

UBS AG  
Form 424B2  
February 22, 2019

**The information in this preliminary pricing supplement is not complete and may be changed. We may not sell these Notes until the pricing supplement, the accompanying product supplement, the index supplement and the accompanying prospectus (collectively, the “Offering Documents”) are delivered in final form. The Offering Documents are not an offer to sell these Notes and we are not soliciting offers to buy these Notes in any state where the offer or sale is not permitted.**

## **Subject to Completion**

### PRELIMINARY PRICING SUPPLEMENT

Dated February 22, 2019

Filed Pursuant to Rule 424(b)(2)

Registration Statement No. 333-225551

(To Prospectus dated October 31, 2018,

Index Supplement dated October 31, 2018

and Product Supplement dated October 31, 2018)

### **UBS AG \$• Trigger Autocallable Notes**

Linked to the least performing index between the Russell 2000<sup>®</sup> Index and the EURO STOXX 50<sup>®</sup> Index due on or about April 12, 2023

## **Investment Description**

UBS AG Trigger Autocallable Notes (the “Notes”) are unsubordinated, unsecured debt securities issued by UBS AG (“UBS” or the “issuer”) linked to the least performing index between the Russell 2000<sup>®</sup> Index and the EURO STOXX 50<sup>®</sup> Index (each, an “underlying asset” and together, the “underlying assets”). UBS will automatically call the Notes (an “automatic call”) if the closing level of each underlying asset on any observation date, including the final valuation date, is equal to or greater than its call threshold level, which is equal to a specified level that is less than its initial level, as indicated below. If the Notes are subject to an automatic call, UBS will pay on the applicable call settlement date following such observation date a cash payment per Note equal to the “call price”, which is your principal amount plus a call return based on the call return rate, and no further payments will be owed to you under the Notes. The call return increases the longer the Notes are outstanding. If the Notes are not subject to an automatic call and the closing level of each underlying asset on the final valuation date (the “final level”) is equal to or greater than its downside threshold, UBS will pay you a cash payment per Note equal to the principal amount. If, however, the Notes are not subject to an automatic call and the final level of any underlying asset is less than its downside threshold, UBS will pay you a cash payment per Note that is less than the principal amount, if anything, resulting in a percentage loss on your initial investment equal to the underlying return of the least performing underlying asset and, in extreme situations, you could lose all of your initial investment. The “least performing underlying asset” is the underlying asset with the lowest underlying return as compared to any other underlying asset. **Investing in the Notes involves significant risks. You may lose a significant portion or all of your initial investment. You will be exposed to the market risk of each underlying asset on each observation date and on the final valuation date and any decline in the level of one underlying asset may negatively affect your return and will not be offset or mitigated by a lesser decline or any**

**potential increase in the level of any other underlying asset. Higher call return rates are generally associated with a greater risk of loss and a greater risk that the Notes will not be subject to an automatic call. Any payment on the Notes, including any repayment of principal, is subject to the creditworthiness of UBS. If UBS were to default on its payment obligations you may not receive any amounts owed to you under the Notes and you could lose all of your initial investment.**

**Features**

**q Automatic Call Feature** — UBS will automatically call the Notes if the closing level of each underlying asset on any observation date, including the final valuation date, is equal to or greater than its call threshold level, which is equal to a specified level that is less than its initial level, as indicated below. If the Notes are subject to an automatic call, UBS will pay on the applicable call settlement date a cash payment per Note equal to the call price for the relevant observation date. The call return increases the longer the Notes are outstanding. Following an automatic call, no further payments will be owed to you under the Notes.

**q Contingent Repayment of Principal at Maturity with Potential for Full Downside Market Exposure** — If by maturity the Notes have not been subject to an automatic call and the final level of each underlying asset is equal to or greater than its downside threshold, UBS will pay you a cash payment per Note equal to the principal amount. If, however, the final level of any underlying asset is less than its downside threshold, UBS will pay you a cash payment per Note that is less than the principal amount, if anything, resulting in a percentage loss on your initial investment equal to the underlying return of the least performing underlying asset. The contingent repayment of principal applies only if you hold the Notes to maturity. Any payment on the Notes, including any repayment of principal, is subject to the creditworthiness of UBS.

**Key Dates\***

Trade Date**	March 22, 2019
Settlement Date**	March 29, 2019
Observation Dates	Annually (see page 2)
Final Valuation Date	April 5, 2023
Maturity Date	April 12, 2023

\* Expected. See page 2 for additional details.

We expect to deliver the Notes against payment on or about the fifth business day following the trade date. Under Rule 15c6-1 of the Securities Exchange Act of 1934, as amended, trades in the secondary market generally are

\*\* required to settle in two business days (T+2), unless the parties to a trade expressly agree otherwise. Accordingly, purchasers who wish to trade the Notes in the secondary market on any date prior to two business days before delivery of the Notes will be required, by virtue of the fact that each Note initially will settle in five business days (T+5), to specify alternative settlement arrangements to prevent a failed settlement of the secondary market trade.

**Notice to investors: the Notes are significantly riskier than conventional debt instruments. The issuer is not necessarily obligated to repay the principal amount of the Notes at maturity, and the Notes may have the same downside market risk as the least performing underlying asset. This market risk is in addition to the credit risk inherent in purchasing a debt obligation of UBS. You should not purchase the Notes if you do not understand or are not comfortable with the significant risks involved in investing in the Notes.**

**You should carefully consider the risks described under “Key Risks” beginning on page 4 and under “Risk Factors” beginning on page PS-9 of the accompanying product supplement before purchasing any Notes. Events relating to any of those risks, or other risks and uncertainties, could adversely affect the market value of, and the return on, your Notes. You may lose a significant portion or all of your initial investment in the Notes. The Notes will not be listed or displayed on any securities exchange or any electronic communications network.**

**Note Offering**

These preliminary terms relate to the Notes. The final terms of the Notes will be set on the trade date.

Underlying Assets	Bloomberg Tickers	Call Return Rate*	Initial Levels	Downside Thresholds	Call Threshold Levels	CUSIP	ISIN
Russell 2000® Index	RTY	At least 11.25% per annum	•	70.00% of the Initial Level	90.00% of the Initial Level	90270KYG8	US90270KYG83
EURO STOXX 50® Index	SX5E		•	70.00% of the Initial Level	90.00% of the Initial Level		

\* The call return is based on the call return rate (to be set on the trade date) and will vary depending on whether, and if called, the call settlement date on which, the Notes are called.

The estimated initial value of the Notes as of the trade date is expected to be between \$956.10 and \$986.10. The range of the estimated initial value of the Notes was determined on the date hereof by reference to UBS' internal pricing models, inclusive of the internal funding rate. For more information about secondary market offers and the estimated initial value of the Notes, see "Key Risks — Fair value considerations" and "— Limited or no secondary market and secondary market price considerations" beginning on page 5 herein.

**See "Additional Information about UBS and the Notes" on page ii. The Notes will have the terms set forth in the accompanying product supplement relating to the Notes, dated October 31, 2018, the accompanying prospectus and this document.**

**Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these Notes or passed upon the adequacy or accuracy of this document, the accompanying product supplement, index supplement or accompanying prospectus. Any representation to the contrary is a criminal offense.**

The Notes are not bank deposits and are not insured by the Federal Deposit Insurance Corporation or any other governmental agency.

**Offering of Notes**

	Issue Price to Public		Underwriting Commissions and Fees <sup>(1)</sup>		Proceeds to UBS AG <sup>(1)</sup>	
	Total	Per Note	Total	Per Note	Total	Per Note
Notes linked to the least performing index between the Russell 2000® Index and the EURO STOXX 50® Index	\$•	\$1,000.00	\$•	\$0.00	\$•	\$1,000.00

<sup>(1)</sup> Our affiliate, UBS Securities LLC, will pay an unaffiliated third-party dealer a structuring fee of \$4.00 per Note with respect to some or all of the Notes. This amount will be deducted from amounts remitted to UBS. All sales of the Notes will be made to certain fee-based advisory accounts for which an unaffiliated third-party is an advisor.

**UBS Securities LLC UBS Investment Bank**

### **Additional Information about UBS and the Notes**

UBS has filed a registration statement (including a prospectus, as supplemented by an index supplement and a product supplement for the Notes) with the Securities and Exchange Commission (the “SEC”) for the Notes to which this document relates. Before you invest, you should read these documents and any other documents related to the Notes that UBS has filed with the SEC for more complete information about UBS and the Notes. You may obtain these documents for free from the SEC website at [www.sec.gov](http://www.sec.gov). Our Central Index Key, or CIK, on the SEC website is 0001114446.

### **You may access these documents on the SEC website at [www.sec.gov](http://www.sec.gov) as follows:**

Market-Linked Securities product supplement dated October 31, 2018:

<http://www.sec.gov/Archives/edgar/data/1114446/000091412118002085/ub47016353-424b2.htm>

Index Supplement dated October 31, 2018:

<http://www.sec.gov/Archives/edgar/data/1114446/000091412118002083/ub46174419-424b2.htm>

Prospectus dated October 31, 2018:

<http://www.sec.gov/Archives/edgar/data/1114446/000119312518314003/d612032d424b3.htm>

References to “UBS”, “we”, “our” and “us” refer only to UBS AG and not to its consolidated subsidiaries. In this document, “Trigger Autocallable Notes” or the “Notes” refer to the Notes that are offered hereby. Also, references to the “accompanying product supplement” mean the UBS product supplement, dated October 31, 2018, references to the “index supplement” mean the UBS index supplement, dated October 31, 2018 and references to “accompanying prospectus” mean the UBS prospectus, titled “Debt Securities and Warrants,” dated October 31, 2018.

This document, together with the documents listed above, contains the terms of the Notes and supersedes all other prior or contemporaneous oral statements as well as any other written materials including all other prior pricing terms, correspondence, trade ideas, structures for implementation, sample structures, brochures or other educational materials of ours. You should carefully consider, among other things, the matters set forth in “Key Risks” beginning on page 4 and in “Risk Factors” beginning on page PS-9 of the accompanying product supplement, as the Notes involve risks not associated with conventional debt securities. We urge you to consult your investment, legal, tax, accounting and other advisors before deciding to invest in the Notes.

If there is any inconsistency between the terms of the Notes described in the accompanying prospectus, the accompanying product supplement, the index supplement and this document, the following hierarchy will govern: first, this document; second, the accompanying product supplement; third, the index supplement and last, the accompanying prospectus.

UBS reserves the right to change the terms of, or reject any offer to purchase, the Notes prior to their issuance. In the event of any changes to the terms of the Notes, UBS will notify you and you will be asked to accept such changes in connection with your purchase. You may also choose to reject such changes in which case UBS may reject your offer to purchase.

## **Investor Suitability**

### **The Notes may be suitable for you if:**

..You fully understand the risks inherent in an investment in the Notes, including the risk of loss of a significant portion or all of your initial investment.

You understand and accept that an investment in the Notes is linked to the performance of the least performing underlying asset and not a basket of the underlying assets, that you will be exposed to the individual market risk of each underlying asset on each observation date, including the final valuation date, and that you may lose a significant portion or all of your initial investment if the final level of any underlying asset is less than its downside threshold on the final valuation date.

You can tolerate a loss of a significant portion or all of your initial investment and are willing to make an investment that may have the same downside market risk as a hypothetical investment in the least performing underlying asset or the stocks comprising the least performing underlying asset.

You believe that the closing level of each underlying asset will be equal to or greater than its call threshold level on one of the specified observation dates, including the final valuation date, and you believe that the level of each underlying asset will appreciate over the term of the Notes by a percentage that is less than the call return rate (to be set on the trade date).

..You can accept that the risks of each underlying asset are not mitigated by the performance of any other underlying asset and the risks of investing in securities with a return based on the performance of multiple underlying assets.

You understand and accept that you will not participate in any appreciation of any underlying asset, that your potential return is limited to the call return and you would be willing to invest in the Notes if the call return rate was set equal to the call return rate indicated on the cover hereof (the actual call return rate will be set on the trade date).

..You would be willing to invest in Notes based on the call threshold levels and the downside thresholds indicated on the cover hereof.

..You can tolerate fluctuations in the price of the Notes prior to maturity that may be similar to or exceed the downside fluctuations in the levels of the underlying assets.

..You do not seek guaranteed current income from your investment and are willing to forgo any dividends paid on the stocks comprising the underlying assets (the "underlying equity constituents").

..You are willing to invest in Notes that may be subject to an automatic call and you are otherwise willing to hold such Notes to maturity and you accept that there may be little or no secondary market for the Notes.

..You understand and are willing to accept the risks associated with the underlying assets.

..You are willing to assume the credit risk of UBS for all payments under the Notes, and understand that if UBS defaults on its obligations you may not receive any amounts due to you including any repayment of principal.

You understand that the estimated initial value of the Notes determined by our internal pricing models is lower than the issue price and that should UBS Securities LLC or any affiliate make secondary markets for the Notes, the price (not including their customary bid-ask spreads) will temporarily exceed the internal pricing model price.

### **The Notes may not be suitable for you if:**

..You do not fully understand the risks inherent in an investment in the Notes, including the risk of loss of a significant portion or all of your initial investment.

You do not understand or are unwilling to accept that an investment in the Notes is linked to the performance of the least performing underlying asset and not a basket of the underlying assets, that you will be exposed to the individual market risk of each underlying asset on each observation date, including the final valuation date, or that you may lose a significant portion or all of your initial investment if the final level of any underlying asset is less than its downside threshold on the final valuation date.

..You require an investment designed to provide a full return of principal at maturity.

You cannot tolerate a loss of all or a significant portion of your investment and you are not willing to make an investment that may have the same downside market risk as an investment in the least performing underlying asset or its underlying equity constituents.

..You believe that the level of at least one underlying asset will decline during the term of the Notes and is likely to be less than its call threshold level on the specified observation dates, including the final valuation date, or, that the level of each underlying asset will appreciate over the term of the Notes by a percentage that is greater than the call return

rate (to be set on the trade date).

You cannot accept that the risks of each underlying asset are not mitigated by the performance of any other underlying asset or the risks of investing in securities with a return based on the performance of multiple underlying assets.

You believe that the final level of any underlying asset will be less than its downside threshold on the final valuation date.

You seek an investment that participates in the full appreciation in the levels of the underlying assets or that has unlimited return potential, or you would be unwilling to invest in the Notes if the call return rate was set equal to the call return rate indicated on the cover hereof (the actual call return rate will be set on the trade date).

You would be unwilling to invest in Notes based on the call threshold levels or the downside thresholds indicated on the cover hereof.

You cannot tolerate fluctuations in the price of the Notes prior to maturity that may be similar to or exceed the downside fluctuations of the underlying assets.

You seek guaranteed current income from this investment or prefer to receive any dividends paid on the underlying equity constituents.

You are unable or unwilling to invest in Notes that may be subject to an automatic call, you are otherwise unable or unwilling to hold the Notes to maturity or you seek an investment for which there will be an active secondary market for the Notes.

You do not understand or are unwilling to accept the risks associated with the underlying assets.

You are not willing to assume the credit risk of UBS for all payments under the Notes, including any repayment of principal.

**The suitability considerations identified above are not exhaustive. Whether or not the Notes are a suitable investment for you will depend on your individual circumstances and you should reach an investment decision only after you and your investment, legal, tax, accounting and other advisors have carefully considered the suitability of an investment in the Notes in light of your particular circumstances. You should review “Information About the Underlying Assets” herein for more information on the underlying assets. You should also review carefully the “Key Risks” section herein for risks related to an investment in the Notes.**

**Preliminary Terms**

Issuer	UBS AG London Branch
Principal Amount	\$1,000 per Note
Term	Approximately 4 years, subject to an automatic call. In the event that we make any change to the expected trade date and settlement date, the calculation agent may adjust the observation dates and call settlement dates (including the final valuation date and maturity date) to ensure that the stated term of the Notes remains the same.
Underlying Assets	The Russell 2000 <sup>®</sup> Index and the EURO STOXX 50 <sup>®</sup> Index.
Automatic Call Feature	UBS will automatically call the Notes if the closing level of each underlying asset on any observation date, including the final valuation date, is equal to or greater than its call threshold level. If the Notes are subject to an automatic call, UBS will pay on the call settlement date a cash payment per Note equal to the call price for the relevant observation date. Following an automatic call, no further payments will be made on the Notes.
Call Return Rate	The call return rate will be at least 11.25% per annum and will be set on the trade date.
Call Return	The call return increases the longer the Notes are outstanding and is based upon the call return rate.
Call Price	The call price equals the principal amount per Note plus the applicable call return. The table below assumes a call return rate of 11.25% per annum. The actual call return rate will be set on the trade date.

Observation Date <sup>(1)</sup>	Call Settlement Date <sup>(1)(2)</sup>	Call Return	Call Price (per Note)
April 1, 2020	April 8, 2020	11.25%	\$1,112.50
April 7, 2021	April 14, 2021	22.50%	\$1,225.00
April 6, 2022	April 13, 2022	33.75%	\$1,337.50
Final Valuation Date	Maturity Date	45.00%	\$1,450.00

<sup>(1)</sup> Subject to the market disruption event provisions set forth under “General Terms of the Securities — Market Disruption Events” in the accompanying product supplement.

<sup>(2)</sup> Five business days following the relevant observation date, except that the call settlement date for the final valuation date is the maturity date.

Payment at Maturity (per Note) **If the Notes are not subject to an automatic call and the final level of each underlying asset is equal to or greater than its downside threshold**, UBS will pay you a cash payment that is equal to:

Principal Amount of \$1,000

**If the Notes are not subject to an automatic call and the final level of at least one underlying asset is less than its downside threshold**, UBS will pay you a cash payment that is less than the principal amount, if anything, equal to:

$\$1,000 \times (1 + \text{Underlying Return of the Least Performing Underlying Asset})$

**In this scenario, you will suffer a percentage loss on your initial investment equal to the underlying return of the least performing underlying asset, regardless of the underlying return of any other underlying asset.**

**Least Performing Underlying Asset** The underlying asset with the lowest underlying return as compared to any other underlying asset.

For each underlying asset, the quotient, expressed as a percentage of the following formula:

**Underlying Return**  $\frac{\text{Final Level} - \text{Initial Level}}{\text{Initial Level}}$

**Call Threshold Level<sup>(3)</sup>** For each underlying asset, a specified level that is less than its initial level, based on a percentage of its initial level, as indicated on the cover hereof.

**Downside Threshold<sup>(3)</sup>** For each underlying asset, a specified level that is less than its initial level, based on a percentage of its initial level, as indicated on the cover hereof.

**Initial Level<sup>(3)</sup>** The closing level of each underlying asset on the trade date.

**Final Level<sup>(3)</sup>** The closing level of each underlying asset on the final valuation date.

<sup>(3)</sup> As determined by the calculation agent and as may be adjusted as described under “General Terms of the Securities — Discontinuance of or Adjustment to an Underlying Index; Alteration of Method of Calculation”, as described in the accompanying product supplement.



## Investment Timeline

**Trade Date** - The initial level of each underlying asset is observed and the final terms of the Notes are set.

**Observation Dates (Annually)** - The Notes will be subject to an automatic call if the closing level of each underlying asset on any observation date, including the final valuation date, is equal to or greater than its call threshold level.

- If the Notes are subject to an automatic call, UBS will pay on the call settlement date a cash payment per Note equal to the call price for the relevant observation date. Following an automatic call, no further payments will be made on the Notes.

- The final level of each underlying asset is observed on the final valuation date and the underlying return of each underlying asset is calculated.

**If the Notes are not subject to an automatic call and the final level of each underlying asset is equal to or greater than its downside threshold,** UBS will pay you a cash payment that is equal to:

Principal Amount of \$1,000

**Maturity Date** **If the Notes are not subject to an automatic call and the final level of at least one underlying asset is less than its downside threshold,** UBS will pay you a cash payment that is less than the principal amount, if anything, equal to:

$\$1,000 \times (1 + \text{Underlying Return of the Least Performing Underlying Asset})$

**In this scenario, you will suffer a percentage loss on your initial investment equal to the underlying return of the least performing underlying asset, regardless of the underlying return of any other underlying asset.**

**Investing in the Notes involves significant risks. You may lose a significant portion or all of your initial investment. Any payment on the Notes, including any repayment of principal, is subject to the creditworthiness of UBS. If UBS were to default on its payment obligations, you may not receive any amounts owed to you under the Notes and you could lose all of your initial investment.**

**If the Notes are not subject to an automatic call, you may lose a significant portion or all of your initial investment. Specifically, if the Notes are not subject to an automatic call and the final level of any underlying asset is less than its downside threshold, you will lose a percentage of your principal amount equal to the underlying return of the least performing underlying asset and, in extreme situations, you could lose all of your initial investment. You will be exposed to the market risk of each underlying asset on each observation date, including the final valuation date, and any decline in the level of one underlying asset may negatively affect your return and will not be offset or mitigated by a lesser decline or any potential increase in the level of any other underlying asset.**

## Key Risks

An investment in the Notes involves significant risks. Investing in the Notes is not equivalent to a hypothetical investment in the least performing underlying asset or its underlying equity constituents. Some of the key risks that apply to the Notes are summarized below, but we urge you to read the more detailed explanation of risks relating to the Notes in the “Risk Factors” section of the accompanying product supplement. We also urge you to consult your investment, legal, tax, accounting and other advisors before you invest in the Notes.

**Risk of loss at maturity** — The Notes differ from ordinary debt securities in that UBS will not necessarily repay the principal amount of the Notes at maturity. If the Notes are not subject to an automatic call and the final level of any underlying asset is less than its downside threshold, you will lose a percentage of your principal amount equal to the underlying return of the least performing underlying asset and, in extreme situations, you could lose all of your initial investment.

**The contingent repayment of principal applies only at maturity** — You should be willing to hold your Notes to maturity. If you are able to sell your Notes prior to an automatic call or maturity in the secondary market, you may have to sell them at a loss relative to your initial investment even if the level of each underlying asset at that time is equal to or greater than its downside threshold and call threshold level. All payments on the Notes are subject to the creditworthiness of UBS.

