in all material respects with all covenants, agreements and conditions contained in this Agreement on its part required to be performed or complied with at or prior to the Closing. Dictaphone shall have delivered to the Buyer at the Closing a certificate of a senior executive officer of Dictaphone certifying that the conditions stated in this Section 7.1 have been fulfilled.

7.2 Consents and Approvals. All material filings required to be made by Dictaphone or the Buyer with any government or governmental authority in connection with the transactions contemplated in this Agreement shall have been made and all necessary authorizations, consents or approvals required from any government or governmental authority shall have been obtained and shall be in full force and effect, other than those set forth on Disclosure Schedule Sections 3.1 and 4.1.

7.3 No Contrary Judgment. On the Closing Date, there shall exist no valid judicial or regulatory order or directive which prohibits the consummation of the transactions contemplated by this Agreement.

7.4 No Material Adverse Effect. From the date of this Agreement to the Closing Date, there shall not have been any event, condition, change, development or effect that has had, or would, or is reasonably expected to, constitute a Material Adverse Effect.

7.5 Minimum Number of Offers Accepted. Buyer and any Buyer Affiliate shall have received, in the aggregate, acceptances of employment by not less than one hundred thirteen (113) U.S. Employees as of the Effective Time, subject to the provisions of Section 5.1(c) with respect to the satisfaction of this condition.

7.6 Deliveries. Dictaphone shall have made or tendered, or caused to be made or tendered, delivery to the Buyer or a Buyer Affiliate, as appropriate, of the following documents:

(a) a counterpart signature page to each Related Agreement (other than the Transition Services Agreement), duly executed by each Seller party thereto, as applicable;

(b) bills of sale or other applicable documents of transfer necessary to effect the sale and transfer of the Tangible Business Assets, the Inventory and any other Purchased Assets that are tangible property as required hereby, duly executed by each Seller party thereto, as applicable;

(c) a counterpart signature page to any assignment agreement, assumption agreement and other applicable document of transfer and assumption necessary to effect the sale and transfer of the Business Intellectual Property, the Assigned Contracts, the Accounts Receivable, the Records and any other Purchased Assets as required hereby, duly executed by each Seller party thereto, as applicable; provided, however, that in connection with the assignment and transfer of the Assigned Contracts, each Seller, Buyer and Buyer Affiliate, as applicable, shall, subject to Section 2.10, execute a single assignment and assumption agreement as to all of the Assigned Contracts other than those listed on Annex 6.9(b) and any other Assigned Contracts mutually agreed to;

(d) UCC−3 termination statements and releases and consents of all lenders to the Sellers who hold an Encumbrance with respect to any of the Purchased Assets;

(e) copies, certified by the Secretary or Assistant Secretary of Dictaphone, of (i) resolutions duly adopted by the board of directors of Dictaphone approving this Agreement, the Related Agreements and the consummation of the transactions contemplated thereby, (ii) Dictaphone's charter and (iii) Dictaphone's bylaws;

(f) a certificate of a senior executive officer of Dictaphone pursuant to Section 7.1;

(g) the Audited Financial Statements and Auditor's Report thereon;

(h) the Estimated Closing Date Balance Sheet;

(i) to the extent required by Section 6.7, the Interim 2005 Financial Statements;

(j) a counterpart signature page to the Termination Agreement, duly executed by Dictaphone;

(k) evidence, reasonably satisfactory to Buyer, of receipt by OSS of the OSS Payment (Buyer acknowledging that this condition may be alternatively satisfied by an appropriate attorney or other escrow arrangement with respect to the OSS Payment and the Purchase Price reasonably satisfactory to both Buyer and Dictaphone); and

(l) such other patent and trademark assignments, assignments of licenses and other customary documents, instruments or certificates as shall be reasonably requested by the Buyer and as shall be consistent with the terms of this Agreement.

ARTICLE 8
CONDITIONS PRECEDENT TO OBLIGATIONS OF DICTAPHONE

The obligation of Dictaphone to proceed with the Closing shall be subject to the satisfaction, on or prior to the Closing Date, of each of the following conditions precedent, any of which may be waived in whole or in part by Dictaphone:

8.1 Accuracy of Representations and Warranties and Performance of Obligations. All representations and warranties made by the Buyer in this Agreement shall be true and correct in all material respects, except for those representations and warranties that are qualified as to materiality which shall be true and correct in all respects, on and as of the Closing Date with the same effect as if such representations and warranties had been made on and as of the Closing Date, except to the extent that any such representation or warranty by its terms relates to an earlier date and except to the extent of any change permitted by the terms of this Agreement or consented to by Dictaphone. The Buyer shall have performed or complied in all material respects with all covenants, agreements and conditions contained in this Agreement on its part required to be performed or complied with at or prior to the Closing. The Buyer shall have delivered to Dictaphone at the Closing a certificate of a senior executive officer of the Buyer certifying that the conditions stated in this Section 8.1 have been fulfilled.

8.2 Consents and Approvals. All material filings required to be made by Dictaphone or the Buyer with any government or governmental authority in connection with the transactions contemplated in this Agreement shall have been made and all necessary authorizations, consents or approvals required from any government or governmental authority shall have been obtained and shall be in full force and effect, other than those set forth in Disclosure Schedule Sections 3.1 and 4.1.

8.3 No Contrary Judgment. On the Closing Date, there shall exist no valid judicial or regulatory order or directive which prohibits the consummation of the transactions contemplated by this Agreement.

8.4 Deliveries. The Buyer shall have made or tendered, or caused to be made or tendered, delivery to Dictaphone of the Purchase Price in accordance with Section 2.5 and the following documents:

(a) a counterpart signature page to each Related Agreement (other than the Transition Services Agreement), duly executed by the Buyer and each Buyer Affiliate party thereto, as applicable;

(b) a counterpart signature page to any assignment agreement, assumption agreement and other applicable document of transfer and assumption to effect the sale and transfer of the Purchased Assets and assumption of Assumed Liabilities as required hereby, duly executed by the Buyer and each Buyer Affiliate party thereto, as applicable; provided, however, that in connection with the assignment and transfer of the Assigned

Contracts, each Seller, Buyer and Buyer Affiliate, as applicable, shall, subject to Section 2.10, execute a single assignment and assumption agreement as to all of the Assigned Contracts other than those listed on Annex 6.9(b) and any other Assigned Contracts mutually agreed to;

(c) copies, certified by the Secretary or Assistant Secretary of the Buyer, of (i) resolutions duly adopted by the board of directors of the Buyer approving this Agreement, the Related Agreements and the consummation of the transactions contemplated thereby, (ii) the Buyer's charter and (iii) the Buyer's bylaws;

(d) a certificate of a senior executive officer of the Buyer pursuant to Section 8.1;

(e) a non−foreign person affidavit as required by Code Section 1445, duly executed by the Buyer;

(f) a counterpart signature page to the Termination Agreement, duly executed by the Buyer and any of its Affiliates party thereto; and

(g) such other customary documents, instruments or certificates as shall be reasonably requested by Dictaphone and as shall be consistent with the terms of this Agreement.

ARTICLE 9
INDEMNIFICATION

9.1 Indemnification by Dictaphone. Subject to the limitations set forth in this Article 9, Dictaphone shall indemnify the Buyer, its Affiliates and its and their respective directors, officers, employees, stockholders, members, partners, agents, attorneys, representatives, successors and permitted assigns, for and hold them harmless against any and all Losses arising from:

(a) any breach or violation of the covenants made in this Agreement or any Related Agreement by a Seller;

(b) any breach of any of the representations and warranties made in Article 3 or in any of the Related Agreements by Dictaphone or a Selling Subsidiary; or

(c) the Retained Liabilities (other than any Liabilities or Losses arising in connection with EU Employees or Swiss Employees which are specifically addressed in Annex 5.6(a)).

