

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 20-F

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

OR

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

For the fiscal year ended December 31, 2003

OR

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

For the transition period from _____ to _____

Commission file number 0-28724

ORCKIT COMMUNICATIONS LTD.

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

ISRAEL

(Jurisdiction of incorporation or organization)

126 Yigal Allon Street, Tel Aviv 67443, Israel

(Address of principal executive offices)

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

Title of each class

Name of each exchange on which registered

None

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

Ordinary Shares, no par value

(Title of Class)

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

None

(Title of Class)

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

As of December 31, 2003, the Registrant had outstanding 4,334,980 Ordinary Shares, no par value.

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

Yes ☒ No ☐

Indicate by check mark which financial statement item the Registrant has elected to follow.

Item 17 ☐ Item 18 ☒

PART I

Unless the context otherwise requires, “Orckit,” “us,” “we” and “our” refer to Orckit Communications Ltd. and its subsidiaries.

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISORS

Not applicable

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable

ITEM 3. KEY INFORMATION

A. SELECTED FINANCIAL DATA

The following selected consolidated financial data as of December 31, 2002 and 2003 and each of the years ended December 31, 2001, 2002 and 2003 are derived from our audited consolidated financial statements set forth elsewhere in this Annual Report, which have been prepared in accordance with generally accepted accounting principles in the United States. The selected consolidated financial data for the years ended December 31, 1999 and 2000 and as of December 31, 1999, 2000 and 2001 are derived from audited consolidated financial statements not appearing in this Annual Report. The selected consolidated financial data set forth below should be read in conjunction with “Item 5. Operating and Financial Review and Prospects” and the consolidated financial statements and the notes thereto and the other financial information appearing elsewhere in this Annual Report.

On June 30, 2000, our business was formally divided into two separate companies: (i) Tikcro Technologies Ltd. (formerly named Tioga Technologies Ltd.), an Israeli company, to which we transferred substantially all of our former semiconductor business, including the business of Silicon Value Ltd., and (ii) Orckit, which continues to own and operate our existing telecom equipment and other businesses. As part of the spin-off, we transferred to Tikcro substantially all the assets and liabilities constituting our semiconductor business in exchange for Tikcro ordinary shares, and distributed all of those Tikcro shares as a stock dividend to our shareholders on a share for share basis. The results of Tikcro are included in our financial statements through June 30, 2000.

All share and share price information in this Annual Report has been adjusted to give retroactive effect to (i) an adjustment allocating 44% of our share price to each share of Orckit and 56% of our share price to each share of Tikcro for all periods prior to our spin-off of Tikcro on June 30, 2000 and (ii) a one-for-five reverse split of our ordinary shares that became effective as of November 27, 2002.

	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>
<u>Statement of Operations</u>	(in thousands, except per share data)				
<u>Data:</u>					
Revenues	\$88,864	\$131,867	\$141,647	\$53,420	\$1,683
Cost of revenues	<u>84,502</u>	<u>133,671</u>	<u>112,007</u>	<u>32,963</u>	<u>748</u>
Gross profit (loss)	4,362	(1,804)	29,640	20,457	935
Research and development	18,195	31,970	22,429	22,266	20,803

expenses					
Less grants	2,409	1,110	3,344	2,975	5,800
Research and development expenses, net	15,786	30,860	19,085	19,291	15,003
Selling, general and administrative expenses	16,151	33,561	16,993	14,699	12,656
Acquisition of research and development In-process	-	28,976	-	-	-
Amortization and impairment of goodwill	-	14,334	26,101	-	-
Operating loss	(27,575)	(109,535)	(32,539)	(13,533)	(26,724)
Financial income, net	2,653	1,975	33,395	17,616	5,108
Other income	<u>=</u>	<u>906</u>	<u>=</u>	<u>=</u>	<u>=</u>
Net income (loss)	\$(24,922)	\$(106,654)	\$856	\$4,083	\$(21,616)
Net income (loss) per share – basic	\$(6.80)	\$(24.6)	\$0.18	\$0.83	\$(4.99)
Net income (loss) per share – diluted	\$(6.80)	\$(24.6)	\$0.18	\$0.79	\$(4.99)
Weighted average number of ordinary shares outstanding-basic	3,668	4,332	4,632	4,932	4,332
Weighted average number of ordinary shares outstanding-diluted	3,668	4,332	4,875	5,163	4,332

	Year Ended December 31,				
	<u>1999</u>	<u>2000</u>	<u>2001</u> (in thousands)	<u>2002</u>	<u>2003</u>
Balance Sheet Data:					
Cash, cash equivalents, bank deposits, marketable securities and long-term investments	\$51,049	\$101,191	\$112,924	\$116,677	\$79,041
Working capital (1)	85,399	133,086	103,895	55,193	34,480
Total assets	127,169	243,823	166,300	135,850	86,331
Convertible Subordinated Notes	-	120,000	66,416	38,179	16,238
Share capital and additional paid-in capital	138,023	313,984	318,651	320,204	317,071
Shareholders' equity	\$91,547	\$71,262	\$76,785	\$82,421	\$57,672

(1) Total current assets net of total current liabilities

B. CAPITALIZATION AND INDEBTEDNESS

Not applicable

C. REASONS FOR THE OFFER AND USE OF PROCEEDS

Not applicable

D. RISK FACTORS

We believe that the occurrence of any one or some combination of the following factors could have a material adverse effect on our business, financial condition and results of operations.

Risks relating to our business and industry

We have a history of substantial losses and might not become profitable on an operating basis.

Through December 31, 2003, we had incurred aggregate net losses of approximately \$259 million. Losses included a charge of approximately \$90 million in 2000 as a result of the spin-off of Tikcro and aggregate charges of \$69 million in 2000 and 2001 for the amortization and impairment of goodwill and in process research and development with respect to companies we acquired. Our operating losses were offset by an aggregate of approximately \$56 million of financial income we recognized during the past three years, primarily from the early retirement of our convertible subordinated notes. We incurred a significant portion of our operating losses during the period through 2002 when our primary business was the sale of asymmetric digital subscriber line, or ADSL, products. We no longer sell these products. Since 2001 we have invested significant funds in technology projects, mainly for new telecom equipment products addressing high transmission of data

for the metropolitan and access areas, through our majority-owned Corrigent and Spediant subsidiaries. As of December 31, 2003, we have not generated any revenues from the sale of products being developed by these subsidiaries. We may not be able to achieve profitability. Even if we achieve profitability, we may not be able to sustain it.

We may not be able to generate revenues from new products.

Our revenues have declined significantly from \$141.6 million in 2001 to \$53.4 million in 2002 and \$1.7 million in 2003 due to the winding down of our legacy ADSL business. We do not expect to generate additional revenues from our legacy ADSL products. In addition, our new Corrigent and Spediant products are not expected to generate significant revenues in 2004. Unless we are able to develop and sell new and innovative products that are accepted in the marketplace, it will be difficult for us to generate significant revenues. We cannot be sure that we will be able to do this.

The slow down in capital expenditures by telecommunications service providers has had and could continue to have a material adverse effect on our results of operations.

The global deterioration of the economy and economic uncertainty in the telecommunications market resulted in a curtailment of capital investment by telecommunications carriers and service providers beginning late in 2000 and continuing throughout 2002 and into 2003. There is still uncertainty with respect to the direction of the economy and the telecommunications market. Many service providers have failed and existing service providers have been reducing or delaying expenditures on new equipment and applications. It is expected that capital investment by wireline telecom carriers in 2004 will be similar to the levels in 2003. A flat capital investment environment is likely to have negative effect on the demand for new technologies and new types of equipment. This could have an adverse affect on us as we attempt to sell the products being developed by Corrigent and Spediant and, as a result, negatively affect our operating results.

We plan to continue to invest substantial capital and other resources in the development and commercial launch of new telecom equipment.

We continue to fund Corrigent in the development of solutions capable of supporting high bandwidth services in telecommunications networks located in metropolitan areas, as well as Spediant in the development of solutions addressing the needs of service providers for fiber-speed broadband services over copper wires. Substantially all of our operating expenses in 2003 related to these efforts. We expect to have a negative cash flow from operations for at least 2004 and 2005. The curtailment of capital investment by telecommunications carriers and service providers could have a material adverse effect on the commercial deployment of these technology projects. Our financing of these projects is expected to continue to reduce our cash balances.

We may need additional financing to continue our growth.

To the extent that we cannot fund our activities through our existing resources, we may need to raise funds through public or private financing. We may be unable to obtain additional financing on acceptable terms or at all and we may have to significantly curtail our operations. To obtain funds through arrangements with strategic partners or others, we may need to relinquish rights to certain of our technologies or potential markets.

Our future growth will depend upon the acceptance of the technologies developed by Corrigent and Spediant and the development of markets for their products.

The markets for products by Corrigent are dependant on resilient packet ring, or RPR, technology. The market for products based on RPR technology may not fully develop, whether as a result of competition, alternative technologies, such as Ethernet over fiber in the metro area, changes in technology, product standards or otherwise. The markets for products by Spediant are dependant on multi-copper wire and inverse multiplexing technology. The market for products based on this technology may not fully develop, whether as a result of competition, alternative technologies, such as long-reach digital subscriber line technology, known as DSL technology, in the access area, changes in technology, product standards or otherwise. Our success depends on the acceptance of the products and technologies of Corrigent and Spediant. We have no control over the development of these target markets. Even if they develop technologies that are accepted, each must develop relationships with providers of telecommunications services in order to be successful. Furthermore, competing technologies in the targeted areas may be utilized in the majority of such target markets. This would leave Corrigent and Spediant with a small market to address.

We may not be able to keep pace with emerging industry standards for products we are developing. This could make these products more costly or unacceptable to potential customers.

Industry-wide standards for RPR products are expected to be adopted in 2004, but adoption may be delayed and proposed standards may be changed. The adoption of standards different from those currently proposed could result in us having to incur additional time and expense to have our products comply with these standards. Industry standards for the bonding of copper pair technology are in early stage of discussions and have not yet been adopted. The failure to comply with evolving standards could limit acceptance of our products. Since our products will be integrated into networks consisting of elements manufactured by various companies, they must comply with a number of current and future industry standards and practices established by various international bodies and industry forums. Standards may be adopted by various industry groups or may be proprietary and nonetheless accepted broadly in the industry. It may take us a significant amount of time to develop and design products incorporating these new standards. We may also have to pay licensing fees to the developers of the technologies that constitute newly adopted standards.

Because telephone companies must obtain in-house and regulatory approvals before they can order our products, expected sales of new products in development are likely to be subject to delays, which may harm our business.

Before telephone companies can purchase our products that are being developed, these products must undergo a lengthy approval process. Evaluation can take several years. Accordingly, we are required to submit enhanced versions of products in development for approval.

The following factors, among others, affect the length of the approval process:

- the time required for telephone companies to determine and publish specifications;
- the complexity of the products involved;
- the technological priorities and budgets of telephone companies; and
- the regulatory requirements applicable to telephone companies.

Delays in the product approval process could seriously harm our business and results of operation.

Because of rapid technological and other changes in the market for telecommunications products, we must continually develop and market new products and product enhancements while reducing production costs.

The market for our products is characterized by:

- rapid technological change;
- frequent product introductions and enhancements;
- evolving industry standards;
- changes in end-user requirements; and
- changes in services offered by telephone companies.

Technologies or standards applicable to our products could become obsolete or fail to gain widespread, commercial acceptance, resulting in losses and inventory write-offs. Rapid technological change and evolving technological standards are resulting in shorter life cycles for our products. Shorter life cycles for our products could cause decreases in product prices at the end of the product life cycle, inventory write-offs and a lower rate of return on our research and development expenditures. We may not be able to respond effectively to technological changes or new product announcements by others or successfully develop or market new products.

Our quarterly results of operations have fluctuated significantly in the past and we expect these fluctuations to continue if our products in development begin to generate revenues.

The following factors have affected our quarterly results of operations in the past and are likely to affect our quarterly results of operations in the future if we are able to sell commercial quantities of products currently in development:

- size and timing of orders, including order deferrals and delayed shipments;
- launching of new product generations;
- length of approval processes or market testing;
- technological changes in the telecommunications industry;

- accuracy of telephone company, distributor and original equipment manufacturer forecasts of their customers' demands;
- changes in our operating expenses;
- the timing of approval of government research and development grants;
- disruption in our sources of supply;
- funding required for the operations of Corrigent and Spediant; and
- general economic conditions.

Telephone companies typically require prompt delivery of products. Sales are typically booked and shipped in the same quarter pursuant to purchase orders. As a result, we expect that once sales of our new products commence, we will be required to maintain or have available sufficient finished goods inventory levels to satisfy anticipated demand on a timely basis. This increases the risk of inventory obsolescence and associated write-offs. A shift in demand could also result in inventory write-offs.

The market for the telecommunication products being developed by us is intensely competitive. Because many of our competitors have much greater resources than we have, it may be difficult for us to effect commercial sales or to achieve operating profitability.

The market for our products that are currently in development is intensely competitive, and we expect competition to increase in the future. Many of our competitors and potential competitors are large and established companies and have better name recognition and greater financial, technical, manufacturing, marketing and personnel resources than we have. Increased competition could adversely affect our future revenues and ability to become profitable on an operating basis through pricing pressure, loss of market share and other factors.

The competitors are numerous and we expect competition to increase in the future. Our principal competitors for our products include Alcatel, Cisco Systems, Inc., ECI Telecom Ltd., Fujitsu, Lucent Technologies Inc., Nortel Networks and Siemens AG.

Government regulation of telephone companies could adversely affect the demand for our products.

FCC regulatory policies affecting the availability of U.S. telephone companies' services, and other terms on which telephone companies conduct their business, may impede our penetration of certain markets. Telephone companies in the markets in other countries in which we operate are also subject to evolving governmental regulation or state monopolies. Changes in laws or regulations in the U.S. or elsewhere, could materially adversely affect our ability, and the ability of our customers, to penetrate certain markets.

Because a limited number of subcontractors are expected to manufacture and assemble our products and supply components, our business could suffer if we cannot retain or replace them.

We use third-party subcontractors to assemble our products. We do not expect to enter into multi-year agreements with assurances of supply with any of our suppliers or subcontractors.

Our expected reliance on third-party subcontractors involves several risks, including:

- the potential absence of adequate capacity if we are able to sell a significant amount of our products;
- the unavailability of, or interruption in access to, certain process technologies; and
- reduced control over product quality, delivery, schedules, manufacturing yields and costs.

We obtain certain key semiconductor components used in our products from a number of single source providers. Shortages of raw materials or production capacity constraints at our subcontractors could negatively affect our ability to meet product delivery obligations and result in increased costs for affected products that we may not be able to recover. Use of subcontractors also involves the risk of reduced control over product quality, delivery schedules and manufacturing yields, as well as limited negotiating power to reduce costs.

A shortage in the supply of key semiconductor and other components could affect our ability to manufacture and deliver our products and result in lower revenues. We may be unable to find alternative sources in a timely manner, if at all, if any of our suppliers were unwilling or unable to provide us with key components. If we cannot obtain sufficient key components as required, or develop alternative sources if and as required in the future, product shipments may be delayed or reduced. This could adversely affect our end-user relationships, business and results of operations.

We could incur substantial costs if customers assert warranty claims or request product recalls.

We expect to offer complex products that may contain errors, defects or failures when introduced or as new versions are released. If we deliver products with defects, errors or bugs or if we undergo a product recall as a result of errors or failures, market acceptance of our products could be lost or delayed and we could be the subject of substantial negative publicity. This could have a material adverse effect on our business and results of operations. We have agreed to indemnify our customers in some circumstances against liability from defects in the products previously sold by us and expect to provide a similar indemnity in connection with sales of products currently in development. In some cases our indemnity also covers indirect damages. Product liability claims could seriously harm our business, financial condition and results of operations.

We are subject to international business risks.

We are marketing our products in development primarily in the United States, Asia and Europe. Accordingly, we are subject to the risks inherent in international business, including:

- compliance with foreign laws and regulations;
- import or currency control restrictions;
- tariffs and other trade barriers;
- local taxation;
- transportation delays; and
- seasonal reduction of business activities.

These factors, as well as different technical standards or product requirements for our systems in different markets, may limit our ability to penetrate some foreign markets.

We depend on a limited number of key personnel who would be difficult to replace. If we lose the service of these individuals, our business will be harmed.

Orckit's growth and success largely depends on the managerial and technical skills of members of senior management. If any of them is unable or unwilling to continue with us, our results of operations could be materially and adversely affected.

Our proprietary technology is difficult to protect and unauthorized use of our proprietary technology by third parties may impair our ability to compete effectively.

We may not be able to prevent the misappropriation of our technology, and our competitors may independently develop technologies that are substantially equivalent or superior to ours. We have filed patent applications covering certain of our technologies. To protect our unpatented proprietary know-how, we rely on technical leadership, trade secrets and confidentiality and non-disclosure agreements. These agreements and measures may not adequately protect our technology and it may be possible for a third party to copy or otherwise obtain and use our technology without authorization or to develop similar technology.

There is a risk that we may violate the proprietary rights of others.

We are subject to the risk of adverse claims and litigation alleging infringement of the intellectual property rights of other companies. Many participants in the telecommunications industry have an increasing number of patents and patent applications and have frequently commenced litigation based on alleged infringement. We indemnify our customers with respect to infringement of third party proprietary rights by our products. In the past, we received notices from other parties regarding alleged violations of their proprietary rights. Third parties may assert infringement claims in the future and these claims may require us to enter into license arrangements or result in costly litigation, regardless of the merits of these claims. Licensing may be unavailable or may not be obtainable on commercially reasonable terms.

We are subject to risks from our financial investments.

We invest the majority of our cash on hand in a variety of financial instruments, including different types of corporate and government bonds, and other financial instruments. Some of these bonds and instruments may be rated below investment grade or not rated. If the obligor of any of the bonds or instruments we hold defaults or undergoes a reorganization in bankruptcy, we may lose all or a portion of our investment in such obligor. This will harm our financial condition. For information on the types of our investments as of December 31, 2003, see Item 11 - "Quantitative and Qualitative Disclosures About Market Risk-Interest Rate Risk Management."

Risks relating to our operations in Israel.

Potential political, economic or military instability in Israel may adversely affect our results of operations.

Our principal offices and many of our subcontractors and suppliers are located in Israel. Accordingly, political, economic and military conditions in Israel affect our operations. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors. A state of hostility, varying in degree and intensity, has led to security and economic problems for Israel. Since October 2000, there has been a marked increase in hostilities between Israel and the Palestinians, which has led to a crisis in the area and adversely affected Israel's relationship with several Arab countries. Any armed conflicts or political instability in the region could negatively affect local business conditions and harm our results of operations. We cannot predict the effect on Orckit of the increase in the degree of violence by Palestinians against Israel or the effect of military action elsewhere in the Middle East. Furthermore, several countries restrict doing business with Israel and Israeli companies, and additional companies may restrict doing business with Israel and Israeli companies as a result of the increase in hostilities. This may also seriously harm our operating results, financial condition and the expansion of our business.

Our results of operations may be negatively affected by the obligation of our personnel to perform military service.

Most of our male employees in Israel are obligated to perform annual military reserve duty. In addition, in the event of a military conflict or other attack on Israel, including the ongoing conflict with the Palestinians, these persons could be required to serve in the military for extended periods of time. The absence of a number of our officers and employees for significant periods could disrupt our operations and harm our business.

Because most of our revenues are generated in non-Israeli currencies and a substantial portion of our expenses are incurred in New Israeli Shekels, our results of operations may be adversely affected by inflation and currency fluctuations.

Most of our revenues are expected to be generated in U.S. dollars and other foreign currencies, while the majority of our payroll expenses and a portion of our other expenses are generated in New Israeli Shekels, or NIS. As a result, we are and could be further exposed to risk that the rate of inflation in Israel may exceed the rate of devaluation of the New Israel Shekel in relation to the dollar and other foreign currencies or that the timing of such devaluation may lag behind inflation in Israel. In that event, the dollar cost of our operations

in Israel would increase and our dollar-measured results of operations would be adversely affected. For example, in 2003 the value of the U.S. dollar declined in relation to the New Israeli Shekel by 7.6%, while the rate of deflation was 1.9%. As a result, our salary expenses, which are primarily linked to the New Israeli Shekel, increased in U.S. dollar terms.

We benefit from government grant programs that have been reduced and may be unavailable to us in the future. Our participation in these programs restricts our ability to freely transfer manufacturing rights and technology out of Israel.

Since our inception, we have relied on Israeli government grants for the financing of a significant portion of our product development expenditures. We have applied to Israel's Office of the Chief Scientist for grants for our contemplated 2004 research and development projects. Due to a reduction of the 2004 budget of Israel's Office of the Chief Scientist, it is expected that the amounts of our grants will be lower than in prior years. This would result in an increase in our research and development expenses.

According to Israeli law, any products developed with grants from the Office of the Chief Scientist are required to be manufactured in Israel, unless we obtain prior approval of a governmental committee. As a condition to obtaining this approval, we may be required to pay the Office of the Chief Scientist up to 300% of the grants we received and to repay these grants at an accelerated rate. In addition, we are prohibited from transferring to third parties in Israel the technology developed with these grants without the prior approval of a governmental committee and we are prohibited from transferring such technology to third parties outside Israel. See "Item 5 - Operating and Financial Review and Prospects - Liquidity and Capital Resources – Government and Other Grants" for additional information about these programs of the Office of the Chief Scientist.

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

We benefit from certain government programs and tax benefits, particularly as a result of the "Approved Enterprise" status of most of our existing facilities. If we fail to meet eligibility conditions in the future, the tax benefits could be canceled and we may be required to refund the tax benefits already received. The applicable law regarding approved enterprise programs is scheduled to expire on June 30, 2004. Accordingly, requests for new programs or expansions that are not approved on or before June 30, 2004 will not confer any tax benefits, unless the term of the law will be extended. These tax benefits may not continue in the future at their current levels or at any level. From time to time, we submit requests for expansion of our approved enterprise programs or for new programs to be designated as approved enterprises. These requests might not be approved, particularly in light of difficult economic conditions in Israel. The termination or reduction of these tax benefits could seriously harm our financial condition and results of operations.

It may be difficult to enforce a U.S. judgment against us, our officers and directors and our Israeli auditors or to assert U.S. securities law claims in Israel.

Service of process upon our directors and officers and our Israeli auditors may be difficult to effect in the United States because almost all these parties reside outside the United States. Any judgment obtained in the United States against such parties may be unenforceable outside the United States.

It is not clear whether civil liabilities under the Securities Act and the Securities Exchange Act can be enforced in Israel. However, subject to time limitations, Israeli courts may enforce a U.S. judgment in a civil matter, if:

- adequate service of process has been effected and the defendant has had a reasonable opportunity to be heard;
- the judgment and its enforcement are not contrary to the law, public policy, security or sovereignty of the State of Israel;
- the judgment was rendered by a court of competent jurisdiction, in compliance with due process and the rules of private international law prevailing in Israel;
- the judgment was not obtained by fraudulent means and does not conflict with any other valid judgment in the same matter between the same parties;
- no action between the same parties in the same matter is pending in any Israeli court at the time the lawsuit is instituted in a U.S. court; and
- the U.S. courts are not prohibited from enforcing judgments of the Israeli courts.

Foreign money judgments enforced in Israel, are generally awarded in New Israeli Shekels, based on the U.S. Dollar/NIS exchange rate in effect on the date of payment. The NIS can be converted into non-Israeli currency and transferred out of Israel. Pending collection, the amount of the NIS-denominated judgment is linked to the Israeli CPI and accrues interest at the annual statutory rate set by Israeli law. Judgment creditors bear the risk of unfavorable exchange rates.

Provisions of Israeli law may delay, prevent or make more difficult an acquisition of Orckit, which could depress our share price.

The Israeli Companies Law generally requires that a merger be approved by the board of directors and a majority of the shares voting on the proposed merger. Unless a court rules otherwise, the merger will not be deemed approved if a majority of the shares present that are held by parties other than the other party to the merger (or by any person who holds 25% or more of the shares or the right to appoint 25% or more of the directors of the other party) vote against the merger. Upon the request of any creditor of a party to the proposed merger, a court may delay or prevent the merger if it concludes that there is a reasonable concern that, as a result of the merger, the surviving company will be unable to satisfy its obligations. In addition, a merger may not be completed unless at least 70 days have passed since the filing of the requisite merger proposal by each party with the Israeli Registrar of Companies.

Also, in certain circumstances an acquisition of shares in a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 25% or greater or 45% or greater shareholder of the company (unless there is already a 25% or greater or a majority shareholder of the company, respectively). If, as a result of an acquisition, the acquirer would hold more than 90% of a company's shares, the acquisition must be made by means of a tender offer for all of the shares.

Additionally, Israeli tax law treats some acquisitions, such as stock-for-stock exchanges between an Israeli company and a foreign company, less favorably than U.S. tax laws. For example, Israeli tax law may, under certain circumstances, subject a shareholder who exchanges his ordinary shares for shares in another corporation to taxation prior to the sale of the shares received in such stock-for-stock swap.

The described restrictions could prevent or make more difficult an acquisition of Orckit, which could depress our share price.

Risks relating to the Market for our Ordinary Shares

Holders of our ordinary shares who are United States residents face income tax risks.

There is a high likelihood that we would be deemed to have been a passive foreign investment company, or PFIC, for 2001, 2002 and 2003. Our treatment as a PFIC could result in a reduction in the after-tax return to the United States holders of our ordinary shares, thus causing a reduction in the value of our shares, and could trigger the application of certain United States tax reporting requirements. For U.S. federal income tax purposes, we are treated as a PFIC for any taxable year in which either:

- 75% or more of our gross income is passive income, or
- at least 50% of the average value of all of our assets for the taxable year produce, or are held for the production of, passive income.

For this purpose, passive income includes dividends, interest, royalties, rents, annuities and the excess of gains over losses from the disposition of assets which produce passive income. As a result of our relatively substantial cash and investment assets and the decline in value of our ordinary shares, there is a high likelihood that we would be deemed to have been a PFIC in 2001, 2002 and 2003 under the asset test. We could also be deemed a PFIC in 2004. A separate determination must be made each year as to whether we are a PFIC. As a result, our PFIC status may change.

Highly complex rules apply to any U.S. holder of our ordinary shares if we are treated as a PFIC for U.S. federal income tax purposes for any year during such U.S. holder's holding period. Accordingly, U.S. holders are urged to consult their tax advisors regarding the application of these tax rules.

United States residents should carefully read Item 10.E "Taxation – United States" for a more complete discussion of the U.S. federal income tax risks related to owning and disposing of our ordinary shares and the consequences of PFIC status.

We do not intend to pay cash dividends.

On June 30, 2000, we distributed a stock dividend on a share-for-share basis of all our shares of Tikcro. We have never declared or paid any cash dividends on our ordinary shares. We currently intend to retain future earnings, if any, for funding growth. Accordingly, we do not expect to pay any cash dividends in the foreseeable future.

Two shareholders may be able to control Orckit.

As of March 31, 2004, Eric Paneth and Izhak Tamir our largest shareholders, each beneficially owns an aggregate of 751,771 ordinary shares representing 16.7% of our outstanding ordinary shares, including (i) 18,750 ordinary shares issuable upon the exercise of options that are currently vested or vest within the next 60 days and (ii) the right to purchase 140,000 shares from us, at any time or from time to time in one or more purchases until February 27, 2005. The purchase price for the ordinary shares under such right to purchase will be equal to the average closing price of our ordinary shares on Nasdaq over the ten trading days immediately preceding the purchase date, plus a premium of 10%. Both are executive officers and members of our Board of Directors. Currently, Messrs. Paneth and Tamir are not party to a shareholders agreement. However, if Messrs. Paneth and Tamir act together, they may have the power to control the outcome of matters submitted for the vote of shareholders, including the approval of significant change in control transactions. The equity interest in Orckit of Mr. Paneth and Mr. Tamir may make certain transactions more difficult and result in delaying or preventing a change in control of Orckit unless approved by one or both of them.

Our shareholder bonus rights plan and the conversion features of the Corrigent Option Plan may delay, prevent or make more difficult a hostile acquisition of Orckit, which could depress our share price.

In November 2001, we adopted a shareholder bonus rights plan pursuant to which share purchase bonus rights were distributed to our shareholders. These rights generally will be exercisable and transferable apart from our ordinary shares only if a person or group acquires beneficial ownership of 15% or more of our ordinary shares, or commences a tender or exchange offer upon consummation of which that person or group would hold such a beneficial interest. Once these rights become exercisable and transferable, the holders of rights, other than the person or group triggering their transferability, will be generally entitled to purchase our ordinary shares at a discount from the market price. The rights will expire on December 31, 2011. While these rights remain outstanding, they may make an acquisition of us more difficult and result in delaying or preventing a change in control of Orckit. Subject to the approval of the Board of Directors of each of Orckit and Corrigent, and based on the relative fair market value of each of relevant companies, options granted by Corrigent may be exercised to acquire shares of Orckit. This conversion could also delay or prevent a change of control of Orckit.

Our stock price has fluctuated significantly and could continue to fluctuate significantly.

The market price for our ordinary shares, as well as the prices of shares of other technology companies, has been volatile. The following factors may cause significant fluctuations in the market price of our ordinary shares:

- fluctuations in our quarterly revenues and earnings or those of our competitors;
- shortfalls in our operating results compared to levels forecast by securities analysts;
- announcements concerning us, our competitors or telephone companies;

- announcements of technological innovations;
- the introduction of new products;
- changes in product price policies involving us or our competitors;
- market conditions in the industry;
- the conditions of the securities markets, particularly in the technology and Israeli sectors; and
- political, economic and other developments in the State of Israel and world-wide.

In addition, stock prices of many technology companies fluctuate significantly for reasons that may be unrelated or disproportionate to operating results. The factors discussed above may depress or cause volatility of our share price, regardless of our actual operating results.

Our ordinary shares are listed for trading in more than one market and this may result in price variations.

Our ordinary shares are listed for trading on the Nasdaq Stock Market, or Nasdaq, and on The Tel Aviv Stock Exchange, or TASE. Trading in our ordinary shares on these markets is made in different currencies (U.S. dollars on Nasdaq and New Israeli Shekels on TASE), and at different times (resulting from different time zones, different trading days and different public holidays in the United States and Israel). Actual trading volume on the TASE is insignificant and as such is subject to volatility. The trading prices of our ordinary shares on these two markets often differ, resulting from the factors described above, as well as differences in exchange rates. Any decrease in the trading price of our ordinary shares on one of these markets could cause a decrease in the trading price of our ordinary shares on the other market.

ITEM 4. INFORMATION ON THE COMPANY

A. HISTORY AND DEVELOPMENT OF THE COMPANY

Our History

Orckit Communications Ltd. was incorporated in 1990 under the laws of the State of Israel. Our principal executive offices are located at 126 Yigal Allon Street, Tel Aviv 67443 Israel and our telephone number is (972-3) 696–2121. Our agent in the United States, Puglisi & Associates, is located at 850 Library Avenue, Suite 204 Newark, Delaware 19711.

Major Developments since January 1, 2003

We continued to fund the development and marketing efforts of the technology and products of Corrigent and Spediant, addressing the need for solutions capable of supporting very high bandwidth services. Corrigent is in the process of developing and commercializing telecommunication equipment supporting high bandwidth services over fiber networks in telecommunications networks located in metropolitan areas. Spediant is in the process of

developing and commercializing telecommunication equipment supporting high bandwidth services over DSL lines in telecommunications networks located in access areas. Access areas include the “first mile” of the network, up to the facilities of the end user. We intend to continue to fund the operations of Corrigent and Spediant from our existing working capital. Substantially all of our operating expenses in 2003 were related to these efforts.

Corrigent Systems

Corrigent is developing products and technology that address the need for telecommunication transport solutions capable of supporting high bandwidth data and voice services in metro networks. Corrigent’s target customers are telecommunications service providers active in metropolitan areas, with a focus on incumbent local exchange carriers. Corrigent’s solution is being designed to enable the provision and management of data and voice transport services in an efficient manner that is expected to reduce the costs of transport service providers. Supporting fiber-optic infrastructures, Corrigent’s system is planned to include a range of data and voice interfaces.

The Corrigent solution is being designed to comply with telecommunications standards and to support emerging telecommunications protocols. It is designed for efficient transport of Internet protocol information, while providing the reliability necessary for the transport of voice services. As of December 31, 2003, Corrigent had 114 employees in the areas of product planning, business development, marketing and sales, research and development, system engineering and administration. Corrigent has offices in Israel, the United States and Japan.

Corrigent has granted, and reserved for grant, options under the Corrigent Stock Option Plan and other employee plans, as applicable, to its employees, consultants, officers and directors. In addition, in order to attract and retain highly qualified personnel of Orckit, employees, officers and directors of Orckit were reserved and granted shares and options to purchase shares of Corrigent. As of December 31, 2003, Corrigent had granted, or reserved for future grant, options and shares to the directors, employees and consultants of Corrigent and Orckit, at a nominal price, representing approximately 30% of its share capital on a fully diluted basis. These options generally vest up to four years from the date of grant and, at the discretion of Orckit and Corrigent, are convertible into Orckit’s ordinary shares. Orckit’s equity interest in Corrigent, which represented approximately 70% of Corrigent’s shares on a fully diluted basis as of December 31, 2003, may be further diluted by future share issuances by Corrigent, if Corrigent should engage in a financing transaction to assist in funding its operations.

