

MICRONET ENERTEC TECHNOLOGIES, INC.  
Form 10-K  
March 19, 2014

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

FORM 10-K

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

For the fiscal year ended December 31, 2013

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 333-100979

MICRONET ENERTEC TECHNOLOGIES, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

27-0016420  
(I.R.S. Employer Identification No.)

28 West Grand Avenue, Suite 3, Montvale, NJ 07645  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (201) 225-0190

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

Title of each class	Name of each exchange on which registered
Common Stock, par value \$0.001	Nasdaq Capital Market
Warrants (expiring April 23, 2018)	Nasdaq Capital Market

Securities registered under Section 12(g) of the Act:

None

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(Title of class)

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

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

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

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer   
Non-accelerated filer

Accelerated filer   
Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes  No

The aggregate market value of the issuer's common equity held by non-affiliates, as of June 28, 2013 was approximately \$14,617,888 based on the price at which shares of common equity were last sold as of June 28, 2013 of \$4.52 per share.

As of March 18, 2014, there were 5,831,246 shares of the issuer's common stock outstanding.

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Unless the context provides otherwise, all references in this Annual Report on Form 10-K for the year ended December 31, 2013, or this Annual Report, to "Micronet Enertec," "we," "us," "our," the "Company," the "Registrant" or similar terms, refer to Micronet Enertec Technologies, Inc. and our wholly-owned subsidiaries and Micronet (as defined below). Unless otherwise noted, (1) all references to "dollars" or "\$" are to United States dollars and all references to "NIS" are to New Israeli shekels. Our website address is included several times in this Annual Report as textual references only and the information in any such website is not incorporated by reference into this Annual Report.

#### CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

The statements contained in this Annual Report on Form 10-K that are not historical facts are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 and other federal securities laws. Such forward-looking statements may be identified by, among other things, the use of forward-looking terminology such as "believes," "intends," "plans" "expects," "may," "will," "should," or "anticipates" or the negative thereof or other variations thereon or comparable terminology, and similar expressions are intended to identify forward-looking statements. We remind readers that forward-looking statements are merely predictions and therefore inherently subject to uncertainties and other factors and involve known and unknown risks that could cause the actual results, performance, levels of activity, or our achievements, or industry results, to be materially different from any future results, performance, levels of activity, or our achievements, or industry results, expressed or implied by such forward-looking statements. Such forward-looking statements appear in Item 1 – "Business" and Item 7 – "Management's Discuss and Analysis of Financial Condition and Results of Operations," as well as elsewhere in this Annual Report and include, among other statements, statements regarding the following:

- Demand for our products as well as future growth, either through internal efforts, development of new products, potential segments and markets or through acquisitions;
- Leveraging our experience and other assets we possess within Micronet to enhance Enertec's offerings;
- Our joint venture in India, its prospects and potential;
- Use of the proceeds from the public offering we consummated in April 2013;
- Levels of research and development costs in the future;
- Continuing controlling of at least a majority of Micronet's share capital;
- Our outlook for the coming months and future periods, including to our expectations regarding future revenue and expenses and capital needs; and
- The sufficiency of our capital resources.

The factors discussed herein, including those risks described in Item 1A. "Risk Factors", and expressed from time to time in our filings with the Securities and Exchange Commission could cause actual results and developments to be materially different from those expressed in or implied by such statements. The forward-looking statements are made only as of the date of this filing, and except as required by law we undertake no obligation to publicly update such forward-looking statements to reflect subsequent events or circumstances.

## PART I

### Item 1. Business.

We are a Delaware corporation that was formed on January 31, 2002. On March 14, 2013, we changed our corporate name from Lapis Technologies, Inc. to Micronet Enertec Technologies, Inc. On April 29, 2013 the Company closed an underwritten public offering of 1,620,000 shares of common stock with additional 243,000 shares of common stock as over allotment rights granted to the underwriter, and warrants to purchase 931,500 shares of common stock (including 121,500 over allotment warrants), at an offering price of \$5.00 per share and \$0.01 per warrant. The warrants have a per share exercise price of \$6.25, are exercisable immediately, and expire April 23, 2018. The Company's shares have been traded on NASDAQ as of April 29, 2013.

We operate through two Israeli-based companies, Enertec Systems 2001 Ltd, or Enertec, our wholly-owned subsidiary, and Micronet Ltd, or Micronet, in which we have a controlling interest, which develop, manufacture, integrate and globally market rugged computers, tablets and computer-based systems and instruments for the commercial, defense and aerospace markets. Our products, solutions and services are designed to perform in severe environments and battlefield conditions.

Micronet operates in the growing commercial Mobile Resource Management, or MRM market. Micronet designs, develops, manufactures and sells rugged mobile computing devices that provide fleet operators and field workforces with computing solutions in challenging work environments. Micronet's vehicle cabin installed and portable tablets are design to increase workforce productivity, enhance corporate efficiency and customer service by offering computing power and communication capabilities. The Micronet products provide fleet operators with visibility into vehicle location, fuel usage, speed and mileage and allow the installation of software applications and communication integration enabling the users to manage the drivers in various aspects such as: driver identification, hours working report, customer/organization working procedures and protocols, rout management and navigation based on tasks and time schedule. End user may also receive real time messages for various services such as pickup and delivery, repair and maintenance, status reports, alerts, notices relating to start and ending of work, digital forms, issuing and printing of invoices and payments.

Micronet's customers consist primarily of Application Service Providers (ASPs) and Solution providers specializing in the MRM market. These companies sell Micronet's products as part of their MRM systems and solutions. Currently, Micronet does not sell directly to end-users. Micronet customers are generally MRM solution and service providers, such as Trimble Navigation Limited, or Trimble through its subsidiaries PeopleNet Communications Corp. ("PeopleNet"), , Trimble constructions and Trimble field services. Micronet products are used by customers in 20 countries. The United States currently constitutes its largest market, representing approximately 88% and 92% of revenue for the years ended December 31, 2013 and 2012, respectively. For the year ended December 31, 2013, Micronet's largest customer was Trimble (including PeopleNet), which represented approximately 82.5% of Micronet's Ltd revenues and 56% of the company's revenues. The next largest customer represented approximately 3.4% of Micronet's Ltd revenues. For the year ended December 31, 2012, Trimble and PeopleNet combined (as a result of the acquisition of PeopleNet by Trimble) represented approximately 79% of Micronet's revenues and 27% of the company's revenues. In the year ended December 31, 2012 no other customer accounted for more than 8% of Micronet's revenue.

We acquired control of Micronet in September 2012. Currently, we own 52.26% of Micronet and 52% on a fully diluted basis. These holdings are the result of certain additional purchases of Micronet shares and issuance of shares by Micronet to third parties occurred between September 2012 and the date hereof as follows: 996,000 Micronet shares constituting approximately 5.5% of Micronet purchased from the Micronet previous controlling shareholders in consideration for a total of approximately USD 600,000; Additional 600,000 Micronet shares constituting

approximately 3% of Micronet purchased in August 2013 from Micronet former Chairman of the board in consideration for a total of approximately USD 660,000; Also Our Micronet holdings were diluted due to the exercise by Micronet's former Chairman of the Board and its current CEO of 1,470,401 options into 1,470,401 shares. As of the date hereof, Micronet's other executives currently hold 95,000 options exercisable for 95,000 ordinary shares which constitute approximately 0.5% of Micronet's outstanding ordinary shares. These options are "in the money", meaning the exercise price is less than the current Micronet share market price

Pursuant to our current strategy and business plans, it is our intention to control at least a majority of the outstanding Micronet ordinary shares.