9.2 Indemnification by the Buyer. Subject to the limitations set forth in this Article 9, the Buyer shall indemnify Dictaphone, its Affiliates and its and their respective directors, officers, employees, stockholders, members, partners, agents, attorneys, representatives, successors and permitted assigns, for and hold them harmless against any and all Losses arising from:

(a) any breach or violation of the covenants made in this Agreement or any Related Agreement by the Buyer or a Buyer Affiliate;

(b) any breach of any of the representations or warranties made in Article 4 or in any of the Related Agreements by the Buyer or a Buyer Affiliate; or

(c) the Assumed Liabilities, except to the extent that the Buyer is entitled to be indemnified in respect thereof pursuant to Section 9.1.

9.3 Notice and Payment of Losses. If a Person obtains knowledge of potential or actual Loss which could reasonably be expected to give or has given rise to a claim under Section 9.1 or 9.2, such Person shall or shall cause the Party entitled to indemnification with whom such Person is Affiliated or otherwise related (the "Injured Party") to promptly notify the Party liable for such indemnification (the "Indemnifying Party") in writing of such Loss (a "Notice of Claim"); provided, however, that failure of an Injured Party timely to give a Notice of Claim to the Indemnifying Party shall not release the Indemnifying Party from its indemnity obligations set forth in this Article 9 except to the extent that such failure adversely affects the ability of the Indemnifying Party to defend such Loss or increases the amount of indemnification which the Indemnifying Party is obligated to pay in respect of such Loss hereunder (in which event the amount of indemnification which the Injured Party shall be entitled to receive shall be reduced to an amount which the Injured Party would have been entitled to receive had such Notice of Claim been timely given). The Injured Party shall use commercially reasonable efforts to mitigate any continuing Losses (including use of commercially reasonable efforts to obtain all insurance proceeds and indemnity payments available to the Injured Party). The amount of any Loss payable hereunder shall be reduced to reflect any amounts (including insurance proceeds) recovered by the Buyer or its Affiliates from third parties after giving of a Notice of Claim and, if Dictaphone makes an indemnification payment hereunder for a Loss before the Buyer or its Affiliates recover any such amounts, then the Buyer shall, or shall cause its Affiliates to, reimburse Dictaphone for the amount of any such recovery. If the Injured Party settles or compromises any third−party claim prior to giving a Notice of Claim to the Indemnifying Party in respect of the Loss relating to such third−party claim, the Indemnifying Party shall be released from its indemnity obligation in respect of such Loss. A Notice of Claim shall specify in reasonable detail, to the extent known by the Injured Party, the nature and, to the extent reasonably calculable, estimated amount of any Loss giving rise to a claim for indemnification. Dictaphone agrees that, notwithstanding Section 9.9 or any review, challenge or adjustment of the Estimated Closing Date Balance Sheet pursuant to Section 2.5(b), in the event a Notice of Claim by an Injured Party alleges a Loss by reason of a breach of representation or warranty by Dictaphone arising out of (a) a deficiency (in excess of any reserve in respect thereof or in respect of the line item on the Closing Date Balance Sheet related thereto) in the aggregate net book value of any category included on the Closing Date Balance Sheet (including Tangible Business Assets, Inventory or Accounts Receivable), (b) a deficiency (in excess of any reserve in respect thereof) in the aggregate dollar amount of the Product Backlog set forth in Section 3.25, without duplication, (c) a deficiency (in excess of any reserve in respect thereof) in the aggregate dollar amount of revenues of the Business set forth on Disclosure Schedule Section 3.4(a), or (d) Assumed Liabilities which should have been included on the Closing Date Balance Sheet in accordance with GAAP in excess of those included on the Closing Date Balance Sheet, then the Buyer shall be deemed to have suffered, and may claim, an amount of Loss equal to (w) the aggregate dollar amount of the deficiency in any category described in clause (a) above, (x) $0.75 for each dollar of any deficiency in the aggregate dollar amount of the Product Backlog described in clause (b) above, without duplication, (y) $0.55 for each dollar of any deficiency in the aggregate dollar amount of the revenues described in clause (c) above, and (z) $1.00 for each dollar of Assumed Liabilities that are actually paid which should have been included on the Closing Date Balance Sheet in accordance with GAAP in excess of those set forth on the Closing Date Balance Sheet, as the case may be, without regard to or limitation as a result of, in any case, any positive Net Adjusted Working Capital Level as of the Closing Date. The Indemnifying Party shall satisfy its obligations under Section 9.1 or 9.2, as the case may be, in respect of a Loss within sixty (60) days after its receipt of a Notice of Claim; provided, however, that, for so long as the Indemnifying Party is disputing its indemnity obligation or defending a third−party claim in respect of such Loss in good faith pursuant to Section 9.4, its obligations to satisfy its indemnity obligations to the Injured Party with respect thereto shall be suspended until a final unappealable judgment of a court of competent jurisdiction is given in relation to the claim for indemnification or the third−party claim, as the case may be, relating to such Loss. The Indemnifying Party shall have thirty (30) Business Days (or such shorter period of time within which the Injured Party may be required to respond to any Proceeding) after receipt of a Notice of Claim to notify the Injured Party (a) whether or not it disputes its indemnity obligation to the Injured Party with respect to such Notice of Claim and (b) whether it elects to defend a third−party claim in respect of the Loss described in such Notice of Claim pursuant to Section 9.4.

9.4 Defense of Third−Party Claims. With respect to any third−party claim set forth in a Notice of Claim (a "Third−Party Claim"), the Indemnifying Party shall be obligated to assume the investigation and defense of such Third−Party Claim in good faith and at its own expense and the Injured Party may participate (but not control) in the defense of such Third−Party Claim and employ separate counsel of its choosing. The Injured Party shall participate in any such defense at its expense unless the Indemnifying Party and the Injured Party are both named parties to the proceedings and the Injured Party shall have reasonably concluded that representation of both parties by the same counsel would be inappropriate based on a written opinion of counsel due to actual or potential material differing interests between them. So long as the Indemnifying Party is defending any such Third−Party Claim in accordance with this Section 9.4, the Injured Party shall not settle or compromise such Third−Party Claim without the consent of the Indemnifying Party. If such Third−Party Claim is settled by the Injured Party without the Indemnifying Party's consent, the Injured Party shall be deemed to have waived all rights to indemnification and all other remedies with respect to such Third−Party Claim, hereunder or otherwise. The Indemnifying Party may settle or compromise such Third−Party Claim without the consent of the Injured Party, unless there will not be a complete release of the Injured Party in connection therewith, in which case the Indemnifying Party may not settle or compromise such Third−Party Claim without the consent of the Injured Party, which consent shall not be unreasonably withheld. The Injured Party shall make available to the Indemnifying Party or its representatives all records and other materials reasonably required for use in investigating and defending any Third−Party Claim. Subject to Sections 6.2 and 6.4, the Injured Party shall cooperate fully with the Indemnifying Party in the investigation and defense of all Third−Party Claims. If the Indemnifying Party elects not to defend any Third−Party Claim, the Injured Party shall have no obligation to do so, but may investigate, defend, settle or compromise such Third−Party Claim at the sole risk and expense of the Indemnifying Party. The Indemnifying Party will not, however, be responsible for any Losses if and to the extent that they arise from action taken or omitted to be taken by the Injured Party in bad faith, fraudulently, negligently or in breach of this Agreement by the Injured Party.