Spediant Systems

Spediant is developing products and technologies that address the needs of service providers for fiber-speed broadband services over the existing copper wire infrastructure. Spediant's products are expected to primarily address the growing demand for Ethernet-based services. Spediant products are being designed to allow providers to increase their broadband services offerings and customer bases, deliver greater bandwidth to small and medium enterprises, or SMEs, and obviate the need for capital expenditures associated with deployment of new fiber. As of December 31, 2003, Spediant had 37 employees in the areas of product planning, research and development and marketing. Spediant has offices in Israel and the United States.

Spediant has granted, and reserved for grant, options under the Spediant Stock Option Plan and other employee plans, as applicable, to its employees, consultants, officers and directors. In addition, in order to attract and retain highly qualified personnel of Orckit, employees, officers and directors of Orckit were reserved and granted options to purchase shares of Spediant. As of December 31, 2003, Spediant had granted, or reserved for future grant, options and shares to the directors, employees and consultants of Spediant and Orckit, at a nominal price, representing approximately 30% of its share capital on a fully diluted basis. The options generally vest up to four years from the date of grant. Orckit's equity interest in Spediant, which represented approximately 70% of Spediant's shares on a fully diluted basis as of December 31, 2003, may be further diluted by future share issuances by Spediant, if Spediant should engage in a financing transaction to assist in funding its operations.

Principal Capital Expenditures

Our principal capital expenditures to date have been the purchase of equipment and other software tools used in our business. These purchases totaled \$2.4 million in 2001, \$1.8 million in 2002 and \$900,000 in 2003. We used internal resources to finance these capital expenditures.

B. BUSINESS OVERVIEW

General

The market in which we operate targets the incumbent local telephone companies, such as the U.S. Bell telephone companies and telecom carriers in Asia and Europe. We predominantly target the emerging market for metro transport products with our Corrigan CM-100 product line, which addresses the need for high data transmissions. With our Spediant EML-8000 product line, we target established and new telecom carriers for the delivery of data services over existing copper wires.

Metro Transport Telecom Markets, Technology and Products

The Metro Transport Market

The fiber optic networks of many telephone companies in metropolitan areas are experiencing a shift from carrying primarily voice traffic to carrying a growing mix of data and voice traffic. Data traffic volumes carried over these metropolitan area networks are surpassing voice traffic volumes. Data traffic is forecasted for further growth over the coming years. This increase in data relative to voice traffic is mainly a result of the rapid growth of the Internet and local area networks.

Offerings of high data services at rates of ten mega bits per second (Mbps) or higher have reached many millions of subscribers in a number of Asian markets, including Japan and Korea. These services are offered either over fiber connections or a combination of fiber and fast access technologies, such as DSL, wireless or cable networks. Recently, major U.S. telecom carriers have announced plans for expansion of fiber rings in metro areas, promoting connectivity of fiber to the premise (FTTP). Connecting subscribers with fiber will allow for significantly higher speed services, mainly data and video services, and as a result, will

require an upgrade of metro telecom equipment with technologies that address very high transmissions of data over fiber networks.

Telephone companies have typically managed their data transfer capacity needs through their existing transport technologies. These technologies were originally designed for transporting voice services. These traditional solutions, however, are not designed to support expected future levels of data traffic. Traditional networks are also inefficient when transporting data as they fail to utilize inherent differences in the type of network support that is required for the transmission of data traffic. Data traffic is generally less susceptible to corruption resulting from minor time delays and less time-sensitive than voice traffic. In addition, data traffic often exhibits a bursty nature, with dynamically varying levels of utilization of communication channels, as opposed to voice traffic which normally requires constant levels of channel utilization.

A new set of solutions is being developed to address the needs of carriers and service providers to be able to support higher levels of data traffic within and between metropolitan areas, commonly referred to as metro transport. These solutions are attempting to take advantage of the characteristics of data traffic without impairing the ability to support traditional voice traffic. We expect that the metro transport solution for the transmission of traditional voice and increased data traffic will combine the efficient transport of data services based on Ethernet protocol with high reliability voice services based on SONET/SDH protocol.

Major metro transport technologies include the following voice and/or data protocols:

SONET / SDH. SONET is the American National Standards Institute, or ANSI, standard for synchronous voice transmission on optical media. The international equivalent of SONET is synchronous digital hierarchy, or SDH. Together, these two voice protocols ensure standards to enable digital networks to interconnect internationally and existing conventional transmission systems to utilize fiber with the help of interfaces that connect network end-users, called tributary attachments.

Ethernet. Ethernet is the most widely-installed local area network, or LAN, technology. It is often used in college dormitories and office buildings. The most commonly installed Ethernet systems are called 10BASE-T and provide transmission speeds up to 10 Mbps.

RPR. Resilient packet ring, or RPR, is an emerging technology that is being designed to integrate Ethernet data protocols for the efficient transmission of data with traditional SONET voice protocols. An industry working group has agreed on a draft standard for RPR. Corrigent has been instrumental in establishing this draft standard, serving actively as a member of the industry work group charged with defining the RPR protocol. However, uniform industry standards for RPR have not yet been adopted and the estimated date for approval of an industry standard has been delayed until mid 2004.

RPR is being developed as an alternative to SONET transport for networks that support high levels of data traffic, while allowing carriers to maintain traditional SONET attributes, such as resiliency. Resiliency refers to the ability to employ a back-up or alternate route in the event of a system or optical fiber failure, as well as the fast restoration of service in the event of any other failure. RPR is expected to allow carriers to conduct performance

monitoring of transmission rates, traffic volume, and failures and alarms, comparable to the monitoring available with traditional SONET-based networks.

Multiprotocol Label Switching. Multiprotocol label switching, or MPLS, is a standards-approved technology for speeding up network traffic flow and making it easier to manage. MPLS involves setting up a specific path for a given sequence of packets, identified by a label put in each packet, thus saving the time needed for a router to look up the address to the next node to forward the packet to. MPLS is called *multiprotocol* because it works with the Internet Protocol, or IP, Asynchronous Transport Mode, or ATM, and frame relay network protocols. In addition to moving traffic faster overall, MPLS makes it easy to manage a network for quality of service, or QoS. For these reasons, MPLS is expected to be adopted as networks begin to carry more and different mixtures of traffic.

RPR's Advantages over Existing Data and Voice Transport Protocols

We believe that RPR is a more efficient voice and data transport protocol than traditional SONET rings that have been retrofitted to handle data traffic for the following reasons:

- Usage of a single fiber ring and spatial reuse capabilities.

SONET utilizes only one ring of optical fibers. A second ring is available in case of a failure in the first ring, but is otherwise not used. This creates unutilized capacity in SONET, as half of the network capacity is idle during normal operations. RPR enables the use of this redundant bandwidth under normal operating conditions, while maintaining the redundancy capabilities. In addition, RPR supports spatial reuse, which allows the re-use of the same ring bandwidth over different spans of the ring.

- Statistical multiplexing qualities

With SONET, data transmitted from one specific network element, or node, to another may be sent only using bandwidth that has been dedicated for that transmission. RPR increases bandwidth efficiency by allowing data transmissions to be broken up into packets and inserted in bandwidth that might have otherwise been dedicated (but not used) for a separate transmission. This process is called statistical multiplexing. When less than all network users are actively transmitting or receiving data at the same time, it results in a more efficient utilization of the total available bandwidth on a network.

Corrigent's Metro Transport Product and RPR Technology

Corrigent's metropolitan area product is designed as a cost-effective optical transport solution that can handle not only the growing demand for data services by telephone company customers and small to medium size businesses, but also support the full range of traditional voice services, in compliance with SONET technical specifications. Corrigent's product is being designed to provide the benefits of both Ethernet and SONET protocols. It is also being designed to avoid integrating costly protocol-dependant routing and switching functionalities that are generally required in adopting SONET platforms to cover data traffic, as well as the costs of adopting Ethernet platforms to handle voice traffic.

Corrigent's CM-100 product utilizes SONET, RPR, and MPLS technologies to effectively support a range of SONET services, Ethernet, Time Division Multiplexer, or TDM, services which are commonly used for voice transmissions, and other data services. This product is being designed to interoperate with both legacy SONET and emerging MPLS core devices. The product is expected to support 2.5 Gigabits per second, or Gbps, and 10 Gbps ring speeds, and interface with:

- 10 megabits/100 megabits Ethernet;
- 1 Gigabit Ethernet; and
- a range of TDM SONET interfaces including:
 - 155 megabits per second SONET interface (known also as OC3);
 - 622 megabits per second SONET interface (known also as OC12); and
 - 2.5 gigabit per second SONET interface (known also as OC48).

Corrigent's CM-100 product is designed to deliver both Ethernet and TDM/Sonet – based services over a packet-based network. These services are carried over MPLS tunnels over an RPR ring in a packetized form that is expected to enable both bandwidth efficiency and lower cost architecture. The CM-100 allows legacy data services, such as frame relay, asynchronous transfer mode, or ATM, and packet over SONET, to be carried in their native form allowing a reduction in the bandwidth used to provide these services. MPLS is used to provide both end-to-end automatic provisioning capabilities and isolation between different users' services, thus providing a preferred method of traffic engineering. MPLS also aids end-to-end interoperability between the transport systems of different vendors.

The CM-100 product has been available for testing since late 2002 and we expect to begin making sales of this product in 2004. This product has been selected for commercial deployment by a telecom provider in Asia targeting Ethernet-based services. Also, Corrigent has signed a distribution agreement with Netmarks Inc. that targets the Japanese market and will seek to address the demand for high capacity transport equipment by telecom carriers and service providers.

DSL Markets, Technology and Products

Industry Background

Growth in the use of the Internet and personal computers has created substantial data traffic over telephone networks from a wide variety of associated services. At the same time, the difficult environment in the telecommunications industry and a depressed world economy have resulted in a reduction in capital expenditure plans. Telephone service initially consisted of analog transmission over copper wire. The commercial introduction of DSL technologies added higher speed transmission over copper wire. Digital transmission over fiber optic or coaxial cable permits greater data capacity and increased reliability and quality at a lower cost than analog transmission. Telephone companies recognize that it is extremely expensive to install fiber optic or coaxial cable in the local loop, the first mile of copper telephone wire between the central office and the consumer. Consequently, the local loop remains primarily twisted copper telephone wire. Without an alternative solution, this twisted copper telephone

wire restricts the ability of telephone companies to increase the speed and diversity of their service offerings to small business and residential users.

DSL Markets

Telephone companies worldwide have recognized that digital subscriber line technology is one of the technologies that may answer the existing need to allow fast data transmission in the “first mile” of the telecom network, up to the facilities of the end user. Accordingly, they are increasingly using DSL technologies to provide digital transmission over the local loop. DSL technologies enable telephone companies to maintain their competitive position by offering high-speed Internet access and enhanced services to customers over the local loop. DSL systems that offer services directly to the telephone companies’ customers’ premises generally use a passive plain old telephone service, commonly known as POTS, splitter on each DSL line, which can be installed both at the central office and at the customer’s premises. The POTS splitter separates the analog telephone channel from the digital data channel that is transmitted over the same twisted copper telephone wire. By isolating the telephone signal from the digital signal, the home telephone line is not affected by the digital transmission. Telephone service is unaffected if the DSL system should fail for any reason.

Spediant Products and Technology

Spediant’s EML-8000 is an access solution being designed to enable telecom carriers to deploy fiber-speed broadband services over traditional copper wires. It is designed to address the growing demand for Ethernet-based services at faster data rates and over longer distances than provided by current DSL solutions. This product line is expected to allow providers to increase their broadband service offerings and customer bases, deliver greater bandwidth to small and medium enterprises, or SMEs, and decrease the need for capital expenditures to deploy new fiber. Spediant’s solution is being designed to provide an answer to growing bandwidth requirements of SMEs for Ethernet services on one end and the desire of carriers to utilize the existing copper infrastructure with attractive services on the other end.

Spediant’s solution is based on Multi Loop DSL, or MLDSL, technology. Rather than treating each copper pair individually, MLDSL treats multiple copper pairs as a logical bundle, making intelligent decisions regarding bandwidth allocation and reactions during changing link conditions. This helps to eliminate mutual interference in the copper binder. EML-8000 is built on standardized technology by binding multiple copper pairs and inversely multiplexing data across them for greater reach and bandwidth. Inverse multiplexing is implemented in such a way that mission-critical data traffic is transparently transported with low latency.

Spediant’s EML-8000 is designed to deliver 10 Mbps at a distance of 12,000 feet from the central office. The cost of installing fiber to serve SMEs is significant for service providers. By binding several copper wiring pairs in the existing infrastructure, the EML-8000 is intended to satisfy the bandwidth needs of SMEs while increasing revenue opportunities for service providers.

Sales, Marketing and Service

Sales and Marketing. Our marketing efforts are directed at telephone companies. Marketing efforts may also be made pursuant to original equipment manufacturers, strategic alliances and other distribution arrangements. We believe that the participation by our subsidiaries in technology committees involved in the establishment of industry standards is a strong marketing tool. As of December 31, 2003, overall marketing and sales efforts were conducted by approximately 16 employees located in Israel, the United States and Japan.

The following is a summary of revenues by geographic area for the last three years:

	Year ended December 31		
	2001	2002	2003
	(In thousands)		
Israel	\$ 2,268	\$ 463	\$35
United States	111,336	44,811	
Europe	23,319	7,601	1,510
Other countries	4,724	545	138
	<u>\$ 141,647</u>	<u>\$ 53,420</u>	<u>\$1,683</u>

Substantially all our revenues for 2001 through 2003 were generated from our FastInternet DSL product line. We no longer sell these products.

Telco Approval Process. Telephone companies are significantly larger than us and consequently are able to exert a high degree of influence over us. Prior to selling our products to telephone companies, we are required to undergo lengthy approval processes. Evaluation can last for over one year for enhanced products or products based on newer technologies.

The length of the approval process is affected by a number of factors, including the complexity of the product involved, technological and budgetary priorities of the telephone companies and regulatory issues affecting telephone companies. A telephone company will usually conduct technical trials after completing a laboratory evaluation that tests a new product's function and performance against industry standards. After completion of technical trials, field trials simulate operations to evaluate performance and to assess ease of installation and operation. In subsequent market trials, a telephone company will attempt to determine the content requirements, the estimated number of subscribers and optimized pricing for the service. During this stage, telephone companies establish procedures, train employees to install and maintain the new product and obtain feedback on the product from their customers and operations personnel. Throughout the approval process, we commit senior technical and marketing personnel to participate in technology, field and market trials and to actively support the evaluation efforts.

Commercial deployment of a new product usually involves substantially greater numbers of systems and locations than the marketing trial stage. In the first phase of commercial deployment, a telephone company installs the equipment in selected locations for certain applications. This phase is followed by general deployment which involves greater numbers of systems and locations. Telephone companies typically select a number of suppliers for general deployment to ensure that their needs can be met. Subsequent orders, if any, are placed under a single or multi-year supply agreement.

Following selection for commercial deployment, the introduction of successive generations of products or upgraded software versions is vital to our business, because it enhances functionality and reduces costs. Our growth substantially depends on commercial acceptance of advanced products and technology by telephone companies, as well as our ability to develop new technologies and sell new products.

Telco Services and Support. We offer repair services as part of our warranty services and technical support services for our products. We do not offer installation services. We expect that our local partner or distributor will provide first level of service and support. More extensive repair and technical support is offered at our headquarters in Israel pursuant to warranty obligations. We also offer telephone support during working hours and provide product training to our carrier customers on a case-by-case basis.

The majority of our products shipped to date are subject to a three-year warranty period and our new products offer similar warranty protection. Our warranty generally covers defects in materials or workmanship and failure to meet published specifications, but excludes damages caused by improper use and all other express or implied warranties. In the event that there are material deficiencies or defects in the design or manufacture of our products, the affected products could be subject to recall. Exposure to indirect damages arising from failures covered by warranty could be significant. We have received claims for compensation from certain of our customers due to warranty related matters. We believe that our potential liability in connection with these claims is not material.

Customers and End-users. We expect to depend on purchases by telephone companies for our product revenues. We have previously sold our products either directly to telephone companies or through original equipment manufacturers, distributors or strategic partners from whom telephone companies then purchase our products.

Manufacturing

We use subcontractors for component sourcing, inventory warehousing, board assembly, testing and shipment. These contracting and manufacturing arrangements have enabled us in the past to produce reliable, high quality products at competitive prices and to achieve on-time delivery of our products. We expect to continue to utilize third parties to manufacture, assemble and test our new products.

Telephone company orders are short-term and may involve short delivery time frames. We expect that the manufacture of products will be mainly against purchase orders, although in the first stages of market penetration we are likely to order products based on sales forecasts only. We and our manufacturers perform final quality control and extensive testing prior to shipping. Product quality and reliability are of prime concern in all phases of the manufacturing process. Our facilities are subject to the ISO9001 certification process. This certification is required in order to sell to many of the telephone companies.

In procuring components, we and our subcontractors rely on a number of suppliers of semiconductor solutions that are the sole source for certain of the components. We expect to use a single-source manufacturing contractor.

Competition

We compete on the basis of technological capability, price, customer service, product features, adherence to standards, quality, reliability, availability and technical support. With respect to products under development, initial competition is expected to be based primarily on technological capability and the ability to develop a product that can be manufactured and sold with a cost structure that will allow for mass deployment to customers of telephone companies. Many of our competitors and potential competitors have greater financial, technological, manufacturing, marketing and personnel resources than we have and have entered into strategic alliances to assist them in commercialization of their products.

Our competitors in our targeted markets of metro and access telecom equipment are numerous and we expect competition to increase in the future. Our principal competitors for our products include Alcatel, Cisco Systems, Inc., ECI Telecom Ltd., Fujitsu, Lucent Technologies Inc., Nortel Networks and Siemens AG.

Intellectual Property Rights

We regard our technology as proprietary. We have obtained several patents and have filed a number of patent applications covering certain key areas of our technologies. In general, we have relied on a combination of technical leadership, trade secret, copyright and trademark law and nondisclosure agreements to protect our unpatented proprietary know-how. Our proprietary technology incorporates algorithms, software, system design and hardware design that we believe is not easily copied. We believe that, because of the rapid pace of technological change in the telecommunications industry, patent and copyright protection are less significant to our competitive position than factors such as the knowledge, ability and experience of our personnel, new product development, market recognition and ongoing product maintenance and support.

Legal Proceedings

We are not a party to any material pending legal proceedings, nor is any of our property the subject of any other material pending legal proceedings.

C. ORGANIZATIONAL STRUCTURE

List of Significant Subsidiaries

Corrigent Systems Inc., a subsidiary, is a Delaware corporation. As of December 31, 2003, Orckit owned approximately 70% of the shares of Corrigent Systems on a fully-diluted basis, including shares reserved for grant.

Spediant Systems Ltd., a subsidiary, is an Israeli corporation. As of December 31, 2003, Orckit owned approximately 70% of the shares of Spediant Systems on a fully-diluted basis, including shares reserved for grant.

D. PROPERTY, PLANTS AND EQUIPMENT

Our principal offices and production facilities in Tel Aviv occupy approximately 50,000 square feet of rental space rented through a series of leases. Our leases expire in the years 2004-2006. We have an option to terminate these lease agreements with six months' prior written notice. We also maintain offices in San Jose, California and Tokyo, Japan. We believe that these facilities are adequate for our current needs and that suitable additional or substitute space will be available when needed.

ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

Statements in this Annual Report concerning our business outlook or future economic performance; anticipated revenues, expenses or other financial items; introductions and advancements in development of products, and plans and objectives related thereto; and statements concerning assumptions made or expectations as to any future events, conditions, performance or other matters, are "forward-looking statements" as that term is defined under the United States Federal Securities Laws. Forward-looking statements are subject to risks, uncertainties and other factors which could cause actual results to differ materially from those stated in such statements. Factors that could cause or contribute to such differences include, but are not limited to, those set forth under "Risk Factors" in this Annual Report as well as those discussed elsewhere in this Annual Report and in our other filings with the Securities and Exchange Commission.

A. OPERATING RESULTS

Our operating and financial review and prospects should be read in conjunction with our financial statements, accompanying notes thereto and other financial information appearing elsewhere in this Annual Report.

Overview

Orckit was founded in 1990. We are an Israeli corporation engaged in the design, development, manufacture and marketing of telecom equipment that enables transmission of broadband services. The substantial majority of our historical revenues were derived from the sale of systems and customer premises modems based on DSL technology. We have terminated the sale of these products and do not expect to generate additional revenues from them. Going forward, we expect to generate revenues from the sales of new products developed by our majority-owned Corrigent and Spediant subsidiaries, although we do not expect to generate significant revenues in 2004.

The end-user base for our products was comprised primarily of large telephone companies, and was concentrated among several telcos in each year. We expect that such concentration will continue as we commence selling our new product lines.

Our products undergo lengthy approval and procurement processes prior to their sale due to the quality specifications of our end-users and the regulated environment in which they operate. Accordingly, we are making significant expenditures in product and market development prior to actually commencing sales of new products. In addition, frequently we are required to make significant expenditures to tailor our products to specific end-user needs during the initial commercialization phase. We expect to continue to depend on a limited number of end-users to generate a significant percentage of total product revenues. Our product sales to end-users are expected to fluctuate significantly from quarter to quarter and year to year.

We intend to continue to evaluate new technologies and related product opportunities and engage in extensive research and development activities related to new technologies. Accordingly, we expect to continue to make significant expenditures for research and development.

Substantially all of our operating expenses in 2003 related to research and development expenses, selling, general and administrative expenses and capital expenditures for the operations and support of Corrigent and Spediant.

Our ability to generate income from operations will primarily depend on our sales volume and the level of our operating expenses. Until significant revenues are generated from the products of Corrigent and Spediant, we expect to continue to incur significant operating losses and to use a significant amount of cash to fund our operations. We expect to start generating revenues from our new product initiatives in 2004 but to continue to have losses at least through 2005.

Critical Accounting Policies and Estimates

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States. These accounting principles require management to make certain estimates, judgments and assumptions based upon the information available at the time they are made, historical experience and various other factors believed to be reasonable under the circumstances. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. Management evaluates its estimates and judgments on an on-going basis. Some of those judgments can be subjective and complex, and consequently actual results may differ from those estimates.

The Company is also subject to risks and uncertainties that may cause actual results to differ from estimates and assumptions, such as changes in the economic environment, competition, foreign exchange, taxation and governmental programs. Certain of these risks, uncertainties and assumptions are discussed in Item 3.D - Risk Factors. To facilitate the understanding of our business activities, described below are certain accounting policies that are relatively more important to the portrayal of our financial condition and results of operations and that require management's subjective judgments. We base our judgments on past experience and various other assumptions that are believed to be reasonable under the circumstances. Please refer to Note 1 to our consolidated financial statements included in this Annual Report for a summary of all of our significant accounting policies.

Revenue Recognition

Revenues from sales of products are recognized when title passes to the customer, provided that appropriate signed documentation of the arrangement, such as a contract, purchase order or letter of agreement, has been received, the fee is fixed or determinable and collectibility is reasonably assured.

Prior to the sale of a new product, we deliver products for trial and evaluation by our customers. Evaluation can take several months for complex products or products based on new technologies. We do not recognize sales revenues from delivery of a new product to customers for evaluation.

Provision for servicing products under warranty

The majority of our products shipped to date are subject to up to a three-year warranty period. We have agreed to indemnify our customers in some circumstances against liability from defects in our products. In some cases our indemnity also covers indirect damages. The Company provides an estimate for warranty expense at the time revenues from the related sales are recognized. The annual provision is calculated as a percentage of the sales, based on historical experience and is established based on our estimate of the amounts necessary to settle product-related matters existing as of the balance sheet date.

The amount of our estimated warranty liability may change if the costs incurred due to product failures increase in the future. In the event of any future problems with our products, we may need to increase the amount of our reserves.

Employee stock option plans

In January 2003, we adopted the Orckit Communications Ltd. 2003 Subsidiary Employee Share Incentive Plan.” Pursuant to the 2003 Plan, we issued, for no consideration, 600,000 of our ordinary shares to employees of our subsidiaries, excluding directors. The shares were deposited with a trustee and vested after a period of three years. According to the 2003 Plan, the shares issued were subject to exchange at any time by us, in our discretion, for options to purchase shares of the applicable subsidiary.

In 2003, 60,000 shares issued under this plan were forfeited and 540,000 shares were exchanged for options to purchase shares of subsidiaries. The accounting treatment applied in respect of the plan is variable accounting until the exchange occurred. Accordingly, compensation in respect of the grant of the shares was measured according to the share price of Orckit and updated to reflect the changes in the share price through the date of the exchange. Aggregate compensation expense in connection with the grant was approximately \$3.8 million, which is to be amortized over the vesting period of the shares granted. In 2003, approximately \$1.3 million of this expense was amortized. Upon the exchange, the plan became a fixed plan and the compensation was fixed according to the share price of Orckit on that date. At the date of exchange, the intrinsic value of options to purchase shares of subsidiaries that employees received was zero.

In addition, the board of directors of each of the subsidiaries, Corrigent Systems and Spediant Systems, approved an employee share option plan. Each of Corrigent Systems and Spediant Systems has granted, and reserved for grant, shares and options under its respective plans to its employees, officers and directors and to personnel of Orckit, including employees, officers and directors of Orckit. As determined by the respective stock option committee, the exercise price of options granted is zero which, in management’s opinion, represents the value of the shares on the date of grant. Accordingly, no compensation cost was included in our financial statements in respect of such grants.

Results of Operations

The following table sets forth certain items from Orckit's consolidated statement of operations as a percentage of total revenues for the periods indicated:

	<u>2001</u>	<u>2002</u>	<u>2003</u>
Revenues	100%	100%	100%
Cost of revenues	79.1	61.7	44.4
Gross profit (loss)	20.9	38.3	55.6
Research and development expenses, net	13.5	36.1	891.4
Selling, general and administrative expenses	12.0	27.5	752.0
Amortization and impairment of goodwill	18.4	--	--
Loss from operations	(23.0)	(25.3)	(1,588.0)
Financial income, net	23.6	33.0	303.5
Net income (loss)	0.6%	7.6%	(1,284.4)%

Revenues. Orckit's revenues have historically consisted primarily of DSL-based product and related service sales. During 2003, our revenues were minimal as we transitioned our business from our legacy DSL products to the development of our new Corrigent and Spediant products. Revenues decreased to \$1.7 million in 2003 from \$141.6 million in 2001 and \$53.4 million in 2002. Product revenues in 2001 and 2002 resulted primarily from sales of DSLAM and DSL-based modem products. The decline in our revenues in 2002 was primarily a result of the selection of competing products by our customers, as well as the slowdown in capital expenditures in the telecommunications industry. We do not expect to generate additional revenues from the sale of our legacy DSL products. We do not expect to generate significant revenues in 2004 from the sale of our new products.

Gross Profit (Loss). Cost of revenues consists primarily of raw materials, subcontracting costs and costs for integration, assembly and testing of finished products. Gross profit was \$935,000 (55.6% of revenues) in 2003 compared to \$20.5 million (38.3% of revenues) in 2002 and \$29.6 million (20.9% of revenues) in 2001. The improvement of gross profit was primarily due to a decrease in the cost of components and assembly for products sold. Gross profit on our legacy DSL products is not necessarily indicative of gross margins that we may generate if we are able to make sales of our new products.

Operating Expenses

	Year ended December 31, (\$ in millions)			a% Change 2002 vs. 2001	% Change 2003 vs. 2002
	2001	2002	2003		
Research and development, net	19.1	19.3	15.0	1.1%	(22.2)%
Selling, general and administrative	17.0	14.7	12.7	(13.5)	(13.9)
Total operating expenses	36.1	34.0	27.7	(5.8)	(18.6)

Research and Development Expenses, net. Research and development expenditures consist primarily of materials, depreciation and salaries and related costs for engineering and technical personnel and subcontracting costs associated with developing new products and for other technology projects. Our costs for research and development are expensed as incurred. Grants from the government of Israel for research and development are offset against our gross research and development expenditures. Research grants were \$3.3 million in 2001, \$3.0 million in 2002 and \$5.8 million in 2003. Research and development expenses decreased in 2003 compared to 2002, mainly due to an increase in research grants, as well as a decrease in the consumption of research and development materials and the use of sub-contractors. We anticipate we will incur a similar level of research and development expenditures in 2004, although we expect that the amount of government research grants we receive in 2004 will be less than in 2003, due to a reduction of the 2004 budget of Israel's Office of the Chief Scientist.

Selling, General and Administrative Expenses. Selling, general and administrative expenses consist primarily of costs relating to promotion, trade shows, compensation costs for non-technical personnel, warranty provisions and other general corporate expenses. Our selling, general and administrative expenses decreased in 2002 and again in 2003 due to the reduction of our marketing and sales activities. We expect that marketing and sales expenses will increase in 2004 and as we increase our marketing and sales efforts in connection with the expected initial commercial sales of the products being developed by Corrigent and Spediant.

Amortization of goodwill. In 2000, due to the acquisition of E.D.S.L., we recorded the amount of \$33 million as goodwill and other intangible assets, which was calculated based on the excess of the cost of the acquisition over the fair value of net assets on the acquisition date that was not attributed to in-process research and development. The goodwill was to be amortized on the straight-line basis over a period of three years. In 2000, an amount of \$6.9 million related to E.D.S.L. was amortized. In 2001, E.D.S.L. halted its operations due to the extreme reduction in capital expenditures of carriers in the markets it targeted. As a result, in 2001 we wrote off the \$23.4 million that represented all outstanding unamortized goodwill in connection with our acquisition of E.D.S.L. and all of the goodwill on our balance sheet.

Financial Income, net. Financial income consists primarily of interest on short term and long term investments and on bank deposits and of gain on early retirement of our convertible subordinated notes. Financial expense consists primarily of interest payments in respect of convertible subordinated notes and amortization of convertible subordinated notes issuance costs. In 2002, we recognized interest income of \$2.9 from a long-term loan we granted to Tikcro. Of this amount, \$1.9 million was for interest accrued in previous years.

Due to our adoption of FAS 145, effective January 1, 2002, we reclassified to financial income gains from the early retirement of our convertible subordinated notes that were previously recorded as an extraordinary gain. During 2003, we retired \$21.9 million principal amount of our convertible subordinated notes, resulting in a gain of \$3.1 million. During 2002, we retired \$28.2 million principal amount of our convertible subordinated notes, resulting in a gain of \$13.2 million. During 2001, we retired \$53.6 million principal amount of convertible subordinated notes, resulting in a gain of \$34.1 million. As of December 31, 2003, the total principal amount of convertible subordinated notes outstanding was \$16.2 million. On April 1, 2004, we completed the redemption of the remaining outstanding convertible subordinated notes at face value.

Financial income, net was \$33.4 million in 2001, \$17.6 million in 2002 and \$5.1 million in 2003. These fluctuations primarily reflect the principal amount of notes retired in the respective years and the prices at which they were retired.

Impact of Inflation, Devaluation and Fluctuation of Currencies on Results of Operations, Liabilities and Assets

A devaluation of the new Israeli shekel in relation to the U.S. dollar would have the effect of decreasing the dollar value of assets in New Israeli Shekels of Orckit, to the extent the underlying value is New Israeli Shekel-based. Such a devaluation also would have the effect of reducing the U.S. dollar amount of any liabilities of Orckit, which are payable in New Israeli Shekels (unless such payables are linked to the U.S. dollar).

Most of our sales are denominated in dollars and our expenses in New Israeli Shekels exceed our revenues received in New Israeli Shekels. Our expenses in new Israeli shekels are principally payroll. The results of operations of Orckit are adversely affected by increases in the rate of inflation in Israel when such increases are not offset by a corresponding devaluation of the new Israeli shekel against the U.S. dollar. For example, in 2003 the value of the U.S. dollar declined in relation to the New Israeli Shekels by 7.6%, while the rate of deflation was 1.9%. As a result, our salary expenses, which are primarily linked to the New Israeli Shekel, increased in U.S. dollar terms.

We are presently engaged in hedging transactions, mainly forward exchange contracts, intended to manage risks relating to foreign currency exchange rate fluctuations. We may, continue to enter into foreign currency derivatives, mainly forward exchange contracts, in order to protect our cash flows in respect of existing assets.

The following table presents information about the rate of inflation in Israel, the rate of devaluation of the NIS against the U.S. dollar, and the rate of inflation of Israel adjusted for the devaluation:

Years Ended December 31,	Israeli Inflation Rate	Israeli Devaluation Rate	Israel Inflation Adjusted for Devaluation
1999.....	1.3	(0.2)	1.5
2000.....	0.0	(2.7)	2.7
2001.....	1.4	9.3	(7.8)
2002	6.5	7.3	(0.8)
2003	(1.9)	(7.6)	5.7

B. LIQUIDITY AND CAPITAL RESOURCES

Orckit has financed its operations primarily through sales of equity, issuance of convertible notes and the receipt of grants to fund research and development, as well as from bank loan proceeds.

Our working capital (total current assets net of total current liabilities) decreased from \$103.9 million as of December 31, 2001 to \$55.2 million as of December 31, 2002 and further decreased to \$34.6 million in 2003. The decrease in our working capital has occurred primarily as a result of using our cash to fund our operating losses and to repurchase our convertible subordinated notes, as well as because of our decision to invest funds in long-term marketable securities, which are not included in working capital. In 2002, the decrease in working capital also resulted from downsizing steps taken by us, along with the move toward outsourcing of our manufacturing processes, which resulted in a decrease in our inventories.