Enertec operates in the Defense and Aerospace markets and designs, develops, manufactures and supplies various customized military computer-based systems, simulators, automatic test equipment and electronic instruments. Enertec's solutions and systems are designed according to major aerospace integrators' requirements and market technological needs and are integrated by them into critical systems such as command and control, missile fire control, maintenance of military aircraft and missiles for use by the Israeli Air Force, Israeli Navy and by foreign defense entities. Approximately 74% and 78% of our revenues for the years ended December 31, 2013 and 2012, respectively, were from independent business units or groups within Israeli Aerospace Industries Ltd., or IAI, the leading Israeli defense system integrator and approximately 19% and 11%, respectively, were from business units of Rafael Advanced Defense Systems Ltd., or Rafael, another Israeli state-owned major defense developer and integrator of critical weapon systems. These distinct units and groups create diversity to our business and revenue streams. The system integrators that are our primary customers market their solutions throughout the world and across the full spectrum of military applications (land, sea and air). Command and control systems represented approximately 67% and 75% of Enertec's revenues for the years ended December 31, 2013 and 2012, respectively and our automated test equipment represented approximately 33% and 22% of Enertec's revenues for the years ended December 31, 2013 and 2012, respectively.

Management believes that the demand for our products, systems and solutions is not affected significantly by fluctuations in any particular geographic market outside the State of Israel because our products, systems and solutions can be tailored to fit the needs of these different disciplines and are not limited to any specific geography.

In order to expand our potential markets and sell into the growing Indian defense market, in 2011 we entered into an agreement for the establishment of a new joint venture with Amtek Defense Technologies Limited, or Amtek, a leading Indian industrial group, to market, manufacture and sell systems and solutions in India based on Enertec's technological and engineering capabilities. Since the entering into the joint venture agreement, in view of certain local Indian regulatory approvals required for the operation of the joint venture entity and the distribution of equity shares, both of them were delayed, Amtek incorporated and operated the joint venture entity.

In May 2013, Amertec Systems Pvt Ltd, or Amertec, the Indian company formed pursuant to the agreement with Amtek received the Indian government authorities' clearance and approval pursuant to the local Indian Foreign Direct Investment regulations for the consummation of their joint venture transaction. This approval enables the Company via its wholly-owned subsidiary, Enertec Electronics Ltd., to subscribe for 26% of the share capital of Amertec. The allocation of the 26% is yet been completed. However, although we believe that a joint venture is the correct platform to sell to the Indian market, due to the elapse of time and since the development of the business is slower than expected, in view of certain changes in local business trends and specific changes in Amtek position, we are currently re-evaluating our position in the joint venture and in the Indian market.

Our overall strategy focuses on continued internal growth through diligent efforts in our traditional growing markets with new technologies and innovative systems and products, as well as the development of new potential segments and markets. To enhance our growth, we also look for appropriate acquisitions to complement and expand our offerings, as well as support our goals and increase our competitive strengths. We concentrate the majority of our resources, including our marketing and sales efforts, in the United States, Israeli and European markets. Currently we do not hold any equity of Amertec.

#### Subsidiaries



We have three subsidiaries and a controlling interest in Micronet. We are the sole owner of Enertec Electronics Ltd., an Israeli corporation, or Enertec Electronics, which is, since 2010, a holding company.

Via Enertec Electronics, directly and indirectly, we are the holder of our current subsidiaries which operate the following businesses:

- Enertec, which operates in the Defense and Aerospace markets and designs, develops, manufactures and supplies various customized military computer-based systems, simulators, automatic test equipment and electronic instruments. In March 2011 Enertec became a wholly-owned subsidiary of Enertec Management Ltd., a private Israeli company wholly owned by Enertec Electronics.
- Micronet, an Israel-based manufacturer and developer of rugged computers, tablets and computer based systems whose shares are traded on the Tel Aviv Stock Exchange, or TASE, in which we acquired a controlling interest in September 2012 through Enertec Electronics. We currently own 52.26% of Micronet's outstanding common shares and 52% on a fully diluted basis.

#### Enertec

Enertec designs, develops and manufactures computer based instruments and aerospace electronic solutions designed to operate in severe environments and battlefield conditions, primarily for military use in air, space land and sea. Enertec's products are grouped into three material product lines: computer-based command and control systems, automatic test equipment and power supplies. These product lines generate approximately 90% of Enertec's annual revenues. The command and control systems are integrated in mission critical air defense missiles and other weapon systems and are designed to operate in severe environments. The automatic test equipment line includes a variety of test systems and simulators that test and assure combat readiness of aircraft and missiles. The power supplies are uniquely designed to support our systems and are also supporting our customers as stand-alone solutions. Enertec's solutions and systems are tailored to customers' specifications and are, or are integrated into, critical weapon systems. Among our main solutions are:

- ruggedized portable command and control systems
  - command and control stations
  - fire control systems for missiles
  - military aircraft support systems
- missile simulators

Enertec holds high security clearance in Israel for the most sensitive defense programs. Our solutions and systems are marketed mainly by the leading Israeli defense industries (system integrators) are used by the Israeli defense forces specifically by the Israeli Air Force and Israeli Navy as well as by other foreign defense entities served by our customers.

Enertec's quality control systems are ISO9000:2008 compliant. ISO9000:2008 is the international standard for quality assurance and quality design. This standard is important to customers that order custom-made products and is made up of a combination of quality system requirements.

Enertec generates revenue mostly through funded development, which involves the development of a small number of products, systems or solutions for evaluation. Thereafter we anticipate moving to production phase and generating revenue through direct sales from the mass production of its developed product. Enertec generates additional revenue from the customization and upgrades to its products.

## New products

In addition to our traditional systems and products, we have been developing new systems, solutions and products in the following areas: (i) operationally resilient computers integrated into various weapon systems, (ii) missile launch platforms, (iii) command and control systems, and (iv) missiles communications systems. These systems utilize advanced know-how developed by Enertec's trained and highly-skilled technical personnel. Management believes that Enertec's know-how and expertise will enable us to further increase our offerings to existing and other customers' strategic projects in space land, air and sea. In November 2013 we announced that Enertec was awarded by a multibillion Israel-based defense contractor working in partnership with a major US contractor in the international marketing of a state of the art missile defense system with a total of \$2.6 million valued order for the development and initial production of a computer-based test, diagnosis and simulation system to support the newest version of an advanced missile defense system.

### Market conditions

The defense market, in which we operate through Enerotec, includes the design and manufacturing of electronic systems developed to enhance large-scale military land, airborne and seaborne tactical platforms. These systems include military computer based systems, simulators, automatic test equipment and electronic instruments that are used or integrated in critical weapon systems such as command and control systems, missile fire control systems, support military aircraft systems and other defense systems and equipment such as night visions systems, unmanned aerial vehicle, or UAV, systems, laser products, airborne photography measures, processing and display of data systems and communications systems. In the Israeli defense market, Israeli providers supply a significant portion of their products to the Israeli defense forces specifically in view of the continuing defense needs of the State of Israel. However, the Israeli defense industry is also a well-respected exporter of its products to armies and defense forces worldwide and such international markets provide for stable demand for military and defense products. We expect a continuing demand in the missile defense niche based on the increasing threats of missile attacks throughout the world. We believe that we are well positioned with our unique know-how and expertise in missile technologies, and expect this segment of the market to be a major contributor to our growth and success in the coming years

### Marketing strategies

Our sales and marketing efforts focus on developing new business opportunities as well as generating follow-on sales from our existing customers. Our sales efforts are generated primarily through our internal sales team, although we also retain third-party selling agents from time to time. Various members of our senior management also serve as effective sales representatives who contribute to the generation of military and corporate business due to their long-standing customer relationships with leading industry integrators and knowledge of our customers' mission-critical technologies, requirements and needed solutions. We continue to explore various Israeli and international business partnerships to increase our sales and market penetration. We actively participate in trade shows involving technology and electronics defense operations. Additionally, our business development efforts include our website, preparation and distribution of marketing materials, advertising directed toward the defense and homeland security market and product demonstrations.