**No interest payments** — UBS will not pay any interest with respect to the Notes.

**Your potential return on the Notes is limited to any call return and you will not participate in any appreciation of any underlying asset or underlying equity constituent** — The return potential of the Notes is limited to the pre-specified call return resulting from an automatic call regardless of any appreciation of any underlying asset. Investors will not participate in any appreciation in the closing level of any underlying asset from its initial level. The Notes will only be subject to an automatic call if the closing level or the final level, as applicable, of each underlying asset is equal to or greater than its call threshold level. In addition, because the call return increases the longer the Notes have been outstanding, the call price payable with respect to earlier observation dates is less than the call price payable with respect to later observation dates. The earlier a Note is subject to an automatic call, the lower your return will be. Because the Notes may be subject to an automatic call as early as the first potential call settlement date, the total return on the Notes could be less than if the Notes remained outstanding until maturity. Furthermore, if the Notes are not subject to an automatic call and the final level of at least one underlying asset is less than its downside threshold, you will be subject to the decline in the level of the least performing underlying asset even though you cannot participate in any appreciation in the level of any underlying asset. As a result, the return on an investment in the Notes could be less than the return on a hypothetical direct investment in any or all of the underlying assets or underlying equity constituents. In addition, as an owner of the Notes, you will not have voting rights or any other rights of a holder of any underlying equity constituent.

**A higher call return rate or lower downside thresholds or call threshold levels may reflect greater expected volatility of each underlying asset, and greater expected volatility generally indicates an increased risk of loss at maturity** — The economic terms for the Notes, including the call return rate, call threshold levels and downside thresholds, are based, in part, on the expected volatility of each underlying asset at the time the terms of the Notes are set. “Volatility” refers to the frequency and magnitude of changes in the level of each underlying asset. The greater the expected volatility of each underlying asset as of the trade date, the greater the expectation is as of that date that the closing level or the final level, as applicable, of each underlying asset could be less than its call threshold level on any observation date (including the final valuation date) and that the final level of each underlying asset could be less than its downside threshold on the final valuation date and, as a consequence, indicates an increased risk of the Notes not being subject to an automatic call and an increased risk of loss, respectively. All things being equal, this greater expected volatility will generally be reflected in a higher call return rate than the yield payable on our conventional debt securities with a similar maturity or on otherwise comparable securities, and/or lower downside thresholds and/or call threshold levels than those terms on otherwise comparable securities. Therefore, a relatively higher call return rate may indicate an increased risk of loss. Further, relatively lower downside thresholds and/or call threshold levels may not necessarily indicate that the Notes have a greater likelihood of a return of principal at maturity and/or paying the call return. You should be willing to accept the downside market risk of the least

performing underlying asset and the potential to lose a significant portion or all of your initial investment.

**Reinvestment risk** — The Notes will be subject to an automatic call if the closing level of each underlying asset is equal to or greater than its call threshold level on any observation date set forth herein. Because the Notes could be subject to an automatic call as early as the first potential call settlement date, the term of your investment may be limited. In the event that the Notes are subject to an automatic call, there is no guarantee that you would be able to reinvest the proceeds at a comparable return and/or with a comparable call return rate for a similar level of risk. In addition, to the extent you are able to reinvest such proceeds in an investment comparable to the Notes, you may incur transaction costs such as dealer discounts and/or fees and hedging costs built into the price of the new securities. Generally, however, the longer the Notes remain outstanding, the less likely the Notes will be subject to an automatic call due to the decline in the level of an underlying asset and the shorter time remaining for the level of any such underlying asset to recover. Such periods generally coincide with a period of greater risk of principal loss on your Notes.

**You are exposed to the market risk of each underlying asset** — Your return on the Notes is not linked to a basket consisting of the underlying assets. Rather, it will be contingent upon the performance of each underlying asset. Unlike an instrument with a return linked to a basket of indices, common stocks or other underlying securities, in which risk is mitigated and diversified among all of the components of the basket, you will be exposed equally to the risks related to each underlying asset. Poor performance by any underlying asset over the term of the Notes will negatively affect your return and will not be offset or mitigated by a positive performance by any other underlying asset. For instance, you may receive a negative return equal to the underlying return of the least performing underlying asset if the final level of any underlying asset is less than its downside threshold, even if the underlying return of any other underlying asset is positive or has not declined as much. Accordingly, your investment is subject to the market risk of each underlying asset.

**Because the Notes are linked to the least performing underlying asset, you are exposed to a greater risk of not receiving the call return and losing a significant portion or all of your initial investment at maturity than if the Notes were linked to a single underlying asset or fewer underlying assets** — The risk that you will not receive the call return and will lose a significant portion or all of your initial investment in the Notes is greater if you invest in the Notes than the risk of investing in substantially similar securities that are linked to the performance of only one underlying asset or fewer underlying assets, as applicable. With more underlying assets, it is more likely that the closing level or final level of any underlying asset will be less than its call threshold level or downside threshold on any observation date or the final valuation date, respectively, than if the Notes were linked to a single underlying asset or fewer underlying assets, as applicable.

In addition, the lower the correlation is between the performance of a pair of underlying assets, the more likely it is that one of the underlying assets will decline in value to a closing level or final level, as applicable, that is less than its call threshold level or downside threshold on any observation date or on the final valuation date. Although the correlation of the underlying assets' performance may change over the term of the Notes, the economic terms of the Notes, including the call return rate, downside thresholds and call threshold levels are determined, in part, based on the correlation of the underlying assets' performance calculated using our internal models at the time when the terms of the Notes are finalized. All things being equal, a higher call return rate and lower downside thresholds and call threshold levels are generally associated with lower correlation of the underlying assets. Therefore, if the performance of a pair of underlying assets is not correlated to each other or is negatively correlated, the risk that you will not receive the call return or that the final level of any underlying asset is less than its downside threshold will occur is even greater despite a lower call threshold level and/or downside threshold. Therefore, it is more likely that you will not receive the call return and that you will lose a significant portion or all of your initial investment at maturity.

**Credit risk of UBS** — The Notes are unsubordinated, unsecured debt obligations of UBS and are not, either directly or indirectly, an obligation of any third party. Any payment to be made on the Notes, including any repayment of principal, depends on the ability of UBS to satisfy its obligations as they come due. As a result, UBS' actual and perceived creditworthiness may affect the market value of the Notes. If UBS were to default on its obligations, you may not receive any amounts owed to you under the terms of the Notes and you could lose all of your initial investment.

**Market risk** — The return on the Notes, which may be negative, is directly linked to the performance of the underlying assets and indirectly linked to the performance of the underlying equity constituents. The levels of the underlying assets can rise or fall sharply due to factors specific to each underlying asset or its underlying equity constituents and their respective issuers (each, an "underlying constituent issuer"), such as stock or commodity price volatility, earnings and financial conditions, corporate, industry and regulatory developments, management changes and decisions and other events, as well as general market factors, such as general stock or commodity market levels and volatility, interest rates and economic and political conditions.

#### **Fair value considerations.**

**The issue price you pay for the Notes will exceed their estimated initial value** — The issue price you pay for the Notes will exceed their estimated initial value as of the trade date due to the inclusion in the issue price of the applicable underwriting commissions and fees, hedging costs, issuance costs and projected profits. As of the close of the relevant markets on the trade date, we will determine the estimated initial value of the Notes by reference to our internal pricing models and the estimated initial value of the Notes will be set forth in the final pricing supplement. The pricing models used to determine the estimated initial value of the Notes incorporate certain variables, including the levels of the underlying assets and underlying equity constituents, the volatility of the underlying assets, any dividends paid on the underlying equity constituents, the correlation among the underlying assets and the underlying equity constituents, as applicable, prevailing interest rates, the term of the Notes and our internal funding rate. Our internal funding rate is typically lower than the rate we would pay to issue conventional fixed or floating rate debt securities of a similar term. The applicable underwriting commissions and fees, hedging costs, issuance costs, projected profits and the difference in rates will reduce the economic value of the Notes to you. Due to these factors, the estimated initial value of the Notes as of the trade date will be less than the issue price you pay for the Notes.

**The estimated initial value is a theoretical price; the actual price that you may be able to sell your Notes in any secondary market (if any) at any time after the trade date may differ from the estimated initial value** — The value of your Notes at any time will vary based on many factors, including the factors described above and in "Market risk" above and is impossible to predict. Furthermore, the pricing models that we use are proprietary and rely in part on certain assumptions about future events, which may prove to be incorrect. As a result, after the trade date, if you attempt to sell the Notes in the secondary market, the actual value you would receive may differ, perhaps materially, from the estimated initial value of the Notes determined by reference to our internal pricing models. The estimated initial value of the Notes does not represent a minimum or maximum price at which we or any of our affiliates would be willing to purchase your Notes in any secondary market at any time.

**Our actual profits may be greater or less than the differential between the estimated initial value and the issue price of the Notes as of the trade date** — We may determine the economic terms of the Notes, as well as hedge our obligations, at least in part, prior to the trade date. In addition, there may be ongoing costs to us to maintain and/or adjust any hedges and such hedges are often imperfect. Therefore, our actual profits (or potentially, losses) in issuing the Notes cannot be determined as of the trade date and any such differential between the estimated initial value and the issue price of the Notes as of the trade date does not reflect our actual profits. Ultimately, our actual profits will be known only at the maturity of the Notes.

**Limited or no secondary market and secondary market price considerations.**

**There may be little or no secondary market for the Notes** — The Notes will not be listed or displayed on any securities exchange or any electronic communications network. UBS Securities LLC and its affiliates intend, but are not required, to make a market for the Notes and may stop making a market at any time. If you are able to sell your Notes prior to maturity, you may have to sell them at a substantial loss. Furthermore, there can be no assurance that a secondary market for the Notes will develop. The estimated initial value of the Notes does not represent a minimum or maximum price at which we or any of our affiliates would be willing to purchase your Notes in any secondary market at any time.

**The price at which UBS Securities LLC and its affiliates may offer to buy the Notes in the secondary market (if any) may be greater than UBS' valuation of the Notes at that time, greater than any other secondary market prices provided by unaffiliated dealers (if any) and, depending on your broker, greater than the valuation provided on your customer account statements** — For a limited period of time following the issuance of the Notes, UBS Securities LLC or its affiliates may offer to buy or sell such Notes at a price that exceeds (i) our valuation of the Notes at that time based on our internal pricing models, (ii) any secondary market prices provided by unaffiliated dealers (if any) and (iii) depending on your broker, the valuation provided on customer account statements. The price that UBS Securities LLC may initially offer to buy such Notes following issuance will exceed the valuations indicated by our internal pricing models due to the inclusion for a limited period of time of the aggregate value of the applicable underwriting commissions and fees, hedging costs, issuance costs and theoretical projected trading profit. The portion of such amounts included in our price will decline to zero on a straight line basis over a period ending no later than the date specified under “Supplemental Plan of Distribution (Conflicts of Interest); Secondary Markets (if any).” Thereafter, if UBS Securities LLC or an affiliate makes secondary markets in the Notes, it will do so at prices that reflect our estimated value determined by reference to our internal pricing models at that time.

The temporary positive differential relative to our internal pricing models arises from requests from and arrangements made by UBS Securities LLC with the selling agents of structured debt securities such as the Notes. As described above, UBS Securities LLC and its affiliates intend, but are not required, to make a market for the Notes and may stop making a market at any time. The price at which UBS Securities LLC or an affiliate may make secondary markets at any time (if at all) will also reflect its then current bid-ask spread for similar sized trades of structured debt securities. UBS Securities LLC reflects this temporary positive differential on its customer statements. Investors should inquire as to the valuation provided on customer account statements provided by unaffiliated dealers.

**Economic and market factors affecting the terms and market price of Notes prior to maturity** — Because structured notes, including the Notes, can be thought of as having a debt component and a derivative component, factors that influence the values of debt instruments and options and other derivatives will also affect the terms and features of the Notes at issuance and the market price of the Notes prior to maturity. These factors include the levels of the underlying assets and the underlying equity constituents; the volatility of each underlying asset and the underlying equity constituents; any dividends paid on the underlying equity constituents; the correlation among the underlying assets; the time remaining to the maturity of the Notes; interest rates in the markets; geopolitical conditions and economic, financial, political, force majeure and regulatory or judicial events; whether each underlying asset is currently or has been less than its call threshold level; the availability of comparable instruments; the creditworthiness of UBS; the then current bid-ask spread for the Notes and the factors discussed under “— Potential conflict of interest” below. These and other factors are unpredictable and interrelated and may offset or magnify each other.

**Impact of fees and the use of internal funding rates rather than secondary market credit spreads on secondary market prices** — All other things being equal, the use of the internal funding rates described above under “—Fair value considerations” as well as the inclusion in the issue price of the applicable underwriting commissions and fees, hedging costs, issuance costs and any projected profits are, subject to the temporary mitigating effect of UBS Securities LLC’s and its affiliates’ market making premium, expected to reduce the price at which you may be able to sell the Notes in any secondary market.

**The Notes are subject to small-capitalization stock risks** — The Notes are subject to risks associated with small-capitalization companies because the Russell 2000<sup>®</sup> Index is comprised of stocks of companies that may be considered small-capitalization companies. These companies often have greater stock price volatility, lower trading volume and less liquidity than large-capitalization companies and therefore the underlying index may be more volatile than an index in which a greater percentage of the constituent stocks are issued by large-capitalization companies. Stock prices of small-capitalization companies are also more vulnerable than those of large-capitalization companies to adverse business and economic developments, and the stocks of small-capitalization companies may be thinly traded. In addition, small-capitalization companies are typically less stable financially than large-capitalization companies and may depend on a small number of key personnel, making them more vulnerable to loss of personnel. Small-capitalization companies are often given less analyst coverage and may be in early, and less predictable, periods of their corporate existences. Such companies tend to have smaller revenues, less diverse product lines, smaller shares of their product or service markets, fewer financial resources and less competitive strengths than large-capitalization companies and are more susceptible to adverse developments related to their products.

**The Notes are subject to non-U.S. securities market risk** — The Notes are subject to risks associated with non-U.S. companies and non-U.S. securities markets because the EURO STOXX 50<sup>®</sup> Index is comprised of stocks of non-U.S. companies that are traded on various non-U.S. exchanges. Generally, non-U.S. securities markets may be more volatile than U.S. securities markets, and market developments may affect non-U.S. markets differently from U.S. securities markets. Direct or indirect government intervention to stabilize these non-U.S. markets, as well as cross shareholdings in non-U.S. companies, may affect trading prices and volumes in those markets. There is generally less publicly available information about non-U.S. companies than about those U.S. companies that are subject to the reporting requirements of the SEC, and non-U.S. companies are subject to accounting, auditing and

financial reporting standards and requirements that differ from those applicable to U.S. reporting companies. Securities prices in non-U.S. countries are subject to political, economic, financial and social factors that may be unique to the particular country. These factors, which could negatively affect the non-U.S. securities markets, include the possibility of recent or future changes in the non-U.S. government's economic and fiscal policies, the possible imposition of, or changes in, currency exchange laws or other non-U.S. laws or restrictions applicable to non-U.S. companies or investments in non-U.S. equity securities and the possibility of fluctuations in the rate of exchange between currencies. The United Kingdom has voted to leave the European Union (popularly known as "Brexit"). The effect of Brexit is uncertain, and Brexit has and may continue to contribute to volatility in the prices of securities of companies located in Europe and currency exchange rates, including the valuation of the euro and British pound in particular. Moreover, certain aspects of a particular non-U.S. economy may differ favorably or unfavorably from the U.S. economy in important respects, such as growth of gross national product, rate of inflation, capital reinvestment, resources and self-sufficiency.

**The Notes are subject to currency exchange risk**— The Notes are subject to currency exchange rate risks because the value of your Notes will not be adjusted for exchange rate fluctuations between the U.S. dollar and the currencies in which the underlying equity constituents of the EURO STOXX 50® Index are based. Therefore, if the applicable currencies appreciate or depreciate relative to the U.S. dollar over the term of the Notes, you will not receive any additional payment or incur any reduction in your return, if any, on the Notes.

**There can be no assurance that the investment view implicit in the Notes will be successful** — It is impossible to predict whether and the extent to which the levels of the underlying assets will rise or fall and there can be no assurance that the closing level or the final level, as applicable, of each underlying asset will be equal to or greater than its call threshold level on any observation date (including the final valuation date), or, if the Notes are not subject to an automatic call, that the final level of each underlying asset will be equal to or greater than its downside threshold. The levels of the underlying assets will be influenced by complex and interrelated political, economic, financial and other factors that affect the underlying constituent issuers. You should be willing to accept the risks associated with the relevant markets tracked by each such underlying asset in general and its underlying equity constituents in particular, and the risk of losing a significant portion or all of your initial investment.

**The underlying assets reflect price return, not total return** — The return on your Notes is based on the performance of the underlying assets, which reflect the changes in the market prices of the underlying equity constituents. It is not, however, linked to a "total return" index or strategy, which, in addition to reflecting those price returns, would also reflect dividends paid on the underlying equity constituents. The return on your Notes will not include such a total return feature or dividend component.

**Changes affecting the underlying assets could have an adverse effect on the value of the Notes** — The policies of each index sponsor as specified under "Information About the Underlying Assets" (together, the "index sponsors"), concerning additions, deletions and substitutions of the underlying equity constituents and the manner in which the index sponsor takes account of certain changes affecting those underlying equity constituents may adversely affect the levels of the underlying assets. The policies of the index sponsors with respect to the calculation of the underlying assets could also adversely affect the levels of the underlying assets. The index sponsors may discontinue or suspend calculation or dissemination of the underlying assets. Any such actions could have an adverse effect on the value of the Notes.

**UBS cannot control actions by the index sponsors and the index sponsors have no obligation to consider your interests** — UBS and its affiliates are not affiliated with the index sponsors and have no ability to control or predict their actions, including any errors in or discontinuation of public disclosure regarding methods or policies relating to the calculation of the underlying assets. The index sponsors are not involved in the Notes offering in any way and has no obligation to consider your interest as an owner of the Notes in taking any actions that might affect the market value of your Notes.

**Potential UBS impact on an underlying asset or any underlying equity constituent** — Trading or transactions by UBS or its affiliates in an underlying asset or underlying equity constituent, listed and/or over-the-counter options, futures, exchange-traded funds or other instruments with returns linked to the performance of that underlying asset or any underlying equity constituent, may adversely affect the market price(s) or level(s) of the applicable underlying asset on any observation date, including the final valuation date and, therefore, the market value of the Notes, any payout pursuant to an automatic call or at maturity.

**Potential conflict of interest** — UBS and its affiliates may engage in business with any underlying constituent issuer, which may present a conflict between the obligations of UBS and you, as a holder of the Notes. There are also potential conflicts of interest between you and the calculation agent, which will be an affiliate of UBS and which will make potentially subjective judgments. The calculation agent will determine whether the Notes are subject to an automatic call and the payment at maturity of the Notes, if any, based on observed levels of the underlying assets. The calculation agent can postpone the determination of the terms of the Notes on the trade date, or the closing level of any underlying asset on any observation date (including the final valuation date). As UBS determines the economic terms of the Notes, including the call return rate, call threshold levels and downside thresholds, and such terms include the applicable underwriting commissions and fees, hedging costs, issuance costs and projected profits, the Notes represent a package of economic terms. There are other potential conflicts of interest insofar as an investor could potentially get better economic terms if that investor entered into exchange-traded and/or OTC derivatives or other instruments with third parties, assuming that such instruments were available and the investor had the ability to assemble and enter into such instruments.

Additionally, UBS and its affiliates act in various capacities with respect to the Notes, including as a principal, agent or dealer in connection with the sale of the Notes. Such affiliates, and any other third-party dealers, may derive compensation from the distribution of the Notes and any such compensation may serve as an incentive to sell these Notes instead of other investments. Furthermore, given that UBS Securities LLC and its affiliates temporarily maintain a market making premium, it may have the effect of discouraging UBS Securities LLC and its affiliates from recommending sale of your Notes in the secondary market.

**Potentially inconsistent research, opinions or recommendations by UBS** — UBS and its affiliates publish research from time to time on financial markets and other matters that may influence the value of the Notes, or express opinions or provide recommendations that are inconsistent with purchasing or holding the Notes. Any research, opinions or recommendations expressed by UBS or its affiliates may not be consistent with each other and may be modified from time to time without notice. Investors should make their own independent investigation of the merits of investing in the Notes and the underlying assets to which the Notes are linked.

**The Notes are not bank deposits** — An investment in the Notes carries risks which are very different from the risk profile of a bank deposit placed with UBS or its affiliates. The Notes have different yield and/or return, liquidity and risk profiles and would not benefit from any protection provided to deposits.