We had cash, cash equivalents, long-term marketable securities and bank deposits of \$79.5 million as of December 31, 2003 compared to \$116.6 million as of December 31, 2002. The majority of this amount was held in securities denominated in U.S. dollars.

We anticipate that our operating expenses will be a material use of our working capital resources for the foreseeable future. In addition, we used approximately \$16.2 million in cash in April 2004 to redeem the remaining outstanding convertible subordinated notes. We believe that we have sufficient working capital to meet our anticipated capital requirements for 2004 and 2005. If we do not have available sufficient cash to finance our operations, we may be required to obtain equity or debt financing. We cannot be certain that we will be able to obtain additional financing on acceptable terms or at all.

Net Cash Provided by/Used in Operating Activities

In 2003, we used \$16.1 million of cash in operating activities, primarily as a result of our net loss, decreases in payables and non-cash gain from the early retirement of our convertible subordinated notes, offset in part by depreciation and impairment of property and equipment, amortization of deferred compensation related to employee stock option grants and trading marketable securities. In 2002, we generated \$6.7 million of cash from operating activities primarily as a result of decreases in inventories and receivables and depreciation and amortization, offset in part by the non-cash gain from the early retirement of our convertible subordinated notes and a decrease in payables. In 2001, we used \$2.0 million of cash in operating activities primarily as a result of the non-cash gain from the early retirement of our convertible subordinated notes and a decrease in payables offset in part by a decreases in inventories and receivables.

Net Cash Provided by/Used in Investing Activities

Our principal investing activity relating to our operations has been the purchase of equipment and other fixed assets used in our business. These purchases totaled \$2.4 million in 2001, \$1.8 million in 2002 and \$900,000 in 2003. Our capital expenditures in 2003 were primarily for the procurement of telecommunications equipment and related software tools. In 2003, our investing activities also included the receipt of \$26.3 million of marketable

securities, the receipt of \$7.0 million from Tikcro in repayment of our loan to Tikcro and the receipt of \$10.3 million from bank deposits. In 2002, our investing activities also included the purchase of \$35.6 million of marketable securities and the receipt of \$13.0 million from Tikcro in partial repayment of our loan to Tikcro.

Convertible Subordinated Notes

In March, 2000, we raised net proceeds of approximately \$120.5 million in a private placement of \$125 million aggregate principal amount of 5.75% convertible subordinated notes due on April 1, 2005. From 2000 to 2003, we repurchased an aggregate of \$108.8 million principal amount of our convertible subordinated notes for an aggregate of \$52.1 million. As a result, as of December 31, 2003, the total principal amount of our convertible subordinated notes outstanding was \$16.2 million. On April 1, 2004, we completed the redemption of the remaining outstanding notes at face value. The repurchases of convertible subordinated notes constituted our primary use of cash in financing activities in 2001, 2002 and 2003.

On March 30, 2004, we borrowed \$16.0 million from a bank in order to finance the early redemption of our convertible subordinated notes. This borrowing bears interest at a rate between 2.08% and 2.17% until the maturity of this loan by July 2005. We intend to repay this loan from the proceeds of our long term marketable securities.

Loan to Tikcro

As part of the spin-off of Tikcro, we loaned \$20 million to Tikcro at an interest rate of approximately 6% per annum. The loan was required to be repaid by March 1, 2005. In 2001, we agreed to defer interest on this loan in an aggregate amount of \$1.9 million. In 2002, Tikcro repaid \$13.0 million of the principal of this loan from the proceeds of a transaction it entered into with STMicroelectronics. In May 2003, Tikcro announced the closing of the sale of its remaining operating assets to STMicroelectronics. Promptly thereafter, Tikcro repaid the remaining amounts outstanding under this loan.

Repurchases of our Ordinary Shares

During 2003, we repurchased for \$5.6 million in cash approximately 882,000 of our ordinary shares, of which 616,590 shares were repurchased from Clal Electronics Industries Ltd. in a private transaction. See Item 7.B – “Related Party Transactions.” The other shares repurchased were bought in the open market. No additional repurchases are currently authorized.

Government and Other Grants

The Government of Israel encourages research and development projects through the Office of Chief Scientist of the Israeli Ministry of Industry and Trade, pursuant to the Law for the Encouragement of Industrial Research and Development, 1984, commonly referred to as the “R&D Law”. Under the R&D Law, a research and development plan that meets specified criteria is eligible for a grant of up to 50% of certain approved research and development expenditures. The plan must be approved by the Office of the Chief Scientist.

Since our inception, we have relied on grants from the Office of the Chief Scientist for the financing of a portion of our product development expenditures. During the three

years ended December 31, 2003, we recorded research and development grants in an aggregate amount of approximately \$12.1 million. As of December 31, 2003, total contingent liabilities to the Office of the Chief Scientist were approximately \$12.0 million. We expect that the Office of the Chief Scientist will approve our applications for grants also for 2004, though at lower amounts than in the past.

Under the terms of the grants we received from the Office of Chief Scientist, we are obligated to pay royalties of 3% during the first three years following commencement of royalty payments, and 4% to 5% thereafter. Royalties are payable up to 100% of the amount of such grants, linked to the U.S. Dollar, plus annual interest at LIBOR. The payment of royalties is on all revenues received in connection with the sale of the products developed pursuant to the funded plans, including revenues licensed ancillary services. These terms are applicable to our Office of Chief Scientist grants that have been approved since January 1, 2000.

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

The R&D Law also provides that know-how developed under an approved research and development program may not be transferred to third parties in Israel without the approval of the research committee. Such approval is not required for the export of any products resulting from such research or development. The R&D Law further provides that the know-how developed under an approved research and development program may not be transferred to any third parties outside Israel.

The R&D Law imposes reporting requirements with respect to certain changes in the ownership of a grant recipient. The law requires the grant recipient and its controlling shareholders and interested parties to notify the Office of the Chief Scientist of any change in control of the recipient or a change in the holdings of the means of control of the recipient that results in a non-Israeli becoming an interested party directly in the recipient and requires the new interested party to undertake to the Office of the Chief Scientist to comply with the R&D Law. In addition, the rules of the Office of the Chief Scientist may require prior approval of the Office of the Chief Scientist or additional information or representations in respect of certain of such events. For this purpose, "control" is defined as the ability to direct the activities of a company other than any ability arising solely from serving as an officer or director of the company. A person is presumed to have control if such person holds 50% or more of the means of control of a company. "Means of control" refers to voting rights or the right to appoint directors or the chief executive officer. An "interested party" of a company includes a holder of 5% or more of its outstanding share capital or voting rights, its chief executive officer and directors, someone who has the right to appoint its chief executive

officer or at least one director, and a company with respect to which any of the foregoing interested parties owns 25% or more of the outstanding share capital or voting rights or has the right to appoint 25% or more of the directors. Accordingly, any non-Israeli who acquires 5% or more of our ordinary shares will be required to notify the Office of the Chief Scientist that it has become an interested party and to sign an undertaking to comply with the R&D Law.

Effective Corporate Tax Rates in Israel

Under the Law for Encouragement of Capital Investments, 1959, known as the Investments Law, by virtue of the "approved enterprise" status granted to some of our investment programs, we are entitled to various tax benefits. The period of tax benefits is seven years, commencing in the first year in which we earn taxable income from the approved enterprise, subject to certain limitations. Under this law, the taxable income of Orckit derived from an investment program designated as an Approved Enterprise is fully exempt from corporate tax for a period of two years, after which the income from these enterprises is taxable at the rate of up to 25% for the remainder of the period of tax benefits five years.

After the applicable benefit period expires, income generated from these Approved Enterprise programs (including income generated from the grant of a usage right with respect to know-how developed by the Approved Enterprise, income generated from royalties and income derived from a service which is auxiliary to such usage right or royalties, provided that such income is generated within the Approved Enterprise's ordinary course of business) will be subject to tax at the full corporate tax rate, currently 36%. We may apply for additional programs or for an extension of our existing programs; however, there can be no assurance that our application will be approved or that we will receive future benefits. The Investments Law is scheduled to expire on June 30, 2004. Accordingly, requests for new programs or expansions that are not approved on or before June 30, 2004 will not confer any tax benefits, unless the term of the Investments Law is extended. Part of our income has been generated through our Approved Enterprises. Should a company that has elected the "alternative package" distribute to its shareholders a cash dividend from tax-exempt income attributable to it, it would incur a tax liability on the amount distributed at the rate (10% to 25%) which would have been applicable had the company not elected the alternate package and it will have to withhold tax at the rate of 15% with respect to the dividend distributed. Orckit's taxes outside of Israel, mainly in the United States, are dependent on our operations in each jurisdiction as well as relevant laws and treaties. See "Item 18 Financial Statements". Under Israeli tax law, at December 31, 2003, we had accumulated losses for tax purposes amounting to approximately \$130 million. These losses are available indefinitely to offset future taxable business income. As of December 31, 2003, our carry forward capital losses for tax purposes were \$40 million.

Reform of the Israeli Tax Regime

In 2002, the Israeli government approved an amendment to the Income Tax Ordinance. The tax reform, effective as of January 1, 2003, reforms certain parts of the Israeli tax system, including, among others, the reduction of the tax rate levied on capital gains (other than gains from the sale of listed securities) derived on or after January 1, 2003, to a general rate of 25% for both individuals and corporations. See Item 10 below "*Additional Information – Taxation – Israel - Tax Reform*" for a discussion of the main aspects of the tax reform.

Dividend Policy

On June 30, 2000, we distributed a stock dividend on a share-for-share basis of all our shares of Tikcro. We have never declared or paid cash dividends on our capital stock. In the foreseeable future, we intend to use any future earnings for the operation and expansion of our business. Accordingly, we do not anticipate paying any cash dividends. Payment of future dividends, if any, will be at the discretion of our board of directors and the audit committee thereof and will depend on various factors, such as our statutory retained earnings, financial condition, operating results and current and anticipated cash needs.

If we declare cash dividends, we will pay those dividends in new Israeli shekels. Current Israeli law permits holders of our ordinary shares who are non-residents of Israel and who acquired their shares with a non-Israeli currency to repatriate all distributions on these shares in that non-Israeli currency.

Inventory

Inventory consists primarily of raw materials for the assembly of our products. Our inventory as of December 31, 2003 and 2002 was \$100,000. There was no change in the amount of our inventory in the years 2002 and 2003 because production units were reduced. As we prepare for commercial selection and increase of product sales, we expect that inventory levels will increase.

C. RESEARCH AND DEVELOPMENT

We focus our research and development efforts on developing new products that address the need for solutions capable of supporting very high bandwidth services in telecommunications networks in metropolitan areas and products that enable fiber-speed broadband services over copper, mainly targeting business users. We obtain extensive product development input from potential users and through participation in industry organizations and standards-setting bodies, such as the American National Standards Institute and the European Telecommunications Standards Institute.

As of December 31, 2003, our research and development staff consisted of 118 employees, most of whom are located in Israel and hold engineering or other advanced technical degrees. Our gross research and development expenses were approximately \$22.4 million in 2001, \$22.3 million in 2002 and \$20.8 million in 2003. These expenses were offset by grants from the Office of the Chief Scientist of the Ministry of Industry and Trade of the Government of Israel of approximately \$3.3 million in 2001, \$3.0 million in 2002 and \$5.8 million in 2003.

We expect that we will continue to commit substantial resources to research and development in the future. Our research and development staff consisted of 113 employees as of December 31, 2001, 103 employees as of December 31, 2002 and 118 employees as of December 31, 2003. As of December 31, 2003, the majority of our research and development employees were employed by Corrigo. The number of research and development employees was similar in the years 2001 through 2003 since we maintained similar research and development efforts, focusing on Corrigo's and Spediant's product lines. We believe that a continued commitment to research and development is required to maintain our technical excellence and launch new innovative products in the metro transport and access markets. We expect that our research and development expenses will increase if

our applications for Office of Chief Scientist grants are not approved or partially approved, or if we elect not to receive these grants.

D. TREND INFORMATION

The deterioration beginning in late 2000 of economies around the world was followed by a significant decline in capital expenditures of telecom carriers from 2001 throughout 2002. Capital investment expenditures of wireline telecom carriers were flat in 2003 compared with 2002. There is still uncertainty with respect to the direction of the economy in our target markets and the telecommunications market. It is expected that capital investment of wireline telecom carriers in 2004 will be similar to the levels of 2003. In response to this trend, we have reduced the number of our employees and have focused our attention and resources on developing and marketing Corrigent's and Spediant's products. We will need to complete the development and further enhance these new products and attract new customers if we are to generate revenues.

E. OFF-BALANCE SHEET ARRANGEMENTS

We do not have any "off-balance sheet arrangements" as such term is defined in Item 5E of Form 20-F.

F. TABULAR DISCLOSURE OF CONTRACTUAL OBLIGATIONS

The following table of our material contractual obligations as of December 31, 2003 summarizes the aggregate effect that these obligations are expected to have on our cash flows in the periods indicated

Contractual Obligations	Payment due by period (\$ in thousands)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-Term Debt Obligations	16,238	--	16,238¹	--	--
Operating Lease Obligations	290	--	290²	--	--
Purchase Obligations	700	700	--	--	--
Other Long-Term Liabilities Reflected on our Balance Sheet under U.S. GAAP	12,421	8,986³	--	--	3,435⁴
Total	29,649	9,686	16,528	--	3,435

- ¹ This amount reflects the balance of our Convertible Subordinated Notes as of December 31, 2003. These notes were redeemed in full on March 31, 2004. On March 30, 2004, we incurred a bank loan in the principal amount of \$16.0 million to finance the early redemption of the notes.
- ² Our premises leases allow for early termination upon six months' prior notice. Accordingly, this amount reflects lease payments for the applicable notice period. For total projected annual rent payments, see note 6b to our financial statements for the year ended December 31, 2003. The amount is presented in the 1-3 years column since this is the average life period of our lease obligations.
- ³ This amount reflects the trade payables, accrued expenses and other payables presented in our balance sheet.
- ⁴ This amount reflects our accrued severance pay liability. The time of its payment, in whole or in part, cannot be predicted and as such this amount is presented in the more than 5 years column. Out of this amount, \$2.7 million have been previously funded by our contributions to employee plans.

In addition, as of December 31, 2003, our contingent liability to the Office of the Chief Scientist in respect of grants received was approximately \$12.0 million. This liability is required to be repaid only as royalties based on revenues derived from products whose development was funded with these grants.

ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

A. DIRECTORS AND SENIOR MANAGEMENT

The following table sets forth certain information with respect to Orckit's directors and executive officers.

<u>Name</u>	<u>Age</u>	<u>Position</u>
Eric Paneth	54	Chairman of the Board and Chief Executive Officer
Izhak Tamir	51	President and Director
Ehud Rokach	40	Chief Executive Officer of Corrigent Systems
Aviv Boim	37	Chief Financial Officer
Eran Tamir	47	Vice President Operations
Yoav Wechsler	49	Vice President, Research and Development of Corrigent Systems
Leon Bruckman	46	Vice President, Chief System Architecture of Corrigent Systems
Eli Magal	38	Vice President, Research and Development of access products
Haim Volinsky	48	Vice President, Sales and Marketing of access products
Yair Shamir	58	Outside Director
Miri Gelbman	52	Outside Director
Moshe Nir	54	Outside Director
Jed M. Arkin	40	Director
Moti Motil	51	Director

The business experience of each of our directors and executive officers is as follows:

Mr. Paneth has been Chairman of the Board of Directors and Chief Executive Officer of Orckit since its founding in 1990. From 1975 until 1983, Mr. Paneth was a senior engineer in the Israeli Government, and from 1985 to 1990, was a technical department head in the Israeli Government. From 1983 until 1985, he was employed by Linkabit Inc., in San Diego,

California. Mr. Paneth holds an advanced engineering degree from the Israel Institute of Technology, commonly known as the Technion. Since January 2000, Mr. Paneth has been a director of Tikcro Technologies Ltd.

Mr. I. Tamir has been President and a Director of Orckit since its founding in 1990. From 1987 until 1989, Mr. Tamir was employed by Comstream Inc., in San Diego, California. From 1985 until 1987, he was vice president of A.T. Communication Channels Ltd., a subsidiary of Bezeq. From 1978 to 1985, he was a senior engineer in the Israeli Government. Mr. Tamir holds an engineering degree from the Technion and an M.B.A. from Tel Aviv University. Since January 2000, Mr. Tamir has been chairman of the board of directors of Tikcro Technologies Ltd.

Mr. Rokach joined Orckit in 1992 and has served as Chief Operating Officer of Orckit since February 2000 and as Chief Executive Officer of Corrigent Systems since October 2000. From 1998 to 2000, Mr. Rokach served as Vice President—Network Access Systems. From 1992 to 1998, Mr. Rokach held several research and development and other positions with Orckit. From 1987 to 1992, he was a senior engineer with the Israeli Government. Mr. Rokach holds an engineering degree from the Technion.

Mr. Boim joined Orckit as Chief Financial Officer in February 1998. From August 1996 until February 1998, he was an associate of BT Alex. Brown Incorporated, an investment banking firm. From August 1993 until August 1996, Mr. Boim was a vice president of Giza Ltd., Tel Aviv, an investment banking firm. Mr. Boim holds a B.A. and an M.A. in economics and management from Tel Aviv University and a L.L.B. from Tel Aviv University Law School.

Mr. E. Tamir joined Orckit as Vice President Operations in April 2000. From 1996 until 2000, Mr. E Tamir who was one of founders of Wizcom Technologies Ltd., served as vice president operations of Wizcom. From 1990 until 1996, Mr. E Tamir served as director of worldwide logistics of Indigo Ltd. From 1985 to 1990, Mr. E Tamir served as director of acquisitions of Scitex Corporation Ltd. Mr. E Tamir holds a BsCEE in machine engineering from Tel Aviv University and is a business economics graduate of the Israeli Institute for Management.

Mr. Wechsler joined Orckit in October 2000 as Vice President of research and development of Corrigent Systems. From August 1999 to July 2000, he served as research and development director at One Path Networks. From September 1997 to August 1999, Mr. Wechsler held engineering management positions at ADC Teledata. Mr. Wechsler holds a B.Sc. and an M.Sc. in Electrical Engineering from the Technion.

Mr. Bruckman joined Orckit in 1999 and has served as Vice President of system engineering since November 1999 and as Vice President and Chief System Architect of Corrigent Systems since September 2000. From April 1996 to October 1999, Mr. Bruckman was Vice President of research and development and system engineering at HyNEX, which was acquired by Cisco. From August 1982 to March 1996, Mr. Bruckman held several positions with the access division of Tadiran Telecommunications, of which the last position was director of research and development. Mr. Bruckman holds a B.Sc. in Electrical Engineering from the Technion Institute and an MBA from Bar-Ilan University, Israel.

Mr. Magal joined Orckit in 1995 and held various engineering management positions until becoming Vice President of research and development of access products in 2001. Mr.

Magal holds a B.S. in Electrical Engineering from the Technion and an M.B.A. from Tel Aviv University.

Mr. *Volinsky* joined Orckit in November 2001 and has served as Vice President sales and marketing of access products. From September 2000 until October 2001, Mr. Volinsky served as a marketing director at Cisco Systems. From 1997 until 2000, Mr. Volinsky served as a Co-General manager and VP of marketing and sales at HyNEX, which was acquired by Cisco. Mr. Volinsky holds a B.Sc. degree from Tel-Aviv University in electrical and electronics engineering.

Mr. *Shamir* has been a Director of Orckit since October 1995. Mr. Shamir serves as the Chairman of the Board and Chief Executive Officer of VCON Telecommunications Ltd., an Israeli technology company listed on *Le Nouveau Marche* in France. Prior to being appointed Chairman of the Board in 2001, Mr. Shamir served as President and as one of VCON's directors since 1997 and as its Chief Executive Officer since 1998. Since April 2000, Mr. Shamir has also served as chairman of Catalyst Investment L.P., an Israeli venture capital firm. From July 1995 through February 1997, Mr. Shamir served as the Executive Vice President of The Challenge Fund LLP, the general partner of the Challenge Fund-Etgar, L.P. From December 1993 to July 1995, he served as the Chief Executive Officer of Elite Food Industries Ltd. Mr. Shamir served as Executive Vice President and general manager of Israel operations of Scitex Corporation Ltd. from February 1988 through December 1994. Mr. Shamir is a director of Mercury Interactive Corp., DSP Group Corporation and Poalim Capital Markets. Mr. Shamir holds a B.Sc. in Electrical Engineering from the Technion and has served on the board of governors of the Technion since 1993.

Ms. *Gelbman* has served since 1999 as founder and General Manager of Milgal Ltd., an Israeli privately-owned appliance distribution and service company. From 1984 to 1998, she was employed by IBM Israel in various positions. Her last role with IBM was as Manager of Quality and Customer Relationship Management (CRM).

Mr. *Nir* has served since 1990 as Founder and CEO of privately-held Business Directions Ltd., a distributor of analytic management software. From 1985 to 1990, he served as manager of the economics and control department and member of the Executive Board of Elite Industries Ltd., a publicly traded food manufacturer in Israel. From 1974 to 1985, he held senior financial and control positions with Tempo Breweries and Soft Drinks Ltd., Tadiran Electronics Industries Ltd. and Clal Israel Ltd. He holds a BA in economics from Tel Aviv University, and an MBA and Post Graduate Diploma in Computer and Information Sciences from the Recanati School of Management, Tel Aviv University

Mr. *Motil* has served since 1996 as Vice President Finance and an associate of Palmot Ltd., an investment company based in Israel. From 1991 until 1996, he served as Chief Financial Officer of the Israeli subsidiary of Jan-Bell Marketing Inc., a retail company. Mr. Motil holds a B.A degree in economics and accounting from Tel-Aviv University and he is a C.P.A.

Mr. *Arkin* has served as Chairman of PeerPressure, Inc., a company that provides peer-to-peer content protection systems, since January 2000 and as Chairman of Madah Com Communications Ltd., a spread-spectrum communications company, since January 2000. From 1999 to 2001, he served as General Manager of merchant banking for Oscar Gruss & Son, a New York-based investment bank. From 1995 to 1998, Mr. Arkin served as Vice President of The Challenge Fund, an Israeli venture capital firm. He holds a B.A. from St.

John's College in Annapolis, Maryland, an M.B.A. from Harvard Business School and a J.D. from Harvard Law School.

There are no family relationships between any of our directors or executive officers. There are no arrangements or understandings between any of our directors or executive officers and any other person pursuant to which our directors or executive officers were selected.

B. COMPENSATION

The aggregate direct remuneration paid by Orckit to all persons as a group (14 persons) who served in the capacity of director or executive officer in 2003 was approximately \$ 2.1 million, which includes \$380,000 of pension, retirement or similar benefits, expenses reimbursed (including professional and other business association dues and expenses) and other fringe benefits. In 2003, we granted to this group options to purchase an aggregate of 100,000 ordinary shares under the Orckit Israeli Share Incentive Plan. These options have vesting periods of four years and an exercise price of \$3.30 per share, which represented the market price of our ordinary shares on the date of grant.

C. BOARD PRACTICES

Nasdaq Requirements

Under the listing requirements of the Nasdaq Stock Market, we are required to have an audit committee, all of whose members are "independent" as defined in Nasdaq's rules. Five out of the seven members of our board of directors, namely, Messrs. Shamir, Arkin, Gelbman, Nir and Motil, are independent directors under the Nasdaq requirements. Messrs. Shamir, Gelbman, Nir and Motil are the sole members of our audit committee.

Israeli Companies Law

We are also subject to the provisions of the Israeli Companies Law, 5759-1999, and regulations adopted thereunder.

Board of Directors

According to the Companies Law and our articles of association, the oversight of the management of our business is vested in our board of directors. The board of directors may exercise all powers and may take all actions that are not specifically granted to our shareholders. As part of its powers, our board of directors may cause us to borrow or secure payment of any sum or sums of money for our purposes, at times and upon terms and conditions as it thinks fit, including the grant of security interests in all or any part of our property. Our board of directors may consist of between three and seven directors and currently consists of seven directors.

Our directors are elected at annual meetings of shareholders by a vote of the holders of at least 66-2/3% of the ordinary shares voting thereon. Directors generally hold office until the next annual meeting of shareholders. Our annual meeting of shareholders is required to be held at least once during every calendar year and not more than fifteen months after the last preceding meeting. The board of directors generally may temporarily fill

vacancies in the board. Directors may be removed earlier from office by a resolution passed at a general meeting of shareholders by a vote of the holders of at least 75% of the ordinary shares voting thereon.

A resolution proposed at any meeting of the board of directors is deemed adopted if approved by a majority of the directors present and voting on the matter.

Outside Directors

Qualifications of Outside Directors

Under the Israeli Companies Law, companies incorporated under the laws of Israel whose shares are listed for trading on a stock exchange or have been offered to the public in or outside of Israel are required to appoint at least two outside directors. Pursuant to our articles of association, we may appoint up to three outside directors. The Companies Law provides that a person may not be appointed as an outside director if the person or the person's relative, partner, employer or any entity under the person's control has, as of the date of the person's appointment to serve as an outside director, or had, during the two years preceding that date, any affiliation with:

- the company;
- any entity controlling the company; or
- any entity controlled by the company or by its controlling entity.

The term affiliation includes:

- an employment relationship;
- a business or professional relationship maintained on a regular basis;
- control; and
- service as an office holder, excluding service as an office holder during the three-month period in which the company first offers its shares to the public.

The Companies Law defines the term "office holder" of a company to include a director, the chief executive officer and any officer of the company who reports directly to the chief executive officer.

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

Until two years from termination of office, a company may not engage an outside director to serve as an office holder and cannot employ or receive services from that person, either directly or indirectly, including through a corporation controlled by that person.

Election of Outside Directors

Outside directors are elected at meetings of shareholders by a vote of the holders of at least 66-2/3% of the ordinary shares voting thereon, provided that either:

- at least one third of the shares of non-controlling shareholders voted at the meeting vote in favor of the outside director's election; or
- the total number of shares of non-controlling shareholders that voted against the election of the outside director does not exceed one percent of the aggregate voting rights in the company.

The initial term of an outside director is three years and may be extended for an additional three years. Outside directors may be removed from office only by a vote of the holders of at least 66-2/3% of the ordinary shares voting thereon, or by a court, and only if the outside directors cease to meet the statutory qualifications for their appointment or if they violate their duty of loyalty to the company. Each committee of a company's board of directors that exercises a power of the board of directors is required to include at least one outside director, except for the audit committee, which is required to include all the outside directors. Our outside directors are: Mr. Shamir, who was re-elected to a second three-year term in 2003, and Ms. Gelbman and Mr. Nir, who were elected in 2002.

Committees

Subject to the provisions of the Companies Law, our board of directors may delegate its powers to committees consisting of board members. Our board has formed an audit committee and an option committee.

Audit Committee

Israeli Companies Law Requirements

Under the Israeli Companies Law, our board of directors is required to appoint an audit committee, comprised of at least three directors, including all of the outside directors, but excluding:

- the chairman of our board of directors;
- a controlling shareholder or a relative of a controlling shareholder; and
- any director employed by us or who provides services to us on a regular basis.

The role of the audit committee is to identify flaws in the management of our business, including in consultation with the internal auditor and our independent accountants, to suggest remedial measures and to approve specified related party transactions. Our audit committee consists of Mr. Yair Shamir, Mr. Moshe Nir, Ms. Miri Gelbman and Mr. Moti Motil.

Nasdaq Requirements

We have adopted an audit committee charter as required by the Nasdaq rules. Our audit committee assists the board of directors in fulfilling its responsibility for oversight of

the quality and integrity of our accounting, auditing and financial reporting practices and financial statements and the independence qualifications and performance of our independent auditors. The audit committee also has the authority and responsibility to oversee our independent auditors, to recommend for shareholder approval the appointment and, where appropriate, replacement of our independent auditors and to pre-approve audit fees and all permitted non-audit services and fees.

Approval of Related Party Transactions

Under the Companies Law and the rules of Nasdaq, the approval of the audit committee is required to effect specified related-party transactions. Under the Companies Law, the audit committee may not approve an action or a transaction with related parties or with its office holders unless at the time of approval at least two outside directors are serving as members of the audit committee and at least one of whom was present at the meeting in which any approval was granted.

Option Committee

Our Option Committee administers our share option plan and is empowered, among other things, to recommend to our Board of Directors option grants, optionees, dates of grant and the exercise price of options. Messrs. Eric Paneth, Izhak Tamir and Yair Shamir are currently the members of our option committee.

Internal Auditor

Under the Companies Law, our board of directors is required to appoint an internal auditor proposed by the audit committee. The role of the internal auditor is to examine, among other things, whether our actions comply with the law and orderly business procedure. The internal auditor may not be an interested party, an office holder, or a relative of any of the foregoing, nor may the internal auditor be our independent accountant or its representative.

The Companies Law defines the term “interested party” to include a person who:

- holds 5% or more of our outstanding share capital or voting rights;
- has the right to appoint one or more directors or the general manager; or
- who serves as a director or as the general manager.

Approval of Specified Related Party Transactions Under Israeli Law

Fiduciary Duties of Office Holders

The Israeli Companies Law imposes a duty of care and a duty of loyalty on all office holders of a company. The duty of care requires an office holder to act with the level of care with which a reasonable office holder in the same position would have acted under the same circumstances. The duty of care includes a duty to use reasonable means to obtain:

- information on the advisability of a given action brought for his approval or performed by him by virtue of his position; and
- all other important information pertaining to these actions.

The duty of loyalty of an office holder includes a duty to:

- refrain from any conflict of interest between the performance of his duties for the company and the performance of his other duties or his personal affairs;
- refrain from any activity that is competitive with the company;
- refrain from exploiting any business opportunity of the company to receive a personal gain for himself or others; and
- disclose to the company any information or documents relating to a company's affairs which the office holder has received due to his position as an office holder.

Disclosure of Personal Interest of an Office Holder

The Israeli Companies Law requires that an office holder of a company disclose to the company any personal interest that he may have and all related material information known to him, in connection with any existing or proposed transaction by the company. The disclosure is required to be made promptly and in any event no later than the board of directors meeting in which the transaction is first discussed. If the transaction is an extraordinary transaction, the office holder must also disclose any personal interest held by:

- the office holder's spouse, siblings, parents, grandparents, descendants, spouse's descendants and the spouses of any of these people; or
- any corporation in which the office holder is a 5% or greater shareholder, director or general manager or in which he has the right to appoint at least one director or the general manager.

Under Israeli law, an extraordinary transaction is a transaction that is:

- not in the ordinary course of business;
- not on market terms; or
- likely to have a material impact of the company's profitability, assets or liabilities.

Once an office holder complies with the above disclosure requirement, the board of directors may approve a transaction between the company and an office holder, or a third party in which an office holder has a personal interest. A transaction that is adverse to the company's interest may not be approved.

If the transaction is an extraordinary transaction, approval of both the audit committee and the board of directors is required, in that order. Under specific circumstances,

shareholder approval may also be required. A director who has a personal interest in a proposed extraordinary transaction which is considered at a meeting of the board of directors or the audit committee may not be present at this meeting or vote on this matter, unless a majority of the members of the board of directors or the audit committee, as the case may be, has a personal interest in the matter. If a majority of members of the board of directors have a personal interest therein, shareholder approval is also required.

Disclosure of Personal Interests of a Controlling Shareholder

Under the Israeli Companies Law, the disclosure requirements which apply to an office holder also apply to a controlling shareholder of a public company. A controlling shareholder is a shareholder who has the ability to direct the activities of a company, including a shareholder that owns 25% or more of the voting rights if no other shareholder owns more than 50% of the voting rights, but excluding a shareholder whose power derives solely from his or her position on the board of directors or any other position with the company. Extraordinary transactions with a controlling shareholder or with a third party in which a controlling shareholder has a personal interest, and the terms of engagement of a controlling shareholder as an office holder or employee, require the approval of the audit committee, the board of directors and the shareholders of the company, in that order. The shareholder approval must be by a majority of the shares voted on the matter, provided that either:

- at least one-third of the shares of shareholders who have no personal interest in the transaction and who vote on the matter vote in favor thereof; or
- the shareholders who have no personal interest in the transaction who vote against the transaction do not represent more than one percent of the voting rights in the company.

For information concerning the direct and indirect personal interests of our office holders and principal shareholders in specified transactions with us, see Item 7A of this Annual Report.

D. EMPLOYEES

The numbers and breakdowns of our employees as of the end of the past three years are set forth in the following table:

	As of December 31,		
	2001	2002	2003
Numbers of employees by geographic location			
Israel	210	172	157
United States	6	11	11
Elsewhere	0	0	2
Total workforce	216	183	170

	As of December 31,		
	2001	2002	2003
Numbers of employees by category of activity			
MIS, finance and administration	43	45	32
Research and development	113	103	118
Manufacturing, testing and quality assurance	39	18	4
Sales and marketing	21	17	16
Total workforce	216	183	170

We had fewer employees as of December 31, 2002 than in December 31, 2001 as a result of reduction of the number of employees in operations, R&D and sales and marketing due to the deterioration of economies around the world and decrease in revenues from our legacy DSL business. On December 31, 2003 the number of employees was similar to December 31, 2002 as there was no substantial change in the scope of research and development, marketing and accompanying activities.