Our strategy is to anticipate the needs of our clients, the relevant market niches, to make investments in research and development (including developing know how, capable manpower) and initiate the development of those products and solutions that we believe will meet the market and customers' needs best. By doing so, we shorten our time to market, improve our market position from technology perspective, and gain an edge on our competition. Furthermore, we have been able to identify those current and potential clients that we believe are likely to place large orders, and we focus our attention on developing our relationship with them. When successful, we are in an excellent position to offer both basic and advanced, sophisticated products enabling us to expand our relationship with these clients and resulting in additional revenue streams. In these cases, deepening our relationship with our clients creates the opportunity to incorporate our solutions into our customers' core components and critical systems. By continuously diversifying into new and more complex products and fully scaled systems, we have been able to set Enerotec apart from its competition. We also continue to increase our suite of custom products based on our proprietary designs and technologies. These products are core components of several long-term military programs spearheaded by our customers, which historically have expected purchase lifecycles over periods of up to 10 years.

Since we expect a continuing demand for our products and solutions in the missile defense niche based on the increasing threats of missile attacks throughout the world we continue to concentrate marketing efforts in this segment of the market while we are well positioned with our unique know-how and expertise in missile technologies. We expect this segment to be a major contributor to our growth and success in the coming years.

As part of our strategy to become a global solution provider, Enertec is in the final process of becoming a certified supplier for the US DOD and for the NATO countries and initiated significant direct marketing efforts to the major US defense organizations.

## Customers

Enertec's customers are primarily leading Israeli defense system integrators. The system integrators' customers are the Israeli Ministry of Defense and other ministries of defense worldwide. The balance of our sales is made directly to the Israeli defense and armed forces (mainly the IDF) that place direct orders.

Approximately 90% of our annual revenues in the past two years were from independent business units or groups within Rafael and the IAI, the two leading Israeli defense system integrators. These distinct units and group create diversity to our business and revenue streams.

The system integrators that are our primary customers market their solutions throughout the world and across the full spectrum of military applications (land, sea and air). Management believes that the demand for our products, systems and solutions is not affected significantly by fluctuations in any particular geographic market outside the State of Israel because our products, systems and solutions can be tailored to fit the needs of these different disciplines and are not limited to any specific geography.

## Backlog

As of December 31, 2013, Enertec had a backlog of orders for our systems, products and services in the amount of approximately \$10.7 million (including \$2.3 million in framework orders, which are orders that can be exercised from time to time but are an obligation of ours for the entire amount). As of December 31, 2012, Enertec had a backlog of orders for our systems, products and services in the amount of approximately \$10.1 million (including \$0.6 million in framework orders).

## Competition

The defense market in which we operate through Enertec is fractured and our main competition comes from customers' internal development and manufacturing divisions and a number of relatively small Israeli companies that specialize in electronic systems.

## Suppliers

Our suppliers are diversified, and we are not dependent upon a limited number of suppliers for essential raw materials, components, services or other items. In order for us to maintain the standards required by our customers, we require that our suppliers be well-established, with facilities and manufacturing abilities that comply with our relevant standards. Although we are not dependent on any one supplier, disruptions in normal business arrangements due to the loss of one or a few suppliers could adversely affect us. Disruptions also may be experienced if our existing suppliers are no longer able to meet our requirements or if there is an industry shortage of electronic or mechanical components. Not only could these disruptions limit our production capacity, but also, if there is a shortage of components, such disruption could result in higher costs. The raw materials we use are either electronic components purchased from suppliers, or mechanical components primarily manufactured by local subcontractors.

## Employees

As of December 31, 2013, we had approximately 87 full-time employees at Enertec. Of these employees, 73 are employed in engineering and manufacturing positions, and the remainder are employed in sales, management and administrative positions. Our employees are not represented by any collective bargaining agreement, and we have never experienced a work stoppage. We believe we have good relations with our employees.

Israeli labor laws and regulations apply to all employees based in Israel. The laws principally covers matters such as paid vacation, paid sick days, length of the workday, payment for overtime and severance payments upon the retirement or death of an employee or termination of employment under specified circumstances. The severance payments may be funded, in whole or in part, through a managers' insurance fund or a pension fund. The payments to the managers' insurance fund or pension fund toward severance amount to 8.3% of wages. Furthermore, Israeli employees and employers are required to pay predetermined sums to the National Insurance Institute of Israel. Since January 1, 1995, these amounts also include payments for health insurance. The payments to the National Insurance Institute amount to approximately 14.5% of wages, of which the employee contributes 66% and the employer contributes 34%.

### Research and development expenditures

Research and development costs totaled approximately \$419,000 and \$218,000 for the years ended December 31, 2013 and 2012, respectively, which equates to approximately 4% and 2% of Enerotec's revenues respectively. These expenditures have adequately satisfied our research and development requirements. We are using our engineering resources to research and design new technologies, products and solutions that we expect to implement into the new projects and large military programs of our core customers.

### Seasonal aspects of our business

The sales of military products and solutions experience seasonal variations because the Israeli Ministry of Defense frequently delays project approvals until near the end of the fiscal year. Therefore, new orders to the military suppliers, including Enerotec, are delayed until the second half of the year. In addition, some of our customers require increased deliveries during the last weeks of the year in order to fulfill contractual delivery obligations to their own customers. As a result, we often experience an increase in our fourth quarter sales relative to sales in other quarters.

### Intellectual property

Although we are not dependent on patents or trademark protection with regard to Enerotec's business and do not expect to be at any time in the future, proprietary rights are important to Enerotec's business because its ability to remain competitive in the market is dependent to a significant degree on its proprietary solutions and the technologies on which they are based. Enerotec develops systems for its clients on a "work for hire" basis. Although, Enerotec does not claim any rights in the products or services that it provides, its proprietary modules and subsystems play an integral and significant part in the development of the products and services that it ultimately delivers. To protect its proprietary rights in these modules and subsystems, Enerotec primarily relies on a combination of copyright and trade secret laws, internal know-how, technological innovations and agreements with third parties, such as license agreements. In addition, Enerotec employs internal controls such as the use of confidentiality and non-disclosure agreements. Enerotec believes its proprietary technology incorporates processes, know-how, methods, algorithms, hardware and software that are the result of more than ten years of experience resulting in in-house expertise and thus are not easily copied. Further, most of the production process is performed in-house with the exception of certain components that are manufactured by subcontractors. This limited outsourcing process allows Enerotec to maintain the majority of its proprietary information and know-how within the company and lowers its exposure to the risk of its technology solutions being copied or used by any third parties.

Enerotec's management, together with its research and development team, closely and continuously monitors the technological developments in the market. Enerotec considers and evaluates on an ad hoc basis whether technology and proprietary assets should be acquired through independent in-house development or through the purchase of patent or other technology licenses.

### Regulation

Enerotec's electronic products must comply with the UL standards of the United States and CE standards of Europe to be eligible for sale in the respective countries subject to these standards. Each system must be tested, qualified and labeled under the relevant standards. This is a complicated and expensive process and once completed, the approved product may not be altered for sale.

### Micronet



Micronet is based in Azor, Israel, near Tel Aviv and is engaged in the design, development, manufacture and global marketing of rugged, automotive-grade, mobile computing devices for fleet and workforce management solutions with computing solutions in challenging work environments. Micronet operates in the MRM market. Micronet designs, develops, manufactures and sells rugged mobile computing devices that provide fleet operators and field workforces with computing solutions in challenging work environments. Micronet's vehicle cabin installed and portable tablets are design to increase workforce productivity, enhance corporate efficiency and customer service by offering computing power and communication capabilities. The Micronet products provide fleet operators among other with visibility into vehicle location, fuel usage, speed and mileage and allow the installation of software applications and communication integration enabling the users to manage the drivers in various aspects such as: driver identification, hours working report, customer/organization working procedures and protocols, rout management and navigation based on tasks and time schedule. End user may also receive real time messages for various services such as pickup and delivery, repair and maintenance, status reports, alerts, notices relating to start and ending of work, digital forms, issuing and printing of invoices and payments.

Micronet conducts its sales and support activities through its Israeli facilities in conjunction with sales offices in the United States and the United Kingdom. Micronet's customers are leading international MRM solution and service providers. The company maintains an in-house research and development staff and operates an ISO 9001-2008 certified manufacturing facility. With the exception of certain components purchased from subcontractors, Micronet manufactures its products and solutions using its own facilities, capabilities and resources, which enables it to control and manage the manufacturing process. Micronet combines more than 30 years of experience in the industry with strong technical capabilities to provide a broad range of products and solutions that have met the rigorous standards of our clients.