9.5 Survival of Representations and Warranties. All of the representations and warranties made by any Party in Articles 3 and 4 shall survive for a period of eighteen (18) months following the Closing Date (and thereafter to the extent that a Notice of Claim is made prior to the expiration of such period with respect to a breach of any such representation or warranty occurring prior to such expiration, but only with respect to the Loss and the breach set out in such Notice of Claim); provided, however, that the representations and warranties contained in (a) Sections 3.1, 3.2, 3.3, 4.1 and 4.2 shall survive the Closing Date without any time limit, (b) Section 3.18 shall survive the Closing Date for a period of twenty−four (24) months following the Closing Date and (c) Section 3.6 shall survive with respect to any Tax described therein until the expiration of the statute of limitations (before giving effect to any extension or waiver in respect thereof) relating to such Tax. No Injured Party shall be entitled to indemnification for breach of any representation and warranty set forth in Articles 3 and 4 unless a Notice of Claim in respect of such breach has been given to the Indemnifying Party within the period of survival of such representation and warranty as set forth herein.

9.6 Limitation on Indemnification.

(a) The provisions for indemnity under Sections 9.1(b) and 9.2(b), as the case may be, shall be effective only when the aggregate amount of all Losses for which indemnification is sought from either Dictaphone or the Buyer, respectively, under such Sections exceeds Two Hundred Fifty Thousand U.S. Dollars (US$250,000) (the "Indemnity Threshold"), in which case the Injured Party shall be entitled to indemnification in respect of the Injured Party's Losses only in excess thereof; provided, further, that any individual Loss for which indemnification is sought pursuant to Sections 9.1(a) or 9.2(b), as applicable, which is less than Ten Thousand U.S. Dollars (US$10,000) shall not be included in calculating whether and the extent to which the Indemnity Threshold has been reached or exceeded (other than Losses attributable to individual breaches of the representations and warranties set forth in Section 3.10(a), 3.10(b) or 3.15 , which individual breaches of any one such Section may be aggregated with other breaches (arising out of events or circumstances of the same type or class) of the same such Section).

(b) The indemnification obligations of Dictaphone pursuant to Sections 9.1(a) and 9.1(b) shall be limited to Losses which, in the aggregate, do not exceed Four Million Five Hundred Thousand U.S. Dollars ($4,500,000) (the "Dictaphone Maximum Indemnity Amount"). In no event shall Dictaphone be liable for indemnification of Losses under such Sections in excess of the Dictaphone Maximum Indemnity Amount. The Dictaphone Maximum Indemnity Amount shall be reduced by the amount of Indemnification Escrowed Funds delivered to the Buyer pursuant to Section 2.7 and the Escrow Agreement, but shall not be reduced by any adjustment to the Purchase Price pursuant to Section 2.5(b). Notwithstanding the foregoing, (A) Losses based upon (y) a breach of representation or warranty made pursuant to Sections 3.1, 3.2, 3.3 and 3.6 or (z) a breach of any covenant in this Agreement (other than a covenant made pursuant to Sections 6.1 or 6.8) shall not be limited to the Dictaphone Maximum Indemnity Amount and (B) the Dictaphone Maximum Indemnity Amount shall include an additional One Million U.S. Dollars ($1,000,000) for, but solely for, Losses based upon a breach of any representation, warranty or covenant made by a Seller in the Manufacturing Agreement.

(c) The indemnification obligations of the Buyer pursuant to Sections 9.2(a) and 9.2(b) shall be limited to Losses which, in the aggregate, do not exceed Four Million Five Hundred Thousand U.S. Dollars ($4,500,000) (the "Buyer Maximum Indemnity Amount") and in no event shall the Buyer be liable for indemnification of Losses under such Sections in excess of the Buyer Maximum Indemnity Amount. Notwithstanding the foregoing, Losses based upon (y) a breach of representation or warranty made pursuant to Sections 4.1 and 4.2 or (z) a breach of any covenant in this Agreement shall not be limited to the Buyer Maximum Indemnity Amount.

(d) Notwithstanding anything in this Agreement to the contrary, no Liability (other than Retained Liabilities), Contract or other matter shall constitute a breach of any representation or warranty of Dictaphone or entitle the Buyer to indemnification hereunder (i) if the Liability, Contract or other matter is specifically identified in the Disclosure Schedule, (ii) if the Liability, Contract or other matter is specifically identified in an amendment to the Disclosure Schedule identified as such and delivered to the Buyer and Buyer's counsel at least one (1) Business Day prior to the Closing, or (iii) if Dictaphone otherwise cures such breach.

9.7 Characterization of Indemnity Payments. Any indemnification payments made pursuant to this Agreement shall be considered, to the extent permissible under applicable Law, as adjustments to the Purchase Price for all Tax purposes.

9.8 Exclusive Remedy. The indemnification provisions set forth in this Article 9 shall provide the sole and exclusive remedy for breaches of, or inaccuracies in, any covenant, agreement, representation or warranty set forth in this Agreement or any Related Agreement or any other agreement ancillary hereto executed pursuant to this Agreement and each Party on behalf of itself and its Affiliates hereby waives all statutory, common law and other claims with respect thereto, other than claims for indemnification pursuant to this Article 9. Notwithstanding the foregoing, each Party and its Affiliates shall be entitled to such equitable remedies to which such Party or its Affiliates may otherwise be entitled, including the ability to apply to any court of competent jurisdiction for specific performance or injunctive relief.

9.9 Other Limitations. Notwithstanding anything to the contrary contained herein, no Party or its Affiliates shall be liable to or otherwise responsible to the other Party or its Affiliates or any Injured Party for consequential, incidental, punitive or special damages or for diminution in value or lost profits that arise out or relate to this Agreement or any Related Agreement or any other agreement ancillary hereto executed pursuant to this Agreement or the performance or breach hereof or thereof or any liability retained or assumed hereunder or thereunder.

9.10 No Duplicative Adjustments. Notwithstanding anything to the contrary contained in this Agreement, to the extent that an adjustment has been made to the Purchase Price or any other payments hereunder for any matter hereunder, such matter shall, to the extent of such adjustment or other payment, not constitute a breach of any term or provision of this Agreement.

9.11 Annex 5.6(a) Representations and Warranties. The representations and warranties set forth in clauses 12 through 20 of Annex 5.6(a) shall be treated as if they were representations and warranties of Dictaphone made in Article 3 for the purposes of this Agreement, including this Article 9.

ARTICLE 10
TERMINATION; SURVIVAL OF AGREEMENT

10.1 Termination. Notwithstanding anything contained herein to the contrary, this Agreement may be terminated:

(a) at the Closing or at any time prior thereto, by mutual written consent of Dictaphone and the Buyer;

(b) by Dictaphone or the Buyer, as the case may be, if the other Party shall have breached any material provision of this Agreement and shall not have cured such breach within thirty (30) days of receiving notice of such breach from the non−breaching Party; and

(c) at any time after the six month anniversary of the date of this Agreement (the "Termination Date") and prior to the Closing, by Dictaphone or the Buyer, as the case may be, if (i) the Closing shall not have been consummated on or before the Termination Date and (ii) the failure to consummate the Closing on or before the Termination Date did not result from the failure by the Party seeking to exercise its right to terminate this Agreement to perform, satisfy or comply with any agreement, covenant or condition contained in this Agreement required to be performed, satisfied or complied with prior to the Closing by such Party.

10.2 Survival of Agreement. If this Agreement is terminated pursuant to Section 10.1, this Agreement, except for the provisions of Sections 6.3(a), 6.3(c) and this Section 10.2 and Article 11, shall become null and void and have no further force or effect and neither the Parties nor any of their respective shareholders, directors, officers, employees, agents, representatives, consultants, subsidiaries or Affiliates shall have any liability in respect of such termination other than (i) as set forth in this Section 10.2 or (ii) any Liability of the Buyer or Dictaphone, as the case may be, for breaches of this Agreement occurring prior to such termination.