We believe that we have been able to attract talented engineering and other technical personnel. None of our employees is represented by a labor union and we have not experienced a work stoppage. We believe that our relationship with our employees is good and that our future success will depend on a continuing ability to hire, assimilate and retain qualified employees.

Certain provisions of the collective bargaining agreements between the Histadrut (General Federation of Labor in Israel) and the Coordination Bureau of Economic Organizations, including the Industrialists Associations, are applicable to our employees by order of the Israeli Ministry of Labor and Welfare. These provisions principally concern cost of living increases, recreation pay and other conditions of employment.

Israeli labor laws and regulations are applicable to all of our employees in Israel. The laws principally concern matters such as paid annual vacation, paid sick days, the length of the workday, payment for overtime, insurance for work-related accidents, severance pay and other conditions of employment. Israeli law generally requires severance pay, which may be funded, in whole or in part, by Managers' Insurance described below, in certain circumstances, including the retirement or death of an employee or termination of employment without cause, as defined under Israeli law. The payments thereto amount to approximately 8.3% of wages. Furthermore, Israeli employees are required to pay predetermined sums to the National Insurance Institute. The payments to the National Insurance Institute are approximately 16% of wages of which the employee contributes approximately 66% and the employer contributes approximately 34%.

A general practice followed by Orckit, although not legally required, is the contribution of funds on behalf of most of its employees to a fund known as Managers' Insurance. This fund provides employees with a lump sum payment upon retirement or with payments on account of severance pay, if legally entitled, upon termination of employment. Each employee who agrees to participate in the Managers' Insurance plan contributes an amount equal to 5% of such employee's base salary and the employer contributes approximately 15% of such salary, which 15% includes the 8.3% for severance pay.

E. SHARE OWNERSHIP

As of March 31, 2004, Messrs. Eric Paneth and Izhak Tamir, each, directly or through a wholly owned company, beneficially owns 751,771 ordinary shares, or 16.7% of our ordinary shares, including (i) options to purchase 18,750 of our ordinary shares at no exercise price per share and (ii) the right to purchase 140,000 shares from us, at any time or from time to time in one or more purchases, until February 2005. The purchase price for the ordinary shares under such right to purchase will be equal to the average closing price of our ordinary shares on Nasdaq over the ten trading days immediately preceding the purchase date, plus a premium of 10%. Except for Messrs. Paneth and Tamir, none of our executive officers or directors beneficially owns 1% or more of our outstanding ordinary shares.

At December 31, 2003, outstanding options to purchase a total of 674,639 ordinary shares were granted by us pursuant to our share incentive plan, of which options to purchase a total of 336,703 ordinary shares were held by our directors and officers (14 persons) as a group. Our share incentive plan is administered by an option committee of our board of directors, which is empowered, among other things, to recommend to our board of directors the optionees, dates of grant and the exercise price of options. Unless otherwise decided by our board of directors or the option committee, options granted under the share incentive plan are non-assignable except by the laws of descent. The outstanding options are exercisable at purchase prices which range from \$0 to \$60 per share, vest mainly over up to periods of five years, and have expiration dates which range from 2004 to 2012.

In January 2003, our board of directors adopted the "Orckit Communications Ltd. 2003 Subsidiary Employee Share Incentive Plan". Shares issued pursuant to this plan are issued to employees and consultants of our majority-owned subsidiaries for no consideration and are subject to reverse vesting. Unvested shares issued pursuant to this plan may be reacquired by us under certain circumstances or may be exchanged for shares or options of the applicable subsidiary under certain circumstances at the election of Orckit or the employees. Our directors are not entitled to participate in this plan. During 2003, 60,000 shares were forfeited and 540,000 shares were exchanged for options to purchase shares of subsidiaries.

Subject to the approval of the Board of Directors of Orckit, Corrigent and Spediant, as the case may be, and based on the relative fair market value of each of the relevant companies, options granted by Corrigent and Spediant may be exercised for securities of Orckit. Each of Corrigent and Spediant has granted or reserved options representing approximately 30% of its fully diluted equity. See Item 4.A for further information with respect to the Corrigent and Spediant Stock Option Plan.

ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

A. MAJOR SHAREHOLDERS

To our knowledge, (A) we are not directly or indirectly owned or controlled (i) by another corporation or (ii) by any foreign government and (B) there are no arrangements, the operation of which may at a subsequent date result in a change in control of Orckit.

As of March 31, 2004, each of Eric Paneth and Izhak Tamir beneficially owns 16.7% of our ordinary shares and collectively beneficially own approximately 32.2% of our ordinary

shares. Accordingly, Messrs. Paneth and Tamir, if they voted together, may have the power to control the outcome of matters submitted to a vote of our shareholders, including the approval of significant change of control transactions.

The following table sets forth, as of March 31, 2004, the number of our ordinary shares, which constitute our only voting securities, beneficially owned by (i) all shareholders known to us to own more than 5% of our outstanding ordinary shares, and (ii) all of our directors and executive officers as a group. The voting rights of all major shareholders are the same. As of March 31, 2004, 4,348,386 of our ordinary shares were outstanding.

<u>Identity of Person or Group</u>	<u>Amount Owned</u>	<u>Percent of Class</u>
Eric Paneth ⁽¹⁾	751,771	16.7%
Izhak Tamir ⁽²⁾	751,771	16.7%
Hermes Investment Management, Ltd. ⁽³⁾	278,000	6.4%
All directors and executive officers as a group (14 persons)	1,598,370 ⁽⁴⁾	33.6%

(1)(2) Includes, in the case of each of Messrs. Tamir and Paneth: (i) 18,750 ordinary shares issuable upon the exercise of options that are currently vested or vest within the next 60 days and (ii) the right to purchase 140,000 shares from us, at any time or from time to time in one or more purchases until February 2005. Under such right to purchase, the purchase price for the ordinary shares will be equal to the average closing price of our ordinary shares on Nasdaq over the ten trading days immediately preceding the purchase date, plus a premium of 10%. As discussed in Item 6.E, securities held by Messrs. Tamir and Paneth of Corrigent may be exercised for shares of Orckit under certain circumstances.

(3) Information is derived from a Schedule 13G, dated November 26, 2003, of BT Pension Scheme, Royal Mail Pension Plan and Hermes Investment Management, Ltd. filed with the Securities and Exchange Commission.

(4) Includes 132,328 ordinary shares which may be purchased pursuant to options exercisable within sixty days following March 31, 2004. As discussed in Item 6.E, securities of Corrigent and Spediant held by directors and executive officers of Orckit may be exercised for shares of Orckit.

As of March 31, 2004, there were 35 holders of record of our ordinary shares in the United States who collectively held approximately 70% of our outstanding ordinary shares. The number of record holders in the United States is not representative of the number of beneficial holders nor is it representative of where such beneficial holders are resident since many of these ordinary shares were held of record by brokers or other nominees.

In January 2003, we repurchased from Clal Electronics Industries Ltd. 616,590 of our ordinary shares and \$12.5 million principal amount of our convertible subordinated notes. Prior thereto, Clal and its affiliates beneficially owned approximately 12.0% of our ordinary shares. Immediately following this transaction, we believe that Clal and its affiliates beneficially own less than 1% of our ordinary shares.

B. RELATED PARTY TRANSACTIONS

Founding Agreements for Corrigent Systems and Spediant Systems

In connection with the founding of Corrigent Systems and Spediant Systems, we entered into founding agreements with these subsidiaries established to undertake our new technology projects. Pursuant to these founding agreements, Orckit contributed and transferred to each subsidiary a team of employees and applicable assets and liabilities related to early stage initiation and development in the business area of each of the technology projects which were conducted prior to such founding. Under the founding agreements, the subsidiaries assumed all employment-related obligations, accrued benefits and severance pay of our employees who have become employees of the subsidiaries. In 2003, Orckit continued to fund Corrigent and Spediant. Certain of our directors, officers and employees have previously been granted securities in Corrigent and Spediant with a nominal exercise price.

Loan Agreement

As part of the plan of separation relating to the spin-off of Tikcro, we loaned to Tikcro \$20 million. This loan bore interest at a rate of approximately 6% per annum and was required to be repaid by March 1, 2005. In February 2002, Tikcro announced that it had entered into a set of agreements with ST Microelectronics, pursuant to which it was to receive certain funding. In 2002, we were repaid \$13.0 million of the principal of this loan and accrued interest due in the amount of \$2.9 million. In May 2003, Tikcro announced the closing of an asset purchase agreement pursuant to which ST Microelectronics acquired all of Tikcro's assets. After the closing of that transaction, Tikcro paid us the remaining amount outstanding under the loan.

Clal Electronics Industries Ltd.

In January 2003, we retired \$12.5 million principal amount of our convertible subordinated notes and repurchased 616,590 of our ordinary shares held by Clal for aggregate consideration of \$14.7 million.

Tikcro Management Agreement

Following the sale of Tikcro's business to STMicroelectronics in April 2003, we agreed to provide Tikcro administrative services. For the services rendered in 2003, Tikcro paid us \$50,000.

Siliquent Technologies

In October 2001, one of our technology projects, Siliquent Technologies, a provider of technology for the storage network applications industry, raised \$10.0 million in equity financing from third parties. Certain of our directors, officers and employees had previously been granted securities in Siliquent with a nominal exercise price. In 2003 we participated in follow on investment rounds in Siliquent and increased our investment by \$1.4 million. Orckit's ownership interest in Siliquent is immaterial.

We believe that any transactions involving affiliated parties were on terms no less favorable to us than could be obtained with non-affiliated parties.

C. INTERESTS OF EXPERTS AND COUNSEL

Not applicable

ITEM 8. FINANCIAL INFORMATION

See Item 18.

ITEM 9. THE OFFER AND LISTING

A. OFFER AND LISTING DETAILS

Our ordinary shares are quoted on the Nasdaq Stock Market and The Tel Aviv Stock Exchange under the symbol ORCT. The following table sets forth, for the periods indicated, the high and low sales prices of our ordinary shares as reported on the Nasdaq Stock Market. The price per share of our ordinary shares has been retroactively adjusted to reflect the one-for-five reverse share split effective as of November 27, 2002 and the spin-off of Tikcro on June 30, 2000, based on the ratio of our share price to Tikcro's share price on that date. This ratio allocated 44% of the price to Orckit and 56% to Tikcro.

<u>Calendar Year</u>	<u>Price Per Share</u>	
	<u>High</u>	<u>Low</u>
2003	\$23.60	\$2.95
2002	\$21.60	\$2.70
2001	\$21.25	\$5.40
2000	\$203.95	\$10.00
1999	\$85.55	\$30.25

<u>Calendar Period</u>	<u>Price Per Share</u>	
	<u>High</u>	<u>Low</u>
2004		
First Quarter	\$23.00	\$14.45
2003		
First Quarter	\$7.10	\$2.95
Second Quarter	\$10.04	\$6.50
Third Quarter	\$9.25	\$6.65
Fourth Quarter	\$23.60	\$7.32
2002		
First Quarter	\$21.60	\$9.65
Second Quarter	\$10.25	\$4.75
Third Quarter	\$5.80	\$3.10
Fourth Quarter	\$4.70	\$2.70

<u>Calendar Month</u>	<u>Price Per Share</u>	
	<u>High</u>	<u>Low</u>
2004		
March	\$16.71	\$14.45
February	\$18.99	\$14.92
January	\$23.00	\$17.25
2003		
December	\$20.69	\$16.21
November	\$23.60	\$13.92
October	\$15.15	\$7.32

The following table sets forth, for the periods indicated, the high and low sales prices of our ordinary shares as reported on the Tel Aviv Stock Exchange.

<u>Calendar Year</u>	<u>Price Per Share</u>	
	<u>High</u>	<u>Low</u>
2003	\$23.38	\$3.55

<u>Calendar Period</u>	<u>Price Per Share</u>	
	<u>High</u>	<u>Low</u>
2004		
First Quarter	\$23.64	\$15.07
2003		
First Quarter	\$7.14	\$3.55
Second Quarter	\$10.58	\$6.86
Third Quarter	\$9.25	\$7.00
Fourth Quarter	\$23.38	\$7.88

<u>Calendar Month</u>	<u>Price Per Share</u>	
	<u>High</u>	<u>Low</u>
2004		
March	\$16.67	\$15.07
February	\$18.78	\$15.27
January	\$23.64	\$18.78
2003		
December	\$20.86	\$16.82
November	\$23.96	\$14.77
October	\$14.98	\$7.88

The share prices as presented above in US dollars were originally denominated in New Israeli Shekels and were converted to US dollars using the average exchange rate between the US dollar and the New Israeli Shekels for the presented period.

The trading of our shares on the TASE in 2002 was insignificant and accordingly, we do not believe sales price information with respect to the limited trading of our ordinary shares on TASE in 2002 is meaningful.

B. *PLAN OF DISTRIBUTION*

Not applicable

C. *MARKETS*

Our ordinary shares are quoted on the Nasdaq Stock Market under the symbol ORCT.

D. *SELLING SHAREHOLDERS*

Not applicable

E. *DILUTION*

Not applicable

F. *EXPENSES OF THE ISSUE*

Not applicable

ITEM 10. *ADDITIONAL INFORMATION*

A. *SHARE CAPITAL*

Not applicable

B. *MEMORANDUM AND ARTICLES OF ASSOCIATIONS*

Objects and Purposes

We were first registered under Israeli law on January 22, 1990 as a private company, and, on July 22, 1996, became a public company. Our registration number with the Israeli registrar of companies is 52-004287-0. Our object is to engage, directly or indirectly, in any lawful undertaking or business whatsoever, including, without limitation, as stipulated in our memorandum of association, which was filed with the Israeli registrar of companies.

Transfer of Shares and Notices

Fully paid ordinary shares may be freely transferred pursuant to our articles of association unless the transfer is restricted or prohibited by another instrument. Unless otherwise prescribed by law, we will provide at least 21 calendar days' prior notice of any general shareholders meeting.

Dividend and Liquidation Rights

Dividends on our ordinary shares may be paid only out of profits and other surplus, as defined in the Companies Law, as of our most recent financial statements or as accrued over a period of two years, whichever is higher. Our board of directors, with the approval of our audit committee, is authorized to declare dividends, provided that there is no reasonable

concern that the dividend will prevent us from satisfying our existing and foreseeable obligations as they become due. In the event of our liquidation, after satisfaction of liabilities to creditors, our assets will be distributed to the holders of ordinary shares in proportion to their respective holdings. These dividend and liquidation rights may be affected by the grant of preferential dividends or distribution rights to the holders of a class of shares with preferential rights that may be authorized in the future.

Voting, Shareholders' Meetings and Resolutions

Holders of ordinary shares have one vote for each ordinary share held on all matters submitted to a vote of shareholders. Under the Companies Law and our articles of association, most resolutions of our shareholders require approval by a simple majority of the ordinary shares voting thereon. Amendments to our articles of association and the election of directors require approval of 66-2/3% of our ordinary shares voting thereon, and liquidation and the removal of directors (other than outside directors) require approval of 75% of our ordinary shares voting thereon.

These voting rights may be affected by the grant of any special voting rights to the holders of a class of shares with preferential rights that may be authorized in the future.

We have two types of general shareholders meetings: the annual general meetings and extraordinary general meetings. Directors are elected only at annual general meeting. These meetings may be held either in Israel or in any other place the board of directors determines. An annual general meeting must be held in each calendar year, but not more than 15 months after the last annual general meeting. Our board of directors may convene an extraordinary meeting, from time to time, at its discretion and is required to do so upon the request of shareholders holding at least 5% of our ordinary shares.

The quorum required for a meeting of shareholders consists of at least two shareholders present in person or by proxy who hold or represent between them at least 25% of the outstanding voting shares, unless otherwise required by applicable rules. Nasdaq generally requires a quorum of 33-1/3%, but we have received an exemption from that requirement based on the generally accepted business practice for companies in Israel to have a quorum requirement of 25%. A meeting adjourned for lack of a quorum generally is adjourned to the same day in the following week at the same time and place or any time and place as the chairman may designate with the consent of a majority of the voting power represented at the meeting and voting on the matter adjourned. At such reconvened meeting the required quorum consists of any two members present in person or by proxy, unless otherwise required by applicable rules. Pursuant to the requirements of Nasdaq, unless we obtain a further exemption from Nasdaq, the quorum required for any such adjourned meetings will be 25%.

Duties of Shareholders

Under the Companies Law, each and every shareholder has a duty to act in good faith in exercising his rights and fulfilling his obligations towards Orckit and other shareholders and to refrain from abusing his power in Orckit, such as in voting in the general meeting of shareholders on the following matters:

- any amendment to the articles of association;

- an increase of our authorized share capital;
- a merger; or
- approval of certain actions and transactions which require shareholder approval.

In addition, each and every shareholder has the general duty to refrain from depriving other shareholders of their rights.

Furthermore, any controlling shareholder, any shareholder who knows that it possesses the power to determine the outcome of a shareholder vote and any shareholder that, pursuant to the provisions of the articles of association, has the power to appoint or to prevent the appointment of an office holder in Orckit or any other power toward Orckit is under a duty to act in fairness towards Orckit. The Companies Law does not describe the substance of this duty of fairness. These various shareholder duties may restrict the ability of a shareholder to act in what the shareholder perceives to be its own best interests.

Anti-Takeover Provisions; Mergers and Acquisitions

The Israeli Companies Law includes provisions that allow a merger transaction and requires that each company that is a party to a merger have the transaction approved by its board of directors and a vote of the majority of its shares, at a shareholders' meeting called on at least 21 days' prior notice. For purposes of the shareholder vote, unless a court rules otherwise, the statutory merger will not be deemed approved if a majority of the shares present that are held by parties other than the other party to the merger, or by any person who holds 25% or more of the shares or the right to appoint 25% or more of the directors of the other party, vote against the merger. Upon the request of a creditor of either party of the proposed merger, the court may delay or prevent the merger if it concludes that there exists a reasonable concern that as a result of the merger, the surviving company will be unable to satisfy the obligations of any of the parties to the merger. In addition, a merger may not be completed unless at least 70 days have passed from the time that the requisite proposal for the merger has been filed by each party with the Israeli Registrar of Companies.

The Companies Law also provides that an acquisition of shares of a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 25% or greater shareholder of the company and there is no existing 25% or greater shareholder in the company. An acquisition of shares of a public company must be made by means of a tender offer if as a result of the acquisition the purchaser would become a 45% or greater shareholder of the company and there is no existing majority shareholder in the company. These requirements do not apply if the acquisition is made in a private placement. If following any acquisition of shares, the acquiror will hold 90% or more of the company's shares, the acquisition may not be made other than through a tender offer to acquire all of the shares of such class. If more than 95% of the outstanding shares are tendered in the tender offer, all the shares that the acquiror offered to purchase will be transferred to it. However, the remaining minority shareholders may seek to alter the consideration by court order.

Israeli tax law also treats stock-for-stock acquisitions between an Israeli company and a foreign company less favorably than does U.S. tax law. For example, Israeli tax law may, under certain circumstances, subject a shareholder who exchanges his ordinary shares for

shares of another corporation to taxation prior to the sale of the shares received in such stock-for-stock swap.

Our articles of association provide that our board of directors may, at any time in its sole discretion, adopt protective measures to prevent or delay a coercive takeover of Orckit, including, without limitation, the adoption of a shareholder rights plan. In November 2001, our board of directors adopted a shareholder bonus rights plan pursuant to which share purchase bonus rights were distributed on December 6, 2001 at the rate of one right for each of our ordinary shares held by shareholders of record as of the close of business on that date.

The rights plan is intended to help ensure that all of our shareholders are able to realize the long-term value of their investment in Orckit in the event of a potential takeover which does not reflect the full value of Orckit and is otherwise not in the best interests of Orckit and its shareholders. The rights plan is also intended to deter unfair or coercive takeover tactics.

Each right initially will entitle shareholders to buy one-half of one of our ordinary shares for \$65.00. The rights generally will be exercisable and transferable apart from our ordinary shares only if a person or group becomes an “acquiring person” by acquiring beneficial ownership of 15% or more of our ordinary shares, subject to certain exceptions set forth in the rights plan, or commences a tender or exchange offer upon consummation of which such person or group would become an “acquiring person.” Subject to certain conditions described in the rights plan, once the rights become exercisable, the holders of rights, other than the acquiring person, will be entitled to purchase ordinary shares at a discount from the market price.

The rights will expire on December 31, 2011 and are generally redeemable by our board of directors, at \$0.01 per right, at any time until the tenth business day following public disclosure that a person or group has become an “acquiring person.”

Our articles of association also provide that as long as any of our securities are publicly traded on a United States market or exchange, all proxy solicitations by persons other than our board of directors must be undertaken pursuant to the United States proxy rules, regardless of whether those proxy rules are legally applicable to us. These provisions of our articles of association could discourage potential acquisition proposals and could delay or prevent a change in control of Orckit.

Modification of Class Rights

Our articles of association provide that the rights attached to any class (unless otherwise provided by the terms of that class), such as voting, rights to dividends and the like, may be varied by a shareholders’ resolution, subject to the sanction of a resolution passed by a majority of the holders of the shares of that class at a separate class meeting.

Indemnification, Exculpation and Insurance of Office Holders

Exculpation of Office Holders

Under the Companies Law, an Israeli company may not exempt an office holder from liability for breach of his duty of loyalty, but may exempt in advance an office holder from liability to the company, in whole or in part, for a breach of his duty of care provided the

articles of association of the company allow it to do so. Our articles of association allow us to exempt our office holders to the fullest extent permitted by law.

Insurance of Office Holders

Our articles of association provide that, subject to the provisions of the Companies Law, we may enter into an insurance contract which would provide coverage for any monetary liability incurred by any of our office holders, with respect to an act performed in the capacity of an office holder for:

- a breach of his duty of care to us or to another person;
- a breach of his duty of loyalty to us, provided that the office holder acted in good faith and had reasonable cause to assume that his act would not prejudice our interests; or
- a financial liability imposed upon him in favor of another person.

We obtained liability insurance covering our officers and directors.

Indemnification of Office Holders

Our articles of association provide that we may indemnify an office holder against the following obligations and expenses imposed on the office holder with respect to an act performed in the capacity of an office holder:

- a financial obligation imposed on him in favor of another person by a court judgment, including a settlement judgment or an arbitrator's award approved by the court; and
- reasonable litigation expenses, including attorneys' fees, incurred by the office holder or which the office holder was ordered to pay by a court in connection with:
 - proceedings we institute against him or that are instituted on our behalf or by another person;
 - a criminal charge from which he is acquitted; or
 - a criminal proceeding in which he is convicted of an offense that does not require proof of criminal intent.

Our articles of association also include provisions:

- authorizing us to undertake in advance to indemnify an office holder as described above, provided that the undertaking is limited to those types of events which our board of directors deems to be anticipated when the undertaking is given and to an amount determined by our board of directors to be reasonable under the circumstances; and
- authorizing us to retroactively indemnify an officer or director.

Limitations on Exculpation, Insurance and Indemnification

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

- a breach by the office holder of his duty of loyalty unless, with respect to insurance coverage, the office holder acted in good faith and had a reasonable basis to believe that the act would not prejudice the company;
- a breach by the office holder of his duty of care if the breach was committed intentionally or recklessly;
- any act or omission committed with the intent to derive an illegal personal benefit; or
- any fine imposed on the office holder.

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

Our articles of association also provide that, subject to the provisions of applicable law, we may procure insurance for or indemnify any person who is not an office holder, including without limitation, any of our employees, agents, consultants or contractors.

C. MATERIAL CONTRACTS

None

D. EXCHANGE CONTROLS

There are currently no Israeli currency control restrictions on payments of dividends or other distributions with respect to our ordinary shares or the proceeds from the sale of the shares, except for the obligation of Israeli residents to file reports with the Bank of Israel regarding certain transactions. However, legislation remains in effect pursuant to which currency controls can be imposed by administrative action at any time.

The ownership or voting of our ordinary shares by non-residents of Israel, except with respect to citizens of countries which are in a state of war with Israel, is not restricted in any way by our memorandum of association or articles of association or by the laws of the State of Israel.

E. TAXATION

The following is a general summary only and should not be considered as income tax advice or relied upon for tax planning purposes.

United States

The following summary describes the material U.S. federal income tax consequences to “U.S. Holders” (as defined below) arising from the purchase, ownership and disposition of our ordinary shares. This summary is based on current provisions of the Internal Revenue Code of 1986, as amended (the “Code”), the final, temporary and proposed U.S. Treasury Regulations promulgated thereunder, and administrative and judicial interpretations thereof, all of which are subject to change, possibly with retroactive effect. This summary is addressed only to holders that are U.S. citizens, individuals resident in the United States for U.S. federal income tax purposes, domestic U.S. corporations, estates the income of which is subject to U.S. federal income tax regardless of the source of their income and any trust if either:

- a U.S. court is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all the substantial decisions of the trust, or
- the trust has a valid election in effect under applicable U.S. Treasury regulations to be treated as a U.S. person (collectively, “U.S. Holders”).

This summary does not consider all aspects of U.S. federal income taxation that may be relevant to particular U.S. Holders by reason of their particular circumstances, including potential application of the alternative minimum tax, or any aspect of state, local or non-U.S. federal tax laws. In addition, this summary is directed only to U.S. Holders that hold ordinary shares as capital assets and does not address the considerations that may be applicable to particular classes of U.S. Holders, including financial institutions, insurance companies, broker-dealers, tax-exempt organizations, holders whose functional currency is not the U.S. Dollar, holders of ordinary shares as part of a “straddle,” “hedge” or “conversion transaction,” holders, directly, indirectly or through attribution, of 10% or more of our outstanding ordinary shares and persons who own ordinary shares through a partnership or other pass-through entity.

Each U.S. Holder should consult with his, her or its own tax advisor as to the particular tax consequences to him, her or it of the purchase, ownership and sale of ordinary shares, including the effects of applicable state, local, foreign or other tax laws and possible changes in the tax laws.

Sale or Exchange of Ordinary Shares

Subject to the discussion below under “Passive Foreign Investment Company Status,” a U.S. Holder’s sale or exchange of ordinary shares generally will result in the recognition by such U.S. Holder of capital gain or loss in an amount equal to the difference between the U.S. Dollar value of the amount realized and the U.S. Holder’s tax basis in the ordinary shares sold. This gain or loss will be long-term capital gain or loss if the ordinary shares sold have been held for more than one year at the time of the sale or exchange. If the U.S. Holder’s holding period on the date of the sale or exchange is one year or less, such gain or loss will be a short-term capital gain or loss. See “—Israel—Capital Gains Tax” for a discussion of taxation by Israel of capital gains realized on sales of capital assets. Any capital loss realized upon the sale, exchange or other disposition of ordinary shares generally is deductible only against capital gains and not against ordinary income, except that in the case of non-corporate U.S. Holders, a capital loss is deductible to the extent of capital gains plus ordinary income

up to \$3,000. In general, any capital gain recognized by a U.S. Holder upon the sale or exchange of ordinary shares will be treated as U.S.-source income for U.S. foreign tax credit purposes. Under the tax treaty between the United States and Israel, gain derived from the sale, exchange or other disposition of ordinary shares by a U.S. Holder who is a resident of the United States for purposes of the treaty and who sells the ordinary shares within Israel may be treated as foreign-source income for U.S. foreign tax credit purposes.

A U.S. Holder's tax basis in his, her or its ordinary shares generally will be the purchase price paid therefor by such U.S. Holder. The holding period of each ordinary share owned by a U.S. Holder will commence on the day following the date of the U.S. Holder's purchase of such ordinary share and will include the day on which the ordinary share is sold by such U.S. Holder.

In the case of a U.S. Holder who uses the cash basis method of accounting and who receives NIS in connection with the sale or other taxable disposition of ordinary shares, the amount realized will be based on the "spot rate" (as defined below under the heading "Treatment of Distributions") as determined on the settlement date of such sale or other taxable disposition. If such U.S. Holder subsequently converts NIS into U.S. Dollars at a conversion rate other than the spot rate in effect on the settlement date, he, she or it would have a foreign currency exchange gain or loss treated as ordinary income or loss for U.S. federal income tax purposes. A U.S. Holder who uses the accrual method of accounting may elect the same treatment required of cash method taxpayers with respect to a sale or other taxable disposition of ordinary shares, provided that the election is applied consistently from year to year. Such election may not be changed without the consent of the U.S. Internal Revenue Service. If an accrual method U.S. Holder does not elect to be treated as a cash method taxpayer (pursuant to the Treasury regulations applicable to foreign currency transactions), such U.S. Holder may be deemed to have realized an immediate foreign currency gain or loss for U.S. federal income tax purposes in the event of any difference between the U.S. Dollar value of the NIS on the date of sale or other taxable disposition and the settlement date. Any such currency gain or loss would be treated as ordinary income or loss and would be subject to tax in addition to any gain or loss recognized by such U.S. Holder on the sale or other taxable disposition of ordinary shares.

Treatment of Distributions

For U.S. federal income tax purposes, the gross amount of any distributions (other than a distribution in liquidation or a distribution in redemption of stock that is treated as an exchange), including the amount of any Israeli taxes withheld therefrom, paid to a U.S. Holder with respect to his, her or its ordinary shares, generally will be treated as a dividend to the extent that the distribution does not exceed such U.S. Holder's share of our current or accumulated earnings and profits, as determined based on U.S. federal tax principles. Such dividends will not be eligible for the dividends received deduction allowed to U.S. corporations under Section 243 of the Code. The amount of any distribution that exceeds such U.S. Holder's share of our current and accumulated earnings and profits will be treated first as a non-taxable return of the U.S. Holder's tax basis in his, her or its ordinary shares to the extent thereof and then as gain from the sale of ordinary shares. The maximum U.S. federal income tax rate on certain dividends paid to individuals through 2008 recently was reduced to 15%. This reduced rate generally will not apply, however, to dividends paid by us if we are treated as a passive foreign investment company in the year the

dividends are paid or in the prior year. See the discussion below under the heading "Passive Foreign Investment Company Status." U.S. Holders are urged to consult their own tax advisors regarding the U.S. federal income tax rate that will be applicable to their receipt of any dividends paid with respect to our ordinary shares.

Dividends paid in NIS must be included in income in a U.S. Dollar amount based on the "spot rate" of exchange in effect on the date the distribution is includable in the U.S. Holder's income, regardless of whether the payment is in fact converted into U.S. Dollars. The "spot rate" generally refers to a rate that reflects a fair market rate of exchange available to the public for currency under a "spot contract" in a free market and involving representative amounts. A "spot contract" is a contract to buy or sell a currency no more than two business days following the date of the execution of the contract. If a spot rate cannot be demonstrated, the U.S. Internal Revenue Service has the authority to determine the spot rate. U.S. Holders will have a tax basis in the NIS for U.S. federal income tax purposes equal to such U.S. Dollar amount. Any subsequent gain or loss on NIS arising from exchange rate fluctuations during the period from the date a U.S. Holder includes the dividend in income to the date such U.S. Holder converts the payment to U.S. Dollars will be taxable as ordinary income or loss and will be treated as U.S. source income or loss for U.S. foreign tax credit purposes.

Dividends with respect to our ordinary shares will constitute "portfolio income" for purposes of the limitation on the use of passive activity losses, and thus generally may not be offset by passive activity losses, and also generally will be treated as "investment income" for purposes of the limitation on the deduction of investment interest expense. Dividends with respect to ordinary shares also generally will be classified as foreign source "passive income" for purposes of computing the foreign tax credit limitation. Foreign income taxes exceeding the credit limitation for the year of payment or accrual may be carried back for two taxable years and forward for five taxable years in order to reduce U.S. federal income taxes, subject to the credit limitation applicable in each of those years. Subject to certain conditions and limitations, any Israeli withholding tax imposed on such dividends generally will be eligible for credit against the recipient U.S. Holder's U.S. federal income tax liability or, at the U.S. Holder's election, may be claimed as a deduction against income in determining such tax liability. The calculation of allowable foreign tax credits and, in the case of a U.S. Holder that elects to deduct foreign taxes, the availability of deductions for foreign taxes paid involve the application of complex rules that depend on a U.S. Holder's particular circumstances. Accordingly, U.S. Holders should consult their own tax advisors regarding their eligibility for foreign tax credits or deductions.

Passive Foreign Investment Company Status

Generally, a foreign corporation is treated as a passive foreign investment company ("PFIC") for U.S. federal income tax purposes for any tax year if, in such tax year, either (i) 75% or more of its gross income, including its pro rata share of the gross income of any company in which it owns 25% or more of the shares by value, is passive in nature (the "Income Test"), or (ii) the average percentage of its assets during such tax year, including its pro rata share of the assets of any company in which it owns 25% or more of the shares by value, which produce, or are held for the production of, passive income (determined by averaging the percentage of the fair market value of its total assets which are passive assets as of the end of each quarter of such year) is 50% or more (the "Asset Test"). While we do not believe that we were a PFIC for any tax year prior to 2001, it is likely that we would be

deemed to have been a PFIC for 2001, 2002 and 2003.