Micronet's ruggedized mobile computing devices are designed and manufactured to fit the special requirements of the MRM market, enabling customers to operate in challenging work environments, such as extreme temperatures, repeated vibrations or dirty and wet or dusty conditions. Micronet's products, in conjunction with available third-party mobile applications solutions, provide fleet operators with real-time visibility into vehicle location, fuel usage, speed and mileage, as well as other insights into their mobile workforce, reducing operating and capital costs while increasing revenue. Micronet's products are used in a wide range of MRM industry sectors, including:

- haulage and distribution, which includes short- and long- haul trucking and distribution servicing of urban retail and wholesale needs, such as delivery of packages, parts and similar items;
  - public transport, which refers mainly to buses, para-transit, taxis and limousine services;
- construction, which refers to vehicle fleets that are involved in the construction industry such as cement trucks and heavy equipment;
- service industries, which include insurance companies, rental car companies and other companies operating large mobile service force of technicians, installers and similar personnel;
  - municipalities, which include waste management and field workers such as public works; and
  - Public safety services, which includes fire departments, ambulances, police and forestry.

Micronet's products are fully programmable and provide customers with the operational flexibility to customize such products for their ongoing needs via a comprehensive development tool kit package that enables them to develop independently and support their own industry-specific applications and solutions.

Micronet's strategy is to continue to leverage its market position in the U.S. and European markets, to become a market leader for MRM products and services.

#### Recent developments

Micronet believes that awareness and demand for MRM solutions is significantly increasing as customers seek to optimize their mobile asset utilization of commercial vehicle fleets and enhance workforce productivity and customer satisfaction.

During 2013, Micronet launched a new product, the CE307, which is designed to satisfy the needs of certain strategic customers using its predecessor, the CE507 model. The CE307 aims to provide customers with enhanced features and capabilities, optimized for their specific requirements, at a lower cost than the CE507. Already, during 2013 Micronet has achieved significant sales of the CE307 to its customers.

Also, Micronet launched in the mid of 2013 its open platform solution, the A-300 family, an android based rugged tablet which was already selected by a leading North American solution provider in the Fleet Management industry. The A-300 tablet will be installed in large commercial fleets providing a comprehensive Fleet Management and Mobile Resource Management solution. With the A-300 on board, commercial fleet operators can go beyond standard 'track and trace' applications, to full mobile workforce management solutions, supporting Driver electronic logs, in-cab Navigation, in-cab Scanning and Printing, in-cab Video Driver training, two-way Messaging and Dispatch, Form-based status reporting, and more. In addition, the new A-300 series features Micronet's new patent-pending Guardian System Design (GSD), a solution that enables cloud based remote technical support and in-field device management over the life time of the product. Key functions include: (i) Remote device management, (ii) Software and hardware self-diagnostics and recovery, and (iii) Fail-safe Firmware and Application over the Air (OTA) updates. This is a SaaS offering that Micronet is implementing, based on a recurring revenue business model. As all other Micronet products, the A-300 is a fully programmable mobile computer, enabling independent application development, using Micronet's comprehensive hardware and software development toolkits. The tablet's advanced system architecture allows flexible integration with various vehicle systems and ancillary equipment used by drivers in and out of the cabin.

During the year ended December 31, 2013, Micronet sold 59,000 devices, compared to 69,000 devices during the year ended December 31, 2012. Its total revenue for the year ended December 31, 2013 decreased by approximately \$3 million or 10%, as compared to the year ended December 31, 2012. U.S. revenue was approximately 88% of the total revenue in the year ended December 31, 2013 as compared to approximately 92% of the total revenue in the year ended December 31, 2012.

Micronet's key initiatives for future revenue growth include the following:

- Expanding sales activities in the North American and European markets.
- Establishing strong relationships with new European and U.S. tier 1 customers and partners.
- Addressing the local fleet of MRM market with the new A-307 that is specifically designed to support sales to local fleets through multiple value added resellers by offering advanced features at competitive prices. To our knowledge, the local fleet market is considered to be among the leading largest and fastest growing segments of the MRM market.
- Supporting the two operating systems, Windows and Android, to satisfy a wider customer base, enabling independent application programming and integration with various mission critical automotive system and enterprise-level software solutions.
- Upgrading and enhancing current products and engaging in new product development based on input from clients and partners.
- Partnering with major truck manufacturers to develop a built-in, fit-to-purpose original equipment manufacturer, or OEM, platform.

Developments in the communication market in recent years have enabled Micronet to integrate its products into new standard technologies, which have reduced communication costs and extended availability, thereby increasing the demand for Micronet's products and solutions. Micronet has made significant investments in its facilities, infrastructures and manufacturing capabilities and has made product enhancements and strengthened functionality.

## Market opportunity

We believe that Micronet is well positioned to pursue a substantial market opportunity. The MRM market, in which we operate through Micronet, is growing and it will continue its double digit growth in the coming years. Clement Driscoll and Mark Licht in Mobile Resource Management Systems Overview; Telematics for Fleet Management USA 2013, dated November 20, 2013, or the Driscoll Licht Report, estimated that in 2013 globally there were approximately 17 million subscribers to MRM services and forecasted that the number will grow to approximately 32 million by 2016. Further as outlined in the Driscoll Licht Report, in the United States, which historically has been Micronet's largest market, there are currently approximately 6.6 million units in service with MRM systems, which number is projected to grow to approximately 10 million by end of 2016. In 2013, the global penetration rate of MRM systems was approximately 8%. The global penetration rate is forecasted to grow to approximately 14% by 2016.

## Products and Services

Micronet currently offers mobile computing devices grouped in three broad categories: Entry Level, Mid-Range and Advanced, that range from basic display products for two-way messaging communication to the CEseries, available in a variety of product configurations with greater functionality. For the year ended December 31, 2013, its advanced products represented approximately 90% of its revenues.

Advanced products (covers our premier tablet computers that have higher level of capability and functionality and are offered at high-end prices)

- CE500 series. It is a Microsoft WinCE based mobile computing platform, specifically designed for vehicle cabin mounted rugged computer and portable MRM applications. It offers either 7-inch (CE-507) or 4.3-inch (CE-504) touch color screens, fixed or portable. The platform features Microsoft Windows Embedded CE 6 operating system, supporting Compact Framework 3.5, and offers a comprehensive development environment for independent application programming and system integration. Its original layered architecture makes the CE-series highly modular and scalable, allowing for variable factory-set configurations by using plug-in modules. This cost effective design simplifies maintenance tasks, significantly extends product life expectancy and lowers total cost of ownership.
- CE300 series. Launched in 2-13, novel layered architecture enables OEMs, and telematics services providers, to remotely track the location and movements of vehicles and other assets, with a rugged, versatile, vehicle-centric and fixed-mount or portable mobile-computing platform for a variety of MRM applications.

Both models feature multiple, integrated wireless options: Quad band GPRS modem, GPS, Wi-Fi, and Bluetooth. All wireless options come with internal antennae. Physical interface options on these models include: USB, Serial RS-232 ports, dedicated interface for Dallas ID button reader, analog inputs, multiple digital inputs and outputs, and control signals for vehicle connectivity.

- A-300 family products. An open platform Android based rugged tablet designed for large commercial fleets providing a comprehensive Fleet Management and Mobile Resource Management solution. The A-300 product supports driver electronic logs, in-cab Navigation, in-cab Scanning and Printing, in-cab Video Driver training, two-way Messaging and Dispatch, Form-based status reporting, and more. In addition, the new A-300 series features Micronet's new patent-pending Guardian System Design (GSD), a solution that enables cloud based remote technical support and in-field device management over the life time of the product. Key functions include: (i) Remote device management (ii) Software and hardware self-diagnostics and recovery (iii) Fail-safe Firmware and Application over the Air (OTA) updates. This is a SaaS offering that Micronet is implementing, based on a recurring revenue business model. As all other Micronet products, the A-300 is a fully programmable mobile

computer, enabling independent application development, using Micronet's comprehensive hardware and software development toolkits. The tablet's advanced system architecture allows flexible integration with various vehicle systems and ancillary equipment used by drivers in and out of the cabin.