**If UBS experiences financial difficulties, FINMA has the power to open restructuring or liquidation proceedings in respect of, and/or impose protective measures in relation to, UBS, which proceedings or measures may have a material adverse effect on the terms and market value of the Notes and/or the ability of UBS to make payments thereunder** — The Swiss Financial Market Supervisory Authority ("FINMA") has broad statutory powers to take measures and actions in relation to UBS if (i) it concludes that there is justified concern that UBS is over-indebted or has serious liquidity problems or (ii) UBS fails to fulfill the applicable capital adequacy requirements (whether on a standalone or consolidated basis) after expiry of a deadline set by FINMA. If one of



these pre-requisites is met, FINMA is authorized to open restructuring proceedings or liquidation (bankruptcy) proceedings in respect of, and/or impose protective measures in relation to, UBS. The Swiss Banking Act grants significant discretion to FINMA in connection with the aforementioned proceedings and measures. In particular, a broad variety of protective measures may be imposed by FINMA, including a bank moratorium or a maturity postponement, which measures may be ordered by FINMA either on a stand-alone basis or in connection with restructuring or liquidation proceedings. The resolution regime of the Swiss Banking Act is further detailed in the FINMA Banking Insolvency Ordinance ("BIO-FINMA"). In a restructuring proceeding, FINMA, as resolution authority, is competent to approve the resolution plan. The resolution plan may, among other things, provide for (a) the transfer of all or a portion of UBS's assets, debts, other liabilities and contracts (which may or may not include the contractual relationship between UBS and the holders of Notes) to another entity, (b) a stay (for a maximum of two business days) on the termination of contracts to which UBS is a party, and/or the exercise of (w) rights to terminate, (x) netting rights, (y) rights to enforce or dispose of collateral or (z) rights to transfer claims, liabilities or collateral under contracts to which UBS is a party, (c) the conversion of UBS's debt and/or other obligations, including its obligations under the Notes, into equity (a "debt-to-equity" swap), and/or (d) the partial or full write-off of obligations owed by UBS (a "write-off"), including its obligations under the Notes. The BIO-FINMA provides that a debt-to-equity swap and/or a write-off of debt and other obligations (including the Notes) may only take place after (i) all debt instruments issued by UBS qualifying as additional tier 1 capital or tier 2 capital have been converted into equity or written-off, as applicable, and (ii) the existing equity of UBS has been fully cancelled. While the BIO-FINMA does not expressly address the order in which a write-off of debt instruments other than debt instruments qualifying as additional tier 1 capital or tier 2 capital should occur, it states that debt-to-equity swaps should occur in the following order: first, all subordinated claims not qualifying as regulatory capital; second, all other claims not excluded by law from a debt-to-equity swap (other than deposits); and third, deposits (in excess of the amount privileged by law). However, given the broad discretion granted to FINMA as the resolution authority, any restructuring plan in respect of UBS could provide that the claims under or in connection with the Notes will be partially or fully converted into equity or written-off, while preserving other obligations of UBS that rank pari passu with, or even junior to, UBS's obligations under the Notes. Consequently, holders of Notes may lose all or some of their investment in the Notes. In the case of restructuring proceedings with respect to a systemically important Swiss bank (such as UBS), the creditors whose claims are affected by the restructuring plan will not have a right to vote on, reject, or seek the suspension of the restructuring plan. In addition, if a restructuring plan has been approved by FINMA, the rights of a creditor to seek judicial review of the restructuring plan (e.g., on the grounds that the plan would unduly prejudice the rights of holders of Notes or otherwise be in violation of the Swiss Banking Act) are very limited. In particular, a court may not suspend the implementation of the restructuring plan. Furthermore, even if a creditor successfully challenges the restructuring plan, the court can only require the relevant creditor to be compensated ex post and there is currently no guidance as to on what basis such compensation would be calculated or how it would be funded.

**Uncertain tax treatment** — Significant aspects of the tax treatment of the Notes are uncertain. You should consult your tax advisor about your tax situation. See "What are the Tax Consequences of the Securities" herein and "Material U.S. Federal Income Tax Consequences", including the section "—Securities Treated as Prepaid Derivatives or Prepaid Forwards", in the accompanying product supplement.

**Hypothetical Examples of How the Notes Might Perform**

The below examples are based on hypothetical terms. The actual terms will be set on the trade date and will be indicated on the cover of the final pricing supplement.

The examples below illustrate the payment upon a call or at maturity for a \$1,000 Note on a hypothetical offering of the Notes, with the following assumptions (amounts may have been rounded for ease of reference):

Principal Amount:	\$1,000
Term:	Approximately 4 years
Call return rate:	11.25% per annum
Observation Dates:	Annually
Initial Level:	
Underlying Asset A:	1,500
Underlying Asset B:	3,500
Call Threshold Level:	
Underlying Asset A:	1,350 (which is 90.00% of the Initial Level)
Underlying Asset B:	3,150 (which is 90.00% of the Initial Level)
Downside Threshold:	
Underlying Asset A:	1,050 (which is 70.00% of the Initial Level)
Underlying Asset B:	2,450 (which is 70.00% of the Initial Level)

**Example 1 — The Closing Level of each Underlying Asset is equal to or greater than its Call Threshold Level on the Observation Date corresponding to the first Potential Call Settlement Date.**

Date	Closing Level	Payment (per Note)
First Observation Date	Underlying Asset A: 1,400 ( <b><u>equal to or greater than</u></b> Call Threshold Level)	\$1,112.50 (Call Price)
	Underlying Asset B: 3,530 ( <b><u>equal to or greater than</u></b> Call Threshold Level)	
	Total Payment	\$1,112.50 (11.25% total return)

Because the Notes are subject to an automatic call on the first potential call settlement date (which is approximately one year after the trade date), UBS will pay on the call settlement date a total of \$1,112.50 per Note (reflecting your principal amount plus the applicable call return), an 11.25% total return on the Notes. You will not receive any further payments on the Notes.

**Example 2 — The Final Level of each Underlying Asset is equal to or greater than its Call Threshold Level on the Final Valuation Date.**

Date	Closing Level	Payment (per Note)
First Observation Date	Underlying Asset A: 1,250 ( <b><u>less than</u></b> Call Threshold Level)	\$0
	Underlying Asset B: 3,000 ( <b><u>less than</u></b> Call Threshold Level)	
Second Observation Date	Underlying Asset A: 1,550 ( <b><u>equal to or greater than</u></b> Call Threshold Level)	\$0
	Underlying Asset B: 2,850 ( <b><u>less than</u></b> Call Threshold Level)	
Third Observation Date	Underlying Asset A: 1,200 ( <b><u>less than</u></b> Call Threshold Level)	\$0
	Underlying Asset B: 2,800 ( <b><u>less than</u></b> Call Threshold Level)	

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Final Valuation Date	Underlying Asset A: 1,750 ( <b><u>equal to or greater than</u></b> Call Threshold Level)	\$1,450.00 (Call Price)
	Underlying Asset B: 3,250 ( <b><u>equal to or greater than</u></b> Call Threshold Level)	
	Total Payment	\$1,450.00 (45.00% total return)

Because the Notes are subject to an automatic call on the final valuation date (which is approximately four years after the trade date), UBS will pay on the call settlement date a total of \$1,450.00 per Note (reflecting your principal amount plus the applicable call return), a 45.00% total return on the Notes.

**Example 3 — The Notes are NOT subject to an Automatic Call and the Final Level of each Underlying Asset is equal to or greater than its Downside Threshold.**

<b>Date</b>	<b>Closing Level</b>	<b>Payment (per Note)</b>		
	Underlying Asset A: 1,300 ( <b><u>less than</u></b> Call Threshold Level)	Palisades West, Building One		
First Observation Date	Underlying Asset B: 2,720 ( <b><u>less than</u></b> Call Threshold Level)	6300 Bee Cave Road Austin, Texas, 78746	1,842,592	8.4%
Rima Senvest Management, LLC (4)				
110 East 55th Street Suite 1600				
New York, New York 10022			1,444,172	6.6%

Name of	Shares	Approximate	Options and
Beneficial Owner	Beneficially	Percent	Stock
	Owned	Beneficially	Appreciation
		Owned	Rights Included
			in Shares
			Beneficially
			Owned (6)
Roumell Asset Management, LLC (5)			
2 Wisconsin Circle, Suite 660			
Chevy Chase, MD 20815	1,280,716	5.8%	
Ofer Elyakim	331,780	1.4%	315,576
Dror Levy	190,521	*	190,521
David Dahan	11,378	*	9,375
Eliyahu Ayalon	549,035	2.3%	539,166
Thomas A. Lacey	11,000	*	10,000
Zvi Limon	250,000	1.1%	250,000
Reuven Regev	25,000	*	25,000
Yair Seroussi	125,000	*	125,000
Yair Shamir	250,000	1.0%	250,000
Patrick Tanguy	135,000	*	135,000
Kenneth H. Traub	24,153	*	10,000
All directors and executive officers as a group (11 persons)	1,902,867	8.0%	1,859,638

\* Less than 1%

- (1) Based on a Schedule 13G/A filed by BlackRock, Inc. on January 11, 2013, with the Securities and Exchange Commission, reporting beneficial ownership as of December 31, 2012.
- (2) Based on a Schedule 13D/A jointly filed by Starboard Value LP, Starboard Value and Opportunity Master Fund Ltd., Starboard Value GP LLC, Starboard Value and Opportunity S LLC, Starboard Principal Co LP, Starboard Principal Co GP LLC, Jeffrey C. Smith, Mark R. Mitchell, Peter A. Feld, Michael Bornak, Norman J. Rice, III and Norman P. Taffe on March 13, 2013 with the Securities and Exchange Commission, reporting aggregate beneficial ownership as of March 12, 2013.
- (3) Based on a Schedule 13G/A jointly filed by Dimensional Fund Advisors LP and Dimensional Holdings Inc. on February 11, 2012, with the Securities and Exchange Commission, reporting beneficial ownership as of December 31, 2012.

- (4) Based on a Schedule 13G jointly filed by Rima Senvest Management, LLC and Richard Mashaal on February 14, 2013, with the Securities and Exchange Commission, reporting beneficial ownership as of December 31, 2012.
- (5) Based on a Schedule 13G jointly filed by James C. Roumell and Roumell Asset Management, LLC on February 4, 2013, with the Securities and Exchange Commission, reporting beneficial ownership as of December 31, 2012.
- (6) For purposes of the above table, with respect to stock appreciation right awards granted to all of our executive officers, the number of shares of our common stock subject to stock appreciation right awards that are currently exercisable or exercisable within 60 days of April 1, 2013 is calculated based on 50% of the units subject to such awards for grants prior to 2009, 75% of the units subject to such awards for grants in 2009, 67% of the units subject to such awards for grants in 2010 and 2011 and 50% of the units subject to such awards for grants in 2012. Our directors do not receive stock appreciation right awards.

**Equity Compensation Plan Information**

The following table sets forth certain information regarding our equity compensation plans as of December 31, 2012.

Plan category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted-average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	1,256,666	\$ 14.17	1,231,574(1)
Equity compensation plans not approved by security holders (2)	5,373,469	\$ 9.66	340,689
<b>Total</b>	<b>6,630,135</b>	<b>\$ 10.52</b>	<b>1,572,263</b>

- (1) The amount includes 587,488 shares of common stock available for future issuance under our 1993 Employee Stock Purchase Plan as of December 31, 2012.
- (2) Neither the Amended and Restated 1998 Non-Officer Employee Stock Option Plan (the 1998 Plan ) nor the Amended and Restated 2003 Israeli Share Incentive Plan (the 2003 Plan ) was previously approved by our stockholders. The total number of shares of common stock available for the grant of options under the 2003 Plan was increased on the first day of each calendar year beginning in 2004 by a number of shares equal to three percent of the number of shares of our common stock outstanding as of such date or a lesser number as determined by the administrator of the plan; provided, however that in May 2011, our board of directors approved an amendment and restatement of the 2003 Plan to eliminate the automatic annual increase in the authorized number of shares of our common stock available for grant under the 2003 Plan after 2012. Furthermore, after stockholder approval of our 2012 Equity Incentive Plan at our 2012 annual meeting of stockholders, the 2003 Plan terminated.

*Amended and Restated 1998 Non-Officer Employee Stock Option Plan*

Our board of directors adopted the 1998 Plan in November 1998. As of December 31, 2012, 5,062,881 shares of common stock were authorized and 340,689 shares of common stock remained available for grant. The board of directors, or a committee designated by the board of directors, administers the 1998 Plan. The administrator has the sole discretion to interpret any provision of the 1998 Plan, and to determine the terms and conditions of awards of non-qualified stock options or stock appreciation rights under the 1998 Plan. Options and stock appreciation

rights currently may be granted to our employees and employees of any of our subsidiaries. Officers may not be granted options or stock appreciation rights under the 1998 Plan. The material features of the 1998 Plan are summarized below.

*Term.* The term of each option or stock appreciation right shall be stated in the applicable option or stock appreciation right agreement.

*Exercise Price or Base Appreciation Right.* The exercise price per share of common stock for an option and the base appreciation amount for a stock appreciation right shall be determined by the administrator.

*Vesting.* Each option or stock appreciation right shall vest in accordance with a schedule as determined by the administrator.

*Early Exercise.* An option may include a provision whereby the participant may elect to exercise any part or all of the option prior to vesting of the option. Any unvested shares received pursuant to such exercise may be subject to a repurchase right in favor of the Company or any other restriction the administrator determines to be appropriate.

*Transferability.* Options and stock appreciation rights are transferable to the extent provided in the applicable option agreement or stock appreciation right agreement.

*Termination of Employment.* A participant may not exercise an option or stock appreciation right after the termination of the participant's employment, director or consulting relationship with us or with any of our subsidiaries, except to the extent specified in the applicable option or stock appreciation right agreement. Where the option or stock appreciation right agreement permits the exercise of the option or stock appreciation right following termination of the participant's employment or other service relationship with us or any of our subsidiaries, the option or stock appreciation right shall terminate to the extent not exercised on the last day of the specified period or the last day of the term of the option or stock appreciation right, whichever occurs first.

*Acquisition of the Company.* If we are acquired whether by sale, transfer of assets, merger or similar transaction, the administrator shall have the authority to provide for the full automatic vesting and exercisability of one or more outstanding unvested options or unvested stock appreciation rights under the 1998 Plan on such terms and conditions as the administrator may specify.

*Amendment and Termination of the Plan.* The 1998 Plan will continue until it is terminated by the board of directors. The board may amend the 1998 Plan at any time or from time to time or may suspend or terminate it, without approval of the stockholders, except as required by law. However, no action by the board of directors or stockholders may alter or impair any option or stock appreciation right previously granted under the 1998 Plan. No option or stock appreciation right may be granted during any suspension of or after termination of the 1998 Plan.

#### *Amended and Restated 2003 Israeli Share Incentive Plan*

Our board of directors adopted the 2003 Plan in November 2002. Pursuant to the plan terms, the number of shares authorized for issuance increased annually on the first business day



of each calendar year equal to three percent of the number of shares of our common stock issued and outstanding as of such date or a lesser number of shares as determined by the board of directors; provided, however that in May 2011, our board of directors approved an amendment and restatement of the 2003 Plan to eliminate the automatic annual increase in the authorized number of shares of our common stock available for grant under the 2003 Plan after 2012. Furthermore, after our stockholders approved the 2012 Equity Incentive Plan at the 2012 annual meeting of stockholders, the 2003 Plan terminated. As of December 31, 2012, 10,700,543 shares of common stock were granted under the 2003 Plan and stock option and stock appreciation rights to acquire 4,349,094 shares of common stock remained outstanding under the 2003 Plan.

The board of directors, or a committee designated by the board of directors, administered the 2003 Plan. The administrator had the sole discretion to interpret any provision of the 2003 Plan and to determine the terms and conditions of the options and stock appreciation rights issued under the 2003 Plan. Our employees and other service providers and employees and other service providers of any of our subsidiaries were eligible to receive grants of options and stock appreciation rights. The material features of the 2003 Plan are summarized below.

*Term.* The term of each option or stock appreciation right were stated in the applicable option agreement or stock appreciation right agreement.

*Exercise Price or Base Appreciation Right.* The exercise price per share of common stock for an option and the base appreciation amount for a stock appreciation right were determined by the administrator and were set forth in the applicable option or stock appreciation right agreement.

*Vesting.* Each option or stock appreciation right vested in accordance with a schedule as determined by the administrator.

*Transferability.* Options and stock appreciation rights were non-transferable except as provided in the option or stock appreciation right agreement. During the lifetime of the participant, the option or stock appreciation right were exercisable only by the participant.

*Termination of Employment.* In the event a participant's employment relationship with us or any of our subsidiaries was terminated other than for cause or as a result of death or disability, the vested portion of the option or stock appreciation right was exercisable for 90 days after the date of termination. In the event a participant's employment relationship with us or any of our subsidiaries was terminated as a result of death or disability, the vested portion of the option or stock appreciation right was exercisable for 12 months after the date of termination. In the event a participant's employment relationship with us or any of our subsidiaries was terminated for cause, the option or stock appreciation right was immediately terminated and ceased to be exercisable. In no event was an option or stock appreciation right exercisable after the expiration date of the option or stock appreciation right.

*Acquisition of the Company.* The terms of an option or stock appreciation right agreement could have provided for the full automatic vesting and exercisability of the option or stock appreciation right in the event we were acquired by sale, transfer of assets, merger or similar transaction.

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## EXECUTIVE COMPENSATION

### Compensation Discussion & Analysis

#### *Overview of Compensation Philosophy and Objectives*

We operate in a very competitive, dynamic and challenging industry. Our compensation policy, as established by the compensation committee of our board of directors, is designed to attract, motivate and retain highly talented individuals who will contribute to our long-term success, reward our executive officers who contribute to our positive financial performance and provide a strong link between our executive officers' compensation and long-term interests of our stockholders. We believe that our executive officers' compensation should not be based on the short-term performance of our stock, whether favorable or unfavorable, but rather that the price of our stock will, in the long-term, reflect our operating performance and ultimately the management of the company by our executive officers. The various compensation levels for our executive officers are set based on the scope of their responsibilities and performance. Our policy for allocating between long-term and currently paid compensation is to ensure adequate base compensation to attract and retain key personnel, while providing them incentives to maximize long-term value for our company and stockholders. We further believe that the executive officers' total annual cash compensation should vary with the company's performance and that the higher an executive officer's level of responsibility within the company, the greater the percentage of such executive officer's compensation should be tied to the company's performance. However, notwithstanding the above principles, we rely upon judgment and not rigid guidelines or formulas in determining the amount and mix of compensation elements for each executive officer. The compensation committee has complete discretion over each element of our executive officers' compensation, except to the extent the company's performance-based bonus plan applies.

The compensation committee, which is comprised solely of independent, non-employee board members, has the authority and responsibility to establish the overall compensation strategy for the company, including reviewing, analyzing and approving the compensation structure for our Chief Executive Officer, other executive officers and other key employees each year; and administer our incentive compensation and benefit plans, 401(k) plan and employee stock purchase plan. The compensation committee regularly updates the board of directors with respect to its undertakings in establishing the company's overall compensation strategy. Messrs. Limon, Shamir and Tanguy were the members of the compensation committee in 2012, with Mr. Shamir acting as the Chairman.

#### *Role of Chief Executive Officer and Compensation Consultants in Compensation Decisions*

Mr. Ayalon, our former Executive Chairman of the board, and Mr. Elyakim, our Chief Executive Officer, have annually reviewed the performance of each executive officer (other than Mr. Elyakim with respect to himself). The assessment by Messrs. Ayalon and Elyakim of the performance of each executive officer, and the individual and corporate performance of each executive officer and their conclusions thereon, including with respect to salary adjustments and annual award amounts, are then presented to the compensation committee in connection with the committee's annual review of each executive officer's total compensation. While the committee considers their recommendations, it independently evaluates the recommendations and makes all final compensation decisions.

Mr. Ayalon resigned as our Executive Chairman, effective May 31, 2011, after which he has continued to serve as a non-executive Chairman. Notwithstanding the fact that Mr. Ayalon has resigned as the Executive Chairman of the board, the compensation committee greatly values Mr. Ayalon's insights about our people which he acquired over the 15 plus years of service on our board and as our Chief Executive Officer. As a result, the compensation committee will continue to solicit Mr. Ayalon's assessment of the performance of each executive officer in connection with its annual review of each executive officer's total compensation.

The charter of the compensation committee authorizes the committee to engage the services of consultants to assist in the determination of our executive officers' compensation. In connection with deliberations associated with establishment of the 2012 performance-based bonus plan, including the parameters for the plan, the compensation committee engaged the services of Compensia, Inc., a compensation consultant, in 2012 to provide the committee with general comparative information about executive compensation of peer companies, general observations about the compensation elements of executive officers of peer companies, general observations about retirement and termination data of executive officers of peer companies and general observations about our executive compensation program. Compensia did not directly recommend any specific compensation elements or specific parameters for the 2012 performance-based bonus plan. Compensia was paid an aggregate of \$11,000 plus out-of-pocket expenses for its services. Compensia was not engaged for any other services relating to the company in 2012. No member of the compensation committee or management has any affiliation with Compensia.

### *Principal Elements of Executive Compensation*

Compensation of our executive officers consists of three principal components: base salary, bonus and long-term incentive compensation consisting of grants of stock options, stock appreciation rights and restricted stock units. The overall compensation of our executive officers is set by the compensation committee, in consultation with the board of directors, after an annual review by the compensation committee of each executive officer's overall performance for the prior year and the overall performance of the company for the prior year. Prior to 2011, the compensation committee did not set specific goals for our executive officers to achieve, other than the general goals of positive financial results, growth of the company's business and dutiful completion of responsibilities consistent with the position of the executive officers. Prior to 2011, the compensation committee did not follow a specific set of guidelines or formulas in determining the amount and mix of compensation elements for each executive officer. Starting in 2011, one element of executive compensation established by our compensation committee, in consultation with the board, was a performance-based bonus plan. As discussed below, the compensation committee approved a performance-based bonus plan for 2012 and 2013.

*Base Salary.* The base salaries of our executive officers are set by the compensation committee. When setting base salary levels, the compensation committee considers competitive market conditions for executive compensation, the company's performance, the performance of the individual executive officer for the then completed year and any promotion or other change in job responsibility of the individual executive officer. The determination of the base salaries of the executive officers is discretionary; no specific goals are considered and no specific weight is given to any particular goal achieved or any other factor by the compensation committee in its annual review.

*2012 Performance-Based Bonus Plan*

In April 2012, our compensation committee of the board approved a 2012 performance-based bonus plan applicable for our Chief Executive Officer, Chief Financial Officer and Chief Operating Officer. The payment of bonuses under the 2012 performance-based bonus plan was based upon the company's achievement of operating income target of \$4 million and revenue target of \$210 million. Bonuses under the plan were capped and no bonuses were payable for 2012 if the company failed to achieve above 90% of the revenue target or 50% of the operating income target. Payment of bonuses (if any) under the performance-based bonus plan was to be made in the following year. Any such bonuses were to be paid in cash in a single lump sum, subject to payroll taxes and tax withholdings. The following is a description of the 2012 performance-based bonus plan as applicable to each of our named executive officers.