There is no definitive method prescribed in the Code, U.S. Treasury Regulations or administrative or judicial interpretations thereof for determining the value of a foreign corporation's assets for purposes of the Asset Test. The legislative history of the U.S. Taxpayer Relief Act of 1997 (the "1997 Act"), however, indicates that for purposes of the Asset Test, "the total value of a publicly-traded foreign corporation's assets generally will be treated as equal to the sum of the aggregate value of its outstanding stock plus its liabilities." It is unclear under current interpretations of the 1997 Act whether other valuation methods could be employed to determine the value of our assets. Under the approach set forth in the legislative history to the 1997 Act, we would be deemed to have been a PFIC for 2001, 2002 and 2003, principally because (a) a significant portion of our assets continued to consist of cash, cash equivalents and short- and long-term investments from the remaining proceeds of our offerings, and (b) the public market value of our ordinary shares was lower in 2001, 2002 and 2003 than in previous years.

If we are treated as a PFIC for U.S. federal income tax purposes for any year during a U.S. Holder's holding period of ordinary shares and the U.S. Holder does not make a QEF Election or a "mark-to-market" election (both as described below):

- "Excess distributions" by us to a U.S. Holder would be taxed in a special way. "Excess distributions" with respect to any U.S. Holder are amounts received by such U.S. Holder with respect to our ordinary shares in any tax year that exceed 125% of the average distributions received by such U.S. Holder from us during the shorter of (i) the three previous years, or (ii) such U.S. Holder's holding period of our ordinary shares before the then-current tax year. Excess distributions must be allocated ratably to each day that a U.S. Holder has held our ordinary shares. Thus, a U.S. Holder must report amounts allocated to the current tax year as ordinary income for that year, pay tax on amounts allocated to each prior tax year in which we were a PFIC at the highest rate on ordinary income in effect for such prior year and pay an interest charge at the rate applicable to deficiencies for income tax.
- The entire amount of any gain realized by a U.S. Holder upon the sale or other disposition of our ordinary shares also would be treated as an "excess distribution" subject to tax as described above.
- The tax basis in ordinary shares acquired from a decedent who was a U.S. Holder would not receive a step-up to fair market value as of the date of the decedent's death, but would instead be equal to the decedent's basis, if lower.

Although we generally will be treated as a PFIC as to any U.S. Holder if we are a PFIC for any year during the U.S. Holder's holding period, if we cease to satisfy the requirements for PFIC classification, the U.S. Holder may avoid the consequences of PFIC classification for subsequent years if he elects to recognize gain based on the unrealized appreciation in the ordinary shares through the close of the tax year in which we cease to be a PFIC.

A U.S. Holder who beneficially owns shares of a PFIC must file Form 8621 (Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund) with the U.S. Internal Revenue Service for each tax year in which he, she or it holds shares in a PFIC. This form describes any distributions received with respect to these shares and any gain realized upon the disposition of these shares.

For any tax year in which we are treated as a PFIC, a U.S. Holder may elect to treat his, her or its ordinary shares as an interest in a qualified electing fund (a “QEF Election”), in which case the U.S. Holder would be required to include in income currently his, her or its proportionate share of our earnings and profits in years in which we are a PFIC regardless of whether distributions of our earnings and profits are actually made to the U.S. Holder. Any gain subsequently recognized by the U.S. Holder upon the sale of his, her or its ordinary shares, however, generally would be taxed as capital gain and the denial of the basis step-up at death described above would not apply.

A U.S. Holder may make a QEF Election with respect to a PFIC for any tax year of the U.S. Holder. A QEF Election is effective for the tax year in which the election is made and all subsequent tax years of the U.S. Holder. Procedures exist for both retroactive elections and the filing of protective statements. A U.S. Holder making the QEF Election must make the election on or before the due date, as extended, for the filing of the U.S. Holder’s income tax return for the first tax year to which the election will apply. We will provide to each U.S. Holder, upon request, the tax information required to make a QEF Election and to make subsequent annual filings.

As an alternative to a QEF Election, a U.S. Holder generally may elect to mark his ordinary shares to market annually, recognizing ordinary income or loss (subject to certain limitations) equal to the difference, as of the close of the tax year, between the fair market value of his, her or its ordinary shares and the adjusted tax basis of such shares. Losses would be allowed only to the extent of net mark-to-market gain accrued under the election. If a mark-to-market election with respect to ordinary shares is in effect on the date of a U.S. Holder’s death, the normally available step-up in tax basis to fair market value will not be available. Rather, the tax basis of the ordinary shares in the hands of a U.S. Holder who acquired them from a decedent will be the lesser of the decedent’s tax basis or the fair market value of the ordinary shares. Once made, a mark-to-market election generally continues unless revoked with the consent of the U.S. Internal Revenue Service.

The implementation of many aspects of the Code’s PFIC rules requires the issuance of regulations which in many instances have yet to be promulgated and which may have retroactive effect. We cannot be sure that any of these regulations will be promulgated or, if so, what form they will take or what effect they will have on the foregoing discussion.

Accordingly, and due to the complexity of the PFIC rules, U.S. Holders should consult their own tax advisors regarding our status as a PFIC for 2003 and any prior and subsequent years the eligibility, manner and advisability of making a QEF Election or a mark-to-market election, and the effect of these elections on the calculation of the amount of foreign tax credit that may be available to a U.S. Holder.

Information Reporting and Backup Withholding

Any dividends paid on the ordinary shares to U.S. Holders may be subject to U.S. federal tax information reporting requirements and the U.S. backup withholding tax

(currently 30% through 2003, but scheduled for reduction to 29% for 2004-2005 and 28% for 2006 and later years). In addition, the proceeds of a U.S. Holder's sale of ordinary shares may be subject to tax information reporting and the U.S. backup withholding tax. Backup withholding will not apply if the U.S. Holder (i) is a corporation or other exempt recipient, or (ii) the U.S. Holder provides a U.S. taxpayer identification number, certifies as to no loss of exemption from backup withholding and otherwise complies with any applicable backup withholding requirements. Any amounts withheld under the U.S. backup withholding tax rules will be allowed as a refund or a credit against the U.S. Holder's U.S. federal income tax, provided the required information is furnished to the U.S. Internal Revenue Service.

Israel

The following discussion, which represents a summary of certain Israeli tax laws affecting our shareholders, including U.S. and other non-Israeli shareholders, is for general information only and is not intended to substitute for careful or specific tax planning. To the extent that the discussion is based on legislation yet to be judicially or administratively interpreted, there can be no assurance that the views expressed herein will accord with any such interpretation in the future by the tax authorities or by the courts. This discussion is not intended, and should not be construed, as legal or professional tax advice, and does not cover all possible tax considerations. Accordingly, each investor should consult his or her own tax advisor as to the particular tax consequences of an investment in the ordinary shares including the effects of applicable Israeli or foreign or other tax laws and possible changes in the tax laws.

Tax Reform

On January 1, 2003, the Law for Amendment of the Income Tax Ordinance (Amendment No. 132), 5762-2002, as amended, known as the tax reform, came into effect.

The tax reform, aimed at broadening the categories of taxable income and reducing the tax rates imposed on employment income, introduced the following measures, among other things:

- Reduction of the tax rate levied on capital gains (other than gains deriving from the sale of listed securities) derived after January 1, 2003 to a general rate of 25% for both individuals and corporations. Regarding assets acquired prior to January 1, 2003, the reduced tax rate will apply to a proportionate part of the gain, in accordance with the holding periods of the asset, before or after January 1, 2003, on a linear basis. In addition, the tax reform enables the carry forward of capital losses without any time restriction;
- Imposition of Israeli tax on all income of Israeli residents, individuals and corporations, regardless of the territorial source of income, including income derived from passive sources such as interest, dividends and royalties;
- Introduction of controlled foreign corporation (CFC) rules into the Israeli tax structure. Generally, under such rules, an Israeli resident who holds, directly or indirectly, 10% or more of the rights in a foreign corporation whose shares are not publicly traded (or which has offered less than 30% of its shares or any rights to its shares to the public), in which more than 50% of the rights are held directly or indirectly by Israeli residents, and a majority of whose income in a tax year is

considered passive income, will be liable for tax on the portion of such income attributed to his holdings in such corporation, as if such income were distributed to him as a dividend;

- Imposition of capital gains tax on capital gains realized as of January 1, 2003 by individuals resident in Israel from the sale of shares of publicly traded companies on the Tel Aviv Stock Exchange and from the sale of shares of publicly traded Israeli companies on certain other stock exchanges (such gain was previously exempt from capital gains tax in Israel in certain cases). For information with respect to the applicability of Israeli capital gains taxes on the sale of ordinary shares, see “Capital Gains Tax” below;
- Effectuation of a new regime for the taxation of shares and options issued to employees, officers and directors; and
- Introduction of tax at a rate of 25% on dividends paid by one Israeli company to another (which are generally not subject to tax), if the source of such dividends is income that was derived outside of Israel.

Capital Gains Tax

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

Pursuant to the tax reform, generally, capital gains tax is imposed on Israeli residents at a rate of 15% on real gains derived on or after January 1, 2003 from the sale of shares in: (i) companies publicly traded on the Tel Aviv Stock Exchange (“TASE”); or (ii) Israeli companies publicly traded on Nasdaq or a recognized stock exchange or regulated market in a country that has a treaty for the prevention of double taxation with Israel; or (iii) companies traded on both the TASE and Nasdaq or a recognized stock exchange or a regulated market outside of Israel (such as Orckit). This tax rate is contingent upon the shareholder not claiming a deduction for financing expenses in connection with such shares (in which case the capital gain will be taxed at a rate of 25%), and does not apply to: (i) the sale of shares to a relative (as defined in the tax reform); (ii) the sale of shares by dealers in securities who will be taxed at a rate of 36% for corporations and at a marginal tax rate of up to 50% for individuals; (iii) the sale of shares by shareholders that report in accordance with the Income Tax Law (Inflationary Adjustments), 5745-1985, referred to as the Inflationary Adjustments Law, who will be taxed at a rate of 36% for corporation and at a marginal tax rate of up to 50% for individuals; or (iv) the sale of shares by shareholders who acquired their shares prior to the issuer’s initial public offering (that are subject to a different tax arrangement). The tax basis of shares acquired prior to January 1, 2003 will be determined in accordance with the average closing share price in the three trading days preceding January 1, 2003. However, a

request may be made to the tax authorities to consider the actual adjusted cost of the shares as the tax basis if it is higher than such average price.

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

In December 2003, regulations promulgated pursuant to the Tax Reform were amended so that, in certain circumstances, capital gains derived from the sale and subsequent (same day) repurchase of shares traded on the TASE or shares of Israeli companies publicly traded on a recognized stock exchange or regulated market in a country that has a treaty for the prevention of double taxation with Israel, may be taxed at a rate equal to the withholding tax rate applicable to revenues derived from such sale. In accordance with an announcement published by the Israeli Income Tax Commission, the withholding tax rate applicable to the sale of such shares until the end of 2003 tax year, which was equal at such time to 1% of the revenues generated in their sale, was determined as the final tax rate applicable to such sale. The amended regulations also determined that the day of such sale and repurchase shall be considered the new date of purchase of such shares. The foregoing was not applicable to: (i) dealers in securities; (ii) shareholders that report in accordance with the Inflationary Adjustments Law; (iii) shareholders who acquired their shares prior to the issuer's initial public offering; (iv) in some cases, shareholders that received their shares within the framework of an employer-employee relationship; or (v) shareholders claiming a deduction for financing expenses in connection with such shares. The regulations further provided that with respect to shares of Israeli companies traded on a stock exchange outside of Israel, the market price determined at the close of the trading day preceding the day of the sale and repurchase of such shares, will constitute the new tax basis for any future sale of such shares.

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

Pursuant to a treaty between the governments of the United States and Israel, known as the U.S.-Israel Tax Treaty, the sale, exchange or disposition of shares by a person who holds the ordinary shares as a capital asset and who qualifies as a resident of the United States within the meaning of the treaty and who is entitled to claim the benefits afforded to a resident by the treaty will generally not be subject to Israeli capital gains tax. This exemption does not apply if the person holds, directly or indirectly, shares representing 10% or more of our voting power during any part of the 12-month period preceding the applicable sale, exchange or disposition, subject to specified conditions. However, under the treaty, the person would be permitted to claim a credit for the capital gains tax paid in Israel against the U.S. federal income tax imposed with respect to the applicable sale, exchange or disposition, subject to the limitations in U.S. laws applicable to foreign tax credits. The treaty does not relate to U.S. state or local taxes.

Tax on Dividends

Non-residents of Israel are subject to income tax on income accrued or derived from sources in Israel. These sources of income include passive income such as dividends, royalties and interest, as well as non-passive income from services rendered in Israel. On distributions of dividends other than bonus shares, or stock dividends, we would be required to withhold income tax at the rate of up to 25%, unless a different rate is provided in a treaty between Israel and the shareholder's country of residence. If the income out of which the dividend is being paid is attributable to an Approved Enterprise, the rate is 15%. Under the U.S.-Israel tax treaty, if the income out of which the dividend is being paid is not attributable to an Approved Enterprise, then income tax with respect to shareholders that are U.S. corporations holding at least 10% of our voting power is required to be withheld at the rate of 12.5%. For more information on Approved Enterprises, please refer to Item 5B of this Annual Report.

F. DIVIDENDS AND PAYING AGENTS

Not applicable

G. STATEMENT BY EXPERTS

Not applicable.

H. DOCUMENTS ON DISPLAY

We are subject to the informational requirements of the Securities Exchange Act of 1934, as amended, applicable to foreign private issuers and fulfill the obligations with respect to such requirements by filing reports with the Securities and Exchange Commission, or SEC. You may read and copy any document we file, including any exhibits, with the SEC without charge at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. Copies of such material may be obtained by mail from the Public Reference Branch of the SEC at such address, at prescribed rates. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Certain of our SEC filings are also available to the public at the SEC's website at <http://www.sec.gov>.

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

I. SUBSIDIARY INFORMATION

Not applicable

ITEM 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

General

We are exposed to market risk, including movements in interest rates and foreign currency exchange rates. Our primary market risk exposure occurs because we generate most of our revenues in U.S. dollars but incur a majority of our salaries and related expenses and part of our other expenses in new Israeli shekels.

From time to time, in management's discretion, we engage in hedging or other transactions intended to manage risks relating to foreign currency exchange rates. As of March 31, 2004, we owned forward transaction assets. We may in the future undertake hedging or other similar transactions or invest in market risk sensitive instruments when our management determines that it is necessary to offset these risks.

Our interest rate and foreign exchange exposures are monitored by tracking actual and projected commitments.

Exchange Rate Risk Management

Our functional currency and that of our subsidiaries is the U.S. dollar.

From time to time, we assess our exposure to exchange rate risks and endeavor to limit this exposure through natural hedging, or by attempting to maintain a similar level of assets and liabilities in any given currency.

The table below presents our balance sheet exposure as of December 31, 2003 at fair value related to market risk sensitive instruments, mainly short term receivables and payables in currencies other than U.S. dollars. Substantially all of such balance is in New Israeli Shekels. The information is presented in U.S. dollars (in millions), which is our reporting currency.

Please see also the explanatory notes below the table.

	New Israeli Shekels	Total
Israel	(3.5)	(3.5)
Total	(3.5)	(3.5)

Explanatory notes:

1) Total balance sheet exposure relating to market risk sensitive instruments is the sum of the absolute figures (excess of liabilities over assets in the amount of \$3.5million). A devaluation of 5% of the U.S. dollar compared to the NIS would cause an increase in expenses of approximately \$175,000.

2) The data presented in the table reflects the exposure after taking into account the effect of the “natural” hedging.

Interest Rate Risk Management

As of December 31, 2003, we had \$10.0 million of cash and cash equivalents, \$273,000 of short-term bank deposits, \$20.5 million of trading securities, \$10.1 million of short term marketable securities, \$6.3 million of long term deposits and \$31.2 million of long-term marketable securities. Our trading and marketable securities mature as follows: \$20.3 million in 2004, and \$41.4 million over a period from 2004 to 2007. Due to the relatively short-term maturities of the Company’s cash, deposits and securities portfolio, an immediate 10% change in the current interest rates (for example, from 5.0% to 5.5%) is not expected to have a material effect on its near-term financial condition or results of operations.

ITEM 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable

PART II

ITEM 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

Not applicable

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

For a discussion of our shareholder bonus rights plan, please refer to Item 10.B of this Annual Report. In connection with the grants in 2003 to Eric Paneth, our Chief Executive Officer and a director, and Izhak Tamir, our President and a director, of the share purchase rights described in Item 6E, this plan was amended to provide that the beneficial ownership of our ordinary shares held by Mr. Paneth or Mr. Tamir will not trigger the rights under this plan.

At our annual general shareholders meeting held in February 2003, our shareholders approved the following amendments to our article of association:

- the vote required to amend our articles of association was changed from a simple majority to 66-2/3% of our outstanding ordinary shares voting on the matter;
- the vote required to (i) elect a director was changed from a simple majority to 66-2/3% of our outstanding ordinary shares voting on the matter and (ii) remove a director was changed from a simple majority to 75% of our outstanding ordinary shares voting on the matter. Also it was clarified that directors may be elected by shareholders only at an annual general meeting and that each director (except outside directors) will serve until the next annual general meeting at which one or more directors are elected following his election;

- the number of “outside directors” (as defined in the Companies Law) was limited to three. The Companies Law requires at least two outside directors, and we currently have three. This amendment will not limit the number of “independent directors” (as defined in the rules of Nasdaq) that we may have;
- the maximum size of our board of directors was changed from 15 to seven directors and the minimum number of continuing directors that are entitled to act as the board of directors in the event of vacancies was changed from a majority of the board of directors to three directors; and
- a requirement that any dividends be approved by our audit committee in addition to our board of directors was added, or if we do not have an audit committee for any reason, by a majority of the “outside directors” (as defined in the Companies Law) then on the board of directors.

ITEM 15. CONTROLS AND PROCEDURES

We performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of December 31, 2003. The evaluation was performed with the participation of our senior management and under the supervision and with the participation of our chief executive officer and chief financial officer. Based on this evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures are effective to alert them on a timely basis to material information required to be included in our periodic reports with the Securities and Exchange Commission.

In addition, there were no changes in our internal control over financial reporting that occurred during 2003 that have materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.

Item 16A. Audit Committee Financial Expert

Our board of directors has determined that Mr. Motil qualifies as an “audit committee financial expert” as defined in Item 16A of Form 20-F.

Item 16B. Code of Ethics

On March 30, 2004, our board of directors adopted our Code of Ethics, a code that applies to all of our officers, directors and employees. We will provide our Code of Ethics free of charge to any person who requests a copy of it. Such requests may be sent to our offices in 126 Yigal Alon Street, Tel Aviv, Israel, attention: Controller.

Item 16C. Principal Accountant Fees and Services

In the annual meeting held in February 2003, our shareholders re-appointed Kesselman & Kesselman, a member of PricewaterhouseCoopers International Limited, to serve as our independent auditors. These accountants billed the following fees to us for professional services in each of the last two fiscal years:

	Year Ended December 31,	
	2003	2002
Audit Fees	\$73,000	\$71,000
Audit-Related Fees	38,500	13,000
Tax Fees	20,000	35,000
All Other Fees	--	--
	<hr/>	
Total	\$131,500	\$119,000

“Audit Fees” are the aggregate fees billed for the audit of our annual financial statements. This category also includes services that generally the independent accountant provides, such as statutory audits including audits required by the Office of the Chief Scientist and other Israeli government institutes, consents and assistance with and review of documents filed with the SEC. “Audit-Related Fees” are the aggregate fees billed for assurance and related services that are reasonably related to the performance of the audit and are not reported under Audit Fees. These fees include mainly accounting consultations regarding the accounting treatment of matters that occur in the regular course of business, implications of new accounting pronouncements and other accounting issues that occur from time to time. “Tax Fees” are the aggregate fees billed for professional services rendered for tax compliance, tax advice, other than in connection with the audit. Tax compliance involves preparation of original and amended tax returns, tax planning and tax advice.

Our Audit Committee has adopted a pre-approval policy for the engagement of our independent accountant to perform certain audit and non-audit services. Pursuant to this policy, which is designed to assure that such engagements do not impair the independence of our auditors, the audit committee pre-approves annually a catalog of specific audit and non-audit services in the categories of Audit Service, Audit-Related Service, Tax Services and other services that may be performed by our independent accountants, and the maximum pre-approved fees that may be paid as compensation for each pre-approved service in those categories. Any proposed services exceeding the maximum pre-approved fees require specific approval by the Audit Committee.

The Audit Committee may delegate its pre-approval authority to one or more of its members, subject to ratification by the entire Audit Committee.

Requests or applications to provide services that require specific approval by the Audit Committee are submitted to the Audit Committee by an executive officer of the Company, together with detailed back-up documentation and a statement as to whether, in the requesting executive officer’s view, the provision of such services by the outside auditor would impair its independence.

ITEM 17. FINANCIAL STATEMENTS

See Item 18.

ITEM 18. FINANCIAL STATEMENTS

Attached. See Item 19(a).

ITEM 19. EXHIBITS

- (a) The following consolidated financial statements and related auditors' report are filed as part of this Annual Report:

	Page
Table of Contents to 2003 Consolidated Financial Statements	F-1
Report of Independent Auditors	F-2
 Consolidated Financial Statements:	
Balance Sheets at December 31, 2002 and 2003	F-3
Statements of Operations for the Years Ended December 31, 2001, 2002 and 2003	F-4
Statements of Changes in Shareholders' Equity for the Years Ended December 31, 2001, 2002 and 2003	F-5
Statements of Cash Flows for the Years Ended December 31, 2001, 2002 and 2003	F-6
Notes to Financial Statements	F-7 – F-26
Report of independent auditors on financial statement schedule	F-27
Schedule - valuation and qualifying accounts	F-28

- (b) Exhibits:

The following exhibits are filed as part of this Annual Report:

<u>Exhibit No.</u>	<u>Exhibit</u>
†1.1 ⁷	Memorandum of Association, as amended.
1.2 ⁷	Fourth Amended and Restated Articles of Association.
1.3 ⁴	Bonus Rights Agreement, dated as of November 20, 2001, between Orckit Communications Ltd. and American Stock Transfer & Trust Company, as Rights Agent.
1.4 ¹	Amendment No. 1, dated as of February 5, 2003, to Bonus Rights Plan, dated as of November 20, 2001, between Orckit Communications Ltd. and American Stock Transfer & Trust Company, as Rights Agent.
2.1 ⁶	Indenture, dated as of March 13, 2000, between Orckit Communications Ltd. and State Street Bank and Trust Company.
2.2 ⁶	5.75% Convertible Subordinated Notes of Orckit Communications Ltd. due April 1, 2005.
4.1 ²	Orckit Israeli Share Incentive Plan, as amended (2000).
†4.5 ³	Lease Agreement, dated September 28, 1999, between Orckit Communications Ltd. and Gush 7093 Helka 162 Ltd., private company # 51-058315-6.
4.6 ⁵	Corrigent Stock Option Plan (2001).
4.7*	Spediant Stock Option Plan
4.8*	Promissory Note dated March 30, 2004 made by Orckit Communications Ltd. to HSBC Bank USA
4.10 ⁷	Orckit Communications Ltd. 2003 Subsidiary Employee Share Incentive Plan.
8.1*	Subsidiaries of Orckit Communications Ltd.
12.1*	Certification of Principal Executive Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act
12.2*	Certification of Principal Financial Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act
13.1*	Certification of Principal Executive Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act

- 13.2* Certification of Principal Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act
- 14.1* Consent of Kesselman & Kesselman, independent auditors of Orckit Communications Ltd.

† Translated in full or summary version; the original language version is on file with Orckit Communications Ltd. and is available upon request.

¹ Incorporated by reference to Orckit Communications Ltd.'s Registration Statement (File No. 000-28724) on Form 8-A/A.

² Incorporated by reference to Orckit Communications Ltd.'s Registration Statement (File No. 333-12178) on Form S-8.

³ Incorporated by reference to Orckit Communications Ltd.'s Annual Report on Form 20-F for the fiscal year ended December 31, 2000.

⁴ Incorporated by reference to Orckit Communications Ltd.'s Registration Statement (File No. 000-28724) on Form 8-A.

⁵ Incorporated by reference to Orckit Communications Ltd.'s Annual Report on Form 20-F for the fiscal year ended December 31, 2001.

⁶ Incorporated by reference to Amendment No. 1 to Orckit Communications Ltd.'s Annual Report on Form 20-F/A for the fiscal year ended December 31, 1999.

⁷ Incorporated by reference to Orckit Communications Ltd.'s Annual Report on Form 20-F for the fiscal year ended December 31, 2002.

* Filed herewith.

SIGNATURES

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

ORCKIT COMMUNICATIONS LTD.

By: /s/ Izhak Tamir

Name: Izhak Tamir

Title: President

Date: April 21, 2004

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

2003 CONSOLIDATED FINANCIAL STATEMENTS

ORCKIT COMMUNICATIONS LTD.
(An Israeli Corporation)
2003 CONSOLIDATED FINANCIAL STATEMENTS

TABLE OF CONTENTS

	Page
REPORT OF INDEPENDENT AUDITORS	F-2
CONSOLIDATED FINANCIAL STATEMENTS:	
Balance sheets	F-3
Statements of operations	F-4
Statements of changes in shareholders' equity	F-5
Statements of cash flows	F-6
Notes to financial statements	F-7 - F-26

The amounts are stated in U.S. dollars (\$) in thousands.

REPORT OF INDEPENDENT AUDITORS

To the shareholders of

ORCKIT COMMUNICATIONS LTD.

We have audited the consolidated balance sheets of Orckit Communications Ltd. (the "Company") and its subsidiaries as of December 31, 2002 and 2003, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Israel and in the United States, including those prescribed by the Israeli Auditors (Mode of Performance) Regulations, 1973. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Company's Board of Directors and management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the aforementioned consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of December 31, 2002 and 2003 and the consolidated results of their operations, the changes in shareholders' equity and their cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States.

Tel Aviv, Israel
February 22, 2004

/s/ Kesselman & Kesselman
Certified Public Accountants (Isr.)

ORCKIT COMMUNICATIONS LTD.
(An Israeli Corporation)
CONSOLIDATED BALANCE SHEETS
(U.S. dollars in thousands)

	December 31	
	2002	2003
A s s e t s		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 10,165	\$ 10,048
Marketable securities (note 10a)	43,139	31,302
Bank deposits (note 10d)	10,545	273
Trade receivables (note 10b)	786	147
Other receivables (note 10c)	2,443	1,596
Inventories	100	100
T o t a l current assets	67,178	43,466
LONG-TERM INVESTMENTS:		
Marketable securities (note 10a)	46,576	31,160
Other (note 10d)	8,403	9,465
	54,979	40,625
LONG-TERM LOAN TO A RELATED PARTY (note 2)	7,000	
PROPERTY AND EQUIPMENT - net (note 3):	6,070	2,093
DEFERRED ISSUANCE COSTS , net of accumulated amortization (note 1g)	623	147
T o t a l assets	\$ 135,850	\$ 86,331
Liabilities and shareholders' equity		
CURRENT LIABILITIES:		
Trade payables	\$ 4,827	\$ 3,108
Accrued expenses and other payables (note 10e)	7,158	5,878
T o t a l current liabilities	11,985	8,986
LONG-TERM LIABILITIES:		
Accrued severance pay (note 4)	3,265	3,435
Convertible subordinated notes (note 5)	38,179	16,238
T o t a l long-term liabilities	41,444	19,673
COMMITMENTS (note 6)		
T o t a l liabilities	53,429	28,659
SHAREHOLDERS' EQUITY (note 7):		
Share capital - ordinary shares of no par value and paid-in capital (authorized 10,000,000 shares; issued: December 31, 2002 - 4,979,593 shares; December 31, 2003 - 5,216,593 shares; outstanding: December 31, 2002 - 4,979,593 shares; December 31, 2003 - 4,334,980 shares)	322,227	325,512
Deferred compensation	(2,023)	(2,797)
Accumulated deficit	(237,783)	(259,399)
Treasury shares, at cost (881,613 ordinary shares)	(5,644)	(5,644)
T o t a l shareholders' equity	82,421	57,672
T o t a l liabilities and shareholders' equity	\$ 135,850	\$ 86,331

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

ORCKIT COMMUNICATIONS LTD.
(An Israeli Corporation)
CONSOLIDATED STATEMENTS OF OPERATIONS
(U.S. dollars in thousands, except per share data)

	Year ended December 31		
	2001	2002	2003
REVENUES (note 10f)	\$ 141,647	\$ 53,420	\$ 1,683
COST OF REVENUES (note 10g)	112,007	32,963	748
GROSS PROFIT	29,640	20,457	935
RESEARCH AND DEVELOPMENT EXPENSES - net (note 10h)	19,085	19,291	15,003
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	16,993	14,699	12,656
AMORTIZATION AND IMPAIRMENT OF GOODWILL (note 10i)	26,101		
OPERATING LOSS	(32,539)	(13,533)	(26,724)
FINANCIAL INCOME - net (note 10j)	33,395	17,616	5,108
NET INCOME (LOSS) FOR THE YEAR	<u>\$ 856</u>	<u>\$ 4,083</u>	<u>\$ (21,616)</u>
EARNINGS (LOSS) PER SHARE (“EPS”) (note 10k):			
Basic	<u>*\$ 0.18</u>	<u>\$ 0.83</u>	<u>\$ (4.99)</u>
Diluted	<u>*\$ 0.18</u>	<u>\$ 0.79</u>	<u>\$ (4.99)</u>
WEIGHTED AVERAGE NUMBER OF SHARES USED IN COMPUTATION OF EPS:			
Basic	<u>*4,632</u>	<u>4,932</u>	<u>4,332</u>
Diluted	<u>*4,875</u>	<u>5,163</u>	<u>4,332</u>

* After giving retroactive effect to the one-for-five reverse share split, see note 7a(2).

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

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(U.S. dollars in thousands)

	<u>Share capital</u>		<u>Additional paid-in capital</u>	<u>Deferred Compensation</u>	<u>Accumulated deficit</u>	<u>Treasury shares</u>	<u>Total shareholders' equity</u>
	<u>Number of shares * (in thousands)</u>	<u>Amount</u>					
BALANCE AT JANUARY 1, 2001	4,495	\$ 663	\$ 313,321		\$ (242,722)		\$ 71,262
CHANGES DURING 2001:							
Net income					856		856
Conversion of convertible subordinated notes into shares	30	3	246				249
Exercise of options granted to employees	350	44	723				767
Deferred compensation related to employee stock option grants			7,214	(7,214)			-,-
Amortization of deferred compensation related to employee stock option grants				3,651			3,651
BALANCE AT DECEMBER 31, 2001	4,875	710	321,504	(3,563)	(241,866)		76,785
CHANGES DURING 2002:							
Net income					4,083		4,083
Exercise of options granted to employees	105	13					13
Amortization of deferred compensation related to employee stock option grants				1,540			1,540
Cancellation of ordinary shares par value		(723)	723				-,-
BALANCE AT DECEMBER 31, 2002	4,980	-,-	322,227	(2,023)	(237,783)		82,421
CHANGES DURING 2003:							
Net loss					(21,616)		(21,616)
Issuance of shares to employees, exchangeable to options, see note 7a(5)	600		2,496	(2,496)			-,-
Exercise of options granted to employees	237		112				112
Acquisition of treasury stock	(882)					(5,644)	(5,644)
Exchange of shares into options, see note 7a(5)	(600)		1,284	(1,284)			-,-
Amortization of deferred compensation related to employee stock option grants, net of elimination of paid-in capital in respect of employee stock option grants due to forfeiture			(607)	3,006			2,399
BALANCE AT DECEMBER 31, 2003	4,335	\$ -,-	\$ 325,512	\$ (2,797)	\$ (259,399)	\$ (5,644)	\$ 57,672

* The figures for 2001 are after giving retroactive effect to the one-for-five reverse share split, see note 7a(2).

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

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

CONSOLIDATED STATEMENTS OF CASH FLOWS

(U.S. dollars in thousands)

	Year ended December 31		
	2001	2002	2003
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (loss) for the year	\$ 856	\$ 4,083	\$ (21,616)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization:			
Property and equipment	4,074	3,568	3,039
Deferred charges	3,411	393	139
Impairment of property and equipment			1,800
Goodwill and other identifiable intangible assets impairment	23,400		
Trading marketable securities, net	(33,214)	1,596	4,623
Gain from early extinguishment of convertible subordinated notes	(34,108)	(13,199)	(3,125)
Interest on long-term investments		(1,245)	(2,019)
Increase (decrease) in accrued severance pay	(798)	105	170
Amortization of deferred compensation related to employee stock option grants, net	3,651	1,540	2,399
Changes in operating assets and liabilities:			
Decrease in trade receivables and other receivables	22,209	8,580	1,486
Decrease in trade payables, accrued expenses and other payables	(31,564)	(7,954)	(2,999)
Decrease in inventories	40,083	9,197	-,
Net cash provided by (used in) operating activities	<u>(2,000)</u>	<u>6,664</u>	<u>(16,103)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property and equipment	(2,415)	(1,842)	(862)
Bank deposits, net	33,015	2,565	10,272
Funds in respect of accrued severance pay	(8)	758	(557)
Long term investments			(499)
Collection of long-term loan granted		13,000	7,000
Maturities of marketable securities held to maturity			26,310
Purchase of marketable securities held to maturity		(35,596)	(1,667)
Net cash provided by (used in) investing activities	<u>30,592</u>	<u>(21,115)</u>	<u>39,997</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Cost of acquisition of treasury shares			(5,644)
Exercise of options granted to employees	767	13	112
Early extinguishment of convertible subordinated notes	(17,825)	(14,488)	(18,479)
Net cash used in financing activities	<u>(17,058)</u>	<u>(14,475)</u>	<u>(24,011)</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	11,534	(28,926)	(117)
BALANCE OF CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>27,557</u>	<u>39,091</u>	<u>10,165</u>
BALANCE OF CASH AND CASH EQUIVALENTS AT END OF YEAR	<u><u>\$ 39,091</u></u>	<u><u>\$ 10,165</u></u>	<u><u>\$ 10,048</u></u>
SUPPLEMENTARY DISCLOSURE OF CASH FLOW INFORMATION - CASH PAID DURING THE YEAR FOR:			
Interest	<u>\$ 6,527</u>	<u>\$ 3,152</u>	<u>\$ 1,077</u>
Advances to income tax authorities	<u>\$ 40</u>	<u>\$ 96</u>	<u>\$ 95</u>

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

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

a. General:

1) *Nature of operations*

Orckit Communications Ltd. ("Orckit") and its subsidiaries (together - the "Company") is an Israeli corporation that is engaged in the design, development, manufacture and marketing of advanced telecom equipment, targeting high capacity broadband services. In the reported years, substantially all of the Company's revenues were derived from the sale of ADSL (Asymmetric Digital Subscriber Line) broadband equipment. Revenues from this product line have decreased significantly and the Company does not expect to derive significant revenues from this product line.