**Development Tool Kit.** Micronet's development package, also called Development Tool Kit, or DTK, is intended for customers who wish to develop their own applications and to support automatic vehicle location, or AVL/fleet management. The development package provides all the tools required for application development quick-start, product testing and product evaluation. ASPs, Value Added Resellers, Solution Providers and System Integrators, specializing in MRM, Asset Control, and Real Time Vehicle Data Monitoring rely on Micronet's flexible and cost-effective systems to supplement their AVL/fleet management, and Computer Aided Dispatching hardware and software solutions.

**Enhanced Technical Support and Professional Services.** Micronet provides enhanced technical support and expert development services, designed to facilitate its customers' development work in connection with Micronet's systems and reduce time to market. Technical and support services are offered in three levels of service:

- **DTK Support:** Standard support, offered at no extra charge, to customers that purchase Micronet's DTKs.
- **Developer Support Services:** Consultation by engineers on application development and integration tasks. The service is offered on a retainer basis and includes code review, debugging and software and hardware engineering consultation.
- **Professional Services — Custom Development:** Custom software application development and integration services that are quoted based on specific customer requirements, and managed by a Micronet project manager. Includes application design and system analysis, programming and integration, documentation and maintenance.

**Mid-Range products** (covers our products with mid-range level of capability and functionality that are offered at mid-range market prices):

- **Net-960CE-S.** Micronet's Net-960CE-S product family features an advanced WinCE.NET (supporting compact framework) development environment. Standard product configurations support an extended range of optional features and functions. These include wireless interfaces like GPS, GPRS, Wi-Fi, Disk on Chip and Bluetooth, as well as multiple vehicle I/O interfaces, communications and connectivity ports (USB, RS-232, J1708, CANBus) and support of peripheral devices, including an external, independent, 3rd party colored screen. The Net-960CE-S models are offered with a comprehensive DTK and software development packages for independent application development, backed by our technical support team.
- **Net-960CE-X.** Micronet's Net-960CE-X product family is a low-budget WinCE-based platform, utilizing C, C++, and Win32 API. It is designed as a rugged fixed-mount enclosure platform with advanced electronics. The Net-960CE-X platform features various interfaces, supporting peripheral devices, vehicle I/Os and wireless communication options, including built-in GPS and GPRS. The Net-960CE-X models are offered with a comprehensive Net-960CE-X DTK and software development kit, or SDK, for independent application development, supported by our technical support team.

**Entry Level products** (covers our more economical products with lower level of capability and functionality and offered at lower prices):

- **M Series (M100 and M200/M201).** Micronet's M-Series is a powerful, yet highly economical line of products, designed to enable versatile vehicle cabin-mounted rugged computer MRM applications. The M-Series is based on ThreadX, an advanced embedded, multithreading real time operating system. In the framework of the M-Series, Micronet offers two standard configurations: fixed mounted and detachable. A DTK and SDK are available, for independent integration and application development.





- Net-960CE. The Net-960E, based on Microsoft Windows CE, includes a range of features, rugged fixed-mount enclosure, advanced electronics and an open Microsoft-standards-based development environment that is highly versatile and scalable. The Net-960E is used for a variety of applications: driver log, interactive messaging, dispatch, status and form based reports. It offers connectivity through 2 RS-232 ports and I/Os to vehicle sensors. It also supports external peripherals, such as driver ID touch button, swipe card, bar-code wand and PS/2 keyboard interface. The Net-960E model has been superseded by the M-Series.

Micronet generates revenues primarily through the sale of its hardware products to service providers who sell those to end users. Micronet does not typically enter into service or maintenance contracts with respect to its products. Micronet customarily provides its customers with a 12-month warranty, with an option to extend such warranty, subject to the payment of applicable fees. Micronet's technical support and DTK support services generate the balance of Micronet's revenues.

### Strategy

Micronet's strategy includes targeting potentially larger scale transactions that we expect could result in higher revenue as well as increased gross margin and overall profitability. Micronet's continuously analyzes the needs of the various vertical markets in which it operates in order to best serve its customers' needs. Micronet's strategy is driven by, and focused on, both continued internal growth of its business through the development of new potential markets, new technologies and innovative systems and products as well as through acquisitions.

Key elements of Micronet's strategy include:

- Continuing to focus on specific vertical markets, major accounts and OEM relationships to achieve broad penetration of its products.
- Continuing to invest efforts in its technology and product development, through collaborations with its partners.
  - Marketing the economical CE300 product to broaden its current offerings.
  - Focusing in marketing efforts and penetration of the A-300 series products.
  - Penetrating and developing the truck OEM market.
- Partnering with and/or acquiring complementary technology to broaden and deepen its offerings and client base.

Micronet believes that one of its core competitive strengths is the breadth of its expertise in mobile data technologies, particularly in MRM technologies for the management of vehicle fleets and mobile workforces.

Micronet intends to enhance its existing products and develop new products by continuing to make significant investments in research and development. Micronet further intends to continue its strategy of internally developing products in order to enter new market segments by collaborating closely with its strategic customers to outline and develop next generation platforms.

Micronet is increasingly pursuing international opportunities. For example, Micronet is seeking to expand and continue penetration into the European market, primarily through its relationship with its exclusive distributor in the United Kingdom.

### Sales and Marketing

Micronet's customers consist primarily of ASPs, and solution providers specializing in the fleet and MRM markets. Currently, Micronet does not sell to end-users. Its customers are generally leading service providers of commercial solutions that integrate a wide range of positioning technologies and computing fleet communications in the MRM market, such as PeopleNet, which is a subsidiary of Trimble, and XRS Corporation, that have large-scale organizations and significant resources and in turn sell Micronet's products to end-users.

Micronet products are used by customers in 20 countries. Micronet's main target markets are currently the U.S. and European markets. The United States currently constitutes its largest market, representing approximately 88% of Micronet's revenue for the year ended December 31, 2013 and 92% for the year ended December 31, 2012. In any given year, a single customer may account for a significant portion of Micronet's revenues. For the year ended December 31, 2013, Trimble and PeopleNet (as a result of the acquisition of PeopleNet by Trimble) represented approximately 82.5% of Micronet's revenue. No other customer accounted for more than 9% of Micronet's revenue. For the year ended December 31, 2012, Micronet's largest customer, Trimble and PeopleNet, located in the United States, represented approximately 79% of its revenues. The next largest customer represented approximately 8% of its revenues.

In September 2011, Micronet signed an exclusive distribution agreement with a United Kingdom distributor for the marketing of its systems to the European market. The objective of this relationship is to expand and continue penetration into the European market. Micronet's products are sold under the exclusive distribution agreement by way of direct sales to customers referred by the distributor in exchange for a commission payable to the distributor.

As of December 31, 2013, in addition to its European distributor as described above, Micronet established a sales team composed of three sales managers who work closely with Micronet's customers on adapting its new upcoming products to customers' expectations and needs.

#### Research and Development

Micronet believes that one of its core competitive strengths is the breadth of its expertise in mobile data technologies, particularly in MRM technologies for the management of vehicle fleets and mobile workforces. Micronet has developed this expertise over a period of 30 years. It has an experienced engineering and product development team. In order to keep up with the rapid technology evolution and the changing needs of the markets in which it operates, Micronet intends to enhance its existing products and to develop new products, by continuing to make significant investments in research and development.

Micronet upgrades and enhances its existing products on an on-going basis, including based on input from its clients and partners and from other sources. Enhancements include the addition of capabilities, improvement of product functionality and performance, and adding features to the existing hardware in order to offer customers a variety of solutions. Micronet is in the pre-release phase of the CE300 series, a new, improved model of the CE500 series that is intended to provide its customers with enhanced features and capabilities, optimized for their specific requirements, at a lower cost.