*Chief Executive Officer*

Criteria		% of Total Bonus
Meeting Operating Income (OI) Target	A=OI Score	Payout is linear between any two points.

OI Score:

0 = at or below 50% of the OI target or if 2012 revenues are at or below 90% of the revenue target

0.7 = if actual OI is 50% above the OI target

1.4 = if actual OI is 100% or above the OI target

Total	(A) × Annual Salary	Target = 0.7×
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Cap = 1.4×

*Chief Financial Officer and Chief Operating Officer*

Criteria		% of Total Bonus
Meeting Operating Income (OI) Target	B=OI Score	Payout is linear between any two points.

OI Score:

## Edgar Filing: UBS AG - Form 424B2

0 = at or below 50% of the OI target or if  
2012 revenues are at or below 90% of the  
revenue target

0.35 = if actual OI is 50% above the OI  
target

0.7 = if actual OI is 100% or above the  
OI target

Total

(B) × Annual Salary

Target = 0.35×

Cap = 0.7×

No bonuses were paid to any of our named executive officers under the 2012 performance-based bonus plan due to the company's failure to achieve 90% of the revenue target and 50% of the operating income target.

*2013 Performance-Based Bonus Plan*

In March 2013, our compensation committee of the board approved a 2013 performance-based bonus plan applicable for the Chief Executive Officer, Chief Financial Officer and Chief Operating Officer. The 2013 performance-based bonus plan is effective as of January 1, 2013. The payment of bonuses under the 2013 performance-based bonus plan is based upon two components: (1) 60% of any bonus payable under the plan is based on the company's achievement of certain financial performance metrics, consisting of annual revenue target, earnings before interest, taxes, depreciation and amortization ( EBITDA ) target and free cash flow target, each based on the company's 2013 annual budget which has been approved by our board, and (2) 40% of any bonus payable under the plan is discretionary and based upon achievement of individual performance goals by the executive officers. The individual performance goals will be determined by our compensation committee, in its sole discretion, taking into account such tangible and intangible individual performance factors as it considers appropriate, including the executive officer's relative contribution to the company's performance during fiscal 2013. The compensation committee's determination as to whether individual performance goals have been met may be subjective in nature. No individual performance goals have currently been set by our compensation committee. Bonuses under the plan are capped. Other than under the circumstances whereby there is a change of control transaction involving the company, payment of bonuses (if any) under the 2013 performance-based bonus plan would be made in the following year. Any such bonuses would be paid in cash in a single lump sum, subject to payroll taxes and tax withholdings. In the event of a change of control of the company (as such an event is defined in the employment agreements for the Chief Executive Officer and the Chief Financial Officer), the 40% of discretionary bonus under the 2013 performance-based bonus plan would be immediately paid and the 60% of bonus under the 2013 performance-based bonus plan based on the company's achievement of financial performance metrics would be paid prorated for the period starting on January 1, 2013 to the date that the change of control transaction is consummated.

In connection with deliberations associated with establishment of the 2013 performance-based bonus plan, including the parameters for the plan, the compensation committee considered the general comparative information about executive compensation of peer companies provided previously by Compensia. No compensation consultant was engaged in 2013.

Due to their strategic significance, we believe that the disclosure of the 2013 annual revenue target, EBITDA target and free cash flow target under the 2013 performance-based bonus plan would cause competitive harm to the company and therefore are not disclosed.

*Chief Executive Officer*

Criteria		% of Total Bonus
A. Annual Revenue Target	$A = 15\% \times \text{Annual Revenue Score}$	

Annual Revenue Score:

0 if annual revenues are more than 10% below plan

0.5 if annual revenues are 10% below plan

1.0 if annual revenues meet plan

2.0 if annual revenues are 10% above plan

The payout based on the annual revenue score is linear between any two points.

B. EBITDA Target	$B = 25\% \times \text{EBITDA Score}$	
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EBITDA Score:

0 at zero or negative EBITDA

1.0 if actual EBITDA meet plan

2.0 if actual EBITDA is 50% above plan

## Edgar Filing: UBS AG - Form 424B2

The payout based on the EBITDA score is linear between any two points.

C. Free Cash Flow Target

$C = 20\% \times \text{Free Cash Flow Score}$

Free Cash Flow Score:

0 if zero or negative free cash flows

1.0 if free cash flows equals plan operating income on a non-GAAP basis

2.0 if actual free cash flows is 100% above plan operating income on a non-GAAP basis

The payout based on the free cash flow score is linear between any two points.

D. Discretionary Component

40% of total bonus payable under the plan

$D = 40\% \text{ to } 80\% \text{ of annual salary}$

Total

$(A+B+C+D) \times \text{Annual Salary}$



The target bonus payout under the 2013 performance-based bonus plan for the Chief Executive Officer is 1.0x of his annual base salary and the cap under the plan is 2.0x of his annual base salary.

*Chief Financial Officer and Chief Operating Officer*

Criteria		% of Total Bonus
A. Annual Revenue Target	$A = 15\% \times \text{Annual Revenue Score}$	

Annual Revenue Score:

0 if annual revenues are more than 10% below plan

0.25 if annual revenues are 10% below plan

0.5 if annual revenues meet plan

1.0 if annual revenues are 10% above plan

The payout based on the annual revenue score is linear between any two points.

B. EBITDA Target	$B = 25\% \times \text{EBITDA Score}$
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EBITDA Score:

0 at zero or negative EBITDA

0.5 if actual EBITDA meet plan

1.0 if actual EBITDA is 50% above plan

## Edgar Filing: UBS AG - Form 424B2

The payout based on the EBITDA score is linear between any two points.

### C. Free Cash Flow Target

$C = 20\% \times \text{Free Cash Flow Score}$

Free Cash Flow Score:

0 if zero or negative free cash flows

0.5 if free cash flows equals plan operating income on a non-GAAP basis

1.0 if actual free cash flows is 100% above plan operating income on a non-GAAP basis

The payout based on the free cash flow score is linear between any two points.

Criteria	% of Total Bonus
D. Discretionary Component	40% of total bonus payable under the plan

D = 20% to 40% of annual salary

Total (A+B+C+D) × Annual Salary

The target bonus payout under the 2013 performance-based bonus plan for the Chief Financial Officer and Chief Operating Officer is 0.5x of their respective annual base salary and the cap under the plan is 1.0x of their respective annual base salary.

*Long-term Incentive Compensation.* Grants of stock options, stock appreciation rights and restricted stock units are made from time to time to our employees, including executive officers, whose contributions have or will have a significant impact on our long-term performance. We began to grant stock appreciation rights to our executive officers beginning in 2006 with a view to conserve the number of shares of our common stock authorized for issued under our various equity incentive plans. We believe that the grant of stock options, stock appreciation rights and restricted stock units (1) align our executive officers' interests with stockholder interests by creating a direct link between compensation and stockholder return; (2) give executive officers a significant, long-term interest in our success; and (3) help retain key executive officers in a competitive market for executive talent. We grant stock options, stock appreciation rights and restricted stock units to our executive officers pursuant to our 2012 Equity Incentive Plan and Amended and Restated 2003 Israeli Share Incentive Plan until May 2012 when the plan terminated. In 2012, we provided long-term awards to our executive officers through the grant of stock appreciation rights, which vest based on continued employment consistent with the general vesting schedules discussed below.

*Compensation of Chief Executive Officer.* The compensation committee's determination of Mr. Elyakim's remuneration generally was based upon methods consistent with those used for the other executive officers. The compensation committee additionally considered the following factors in evaluating the performance of, and setting the compensation for, Mr. Elyakim: (1) changes in revenues and net income from the previous year; (2) changes in our market share as compared both to our industry peers and to the previous year; (3) changes in the stock price of our common stock as compared both to our industry peers and to the previous year; (4) his contribution to an enhanced research and development strategy in response to changing market trends; (5) his contribution to the hiring and retention of top management personnel; and (6) the time and effort that he individually applied in connection with the execution of his duties. The compensation committee believes that the salary and long-term incentive compensation paid to Mr. Elyakim during 2012 were appropriate based on the above criteria.

***Equity Incentive Programs***

We intend that our equity incentive awards be the primary vehicle for offering long-term incentives and rewarding our executive officers and key employees. We also regard our equity incentive awards as a key retention tool. This is a very important factor in our determination of the type of award to grant and the number of underlying shares that are granted in connection with that award.

Equity incentive awards are granted based upon the compensation committee's annual review of each executive officer's performance for the prior year. The size of each grant is generally set at a level that the compensation committee deems appropriate to create a meaningful opportunity for stock ownership, the individual's position with the company and the individual's potential for future responsibility and promotion. In the grant of awards, the compensation committee further considers the executive officer's past performance, the total compensation being paid to the executive officer, the number of equity awards granted to the executive officer during previous years and the vesting status of such awards, and the comparability with equity awards made to our other executive officers and similarly situated executive officers at peer companies. All equity awards are made at the market price at the time of the awards. The determination for the grant of equity incentive awards is discretionary; no specific goals are considered and no specific weight is given to any particular goal achieved or any other factor by the compensation committee.

*Stock Option Awards Granted.* We grant stock option awards to our executive officers and key employees based upon the criteria discussed above. However, there is no set formula for the granting of stock option awards to individual executive officers. Generally, stock options previously granted to our executive officers vest as to 25% of the grant on the first anniversary of the grant date with the remaining options vesting quarterly over the next three years and expiring seven years from the grant date. No stock options were granted to our executive officers in 2012.

*Stock Appreciation Right Awards Granted.* Due to the evolution of regulatory, tax and accounting treatment of equity incentive programs and because it is important for us to retain our executive officers and key employees, we realized that it is important that we explore the use of other forms of equity awards. During 2006, we began to grant our executive officers stock appreciation rights, capped with a ceiling. The stock appreciation right confers upon our executive officers the right to stock appreciation over a preset price during a specified period of time. When the stock appreciation right is exercised, the appreciation amount is paid by the issuance of shares of our common stock. For stock appreciation right awards granted prior to 2009, the maximum number of shares of our common stock issuable upon exercise of the stock appreciation right award equaled 50% of the number of stock appreciation rights granted. With respect to the stock appreciation right awards granted in 2009 to our executive officers, the maximum number of shares of our common stock issuable upon exercise of the stock appreciation right award equaled 75% of the number of stock appreciation rights granted. The change to the ceiling percentage was implemented in 2009 in recognition of the unprecedented market conditions in late 2008 and 2009 that drove down the stock price of the company's stock significantly which resulted in approximately half of the outstanding equity awards to executive officers being out of the money. In January 2010 and 2011, the compensation committee granted stock appreciation right awards to our executive officers with the maximum number of shares of our common stock issuable upon exercise of the stock appreciation right awards equal to 67% of

the number of stock appreciation rights granted. In January 2012, the compensation committee granted stock appreciation right awards to our executive officers with the maximum number of shares of our common stock issuable upon exercise of the stock appreciation right award equal to 50% of the number of stock appreciation rights granted.

Stock appreciation rights granted to our executive officers generally vest as to 25% of the grant on the first anniversary of the grant date with the remaining stock appreciation rights vesting quarterly over the next three years and expiring seven years from the date of grant.

Grant of stock appreciation rights to our executive officers are generally made based upon the criteria discussed above. However, there is no set formula for the grant of stock appreciation rights to individual executive officers. During 2012, 1,100,000 stock appreciation right units were granted to our employees. Our named executive officers, namely Messrs. Elyakim, Levy and Dahan, received 105,000, 50,000 and 60,000 stock appreciation right units, respectively, or 20% of the total stock appreciation right units granted in 2012. The amounts of the above referenced stock appreciation rights granted to each of the named executive officers in 2012 are specified in the 2012 grants of plan based awards table of the proxy statement.

*Restricted Stock Units Granted.* Similar to the rationale for moving to the grant of stock appreciation rights, starting in 2013, the compensation committee decided to grant our executive officers restricted stock units. We grant restricted stock units to our executive officers based upon the same criteria as grants of stock options and stock appreciation rights. We seek to incentivize both retention and stock price appreciation through the grants. In January 2013, the compensation committee granted restricted stock units to Messrs. Elyakim, Levy and Dahan in the amounts of 66,000, 25,000 and 20,000, respectively.

*Timing of Grants.* Equity incentive awards to our executive officers and other key employees are typically granted annually in conjunction with the compensation committee's review of their individual performance during the prior year. Stock options, stock appreciation rights and restricted stock units are not necessarily granted to each employee every year. Grants of stock options, stock appreciation rights and/or restricted stock units to newly hired executive officers who are eligible to receive them generally are made at the next regularly scheduled compensation committee or board meeting following their hire date.

*Stock Ownership Guidelines.* We do not currently require our executive officers and members of our board to own a minimum number of shares of our common stock. The compensation committee is satisfied that stock and option holdings among our executive officers and directors are sufficient at this time to provide motivation and to align this group's interests with those of our stockholders.

#### ***Retirement Benefits and Perquisites***

We do not offer any retirement benefits to our Israeli-based executive officers except for social benefits required pursuant to Israeli labor laws, or are common practice in Israel and are generally available to all Israeli employees. Specifically, based on Israeli labor laws, an Israeli employee is entitled to severance pay upon termination of employment for any reason, including retirement, based on the most recent monthly salary of such employee multiplied by the number of years of employment of such employee. We make a payment of 8.333% of each employee's monthly base salary to an insurance or pension fund to pay for this future liability owed to Israeli

employees upon termination of their employment. In addition, we make a payment of 5% of each employee's monthly base salary to another insurance or pension fund, which accrued amount may be withdrawn by the employee after retirement or, subject to various tax restrictions in Israel, after leaving our employment. We generally provide all of our Israeli employees with a car for business-related purposes and pay the associated expenses. Also, as is customary in Israel applicable to all Israeli employees, we provide our Israeli employees with a certain amount of monthly contributions (7.5% of their base salary) for the benefit of each employee's study and training purposes. The amounts of the above referenced benefits contributed by us to each of the named executive officers in 2012 are specified in the summary compensation table of the proxy statement.

We currently do not provide any material retirement benefits or perquisites to our executive officers that are not generally available to our employees.

#### ***Employment Agreements and Post-Termination Protection***

The compensation committee also recognizes that, from time to time, it is appropriate to enter into agreements with certain key employees to ensure that we continue to retain their services and to promote stability and continuity within our company. Moreover, employment agreements are generally customary for employees residing in Israel. We have entered into employment agreements with our named executive officers. The varied terms of their employment agreements reflect the importance of retaining their services and their potential contributions to the attainment of our long-term goals. None of the employment agreements with our named executive officers provide for tax gross ups and none includes any single trigger change-in-control provisions. The employment agreements with our named executive officers are described in the employment agreements section of the proxy statement.

#### ***Financial Restatements***

The compensation committee has not adopted a policy with respect to whether we will make retroactive adjustments to any cash- or equity-based incentive compensation paid to executive officers (or others) where the payment was predicated upon the achievement of financial results that were subsequently the subject of a restatement. Our compensation committee believes that this issue is best addressed when the need actually arises, when all of the facts regarding the restatement are known.

#### ***Tax and Accounting Treatment of Compensation***

Section 162(m) of the Internal Revenue Code, enacted in 1993, generally disallows a tax deduction to publicly held companies for compensation exceeding \$1 million paid to certain of the company's executive officers. The limitation applies only to compensation which is not considered to be performance-based. Our 2001 Stock Equity Plan and 2012 Equity Incentive Plan are structured so that any compensation deemed paid to an executive officer in connection with the exercise of option grants made under the plan will qualify as performance-based compensation which will not be subject to the \$1 million limitation. Generally, our executive officers are granted stock options, stock appreciation rights and restricted stock units under the 2012 Equity Incentive Plan and were granted stock options and stock appreciation rights under the 2001 Stock Equity Plan and 2003 Israeli Share Incentive Plan prior to their termination. The compensation committee is aware of the limitations imposed by Section 162(m), and the exemptions available therefrom, and will address the issue of deductibility when and if circumstances warrant. The

compensation committee also reserves the right to use its judgment to authorize compensation payments that do not comply with the exemptions in Section 162(m) when the committee believes that such payments are appropriate and in the best interests of our stockholders, after taking into account changing business conditions or the executive officer's performance. In addition, the compensation committee cannot ensure that compensation intended to qualify for deductibility under Section 162(m) will in fact be deductible because: (1) a number of requirements must be satisfied in order for the compensation to qualify; and (2) uncertainties as to the application and interpretation surrounding this section currently exist.

### **Compensation Committee Report**

The compensation committee has reviewed and discussed the Compensation Discussion and Analysis set forth above with our management. Based on its review and discussions, the committee recommended to our board of directors that the Compensation Discussion and Analysis be included in this report.

Submitted by the compensation committee:

Yair Shamir

Zvi Limon

Patrick Tanguy

**2012 Summary Compensation Table**

The following table sets forth the total compensation awarded to, earned by or paid to our principal executive officer, principal financial officer and the other executive officers whose total compensation in fiscal year 2012 exceeded \$100,000 for the periods presented. We refer to these executive officers as our named executive officers.

Name and Principal Position	Year	Salary (\$)	Bonus (\$) (1)	Option Awards (\$ (2)	All Other	Total (\$)
					Compensation (\$ (3)	
Ofer Elyakim Chief Executive Officer	2012	260,000		268,254	177,851	706,105
	2011	260,000		327,817	101,507	689,324
	2010	260,000	90,000	553,933	106,627	1,010,560
Dror Levy * Chief Financial Officer and Secretary	2012	186,625		111,757	86,130	384,512
	2011	201,224		144,054	89,794	435,072
	2010	184,838	45,000	260,316	82,037	572,191
David Dahan * Chief Operating Officer (4)	2012	180,514		138,785	57,199	376,498
	2011					
	2010					

- (1) Represents the bonus amounts awarded to Messrs. Elyakim and Levy in 2010 at the discretion of the compensation committee of the board of directors. No bonuses were awarded to the above named executive officers in 2011 or 2012.
  - (2) The amounts shown in this column do not reflect compensation actually received by the named executive officer. Instead, the amounts represent the aggregate grant date fair value of the awards based on FASB ASC No. 718, Stock Compensation ( FASB ASC No. 718 ). In addition, the amounts shown in this column include the benefit provided to our named executive officers under our Employee Stock Purchase Plan, which is derived mainly from a discount of 15% to fair market value when share purchases are made during the purchase period under the plan. The above benefit is available to all eligible employees.
  - (3) See the table captioned 2012 All Other Compensation below for greater detail.
  - (4) Mr. Dahan became an executive officer of the company effective February 1, 2012.
- \* Base salaries of Messrs. Levy and Dahan are denominated in New Israeli Shekel (NIS). The NIS amounts are translated into U.S. dollar at the average annual exchange rate of NIS 3.86 into U.S. dollar.



**2012 All Other Compensation**

The following tables set forth all other compensation awarded to, earned by or paid to each of our named executive officers during fiscal year 2012. The NIS amounts relating to the 2012 all other compensation for Messrs. Elyakim, Levy and Dahan are translated into U.S. dollar at the average annual exchange rate of NIS into U.S. dollar.

Name	Israeli Social Benefits (1)	Car Allowance (2)	Education Fund (3)	Vacation (4)	Social Security Payments (5)	Disability Insurance Payments (6)	Other(7)	Total (\$)
Ofer Elyakim	35,046	13,294	19,719	12,745	7,286	2,932	86,829	177,851
Dror Levy	24,877	24,922	13,998	8,483	7,425	1,306	5,118	86,130
David Dahan	24,044		13,539	9,577	6,679	1,083	2,278	57,199

- (1) Based on Israeli labor laws, an Israeli employee is entitled to severance pay upon termination of employment by the employer for any reason, including retirement, based on the most recent monthly base salary of such employee multiplied by the number of years of employment of such employee. We make a payment of 8.333% of each employee's monthly base salary to an insurance or pension fund to pay for this future liability payable to our employees upon termination of their employment. In addition, we make a payment of 5% of each employee's monthly base salary to another insurance or pension fund, which accrued amount may be withdrawn by the employee after retirement or, subject to various tax restrictions in Israel, after leaving our employment. The amounts represent the above referenced contributions we made on behalf of each of the named executive officers in 2012.
- (2) We generally provide all of our Israeli employees with a car for business-related purposes and pay the associated expenses for Mr. Dahan, the car allowance is part of his base salary.
- (3) As is customary in Israel applicable to all Israeli employees, we provide our Israeli employees with a certain amount of monthly contributions (7.5% of their base salary) for the benefit of each employee's study and training purposes, which amounts contributed by us to each of the named executive officers in 2012 are as specified.
- (4) Represents the dollar value of any positive difference between the vacation days to which the named executive officer is entitled in 2012 and the vacation days used by such named executive officer in 2012.

- (5) Represents payments we made to the Israeli government that the employees will receive in the event of unemployment or other disability.
- (6) As is customary in Israel, we make a payment of up to 2.5% of each employee's monthly base salary to cover employer liability associated with employment disability.
- (7) Includes an amount of \$84,370 paid to Mr. Elyakim as a tax reimbursement for additional taxes he was required to pay to the Israeli tax authorities due to his relocation to Hong Kong and for the period during which he was in Hong Kong. Mr. Elyakim's relocation to Hong Kong was for the company's benefit and occurred prior to him becoming one of our executive officers.

**2012 Grants of Plan Based Awards**

The following table sets forth each equity award granted to our named executive officers during fiscal year 2012.