Orckit has initiated and funded a number of technology projects that are being developed by subsidiaries of Orckit, including the development, manufacturing and marketing of RPR-based telecom equipment by Corrigent Systems, and DSL-based telecom equipment by Spediant Systems.

2) *Functional currency*

The currency of the primary economic environment in which the operations of the Company and its subsidiaries are conducted is the U.S. dollar ("dollar" or "\$"), since most of their revenues were and are expected to be earned in dollars, most purchases of materials and components are made in dollars, most of the financing activities of the Company are in dollars and most of its assets are denominated in dollars.

Transactions and balances originally denominated in dollars are presented in their original amounts. Balances in non-dollar currencies are translated into dollars using historical and current exchange rates for non-monetary and monetary balances, respectively. For non-dollar transactions reflected in the statements of operations, the exchange rates at transaction dates are used. Depreciation and amortization and changes in inventories derived from non-monetary items are based on historical exchange rates. The resulting currency transaction gains or losses are carried to financial income or expenses, as appropriate.

3) *Accounting principles*

The consolidated financial statements are prepared in accordance with generally accepted accounting principles ("GAAP") in the United States.

4) *Use of estimates in the preparation of financial statements*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reported years. Actual results could differ from those estimates.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

b. Principles of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries.

Intercompany balances and transactions have been eliminated.

c. Marketable securities

Marketable securities classified as trading securities are recorded at fair market value, with unrealized gains and losses included in financial income or expenses.

Debt securities that the Company plans to and based on its assessment has the ability to, hold to maturity, are classified as "held to maturity" and are recorded at amortized cost. The premium or discount is amortized over the period to maturity and included in financial income.

d. Property and equipment:

- 1) These assets are stated at cost.
- 2) The assets are depreciated by the straight-line method on the basis of their estimated useful life, as follows:

	<u>Years</u>
Computers, software and equipment	3-5
Office furniture and equipment	6-16

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

e. Impairment in value of property and equipment

Effective January 1, 2002, the Company adopted FAS 144 "Accounting for the Impairment or Disposal of Long-Lived Assets" ("FAS 144"). FAS 144 require that long-lived assets, held and used by an entity be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. Under FAS 144, if the sum of the expected future cash flows (undiscounted and without interest charges) of the long-lived assets is less than the carrying amount of such assets, an impairment loss would be recognized, and the assets would be written down to their estimated fair values.

f. Goodwill and other identifiable intangible assets

Prior to January 1, 2002, the Company amortized goodwill and other identifiable intangible assets in equal annual installments, over a period of 3 years. In addition, the Company accounted for the impairment of goodwill and other identifiable intangible assets in accordance with FAS 121 "Accounting for the Impairment of Long-Lived Assets and for the Long-Lived Assets to be Disposed of". As a result, in 2001 the Company wrote off its remaining goodwill and other identifiable intangible assets.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):**

Effective January 1, 2002, the Company adopted FAS 142 “Goodwill and Other Intangibles Assets”. However, the Company had neither goodwill nor other identifiable intangible assets in 2002. Accordingly, this adoption has no effect on the results of operations for 2002 and 2003.

The following table illustrates the Company's net income adjusted to eliminate the effect of goodwill amortization expense for 2001:

	Year ended December 31		
	2001 *	2002	2003
	In thousands, except for per share data		
Net income (loss), as reported	\$ 856	\$ 4,083	\$ (21,616)
Add back - goodwill amortization	2,701	-,-	-,-
Adjusted net income (loss)	<u>\$ 3,557</u>	<u>\$ 4,083</u>	<u>\$ (21,616)</u>
Earnings (loss) per share:			
Basic – as reported	\$ 0.18	\$ 0.83	\$ (4.99)
Basic - adjusted	\$ 0.77	\$ 0.83	\$ (4.99)
Diluted - as reported	\$ 0.18	\$ 0.79	\$ (4.99)
Diluted - adjusted	\$ 0.73	\$ 0.79	\$ (4.99)

* The entire unamortized balance of goodwill, in the amount of \$23.4 million, was written off in 2001, see also note 10i.

g. Deferred issuance costs

Issuance costs of convertible subordinated notes, in the original amount of \$ 4,531,000, are amortized by the straight-line method, in proportion to the balance of notes outstanding, over the period from issuance date to the maturity date. Upon the retirement of any notes, the unamortized balance is adjusted proportionately.

h. Treasury shares

Company shares purchased by the Company are presented as a reduction of shareholders' equity, at their cost to the Company.

i. Revenue recognition

Revenues from sales of products are recognized when title passes to the customer, provided that appropriate signed documentation of the arrangement, such as a contract, purchase order or letter of agreement, has been received, the fee is fixed or determinable and collectibility is reasonably assured.

j. Provision for servicing products under warranty

The Company grants warranty servicing for products sold. The Company provides for such warranty at the time revenues from the related sales are recognized. The annual provision is calculated as a percentage of the sales, based on historical experience.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

k. Research and development expenses

Research and development expenses are charged to income as incurred. Governments grants received for development of projects are recognized as a reduction of the expenses.

l. Allowance for doubtful accounts

The allowance in respect of trade receivables has been determined for specific debts doubtful of collection, see note 10b.

m. Cash equivalents

The Company considers all highly liquid investments, which include short-term bank deposits (up to three months from date of deposit) that are not restricted as to withdrawal or use, to be cash equivalents.

n. Earnings (loss) per share

Basic earning per share is computed by dividing the net income (loss) by the weighted average number of shares outstanding during each year, net of treasury and restricted shares.

In computing diluted earning per share, the potential dilutive effect of outstanding stock options was taken into account using the treasury stock method. See also note 10k.

Weighted average number of ordinary shares outstanding used in the computation of the basic and diluted net income (loss) per share has been calculated after giving retroactive effect in all the reported periods to a one-for-five reverse share split effective as of November 27, 2002 (see note 7a(2)).

o. Comprehensive income

The Company has no comprehensive income components other than net income (loss).

p. Stock based compensation

The Company accounts for employee stock based compensation in accordance with Accounting Principles Board Opinion ("APB") No. 25 "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations. Under APB 25, compensation cost for employee stock option plans is measured using the intrinsic value based method of accounting (see also note 7a(5)). In accordance with Statement of Financial Accounting Standards ("FAS") No. 123 of the Financial Accounting Standards Board of the United States ("FASB") - "Accounting for Stock-Based Compensation" the Company discloses pro forma data assuming the Company had accounted for employee stock option grants using the fair value-based method defined in FAS 123.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):**

The following table illustrates the effect on net income (loss) and earnings (loss) per share assuming the Company had applied the fair value recognition provisions of FAS 123 to its stock-based employee compensation

	Year ended December 31		
	2001	2002	2003
	In thousands, except for per share data		
Net income (loss), as reported	\$ 856	\$ 4,083	\$ (21,616)
Add: stock based employee Compensation expense, included in reported net income (loss)	3,651	1,540	2,399
Deduct: stock based employee Compensation expense determined under fair value method for all awards	(10,824)	(2,916)	(3,177)
Pro forma net income (loss)	<u>\$ (6,317)</u>	<u>\$ 2,707</u>	<u>\$ (22,394)</u>
Earnings (loss) per share:			
Basic - as reported	\$ 0.18	\$ 0.83	\$ (4.99)
Basic - pro forma	\$ (1.15)	\$ 0.55	\$ (5.17)
Diluted - as reported	\$ 0.18	\$ 0.79	\$ (4.99)
Diluted - pro forma	\$ (1.15)	\$ 0.52	\$ (5.17)

q. Deferred income taxes

Deferred taxes are determined utilizing the asset and liability method, based on the estimated future tax effects differences between the financial accounting and tax bases of assets and liabilities under the applicable tax laws. Valuation allowances are included in respect of deferred tax assets when it is more likely than not that no such assets will be realized (see also note 8).

r. Shipping and handling fees and costs

Shipping and handling costs are classified as a component of cost of revenues.

s. Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity

In May 2003, the FASB issued FAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" (FAS 150). FAS 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. FAS 150 is effective for financial instruments entered into or modified after May 31, 2003, and otherwise (except for certain instruments) is effective at the beginning of the first interim period beginning after June 15, 2003. Effective July 1, 2003, the Company adopted FAS 150. The adoption of FAS 150 did not have a material effect on the company's financial position or results of operations.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):

t. Guarantor's Accounting and Disclosure Requirements for Guarantees

In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 requires that a liability be recorded on the guarantor's balance sheet upon issuance of a guarantee. In addition, FIN 45 requires disclosures about the guarantees that an entity has issued.

For U.S. GAAP purposes, the company has applied the recognition provisions of FIN 45 prospectively to guarantees issued or modified after December 31, 2002 as required by the interpretation. The recognition provisions of FIN 45 did not have a material effect on the company's consolidated financial statements. See note 10e for additional disclosures required under FIN 45.

u. Recently issued accounting pronouncements:

1) FIN 46 and FIN 46 (revised)

In January 2003, the FASB issued FASB Interpretation No. 46, "Consolidation of Variable Interest Entities" (FIN 46). Under FIN 46, entities are separated into two populations: (1) those for which voting interests are used to determine consolidation (this is the most common situation) and (2) those for which variable interests are used to determine consolidation. FIN 46 explains how to identify Variable Interest Entities (VIEs) and how to determine when a business enterprise should include the assets, liabilities, non controlling interests, and results of activities of a VIE in its consolidated financial statements.

Since issuing FIN 46, the FASB has proposed various amendments to the Interpretation and has deferred its effective dates. Most recently, in December 2003, the FASB issued a revised version of FIN 46 (FIN 46-R), which also provides for a partial deferral of FIN 46. This partial deferral established the effective dates for public entities to apply FIN 46 and FIN 46-R based on the nature of the variable interest entity and the date upon which the public company became involved with the variable interest entity. In general, the deferral provides that (i) for variable interest entities created before February 1, 2003, a public entity must apply FIN 46-R at the end of the first interim or annual period ending after March 15, 2004, and may be required to apply FIN 46 at the end of the first interim or annual period ending after December 15, 2003, if the variable interest entity is a special purpose entity, and (ii) for variable interest entities created after January 31, 2003, a public company must apply FIN 46 at the end of the first interim or annual period ending after December 15, 2003, as previously required, and then apply FIN 46-R at the end of the first interim or annual reporting period ending after March 15, 2004.

The Company has currently no variable interests in any VIE. Accordingly, the Company believes that the adoption of FIN 46 and FIN 46-R will not have material impact on its financial position, results of operations and cash flows.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)**NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (continued):****2) FAS 132 (revised)**

In December 2003, the FASB issued SFAS No. 132 (revised 2003), "Employers' Disclosures about Pensions and Other Postretirement Benefits, an amendment of FASB Statements No. 87, 88 and 106, and a revision of FASB Statement No. 132 ("FAS 132 (revised 2003)") ". This Statement revises employers' disclosures about pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans. The new rules require additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other postretirement benefit plans.

Part of the new disclosures provisions are effective for 2003 calendar year-end financial statements, and accordingly have been applied by the company in these consolidated financial statements. The rest of the provisions of this Statement, which have a later effective date, are currently being evaluated by the Company.

v. Reclassifications

Certain comparative figures have been reclassified to conform to the current year presentation.

NOTE 2 - LONG-TERM LOAN TO A RELATED PARTY

In 2000, a loan agreement was entered into with Tikcro Technologies Ltd. ("Tikcro", previously known as Tioga Technologies Ltd.) as part of the spin-off of the Company's semiconductor business to Tikcro. The agreement provided for borrowings in the amount of up to \$20 million with loans bearing interest at rate of approximately 6% per annum. Tikcro borrowed \$20 million under this loan agreement.

During 2002, Tikcro repaid \$ 13.0 million in principal amount of the loan. In 2003, Tikcro paid the remaining principal balance outstanding on the loan plus accrued interest.

NOTE 3 - PROPERTY AND EQUIPMENT

Composition of assets, grouped by major classification, is as follows:

	December 31	
	2002	2003
	In thousands	
Cost:		
Computers, software and equipment	\$ 16,090	\$ 16,931
Office furniture and equipment	1,375	1,380
Leasehold improvements	2,175	2,190
	<u>\$ 19,640</u>	<u>\$ 20,501</u>
Less - accumulated depreciation and amortization		
	<u>13,570</u>	<u>18,408</u>
	<u>\$ 6,070</u>	<u>\$ 2,093</u>

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 3 - PROPERTY AND EQUIPMENT (continued):

Depreciation expenses totaled \$ 4,074,000, \$ 3,568,000 and \$ 3,039,000 in the years ended December 31, 2001, 2002 and 2003, respectively.

In addition, the Company recorded an impairment of property and equipment in the amount of approximately \$1.8 million, representing write-off of property and equipment relating to the ADSL product line (see also note 1a)

NOTE 4 - SEVERANCE PAY:

- a. Israeli labor laws and agreements require payment of severance pay upon dismissal of an employee or upon termination of employment in certain other circumstances. The Company's severance pay liability to its employees, mainly based upon length of service and the latest monthly salary (one month's salary for each year worked) is reflected by the balance sheet accrual under "accrued severance pay". The Company records the liability as if it were payable at each balance sheet date on an undiscounted basis.

The liability is partly funded by purchase of insurance policies or pension funds and the amounts funded are included in the balance sheet under "long term investments - other". The policies are the Company's assets and under labor agreements, subject to certain limitations, they may be transferred to the ownership of the beneficiary employees. The amounts funded as of December 31, 2002 and 2003 are approximately \$ 2,150,000 and \$ 2,707,000, respectively.

In several of the Company's agreements, the Company makes regular deposits with the insurance companies for securing the employee rights upon retirement. Thus, in accordance with these agreements, the Company is fully relieved from any severance pay liability. The liability accrued in respect of these employees and the amounts funded, as of the agreement date, are not reflected in the balance sheets, since the amounts funded are not under the control and management of the Company.

- b. The amounts of pension and severance pay expense were \$ 1,001,000, \$ 844,000 and \$ 776,000 for the years ended December 31, 2001, 2002 and 2003, respectively, of which \$ 15,000 in 2003 was in respect of the insurance policies that were expensed but not reflected in the balance sheet as described above.
- c. The Company expects to contribute in 2004, \$ 900,000 to the insurance companies and pension funds, in respect of its severance pay liabilities expected for 2004 operations.

NOTE 5 - CONVERTIBLE SUBORDINATED NOTES:

- a. Under an Offering Memorandum dated March 7, 2000, the Company issued \$ 125,000,000 principal amount of convertible subordinated notes (the "Notes") that are due on April 1, 2005. The Notes bear interest at an annual rate of 5.75% payable April 1 and October 1 of each year. Unless previously redeemed, the Notes are convertible by the holder at any time through maturity into ordinary shares of the Company and Tikcro. The conversion rate is equal to 2.34962 ordinary shares of Orckit plus 11.7481 ordinary shares of Tikcro for each \$ 1,000 principal amount of Notes. The Notes are redeemable at the option of the Company, in whole or in part, at any time on or after April 1, 2003 at the redemption price, plus interest accrued to the redemption date. Each holder of Notes will have the right to cause the Company to purchase all of such holder's Notes in the event of a change of control in the Company, for cash or shares, at the election of the Company.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 5 - CONVERTIBLE SUBORDINATED NOTES (continued):

b. Early extinguishment of the Notes

During 2001, 2002 and 2003, the Company retired \$ 53.6 million, \$ 28.2 million and \$ 22.0 principal amount of the Notes. As of December 31, 2003, the total principal amount of Notes outstanding was \$ 16.2 million.

The Company has recorded in financial income gains of \$ 34.1 million, \$ 13.2 million and \$ 3.1 million from early extinguishments of Notes in the years ended December 31, 2001, 2002 and 2003, respectively.

- c. In January 2003, the Company repurchased from Clal Electronic Industries Ltd. ("Clal"), at the time a related party, 616,590 of Orckit's ordinary shares and \$12.5 million principal amount of Orckit's Notes for a total consideration of approximately \$14.7 million in cash. The Company attributed \$11 million of the consideration to the principal amount of the Notes and accrued interest and \$ 3.7 million of the consideration to the repurchase of the shares.
- d. On January 15, 2004, Orckit announced that its Board of Directors had approved the redemption of all of the outstanding Notes. The redemption price is equal to the principal amount of the Notes plus accrued and unpaid interest to the redemption date. The Notes are expected to be redeemed in full on April 1, 2004.

NOTE 6 - COMMITMENTS:

a. Royalty commitment

The Company is committed to pay royalties to the Government of Israel on proceeds from sales of products funded, in part, by Government grants. At the time the grants were received, successful development of the related projects was not assured.

In the case of failure of a project that was partly financed by royalty-bearing Government participations, the Company is not obligated to pay any royalties to the Government.

The royalty rate, based on the sales of products or development resulting from funded research and development projects, was fixed at 3% during the first three years and 4-5% thereafter. Royalties are payable up to 100% of the amount of such grants, with the addition of annual interest based on LIBOR. The total aggregate contingent liability of the Company and its subsidiaries in respect of royalties to the Government of Israel at December 31, 2003 was approximately \$12 million.

In the event that any of the manufacturing rights or technology are transferred out of Israel, subject to the approval of the Government of Israel, the Company would be required to pay royalties at a higher rate and an increased aggregate pay back amount in the range of 120% to 300% of the grants received, based on the applicable project.

b. Lease commitments

The Company has entered into one main operating lease agreement for the premises it uses. The Company has an option to terminate this agreement by giving a six month notice in advance.

The projected annual rental payments for 2004, at rates in effect at December 31, 2003, are approximately \$ 500,000.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 – SHAREHOLDERS' EQUITY:

a. Share capital:

- 1) The Company's ordinary shares are traded in the United States on the Nasdaq National Market, under the symbol "ORCT". As of April 2002, the Company's ordinary shares also began to trade on the Tel-Aviv Stock Exchange.

- 2) *Reverse share split*

On November 12, 2002, the Company's shareholders approved a one-for-five reverse share split, pursuant to which every five ordinary shares were combined into one ordinary share. Prior to the reverse share split, the shareholders of the Company approved an amendment to the Article of Association of the Company, changing the Ordinary Shares of NIS 0.10 par value into Ordinary Shares with no par value. All share and per share data included in these financial statements have been retroactively adjusted to reflect the one-for-five reverse share split, which was effective as of November 27, 2002. The conversion ratio of the Notes and the number of options and their exercise price were adjusted as a result of the reverse share split.

- 3) *Treasury shares*

During 2003, the Company acquired 881,613 ordinary shares of the Company at a cost of \$ 5,644,000 (see also note 5c).

- 4) *Exercise of options*

Under the Employee Share Option Plan (see b. below), options to purchase 349,907, 105,466, and 237,368 ordinary shares were exercised in the years ended December 31, 2001, 2002 and 2003, respectively.

- 5) In January 2003, the Company adopted the "Orckit Communications Ltd. 2003 Subsidiary Employee Share Incentive Plan" (the "2003 Plan"). Pursuant to the 2003 Plan and subject to applicable laws and regulations, the Company issued, for no consideration, 600,000 of its ordinary shares to employees of its subsidiaries, excluding directors of the Company. The shares were duly authorized and validly issued, fully paid and nonassessable. The shares were deposited with a trustee and were to vest after a period of 3 years. According to the 2003 Plan, the shares issued may be exchanged at any time by the Company, in its discretion, for a number of options to purchase shares of the applicable subsidiary.

During 2003, 60,000 shares were forfeited and 540,000 shares were exchanged to options to purchase shares of subsidiaries. The accounting treatment applied in respect of the plan is variable accounting until the exchange occurred. Accordingly, compensation in respect of the grant of the shares was measured according to the share price of Orckit and updated to reflect the changes in the share price through the date of the exchange. The compensation measured totaled approximately \$ 3.8 million, which is to be amortized over the vesting period of the options granted, of which in 2003 approximately \$1.3 was amortized. Upon the exchange, the plan became a fixed plan and the compensation was fixed according to the share price of Orckit on that date. At the date of exchange, the intrinsic value of options to purchase shares of subsidiaries that employees received was zero.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - SHAREHOLDERS' EQUITY (continued):

b. Employee Share Option Plan:

- On February 18, 1994, the Company's Board of Directors approved an Employee Share Option Plan (the "Plan"). The total aggregate number of shares authorized for which options could be granted under the Plan (as amended in 2003) was 2,198,047 at December 31, 2003, of which options to purchase 132,007 and 457,723 shares, at December 31, 2002 and 2003, respectively, were available for future grant. With respect to options outstanding at December 31, 2003, see (2) below. Each option can be exercised to purchase one ordinary share having the same rights as the other ordinary shares. The shares underlying these options were registered with the United States Securities and Exchange Commission.

The options usually vest linearly over a period of up to 5 years as determined on the date of grant.

- A summary of the status of the Plan as of December 31, 2001, 2002 and 2003, and changes during the years ended on those dates is presented below.

	Year ended December 31					
	2001(1)		2002		2003	
	Number	Weighted average exercise price	Number	Weighted average exercise price	Number	Weighted average exercise price
Options outstanding at beginning of year	1,257,537	\$ 10.2	829,429	\$ 6.7	837,723	\$ 7.2
Changes in options during the year:						
Granted, at market value	255,420	\$ 5.0	190,000	\$ 3.6	232,500	\$ 3.5
Exercised	(349,907)	\$ 2.3	(105,466)		(237,368)	\$ 0.5
Forfeited	(333,621)	\$ 23.2	(76,240)	\$ 1.7	(158,216)	\$ 4.2
Options outstanding at year-end	<u>829,429</u>	\$ 6.7	<u>837,723</u>	\$ 7.2	<u>674,639</u>	\$ 9.0
Options exercisable at year-end	<u>327,355</u>	\$ 12.3	<u>431,903</u>	\$ 10.8	<u>399,411</u>	\$ 12.9
Weighted average fair value of options granted during the year (2)		<u>\$ 7.5</u>		<u>\$ 3.8</u>		<u>\$ 4.0</u>

(1) In 2001, options to purchase 720,000 shares granted during 2001 and earlier years, with a weighted average exercise price of \$30.50 per share, were re-priced to the par value of the ordinary shares.

(2) The fair value of each option grant is estimated on the date of grant, inter alia, using the Black-Scholes option-pricing model with the following weighted average assumptions: Dividend yield is 0% for all years, expected volatility: 2001 - 115%; 2002 - 81%; 2003 - 59%. Risk-free interest rate: 2001 - 4.00%; 2002 - 4.00%; 2003 1.5% and average expected life of approximately 3 years.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - SHAREHOLDERS' EQUITY (continued):

3) The following table summarizes information about options outstanding at December 31, 2003:

Range of exercise price	Options outstanding			Options exercisable	
	Number outstanding at December 31, 2003 (1)	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at December 31, 2003	Weighted average exercise price
\$		Years	\$		\$
0	200,318	6.2	0	158,493	0
3-7	265,840	9.4	3.5	49,570	3.5
8-15	36,000	8.3	8.3	19,375	8.3
20-30	83,759	4.4	21.6	83,760	21.6
30-60	88,722	5.6	34.1	88,213	34.1
	<u>674,639</u>		9.0	<u>399,411</u>	12.9

(1) Including options to purchase 200,000 ordinary shares at a weighted average exercise price of \$3.1 that were granted to directors of the Company.

c. Grant of stock and option plans of subsidiaries

The Board of Directors of the Company's subsidiaries, Corrigent Systems and Spediant Systems, approved employee share option plans (the "Corrigent Subsidiary Plan", the "Spediant Subsidiary Plan", and together, the "Subsidiaries Plans"). Each of Corrigent Systems and Spediant Systems has granted, and reserved for grant, shares and options under its respective Subsidiary Plan and other plans, as applicable, to its employees, officers and directors and to personnel of Orckit, including employees, officers and directors of Orckit. As determined by the respective stock option committee, the exercise price of options granted is zero which represents the value of the shares on grant day. The vesting period of options granted is up to four years from the date of grant. As of December 31, 2003, on a fully diluted basis, Orckit's holding in each of Corrigent and Spediant was approximately 70%.

The intrinsic value and the weighted fair value of options granted by the subsidiaries is \$ 0. Accordingly, no compensation expense in respect of the options granted was recorded other than \$ 1.3 million amortization of compensation measured upon exchange of Orckit shares, see a(5) above.

d. Dividends

In the event cash dividends are declared by the Company, such dividends will be declared and paid in Israeli currency.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 7 - SHAREHOLDERS' EQUITY (continued):

e. Shareholder Bonus Rights Plan

On November 21, 2001, the Company's Board of Directors adopted a Shareholder Bonus Rights Plan (the "Rights Plan") pursuant to which share purchase bonus rights (the "Rights") were distributed on December 6, 2001 at the rate of one Right for each of the Company's ordinary shares held by shareholders of record as of the close of business on that date.

The Rights Plan is intended to help ensure that all of the Company's shareholders are able to realize the long-term value of their investment in the Company in the event of a potential takeover which does not reflect the full value of the Company and is otherwise not in the best interests of the Company and its shareholders. The Rights Plan is also intended to deter unfair or coercive takeover tactics.

The Rights generally will be exercisable and transferable apart from the Company's ordinary shares only if a person or group becomes an "Acquiring Person" by acquiring beneficial ownership of 15% or more of the Company's ordinary shares, subject to certain exceptions set forth in the Rights Plan, or commences a tender or exchange offer upon consummation of which such person or group would become an Acquiring Person. Subject to certain conditions described in the Rights Plan, once the Rights become exercisable, the holders of Rights, other than the Acquiring Person, will be entitled to purchase ordinary shares at a discount from the market price.

NOTE 8 - TAXES ON INCOME:

a. Tax benefits under the Law for the Encouragement of Capital Investments, 1959 (the "law")

Under the law, by virtue of the "approved enterprise" status granted to its enterprise, the Company is entitled to various tax benefits, including the following:

1) *Reduced tax rates*

The period of tax benefits is 7 years, commencing in the first year which the Company earns taxable income from the approved enterprise, subject to certain limitations. Income derived from the approved enterprise is tax exempt for a period of 2 years, after which the income from these enterprises is taxable at the rate of 25% for 5 years, the remainder of the period of tax benefits.

2) *Conditions for entitlement to the benefits*

The entitlement to the above benefits is conditional upon the Company's fulfilling the conditions stipulated by the law, regulations published thereunder and the instruments of approval for the specific investments in approved enterprises. In the event of failure to comply with these conditions, the benefits may be cancelled and the Company may be required to refund the amount of the benefits, in whole or in part, with the addition of linkage differences to the Israeli consumer price index (the "Israeli CPI") and interest.

In the event of distribution of cash dividends out of income which was tax exempt as above, the Company would have to pay 25% tax in respect of the amount distributed.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - TAXES ON INCOME (continued):

b. Measurement of the results for tax purposes under the Income Tax (Inflationary Adjustments) Law, 1985

Results for tax purposes are measured on a real basis - adjusted for the increase in the Israeli CPI. As explained in note 1a(3), the financial statements are presented in dollars. The difference between the change in the Israeli CPI and the NIS-dollar exchange rate - both on annual and cumulative bases - causes a difference between taxable income and income reflected in these financial statements.

Paragraph 9 (f) of FAS 109, "Accounting for Income Taxes", prohibits the recognition of deferred tax liabilities or assets that arise from differences between the financial reporting and tax bases of assets and liabilities that are measured from the local currency into dollars using historical exchange rates, and that result from changes in exchange rates or indexing for tax purposes. Consequently, the abovementioned differences were not reflected in the computation of deferred tax assets and liabilities.

c. Tax rates applicable to income from other sources:

1) Income from other sources in Israel

Income not eligible for approved enterprise benefits mentioned in a. above is taxed at the statutory corporate rate of 36%.

2) Income of non-Israeli subsidiaries

Non-Israeli subsidiaries are taxed according to the tax laws in their countries of residence.

d. Deferred income taxes

At December 31, 2003, the Company and its subsidiaries had accumulated tax losses amounting to approximately \$ 130 million (December 31, 2002 - approximately \$88 million) and carryforward capital losses for tax purposes of approximately \$ 40 million (December 31, 2002 - \$ 35 million). These losses are mainly denominated in NIS, linked to the Israeli CPI and are available indefinitely to offset future taxable business income. The Company and each of its subsidiaries are assessed on a stand-alone basis, hence accumulated tax losses in each of the entities can offset future taxable business income in the entity they were generated.

At December 31, 2003, the Company and its subsidiaries had net deferred tax asset (mostly in respect of carryforward losses and capital losses), in the amount of approximately \$ 44 million (December 31, 2002 - approximately \$40 million; December 31, 2001 - approximately \$36 million). A valuation allowance for the entire amount of such asset was set up, and consequently no deferred tax asset is recorded in the balance sheet, since it is more likely than not that the deferred tax assets will not be realized in the foreseeable future.

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 8 - TAXES ON INCOME (continued):

e. Tax rate reconciliation

In 2003, the main reconciling item from the statutory tax rate of the Company (36%, representing a theoretical tax benefit of approximately \$ 8 million) to the effective tax rate (0%) is the non-recognition of tax benefits in respect of tax losses incurred in the reported year. In 2002 and 2001, the main reconciling item from the statutory tax rate of the Company (36%, representing theoretical tax expenses of approximately \$ 1.5 million and \$300,000 respectively) to the effective tax rate (0%) is the utilization of carryforward tax losses for which deferred taxes were not created in previous years.

f. Tax assessments

The Company has received final assessments through the year ended December 31, 2000.

NOTE 9 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT:

a. Balances in non-dollar currencies:

1) As follows:

	December 31, 2003
	<u>In thousands</u>
Assets	<u>4,979</u>
Liabilities	<u>8,290</u>

The above mainly represents balances in Israeli currency.

2) Data regarding the rate of exchange and the Israeli CPI:

	Year ended December 31		
	<u>2001</u>	<u>2002</u>	<u>2003</u>
Rate of devaluation (evaluation) of the Israeli Currency against the dollar	9.3%	7.3%	(7.6)%
Rate of increase (decrease) in the Israeli CPI	1.4%	6.5%	(1.9)%
Exchange rate at end of year - \$ 1=	NIS 4.416	NIS 4.737	NIS 4.379

b. Fair value of financial instruments

The fair value of financial instruments included in working capital and of the Notes is usually identical or close to their carrying value.

As to the fair value of the Company's securities that are held to maturity, see note 10a(2).

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 9 - FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued):

c. Concentrations of credit risks

At December 31, 2002 and 2003, primarily all of the Company's and its subsidiaries' cash and cash equivalents were held by Israeli and International bank institutions. Primarily all of the Company's marketable securities were held by international bank institutions. Such securities represented debentures issued by a number of corporations. The Company evaluates on a current basis its financial exposure with any financial institution or commercial issuer.

The Company is of the opinion that the exposure to credit risk relating to trade receivables is limited. An appropriate allowance for doubtful accounts is included in the accounts.

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION:

Balance sheets:

a. Marketable securities:

1) *Trading securities*

At December 31, 2003, the Company held trading securities in the amount of \$ 20.5 million (December 31, 2002 - \$ 25.1 million). These securities are classified as short-term investments.

2) *Held-to-maturity tradable securities*

The securities mature over the following years:

	December 31	
	2002	2003
	In thousands	
	Carrying amounts	
Classified as short-term investments	\$16,856	\$10,054
Due after 1 year up to 4 years	46,576	31,160
	<u>\$63,432</u>	<u>\$41,214</u>

At December 31, 2003, the fair value of the Company's held-to-maturity tradable securities is \$ 42.2 million (December 31, 2002 - \$ 64.1 million). The difference between the carrying amounts and the fair value is a result of unrealized gains in the amount of approximately \$1 million (December 31, 2002 - \$700,000).