Micronet seeks to design and manage product life cycles through a controlled and structured process. It involves customers and industry experts from its target markets in the definition and refinement of its product development. Product development emphasis is placed on meeting industry standards, ease of integration, cost reduction, design-for manufacturability, versatility and innovation, and quality and reliability.

During the fiscal years ended December 31, 2013 and 2012, Micronet spent NIS 8.6 million (approximately \$2.3 million) and NIS 6.2 million (approximately \$1.6 million), respectively, on research and development activities. Micronet uses its own resources to finance its research and development activities and none of the cost of such activities is borne by its customers.

In April 2013, Micronet Ltd submitted to the Israeli Office of the Chief Scientist (OCS) request for financial support within a framework of a research and development program for a new product. In September 2013, a funding for Micronet in a total amount of 5.5 million NIS (approximately \$ 1,571,000) was approved by the OCS. The funding is provided by the OCS for a period of one year (starting April 2013) at a level of 30% from the aforementioned amount.

To the date hereof, Micronet Ltd has received an amount of 1.082 Million NIS (approximately \$309,000) out of the approved OCS funding.

## Competition

Micronet operates in a highly competitive industry. Further, during the last few years, competition in the field of mobile computers has significantly increased with the mass entrance and introduction to the market of smartphones, tablets, and laptops, as well as various GPS-based hand-held devices featuring additional functionalities.

Micronet's current business is focused on customers that are implementing "tailor made" solutions characterized by highly professional, mission critical and complex technological solutions. These solutions are based on Micronet's products and must sustain and maintain performance under extreme and challenging field conditions for extended periods of time.

Micronet believes it has approximately six direct competitors operating in Micronet's main markets. Most of these competitors are private companies or companies that do not disclose their sales or other financial information, making it difficult to estimate Micronet's market share and position in the market. Micronet believes that its most significant competitors include: Beijer Electronics, Inc., Morey Corporation (U.S.A.), Mobile Devices Corporation, MOTIA Co. Ltd, Advantech Co., Ltd. and Garmin USA, Inc.

This intensely competitive industry is characterized by rapidly changing technologies, evolving industry standards, frequent new product introductions and changes in customer requirements. In order to maintain its competitive strength, Micronet must continue to develop and introduce on a timely and cost-effective basis, new products and product features which are in line with the technological developments and emerging industry standards and address the increasingly sophisticated needs of its customers.

Micronet's management believes its strongest competitive advantages are the durability of its products and reputation in the industry. Its competitive strengths include the following:

- 30 years of field-proven experience, including engineering and manufacturing know-how;
- ability to deliver solutions and products to organizations and customers that are leaders in their respective industries;
- ability to integrate advanced technological capabilities to develop new solutions and products with its own manufacturing infrastructures and facilities, with full control over the end-to-end production process and cost-efficiencies;
  - short "food chain" professional and direct marketing methodology focused on main target customers;
    - reputation as a leading supplier in relevant markets;
    - lasting working relationships with customers;
  - an experienced, dedicated and competent management team; and
- Proprietary technology and know-how that allows rapid configuration and implementation of new solutions to meet the special customer needs.

## Manufacturing

With the exception of certain components purchased from subcontractors, Micronet manufactures its products and solutions using its own facilities, capabilities and resources, which enables it to control and manage the manufacturing process and ensure timely delivery. The manufacturing process includes development of electronic cards, assembly of microchips on the electronic cards and the assembly thereof within the unit, final testing and quality tests. On a case by case basis, subcontractors specializing in certain development or manufacturing aspects may be retained to achieve improvement, efficiency or reduction of costs of development and/or manufacturing processes.

Following certain enhancements in its manufacturing and production capabilities in the last two years, Micronet has excess manufacturing capacity and has the ability to meet current or foreseeable manufacturing needs without making any significant investments. Implemented enhancements include:

- upgraded production and assembly line and purchased new machinery with significant higher component implementation scale;
- increased factory facilities and upgraded various infrastructures;
- entered into an agreement with a leading subcontractor in the field that operates two additional manufacturing facilities, has significant procurement and manufacturing capabilities and resources outside Israel that are available to Micronet;
- Certified subcontractors to perform manufacturing process to ensure flexible manufacturing infrastructures and deployment that can be used for disaster recovery scenarios or rapid increase in production needs.

If additional manufacturing resources are needed to meet increased demand for Micronet's products, manufacturing capacity can be enhanced by outsourcing manufacturing processes, recruiting and training additional employees, adding shifts to the labor cycle and purchasing additional manufacturing equipment and machinery or other required infrastructures.

#### Intellectual Property

Proprietary rights are important to Micronet's business because its ability to remain competitive in the market is dependent to a significant degree on its proprietary solutions and products and the technology on which they are based. To protect its proprietary rights, Micronet primarily relies on a combination of copyright and trade secret laws, internal know-how, and agreements with third parties, such as license agreements. In addition, Micronet employs internal controls such as the use of confidentiality and non-disclosure agreements. Micronet believes its proprietary technology incorporates processes, know-how, methods, algorithms, hardware and software that are the result of more than 20 years of experience and in-house expertise and thus are not easily copied. Further, most of the production process is performed in house with the exception of certain specific components that are manufactured by a subcontractor. This limited outsourcing process allows Micronet to maintain the majority of its proprietary information and know-how within the company and lowers its exposure to the risk of its products or solution being copied or used by any third parties.

There is a significant amount of litigation with respect to intellectual property in the industry in which Micronet operates. Micronet has not, to date, been the subject of any claims or proceedings with regards to infringement of third party's proprietary rights and it believes that its products, solutions and services do not violate or infringe any third party's intellectual property rights.

Micronet's management, together with its research and development team, monitor closely and continuously all technological developments in the market. Micronet considers and evaluates on an ad hoc basis whether technology and proprietary assets should be acquired through independent in-house development or through the purchase of patent or other technological licenses. Where the purchase of third party proprietary technology, solution or products is required and can be of advantage to its business, Micronet would purchase a license and pay appropriate royalties or license fees. Micronet currently has all third-party licenses that it believes are necessary to maintain and develop its business.

#### Government Regulation

Micronet's business is subject to certain international standards such as FCC Part 15B, FCC ID, CE, and RoHS which define compatibility of interface and telecommunications standards to those implemented in Europe by the European Commission and in the U.S. by the Federal Communications Commission. Its solutions and products also comply with the E-Mark European standard, which is the standard that defines the compatibility of interface and telecommunications to all appliances installed in and around an automobile.



## Employees

As of December 31, 2013, we had approximately 86 full-time employees at Micronet. Of these employees, 65 are employed in engineering and manufacturing positions and sales, and the remainder are employed development, management and administrative positions. Our employees are not represented by any collective bargaining agreement, and we have never experienced a work stoppage. We believe we have good and sustainable relations with our employees.

Israeli labor laws and regulations apply to all employees based in Israel. The laws principally concern matters such as paid vacation, paid sick days, length of the workday, payment for overtime and severance payments upon the retirement or death of an employee or termination of employment under specified circumstances. The severance payments may be funded, in whole or in part, through a managers' insurance fund or a pension fund. The payments to the managers' insurance fund or pension fund toward severance amount to 8.3% of wages. Furthermore, Israeli employees and employers are required to pay predetermined sums to the National Insurance Institute of Israel. Since January 1, 1995, these amounts also include payments for health insurance. The payments to the National Insurance Institute amount to approximately 14.5% of wages, of which the employee contributes 66% and the employer contributes 34%.

We, including our subsidiaries, employed an aggregate of 193 employees on December 31, 2013.

## SEGMENT REPORTING

Operating segments are based upon our internal organization structure, the manner in which our operations are managed and the availability of separate financial information. Following the purchase of controlling shares of Micronet in September 2012 we have two operating segments: defense and aerospace segment conducted by Enertec and mobile resource management conducted by Micronet. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" and our consolidated financial statements included in "Exhibits and Financial Statement Schedules" of this Annual Report for further financial information on our operating segments.