Name	Grant Date	Approval Date	Threshold (#)	Target (#)	Maximum (#)	Units or Stock Awards	All Other Awards:		Exercise or Option Awards	Closing Price on Grant Date (\$/Sh)	Fair Value of Stock and Option Awards (\$)
							Number of Shares Underlying	Number of Securities			
Ofer Elyakim	2/1/2012	2/1/2012					52,500	\$ 6.16	\$ 6.16	257,040	
Dror Levy	2/1/2012	2/1/2012					25,000	\$ 6.16	\$ 6.16	111,757	
David Dahan	2/1/2012	2/1/2012					30,000	\$ 6.16	\$ 6.16	134,108	

- (1) Represents shares underlying stock appreciation right units made pursuant to our Amended and Restated 2003 Israeli Share Incentive Plan. Stock appreciation rights granted to our executive officers generally vest as to 25% of the grant on the first anniversary of the grant date with the remaining stock appreciation rights vesting quarterly over the next three years and expiring seven years from the date of grant. When the vested stock appreciation rights granted in 2012 are exercised, the number of underlying shares that may be received upon exercise cannot exceed 50% of the number of stock appreciation right units granted.
- (2) Represents the fair value of the stock appreciation rights as of the date they were granted, computed in accordance with FASB ASC 718 but disregarding adjustments for forfeiture assumptions. For a discussion of valuation assumptions under FASB ASC 718, see Note 2 to our 2012 Consolidated Financial Statements included in our 2012 Annual Report on Form 10-K.

**Outstanding Equity Awards at Fiscal Year-End 2012**

The following table sets forth information concerning unexercised options and stock appreciation rights held by each of our named executive officers as of December 31, 2012. None of our named executive officers had any stock awards outstanding at fiscal year-end 2012.

Name	Number of Securities Underlying Unexercised Options (#)	Number of Securities Underlying Unexercised Options (#)	Option Awards Equity Incentive Plan Awards: Number of Securities Underlying Unexercised Unearned Options (#)	Option Exercise Price (\$)(3)	Option Expiration Date(4)(5)
	Exercisable	Unexercisable			
Offer Elyakim	25,000(1)	0		27.36	2/7/2013
	7,500(1)	0		21.70	1/24/2014
	37,500(1)	0		10.23	1/30/2015
	112,500(2)	7,500(2)		5.97	2/2/2016
	80,210(1)	36,456(1)		7.26	1/27/2017
	30,626(1)	39,374(1)		7.49	1/31/2018
	0	52,500(1)		6.16	2/1/2019
Dror Levy	10,000(1)	0		28.59	4/5/2013
	20,000(1)	0		21.70	1/24/2014
	35,000(1)	0		10.23	1/30/2015
	63,281(1)	4,219(1)		5.97	2/2/2016
	36,666(1)	16,667(1)		7.26	1/27/2017
	13,126(1)	16,874(1)		7.49	1/31/2018
	0	25,000(1)		6.16	2/1/2019
David Dahan	0	30,000(1)		6.16	2/1/2019

- (1) Represents shares underlying stock appreciation rights granted pursuant to our Amended and Restated 2003 Israeli Share Incentive Plan.
- (2) Represents shares underlying stock option award granted pursuant to our 1998 Non-Officer Employee Stock Option Plan.
- (3) All stock options and stock appreciation rights were granted at fair market value on the grant date, as reported on NASDAQ.
- (4) The table sets forth the number of units granted pursuant to a stock appreciation right award. When the vested stock appreciation rights granted prior to 2009 are exercised, the number of underlying shares that may be received upon exercise cannot exceed 50% of the number of stock appreciation right units granted. When the vested stock appreciation rights granted in 2009, 2010, 2011 and 2012 are exercised, the number of underlying shares that may be received upon exercise cannot exceed 75%, 67%, 67% and 50%, respectively, of the number of stock appreciation right units granted.
- (5) Stock options granted to our executive officers generally vest as to 25% of the grant on the first anniversary of the grant date with the remaining options vesting quarterly over the next three years and expiring seven years from the grant date.



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### **2012 Option Exercises and Stock Vested**

None of our Named Executive Officers has received any stock awards and therefore no shares were acquired upon vesting of any stock awards. None of our Named Executive Officers exercised any equity awards in 2012.

### **Nonqualified Deferred Compensation**

We do not provide any nonqualified defined contribution or other deferred compensation plans to our named executive officers.

### **Employment Agreements**

Each of our named executive officers has a written employment agreement with us.

In connection with Ofer Elyakim's appointment as our Chief Executive Officer in July 2009, he entered into an employment agreement with DSP Israel, effective July 1, 2009. Mr. Elyakim's current annual salary was increased in January 2013 and is now \$300,000, subject to adjustment from time to time. In addition to any other bonus program approved by the board, Mr. Elyakim is entitled to an annual bonus, under the terms of the performance-based bonus plan approved by the compensation committee of our board of directors. Mr. Elyakim is employed at will. In November 2012, our compensation committee unanimously approved an amendment to Mr. Elyakim's employment agreement, effective on November 5, 2012. Pursuant to the amendment, if Mr. Elyakim desires to terminate his employment with the company (which for purposes of Mr. Elyakim's employment agreement includes any subsidiary of the company) without good reason (as defined in his employment agreement), he will have to notify the company eighteen months in advance. Similarly, if the company desires to terminate Mr. Elyakim's employment with the company without cause, it will have to notify Mr. Elyakim eighteen months in advance. However, if the company wishes to terminate Mr. Elyakim's employment but fails to provide him with the eighteen-month advance written notice, Mr. Elyakim would be entitled to receive an amount equal to eighteen months of his then-effective salary. If the requisite advance notice of eighteen months is provided by Mr. Elyakim to the company if he desires to terminate his employment with the company without good reason, then: (i) all of his rights under his employment agreement would continue during the eighteen-month period, and (ii) all equity awards held by him prior to the termination of his employment with the company would accelerate and immediately vest eighteen months following the date of such requisite notice and be exercisable in whole or in part at any time from the date of the vesting of the respective equity awards for a period of two years. In addition, if Mr. Elyakim's employment with the company is terminated by (i) the company following a change in control (as defined in his employment agreement); (ii) Mr. Elyakim for good reason; or (iii) the company without cause (as defined in his employment agreement), all of Mr. Elyakim's rights under his employment agreement would continue for eighteen months and all equity awards held by Mr. Elyakim would accelerate and immediately vest and be exercisable in whole or in part at any time for two years following the termination of his employment. On March 5, 2013, the employment agreement of Mr. Elyakim was amended, effective as of March 5, 2013, with unanimous approval by our compensation committee. The amendment amended, restated and clarified the specific circumstances upon which we may terminate Mr. Elyakim's employment for cause.

In June 2002, in connection with Dror Levy's initial employment as our Controller, he entered into an employment agreement with DSP Israel. No further agreement was entered into with Mr. Levy when he became our Chief Financial Officer. Mr. Levy's current annual salary was increased in January 2013 and is now approximately \$216,000, subject to adjustment from time to time (Mr. Levy's salary is determined in NIS and is 800,000 NIS annually). In addition to any other bonus program approved by the board, Mr. Levy is entitled to an annual bonus under the terms of the performance-based bonus plan approved by the compensation committee of our board of directors. Mr. Levy is employed at will. In November 2012, our compensation committee unanimously approved an amendment to Mr. Levy's employment agreement, effective on November 5, 2012. Pursuant to the amendment, if Mr. Levy desires to terminate his employment with the company (which for purposes of Mr. Levy's employment agreement includes any subsidiary of the company) without good reason (as defined in his employment agreement), he will have to notify the company one year in advance. Similarly, if the company desires to terminate Mr. Levy's employment with the company without cause, it will have to notify Mr. Levy one year in advance. However, if the company wishes to terminate Mr. Levy's employment but fails to provide him with the one-year advance written notice, Mr. Levy would be entitled to receive an amount equal to one year of his then-effective salary. If the requisite advance notice of one year is provided by Mr. Levy to the company if he desires to terminate his employment with the company without good reason, then: (i) all of his rights under his employment agreement would continue during the one-year period, and (ii) all equity awards held by him prior to the termination of his employment with the Company would accelerate and immediately vest one year following the date of such requisite notice and be exercisable in whole or in part at any time from the date of the vesting of the respective equity awards for a period of one year. In addition, if Mr. Levy's employment with the company is terminated by (i) the company following a change in control (as defined in his employment agreement); (ii) Mr. Levy for good reason; or (iii) the company without cause (as defined in his employment agreement), all of Mr. Levy's rights under his employment agreement would continue for one year and all equity awards held by Mr. Levy would accelerate and immediately vest and be exercisable in whole or in part at any time for one year following the termination of his employment. On March 5, 2013, the employment agreement of Mr. Levy was amended, effective as of March 5, 2013, with unanimous approval by our compensation committee. The amendment amended, restated and clarified the specific circumstances upon which we may terminate Mr. Levy's employment for cause.

In connection with David Dahan's appointment as our Chief Operating Officer, he executed an employment agreement with DSP Group Israel. Pursuant to the agreement, Mr. Dahan's annual salary is approximately \$202,000, subject to adjustment from time to time (Mr. Dahan's salary is determined in New Israeli Shekel (NIS) and is 62,600 NIS per month). Mr. Dahan also is eligible to receive an annual bonus under the terms of the performance-based bonus plan approved by the compensation committee of our board of directors. Mr. Dahan is employed at will. In the event Mr. Dahan desires to terminate his employment with us, he must notify us three months in advance. Similarly, if we desire to terminate Mr. Dahan's employment with us, we must notify Mr. Dahan three months in advance; provided that we may terminate Mr. Dahan's employment immediately without notice for cause (as defined in his employment agreement). Other than for cause, we also may terminate Mr. Dahan's employment without the three-months advance notice if we pay him an amount equal to three-months of his then-effective salary. Mr. Dahan's employment agreement does not provide for any additional compensation in

the event of termination of his employment or a change in control of the company. On March 5, 2013, the employment agreement of Mr. Dahan was amended effective as of March 5, 2013, with unanimous approval by our compensation committee. The amendment amended, restated and clarified the specific circumstances upon which we may terminate Mr. Dahan's employment for cause.

**Potential Payments Upon Termination or Change of Control**

The following tables set forth the amount of compensation to each of Messrs. Elyakim, Levy and Dahan in the event termination of such executive officer's employment or a change in control of our company occurred as of December 31, 2012.

Name: Ofer Elyakim	Voluntary Termination by				Upon a Change in Control and Termination (\$)
	Termination for Cause (\$)	Employee After Provision of Requisite Notice (\$)	Termination upon Death of Employee (\$)	Termination w/o Cause or for Good Reason (\$)	
Base Salary				598,190	598,190
Bonus					120,000
Vested and Unvested Options/SARs (1)					
Accrued Vacation Pay	67,045	67,045	67,045	67,045	67,045
<b>Total</b>	<b>67,045</b>	<b>67,045</b>	<b>67,045</b>	<b>665,235</b>	<b>785,235</b>

(1) As of December 31, 2012 (the last trading day of fiscal 2012), Mr. Elyakim had no in-the-money options or SARs outstanding.

Name: Dror Levy	Voluntary Termination by				Upon a Change in Control and Termination (\$)
	Termination for Cause (\$)	Employee After Provision of Requisite Notice (\$)	Termination upon Death of Employee (\$)	Termination w/o Cause or for Good Reason (\$)	
Base Salary				304,122	304,122
Bonus					42,861
Vested and Unvested Options/SARs (1)					
Accrued Vacation Pay	47,082	47,082	47,082	47,082	47,082
<b>Total</b>	<b>47,082</b>	<b>47,082</b>	<b>47,082</b>	<b>351,204</b>	<b>394,065</b>

(1) As of December 31, 2012 (the last trading day of fiscal 2012), Mr. Levy had no in-the-money options or SARs outstanding.

Name: David Dahan	Termination for Cause (\$)	Voluntary Termination by Employee After Provision of Requisite Notice (\$)	Termination upon Death of Employee (\$)	Termination w/o Cause or for Good Reason (\$)	Upon a Change in Control and Termination (\$)
Base Salary				51,041	
Bonus					40,833
Vested and Unvested Options/SARs (1)					
Accrued Vacation Pay	9,729	9,729	9,729	9,729	9,729
<b>Total</b>	<b>9,729</b>	<b>9,729</b>	<b>9,729</b>	<b>60,770</b>	<b>50,562</b>

(1) As of December 31, 2012 (the last trading day of fiscal 2012), Mr. Dahan had no in-the-money options or SARs outstanding.

#### **DIRECTOR COMPENSATION**

We use a combination of cash and stock-based incentive compensation to attract and retain qualified candidates to serve on our board. In setting director compensation, we consider the significant amount of time that directors expend in fulfilling their duties to the company as well as the skill-level we require of members of our board. We do not currently have a minimum share ownership requirement for our directors.

#### **Cash Compensation Paid to Board Members**

Directors who are also employees do not receive any additional compensation for their services as directors. Directors who are not employees receive an annual retainer of \$32,000, payable in quarterly installments of \$8,000 each. The retainer contemplates attendance at four board meetings per year. Additional board meetings of a face-to-face nature are compensated at a rate of \$1,000 per meeting. In addition, committee meetings of a face-to-face nature and on a telephonic basis are compensated at a rate of \$1,000 per meeting. All directors are reimbursed for expenses incurred in connection with attending board and committee meetings.

#### **Stock Option Program**

Each of our non-employee directors is also entitled to participate in our 1993 Director Stock Option Plan (the 1993 Plan). The director option plan provides for the grant of non-statutory options to our non-employee directors. The director option plan is designed to work automatically; however, to the extent administration is necessary, it will be provided by our board of directors. The director option plan provides that each eligible director is granted an option to purchase 30,000 shares of our common stock on the date on which he first becomes a director (the First Option). Thereafter, each non-employee director is granted a subsequent option to purchase 15,000 shares of our common stock on January 1 of each year if, on such date, he shall have served on our board of directors for at least six months (a Subsequent Option). In addition, an additional option to purchase 15,000 shares of our common stock (a Committee Option) is granted on January 1 of each year to each non-employee director for each committee of the board on which he shall have served as a chairperson for at least six months.



Subject to stockholder approval of the increase in the name of shares authorized under the company's Amended and Restated 2012 Equity Incentive Plan (the 2012 Plan), we intend to grant our non-employee directors stock options under a subplan under the 2012 Plan. This subplan generally will have similar terms as the 1993 Plan. For more information about the terms of the director subplan under the 2012 Plan, see Proposal 3 of the proxy statement.

The following table sets forth the compensation paid to each of our non-employee directors during fiscal year 2012.

Name	Fees Paid in			Total (\$)
	Cash (\$)	Stock Awards (\$)	Option Awards (\$)(1)	
Eliyahu Ayalon (2)	32,000		41,245	73,245
Thomas A. Lacey (3)	16,000		92,155	108,155
Zvi Limon (4)	38,000		82,491	120,491
Reuven Regev (5)	33,000		41,245	74,245
Yair Seroussi (6)	36,000		41,245	77,245
Yair Shamir (7)	38,000		82,491	120,491
Kenneth Traub (8)	16,000		92,155	108,155
Patrick Tanguy (9)	38,000		41,245	79,245

- (1) The amounts shown in this column do not reflect compensation actually received by the directors. Instead, the amounts represent the aggregate grant date fair value of the awards based on FASB ASC No. 718.
- (2) On January 1, 2012, Mr. Ayalon was granted a Subsequent Option (15,000) at an exercise price of \$5.21 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Ayalon had outstanding stock options to purchase 589,167 shares of our common stock.
- (3) On May 15, 2012, in connection with Mr. Lacey's appointment as a director, he was granted a First Option (30,000) at an exercise price of \$5.98 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Lacey had outstanding stock options to purchase 30,000 shares of our common stock.
- (4) On January 1, 2012, Mr. Limon was granted a Subsequent Option (15,000) and a Committee Option (15,000), each at an exercise price of \$5.21 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Limon had outstanding stock options to purchase 286,666 shares of our common stock.

- (5) On January 1, 2012, Mr. Regev was granted a Subsequent Option (15,000) at an exercise price of \$5.21 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Regev had outstanding stock options to purchase 45,000 shares of our common stock.
- (6) On January 1, 2012, Mr. Seroussi was granted a Subsequent Option (15,000) at an exercise price of \$5.21 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Seroussi had outstanding stock options to purchase 140,000 shares of our common stock.
- (7) On January 1, 2012, Mr. Shamir was granted a Subsequent Option (15,000) and a Committee Option (15,000), each at an exercise price of \$5.21 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Shamir had outstanding stock options to purchase 280,000 shares of our common stock.
- (8) On May 15, 2012, in connection with Mr. Traub's appointment as a director, he was granted a First Option (30,000) at an exercise price of \$5.98 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Traub had outstanding stock options to purchase 30,000 shares of our common stock.
- (9) On January 1, 2012, Mr. Tanguy was granted a Subsequent Option (15,000) at an exercise price of \$5.21 per share under the 1993 Director Stock Option Plan. As of December 31, 2012, Mr. Tanguy had outstanding stock options to purchase 160,000 shares of our common stock.

**CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

We have entered into indemnification agreements with each of our directors and executive officers. Such agreements require us to indemnify such individuals to the fullest extent permitted by Delaware law.

All transactions between us and our officers, directors, principal stockholders and affiliates have been and will be approved by a majority of our board of directors, including a majority of our disinterested, non-employee directors on the board, and have been or will be on terms no less favorable to us than could be obtained from unaffiliated third parties. There were no related party transactions in 2012.

**Review, Approval or Ratification of Transactions with Related Persons**

We have adopted a written policy regarding related person transactions which is incorporated in the Charter of the Audit Committee. Pursuant to this policy, our Audit Committee must review and approve any such transactions.

**PROPOSAL NO. 2**

**AMENDMENT AND RESTATEMENT OF THE**

**1993 EMPLOYEE STOCK PURCHASE PLAN**

Our stockholders are being asked to approve an amendment and restatement of our Amended and Restated 1993 Employee Stock Purchase Plan (the Purchase Plan). The proposed amendment and restatement of the Purchase Plan will increase the number of shares reserved for issuance under the Purchase Plan from 3,300,000 shares to 3,800,000 shares. The purpose of amending and restating the Purchase Plan is to enable us to continue to attract and retain talented employees by offering them participation in the Purchase Plan.

Our board of directors has approved the proposed amendment and restatement of the Purchase Plan as described above.

The purpose of the Purchase Plan is to provide our employees and employees of our subsidiaries with an opportunity to purchase common stock through accumulated payroll deductions. The Purchase Plan is intended to qualify as an Employee Stock Purchase Plan under Section 423 of the Internal Revenue Code of 1986 (the Code). Accordingly, the provisions of the Purchase Plan will be construed so as to extend and limit participation in the Purchase Plan in a manner consistent with the requirements of the Code. The Purchase Plan is intended to enable us and our subsidiaries to attract and retain the best available personnel, to provide additional incentive to current employees, and to promote the success of the company's business. The board of directors believes that our long-term success is dependent upon the ability of the company and our subsidiaries to attract and retain superior individuals who, by virtue of their ability and qualifications, make important contributions to us.

Subject to stockholder approval, we plan to register the additional 500,000 shares reserved under the Purchase Plan on a Registration Statement on Form S-8.

A general description of the principal terms of the Amended and Restated Purchase Plan as proposed is set forth below. However, the summary does not purport to be a complete description of all of the provisions of the Purchase Plan.

**General Description**

The Purchase Plan was adopted by our board of directors and approved by our stockholders in 1993. There are currently 3,300,000 shares of common stock reserved for issuance under the Purchase Plan. If the amendment and restatement of the Purchase Plan is approved by the stockholders, the number of shares of common stock reserved for issuance under the Purchase Plan will be increased by 500,000 shares from 3,300,000 shares to 3,800,000 shares. As of April 1, 2013, a total of 2,902,575 shares have been purchased under the Purchase Plan, and 397,425 shares of common stock remained available for purchase thereunder. As of April 1, 2013, the closing price of a share of our common stock as reported on the NASDAQ Global Market was \$7.69.

The number of shares of our common stock reserved for issuance under the Purchase Plan is also subject to adjustment in the event of a stock split, stock dividend or other similar change in the common stock or the capital structure of the company.

The Purchase Plan is administered by the board of directors, or a committee of the board as designated by the board from time to time (the Plan Administrator), which has the authority to determine the terms and conditions under which purchase rights are to be granted under the Purchase Plan for any offering period during the term of the Purchase Plan, and to resolve all questions relating to the administration of the plan.

The purpose of the Purchase Plan is to provide our employees who participate in the Purchase Plan with an opportunity to purchase common stock through payroll deductions. The Purchase Plan is intended to qualify as an employee stock purchase plan under the provisions of Section 423 of the Code. Employees, including officers, of the company and certain of our subsidiaries (as designated by our board of directors) are eligible to participate in the Purchase Plan. Payroll deductions may be up to 10% (in whole percentage increments) of a participant's compensation (as defined in the Purchase Plan). Notwithstanding the foregoing, to the extent necessary to comply with Section 423(b)(8) of the Code, a participant's payroll deductions may be decreased to zero percent during any purchase period that is scheduled to end during the relevant calendar year.

Any person who is employed by us or certain of our subsidiaries (as designated our board of directors) for at least 20 hours per week and more than five months in a calendar year is eligible to participate in the Purchase Plan, provided that the employee is employed on the first trading day of an offering period and subject to certain limitations imposed by Section 423(b) of the Code. Eligible employees become participants in the Purchase Plan by delivering to us a subscription agreement authorizing payroll deductions prior to the commencement of the applicable offering period, unless a later date is set by our board of directors for all eligible employees. At December 31, 2012, the potential number of participants in the Purchase Plan was approximately 320 employees.

The Purchase Plan has consecutive, overlapping offering periods of 24 months duration commencing each January 1 and July 1. The Plan Administrator may alter the duration of the offering periods if such change is announced at least 15 days prior to the scheduled beginning of the first offering period to be affected thereafter.