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):

	December 31	
	2002	2003
	In thousands	
b. Trade receivables:		
Open accounts	\$ 869	\$ 230
Less - allowance for doubtful accounts	<u>83</u>	<u>83</u>
	<u>\$ 786</u>	<u>\$ 147</u>
Allowance for doubtful accounts:		
Balance at beginning of year	\$ 549	\$ 83
Increase (decrease) during the year	<u>(466)</u>	
Balance at end of year	<u>\$ 83</u>	<u>\$ 83</u>
c. Other receivables		
Employees and employee institutions	\$ 133	\$ 63
Government of Israel	813	996
Prepaid expenses	778	493
Sundry	<u>719</u>	<u>44</u>
	<u>\$ 2,443</u>	<u>\$ 1,596</u>

d. Bank deposits

At December 31, 2003, the Company had short-term bank deposits - denominated in dollars in the amount of \$ 300,000, and long-term bank deposits - denominated in dollars and bearing annual interest at a fixed rate of 4.42% - in the amount of \$ 6.3 million.

e. Accrued expenses and other payables:

	December 31	
	2002	2003
	In thousands	
Employees and employee institutions	\$ 1,375	\$ 2,088
Provision for vacation pay	1,654	2,162
Provision for servicing products under warranty *	1,218	434
Accrued royalties	772	122
Accrued interest	549	233
Sundry	<u>1,590</u>	<u>839</u>
	<u>\$ 7,158</u>	<u>\$ 5,878</u>

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)**NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):**

	December 31	
	2002	2003
	In thousands	
* The changes in the balance during the year:		
Balance at beginning of year	\$2,330	\$1,218
Payments made under the warranty	(122)	(98)
Product warranties issued for new sales	658	34
Changes in accrual in respect of pre-existing warranties	(1,648)	(720)
Balance at end of year	<u>\$1,218</u>	<u>\$434</u>

Statements of operations:**f. Segment information and revenues from principal customers**

The Company operates in one operating segment.

Disaggregated financial data is provided below as follows: (1) revenues by geographic area; and (2) revenues from principal customers:

1) *Geographic information*

Following is a summary of revenues by geographic area. The Company sells its products mainly to telecommunications carriers. Revenues are attributed to geographic areas based on the location of the end users as follows:

	Year ended December 31		
	2001	2002	2003
	In thousands		
Israel	\$ 2,268	\$ 463	\$ 35
United States	111,336	44,811	
Europe	23,319	7,601	1,510
Other countries	4,724	545	138
	<u>\$ 141,647</u>	<u>\$ 53,420</u>	<u>\$ 1,683</u>

Most of the Company's property and equipment are located in Israel.

2) Revenues from principal customers - revenues from single customers each of which exceeds 10% of total revenues in the relevant year:

	Year ended December 31		
	2001	2002	2003
	In thousands		
Customer A	<u>\$ 111,208</u>	<u>\$ 43,912</u>	
Customer B	<u>\$ 20,973</u>	<u>\$ 7,209</u>	<u>\$ 530</u>

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (continued):**g. Cost of revenues:**

	Year ended December 31		
	2001	2002	2003
	In thousands		
Materials consumed, subcontractors and other production expenses (*)	\$ 84,136	\$ 27,702	\$ 533
Payroll and related expenses	3,517	1,207	
Depreciation	631	174	199
Decrease in inventories of products in process and finished products	23,723	3,274	
Other		606	16
	<u>\$ 112,007</u>	<u>\$ 32,963</u>	<u>\$ 748</u>

h. Research and development expenses - net:

Total expenses	\$ 22,429	\$ 22,266	\$ 20,803
L e s s - grants and participations, see note 7	3,344	2,975	5,800
	<u>\$ 19,085</u>	<u>\$ 19,291</u>	<u>\$ 15,003</u>

(*) Including purchases from Tikcro, which amount to \$ 1,418,000 and \$ 200,000 for the years ended December 31, 2001 and 2002, respectively.

i. Amortization and impairment of goodwill

In 2001, the Company elected to halt operations of an acquired subsidiary and filed a request in the Israeli district court for liquidation of its assets and debts. As a result, an amount of \$23.4 million which represented all outstanding unamortized goodwill and other intangible assets was written off by the Company.

j. Financial income - net:

	Year ended December 31		
	2001	2002	2003
	In thousands		
Income:			
Interest on bank deposits	\$ 3,184	\$ 1,207	\$ 557
Gain and interest on marketable securities	2,567	3,819	2,883
Gain from early extinguishments of notes	34,108	13,199	3,125
Interest on long-term loan (see note 2)		2,885	114
Other	595	198	62
	<u>\$ 40,454</u>	<u>\$ 21,308</u>	<u>\$ 6,741</u>

ORCKIT COMMUNICATIONS LTD.

(An Israeli Corporation)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

NOTE 10 - SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION

(continued):

	Year ended December 31		
	2001	2002	2003
	In thousands		
Expenses:			
Interest in respect of convertible subordinated notes	\$ 5,862	\$ 3,086	\$ 1,114
Amortization of convertible subordinated notes issuance costs	710	393	139
Other (mainly currency transaction gains and losses) - net	487	213	380
	<u>7,059</u>	<u>3,692</u>	<u>1,633</u>
	<u>\$ 33,395</u>	<u>\$ 17,616</u>	<u>\$ 5,108</u>

k. Net income (loss) per share

	Year ended December 31		
	2001	2002	2003
	In thousands		
Numerator - Basic			
Net income (loss)	<u>\$ 856</u>	<u>\$ 4,083</u>	<u>\$ (21,616)</u>
Denominator - Basic			
Weighted average ordinary shares outstanding (net of treasury shares)	<u>4,632</u>	<u>4,932</u>	<u>4,332</u>
Basic net income (loss) per share	<u>\$ 0.18</u>	<u>\$ 0.83</u>	<u>\$ (4.99)</u>
Numerator - Diluted	<u>\$ 856</u>	<u>\$ 4,083</u>	<u>\$ (21,616)</u>
Denominator - Diluted			
Weighted average ordinary shares outstanding	4,632	4,932	4,332
Dilutive potential of ordinary shares equivalents - options	<u>243</u>	<u>231</u>	<u></u>
	<u>4,875</u>	<u>5,163</u>	<u>4,332</u>
Diluted net income (loss) per share	<u>\$ 0.18</u>	<u>\$ 0.79</u>	<u>\$ (4.99)</u>

The potential effect of the convertible subordinated notes was not taken into account, since its effect is anti-dilutive. In 2003, the potential effect of the options was not taken into account, since its effect is anti-dilutive.

**REPORT OF INDEPENDENT AUDITORS ON
FINANCIAL STATEMENT SCHEDULE**

To the Board of Directors of
ORCKIT COMMUNICATIONS LTD.

Our audits of the consolidated financial statements of Orckit Communications Ltd. referred to in our report dated February 22, 2004 also included an audit of a Schedule – Valuation and Qualifying Accounts for each of the three years in the period ended December 31, 2003 (the “Schedule”). In our opinion, the Schedule presents fairly in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements.

Tel-Aviv, Israel
February 22, 2004

/s/ Kesselman & Kesselman
Certified Public Accountants (Israel)

ORCKIT COMMUNICATIONS LTD.
SCHEDULE - VALUATION AND QUALIFYING ACCOUNTS
Three Years Ended December 31, 2003
(U.S. \$ In thousands)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
	Balance at beginning of period	Additions charged to expenses	Deductions	Balance at end of period
Allowance for doubtful accounts:				
Year ended December 31, 2003	<u>\$ 83</u>	<u>\$ 63</u>	<u>\$ (63)</u>	<u>\$ 83</u>
Year ended December 31, 2002	<u>\$ 549</u>		<u>\$ (466)</u>	<u>\$ 83</u>
Year ended December 31, 2001	<u>\$ 150</u>	<u>\$ 399</u>		<u>\$ 549</u>

Orckit Communications Ltd.
Exhibit Index

<u>Exhibit Number</u>	<u>Title</u>
4.7	Spediant Stock Option Plan
4.8	Promissory Note dated March 30, 2004 made by Orckit Communications Ltd. to HSBC Bank USA
8.1	Subsidiaries of Orckit Communications Ltd.
12.1	Certification of Principal Executive Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act
12.2	Certification of Principal Financial Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act
13.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act
13.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act
14.1	Consent of Kesselman & Kesselman, independent auditors of Orckit Communications Ltd.

SPEDIANT SYSTEMS LTD.

SPEDIANT STOCK OPTION PLAN

A. NAME AND PURPOSE

1. **Name:** This plan, as amended from time to time, shall be known as the “Spediant Stock Option Plan” (the “**Plan**”).

2. **Purpose:** The purpose and intent of the Plan is to provide incentives to employees, directors, consultants and contractors of Spediant Systems Ltd. (“**Spediant**”) or Orckit Communications Ltd. (“**Orckit**”), companies organized under the laws of the State of Israel and any of Orckit’s controlled affiliates, or Spediant Systems, Inc, a company organized under the laws of the State of Delaware (collectively the “**Companies**”), by providing them with opportunities to purchase Ordinary Shares, no nominal value (“**Shares**”) of the Company, pursuant to a plan approved by the Board of Directors of the Company (the “**Board**”). Grants pursuant to the Plan will be subject to applicable tax laws, which may include, but not be limited to, the provisions of the US Internal Revenue Code of 1986, as amended (the “**Code**”), regarding incentive stock options (“**ISO’s**”) (Code Section 422), US non-statutory stock options (“**NSO’s**”) (not intended to satisfy the requirements of Code Section 422), or to Section 102 of the Israeli Income Tax Ordinance [New Version] 1961.

B. GENERAL TERMS AND CONDITIONS OF THE PLAN

3. **Administration:**

3.1 The Board may appoint a Share Incentive Committee which will consist of such number of Directors or officers of the Company, as may be fixed from time to time by the Board. The Board shall appoint the members of the Committee, may from time to time remove members from, or add members to, the Committee and shall fill vacancies in the Committee however caused. The Plan will be administered by the Share Incentive Committee, or where not permitted according to any applicable law, by the Board (collectively - the “**Committee**”).

3.2 The Committee shall select one of its members as its Chairman and shall hold its meetings at such times and places as it shall determine. Actions taken by a majority of the members of the Committee, at a meeting at which a majority of its members is present, or acts reduced to, or approved in, writing by all members of the Committee, shall be the valid acts of the Committee. The Committee may appoint a Secretary, who shall keep records of its meetings and shall make such rules and regulations for the conduct of its business as it shall deem advisable.

3.3 Subject to the general terms and conditions of this Plan, the Committee shall have the full authority in its discretion, from time to time and at any time, to determine (i) the persons (the "**Grantees**") to whom options to purchase Shares (the "**Options**") shall be granted, (ii) the number of Shares to be covered by each Option, (iii) the time or times at which the same shall be granted, (iv) the schedule and conditions on which such Options may be exercised and on which such Shares shall be paid for, (v) the type of plan or taxation route that shall govern the Options, as applicable (ISO, NSO, Section 102 or otherwise), (vi) to establish sub plans ("**Sub Plan**") for certain Grantees, as determined by the Committee (each Sub Plan shall be considered a Plan for purposes of this Plan), and/or (vi) any other matters which are necessary or desirable for, or incidental to the administration of the Plan.

3.4 The Committee may, from time to time, adopt such rules and regulations for carrying out the Plan as it may deem necessary. No member of the Board or of the Committee shall be liable for any act or determination made in good faith with respect to the Plan or any Option granted thereunder.

3.5 The interpretation and construction by the Committee of any provision of the Plan or of any Option thereunder shall be final and conclusive unless otherwise determined by the Board.

4. **Eligible Grantees:**

4.1 The Committee, at its discretion, may grant Options to any employee, director, consultant or contractor of the Company or its subsidiaries. Anything in this Plan to the contrary notwithstanding, grants of Options to directors, shall be authorized and implemented only in accordance with the provisions of applicable law.

4.2 The grant of an Option to a Grantee hereunder, shall neither entitle such Grantee to participate, nor disqualify him from participating, in any other grant of options pursuant to this Plan or any other share option plan of the Company.

5. **Grant of Options and Issuance of Shares in Trust:**

5.1 The effective date of the grant of an Option (the "**Date of Grant**") shall be the date the Committee resolved to award the Option, unless otherwise specified by the Committee in its determination relating to the award of such Option.

5.2 Anything herein to the contrary notwithstanding, Options granted under the Plan to Grantees may be granted by the Company to a trustee designated by the Committee and, if required under applicable law, approved by the Israeli Commissioner of Income Tax (the "**Trustee**"), and the Trustee shall hold each such Option and the Shares issued upon exercise thereof in trust (the "**Trust**") for the benefit of the Grantee in respect of whom such Option was granted (the "**Beneficial Grantee**"). All certificates representing Shares issued to the Trustee under the Plan shall be deposited with the Trustee, and shall be held by the Trustee until such time that such Shares are released from the Trust as herein provided.

5.3 (a) With respect to Options granted to the Trustee under Sections 102(a) or 102(b) of the Israeli Income Tax Ordinance ("**102 Options**"), the following shall apply:

(i) A Grantee granted 102 Options shall not be entitled to sell the Shares received upon exercise thereof (the "**Exercised Shares**") or to transfer such Exercised Shares (or such 102 Options) from the Trust prior to the "End of the Period" (as defined in Section 102 of the Income Tax Ordinance);

(ii) Any and all rights issued in respect of the Exercised Shares, including bonus shares but excluding cash dividends ("**Rights**"), shall be issued to the Trustee and held by the Trustee until the End of the Period, and such Rights shall be subject to the taxation route which is applicable to such Exercised Shares.

Notwithstanding the aforesaid, Exercised Shares or Rights may be sold or transferred, and the Trustee may release such Exercised Shares (or 102 Options) or Rights from Trust, prior to the End of the Period, provided however, that tax is paid or withheld in accordance with Section 102(b)(4) of the Ordinance, and subject to the other provisions of this Plan.

(b) In the event an Option is granted under Section 102(c) of the Income Tax Ordinance to a Grantee who is an employee at the time of such grant, if the Grantee's employment is terminated, for any reason, such Grantee shall provide the Company with a guarantee or collateral, as determined by the Committee, securing the payment of all taxes required to be paid upon the sale of the Exercised Shares received upon exercise of such Option.

5.4 Anything in this Plan to the contrary notwithstanding (including the provisions of Section 10 hereof) and subject to the requirements of any applicable law, no Options or Shares shall be released from the Trust and no Grantee shall be entitled to exercise Options until the earlier of (i) the lapse of seven (7) years from the Date of Grant; or (ii) the date on which the Options are exercisable for securities traded on a stock exchange or for cash.

5.5 Voting Rights. All voting rights attached to the shares upon the exercise of Options granted under the Plan (including without limitation upon conversion pursuant to Section 5.6 below or upon acceleration pursuant to Section 11 below), shall be held by the Trustee, for so long as such shares are held by the Trustee. The Trustee will vote such shares according to the instruction of the majority of the Voting Stock (as defined below) of the Company applicable to shares that are not subject to repurchase (the “**Majority of the Voting Stock**”). The Trustee shall not vote any such shares at any shareholders' meeting, either of the Company or of any other applicable company subject to Section 5.6 below, unless it has received instructions from the Majority of the Voting Stock as to how to vote such shares at the said shareholders' meeting.

5.6 Conversions into shares of Other Companies. The Board may, at any time and at its discretion, convert all or part of (i) the Options into options to purchase shares of other company(ies) (including shares of Orckit or any of its affiliates) (the “**Target Company**”), or (ii) in the event of any Shares issued upon exercise of such Option, convert all or part of such Shares into shares of the Target Company.

The conversion ratio upon which such conversion shall be conducted, shall be determined by the Board according to the fair market value of the shares of the Target Company and the Company (the “**Conversion ratio**”).

6. **Reserved Shares:** The Company has reserved authorized but unissued Shares for purposes of the Plan subject to adjustments as provided in Section 11 hereof. The Board may increase the number of authorized but unissued Shares for purposes of the Plan from time to time. All Shares under the Plan, in respect of which the right hereunder of a Grantee to purchase the same shall, for any reason, terminate, expire or otherwise cease to exist, shall again be available for grant through Options under the Plan.

7. **Grant of Options:** The Committee in its discretion may award to Grantees Options available under the Plan. Unless otherwise specified by the committee, each Option shall expire ten years after the Date of Grant or otherwise as provided in section 10.1 below provided that the expiration date and the vesting schedule may be changed in whole or per person at the Committee’s sole discretion.

8. **Exercise Price:** The exercise price per Share covered by each Option shall be determined by the Committee in its sole and absolute discretion in accordance with applicable law, subject to guidelines as shall be issued by the Board from time to time (“**Exercise Price**”).

9. **Exercise of Options:**

9.1 Options shall be exercisable pursuant to the terms under which they were awarded and subject to the terms and conditions of the Plan. Anything herein to the contrary notwithstanding, but without derogating from the provisions of Section 10 hereof, if any Option has not been exercised and the Shares covered thereby not paid for within ten (10) years after the Date of Grant (or any shorter period determined by the Committee) or otherwise as provided in section 10.1(d) below, such Option and the right to acquire such Shares shall terminate, all interests and rights of the Grantee in and to the same shall ipso facto expire. The option committee may limit execution of Options for certain periods.

9.2 Each payment for Shares shall be in respect of a whole number of Shares, and shall be effected in cash or by a bank's check payable to the order of the Company, or such other method of payment acceptable to the Company.

10. **Termination of Employment or Service:**

10.1 Subject to the provisions of Section 5.4 hereto, in the event that a Grantee who was an employee of the Companies on the Date of Grant of any Options ceases, for any reason, to be employed by the Companies ("Termination of Employment"), all Options theretofore granted to such Grantee when such Grantee was an employee of the Companies shall terminate as follows (for the purpose of this Plan, the date of Termination of Employment shall be deemed as occurring not later than two months after notifying the employee of termination, or receiving notice of termination from the employee, as the case may be, unless determined otherwise by the Company's management ("**Date of Termination of Employment**")):

(a) All such Options, which are not vested at the Date of Termination of Employment shall terminate immediately.

(b) If the Grantee's Termination of Employment is due to (i) the Grantee has committed any flagrant criminal offense, or (ii) the Grantee has committed a fraudulent act towards the Companies, or (iii) the Grantee caused intentionally, by act or omission, any financial damage to the Companies, all the Options whether vested or not shall ipso facto expire immediately and be of no legal effect.

(c) Subject to Sub Sections (a) and (b) above, unless otherwise determined by the Committee, all vested Options shall expire six months following the Date of Termination of Employment, if not exercised prior to such date.

10.2 The transfer of a Grantee from the Company to the affiliated Company, shall not be deemed a Termination of Employment for purposes hereof. Whether an authorized leave of absence on military, governmental or public service or otherwise, or termination of employment under certain conditions, shall constitute Termination of Employment for the purposes hereof shall be conclusively determined by the Committee.

10.3 Subject to the provisions of Section 5.4 hereto, in the event that a Grantee who is a director, consultant or contractor of the Companies, ceases, for any reason, to serve as such prior to the vesting of any of his Options, all Options theretofore granted to such Grantee which are not yet so vested in such Grantee shall terminate on such date of cessation of service as a director, consultant or contractor (“**Date of Cessation**”) and the provisions of Sections 10.1(a), 10.1(b), 10.1(c) and 10.1(d) shall apply *mutatis mutandis*, to such cessation of service. For the purposes of this Section 10, Date of Cessation shall mean:

(a) With regard to directors, the date on which a director submits notice of resignation from the Board or the date on which the shareholders of the Companies remove such director from the Board; and

(b) With regard to consultants and contractors, the date on which the consulting or contractor agreement between such consultant or contractor, as applicable, and the Companies or the date on which either of the parties to such agreement sends the other notice of its intention to terminate said agreement.

10.4 Notwithstanding the foregoing provisions of this Section 10, the Committee may provide, either at the time an Option is granted or thereafter, that such Option may be exercised after the periods provided for in this Section 10, but in no event beyond the term of the Option.

11. Adjustment Upon Changes in Capitalization:

11.1 Subject to any required action by the shareholders of the Company, the number of Shares covered by each outstanding Option, and the number of Shares which have been authorized for issuance under the Plan but as to which no Options have yet been granted or which have been returned to the Plan upon cancellation or expiration of an Option, as well as the price per share of Shares covered by each such outstanding Option, shall be proportionately adjusted for 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 the payment of a stock dividend (bonus shares) with respect to the Shares or any other increase or decrease in the number of issued Shares effected without receipt of consideration by the Company; 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 Committee, whose determination in that respect shall be final, binding and conclusive. Except as expressly provided herein, no issuance by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall affect, and no adjustment by reason thereof shall be made with respect to, the number or price of Shares subject to an Option.

11.2 Unless otherwise provided by the Board, in the event of the proposed dissolution or liquidation of the Company, all outstanding Options will terminate immediately prior to the consummation of such proposed action.

11.3 If, upon a Merger or Sale of all of the Company's Assets (as hereinafter defined), the consideration received (the "Consideration") shall be the exchange of the securities of the Company for the securities of another corporation or a parent or subsidiary of such other corporation (each, a "**Successor Entity**"), then, each Option shall, at the sole and absolute discretion of the Committee, either:

(a) Be substituted for options to purchase shares of the Successor Entity, and appropriate adjustments shall be made in the exercise price per share to reflect such exchange; or

(b) Be assumed by the Successor Entity such that the Grantee may exercise the Options for such number of shares of the Successor Entity or amount of other securities thereof, and appropriate adjustments shall be made in the purchase price per share to reflect such exchange.

Anything herein to the contrary notwithstanding, the provisions of this Section 11.3 shall be subject to all the terms and provisions of the Plan remaining in full force and effect.

"Merger" means a merger or consolidation or a similar business combination, 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 the persons holding those securities immediately prior to such transaction.

“Sale of All of the Company’s Assets” means the sale, transfer or other disposition of all or substantially all of the Company’s assets.

11.4 Unless otherwise provided by the Company’s incorporation documents, in the event that all or substantially all of the issued and outstanding share capital of the Company is to be sold (the “**Sale**”), each Grantee shall be obligated to participate in the Sale and sell its shares and/or Options in the Company, provided, however, that any and all rights, preferences, and privileges previously granted to any such Grantee shall remain in effect and shall apply to the shares and/or Options sold under this Section 11.4.

11.5 Change of Control: “Change of Control” shall mean the occurrence of any of the following for as long as Orckit (directly or indirectly) holds more than 50% of the Voting Stock of the Company:

(a) any “person,” as such term is currently used in Section 13(d) of the Securities Exchange Act of 1934, as amended (the “1934 Act”) (a “**person**”), becomes a “beneficial owner” (as such term is currently used in Rule 13d-3 promulgated under the 1934 Act (a “**Beneficial Owner**”) of 10% or more of the Voting Stock of Orckit without the approval of the Board of Directors of Orckit, provided that if any person is the Beneficial Owner of 10% or more of the Voting Stock of Orckit on January 1st, 2001, based on such person’s reports filed pursuant to Section 13(d) of the 1934 Act and the related regulations or otherwise reported to the Company in writing, a “Change of Control” under this clause (a) shall not be deemed to occur unless and until such person’s Beneficial Ownership of the Voting Stock of Orckit has increased by 10% or more following January 1st, 2001 without the approval of the Board of Directors of Orckit;

(b) the Board of Directors of Orckit adopts any plan of liquidation providing for the distribution of all or substantially all of Orckit’s assets;

(c) all or substantially all of the assets or business of Orckit, including its holdings in the Company, are disposed of in any one or more transactions pursuant to a merger, consolidation or other transaction (unless the shareholders of Orckit immediately prior to such merger, consolidation or other transaction beneficially own, directly or indirectly, in substantially the same proportion as they owned the Voting Stock of Orckit, all of the Voting

Stock or other ownership interests of the entity or entities, if any, that succeed to the business of Orckit);

(d) Orckit combines with another company and is the surviving corporation but, immediately after the combination, the shareholders of Orckit immediately prior to the combination hold, directly or indirectly, fifty percent (50%) or less of the Voting Stock of the combined company; or

(e) Continuing Directors cease to constitute at least a majority of the Board of Directors of Orckit.

“Voting Stock” of any entity shall mean the issued and outstanding share capital or other securities of any class or classes having general voting power under ordinary circumstances, in the absence of contingencies, to elect the members of the board of directors (or members of a similar managerial body if such entity has no board of directors) of such entity.

“Continuing Director” means a director who either was a director of Orckit on January 1st, 2001 or who became a director of Orckit subsequent to January 1st, 2001 and whose election, or nomination for election by Orckit’s shareholders, was approved by a majority of the Continuing Directors then on the Board of Directors of Orckit.

11.6 Acceleration of Vesting Period. In the event of any Change of Control, that was not approved by the board of directors of Orckit prior to such Change of Control, the following provisions shall apply:

(A) (i) immediately prior to such Change of Control, each outstanding Option not then vested, shall automatically vest and immediately thereafter, become exercised into a number of shares of Orckit to be determined in accordance with the Conversion Ratio (“**Accelerated Unvested Shares**”), and (ii) each outstanding vested Option not then exercised shall automatically become exercised into shares of Orckit to be determined in accordance with the Conversion Ratio (“**Accelerated Vested Shares**”), so that all options granted under this Plan shall, immediately prior to the effective date of the Change

in Control, be fully exercised into the shares of Orckit. The Accelerated Unvested Shares and the Accelerated Vested Shares shall hereinafter collectively be referred to as the “Accelerated Shares”.

If the paid Exercise price will exceed the par value of the shares of Orckit, the Company at its discretion, may assist the Grantee and provide him with a loan in order to finance the purchase upon terms and conditions as determined by the Board. If a loan is not provided by the Board in respect of that portion of the Exercise Price exceeding par value, then acceleration of any then outstanding Option(s) shall occur only upon the approval of the Grantee.

(B) All Accelerated Shares received in accordance with (A), shall immediately become subject to a Repurchase Option (as hereinafter defined). The Accelerated Unvested Shares shall become Accelerated Vested Shares at the same ratio that the Options underlying such Restricted Shares would have become vested, had such Change of Control not occurred.

11.7 Repurchase Option. If following an event set out in Section 11.6(A), there shall occur an event set out in Section 10 of this Plan that would have caused any Options to terminate (“**An Offering Event**”), then, with respect to that Grantee only: (i) no additional Accelerated Unvested Shares shall become Accelerated Vested Shares, and (ii) subject to the provisions of Section 11.8 either the Company (or Orckit if a conversion into Orckit shares has occurred) shall thereafter have the right to repurchase all or part of the the Accelerated Unvested Shares, or upon the event set out in Section 10.1(b), of the Accelerated Shares (“**Repurchase Option**”).

11.8 Exercise of the Repurchase Option.

(i) Upon the occurrence of an Offering Event, the Company, or Orckit, may exercise the Repurchase Option by delivering personally, or by registered or certified mail, to the Grantee (or his permitted transferee or legal representative, as the case may be), within ninety (90) days after the date of the Offering Event, a notice in writing indicating its election to exercise its Repurchase Option and the number of shares to be purchased, and setting forth a date foreclosing not later than thirty (30) days from the date of

giving such notice.

(ii) At the closing for the repurchase of the shares pursuant to the exercise of the Repurchase Option, the holder of the certificate(s) representing such shares being transferred shall deliver said certificate or certificates evidencing such shares to the respective purchaser, duly endorsed for transfer, and the respective purchaser shall tender payment of the Option Price (as hereinafter defined) for the shares being purchased. The Option Price shall be payable in full in cash, or by check, provided that the Company may elect to offset against and deduct from any payment of the Option Price any indebtedness then owed by Grantee to the Company.

The “**Option Price**” shall be equal to the Exercise Price and in the event that a loan was provided to the Grantee as set out in Section 11.6 above, then such Exercise Price shall be increased in accordance with the then outstanding amount of the loan and interest due from the Grantee.

12. **Limitations on Transfer:** Unless otherwise determined by the Committee, no Option shall be assignable or transferable by the Grantee to whom granted otherwise than by will or the laws of descent and distribution, and an Option may be exercised during the lifetime of the Grantee only by such Grantee or by such Grantee's guardian or legal representative. The terms of such Option shall be binding upon the beneficiaries, executors, administrators, heirs and successors of such Grantee.

13. **Amendment of the Plan:** Subject to applicable laws, the Board may, at any time and from time to time, terminate or amend the Plan in any respect. In no event may any action of the Company alter or impair the rights of a Grantee, without his consent, under any Option previously granted to him.

14. **Tax Consequences:** All tax consequences and obligations regarding any other compulsory payments (of the Company or the Companies or the Grantee) arising from the grant or exercise of any Option, from the payment for, or the subsequent disposition of, Shares covered thereby or from any other event or act (of the Company or the Companies or the Grantee) hereunder, shall be borne solely by the Grantee, and the Grantee shall indemnify the Company or the Companies and the Trustee and hold them harmless against and from any and all

liability for any such tax or other compulsory payment, or interest or penalty thereon, including without limitation, liabilities relating to the necessity to withhold, or to have withheld, any such tax or other compulsory payment from any payment made to the Grantee.

15. Miscellaneous:

15.1 Continuance of Employment. Neither the Plan nor the grant of an Option thereunder shall impose any obligation on the Companies to continue the employment of any Grantee, and nothing in the Plan or in any Option granted pursuant thereto shall confer upon any Grantee any right to continue in the employ of the Companies, or restrict the right of the Companies to terminate such employment at any time.

15.2 Governing Law. The Plan and all instruments issued thereunder or in connection therewith, shall be governed by, and interpreted in accordance with, the laws of the State of New York. All disputes related to this Plan shall be resolved in accordance with commercial arbitration law by a single arbitrator selected by the Company.

15.3 Application of Funds. The proceeds received by the Company from the sale of Shares pursuant to Options granted under the Plan will be used for general corporate purposes of the Company.

15.4 Multiple Agreements. The terms of each Option may differ from other Options granted under the Plan at the same time, or at any other time. The Committee may also grant more than one Option to a given Grantee during the term of the Plan, either in addition to, or in substitution for, one or more Options previously granted to that Grantee. The grant of multiple Options may be evidenced by a single instrument of grant or multiple instruments of grant, as determined by the Committee.

15.5 Non-Exclusivity of the Plan. The adoption of the Plan by the Board shall not be construed as amending, modifying or rescinding any previously approved incentive arrangement or as creating any limitations on the power of the Board to adopt such other incentive arrangements as it may deem desirable, including, without limitation, the granting of stock options otherwise than under the Plan, and such arrangements may be either applicable generally or only in specific cases.

PROMISSORY NOTE
(LIBOR PRICING)

\$11,000,000.00

New York, New York
Date: March 30, 2004

FOR VALUE RECEIVED, the undersigned ("Maker") promises to pay to the order of HSBC BANK USA ("Bank") at its office located at 452 Fifth Avenue, New York, New York 10018 or at any of its other banking offices in New York as Bank may designate by written notice to Maker, the sum of ELEVEN MILLION UNITED STATES DOLLARS ON July 15, 2005, (the Maturity Date) together with interest from the date hereof on the unpaid principal of this Note until paid in full at the rate set forth below.

Interest on the unpaid principal amount of this Note shall be due and payable on September 27, 2004 and on the date on which the principal balance is due whether by acceleration or on the Maturity Date. This Note shall bear interest at a fixed rate per annum equal to 0.65% above LIBOR (the "Contract Rate"). "LIBOR" means the interest rate equal to the London Interbank Offered Rate shown on Bridge Telerate Screen, page 3750 or any successor page thereto, at the 11:00 A.M. (London time) fixing, rounded upward to the nearest 1/8th of 1%, two Business Days prior to the date of this Note for deposits of United States Dollars in an amount comparable to the principal amount of this Note for a period equal to 473 days.

After the principal of this Note becomes due, interest under this Note shall be payable on demand and interest shall accrue at a fluctuating rate per annum equal to 2% per annum above the Contract Rate. Interest shall be calculated on the basis of a 360-day year for actual days elapsed. In no event shall the interest rate applicable at any time to this Note exceed the maximum rate permitted by law.

This Note shall be payable in lawful money of the United States of America in immediately available funds. All payments on this Note shall be applied to the payment of accrued interest before being applied to the payment of principal. Any payment which is required to be made on a day which is not a Business Day (as defined below) shall be payable on the next succeeding Business Day and such additional time shall be included in the computation of interest. In the event that any other Obligations (as defined below) of Maker to Bank are due at any time that Bank receives a payment from Maker on account of this Note or any such other Obligations of Maker, Bank may apply such payment to amounts due under this Note or any such other Obligations in such manner as Bank, in its discretion, elects, regardless of any instructions from Maker to the contrary. As used herein, "Business Day" shall mean a day on which banks are regularly open for business in both London and New York City, New York other than a Saturday, Sunday or day on which banks are permitted to remain closed.