### Item 1A. Risk Factors.

Investing in our securities involves a high degree of risk. Investors should carefully consider the following risk factors, as well as the other information in this Annual Report (including our financial statements and the related notes appearing at the end of this report), before deciding whether to invest in our securities. Investment risks can be market-wide as well as unique to a specific industry or company. The market risks faced by an investor in our common stock are similar to the uncertainties faced by investors in a broad range of industries. There are, however, some risks that apply more specifically to the Company because our business is focused on developing, manufacturing, integrating and marketing globally rugged and military computers, tablets and computer based systems and instruments for the commercial, defense and aerospace markets. These customer relationships involve certain unique risks. Our business is also exposed mainly to common risks, such as the ongoing development of high technology products and the price, availability and quality of commodities and subsystems. Additional risks and uncertainties not presently known to us or that we currently deem immaterial also may impair our business operations. The occurrence of any of the following risks could harm our business, financial condition, results of operations or growth prospects. In that case, the trading price of our securities could decline, and investors may lose all or part of their investment.

### Risks Related to Our Business and Industry

Potential political, economic and military instability in Israel could adversely affect our operations. The principal offices and operating facilities of Enertec and Micronet are located in Israel. Accordingly, political, economic and military conditions in Israel directly affect our operations. 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 an increase in hostilities between Israel and the Palestinian Arabs, which has adversely affected the peace process and has negatively influenced Israel's relationship with its Arab citizens and several Arab countries, including the Israel-Gaza conflict. Such ongoing hostilities may hinder Israel's international trade relations and may limit the geographic markets where we can sell our products and solutions. Hostilities involving or threatening Israel, or the interruption or curtailment of trade between Israel and its present trading partners, could materially and adversely affect our operations.

In addition, Israel-based companies and companies doing business with Israel have been the subject of an economic boycott by members of the Arab League and certain other predominantly Muslim countries since Israel's establishment. Although Israel has entered into various agreements with certain Arab countries and the Palestinian Authority, and various declarations have been signed in connection with efforts to resolve some of the economic and political problems in the Middle East, we cannot predict whether or in what manner these problems will be resolved. Wars and acts of terrorism have resulted in significant damage to the Israeli economy, including reducing the level of foreign and local investment.

Furthermore, certain of our officers and employees may be obligated to perform annual reserve duty in the Israel Defense Forces and are subject to being called up for active military duty at any time. All Israeli male citizens who have served in the army are subject to an obligation to perform reserve duty until they are between 40 and 49 years old, depending upon the nature of their military service.

If we are unable to develop new products and maintain a qualified workforce we may not be able to meet the needs of our customers in the future.

Virtually all of the products that we produce and sell are highly engineered and require sophisticated manufacturing and system-integration techniques and capabilities. The markets and industry in which we operate are characterized by rapidly changing technologies. The products, systems and solutions needs of our customers change and evolve regularly. Accordingly, our future performance depends on our ability to develop and manufacture competitive products and solutions, and bring those products to market quickly at cost-effective prices. In addition, because of the highly specialized nature of our business, we must be able to hire and retain the skilled and qualified personnel necessary to perform the services required by our customers. If we are unable to develop new products that meet customers' changing needs or successfully attract and retain qualified personnel, our future revenues and earnings may be adversely affected.

We are dependent on the services of our executive officers, whose potential conflicts of interest may not permit us to effectively execute our business strategy. We currently depend on the continued services and performance of our executive officers, particularly David Lucatz, our Chairman and also Micronet's LTD chairman, Chief Executive Officer and President. Mr. Lucatz also serves as the President, Chairman and Chief Executive Officer of D.L. Capital Ltd., or DLC, the primary asset of which is its ownership of shares of our common stock. We have a management and consulting services agreement with DLC. Pursuant to a separate management and consulting services agreement, Mr. Lucatz has agreed to devote 60% of his time to Micronet matters for the three-year term of that agreement. Our business and results of operations may suffer if Mr. Lucatz, or any of our other executive officers or directors, is unable to devote the attention necessary to our overall business strategy and operations.

Developing new technologies entails significant risks and uncertainties that may cause us to incur significant costs and could have a material adverse effect on our operating results, financial condition, and/or cash flows. A significant portion of our business relates to developing sophisticated products and applications. New technologies may be untested or unproven. In addition, we may incur significant liabilities that are unique to our products and services. While we maintain insurance for some business risks, it is not practicable to obtain coverage to protect against all operational risks and liabilities. In addition, we may seek limitation of potential liability related to the sale and use of our products and systems. We may elect to provide products or services even in instances where we are unable to obtain such indemnification or qualification. Accordingly, we may be forced to bear substantial costs resulting from risks and uncertainties of our products and products under development, which could have a material adverse effect on our operating results, financial condition and/or cash flows.



If we are unable to effectively protect our proprietary technology, our business and competitive position may be harmed. Our success and ability to compete are dependent on our proprietary technology. The steps each of our operations, Enertec and Micronet, has taken to protect its proprietary rights may not be adequate and we may not be able to prevent others from using our proprietary technology. The methodologies and proprietary technology that constitute the basis of each of Enertec's and Micronet's solutions and products are not protected by patents. Existing trade secret, copyright and trademark laws and non-disclosure agreements to which each of Enertec and Micronet is a party offer only limited protection. Therefore, others, including Enertec's or Micronet's competitors, may develop and market similar solutions and products, copy or reverse engineer elements of Enertec's systems or Micronet's production lines, or engage in the unauthorized use of Enertec's or Micronet's intellectual property. Any misappropriation of Enertec's or Micronet's proprietary technology or the development of competitive technology may have a significant adverse effect on Enertec's or Micronet's ability to compete and may harm our business and financial position.

We may incur substantial costs as a result of litigation or other proceedings relating to intellectual property rights. Third parties may challenge the validity of Enertec's or Micronet's intellectual property rights or bring claims regarding Enertec's or Micronet's infringement of a third party's property rights. This may result in costly litigation or other time-consuming and expensive judicial or administrative proceedings, which could deprive us of valuable rights, cause us to incur substantial expenses and cause a diversion for technical and management personnel. An adverse determination may subject us to significant liabilities or require us to seek licenses that may not be available from third parties on commercially favorable terms, if at all. Further, if such claims are proven valid, through litigation or otherwise, we may be required to pay substantial financial damages or be required to discontinue or significantly delay the development, marketing, sale or licensing of the affected products and intellectual property rights.

Our earnings and margins may be negatively impacted if we are unable to perform under our contracts. When agreeing to contractual terms, our management makes assumptions and projections about future conditions or events. These projections assess:

- the productivity and availability of labor;
- the complexity of the work to be performed;
- the cost and availability of materials;
- the impact of delayed performance; and
- The timing of product deliveries.

If there is a significant change in one or more of these circumstances or estimates, or if we face unexpected contract costs, the profitability of one or more of these contracts may be adversely affected and could affect, among other things, our earnings and margins, due to the fact that our contracts are often made on a fixed-price basis.

Our earnings and margins could be negatively affected by deficient subcontractor performance or unavailable raw materials or components. We rely on other companies to provide raw materials, major components and subsystems for our products. Subcontractors perform some of the services that we provide to our customers. We depend on these subcontractors and vendors to meet our contractual obligations in full compliance with customer requirements. Occasionally, we rely on only one or two sources of supply that, if disrupted, could have an adverse effect on our ability to meet our commitments to customers. Our ability to perform our obligations as a prime contractor may be adversely affected if one or more of these suppliers is unable to provide the agreed-upon supplies or perform the agreed-upon services in a timely and cost-effective manner. Further, deficiencies in the performance of our subcontractors and vendors could result in a customer terminating a contract for default. A termination for default

could expose us to liability and adversely affect our financial performance and our ability to win new contracts.

We depend on major customers for a significant portion of our revenues and our future revenues and earnings could be negatively impacted by the loss or reduction of the demand for our products or services by such customers. A significant portion of our annual revenues in the past two years derived from a few leading customers that are large scale strategic Israeli defense groups (Rafael, IAI). Following the acquisition of Micronet, PeopleNet, a subsidiary of Trimble, which operates in the U.S. market, has been added as a major customer. In view of the above, as of December 31, 2013, we had three customers that combined account for approximately 85.13% of our revenues. This is in comparison to 2012 during which we had three customers which accounted for 80.95% of revenues as of December 31, 2012.