ARTICLE 11
MISCELLANEOUS PROVISIONS

11.1 Expenses. Except as otherwise provided in this Agreement and regardless of whether the transactions contemplated by this Agreement are consummated, each Party agrees to pay all expenses, fees and costs (including, without limitation, legal, accounting and consulting expenses) incurred by it in connection with the transactions contemplated hereby.

11.2 Notice. All notices, requests, demands and other communications required or permitted under this Agreement shall be given or made in writing and shall be deemed to have been duly given and made (i) in the case of personal delivery or delivery by facsimile or email, on the date of such delivery, (ii) in the case of delivery by a nationally−recognized overnight courier, on the next Business Day following dispatch and (iii) in the case of mailing, by certified mail, return receipt requested, postage prepaid, on the third Business Day following such mailing, in each case addressed at the mailing or email address or facsimile number shown in this Section 11.2 for, or such other address as may be designated in writing hereafter by such, Party:

If to the Buyer or any Buyer Affiliate:

Nice Systems Inc.
301 Route 17, 10th Floor
Rutherford, New Jersey 07070
Telephone: 201−964−2600
Fax: 201−964−2610
Attention: David Z. Ottensoser, Esq.

With copies to:

Brown Raysman Millstein Felder & Steiner LLP
900 Third Avenue
New York, New York 10022
Telephone: 212−895−2310
Fax: 212−895−2900
Email: dscherzer@brownraysman.com
Attention: Dov H. Scherzer, Esq.

And:

Telephone: 212−895−2240
Fax: 212−895−2900
Email: dwarburg@brownraysman.com
Attention: David M. Warburg, Esq.

If to Dictaphone or any Selling Subsidiary:

Dictaphone Corporation
3191 Broadbridge Avenue
Stratford, Connecticut 06614
Telephone: 203−381−4555
Fax: 203−683−3279
Email: scott.bloom@dictaphone.com
Attention: General Counsel

With copies to:

Kelley Drye & Warren LLP
Two Stamford Plaza
281 Tresser Boulevard
Stamford, Connecticut 06901
Telephone: 203−351−8032
Fax: 203−327−2669
Email: mrbarker@kelleydrye.com
Attention: M. Ridgway Barker

11.3 Entire Agreement. This Agreement, the letter agreement, dated as of the date hereof, regarding certain costs, between the Buyer and Dictaphone, and the letter agreement referenced in Section 5.1(c) embody the entire agreement and understanding of the Parties with respect to the subject matter hereof and supersede all prior and contemporaneous agreements and understandings relative to such subject matter.

11.4 Severability. Except as otherwise provided in Section 6.5(c), if any provision hereof shall be held invalid or unenforceable by any court of competent jurisdiction or shall become invalid or unenforceable as a result of future legislative action, such holding or action shall be strictly construed and shall not affect the validity or effect of any other provision hereof, as long as the remaining provisions, taken together, are sufficient to carry out the overall intentions of the Parties as evidenced hereby.

11.5 Assignment; Binding Agreement. This Agreement and various rights and obligations arising hereunder shall inure to the benefit of and be binding upon the Parties and their successors and permitted assigns. Neither this Agreement nor any of the rights or obligations hereunder shall be transferred, delegated or assigned by either of the Parties without the prior written consent of the other Party (which consent shall not be unreasonably withheld), except that (a) prior to or after Closing, Buyer shall have the right to transfer and assign its rights (and delegate its obligations and liabilities) hereunder to any of Buyer's Affiliates and (b) commencing ninety (90) days after Closing, Dictaphone shall have the right to transfer and assign its rights (and delegate its obligations and liabilities) hereunder (i) to any Person who is the acquiror in a sale or other disposition of a majority of Dictaphone's businesses or assets, (ii) as security for any financing of Dictaphone or its Affiliates or of an acquiror of a majority of Dictaphone's businesses or assets, and (iii) to any of Dictaphone's Affiliates. No such assignment, transfer or delegation shall relieve the Buyer or Dictaphone, as applicable, of any of their respective liabilities or obligations hereunder. Notwithstanding the foregoing, no assignment or transfer shall be made of such rights unless the assignee also expressly assumes all obligations and liabilities of the assigning Party under this Agreement and the Related Agreements (other than the Manufacturing Agreement and any Related Agreement that has expired or been terminated and the Trademark License Agreement to the extent that it has otherwise been assigned), provided, however, that the Technology License Agreement (or the appropriate parts thereof) may be separately assigned or transferred to no more than two Persons as part of a sale or other disposition of a majority of the businesses or assets of Integrated Voice Systems or Healthcare Solutions Group and, for the avoidance of doubt, a Dictaphone Successor shall assume the obligations under Sections 5.7 and 6.5 as a Dictaphone Successor. Any assignment in violation of the foregoing shall be null and void.

11.6 Counterparts. This Agreement may be executed simultaneously in multiple counterparts, and in separate counterparts, each of which shall be deemed an original, but all of which taken together shall constitute one and the same instrument.

11.7 Headings; Interpretation. The Article and Section headings contained in this Agreement are inserted for convenience only and shall not affect in any way the meaning or interpretation of this Agreement. Each reference in this Agreement to an Article, Section, Disclosure Schedule, Annex or Exhibit, unless otherwise indicated, shall mean an Article or a Section of this Agreement or a Disclosure Schedule, Annex or Exhibit attached to this Agreement, respectively. References herein to "days", unless otherwise indicated, shall mean consecutive calendar days. All Parties have participated substantially in the negotiation and drafting of this Agreement and no ambiguity herein should be construed against the draftsman.

11.8 Governing Law. This Agreement shall be governed by, and construed in accordance with, the law of the State of New York applicable to contracts to be carried out wholly within such State.

11.9 Dispute Resolution.

(a) Except as otherwise provided in this Section 11.9, the Parties will attempt in good faith to resolve any controversy or claim between them arising out of or relating to this Agreement, including any dispute relating to the negotiation, formation, execution or delivery of this Agreement (a "Dispute"), promptly by negotiations.

(b) Notice of any Dispute must be given in writing and delivered to the other Party and may request the other Party to meet at a mutually agreeable time and place. Each Party to the Dispute must designate an executive and require him or her to meet at least once within the first fifteen (15) days after the delivery of the written notice and attempt to resolve the Dispute.

(c) If the matter has not been resolved within fifteen (15) days of delivery of the written notice described in this Section 11.9, the Dispute shall be settled by arbitration in accordance within the commercial arbitration rules (the "AAA Rules") of the American Arbitration Association ("AAA"). The arbitration proceeding, including the rendering of an award, shall take place in New York County, New York, and shall be administered by the nearest AAA office.

(d) The arbitral tribunal shall be appointed within thirty (30) days of the notice of the Dispute and shall consist of three (3) arbitrators, one of whom shall be appointed by the Buyer, one by Dictaphone, and the third, jointly, by both the Buyer and Dictaphone; provided, however, if the Buyer and Dictaphone do not select the third arbitrator within such thirty−day period, such arbitrator shall be chosen by the AAA as soon as practicable following notice to the AAA by either of the Parties of their inability to choose the third arbitrator.

(e) Notwithstanding anything contained in the AAA Rules to the contrary: (i) each Party shall be allowed to conduct discovery through written requests for information, document requests, requests for stipulations of fact, and depositions; (ii) the nature and extent of such discovery shall be determined by the arbitration panel, taking into account the needs of the Parties and the desirability of making discovery expeditious and cost−effective; (iii) the arbitration panel may issue orders to protect the confidentiality of information to be disclosed in discovery; and (iv) the arbitration panel's discovery rulings may be enforced in any court of competent jurisdiction. All hearings shall be conducted on an expedited schedule, and all proceedings shall be confidential. Either Party may at its expense make a stenographic record thereof.