Maker shall be entitled to prepay the outstanding principal amount of this Note in whole or in part before 11:00 A.M. on any Business Day without the prior consent of Bank provided that any such prepayments shall be made together with (i) the payment of all interest accrued on the prepaid principal to the date of prepayment and (ii) the payment of the Liquidated Cost (as defined

below). As used herein, "Liquidated Cost" means, with respect to any prepayment, an amount necessary to compensate Bank for the cost of reinvesting, for the period extending to the last day of an Interest Period, the prepaid principal amount received by Bank at a rate or rates which may be less than the Contract Rate. Maker and Bank acknowledge that determining the actual amount of the Liquidated Cost may be difficult or impossible in any specific instance and accordingly Maker agrees with Bank that the Liquidated Cost shall equal the excess, if any, of (i) the product of (A) the amount of principal prepaid, multiplied by (B) the Contract Rate divided by 360, multiplied by (C) the remaining number of days from the date of the prepayment to the end of the Interest Period, over (ii) that amount of interest which Bank determines that the holder of a Treasury Obligation (as defined below) selected by Bank in the amount (or as close to such amount as is feasible) of the prepaid principal and having a maturity date on the last day of the Interest Period (or as soon thereafter as is feasible), would earn if that Treasury Obligation were purchased in the secondary market on the date of the prepayment and were held to the last day of the Interest Period. Maker agrees that the determination of Liquidated Cost shall be based on amounts which a holder of a Treasury Obligation could receive under these circumstances, whether or not Bank actually invests the prepaid principal amount in any Treasury Obligation. As used herein, "Treasury Obligation" means a note, bill or bond issued by the United States Treasury Department as a full faith and credit general obligation of the United States. Maker agrees that the payment of Liquidated Cost as a premium in connection with any prepayment is reasonable to compensate Bank for lost income resulting from such prepayment because Maker is receiving the benefit of having the Contract Rate priced based on LIBOR.

Upon the occurrence of any of the following (each, an "Event of Default") with respect to any Maker, indorser or guarantor of the indebtedness evidenced by this Note: (i) default in payment of any amount due under this Note or failure to comply with any warranty representation or covenant made herein; (ii) any of them shall commence any case, proceeding or other action under any law relating to bankruptcy, insolvency, reorganization or relief of debtors, seeking to have an order for relief entered with respect to any of them, or seeking to adjudicate any of them a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to any of them or any of their debts, or seeking appointment of a receiver, trustee, custodian or other similar official for any of them or for all or any substantial part of the assets of any of them, or any of them shall make a general assignment for the benefit of its creditors, or there shall be commenced against any of them any case, proceeding or other action of a nature referred to in this clause (ii), or there shall be commenced against any of them any case, proceeding or other action seeking issuance of a warrant of attachment, execution, distraint or similar process against all or any substantial part of the assets of any of them which results in the entry of an order for any such relief, or any of them shall take any action in furtherance of, or indicating its consent to, approval of, or acquiescence in, any of the acts set forth in this clause (ii), or any of them shall generally not, or shall be unable to, or shall admit in writing its inability to, pay its debts as they become due; (iii) entry of a judgment against any of them in an amount in excess of \$1,000,000 which has not been satisfied or vacated within 30 days of entry; (iv) failure to pay or remit any tax when assessed or due (unless appealed in good faith within 60 days); (v) dissolution; (vi) failing to furnish Bank with any requested financial information or failing to permit inspection of books or records by Bank or any of its agents, attorneys or accountants within 20 days following Bank's request; (vii) making any misrepresentation to Bank in obtaining credit for any of them; then, in the case of any Event of Default other than those referred to in clause (ii) of this

sentence, Bank may declare by notice to Maker any and all Obligations of Maker to be immediately due and payable, and in case of any Event of Default referred to in clause (ii) of this sentence all of the Obligations of Maker shall automatically become due and payable immediately without notice or demand.

Bank shall have a continuing lien and/or right of set-off on, and is hereby granted a security interest in, all deposits (general and special) and credits with Bank or any Bank Affiliate of any Maker and indorser, and may apply all or part of the same to any Obligations of Maker hereunder, at any time or times, without notice. Bank shall have a continuing lien on and is granted a security interest in all property of every Maker and indorser and the proceeds thereof held or received by Bank or any Bank Affiliate in an amount equal to the Collateral Value of such property required to pay the Obligations. As used herein the term "Collateral Value", shall mean the sum of any cash held and the sum of the respective products obtained by multiplying the fair market value, as determined by the Bank, of each type of marketable Security held in such Account, by the applicable percentage for such type of security in accordance with Bank's policy in effect from time to time. As used in this Note, the term "Bank Affiliate" includes any individual, partnership or corporation acting as nominee or agent for Bank, and any corporation or bank which is directly or indirectly owned or controlled by, or under common control with, Bank. Any notice of disposition of property shall be deemed reasonable if mailed at least five days before such disposition to the last address of Maker or indorser on Bank's records. If the Obligations of Maker to Bank evidenced by this Note are secured by a security agreement and/or other security documents which Maker has separately delivered to Bank (whether or not such documents make specific reference to this Note), reference to such documents is made for a description of the collateral provided thereby and of the rights of Maker and Bank therein. The rights and remedies of Bank provided for hereunder (including but not limited to the right to accelerate Obligations of Maker and to realize on any security for any such Obligations) are cumulative with the rights and remedies of Bank available under any other instrument or agreement or under applicable law. As used in this Note, the term "Obligations" of a person means all amounts payable under this Note. "Person" means any individual, partnership, limited partnership, corporation, association, trust or other entity.

In the case of the occurrence of an Event of Default, each Maker and indorser shall be jointly and severally liable for all costs of enforcement and collection of this Note incurred by Bank or any other holder of this Note, including but not limited to reasonable attorneys' fees, disbursements and court costs. In addition, in the event of a default hereunder, Maker shall pay all reasonable attorneys' fees and disbursements incurred by Bank in obtaining advice as to its rights and remedies in connection with such default.

Maker and each indorser hereby separately waive presentment, demand for payment, notice of dishonor, protest and notice of protest, and any or all other notices or demands in connection with the delivery, acceptance, performance, default, endorsement or guarantee of this Note. The liability of any Maker or indorser hereunder shall be unconditional and shall not be in any manner affected by any indulgence whatsoever granted or consented to by the holder hereof, including but not limited to any extension of time, renewal, waiver or other modification. Any failure of the holder to exercise any right hereunder shall not be construed as a waiver of the right to exercise the same or any other right at any time and from time to time thereafter. Bank or any holder may accept late payments, or partial payments, even though marked "payment in full" or containing

words of similar import or other conditions, without waiving any of its rights. No amendment, modification or waiver of any provision of this Note nor consent to any departure by Maker therefrom shall be effective, irrespective of any course of dealing, unless the same shall be in writing and signed by Bank, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. This Note cannot be changed or terminated orally or by estoppel or waiver or by any alleged oral modification regardless of any claimed partial performance referable thereto.

Any notice from Bank to Maker or any indorser shall be deemed given when delivered to Maker or such indorser by hand or when deposited in the United States mail and addressed to Maker or such indorser at the last address of Maker or such indorser appearing on Bank's records.

This Note shall be governed by and construed in accordance with the laws of the State of New York applicable to instruments made and to be performed wholly within that state. If any provision of this Note is held to be illegal or unenforceable for any reason whatsoever, such illegality or unenforceability shall not affect the validity of any other provision hereof.

MAKER AND EACH INDORSER AGREE THAT ANY ACTION, DISPUTE, PROCEEDING, CLAIM OR CONTROVERSY BETWEEN MAKER OR SUCH INDORSER AND BANK, WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE ("DISPUTE" OR "DISPUTES") SHALL, AT BANK'S ELECTION, WHICH ELECTION MAY BE MADE AT ANY TIME PRIOR TO THE COMMENCEMENT OF A JUDICIAL PROCEEDING BY BANK, OR IN THE EVENT OF A JUDICIAL PROCEEDING INSTITUTED BY MAKER OR SUCH INDORSER AT ANY TIME PRIOR TO THE LAST DAY TO ANSWER AND/OR RESPOND TO A SUMMONS AND/OR COMPLAINT MADE BY MAKER OR SUCH INDORSER, BE RESOLVED BY ARBITRATION IN ACCORDANCE WITH THE PROVISIONS OF THIS PARAGRAPH AND SHALL, AT THE ELECTION OF BANK, INCLUDE ALL DISPUTES ARISING OUT OF OR IN CONNECTION WITH (1) THIS NOTE OR ANY RELATED AGREEMENTS OR INSTRUMENTS, (2) ALL PAST, PRESENT AND FUTURE AGREEMENTS INVOLVING MAKER OR SUCH INDORSER AND BANK, (3) ANY TRANSACTION RELATED TO THIS NOTE AND ALL PAST, PRESENT AND FUTURE TRANSACTIONS INVOLVING MAKER OR SUCH INDORSER AND BANK, AND (4) ANY ASPECT OF THE PAST, PRESENT OR FUTURE RELATIONSHIP OF MAKER OR SUCH INDORSER AND BANK. Bank may elect to require arbitration of any Dispute with Maker or any indorser without thereby being required to arbitrate all Disputes between Bank and Maker or such indorser. Any such Dispute shall be resolved by binding arbitration in accordance with Article 75 of the New York Civil Practice Law and Rules and the Commercial Arbitration Rules of the American Arbitration Association ("AAA"). In the event of any inconsistency between such Rules and these arbitration provisions, these provisions shall supersede such Rules. All statutes of limitations which would otherwise be applicable shall apply to any arbitration proceeding under this paragraph. In any arbitration proceeding subject to this paragraph, the arbitration panel (the "arbitrator") is specifically empowered to decide (by documents only, or with a hearing, at the arbitrator's sole discretion) pre-hearing motions which are substantially similar to pre-hearing motions to dismiss and motions for summary adjudication. In any such arbitration proceeding, the arbitrator shall not have the power or

authority to award punitive damages to any party. Judgment upon the award rendered may be entered in any court having jurisdiction. Whenever an arbitration is required, the parties shall select an arbitrator in the manner provided in this paragraph. No provision of, nor the exercise of any rights under, this paragraph shall limit the right of Bank (1) to foreclose against any real or personal property collateral through judicial foreclosure, by the exercise of the power of sale under a deed of trust, mortgage or other security agreement or instrument, pursuant to applicable provisions of the Uniform Commercial Code, or otherwise herein pursuant to applicable law, (2) to exercise self-help remedies including but not limited to setoff and repossession, or (3) to request and obtain from a court having jurisdiction before, during or after the pendency of any arbitration, provisional or ancillary remedies and relief including but not limited to injunctive or mandatory relief or the appointment of a receiver. The institution and maintenance of an action or judicial proceeding for, or pursuit of, provisional or ancillary remedies or exercise of self-help remedies shall not constitute a waiver of the right of Bank, even if Bank is the plaintiff, to submit the Dispute to arbitration if Bank would otherwise have such right. Whenever an arbitration is required under this paragraph, the arbitrator shall be selected, except as otherwise herein provided, in accordance with the Commercial Arbitration Rules of the AAA. A single arbitrator shall decide any claim of \$100,000 or less and he or she shall be an attorney with at least five years' experience. Where the claim of any party exceeds \$100,000, the Dispute shall be decided by a majority of three arbitrators, at least two of whom shall be attorneys (at least one of whom shall have not less than five years' experience representing commercial banks). The arbitrator shall have the power to award recovery of all costs and fees (including attorneys' fees, administrative fees, arbitrator's fees, and court costs) to the prevailing party. In the event of any Dispute governed by this paragraph, each of the parties shall, subject to the award of the arbitrator, pay an equal share of the arbitrator's fees.

MAKER AND EACH INDORSER AGREE THAT ANY ACTION, SUIT OR PROCEEDING IN RESPECT OF OR ARISING OUT OF THIS NOTE MAY BE INITIATED AND PROSECUTED IN THE STATE OR FEDERAL COURTS, AS THE CASE MAY BE, LOCATED IN NEW YORK COUNTY, NEW YORK AND ANY ARBITRATION PROCEEDING PURSUANT HERETO SHALL BE CONDUCTED IN NEW YORK, NEW YORK. MAKER AND EACH INDORSER CONSENT TO AND SUBMIT TO THE EXERCISE OF JURISDICTION OVER ITS PERSON BY ANY SUCH COURT HAVING JURISDICTION OVER THE SUBJECT MATTER, WAIVE PERSONAL SERVICE OF ANY AND ALL PROCESS UPON IT AND CONSENT THAT ALL SUCH SERVICE OF PROCESS BE MADE BY REGISTERED MAIL DIRECTED TO MAKER OR SUCH INDORSER AT ITS ADDRESS SET FORTH BELOW OR TO ANY OTHER ADDRESS AS MAY APPEAR IN BANK'S RECORDS AS THE ADDRESS OF MAKER OR SUCH INDORSER.

IN ANY ACTION, SUIT OR PROCEEDING IN RESPECT OF OR ARISING OUT OF THIS NOTE, BANK, MAKER AND EACH INDORSER WAIVE TRIAL BY JURY, AND MAKER AND EACH INDORSER ALSO WAIVE (I) THE RIGHT TO INTERPOSE ANY SET-OFF OR COUNTERCLAIM OF ANY NATURE OR DESCRIPTION, (II) ANY OBJECTION BASED ON FORUM NON CONVENIENS OR VENUE, AND (III) ANY CLAIM FOR CONSEQUENTIAL, PUNITIVE OR SPECIAL DAMAGES.

If this Note is executed by more than one person, then each such person shall be jointly and severally liable on this Note, and the term "Maker" shall mean each, any or all of such persons.

Bank is authorized to fill in any blank spaces and to otherwise complete this Note and correct any patent errors herein.

Signature of Maker

Name of Maker (if not a natural person)

Orckit Communications Ltd

Print Name

By: /s/ Izhak Tamir, President

Address for Notices

Signature of Authorized Signatory

Signature of Maker

Print Name and Title

Izhak Tamir, President

Print Name

Address for Notices

Address for Notices

126 Yigal Alon st; Tel Aviv; Israel

[If Maker is not a natural person,
indicate the type of entity below]

The Maker signing above is a:

- 1 partnership
organized under the
laws of _____.
- 2 limited partnership
organized under the
laws of _____.
- X 3 corporation organized
under the laws of
Israel_____.
- 4 other (specify):

PROMISSORY NOTE
(LIBOR PRICING)

\$5,000,000.00

New York, New York

Date: March 30, 2004

FOR VALUE RECEIVED, the undersigned ("Maker") promises to pay to the order of HSBC BANK USA ("Bank") at its office located at 452 Fifth Avenue, New York, New York 10018 or at any of its other banking offices in New York as Bank may designate by written notice to Maker, the sum of FIVE MILLION UNITED STATES DOLLARS ON May 15, 2005, (the Maturity Date) together with interest from the date hereof on the unpaid principal of this Note until paid in full at the rate set forth below.

Interest on the unpaid principal amount of this Note shall be due and payable on September 27, 2004 and on the date on which the principal balance is due whether by acceleration or on the Maturity Date. This Note shall bear interest at a fixed rate per annum equal to 0.65% above LIBOR (the "Contract Rate"). "LIBOR" means the interest rate equal to the London Interbank Offered Rate shown on Bridge Telerate Screen, page 3750 or any successor page thereto, at the 11:00 A.M. (London time) fixing, rounded upward to the nearest 1/8th of 1%, two Business Days prior to the date of this Note for deposits of United States Dollars in an amount comparable to the principal amount of this Note for a period equal to 412 days.

After the principal of this Note becomes due, interest under this Note shall be payable on demand and interest shall accrue at a fluctuating rate per annum equal to 2% per annum above the Contract Rate. Interest shall be calculated on the basis of a 360-day year for actual days elapsed. In no event shall the interest rate applicable at any time to this Note exceed the maximum rate permitted by law.

This Note shall be payable in lawful money of the United States of America in immediately available funds. All payments on this Note shall be applied to the payment of accrued interest before being applied to the payment of principal. Any payment which is required to be made on a day which is not a Business Day (as defined below) shall be payable on the next succeeding Business Day and such additional time shall be included in the computation of interest. In the event that any other Obligations (as defined below) of Maker to Bank are due at any time that Bank receives a payment from Maker on account of this Note or any such other Obligations of Maker, Bank may apply such payment to amounts due under this Note or any such other Obligations in such manner as Bank, in its discretion, elects, regardless of any instructions from Maker to the contrary. As used herein, "Business Day" shall mean a day on which banks are regularly open for business in both London and New York City, New York other than a Saturday, Sunday or day on which banks are permitted to remain closed.

Maker shall be entitled to prepay the outstanding principal amount of this Note in whole or in part before 11:00 A.M. on any Business Day without the prior consent of Bank provided that any such prepayments shall be made together with (i) the payment of all interest accrued on the prepaid principal to the date of prepayment and (ii) the payment of the Liquidated Cost (as defined

below). As used herein, "Liquidated Cost" means, with respect to any prepayment, an amount necessary to compensate Bank for the cost of reinvesting, for the period extending to the last day of an Interest Period, the prepaid principal amount received by Bank at a rate or rates which may be less than the Contract Rate. Maker and Bank acknowledge that determining the actual amount of the Liquidated Cost may be difficult or impossible in any specific instance and accordingly Maker agrees with Bank that the Liquidated Cost shall equal the excess, if any, of (i) the product of (A) the amount of principal prepaid, multiplied by (B) the Contract Rate divided by 360, multiplied by (C) the remaining number of days from the date of the prepayment to the end of the Interest Period, over (ii) that amount of interest which Bank determines that the holder of a Treasury Obligation (as defined below) selected by Bank in the amount (or as close to such amount as is feasible) of the prepaid principal and having a maturity date on the last day of the Interest Period (or as soon thereafter as is feasible), would earn if that Treasury Obligation were purchased in the secondary market on the date of the prepayment and were held to the last day of the Interest Period. Maker agrees that the determination of Liquidated Cost shall be based on amounts which a holder of a Treasury Obligation could receive under these circumstances, whether or not Bank actually invests the prepaid principal amount in any Treasury Obligation. As used herein, "Treasury Obligation" means a note, bill or bond issued by the United States Treasury Department as a full faith and credit general obligation of the United States. Maker agrees that the payment of Liquidated Cost as a premium in connection with any prepayment is reasonable to compensate Bank for lost income resulting from such prepayment because Maker is receiving the benefit of having the Contract Rate priced based on LIBOR.

Upon the occurrence of any of the following (each, an "Event of Default") with respect to any Maker, indorser or guarantor of the indebtedness evidenced by this Note: (i) default in payment of any amount due under this Note or failure to comply with any warranty representation or covenant made herein; (ii) any of them shall commence any case, proceeding or other action under any law relating to bankruptcy, insolvency, reorganization or relief of debtors, seeking to have an order for relief entered with respect to any of them, or seeking to adjudicate any of them a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to any of them or any of their debts, or seeking appointment of a receiver, trustee, custodian or other similar official for any of them or for all or any substantial part of the assets of any of them, or any of them shall make a general assignment for the benefit of its creditors, or there shall be commenced against any of them any case, proceeding or other action of a nature referred to in this clause (ii), or there shall be commenced against any of them any case, proceeding or other action seeking issuance of a warrant of attachment, execution, distraint or similar process against all or any substantial part of the assets of any of them which results in the entry of an order for any such relief, or any of them shall take any action in furtherance of, or indicating its consent to, approval of, or acquiescence in, any of the acts set forth in this clause (ii), or any of them shall generally not, or shall be unable to, or shall admit in writing its inability to, pay its debts as they become due; (iii) entry of a judgment against any of them in an amount in excess of \$1,000,000 which has not been satisfied or vacated within 30 days of entry; (iv) failure to pay or remit any tax when assessed or due (unless appealed in good faith within 60 days); (v) dissolution; (vi) failing to furnish Bank with any requested financial information or failing to permit inspection of books or records by Bank or any of its agents, attorneys or accountants within 20 days following Bank's request; (vii) making any misrepresentation to Bank in obtaining credit for any of them; then, in the case of any Event of Default other than those referred to in clause (ii) of this

sentence, Bank may declare by notice to Maker any and all Obligations of Maker to be immediately due and payable, and in case of any Event of Default referred to in clause (ii) of this sentence all of the Obligations of Maker shall automatically become due and payable immediately without notice or demand.

Bank shall have a continuing lien and/or right of set-off on, and is hereby granted a security interest in, all deposits (general and special) and credits with Bank or any Bank Affiliate of any Maker and indorser, and may apply all or part of the same to any Obligations of Maker hereunder, at any time or times, without notice. Bank shall have a continuing lien on and is granted a security interest in all property of every Maker and indorser and the proceeds thereof held or received by Bank or any Bank Affiliate in an amount equal to the Collateral Value of such property required to pay the Obligations. As used herein the term "Collateral Value", shall mean the sum of any cash held and the sum of the respective products obtained by multiplying the fair market value, as determined by the Bank, of each type of marketable Security held in such Account, by the applicable percentage for such type of security in accordance with Bank's policy in effect from time to time. As used in this Note, the term "Bank Affiliate" includes any individual, partnership or corporation acting as nominee or agent for Bank, and any corporation or bank which is directly or indirectly owned or controlled by, or under common control with, Bank. Any notice of disposition of property shall be deemed reasonable if mailed at least five days before such disposition to the last address of Maker or indorser on Bank's records. If the Obligations of Maker to Bank evidenced by this Note are secured by a security agreement and/or other security documents which Maker has separately delivered to Bank (whether or not such documents make specific reference to this Note), reference to such documents is made for a description of the collateral provided thereby and of the rights of Maker and Bank therein. The rights and remedies of Bank provided for hereunder (including but not limited to the right to accelerate Obligations of Maker and to realize on any security for any such Obligations) are cumulative with the rights and remedies of Bank available under any other instrument or agreement or under applicable law. As used in this Note, the term "Obligations" of a person means all amounts payable under this Note. "Person" means any individual, partnership, limited partnership, corporation, association, trust or other entity.

In the case of the occurrence of an Event of Default, each Maker and indorser shall be jointly and severally liable for all costs of enforcement and collection of this Note incurred by Bank or any other holder of this Note, including but not limited to reasonable attorneys' fees, disbursements and court costs. In addition, in the event of a default hereunder, Maker shall pay all reasonable attorneys' fees and disbursements incurred by Bank in obtaining advice as to its rights and remedies in connection with such default.

Maker and each indorser hereby separately waive presentment, demand for payment, notice of dishonor, protest and notice of protest, and any or all other notices or demands in connection with the delivery, acceptance, performance, default, endorsement or guarantee of this Note. The liability of any Maker or indorser hereunder shall be unconditional and shall not be in any manner affected by any indulgence whatsoever granted or consented to by the holder hereof, including but not limited to any extension of time, renewal, waiver or other modification. Any failure of the holder to exercise any right hereunder shall not be construed as a waiver of the right to exercise the same or any other right at any time and from time to time thereafter. Bank or any holder may accept late payments, or partial payments, even though marked "payment in full" or containing

words of similar import or other conditions, without waiving any of its rights. No amendment, modification or waiver of any provision of this Note nor consent to any departure by Maker therefrom shall be effective, irrespective of any course of dealing, unless the same shall be in writing and signed by Bank, and then such waiver or consent shall be effective only in the specific instance and for the specific purpose for which given. This Note cannot be changed or terminated orally or by estoppel or waiver or by any alleged oral modification regardless of any claimed partial performance referable thereto.

Any notice from Bank to Maker or any indorser shall be deemed given when delivered to Maker or such indorser by hand or when deposited in the United States mail and addressed to Maker or such indorser at the last address of Maker or such indorser appearing on Bank's records.

This Note shall be governed by and construed in accordance with the laws of the State of New York applicable to instruments made and to be performed wholly within that state. If any provision of this Note is held to be illegal or unenforceable for any reason whatsoever, such illegality or unenforceability shall not affect the validity of any other provision hereof.

MAKER AND EACH INDORSER AGREE THAT ANY ACTION, DISPUTE, PROCEEDING, CLAIM OR CONTROVERSY BETWEEN MAKER OR SUCH INDORSER AND BANK, WHETHER SOUNDING IN CONTRACT, TORT OR OTHERWISE ("DISPUTE" OR "DISPUTES") SHALL, AT BANK'S ELECTION, WHICH ELECTION MAY BE MADE AT ANY TIME PRIOR TO THE COMMENCEMENT OF A JUDICIAL PROCEEDING BY BANK, OR IN THE EVENT OF A JUDICIAL PROCEEDING INSTITUTED BY MAKER OR SUCH INDORSER AT ANY TIME PRIOR TO THE LAST DAY TO ANSWER AND/OR RESPOND TO A SUMMONS AND/OR COMPLAINT MADE BY MAKER OR SUCH INDORSER, BE RESOLVED BY ARBITRATION IN ACCORDANCE WITH THE PROVISIONS OF THIS PARAGRAPH AND SHALL, AT THE ELECTION OF BANK, INCLUDE ALL DISPUTES ARISING OUT OF OR IN CONNECTION WITH (1) THIS NOTE OR ANY RELATED AGREEMENTS OR INSTRUMENTS, (2) ALL PAST, PRESENT AND FUTURE AGREEMENTS INVOLVING MAKER OR SUCH INDORSER AND BANK, (3) ANY TRANSACTION RELATED TO THIS NOTE AND ALL PAST, PRESENT AND FUTURE TRANSACTIONS INVOLVING MAKER OR SUCH INDORSER AND BANK, AND (4) ANY ASPECT OF THE PAST, PRESENT OR FUTURE RELATIONSHIP OF MAKER OR SUCH INDORSER AND BANK. Bank may elect to require arbitration of any Dispute with Maker or any indorser without thereby being required to arbitrate all Disputes between Bank and Maker or such indorser. Any such Dispute shall be resolved by binding arbitration in accordance with Article 75 of the New York Civil Practice Law and Rules and the Commercial Arbitration Rules of the American Arbitration Association ("AAA"). In the event of any inconsistency between such Rules and these arbitration provisions, these provisions shall supersede such Rules. All statutes of limitations which would otherwise be applicable shall apply to any arbitration proceeding under this paragraph. In any arbitration proceeding subject to this paragraph, the arbitration panel (the "arbitrator") is specifically empowered to decide (by documents only, or with a hearing, at the arbitrator's sole discretion) pre-hearing motions which are substantially similar to pre-hearing motions to dismiss and motions for summary adjudication. In any such arbitration proceeding, the arbitrator shall not have the power or

authority to award punitive damages to any party. Judgment upon the award rendered may be entered in any court having jurisdiction. Whenever an arbitration is required, the parties shall select an arbitrator in the manner provided in this paragraph. No provision of, nor the exercise of any rights under, this paragraph shall limit the right of Bank (1) to foreclose against any real or personal property collateral through judicial foreclosure, by the exercise of the power of sale under a deed of trust, mortgage or other security agreement or instrument, pursuant to applicable provisions of the Uniform Commercial Code, or otherwise herein pursuant to applicable law, (2) to exercise self-help remedies including but not limited to setoff and repossession, or (3) to request and obtain from a court having jurisdiction before, during or after the pendency of any arbitration, provisional or ancillary remedies and relief including but not limited to injunctive or mandatory relief or the appointment of a receiver. The institution and maintenance of an action or judicial proceeding for, or pursuit of, provisional or ancillary remedies or exercise of self-help remedies shall not constitute a waiver of the right of Bank, even if Bank is the plaintiff, to submit the Dispute to arbitration if Bank would otherwise have such right. Whenever an arbitration is required under this paragraph, the arbitrator shall be selected, except as otherwise herein provided, in accordance with the Commercial Arbitration Rules of the AAA. A single arbitrator shall decide any claim of \$100,000 or less and he or she shall be an attorney with at least five years' experience. Where the claim of any party exceeds \$100,000, the Dispute shall be decided by a majority of three arbitrators, at least two of whom shall be attorneys (at least one of whom shall have not less than five years' experience representing commercial banks). The arbitrator shall have the power to award recovery of all costs and fees (including attorneys' fees, administrative fees, arbitrator's fees, and court costs) to the prevailing party. In the event of any Dispute governed by this paragraph, each of the parties shall, subject to the award of the arbitrator, pay an equal share of the arbitrator's fees.

MAKER AND EACH INDORSER AGREE THAT ANY ACTION, SUIT OR PROCEEDING IN RESPECT OF OR ARISING OUT OF THIS NOTE MAY BE INITIATED AND PROSECUTED IN THE STATE OR FEDERAL COURTS, AS THE CASE MAY BE, LOCATED IN NEW YORK COUNTY, NEW YORK AND ANY ARBITRATION PROCEEDING PURSUANT HERETO SHALL BE CONDUCTED IN NEW YORK, NEW YORK. MAKER AND EACH INDORSER CONSENT TO AND SUBMIT TO THE EXERCISE OF JURISDICTION OVER ITS PERSON BY ANY SUCH COURT HAVING JURISDICTION OVER THE SUBJECT MATTER, WAIVE PERSONAL SERVICE OF ANY AND ALL PROCESS UPON IT AND CONSENT THAT ALL SUCH SERVICE OF PROCESS BE MADE BY REGISTERED MAIL DIRECTED TO MAKER OR SUCH INDORSER AT ITS ADDRESS SET FORTH BELOW OR TO ANY OTHER ADDRESS AS MAY APPEAR IN BANK'S RECORDS AS THE ADDRESS OF MAKER OR SUCH INDORSER.

IN ANY ACTION, SUIT OR PROCEEDING IN RESPECT OF OR ARISING OUT OF THIS NOTE, BANK, MAKER AND EACH INDORSER WAIVE TRIAL BY JURY, AND MAKER AND EACH INDORSER ALSO WAIVE (I) THE RIGHT TO INTERPOSE ANY SET-OFF OR COUNTERCLAIM OF ANY NATURE OR DESCRIPTION, (II) ANY OBJECTION BASED ON FORUM NON CONVENIENS OR VENUE, AND (III) ANY CLAIM FOR CONSEQUENTIAL, PUNITIVE OR SPECIAL DAMAGES.

If this Note is executed by more than one person, then each such person shall be jointly and severally liable on this Note, and the term "Maker" shall mean each, any or all of such persons.

Bank is authorized to fill in any blank spaces and to otherwise complete this Note and correct any patent errors herein.

Signature of Maker

Name of Maker (if not a natural person)

Orckit Communications Ltd

Print Name

By: /s/ Izhak Tamir, President

Signature of Authorized Signatory

Address for Notices

Print Name and Title

Signature of Maker

Izhak Tamir, President

Print Name

Address for Notices

126 Yigal Alon st; Tel Aviv; Israel

Address for Notices

[If Maker is not a natural person,
indicate the type of entity below]

The Maker signing above is a:

- 1 partnership
organized under the
laws of _____.
- 2 limited partnership
organized under the
laws of _____.
- X3 corporation organized
under the laws of
Israel_____.
- 4 other (specify):

Exhibit 8.1

Subsidiaries of Orckit Communications Ltd.

Corrigent Systems Inc., a Delaware corporation.

Spediant Systems Ltd., an Israeli corporation.

Exhibit 12.1

Certification of Principal Executive Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act

I, Eric Paneth, Chief Executive Officer of Orckit Communications Ltd., certify that:

1. I have reviewed this annual report on Form 20-F of Orckit Communications Ltd.:
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the company and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;
 - b. evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report my conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c. disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are

reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and

- b. any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Dated: April 21, 2004

By: /s/ Eric Paneth

Name: Eric Paneth

Title: Chief Executive Officer

(Principal Executive Officer)

Exhibit 12.2

Certification of Principal Financial Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act

I, Aviv Boim, Chief Financial Officer of Orckit Communications Ltd., certify that:

1. I have reviewed this annual report on Form 20-F of Orckit Communications Ltd.:
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in this report;
4. The company's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the company and have:
 - a. designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under my supervision, to ensure that material information relating to the company, including its consolidated subsidiaries, is made known to me by others within those entities, particularly during the period in which this report is being prepared;
 - b. evaluated the effectiveness of the company's disclosure controls and procedures and presented in this report my conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c. disclosed in this report any change in the company's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting; and
5. The company's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the company's auditors and the audit committee of the company's board of directors (or persons performing the equivalent functions):
 - a. all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are

reasonably likely to adversely affect the company's ability to record, process, summarize and report financial information; and

- b. any fraud, whether or not material, that involves management or other employees who have a significant role in the company's internal control over financial reporting.

Dated: April 21, 2004

By: /s/ Aviv Boim

Name: Aviv Boim

Title: Chief Financial Officer

(Principal Financial Officer)

Exhibit 13.1

Certification of Principal Executive Officer pursuant to 18 U.S.C. § 1350,
as adopted pursuant to § 906 of the Sarbanes-Oxley Act

In connection with the annual report on Form 20-F for the fiscal year ended December 31, 2003 of Orckit Communications Ltd. (the “Company”) as filed with the U.S. Securities and Exchange Commission (the “Commission”) on the date hereof (the “Report”) and pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, Eric Paneth, Chief Executive Officer of the Company, certify that:

- the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: April 21, 2004

By: /s/ Eric Paneth

Name: Eric Paneth

Title: Chief Executive Officer
(Principal Executive Officer)

Exhibit 13.2

Certification of Principal Financial Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act

In connection with the annual report on Form 20-F for the fiscal year ended December 31, 2003 of Orckit Communications Ltd. (the “Company”) as filed with the U.S. Securities and Exchange Commission (the “Commission”) on the date hereof (the “Report”) and pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, Aviv Boim, Chief Financial Officer of the Company, certify that:

- the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: April 21, 2004

By: /s/ Aviv Boim

Name: Aviv Boim

Title: Chief Financial Officer
(Principal Financial Officer)

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (No. 333-05670, No. 333-8824 and No. 333-12178) and in the Registration Statements on Form F-3 (No. 333-12100 and No. 333-12236) of Orkit Communications Ltd. of our reports dated February 22, 2004, relating to the financial statements and financial statement schedule, which appear in this Form 20-F.

Tel-Aviv, Israel
April 19, 2004

/s/ Kesselman & Kesselman
Certified Public Accountants (Isr.)