The price per share at which shares are sold under the Purchase Plan is equal to 85% of the fair market value of the common stock on the enrollment date or on the exercise date, whichever is lower. The fair market value of the common stock on a given date is the closing sale price of the common stock on the NASDAQ Global Select Market as of such date. The number of shares of common stock which may be purchased is subject to adjustment in the event of a stock split, stock dividend or other similar change in the common stock or the capital structure of the company. We make no cash contributions to the Purchase Plan, but bear the expenses of administration.

At the beginning of an offering period, each participant will be granted the right to purchase up to the number of shares determined by dividing 10% of the participant's

compensation receivable during the offering period by the applicable purchase price. No employee shall be granted a purchase right under the Purchase Plan (1) if immediately after the grant of the purchase right, the employee would own 5% or more of the total combined voting power or value of all classes of stock of the company or of any of our subsidiaries (including stock which may be purchased under the Purchase Plan or issued pursuant to any other options) or (2) which would permit the employee to buy more than \$25,000 worth of stock (determined at the fair market value of the shares at the time the purchase right is granted) in any calendar year. No fractional shares will be purchased; any payroll deductions accumulated in a participant's account which are not sufficient to purchase a full share shall be carried over to the next purchase period or offering period, whichever applies, or returned to the participant, if the participant withdraws from the Purchase Plan.

A participant may increase or decrease the rate of his or her payroll deduction for the remainder of an offering period by filling out a new subscription agreement and delivering it to us (or our designee). The participant's new subscription agreement will remain in effect for the entire offering period and each subsequent offering period, unless the participant further modifies his subscription or terminates his participation in the Purchase Plan.

A participant's interest in a given offering period may be terminated in whole, but not in part, by delivering to us a written notice which indicates the participant's withdrawal from such offering period. Such withdrawal may be elected at any time prior to the end of the applicable offering period. Any withdrawal by the participant of accumulated payroll deductions for a given offering period automatically terminates the participant's interest in that offering period. If a participant withdraws from an offering period, payroll deductions will not resume at the beginning of the succeeding offering period unless the participant delivers to us a new subscription agreement.

Upon termination of a participant's employment relationship, including by virtue of his or her having failed to remain an employee with us for at least twenty (20) hours per week during an offering period in which the employee is a participant, the payroll deductions credited to such participant's account during the offering period but not yet used to exercise the option will be returned to such participant or, in the case of his or her death, to the person or persons entitled thereto, and such participant's option will be automatically terminated.

No rights or accumulated payroll deductions of a participant under the Purchase Plan may be pledged, assigned, transferred or otherwise disposed of for any reason (other than by will and the laws of descent and distribution, as provided in the Purchase Plan) and any such attempt may be treated by us as an election to withdraw from the Purchase Plan.

Subject to any required action by our stockholders, in the event any change, such as a stock split or dividend, is made in our capitalization which results in an increase or decrease in the number of outstanding shares of common stock without receipt of consideration by the company, an appropriate adjustment shall be made in the number of shares under the Purchase Plan and the price per share covered by each outstanding option. In the event of a proposed dissolution or liquidation of the company, the offering periods in progress will terminate immediately prior to the consummation of such dissolution or liquidation, unless otherwise provided by our board of directors. In the event of a sale of all or substantially all of the assets of

the company, or the merger of the company with or into another corporation, each option under the Purchase Plan shall be assumed, or an equivalent option shall be substituted, by such successor corporation or a parent or subsidiary of such successor corporation, unless the Plan Administrator determines, in the exercise of its sole discretion and in lieu of such assumption or substitution, to shorten the offering period then in progress by setting a new exercise date (the New Exercise Date). If the Plan Administrator shortens the offering period then in progress in lieu of assumption in the event of a sale of assets or merger as described above, the Plan Administrator shall notify each participant in writing, at least ten business days prior to the New Exercise Date, that the exercise date for his or her option has been changed to the New Exercise Date and that his or her option will be exercised automatically on the New Exercise Date, unless prior to such date he or she has withdrawn from the offering period.

#### **Amendment and Termination of the Purchase Plan**

Our board of directors may amend the Purchase Plan at any time or from time to time or may terminate the Purchase Plan without approval of the stockholders. To the extent necessary to comply with applicable provisions of federal securities laws, state corporate and securities laws, the rules of any applicable stock exchange or national market system, and the rules of any foreign jurisdiction applicable to purchase rights granted to residents therein, we will obtain stockholder approval of any amendment to the Purchase Plan in such a manner and to such a degree as required. No amendment may alter any option previously granted under the Purchase Plan without the consent of the affected participant if such amendment would adversely affect the rights of the participant under the option, provided that the Purchase Plan or any one or more offering periods may be terminated by the Plan Administrator on any exercise date or by the Plan Administrator establishing a new exercise date with respect to any offering period and/or purchase period then in progress if the Plan Administrator determines that the termination of the Purchase Plan or such one or more offering periods is in the best interests of the company and our stockholders. Without stockholder consent and without regard to whether any participant rights may be considered to have been adversely affected, the Plan Administrator shall be entitled to limit the frequency and/or number of changes in the amount withheld during offering periods, change the length of purchase periods within any offering period, change the length of subsequent offering periods, determine whether subsequent offering periods shall be consecutive or overlapping, establish the exchange ratio applicable to amounts withheld in a currency other than U.S. dollars, establish additional terms, conditions, rules or procedures to accommodate the rules or laws of applicable foreign jurisdictions, permit payroll withholding in excess of the amount designated by a participant in order to adjust for delays or mistakes in our processing of properly completed withholding elections, establish reasonable waiting and adjustment periods and/or accounting and crediting procedures to ensure that amounts applied toward the purchase of common stock for each participant properly correspond with amounts withheld from the participant's compensation, and establish such other limitations or procedures as the Plan Administrator determines in its sole discretion advisable and which are consistent with the Purchase Plan. The Purchase Plan will remain in effect until terminated by the board.

#### **Amended Purchase Plan Benefits**

The benefits to be received by our employees pursuant to the amended and restated Purchase Plan are not determinable at this time.

The following table sets forth information with respect to purchases under the Purchase Plan during the fiscal year ended December 31, 2012. The executive group in 2012 consisted of Messrs. Elyakim, Levy and Dahan (as of February 1, 2012). The non-executive director group in 2012 consisted of Messrs. Ayalon, Limon, Reuven, Seroussi, Shamir, Silver (until May 2012) and Tanguy, as well as Messrs. Lacey and Traub as of May 15, 2012. Please note, however, that directors are not allowed to participate in the Purchase Plan.

Identity of Group	Purchases	% of Total Purchases (1)	Weighted Average Purchase Price Per Share (\$)
Ofer Elyakim			
Chief Executive Officer	4,802	1.2%	4.4200
Dror Levy			
Chief Financial Officer and Secretary	0	0	0
David Dahan			
Chief Operating Officer	2,003	0.5%	4.8960
Executive Group	6,805	1.7%	4.5536
Non-Executive Director Group	0	0	0
Non-Executive Employee Group	401,884	98.3%	4.5841

(1) Based on a total of 408,689 shares of common stock purchased under the Purchase Plan during the fiscal year ended December 31, 2012.

#### **Certain U.S. Federal Income Tax Information**

The following summarizes the federal income tax consequences of participation under the Purchase Plan and certain tax effects to us based upon federal income tax laws in effect on the date of this proxy statement. This summary does not purport to be complete, and does not discuss any non-U.S., state or local tax consequences. In addition, the discussion does not address tax consequences which may vary with, or are contingent on, a participant's individual circumstances. Each participant in the Purchase Plan is strongly urged to consult with his or her tax advisor regarding participation in the Purchase Plan.

The Purchase Plan and the right of participants to make purchases thereunder are intended to qualify under the provisions of Section 423 of the Code. Under these provisions, no income will be taxable to a participant at the time of grant of the purchase right or purchase of shares. Amounts deducted from a participant's pay under the Purchase Plan are part of the employee's regular compensation and remain subject to federal, state and local income and employment withholding taxes.

Taxable income will not be recognized until there is a sale or other disposition of the shares acquired under the Purchase Plan or in the event the participant should die while still owning the purchased shares.

If the participant sells or otherwise disposes of the purchased shares within two years after the start date of the offering period in which such shares were acquired or within one year after the actual purchase date of those shares, then the participant will recognize ordinary income



in the year of such sale or disposition equal to the amount by which the fair market value of the shares on the purchase date exceeded the purchase price paid for those shares, and we will be entitled to an income tax deduction, for the taxable year in which such sale or disposition occurs, equal in amount to such excess.

If the participant sells or disposes of the purchased shares more than two years after the start date of the offering period in which such shares were acquired and more than one year after the actual purchase date of those shares, then the participant will recognize ordinary income in the year of such sale or disposition equal to the lesser of (i) the amount by which the fair market value of the shares on the sale or disposition date exceeds the purchase price paid for those shares or (ii) 15% of the fair market value of the shares on the start date of the offering period, and any additional gain upon the disposition will be taxed as long-term capital gain. We will not be entitled to any income tax deduction with respect to such sale or disposition.

If the participant still owns the purchased shares at the time of his or her death, the lesser of (i) the amount by which the fair market value of the shares on the date of death exceeds the purchase price or (ii) 15% of the fair market value of the shares on his or her entry date into the offering period in which those shares were acquired will constitute ordinary income in the year of death.

**Required Vote**

The affirmative vote of the holders of a majority of the shares of our common stock present or represented at the annual meeting is required to approve the amendment and restatement of the Purchase Plan. Abstentions will have the same effect as no votes on this proposal, whereas broker non-votes will have no effect.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE APPROVAL OF  
THE PROPOSED AMENDMENT AND RESTATEMENT OF THE 1993 EMPLOYEE  
PURCHASE PLAN**

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**PROPOSAL NO. 3:**

**APPROVAL OF THE AMENDMENT AND RESTATEMENT OF THE 2012 EQUITY INCENTIVE PLAN**

**General**

Our stockholders are being asked to approve an amendment and restatement of our 2012 Equity Incentive Plan (the "2012 Plan"). The proposed amendment and restatement of the 2012 Plan will increase the number of shares reserved for issuance under the 2012 Plan from 350,000 shares to 1,450,000 shares. The purpose of amending and restating the 2012 Plan is to enable us to continue to attract and retain the best available personnel, including employees and directors, by offering them participation in the 2012 Plan.

Our board of directors has approved the proposed amendment and restatement of the 2012 Plan as described above. We believe strongly that the approval of the amendment and restatement of the 2012 Plan is essential to our success. Our employees are our most valuable assets. Stock options and the other awards permitted under the 2012 Plan are vital to our ability to attract and retain outstanding and highly skilled employees, especially in the competitive labor markets in which we compete. These awards also are crucial to our ability to motivate employees to achieve our goals. The terms of the 2012 Plan are designed to allow the Company to continue to attract, retain and motivate people whose skills and performance are critical to the Company's success. We will continue to monitor the environment in which we operate and make changes to our equity compensation program to help us meet our goals, including achieving long-term stockholder value.

In addition, we are sensitive to the concerns of our stockholders regarding dilution. Therefore, our board of directors commits to our stockholders that we will not grant a number of shares subject to options, stock appreciation rights or other stock awards to employees or non-employee directors at an annual average rate greater than 5.83% over the next three fiscal years (commencing on January 1, 2013). For purposes of calculating the annual average rate, the numerator for calculating the percentage for each fiscal year shall be the total number of shares granted in such fiscal year and the denominator shall be the weighted average number of common stock outstanding at the end of fiscal year. For this purpose, when determining the number of shares granted in a year, any full-value awards (these are restricted stock awards and restricted stock units, but not stock options) will count as equivalent to 1.5 shares.

Subject to stockholder approval, we plan to register the additional 1,100,000 shares reserved under the 2012 Plan on a Registration Statement on Form S-8.

As of April 1, 2013, the closing sales price of a share of the Company's common stock as reported on the NASDAQ Global Market was \$7.69. As of December 31, 2012, the potential number of participants in the 2012 Plan was approximately 320 employees.

A general description of the principal terms of the Amended and Restated 2012 Plan as proposed is set forth below. However, the summary does not purport to be a complete description of all of the provisions of the 2012 Plan.

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## General Description

**Purpose.** The purposes of the 2012 Plan are to attract and retain the best available personnel, to provide additional incentives to our employees, consultants and directors through ownership of our Shares, and to promote the success of the Company's business.

**Shares Reserved for Issuance under the 2012 Plan.** If approved by our stockholders, the total number of Shares reserved for issuance under the 2012 Plan will be 1,450,000 Shares.

The maximum number of Shares with respect to which options and stock appreciation rights may be granted to a participant during a calendar year is 175,000 Shares. In connection with a participant's commencement of service with the Company or a related entity of the Company, the participant may be granted options and stock appreciation rights for up to an additional 175,000 Shares, which would not count against the limit set forth in the previous sentence. For awards of restricted stock and restricted stock units that are intended to be performance-based compensation under Section 162(m) of the Code, the maximum number of Shares subject to such awards that may be granted to a participant during a calendar year is 175,000 Shares.

**Share Counting.** Any Shares covered by an award which is forfeited, canceled, expires or is settled in cash shall be deemed not to have been issued for purposes of determining the maximum number of Shares which may be issued under the 2012 Plan. Shares that have actually been issued under the 2012 Plan pursuant to an award shall not be returned to the 2012 Plan and shall not become available for future grant under the 2012 Plan, except where unvested Shares are forfeited or repurchased by the Company at the lower of their original purchase price or their fair market value at the time of such repurchase. Shares tendered or withheld in payment of an option exercise price, Shares withheld by the Company to pay any tax withholding obligation, and all Shares covered by the portion of a stock appreciation right that is exercised (regardless of whether Shares are actually issued in connection with such exercise) shall not be returned to the 2012 Plan and shall not become available for future issuance under the 2012 Plan.

**Administration.** The 2012 Plan will be administered by the 2012 Plan administrator (the Administrator), defined as the Board or one (1) or more committees designated by the Board. The Compensation Committee will initially act as the Administrator. With respect to grants to Officers and Directors, the Compensation Committee shall be constituted in such a manner as to satisfy applicable laws, including Rule 16b-3 promulgated under the Exchange Act and Section 162(m) of the Code.

**No Repricings without Stockholder Approval.** The Company shall obtain stockholder approval prior to (i) the reduction of the exercise price of any option or the base appreciation amount of any stock appreciation right awarded under the 2012 Plan or (ii) the cancellation of an option or stock appreciation right at a time when its exercise price or base appreciation amount exceeds the fair market value of the underlying Shares, in exchange for another option, stock appreciation right, restricted stock or other award or for cash (unless the cancellation and exchange occurs in connection with a Corporate Transaction (as defined in the 2012 Plan and as described below)). Notwithstanding the foregoing, cancelling an option or stock appreciation right in exchange for another option, stock appreciation right, restricted stock, or other award with an exercise price, purchase price or base appreciation amount that is equal to or greater than the exercise price or base appreciation amount of the original option or stock appreciation right will not be subject to stockholder approval.

**Terms and Conditions of Awards.** The 2012 Plan provides for the grant of stock options, restricted stock, restricted stock units, dividend equivalent rights and stock appreciation rights (collectively referred to as awards). Stock options granted under the 2012 Plan may be either incentive stock options under the provisions of Section 422 of the Code, or nonqualified stock options. Incentive stock options may be granted only to employees. Awards other than incentive stock options may be granted to our employees, consultants and directors or to employees, consultants and directors of our related entities. To the extent that the aggregate fair market value of the Shares subject to options designated as incentive stock options which become exercisable for the first time by a participant during any calendar year exceeds \$100,000, such excess options shall be treated as nonqualified stock options. Under the 2012 Plan, awards may be granted to such employees, consultants or directors who are residing in non-U.S. jurisdictions as the Administrator may determine from time to time. Each award granted under the 2012 Plan shall be designated in an award agreement.

Subject to applicable laws and except as otherwise provided by the Board, the Administrator will have the authority, in its discretion, to select employees, consultants and directors to whom awards may be granted from time to time, to determine whether and to what extent awards are granted, to determine the number of Shares or the amount of other consideration to be covered by each award, to approve forms of award agreement for use under the 2012 Plan, to determine the terms and conditions of any award (including the vesting schedule applicable to the award), to amend the terms of any outstanding award granted under the 2012 Plan (provided that any amendment that would adversely affect a participant's rights under an outstanding award would not be made without the participant's written consent), to construe and interpret the terms of the 2012 Plan and awards granted, to establish additional terms, conditions, rules or procedures to accommodate the rules or laws of applicable non-U.S. jurisdictions and to take such other action, not inconsistent with the terms of the 2012 Plan, as the Administrator deems appropriate.

The term of any award granted under the 2012 Plan will be stated in the applicable award agreement but may not exceed a term of more than ten years (or five years in the case of an incentive stock option granted to any participant who owns stock representing more than 10% of our combined voting power or any parent or subsidiary of us), excluding any period for which the participant has elected to defer the receipt of the Shares or cash issuable pursuant to the award pursuant to a deferral program the Administrator may establish in its discretion.

The 2012 Plan authorizes the Administrator to grant incentive stock options at an exercise price not less than 100% of the fair market value of our common stock on the date the option is granted (or 110%, in the case of an incentive stock option granted to any employee who owns stock representing more than 10% of our combined voting power or any parent or subsidiary of us). In the case of nonqualified stock options, stock appreciation rights, and awards intended to qualify as performance-based compensation, the exercise price, base appreciation amount or purchase price, if any, shall be not less than 100% of the fair market value per Share on the date of grant. In the case of all other awards granted under the 2012 Plan, the exercise or purchase price shall be determined by the Administrator. The exercise or purchase price is generally payable in cash, check, Shares or, with respect to options, payment through a broker-dealer sale and remittance procedure or a net exercise procedure, or any combination of the foregoing methods of payment.

Under the 2012 Plan, the Administrator may establish one or more programs to permit selected participants the opportunity to elect to defer receipt of consideration payable under an award. The Administrator also may establish under the 2012 Plan separate programs for the grant of particular forms of awards to one or more classes of participants.

**Section 162(m) of the Code.** The maximum number of Shares with respect to which options and stock appreciation rights may be granted to a participant during a calendar year is 175,000 Shares. In connection with a participant's commencement of service with the Company or a related entity of the Company, the participant may be granted options and stock appreciation rights for up to an additional 175,000 shares, which would not count against the limit set forth in the previous sentence. The foregoing limitations shall be adjusted proportionately by the Administrator in the event of a stock split, reverse stock split, stock dividend, combination or reclassification of Shares or other similar change in our Shares or our capital structure. Under Code Section 162(m) no deduction is allowed in any taxable year of the Company for compensation in excess of \$1 million paid to the Company's covered employees. An exception to this rule applies to compensation that is paid to a covered employee pursuant to a stock incentive plan approved by stockholders and that specifies, among other things, the maximum number of Shares with respect to which options and stock appreciation rights may be granted to eligible participants under such plan during a specified period. Compensation paid pursuant to options and stock appreciation rights granted under such a plan and with an exercise price or base appreciation amount equal to the fair market value of common stock on the date of grant is deemed to be inherently performance-based, since such awards provide value to participants only if the stock price appreciates. To the extent required by Section 162(m) of the Code or the regulations thereunder, in applying the foregoing limitations, if any option or stock appreciation right is canceled, the canceled award shall continue to count against the maximum number of Shares with respect to which an award may be granted to a participant.

For awards of restricted stock and restricted stock units that are intended to be performance-based compensation under Section 162(m) of the Code, the maximum number of Shares subject to such awards that may be granted to a participant during a calendar year is 175,000 Shares. The foregoing limitation shall be adjusted proportionately by the plan administrator in the event of a stock split, reverse stock split, stock dividend, combination or reclassification of Shares or other similar change in our Shares or our capital structure. In order for restricted stock and restricted stock units to qualify as performance-based compensation, the Administrator must establish a performance goal with respect to such award in writing not later than 90 days after the commencement of the services to which it relates (or, if earlier, the date after which 25% of the period of service to which the performance goal relates has elapsed) and while the outcome is substantially uncertain. In addition, the performance goal must be stated in terms of an objective formula or standard.

Under Code Section 162(m), a covered employee is the Company's chief executive officer and the three other most highly compensated officers of the Company other than the chief financial officer.

The 2012 Plan includes performance criteria that may be considered, individually or in combination, by the Administrator when granting performance-based awards, including the following: (i) sales and net sales, (ii) appreciation in and/or maintenance of the price of Shares or any other publicly-traded securities of the Company, (iii) expense levels, (iv) sales or licenses of the Company's assets, including its intellectual property, whether in a particular jurisdiction or territory or globally, or through partnering transactions, (v) implementation, completion or attainment of measurable objectives with respect to research, development, manufacturing, commercialization, products or projects, production volume levels, acquisitions and divestitures and recruiting and maintaining personnel, (vi) financing and other capital raising transactions (including sales of the Company's equity or debt securities, factoring transactions), (vii) revenue growth or product revenue growth, (viii) profits (including gross profits, operating profits, net operating profits, controllable profits and profit margins), (ix) financial ratios, including those measuring liquidity, activity, profitability or leverage, (x) cost of capital or assets under management, (xi) net operating income (before or after taxes) or operating income (before or after taxes), (xii) earnings (including earnings before taxes, earnings before interest and taxes, earnings before interest, taxes and depreciation, earnings before interest, taxes and amortization or earnings before interest, taxes, depreciation and amortization), (xiii) revenue, (xiv) strategic partnerships or transactions (including in-licensing and out-licensing of intellectual property and establishing relationships with commercial entities with respect to the marketing, distribution and sale of the Company's products (including with group purchasing organizations, distributors and other vendors)), (xv) co-development, co-marketing, profit sharing, joint venture or other similar arrangements, (xvi) pre- or after-tax income (before or after allocation of corporate overhead and bonus), (xvii) market share, (xviii) regulatory achievements (including submitting or filing applications or other documents with regulatory authorities or receiving approval of any such applications or other documents; passing pre-approval inspections (whether of the Company or third parties)), (xix) operating margins, gross margins or cash margins, (xx) earnings per share, (xxi) comparisons with various stock market indices, (xxii) stockholder equity, (xxiii) debt reduction, (xxiv) net income (before or after taxes), (xxv) reductions in costs, (xxvi) year-end cash, (xxvii) return on equity, (xxviii) operating cash flow or cash flow per share (before or after dividends) and cash flow or cash flow per share (before or after dividends), (xxix) working capital levels, including cash, inventory and accounts receivable, (xxx) total shareholder return, (xxxii) return on capital (including return on total capital or return on invested capital), (xxxiii) research and development achievements, (xxxiv) return on assets or net assets, (xxxv) cash flow return on investment, (xxxvi) operating efficiencies, (xxxvii) economic value-added models or equivalent metrics, (xxxviii) success in recruitment of financial advisors, (xxxix) customer growth, (xxxix) employee or customer satisfaction (including objective customer indicators), (xxxx) productivity, (xxxxi) supplier awards from significant customers, (xxxxii) credit rating, (xxxxiii) contract awards or backlog, (xxxxix) bookings or orders, (xxxxv) budget comparisons, and (xxxxvi) improvements in capital structure. The performance criteria may be applicable to the Company, any parent or subsidiary of the Company, and/or any individual business units of the Company or any parent or subsidiary of the Company.