(f) The award of the arbitral tribunal shall be final, except as otherwise provided by the laws of the State of New York and the federal laws of the United States to the extent applicable. Judgment upon such award may be entered by the prevailing Party in any court having jurisdiction.

(g) The award of the arbitral tribunal may be alternatively or cumulatively for monetary damages, an order requiring the performance of non−mandatory obligations or any other appropriate order or remedy, including injunction and specific performance. The arbitral tribunal may issue interim awards and order any provisional measures which should be taken to preserve the respective rights of either Party. Notwithstanding anything contained in this Section 11.9 or the AAA Rules to the contrary, the arbitrators shall not make any award in breach of or inconsistent with Article 9 and Section 2.5.

(h) The cost of the arbitration proceeding, including reasonable attorney's fees for all Parties, if there are any, shall be paid by the non−prevailing Party as determined by the arbitral tribunal.

(i) Notwithstanding any other provision in this Agreement, any Party may seek and obtain damages and injunctive and other equitable relief from a court of competent jurisdiction without resorting to negotiations or arbitration for any dispute related to Section 6.3 or 6.5.

(j) The provisions of this Section 11.9 shall not be applicable to disputes which are specifically designated as being subject to the dispute resolution provisions of Section 2.5(b)(iv).

11.10 Disclosure Schedule Generally. The information furnished in the Disclosure Schedule is arranged in sections corresponding to the Sections of this Agreement, and the disclosures in any section of the Disclosure Schedule shall qualify (i) the corresponding Section of this Agreement and (ii) other Sections of this Agreement to the extent (notwithstanding the absence of a specific cross−reference), that it is clear from a reasonable reading of the Disclosure Schedule and such other Sections of this Agreement that such disclosure is also applicable to such other Sections of this Agreement. The Disclosure Schedule and the information and disclosures contained in the Disclosure Schedule is intended only to qualify and limit the representations and warranties of Dictaphone contained in this Agreement and shall not be deemed to expand in any way the scope of any such representation or warranties.

The inclusion of any information in the Disclosure Schedule shall not be deemed to be an admission or acknowledgment that such information is material or outside the Ordinary Course or as to any violation of any Law or Contract.

11.11 No Third−Party Beneficiaries or Other Rights. Nothing herein shall grant to or create in any Person not a party hereto (other than an Injured Party and other than an Affiliate where expressly provided), including an employee of Dictaphone or the Buyer, any right to any benefits hereunder, and no such Person shall be entitled to sue either Party with respect thereto. The representations and warranties contained in this Agreement are made for purposes of this Agreement only and shall not be construed to confer any additional rights on the Parties under applicable state, federal or foreign securities laws.

11.12 Amendments; Waivers. Any of the provisions of this Agreement may be amended, modified or waived only by a written instrument signed by an authorized executive officer of each of the Parties. The failure of any Party to enforce at any time any of the provisions of this Agreement shall in no way be construed to be a waiver of any such provision, nor in any way to affect the validity of this Agreement or any part hereof or the right of such Party thereafter to enforce each and every such provision. No waiver of any breach of, or noncompliance with, this Agreement shall be held to be a waiver of any other or subsequent breach or noncompliance.

THIS AGREEMENT CONTAINS A BINDING ARBITRATION PROVISION WHICH MAY BE ENFORCED BY THE PARTIES.

IN WITNESS WHEREOF, each of the Parties has caused this Agreement to be executed as of the date first above written.

NICE SYSTEMS INC.

By: ______________________________
Name: ______________________________
Title: ______________________________

DICTAPHONE CORPORATION

By: ______________________________
Name: ______________________________
Title: ______________________________

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EXECUTION VERSION

AMENDMENT NO. 1 TO
ASSET PURCHASE AND SALE AGREEMENT

THIS AMENDMENT NO. 1 TO ASSET PURCHASE AND SALE AGREEMENT (this "Amendment") is made and entered into as of May 31, 2005, by and between Dictaphone Corporation, a Delaware corporation ("Dictaphone"), and NICE Systems Inc., a Delaware corporation ("Buyer"), in connection with that certain Asset Purchase and Sale Agreement, dated as of April 11, 2005, by and among Buyer and Dictaphone (the "Agreement").

WITNESSETH:

WHEREAS, pursuant to Section 11.12 thereof, the Agreement may be amended only by a written agreement signed by Buyer and Dictaphone; and

WHEREAS, Buyer and Dictaphone are desirous of amending the Agreement as set forth herein;

NOW, THEREFORE, in consideration of the premises, the parties hereto, intending to be legally bound, hereby agree as follows:

1. Defined Terms

All capitalized terms used in this Amendment and not otherwise defined herein shall have the respective meanings assigned thereto in the Agreement.

2. Amendments and Modifications to the Agreement

(a) Article 1 is hereby amended by adding the following definitions of "Amendment", "Audit Escrowed Funds", "SEC Required Financial Statements", "2002 Audited Financial Statements", "2003 Audited Financial Statements" and "2005 Audited Financial Statements" therein as follows:

"Amendment" means Amendment No. 1 to Asset Purchase Agreement, between the Buyer and Dictaphone, dated as of May 31, 2005.

"Audit Escrowed Funds" has the meaning set forth in Section 2.5(a).

"SEC Required Financial Statements" has the meaning set forth in Section 6.7(c).

"2002 Audited Financial Statements" means the audited balance sheet of the Business as of December 31, 2002 and the related audited statement of operations and statement of cash flows for the nine months ended December 31, 2002, prepared on a "carved−out" basis in accordance with U.S. GAAP and as otherwise set forth in Section 6.7(c).

"2003 Audited Financial Statements" means the audited balance sheet of the Business as of December 31, 2003 and the related audited statement of operations and statement of cash flows for the twelve months ended December 31, 2003, prepared on a "carved−out" basis in accordance with U.S. GAAP and as otherwise set forth in Section 6.7(c).

"2005 Audited Financial Statements" means the audited balance sheet of the Business as of May 31, 2005 and the related audited statement of operations and statement of cash flows for the five months ended May 31, 2005, prepared on a "carved−out" basis in accordance with U.S. GAAP and as otherwise set forth in Section 6.7(c).

(b) Article 1 of the Agreement is hereby amended by amending and restating the definition of "Interim 2005 Financial Statements" therein to read in its entirety as follows:

"Interim 2005 Financial Statements" means the unaudited financial statements relating to the Business, prepared on a "carved−out" basis in accordance with U.S. GAAP and the applicable requirements of Rule 3−05 of Regulation S−X, consisting of the adjusted balance sheet of the Business as of the end of the fiscal quarter ending immediately prior to the Closing Date and the related adjusted statement of operations and statement of cash flows for each of the three−month periods then ended.

(c) Section 2.5(a) of the Agreement is hereby amended by amending and restating such section to read in its entirety as follows:

"Purchase Price. In consideration for Dictaphone's and the Selling Subsidiaries' sale, assignment, transfer, conveyance and delivery of the Purchased Assets to the Buyer and the Buyer Affiliates, the Buyer shall pay to Dictaphone on behalf of Dictaphone and the Selling Subsidiaries a purchase price of U.S. Thirty−Eight Million Five Hundred Thousand Dollars (US$38,500,000.00) (the "Purchase Price") (provided, however, that the Purchase Price is subject to adjustment pursuant to Section 2.5(b)) and assume, duly perform and discharge, or cause the Buyer Affiliates to assume, duly perform and discharge, when due all of the outstanding obligations of Dictaphone and its Affiliates under the Assumed Liabilities in accordance with Section 2.3. At the Closing, the Purchase Price shall be paid as follows: (x) U.S. Thirty−One Million Six Hundred Fifty Thousand Dollars (US$31,650,000.00) shall be paid directly to Dictaphone, (y) U.S. Three Million Dollars (US$3,000,000.00) shall be deposited in escrow (with any accrued interest earned thereon, the "Indemnification Escrowed Funds") in accordance with Section 2.7 and the terms and conditions of the Escrow Agreement, as security for the indemnification obligations of Dictaphone set forth in Article 9 and (z) U.S. Three Million Eight Hundred Fifty Thousand Dollars (US$3,850,000) shall be deposited in escrow (with any accrued interest earned thereon, the "Audit Escrowed Funds") in accordance with Section 2.7 and the terms and conditions of the Escrow Agreement, as security for the obligations of

Dictaphone set forth in Section 6.7(c). All amounts payable under this Section 2.5 are stated exclusive of any value added or similar sales tax which shall be payable in addition."