Israeli defense spending historically has been driven by perceived threats to the country's national security. Although Israel has been under a sustained elevated threat level in recent years, we cannot provide any assurance that its defense budget will continue to grow at the pace it has over the past decade. A decrease in Israel's defense spending or changes in spending allocation could result in one or more of our programs being reduced, delayed or terminated. Reductions in our existing programs could adversely affect our future revenues and earnings. In the MRM market, most of our major customers do not have any obligation to purchase additional products or services from us. Therefore, we cannot provide any assurance that any of our leading customers will continue to purchase solutions, products or services at levels comparable to previous years. A substantial loss or reduction in Micronet's existing programs could adversely affect our future revenues and earnings.

We operate in a highly competitive and fragmented market and may not be able to maintain our competitive position in the future. A number of larger competitors have recently entered the MRM market in which Micronet operates. These large companies have far greater development and capital resources than Micronet. Further, there are competitors of Micronet that offer solutions, products and services similar to those offered by Micronet. If they continue, these trends could undermine Micronet's competitive strength and position and adversely affect our earnings and financial condition.

Micronet may cease to be eligible for, or receive reduced, tax benefits under Israeli law, which could negatively impact our profits in the future. Micronet currently receives certain tax benefits under the Israeli Law for Encouragement of Capital Investments of 1959, as a result of the designation of its production facility as an "Approved Enterprise." To maintain its eligibility for these tax benefits, Micronet must continue to meet several conditions including, among others, generating more than 25% of its gross revenues outside the State of Israel and continuing to qualify as an "Industrial Company" under Israeli tax law. An Industrial Company, according to the applicable Israeli law (Law for the Encouragement of Industry (Taxes), 1969), is a company that resides in Israel (either incorporated in Israel or managed and controlled from Israel) that, during the relevant tax year, derives at least 90% of its income from an Industrial Factory. An Industrial Factory means a factory that is owned by an Industrial Company and where its manufacturing operations constitute a vast majority of the factory's total operations/business. The tax benefits of qualifying as an Industrial Company include a reduction of the corporate tax from 25% to 12% in 2013. In addition, in recent years the Israeli government has reduced the benefits available under this program and has indicated that it may further reduce or eliminate benefits in the future. There is no assurance that Micronet will continue to qualify for these tax benefits or that such tax benefits will continue to be available at their current level, or at all. The termination or reduction of these tax benefits would increase the amount of tax payable by Micronet and, accordingly, reduce its net profit after tax and negatively impact our profits.

Because almost all of our officers and directors are located in non-U.S. jurisdictions, you may have no effective recourse against our management for misconduct. Currently, a majority of our directors and officers are or will be nationals and/or residents of countries other than the United States, and all or a substantial portion of their assets are located outside the United States. As a result, it may be difficult for investors to enforce within the United States any judgments obtained against such officers or directors, including judgments predicated upon the civil liability provisions of the securities laws of the United States or any U.S. state. Additionally, it may be difficult to enforce civil

liabilities under U.S. securities law in original actions instituted in Israel. Israeli courts may refuse to hear a claim based on a violation of U.S. securities laws because Israel is not the most appropriate forum to bring such a claim. In addition, even if an Israeli court agrees to hear a claim, it may determine that Israeli law and not U.S. law is applicable to hear the claim. If U.S. law is found to be applicable, the content of applicable U.S. law must be proved as a fact, which can be a time-consuming and costly process. Certain matters of procedure will also be governed by Israeli law.



Our financial results may be negatively affected by foreign exchange rate fluctuations. Our revenues are mainly denominated in U.S. currency and our costs are mainly denominated in Israeli currency. Where possible, we match sales and purchases in these and other currencies to achieve a natural hedge. Currently, neither Enertec nor Micronet has a policy with respect to the use of derivative instruments for hedging purposes, except that both Enertec and Micronet will consider engaging in such hedging activities on a case by case basis. To the extent we are unable to fully match our sales and purchases in different currencies, our business will be exposed to fluctuations in foreign exchange rates.

If we fail to manage our growth, our business could be disrupted and our profitability could be reduced. We have experienced rapid growth in recent periods through both the acquisition of Micronet and organic growth. As a result of our acquisition of Micronet, the number of our employees has effectively doubled since September 2012. We expect our growth may significantly strain our management and other operational and financial resources. In particular, growth increases the integration challenges involved in recruiting, training and retaining skilled technical, marketing and management personnel; maintaining high quality standards; preserving our corporate culture, values and entrepreneurial environment; developing and improving our internal administrative infrastructure, particularly our financial, operational, communications and other internal controls; and maintaining high levels of client satisfaction. If we are unable to manage growth effectively, our business, financial condition and results of operations will be materially adversely affected.

Our quarterly revenues may fluctuate as a result of seasonal variation within the Israeli military procurement industry. Enertec's revenues experience seasonal variations because Israeli Ministry of Defense project approvals are frequently provided after the start of the fiscal year. Therefore, new orders to the military suppliers, including Enertec, are often delayed until the second half of the year. In addition, some of our customers require deliveries during the fourth quarter of the year in order to fulfill contractual delivery obligations to their own customers. As a result, we often experience an increase in our fourth quarter sales relative to sales in other quarters.

If our beneficial ownership of Micronet's ordinary shares declines, we may not be able to treat Micronet as our subsidiary, which may adversely affect our financial condition and results of operations. We currently hold 52.2% of Micronet's outstanding ordinary shares through our subsidiary Enertec Electronics. If we are unable to consider Micronet as a consolidated subsidiary, our financial condition and results of operations may be adversely affected and may cause interest in or the market price of our securities to decline.

#### Risks Related to Ownership of our Securities

Your ability to influence corporate decisions may be limited because ownership of our common stock is concentrated. As of March 28, 2014, Mr. Lucatz, our Chairman, Chief Executive Officer and President beneficially owns 2,597,200 shares, or approximately 44.54%, of our outstanding common stock. As a result, Mr. Lucatz, may effectively control matters requiring stockholder approval, including the election of directors and approval of significant corporate transactions. Such concentration of ownership may also have the effect of delaying or preventing a change in control of the company, and this may have a material adverse effect on the trading price of our common stock.

Provisions in our corporate charter documents and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management. Provisions in our certificate of incorporation, as amended, and amended and restated bylaws may discourage, delay or prevent a merger, acquisition or other change in control of us that stockholders may consider favorable, including transactions in which you might otherwise receive a premium for your common stock. These provisions could also limit the price that investors might be willing to pay in the future for our securities, thereby depressing the market price of our securities. In addition, these provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace

members of our board of directors. Because our board of directors is responsible for appointing the members of our management team, these provisions could in turn affect any attempt by our stockholders to replace current members of our management team.

Moreover, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the General Corporation Law of the State of Delaware, or the DGCL, which prohibits a person who owns in excess of 15% of our outstanding voting stock from merging or combining with us for a period of three years after the date of the transaction in which the person acquired in excess of 15% of our outstanding voting stock, unless the merger or combination is approved in a prescribed manner. We have not opted out of the restrictions under Section 203.

Our stockholders may experience significant dilution as a result of any additional financing using our equity securities and/or debt securities. To the extent that we raise additional funds by issuing equity securities or convertible debt securities, our stockholders may experience significant dilution. Sale of additional equity and/or convertible debt securities at prices below certain levels will trigger anti-dilution provisions with respect to certain securities we have previously sold. If additional funds are raised through a credit facility or the issuance of debt securities or preferred stock, lenders under the credit facility or holders of these debt securities or preferred stock would likely have rights that are senior to the rights of holders of our common stock, and any credit facility or additional securities could contain covenants that would restrict our operations.

If the price of our common stock is volatile, purchasers of our common stock could incur substantial losses. The price of our common stock has been, and may continue to be volatile. The market price of our common stock may be influenced by many factors, including but not limited to the following:

- announcements of developments related to our business;
- quarterly fluctuations in our actual or anticipated operating results;