***Change in Capitalization.*** Subject to any required action by the stockholders of the Company, the number of Shares covered by outstanding awards, the number of Shares that have been authorized for issuance under the 2012 Plan, the exercise or purchase price of each outstanding award, the maximum number of Shares that may be granted subject to awards to any participant in a calendar year, as well as other terms that the Administrator determines require

adjustment, shall be proportionally adjusted by the Administrator in the event of (i) any increase or decrease in the number of issued Shares resulting from a stock split, reverse stock split, stock dividend, combination or reclassification of the Shares or similar transaction affecting the Shares, (ii) any other increase or decrease in the number of issued Shares effected without receipt of consideration by the Company or (iii) any other transaction with respect to our Shares including a corporate merger, consolidation, acquisition of property or stock, separation (including a spin-off or other distribution of stock or property), reorganization, liquidation (whether partial or complete), distribution of cash or other assets to stockholders other than a normal cash dividend, or any similar transaction; provided, however, that conversion of any convertible securities of the Company shall not be deemed to have been effected without receipt of consideration. Such adjustment shall be made by the Administrator and its determination shall be final, binding and conclusive.

**Corporate Transaction.** Effective upon the consummation of a Corporate Transaction, all outstanding awards under the 2012 Plan will terminate unless the awards are assumed in connection with the Corporate Transaction. In addition, except as provided otherwise in an individual award agreement, for the portion of each award that is neither assumed nor replaced, such portion of the award shall automatically become fully vested and exercisable and be released from any repurchase or forfeiture rights (other than repurchase rights exercisable at fair market value) for all of the Shares (or other consideration) at the time represented by such portion of the award, immediately prior to the specified effective date of such Corporate Transaction, provided that the Grantee's Continuous Service has not terminated prior to such date.

Under the 2012 Plan, Corporate Transaction includes a merger or consolidation in which the Company is not the surviving entity, except for a transaction the principal purpose of which is to change the state in which the Company is incorporated; the sale, transfer or other disposition of all or substantially all of the assets of the Company; the complete liquidation or dissolution of the Company; any reverse merger or series of related transactions culminating in a reverse merger in which the Company is the surviving entity but (i) the Shares outstanding immediately prior to such merger are converted or exchanged by virtue of the merger into other property or (ii) in which securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities are transferred to a person or persons different from those who held such securities immediately prior to such merger or the initial transaction culminating in such merger; and an acquisition in a single or series of related transactions by any person or related group of persons (other than the Company or by a Company-sponsored employee benefit plan) of beneficial ownership of securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities.

**Change in Control.** Except as provided otherwise in an individual award agreement, in the event of a Change in Control (other than a Change in Control which also is a Corporate Transaction), all outstanding awards under the 2012 Plan automatically shall become fully vested and exercisable and be released from any repurchase or forfeiture rights (other than repurchase rights exercisable at fair market value), immediately prior to the specified effective date of such Change in Control, for all of the Shares (or other consideration) at the time represented by such awards, provided that the grantee's continuous service, as such term is defined in the 2012 Plan, has not terminated prior to such date.

Under the 2012 Plan, a Change in Control is defined as a change in ownership or control of the Company effected through either of the following transactions: (i) the direct or indirect acquisition by any person or related group of persons (other than an acquisition from or by the Company or by a Company-sponsored employee benefit plan or by a person that directly or indirectly controls, is controlled by, or is under common control with, the Company) of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act of 1934) of securities possessing more than fifty percent (50%) of the total combined voting power of the Company's outstanding securities pursuant to a tender or exchange offer made directly to the Company's stockholders which a majority of the continuing directors who are not affiliates or associates of the offeror do not recommend such stockholders accept, or (ii) a change in the composition of the board over a period of twelve months or less such that one-third of the board members (rounded up to the next whole number) ceases, by reason of one or more contested elections for Board membership, to be comprised of individuals who are continuing directors.

***Amendment, Suspension or Termination of the 2012 Plan.*** The Board may at any time amend, suspend or terminate the 2012 Plan. The 2012 Plan will terminate on May 15, 2022 unless earlier terminated by the Board. To the extent necessary to comply with applicable provisions of federal securities laws, state corporate and securities laws, the Code, applicable rules of any stock exchange or national market system, and the rules of any foreign jurisdiction applicable to awards granted to residents of the jurisdiction, the Company shall obtain stockholder approval of any such amendment to the 2012 Plan in such a manner and to such a degree as required. No suspension or termination of the 2012 Plan will adversely affect any rights under awards already granted to a participant.

***Awards to Israeli Residents.*** The 2012 Plan is designed to comply with the provisions of the Israeli Income Tax Ordinance New Version, 1961, as amended (the Tax Ordinance), and is intended to enable the Administrator to grant options under the 2012 Plan to participants who are, or are deemed to be, Israeli residents. Specifically, the 2012 Plan permits option awards to employees pursuant to Section 102 of the Tax Ordinance and option awards to non-employees pursuant to Section 3(i) of the Tax Ordinance. For this purpose, employee refers to employees, officers and directors of the Company or a related entity who are not considered Controlling Shareholders pursuant to, or otherwise excluded by, the Tax Ordinance. In accordance with the terms and conditions imposed by the Tax Ordinance, participants who are, or are deemed to be, Israeli residents and who receive option awards under the 2012 Plan may be afforded certain tax benefits in Israel.

***Director Option Sub-Plan.*** In connection with the 2012 Plan, the Board adopted a Director Option Sub-Plan (the Sub-Plan). The Sub-Plan draws on the 2012 Plan for Shares and is designed to provide for the grant of options to non-employee directors of the Company on a formula basis on substantially the same terms as the Company's 1993 Director Stock Option Plan has done historically. Under the Sub-Plan, non-employee directors of the Company who join the Board will receive a first grant of an option to purchase 30,000 Shares. On January 1 of each year, non-employee directors of the Company with at least 6 months of Board service will receive a subsequent grant of an option to purchase 15,000 Shares. On January 1 of each



year, non-employee directors who are Committee chairs and have at least 6 months of service as chair will receive a committee option to purchase an additional 15,000 Shares. Options granted under the Sub-Plan generally vest as to 1/3 of the Shares on each of the first three anniversaries of the grant date, subject to Board service, and fully accelerate on a Change in Control or Corporate Transaction as defined under the 2012 Plan. The Sub-Plan permits the Administrator to make first grants, subsequent grants and committee options to non-employee directors of the Company who are Israeli residents pursuant to Sections 3(i) and 102 of the Tax Ordinance.

#### **Certain U.S. Federal Tax Consequences**

The following summary of the U.S. federal income tax consequences of the 2012 Plan transactions is based upon federal income tax laws in effect on the date of this Proxy Statement. This summary does not purport to be complete, and does not discuss state, local or non-U.S. tax consequences.

*Nonqualified Stock Options.* The grant of a nonqualified stock option under the 2012 Plan will not result in any federal income tax consequences to the participant or to the Company. Upon exercise of a nonqualified stock option, the participant is subject to income taxes at the rate applicable to ordinary compensation income on the difference between the option exercise price and the fair market value of the Shares at the time of exercise. This income is subject to withholding for federal income and employment tax purposes. The Company is entitled to an income tax deduction in the amount of the income recognized by the participant, subject to possible limitations imposed by Section 162(m) of the Code and so long as the Company withholds the appropriate taxes with respect to such income (if required) and the participant's total compensation is deemed reasonable in amount. Any gain or loss on the participant's subsequent disposition of the Shares will receive long or short-term capital gain or loss treatment, depending on whether the Shares are held for more than one year following exercise. The Company does not receive a tax deduction for any such gain.

A nonqualified stock option can be considered deferred compensation and subject to Section 409A of the Code. A nonqualified stock option that does not meet the requirements of Code Section 409A can result in the acceleration of income recognition, an additional 20% tax obligation, plus penalties and interest.

*Incentive Stock Options.* The grant of an incentive stock option under the 2012 Plan will not result in any federal income tax consequences to the participant or to the Company. A participant recognizes no federal taxable income upon exercising an incentive stock option (subject to the alternative minimum tax rules discussed below), and the Company receives no deduction at the time of exercise. In the event of a disposition of stock acquired upon exercise of an incentive stock option, the tax consequences depend upon how long the participant has held the Shares. If the participant does not dispose of the Shares within two years after the incentive stock option was granted, nor within one year after the incentive stock option was exercised, the participant will recognize a long-term capital gain (or loss) equal to the difference between the sale price of the Shares and the exercise price. The Company is not entitled to any deduction under these circumstances.

If the participant fails to satisfy either of the foregoing holding periods (referred to as a disqualifying disposition), he or she must recognize ordinary income in the year of the disposition. The amount of ordinary income generally is the lesser of (i) the difference between the amount realized on the disposition and the exercise price or (ii) the difference between the fair market value of the stock at the time of exercise and the exercise price. Any gain in excess of the amount taxed as ordinary income will be treated as a long or short-term capital gain, depending on whether the stock was held for more than one year. The Company, in the year of the disqualifying disposition, is entitled to a deduction equal to the amount of ordinary income recognized by the participant, subject to possible limitations imposed by Section 162(m) of the Code and so long as the participant's total compensation is deemed reasonable in amount.

The spread under an incentive stock option i.e., the difference between the fair market value of the Shares at exercise and the exercise price is classified as an item of adjustment in the year of exercise for purposes of the alternative minimum tax. If a participant's alternative minimum tax liability exceeds such participant's regular income tax liability, the participant will owe the larger amount of taxes. In order to avoid the application of alternative minimum tax with respect to incentive stock options, the participant must sell the Shares within the calendar year in which the incentive stock options are exercised. However, such a sale of Shares within the year of exercise will constitute a disqualifying disposition, as described above.

*Stock Appreciation Rights.* Recipients of stock appreciation rights (SARs) generally should not recognize income until the SAR is exercised (assuming there is no ceiling on the value of the right). Upon exercise, the recipient will normally recognize taxable ordinary income for federal income tax purposes equal to the amount of cash and fair market value of the shares, if any, received upon such exercise. Recipients who are employees will be subject to withholding for federal income and employment tax purposes with respect to income recognized upon exercise of a SAR. Recipients will recognize gain upon the disposition of any shares received on exercise of a SAR equal to the excess of (i) the amount realized on such disposition over (ii) the ordinary income recognized with respect to such shares under the principles set forth above. That gain will be taxable as long or short-term capital gain depending on whether the shares were held for more than one year. We will be entitled to a tax deduction to the extent and in the year that ordinary income is recognized by the recipient, subject to possible limitations imposed by Section 162(m) of the Code and so long as we withhold the appropriate taxes with respect to such income (if required) and the recipient's total compensation is deemed reasonable in amount.

A SAR can be considered non-qualified deferred compensation and subject to Section 409A of the Code. A SAR that does not meet the requirements of Code Section 409A can result in the acceleration of income recognition, an additional 20% tax obligation, plus penalties and interest.

*Restricted Stock.* The grant of restricted stock will subject the recipient to ordinary compensation income on the difference between the amount paid for such stock and the fair market value of the Shares on the date that the restrictions lapse. This income is subject to withholding for federal income and employment tax purposes. The Company is entitled to an income tax deduction in the amount of the ordinary income recognized by the recipient, subject to possible limitations imposed by Section 162(m) of the Code and so long as the Company withholds the appropriate taxes with respect to such income (if required) and the participant's total compensation is deemed reasonable in amount. Any gain or loss on the recipient's subsequent disposition of the Shares will receive long or short-term capital gain or loss treatment depending on how long the stock has been held since the restrictions lapsed. The Company does not receive a tax deduction for any such gain.

Recipients of restricted stock may make an election under Section 83(b) of the Code ( Section 83(b) Election ) to recognize as ordinary compensation income in the year that such restricted stock is granted, the amount equal to the spread between the amount paid for such stock and the fair market value on the date of the issuance of the stock. If such an election is made, the recipient recognizes no further amounts of compensation income upon the lapse of any restrictions and any gain or loss on subsequent disposition will be long or short-term capital gain to the recipient. The Section 83(b) Election must be made within thirty days from the time the restricted stock is issued.

*Restricted Stock Units.* Recipients of restricted stock units generally should not recognize income until such units are converted into cash or Shares. Upon conversion, the recipient will normally recognize taxable ordinary income for federal income tax purposes equal to the amount of cash and fair market value of the Shares, if any, received upon such conversion. Recipients who are employees will be subject to withholding for federal income and employment tax purposes with respect to income recognized upon conversion of the restricted stock units. Participants will recognize gain upon the disposition of any Shares received upon conversion of the restricted stock units equal to the excess of (i) the amount realized on such disposition over (ii) the ordinary income recognized with respect to such Shares under the principles set forth above. That gain will be taxable as long or short-term capital gain depending on whether the Shares were held for more than one year. The Company will be entitled to a tax deduction to the extent and in the year that ordinary income is recognized by the recipient, subject to possible limitations imposed by Section 162(m) of the Code and so long as the Company withholds the appropriate taxes with respect to such income (if required) and the recipient's total compensation is deemed reasonable in amount.

Restricted stock units also can be considered non-qualified deferred compensation and subject to Section 409A of the Code. A grant of restricted stock units that does not meet the requirements of Code Section 409A will result in an additional 20% tax obligation, plus penalties and interest to such recipient.

*Dividends and Dividend Equivalents.* Recipients of stock-based awards that earn dividends or dividend equivalents will recognize taxable ordinary income on any dividend payments received with respect to unvested and/or unexercised shares subject to such awards, which income is subject to withholding for federal income and employment tax purposes. We are entitled to an income tax deduction in the amount of the income recognized by a participant, subject to possible limitations imposed by Section 162(m) of the Code and so long as we withhold the appropriate taxes with respect to such income (if required) and the individual's total compensation is deemed reasonable in amount.

**2012 Plan Benefits**

The executive group in 2012 consisted of Messrs. Elyakim, Levy and Dahan (as of February 1, 2012). The non-executive director group in 2012 consisted of Messrs. Ayalon, Limon, Reuven, Seroussi, Shamir, Silver (until May 2012) and Tanguy, as well as Messrs. Lacey and Traub as of May 15, 2012. There were no equity awards granted in 2012 pursuant to the 2012 Plan.

**Required Vote**

The affirmative vote of the holders of a majority of the shares of our common stock present or represented at the annual meeting is required to approve the amendment and restatement of the 2012 Plan. Abstentions will have the same effect as no votes on this proposal, whereas broker non-votes will have no effect.

**OUR BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE APPROVAL OF  
THE PROPOSED AMENDMENT AND RESTATEMENT OF THE 2012 EQUITY INCENTIVE  
PLAN.**

**PROPOSAL NO. 4**

**RATIFICATION OF SELECTION OF INDEPENDENT AUDITORS**

Our audit committee has selected Kost Forer Gabbay & Kasierer (a member of Ernst & Young Global) as our auditors for the current fiscal year, subject to ratification by our stockholders at the annual meeting. We expect a representative of Kost Forer Gabbay & Kasierer (a member of Ernst & Young Global) to be available via teleconference to respond to appropriate questions and to make a statement if he or she so desires, but no representative will be present at the annual meeting.

Neither our bylaws nor other governing documents or law require stockholder ratification of the selection of Kost Forer Gabbay & Kasierer (a member of Ernst & Young Global) as our independent accountants. However, the audit committee of the board of directors is submitting the selection of Kost Forer Gabbay & Kasierer (a member of Ernst & Young Global) to the stockholders for ratification as a matter of good corporate practice. If the stockholders fail to ratify the selection, the audit committee will reconsider whether or not to retain that firm. Even if the selection is ratified, the audit committee in its discretion may direct the appointment of different independent accountants at any time during the year if they determine that such a change would be in our best interests and the best interests of our stockholders.

In connection with the audit of the 2012 financial statements, we entered into an engagement agreement with Kost Forer Gabbay & Kasierer which set forth the terms by which Kost Forer Gabbay & Kasierer will perform audit services for us. That agreement is subject to alternative dispute resolution procedures and an exclusion of punitive damages.

**Required Vote**

The affirmative vote of the holders of a majority of the shares of our common stock present or represented at the annual meeting is required to approve the ratification of the selection of Kost Forer Gabbay & Kasierer as our independent auditors for fiscal year 2013. Abstentions will have the same effect as no votes on this proposal, whereas broker non-votes will have no effect.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE RATIFICATION**

**OF**

**THE SELECTION OF KOST FORER GABBAY & KASIERER.**

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**Report of the Audit Committee of the Board of Directors**

*Notwithstanding anything to the contrary set forth in any of the Company's previous filings under the Securities Act of 1933, as amended (the Securities Act) or the Exchange Act of 1934, that might incorporate future filings, including this proxy statement, with the Securities and Exchange Commission, in whole or in part, the following report shall not be deemed to be incorporated by reference into any such filings, nor shall the following report be deemed to be incorporated by reference into any future filings under the Securities Act or the Exchange Act.*

The audit committee is directly responsible for the appointment, compensation, retention and oversight of the Company's independent auditors. Additionally, the audit committee must approve all audit and non-audit services performed by the Company's independent auditors. Furthermore, the audit committee is responsible for reviewing and evaluating the Company's accounting principles and the Company's system of internal accounting controls. Management is responsible for the financial reporting process, including the system of internal controls and for the preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States. The Company's independent auditors, Kost Forer Gabbay & Kasierer, a member of Ernst & Young Global, are responsible for auditing those financial statements. However, the members of the audit committee are not professionally engaged in the practice of accounting or auditing and are not experts in the fields of accounting or auditing. The audit committee relies, without independent verification, on the information provided to the committee and on the representations made by management and the independent auditors.

The audit committee hereby reports as follows:

1. The audit committee has reviewed and discussed the audited financial statements with the Company's management and Kost Forer Gabbay & Kasierer, the Company's independent auditors.
2. The audit committee has discussed with Kost Forer Gabbay & Kasierer (a) their judgments as to the quality of the Company's accounting policies, and (b) the matters required to be discussed with the committee under auditing standards generally accepted in the United States, including Statement on Auditing Standards No. 61, as amended (AICPA, Professional Standards, Vol. 1. AU section 380), as adopted by the Public Company Accounting Oversight Board in Rule 3200T.
3. The audit committee met with management periodically during the year to consider the adequacy of the Company's internal controls and the quality of its financial reporting and discussed these matters with the Company's independent auditors and with appropriate Company financial personnel and internal auditors.
4. The audit committee discussed with the Company's senior management, Kost Forer Gabbay & Kasierer and internal auditors the process used for the Company's Chief Executive Officer and Chief Financial Officer to make the certifications required by the Securities and Exchange Commission and the Sarbanes-Oxley Act of 2002 in connection with the Annual Report on Form 10-K and other periodic filings with the Commission.

5. The audit committee has received the written disclosures and the letter from Kost Forer Gabbay & Kasierer required by the Public Company Accounting Oversight Board regarding its communications with the audit committee concerning independence. The audit committee considered whether the audit and non-audit services provided by Kost Forer Gabbay & Kasierer were compatible with maintaining its independence from the Company. Based on discussions with Kost Forer Gabbay & Kasierer, the audit committee determined that the audit and non-audit services provided to the Company by Kost Forer Gabbay & Kasierer were compatible with maintaining the independence of Kost Forer Gabbay & Kasierer.
  
6. Based on the reviews and discussions referred to in paragraphs (1) through (5) above, the audit committee recommended to the Company's board of directors, and the board approved, the audited financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, that was filed with the Securities and Exchange Commission on March 18, 2013.
  
7. The audit committee has also recommended the selection of Kost Forer Gabbay & Kasierer and, based on the committee's recommendation, the board of directors has selected Kost Forer Gabbay & Kasierer as the Company's independent auditors for the fiscal year ending December 31, 2013. The board of directors is submitting the selection of Kost Forer Gabbay & Kasierer to the stockholders for ratification.

Submitted by the audit committee:

Zvi Limon  
Yair Seroussi  
Yair Shamir  
Patrick Tanguy

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**PRINCIPAL ACCOUNTANT FEES AND SERVICES**
**Audit Fees**

Kost Forer Gabbay & Kasierer performed services for us in fiscal 2012 and 2011 related to financial statement audit work, quarterly reviews, Forms S-8 reviews, tax services, special projects and other ongoing consulting projects. Fees paid or accrued to Kost Forer Gabbay & Kasierer in fiscal 2012 and 2011 were as follows:

	2012	2011
Audit Fees (1)	\$ 360,000	\$ 380,000
Audit-Related Fees (2)		
Tax Fees (3)	\$ 162,930	\$ 74,000
All Other Fees (4)	\$ 51,842	
<b>Total</b>	<b>\$ 574,772</b>	<b>\$ 454,000</b>

- (1) Audit fees represent fees for the audit of consolidated financial statements for the fiscal years ended December 31, 2012 and 2011 and the review of financial statements included in our quarterly reports on Form 10-Q.
- (2) Audit-related fees represent fees for accounting professional services on actual or contemplated transactions.
- (3) Tax fees represent fees for professional services rendered by our auditors for tax compliance, tax planning and tax advice on actual or contemplated transactions and advisory services for other tax compliance matters.
- (4) All other fees include fees for professional services rendered by our auditors for national insurance audit in Israel and participation in various grant projects from the Office of Chief Scientist in Israel.