(d) Section 2.5(b)(iv) of the Agreement is hereby amended by replacing "sixty (60) days" in the first sentence thereof with "September 15, 2005".

(e) Section 2.6 of the Agreement is hereby amended by replacing "Section 2.5(a)(i)" in the last sentence thereof with "Section 2.5(a)".

(f) Section 2.7(a) of the Agreement is hereby amended by amending and restating such section to read in its entirety as follows:

"Creation of Escrow. On the Closing Date, the Buyer shall deposit or cause to be deposited the Indemnification Escrowed Funds, the Audit Escrowed Funds and, if applicable, the Balance Sheet Escrowed Funds with the Escrow Agent in a separate account, and such Indemnification Escrowed Funds, Audit Escrowed Funds and Balance Sheet Escrowed Funds shall be held by the Escrow Agent in accordance with the terms and conditions of the Escrow Agreement as security solely for the indemnification obligations of Dictaphone to the Buyer set forth in Article 9 (in the case of the Indemnification Escrowed Funds), as security solely for Dictaphone's obligations to the Buyer set forth in Section 6.7(c) (in the case of the Audit Escrowed Funds) and pending determination of the final Net Adjusted Working Capital Level as of the Closing pursuant to Section 2.5(b) (in the case of the Balance Sheet Escrowed Funds), respectively."

(g) Section 2.7 of the Agreement is hereby amended by adding the following clause (e) therein:

"(e) Release of Audit Escrowed Funds. The Audit Escrowed Funds shall be released to Dictaphone in accordance with the terms and provisions of the Escrow Agreement upon delivery of (i) the 2003 Audited Financial Statements and the Interim 2005 Financial Statements and (ii) either (A) the 2002 Audited Financial Statements or (B) the 2005 Audited Financial Statements by Dictaphone to the Buyer in accordance with the terms and provisions, including applicable delivery dates, of Section 6.7(c). If Dictaphone has not delivered to the Buyer (i) the 2003 Audited Financial Statements and the Interim 2005 Financial Statements and (ii) either (A) the 2002 Audited Financial Statements or (B) the 2005 Audited Financial Statements in accordance with the terms and provisions, including applicable delivery dates, of Section 6.7(c), some or all of the Audit Escrowed Funds shall be released to the Buyer and the balance, if any, shall be released to Dictaphone, in each case in accordance with Section 6.7(c)."

(h) Section 5.6(b) of the Agreement is hereby amended by amending and restating such section to read in its entirety as follows:

"Canadian Employees. Unless otherwise specifically provided herein, the Canadian Employees will be subject to the same terms and provisions as the U.S.

Employees, except to the extent otherwise required to comply with Canadian law; provided, however, that the Buyer shall only be required to make or cause a Buyer Affiliate to make an offer of employment to ten (10) Canadian Employees at least three (3) Business Days prior to the Closing. Notwithstanding any statutory or other rights that any Canadian Employee may have, to the extent that the payment of any claims with respect to termination of his or her employment or severance benefits or government required termination liabilities to any transferred Canadian Employee who received and accepted an offer from the Buyer or a Buyer Affiliate is required as a result of (i) the consummation of the transactions contemplated by this Agreement and any concurrent or deemed transfers of employment or (ii) termination of the employment of any Canadian Employee who is a Transferred Employee by the Buyer after the Closing Date, such claims, severance benefits and government−required termination liabilities shall be the sole responsibility of the Buyer. The Buyer shall, and shall cause its Affiliates to, recognize all service of each transferred Canadian Employee with Dictaphone or any other Seller or predecessor thereof for all purposes, including eligibility to participate, vesting credit, entitlement for benefits and benefit accrual, except to the extent such treatment would result in duplicative benefits."

(i) The heading of Section 6.7 of the Agreement is hereby amended by amending and restating such heading to read in its entirety as follows:

"Delivery of Audited Financial Statements, Closing Date Balance Sheet, Interim 2005 Financial Statements and Other Audited Financial Statements."

(j) Section 6.7 of the Agreement is hereby amended by deleting clauses (c) and (d) thereof and replacing such clauses with the following clause (c):

"(c) (i) The Parties agree that audited financial statements of the Business covering a thirty−three (33) month period and, to the extent not included in such period, the Interim 2005 Financial Statements, are required by the Buyer to enable the Buyer's parent to be able to file with the Securities and Exchange Commission, as part of such periodic or other reports and registration statements as it may desire to file under the U.S. federal securities laws, consolidated financial statements of the Business in accordance with Rule 3−05 of Regulation S−X (collectively, the "SEC Required Financial Statements"). The Parties also agree that such thirty−three (33) month period may consist of the 2003 and 2004 calendar years together with either the nine months ended December 31, 2002 or the nine months ended September 30, 2005 (of which the first five months ended May 31, 2005 would be addressed by the 2005 Audited Financial Statements). The Parties hereby acknowledge that neither Party could have known or anticipated prior to receipt of the Audited Financial Statements that the Buyer requires the 2003 Audited Financial Statements and either (i) the 2002 Audited Financial Statements or (ii) the 2005 Audited Financial Statements as part of the SEC Required Financial Statements.

(ii) Dictaphone, at its own expense, shall have prepared and delivered to the Buyer, on or prior to August 16, 2005, the 2002 Audited Financial Statements and the 2003 Audited Financial Statements, in each case together with the Auditor's Reports thereon, and the Interim 2005 Financial Statements, and in each case except to the extent Buyer's parent has received waivers (or similar actions) in writing from the Securities and Exchange Commission (or its staff) or other appropriate governmental authority prior to August 16, 2005 with respect to requirements otherwise applicable to the SEC Required Financial Statements. If Dictaphone fails to deliver the 2002 Audited Financial Statements to the Buyer by September 20, 2005, Dictaphone shall deliver, instead of the 2002 Audited Financial Statements, the 2005 Audited Financial Statements, together with the Auditor's Report thereon and except to the extent Buyer's parent has received waivers (or similar actions) in writing from the Securities and Exchange Commission (or its staff) or other appropriate governmental authority prior to August 16, 2005 with respect to requirements otherwise applicable to the SEC Required Financial Statements. Except as otherwise specifically permitted by such waivers (or other actions), (a) the 2003 Audited Financial Statements, the 2002 Audited Financial Statements, the Interim 2005 Financial Statements and the 2005 Audited Financial Statements, as applicable, (i) will be derived from the books and records of the Business, (ii) will fairly present, in all material respects, the financial position and results of operations of the Business at the dates and for the periods indicated in accordance with U.S. GAAP and the applicable requirements of Rule 3 05 of Regulation S−X, and (iii) will (other than the Interim 2005 Financial Statements) be accompanied by Auditor's Reports, (b) the statements of profit and loss included in the 2002 Audited Financial Statements, the 2003 Audited Financial Statements, the Interim 2005 Financial Statements and the 2005 Audited Financial Statements, as applicable, will not reflect any material operations of any Person or business that did not constitute a part of the Business as then conducted by Dictaphone and its subsidiaries (but will include allocations of corporate overhead and other expenses based on estimates prepared in good faith by Dictaphone to the extent permitted by U.S. GAAP and the applicable requirements of Rule 3 05 of Regulation S−X with respect to "carve−out" financial statements) and (c) the balance sheets included in the 2002 Audited Financial Statements, the 2003 Audited Financial Statements, the Interim 2005 Financial Statements and the 2005 Audited Financial Statements, as applicable, will not include any material assets or liabilities that did not constitute a part of the Business as then conducted by Dictaphone and its subsidiaries.

(iii) After the delivery of the 2002 Audited Financial Statements, the 2003 Audited Financial Statements, the Interim 2005 Financial Statements and the 2005 Audited Financial Statements, as applicable, Dictaphone shall, upon request, cooperate with the Buyer in obtaining, at any time or from time to time (with respect to no more than six (6) separate filings with the Securities and Exchange Commission) until December 31, 2006, from the independent auditor that prepared the Audited Reports an Auditor's Consent. The Buyer shall be responsible for all fees and disbursements billed by the auditor for its services in providing any Auditor's Consent, including any costs incurred with respect to responding to any inquiries from the Securities and Exchange Commission (or its staff) or any other governmental authority (excluding any costs incurred in connection with seeking or obtaining any waiver referred to above).

(iv) In connection with the obligations under this Section 6.7(c), each Party agrees to cooperate and collaborate at its own expense with the other Party in (A) preparing the 2002 Audited Financial Statements, 2003 Audited Financial Statements, the Interim 2005 Financial Statements and 2005 Audited Financial Statements, as applicable, (B) preparing and filing any submission to be made to the Securities and Exchange Commission (or its staff) or any other governmental authority, including any requests for waivers or extensions made by Buyer's parent with respect to the 2003 Audited Financial Statements (and the Buyer shall cause Buyer's parent to pursue waivers and extensions with respect to the 2003 Audited Financial Statements when and as requested by Dictaphone unless pursuing such waivers or extension would be unreasonable), and (C) responding to any comments, requests for information or inquires therefrom. In addition, each Party shall (i) notify promptly the other Party of any comments, requests or inquiries made by the Securities and Exchange Commission (or its staff) or other governmental authority relating thereto, (ii) provide copies of all written submissions to and communications with or from the Securities and Exchange Commission (or its staff) or any other governmental authority to the other Party relating thereto and (iii) permit the other Party and its advisors to participate in discussions, and attend meetings, with any the Securities and Exchange Commission (or its staff) or any other governmental authority relating thereto.

(v) If Dictaphone fails to deliver the 2002 Audited Financial Statements to the Buyer on or prior to August 16, 2005, U.S. One Hundred Thousand Dollars (US$100,000) per week shall be released from the Audit Escrowed Funds to the Buyer for each full week that Dictaphone has not delivered the 2002 Audited Financial Statements to the Buyer through September 6, 2005 and U.S. Two Hundred Thousand Dollars (US$200,000) per week shall be released from the Audit Escrowed Funds to the Buyer for each full week thereafter through September 20, 2005 that Dictaphone has not delivered the 2002 Audited Financial Statements to the Buyer. If Dictaphone fails to deliver the 2003 Audited Financial Statements and the Interim 2005 Financial Statements to the Buyer on or prior to August 16, 2005, U.S. One Hundred Thousand Dollars (US$100,000) per week shall be released from the Audit Escrowed Funds to the Buyer for each full week that Dictaphone has not delivered the 2003 Audited Financial Statements and the Interim 2005 Financial Statements to the Buyer through September 6, 2005 and U.S. Two Hundred Thousand Dollars (US$200,000) per week shall be released from the Audit Escrowed Funds to the Buyer for each full week thereafter that Dictaphone has not delivered the 2003 Audited Financial Statements and the Interim 2005 Financial Statements to the Buyer. If Dictaphone has failed to deliver the 2002 Audited Financial Statements and fails to deliver the 2005 Audited Financial Statements to the Buyer on or prior to September 20, 2005, U.S. One Hundred Thousand Dollars (US$100,000) per week shall be released from the Audit Escrowed Funds to the Buyer for each full week that Dictaphone has not delivered the 2005 Audited Financial Statements to the Buyer through October 6, 2005 and U.S. Two Hundred Thousand Dollars (US$200,000) per week shall be released from the Audit Escrowed Funds to the Buyer for each full week thereafter that Dictaphone has not delivered the 2005 Audited Financial Statements to the Buyer. Any amounts to be released from the Audit Escrowed Funds for failure to deliver the 2005 Audited Financial Statements shall be in addition to and not in substitution for any amounts to be released from the Audit Escrowed Funds for failure to deliver the 2003 Audited Financial Statements or the Interim 2005 Financial Statements. Notwithstanding anything contained herein to the contrary, upon delivery of (a) the 2003 Audited Financial Statements and the Interim 2005 Financial Statements and (b) either (i) the 2002 Audited Financial Statements or (ii) the 2005 Audited Financial Statements, the Audit Escrowed Funds or remaining balance shall be released to Dictaphone.

(vii) To the extent that Dictaphone is unable to prepare and have audited any of the 2002 Audited Financial Statements, the 2003 Audited Financial Statements, the Interim 2005 Financial Statements or the 2005 Audited Financial Statements due to a failure by the Buyer to provide access to information regarding the Business or to former Dictaphone personnel, and Dictaphone has promptly after the occurrence of any alleged lack of cooperation given the Buyer written notice specifically identifying the alleged lack of cooperation, the dates set forth above shall be extended to reflect any delay reasonably and directly arising therefrom.

(viii) Notwithstanding anything contained herein to the contrary, the aggregate amounts payable to the Buyer with respect to Dictaphone's failure to deliver the 2002 Audited Financial Statements, the 2003 Audited Financial Statements, the Interim 2005 Financial Statements and the 2005 Audited Financial Statements, as applicable, pursuant to this Section 6.7(c) shall not exceed the Audit Escrowed Funds, any failure of Dictaphone to perform its obligations under this Section 6.7(c) shall not be subject to any indemnity obligations under Article 9 of this Agreement and Dictaphone's liabilities under this Section 6.7(c) shall in no event exceed the Audit Escrowed Funds."

(k) Section 11.5 of the Agreement is hereby amended by amending and restating such section to read in its entirety as follows:

> "Assignment; Binding Agreement. This Agreement and various rights and obligations arising hereunder shall inure to the benefit of and be binding upon the Parties and their successors and permitted assigns. Neither this Agreement nor any of the rights or obligations hereunder shall be transferred, delegated or assigned by either of the Parties without the prior written consent of the other Party (which consent shall not be unreasonably withheld), except that (a) prior to or after Closing, Buyer shall have the right to transfer and assign its rights (and delegate its obligations and liabilities) hereunder to any of Buyer's Affiliates and (b) commencing ninety (90) days after Closing, Dictaphone shall have the right to