The audit committee approved 100% of the above set forth fees in 2012 and 2011.

**Audit and Non-Audit Services Pre-Approval Policy**

Under the Sarbanes-Oxley Act of 2002, all audit and non-audit services performed by Kost Forer Gabbay & Kasierer, our independent auditors, must be approved in advance by the audit committee to assure that such services do not impair the auditors' independence from the company. In January 2004, the audit committee adopted an audit and non-audit services pre-approval policy which sets forth the procedures and conditions pursuant to which audit and non-audit services to be performed by the independent auditors are to be pre-approved. Pursuant to the policy, certain services or category of services described in detail in the policy may be pre-approved generally on an annual basis together with pre-approved maximum fee levels for such services. The services eligible for annual pre-approval consist of audit services, audit-related services, tax services and other services. If not pre-approved on an annual basis, proposed services must otherwise be separately approved prior to being performed by the independent



auditors. The audit committee may also pre-approve particular services on a case-by-case basis. In addition, any services that receive annual pre-approval but exceed the pre-approved maximum fee level also will require separate approval by the audit committee prior to being performed. The audit committee may delegate authority to pre-approve audit and non-audit services to any member of the audit committee, but may not delegate such authority to management. Our independent auditors and Chief Financial Officer are required to periodically report to the audit committee regarding the extent of services provided by the independent auditors in accordance with the pre-approval policy and the fees for the services performed to date.

**PROPOSAL NO. 5**

**ADVISORY VOTE ON COMPENSATION OF THE NAMED EXECUTIVE OFFICERS**

At last year's annual meeting, we provided our stockholders with the opportunity to cast an advisory vote regarding the compensation of our named executive officers as disclosed in our proxy statement for the 2012 annual meeting of stockholders. At our 2012 annual meeting, our stockholders overwhelmingly approved the proposal, with approximately 80% of the votes cast voting in favor of the proposal. After consideration of the 2011 voting results, our board of directors elected to hold a stockholder say-on-pay vote annually. Accordingly, this year we are again asking our stockholders to vote For the compensation of our executive officers as disclosed in this proxy statement. Our board of directors and our compensation committee value the opinions of our stockholders. We will consider our stockholders' concerns and our compensation committee will evaluate whether any actions are necessary to address those concerns. In addition to our annual advisory vote on executive compensation, we are committed to ongoing engagement with our stockholders on executive compensation and corporate governance issues.

As described in detail under the heading *Compensation Discussion and Analysis*, our compensation philosophy supports our key business objectives of creating value for, and promoting the interests of, our stockholders. In order to align the interests of our executives with those of our stockholders, we believe that our executive compensation arrangements must provide our named executive officers with competitive compensation opportunities, based upon both their contribution to the development and financial success of the company and their personal performance. We believe our executive compensation arrangements strikes the appropriate balance between utilizing responsible, measured pay practices and effectively incentivizing our executives to dedicate themselves fully to value creation for our stockholders. This balance is evidenced by the following:

Our compensation arrangements for the named executive officers are simple, consisting principally of base salary, annual bonus, which may or may not be awarded annually at the discretion of the compensation committee prior to 2011 and based on a performance-based bonus plan starting in 2011, and long-term incentive award, in the form of stock options, stock appreciation rights or restricted stock units, which again may or may not be awarded annually at the discretion of the compensation committee.

We provide a significant part of executive compensation in the form of performance based incentives. Starting in 2011, our board established a performance-based bonus plan whereby bonuses are awarded under the plan based on achievement of the company's financial goals based on an annual budget approved by our board. The financial goals under the performance-based bonus plans are generally challenging. Bonuses under the performance-based plan are capped and a significant portion of the bonuses would not be payable for a particular year if the company fails to achieve such financial goals. No bonuses were paid to our executive officers under the 2011 and 2012 performance-based bonus plans as a result of failure to meet the financial goals under the respective plans.

A significant portion of our named executive officer's compensation is in the form of long-term incentive awards, currently consisting of stock options, stock appreciation rights and restricted stock units. Such equity awards vest 25% on the first anniversary of the grant date and the remaining equity awards vest quarterly over the following three years.

We align base salaries with strong pay-for-performance orientation and our compensation committee generally takes a conservative approach on base salary increases. For example, the base salaries of our named executive officers were reduced in 2009 by ten percent from their respective 2008 amounts in consideration of deteriorating market conditions, our financial performance and the company's desire to reduce operating expenses. The base salaries were restored to their respective 2008 amounts in 2010 for all our named executive officers. Our named executive officers did not receive any increases to their base salary in 2011 or 2012. Only in 2013 did our Chief Executive Officer and Chief Financial Officer receive a small increase of approximately 9% in their respective base salaries.

We do not provide any nonqualified defined contribution or other deferred compensation plans to our named executive officers.

We do not provide tax gross-ups to our named executive officers.

None of the employment agreements with our named executive officers includes any single trigger change-in-control provisions or golden parachute arrangements.

The perquisites offered to our named executive officers based in Israel are those generally provided to all of our employees based in Israel.

The compensation committee is updated on compensation best practices and trends. The committee from time to time as appropriate engages the services of a compensation consultant to provide advice on compensation trends and market information to assist the committee in designing our compensation programs and making compensation decisions.

The vote on this resolution is not intended to address any specific element of compensation; rather, the advisory vote relates to the compensation of our named executive officers, as described in this proxy statement. The vote is advisory, and therefore it is not binding on the company, the compensation committee or our board of directors. The compensation committee will carefully consider the outcome of the vote when considering future executive compensation arrangements.

#### **Required Vote**

The affirmative vote of a majority of the shares present or represented and entitled to vote either in person or by proxy is required to approve this Proposal 5. Abstentions will have the same effect as no votes on this proposal, whereas broker non-votes will have no effect.

Accordingly, we ask our stockholders to vote on the following resolution at the annual meeting:

RESOLVED, that the compensation of the named executive officers, as disclosed in the Company's proxy statement for the 2013 Annual Meeting of Stockholders pursuant to the compensation disclosure rules of the Securities and Exchange Commission, including Compensation Discussion and Analysis, compensation tables and narrative discussion, is hereby APPROVED.

**THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS A VOTE FOR THE  
APPROVAL OF THE COMPENSATION OF OUR NAMED EXECUTIVE OFFICERS,  
AS DISCLOSED IN THIS PROXY STATEMENT.**

**PROPOSAL NO. 6**

**ADJOURNMENT OR POSTPONEMENT OF THE ANNUAL MEETING**

We are asking our stockholders to vote on a proposal to adjourn or postpone the annual meeting, if necessary, to permit further solicitation of proxies in the event there are insufficient votes at the time of the annual meeting to adopt and approve proposals 1 through 5 set forth in this proxy statement. We currently do not intend to adjourn or postpone our annual meeting if there are sufficient votes to adopt and approve proposals 1 through 5.

**Required Vote**

The affirmative vote of the holders of a majority of the shares of our common stock present or represented at the annual meeting is required to approve the proposal to adjourn or postpone the annual meeting, if necessary. Abstentions will have the same effect as no votes on this proposal, whereas broker non-votes will have no effect.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE APPROVAL OF  
THE PROPOSAL TO ADJOURN OR POSTPONE THE ANNUAL MEETING, IF  
NECESSARY**

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## STOCKHOLDER PROPOSALS

*Requirements for Stockholder Proposals to Be Brought Before an Annual Meeting and Considered for Inclusion in our Proxy Materials.* In addition to submitting information related to the proposal as described elsewhere in this proxy statement, pursuant to Rule 14a-8 under the Exchange Act and the Company's bylaws, stockholder proposals intended for consideration by the Company for presentation and inclusion in its proxy materials for the annual meeting of stockholders to be held in 2014 must be received by Dror Levy, Secretary, DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131, no later than [ ], 2014 in order to be considered for inclusion in our proxy materials for that meeting.

*Discretionary Authority.* The proxies to be solicited by our board of directors for the 2014 annual meeting will confer discretionary authority on the proxy holders to vote on any stockholder proposal presented at such annual meeting if we fail to receive notice of such stockholder's proposal for the meeting by [ ], 2014.

## OTHER MATTERS

### Annual Report

Our annual report for the fiscal year ended December 31, 2012 has been mailed concurrently with the mailing of these proxy materials to all stockholders entitled to notice of, and to vote at, the annual meeting.

### Form 10-K

Our annual report on Form 10-K for the fiscal year ended December 31, 2012 is included in the annual report for the fiscal year ended December 31, 2012, which is mailed concurrently with the mailing of these proxy materials. Upon written request to our Secretary, Dror Levy, at the address of our principal executive offices, the exhibits set forth on the exhibit index of the Form 10-K may be made available at a reasonable charge.

### Internet Availability of Proxy Materials

In addition to the mailing, the notice of the annual meeting, this proxy statement and the **GOLD** proxy card are available for your review, print and download on our website at [www.dspg.com](http://www.dspg.com). **Our website and the information contained therein or connected thereto are not intended to be incorporated into this proxy statement.**

### Householding of Annual Meeting Materials

In December 2000, the Securities and Exchange Commission adopted new rules that permit us to send a single set of annual reports and proxy statements to any household at which two or more stockholders reside if we believe they are members of the same family. Each stockholder will continue to receive a separate proxy card. Upon written request to our Secretary, Dror Levy, at the address of our principal executive offices or by phone at (408) 986-4300, you may revoke your decision to household, and we will deliver a separate copy of the annual report or proxy statement, as applicable, to you at the shared address within 30 days of your request.

A number of brokerage firms have already instituted householding. If your family has multiple accounts of our stock, you may have received householding notification from your broker. Please contact your broker directly if you have questions, require additional copies of the proxy statement or annual report, or wish to revoke your decision to household, and thereby receive multiple reports.

**Other Matters**

Our board of directors knows of no other business which will be presented at the annual meeting. If any other business is properly brought before the annual meeting, it is intended that **GOLD** proxies in the enclosed form will be voted in respect thereof in accordance with the judgments of the proxy holders.

It is important that the proxies be returned promptly and that your shares are represented. Stockholders are urged to mark, date, execute and promptly return the accompanying **GOLD** proxy card in the enclosed envelope.

By Order of the Board of Directors,

/s/ Ofer Elyakim

Ofer Elyakim  
*Chief Executive Officer*

[ ], 2013

San Jose, California

**INFORMATION CONCERNING PARTICIPANTS IN**

**THE COMPANY'S SOLICITATION OF PROXIES**

The following tables ( Directors and Nominees and Officers and Employees ) set forth the name, principal business address and the present principal occupation or employment, and the name, principal business and address of any corporation or other organization in which their employment is carried on, of our directors, nominees, officers and employees who, under the rules of the Securities and Exchange Commission, are considered to be participants in our solicitation of proxies from our stockholders in connection with our 2013 annual meeting of stockholders.

**Directors and Nominees**

The principal occupations of our directors and nominees who are considered participants in our solicitation are set forth under the section titled Proposal No. 1: Election of Directors of this proxy statement. The name and business addresses of the organization of employment of our directors and nominees are as follows:

<b>Name</b>	<b>Business Address</b>	<b>Address of Organization of Principal Occupation or Employment</b>
Eliyahu Ayalon	c/o DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131	E.E. Ayalon Assets Ltd. 9 Kerem Hazeitim St. Savion, Israel 56536
Ofer Elyakim	c/o DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131	DSP Group, Inc. 2580 North First Street, Suite 460 San Jose, CA 95131
Zvi Limon	c/o DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131	Magma Venture Fund 1 Azrieli Center The Round Tower, 35 <sup>th</sup> floor Tel-Aviv 67021
Reuven Regev	c/o DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131	Topscan Ltd. 5 Etgar Street Tirat Hacarmel, Israel 39103
Yair Seroussi	c/o DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131	Bank Hapoalim 63 Yehuda Halevi Street Tel Aviv, Israel 61000
Patrick Tanguy	c/o DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131	Wendel Group 89 Rue Taitbout





**Officers and Employees**

The principal occupations of our executive officers and employees who are considered participants in our solicitation of proxies are set forth below. The principal occupation refers to such person's position with the Company or one of its subsidiaries, and the business address for each person is DSP Group, Inc., DSP Group, Inc., 2580 North First Street, Suite 460, San Jose, CA 95131.

<b>Name</b>	<b>Occupation</b>
Ofer Elyakim	Chief Executive Officer
Dror Levy	Chief Financial Officer and Secretary
Christopher Basta	Director of Investor Relations

**Information Regarding Ownership of DSP Group, Inc. Securities by Participants**

The number of shares of our common stock held by our directors and named executive officers as of April 1, 2013 is set forth under the SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT section of the proxy statement. As of April 1, 2013, Mr. Basta owned 2000 shares of our common stock, 100 call options for our common stock and 10,000 restricted stock units granted pursuant to our 2012 Equity Incentive Plan.

**Information Regarding Transactions in DSP Group, Inc. Securities by Participants**

The following table sets forth information regarding purchases and sales of our securities by each of the participants listed above under Directors and Nominees and Officers and Employees during the past two years. Unless otherwise indicated, all transactions were in the public market or pursuant to our equity compensation plans and none of the purchase price or market value of those securities is represented by funds borrowed or otherwise obtained for the purpose of acquiring or holding such securities.

<b>Name</b>	<b>Shares of Common Stock Purchased or Sold</b>		
	<b>Date</b>	<b>(January 1, 2011</b>	<b>April 1, 2013)</b>
	<b># of Shares</b>	<b>Transaction Description</b>	
Eliyahu Ayalon	1/2/11	1,181	(1)
	1/31/11	70,000	(5)
	1/1/12	15,000	(7)
	1/1/13	15,000	(7)
Ofer Elyakim	1/2/11	1,800	(1)
	31/1/11	70,000	(5)
	7/1/11	2,767	(1)
	1/2/12	1,854	(1)
	2/1/12	52,500	(5)
	5/17/12	1,000	(2)
	7/1/12	2,935	(1)
	8/3/12	1,000	(2)
	1/2/13	1,867	(1)
	1/29/13	66,000	(6)

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Zvi Limon	1/1/11	30,000	(7)
	1/1/12	30,000	(7)
	1/1/13	30,000	(7)
Reuven Regev	1/1/12	15,000	(7)
	1/1/13	15,000	(7)
Yair Seroussi	1/1/11	15,000	(7)
	1/1/12	15,000	(7)
	1/1/13	15,000	(7)
Yair Shamir	1/1/11	30,000	(7)
	1/1/12	30,000	(7)
	1/1/13	30,000	(7)
Patrick Tanguy	1/1/11	15,000	(7)
	1/1/12	15,000	(7)
	1/1/13	15,000	(7)

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Dror Levy	1/2/10	2,071	(4)
	1/31/11	30,000	(5)
	7/1/11	2,176	(4)
	1/2/12	2,228	(4)
	2/1/12	25,000	(5)
	1/29/13	25,000	(6)
Christopher Basta	2/3/12	100	(8)
	2/9/12	50	(8)
	2/13/12	16,500	(2)
	2/16/12	5,000	(2)
	3/12/12	8,500	(2)
	3/23/12	5,000	(3)
	7/20/12	5,000	(3)
	8/16/12	150	(9)
	8/28/12	5,000	(3)
	10/9/12	3,000	(2)
	10/10/12	2,000	(3)
	10/12/12	6,000	(3)
	11/13/12	1,000	(3)
	11/13/12	50	(8)
	11/14/12	50	(8)
11/14/12	4,000	(3)	
11/16/12	5,000	(3)	
1/29/13	10,000	(6)	
2/01/13	2,000	(2)	

- (1) Purchase of common stock through the DSP Group, Inc. Employee Stock Purchase Plan.
- (2) Open market purchase of common stock.
- (3) Open market sale of common stock.
- (4) Cashless purchase and open market sale of common stock through the DSP Group, Inc. Employee Stock Purchase Plan
- (5) Grant of stock appreciation rights pursuant to the DSP Group, Inc. 2003 Israeli Share Incentive Plan.
- (6) Grant of restricted stock units pursuant to the DSP Group, Inc. 2012 Stock Incentive Plan.
- (7) Grant of stock options pursuant to the DSP Group, Inc. 1993 Director Stock Option Plan.
- (8) Open market purchase of call option.
- (9) Open market sale of call option.

**Miscellaneous Information Concerning Participants**

Other than as set forth in this Appendix A or the proxy statement, none of the participants or their associates (i) beneficially owns (within the meaning of Rule 13d-3 under the Exchange Act), directly or indirectly, any shares or other securities of the company or any of our

subsidiaries or (ii) has any substantial interest, direct or indirect, by security holdings or otherwise, in any matter to be acted upon at the annual meeting. In addition, except as set forth in this Appendix A or the proxy statement, neither we nor any of the participants listed above has been within the past year a party to any contract, arrangement or understanding with any person with respect to any of our securities, including, but not limited to, joint ventures, loan or option arrangements, puts or calls, guarantees against loss or guarantees of profit, division of losses or profits or the giving or withholding of proxies.

Other than as set forth in this Appendix A or the proxy statement, none of the participants listed above or any of their associates have (i) other than the employment agreements described in the Employment Agreements section of the proxy statement, any arrangements or understandings with any person with respect to any future employment by the company or our affiliates or with respect to any future transactions to which we or any of our affiliates will or may be a party or (ii) a direct or indirect material interest in any transaction or series of similar transactions since the beginning of our last fiscal year or any currently proposed transactions, or series of similar transactions, to which we or any of our subsidiaries was or is to be a party in which the amount involved exceeds \$120,000.

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**THIS PROXY IS SOLICITED ON BEHALF OF**  
**THE BOARD OF DIRECTORS OF DSP GROUP, INC.**  
**FOR THE 2013 ANNUAL MEETING OF STOCKHOLDERS**

The undersigned stockholder of DSP GROUP, INC., a Delaware corporation (the "Company"), hereby acknowledges receipt of the Notice of Annual Meeting of Stockholders and Proxy Statement, each dated [ ], 2013, the Company's Annual Report for the year ended December 31, 2012 and the Company's Annual Report on Form 10-K for the year ended December 31, 2012 and hereby appoints Ofer Elyakim and Dror Levy, or either of them, proxies, with full power to each of substitution, on behalf and in the name of the undersigned, to represent the undersigned at the 2013 Annual Meeting of Stockholders of the Company to be held on Monday, June 10, 2013, at 10:00 a.m., local time, at the Le Parker Meridien, New York 119 W 56th St., New York City, New York, and at any postponement or adjournment thereof, and to vote all shares of common stock of the Company which the undersigned would be entitled to vote if then and there personally present, on the matters set forth below.

**THIS PROXY WILL BE VOTED AS DIRECTED OR, IF NO CONTRARY DIRECTION IS INDICATED, WILL BE VOTED (1) FOR THE ELECTION OF THE CLASS I DIRECTOR NOMINEES, (2) FOR PROPOSALS 2, 3, 4, 5 AND 6, AND (3) AS SAID PROXIES DEEM ADVISABLE ON SUCH OTHER MATTERS AS MAY PROPERLY COME BEFORE THE MEETING.**

1. ELECTION OF THREE CLASS I DIRECTORS:

\_\_\_\_\_ FOR the nominees listed below

\_\_\_\_\_ WITHHOLD AUTHORITY to

(except as indicated)

vote for the nominees listed below

**If you wish to withhold authority to vote for the following nominees, strike a line through such nominee's name listed below.**

Eliyahu Ayalon as Class I Director

Zvi Limon as Class I Director

Reuven Regev as Class I Director

2. PROPOSAL TO INCREASE THE NUMBER OF SHARES AUTHORIZED UNDER THE AMENDED AND RESTATED 1993 EMPLOYEE PURCHASE PLAN BY 500,000 SHARES:

\_\_\_\_\_ FOR \_\_\_\_\_ AGAINST \_\_\_\_\_ ABSTAIN  
3. PROPOSAL TO INCREASE THE NUMBER OF SHARES AUTHORIZED UNDER THE AMENDED AND RESTATED 2012 EQUITY INCENTIVE PLAN BY 1,100,000 SHARES:

\_\_\_\_\_ FOR \_\_\_\_\_ AGAINST \_\_\_\_\_ ABSTAIN  
4. PROPOSAL TO RATIFY THE SELECTION OF KOST FORER GABBAY & KASIERER AS THE COMPANY'S INDEPENDENT AUDITORS FOR FISCAL 2013:

\_\_\_\_\_ FOR \_\_\_\_\_ AGAINST \_\_\_\_\_ ABSTAIN  
5. ADVISORY VOTE TO APPROVE THE COMPANY'S NAMED EXECUTIVE OFFICER COMPENSATION:

\_\_\_\_\_ FOR \_\_\_\_\_ AGAINST \_\_\_\_\_ ABSTAIN  
6. PROPOSAL TO ADJOURN OR POSTPONE ANNUAL MEETING, AS NECESSARY:

\_\_\_\_\_ FOR \_\_\_\_\_ AGAINST \_\_\_\_\_ ABSTAIN

The undersigned acknowledges receipt of the accompanying Notice of Annual Meeting of Stockholders and Proxy Statement.

DATED: [ ], 2013

(Signature)

(Signature)

This Proxy should be marked, dated and signed by the stockholder(s) exactly as his or her name appears hereon, and returned promptly in the enclosed envelope. Persons signing in a fiduciary capacity should so indicate. If shares are held by joint tenants or as community property, both should sign.