transfer and assign its rights (and delegate its obligations and liabilities) hereunder (i) to any Person who is the acquiror in a sale or other disposition of a majority of Dictaphone's businesses or assets, (ii) as security for any financing of Dictaphone or its Affiliates or of an acquiror of a majority of Dictaphone's businesses or assets, and (iii) to any of Dictaphone's Affiliates. No such assignment, transfer or delegation shall relieve the Buyer or Dictaphone, as applicable, of any of their respective liabilities or obligations hereunder. Notwithstanding the foregoing, no assignment or transfer shall be made of such rights unless the assignee also expressly assumes all obligations and liabilities of the assigning Party under this Agreement and the Related Agreements (other than the Manufacturing Agreement and any Related Agreement that has expired or been terminated and the Trademark License Agreement to the extent that it has otherwise been assigned); provided, however, that the Technology License Agreement (or the appropriate parts thereof) may be separately assigned or transferred to no more than one Person as part of a sale or other disposition of a majority of the domestic businesses or assets of Integrated Voice Systems, to no more than one Person as part of a sale or other disposition of a majority of the international businesses or assets of Integrated Voice Systems, to no more than one Person as part of a sale or other disposition of a majority of the domestic businesses or assets of Healthcare Solutions Group and to no more than one Person as part of a sale or other disposition of a majority of the international businesses or assets of Healthcare Solutions Group and, for the avoidance of doubt, a Dictaphone Successor shall assume the obligations under Sections 5.7 and 6.5 as a Dictaphone Successor. Notwithstanding anything contained in this Agreement or any Related Agreement to the contrary, Dictaphone and its Affiliates shall have the right to sell, transfer or otherwise dispose of the international business of Integrated Voice Systems separate from the domestic business of Integrated Voice Systems and the international business of Healthcare Solutions Group separate from the domestic business of Healthcare Solutions Group, through an asset sale, stock sale, merger or other form of business divestiture or combination, without Buyer's consent and without any assignment or delegation to or assumption by the purchaser, transferee or recipient of the international business of (and without the purchaser, transferee or recipient of the international business becoming or continuing to be subject to) any of the liabilities or obligations of Dictaphone or its Affiliates under this Agreement or any Related Agreement, provided that the total revenue of such international business being sold or otherwise transferred does not exceed twenty percent (20%) of total Dictaphone revenue, excluding EMS, based on Dictaphone's most recent regularly prepared quarterly financial statements available at such time and that the purchaser, transferee or recipient of such international business assumes or continues to be subject to Sections 5.7 and 6.5 of this Agreement as a Dictaphone Successor. For the purpose of this Section 11.5, the words "purchaser, transferee or recipient" include any Affiliate or subsidiary of Dictaphone engaged in the international business which is sold, transferred or otherwise disposed of in connection with, or is the successor of, any such transaction. Notwithstanding anything contained in this Agreement to the contrary, the Parties agree that such purchaser, transferee or recipient of such international business that is an assignee of the Technology License Agreement will assume the respective obligations pertaining to Integrated Voice Systems or Healthcare Solutions Group, as applicable, thereunder. Any assignment in violation of the foregoing shall be null and void."

(l) The Escrow Agreement attached to the Agreement as Exhibit E is hereby amended by amending and restating the Escrow Agreement to read in its entirety as attached hereto as Exhibit A.

3. Insurance. Pursuant to Section 6.14 of the Agreement, the Buyer will pay to Dictaphone fifty percent (50%) of the Seventy−Seven Thousand Nine Hundred Ninety−Five Dollar (U.S.$77,995.00) tail insurance policy premium concurrently with its payment by Dictaphone, upon submission of the invoice for such premium.

4. Delivery of Audited Financial Statements. Buyer acknowledges that the Audited Financial Statements have been timely delivered to Buyer by Dictaphone pursuant to the Agreement.

5. Effective Time. The Parties acknowledge that, if the Closing occurs from May 31, 2005 through June 1, 2005, the Effective Time of the Closing shall be deemed to be 11:59 eastern time at the end of the day on May 31, 2005. The Parties acknowledge that Dictaphone shall own the Business through May 31, 2005 and that the Buyer shall own the Business as of June 1, 2005.

6. Miscellaneous

This Amendment may not be modified or amended, or any of its terms or provisions (or the breach thereof) waived, except by an agreement in writing executed by the parties to this Amendment. This Amendment shall be governed by, and construed in accordance with, the law of the State of New York applicable to contracts to be carried out wholly within such State. The headings of the paragraphs of this Amendment are inserted for convenience of reference only and shall not be deemed to constitute a part nor to affect the meaning or interpretation of any provisions of this Amendment. This Amendment may be executed in counterparts, each of which shall be an original, and all of which together shall be one and the same instrument. Delivery of a counterpart by facsimile shall be as effective as delivery of an original counterpart.

* * *

IN WITNESS WHEREOF, Buyer and Dictaphone have caused this Amendment to be duly executed and delivered, all as of the day and year first above written.

BUYER:

NICE SYSTEMS INC.

By: ______________________________
Name:
Title:

DICTAPHONE:

DICTAPHONE CORPORATION

By: ______________________________
Name:
Title:

Exhibit A

Escrow Agreement

See attached.

Significant Subsidiaries

The following is a list of all of our significant subsidiaries, including the name, country of incorporation or residence, the proportion of our ownership interest in each and, if different, the proportion of voting power held by us.

Name of Subsidiary	Country of Incorporation or Residence	Percentage of Ownership Interest	Percentage of Voting Power (if Different from Ownership Interest)
NICE Systems, Inc.	United States	100 %	—
NICE Systems GmbH	Germany	100 %	—
NICE Systems Canada Ltd.	Canada	100 %	—
NICE CTI Systems UK Ltd.	United Kingdom	100 %	—
STS Software Systems (1993) Ltd.	Israel	100 %	—
NICE APAC Ltd.	Hong Kong	100 %	—
NiceEye BV	Netherlands	100 %	—
NiceEye Ltd.	Israel	100 %	—
Nice Systems S.A.R.L.	France	100 %	—
Racal Recorders, Ltd.	United Kingdom	100 %	—
Nice Interactive Solutions India Private Ltd.	India	100 %	—
Nice Japan Ltd.	Japan	100 %	—
Nice Systems Latin America, Inc.	United States	100 %	—

Exhibit 10.1

CONSENT OF REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statements on Form S−8 (Registration Nos. 333−11842, 333−9352, 333−11154, 333−13686, 333−111112 and 333−111113) and on Form F−3 (Registration Nos. 333−12996, 333−11250 and 333−109766) of our report dated February 2, 2005, with respect to the consolidated financial statements of NICE Systems Ltd. included in this Annual Report on Form 20−F for the year ended December 31, 2004.

Tel−Aviv, Israel
June 29, 2005

/s/ KOST FORER GABBAY & KASIERER
KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

Exhibit 12.1

CERTIFICATIONS

I, Haim Shani, certify that:

1. I have reviewed this annual report on Form 20−F of NICE Systems Ltd.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a−15(e) and 15d−15(e)) for the registrant and we have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: June 29, 2005

By: /s/ Haim Shani
Haim Shani, Chief Executive Officer

Exhibit 12.2

CERTIFICATIONS

I, Ran Oz, certify that:

1. I have reviewed this annual report on Form 20−F of NICE Systems Ltd.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a−15(e) and 15d−15(e)) for the registrant and we have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: June 29, 2005

By: /s/ Ran Oz
Ran Oz, Chief Financial Officer

Exhibit 13.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES−OXLEY ACT OF 2002

In connection with the Annual Report on Form 20−F of NICE Systems Ltd. (the "Company") for the year ended December 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Haim Shani, Chief Executive Officer of the Company, certifies, pursuant to 18 U.S.C. sec. 1350, as adopted pursuant to sec. 906 of the Sarbanes−Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

June 29, 2005

By: /s/ Haim Shani
Haim Shani, Chief Executive Officer

Exhibit 13.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES−OXLEY ACT OF 2002

In connection with the Annual Report on Form 20−F of NICE Systems Ltd. (the “Company”) for the year ended December 31, 2004 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned, Ran Oz, Chief Financial Officer of the Company, certifies, pursuant to 18 U.S.C. sec. 1350, as adopted pursuant to sec. 906 of the Sarbanes−Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

June 29, 2005

By: /s/ Ran Oz
Ran Oz, Chief Financial Officer