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**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, 2012

OR

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

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

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

Date of event requiring this shell company report .....

Commission file number: 0-16050

**TAT TECHNOLOGIES LTD.**

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

**Israel**

(Jurisdiction of incorporation or organization)

**P.O. Box 80, Gedera 70750, Israel**

(Address of principal executive offices)

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

Title of each class  
**Ordinary Shares, NIS 0.90 Par Value**

Name of each exchange on which registered  
**NASDAQ Global Market**

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

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

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

**Ordinary Shares, par value NIS 0.90 per share..... 8,798,570**  
(as of December 31, 2012)

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

Yes ☐ No ☒

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

Yes ☐ No ☒

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

Yes ☒ No ☐

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

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☒

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

U.S. GAAP ☒

International Financial Reporting Standards as issued by the  
International Accounting Standards Board ☐

Other ☐

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

Item 17 ☐ Item 18 ☐

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☒

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## INTRODUCTION

TAT Technologies Ltd. (the Company or TAT) is a provider of a variety of services and products to the commercial and military aerospace and ground defense industries through our Gedera facility in Israel or Gedera, as well as through our subsidiaries, Bental Industries Ltd., or Bental, in Israel and Limco-Piedmont Inc., or Limco-Piedmont in the U.S. Limco-Piedmont operates through Limco Airepair Inc., or Limco and Piedmont Aviation Component Services LLC or Piedmont.

As of December 31, 2012, we operated under four segments: (i) Original Equipment Manufacturing or “OEM” of Heat Management Solutions through our Gedera facility; (ii) OEM of Electric Motion Systems through our Bental subsidiary; (iii) Heat Transfer Services and Products through our Limco subsidiary; and (iv) Maintenance, Repair and Overhaul or “MRO” services for Aviation Components through our Piedmont subsidiary. Until December 31, 2010, TAT operated under three segments.

Through our Gedera facility, we are an OEM of a broad range of heat transfer components, air conditioning systems and other cooling systems used in mechanical and electronic systems on board military and commercial aircraft as well as on ground systems. The Gedera facility is also an OEM of a wide range of aviation accessories and provides limited MRO services for military and commercial customers, mainly for aviation accessories as well as for certain heat transfer components.

Through our Bental subsidiary, we are an OEM of a broad range of electric motion systems. Bental is engaged in the design, manufacture and sale of motors, generators, and other electro-mechanical motion systems primarily for the defense and aerospace markets.

Through our Limco subsidiary, we provide Heat Transfer services and products to the aerospace industry. Limco is an FAA (Federal Aviation Administration) certified repair station and provides aircraft MRO services and products for airlines, air cargo carriers, maintenance service centers and the military, primarily for heat transfer components. In addition to Limco’s MRO services, Limco is an OEM of heat transfer equipment for airplane manufacturers and other related products.

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Through our Piedmont subsidiary, we provide MRO services to the aerospace industry. Piedmont's FAA certified repair station provides MRO services for airlines, air cargo carriers, maintenance service centers and to a lesser extent the military, primarily for landing gear and auxiliary power units (APU).

In addition, TAT, through its Piedmont subsidiary, holds approximately 29.64% of the equity securities of First Aviation Services Inc., or FAvS (See Item 4 – “Information of the Company; History and development of TAT”).

FAvS, together with its subsidiaries, is a supplier of aircraft parts and components to the aviation industry worldwide, and is a provider of third party logistics and inventory management services to the aerospace industry. FAvS offers certain MRO services through three FAA authorized facilities.

Our Ordinary shares are publicly traded on the NASDAQ Global Market under the symbol “TATT” (from year 1987) and on the Tel Aviv Stock Exchange under the symbol “TAT Tech” (from year 2005). As used in this annual report, the terms “TAT”, “we”, “us” and “our” mean TAT Technologies Ltd. and its subsidiaries, unless otherwise indicated.

Our consolidated financial statements appearing in this annual report are prepared in U.S. dollars and in accordance with generally accepted accounting principles in the United States, or U.S. GAAP. All references in this annual report to “dollars” or “\$” are to U.S. dollars and all references in this annual report to “NIS” are to New Israeli Shekels.

Statements made in this annual report concerning the contents of any contract, agreement or other document are summaries of such contracts, agreements or documents and are not complete descriptions of all of their terms. If we filed any of these documents as an exhibit to this annual report or to any previous filing with the Securities and Exchange Commission, you may read the document itself for a complete recitation of its terms.

Except for the historical information contained in this annual report, the statements contained in this annual report are “forward looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and the Private Securities Litigation Reform Act of 1995, as amended, with respect to our business, financial condition and results of operations. Such forward-looking statements reflect our current view with respect to future events and financial results. Statements which use the terms “believe”, “expect”, “plan”, “intend”, “estimate”, and similar expressions are intended to identify forward-looking statements. We remind readers that forward-looking statements are merely predictions and therefore inherently subject to uncertainties and other factors and involve known and unknown risks that could cause the actual results, performance, levels of activity, or our achievements, or industry results, to be materially different from any future results, performance, levels of activity, or our achievements expressed or implied by such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. Except as required by applicable law, including the securities laws of the United States, we undertake no obligation to publicly release any update or revision to any forward looking statements to reflect new information, future events or circumstances, or otherwise after the date hereof. We have attempted to identify significant uncertainties and other factors affecting forward-looking statements in the Risk Factors section that appears in Item 3D. “Key Information - Risk Factors.”

**PART I**

**Item 1. Identity of Directors, Senior Management and Advisers**

Not applicable.

**Item 2. Offer Statistics and Expected Timetable**

Not applicable.

**Item 3. Key Information**

**A. Selected Financial Data**

TAT's selected historical information is derived from the audited consolidated financial statements of TAT as of December 31, 2012 and 2011 and for each of its fiscal years ended December 31, 2012, 2011 and 2010, which are included elsewhere in this annual statement, and have been prepared in accordance with U.S. GAAP. The selected financial data for the year ended December 31, 2009 and December 31, 2008 is derived from audited consolidated financial statements of TAT not included in the annual statements, which have been prepared in accordance with U.S. GAAP. The selected consolidated financial data set forth below should be read in conjunction with and are qualified by reference to Item 5, "Operating and Financial Review and Prospects", and our consolidated financial statements and notes thereto included elsewhere in this annual report.

**Income Statement Data:**

	Year Ended December 31,				
	2012	2011	2010	2009	2008
	(in thousands, except share and per share data)				
Revenues:					
Products	\$ 46,270	\$ 47,508	\$ 38,954	\$ 34,751	\$ 31,724
Services	41,652	37,889	40,801	48,340	71,565
Total revenues	87,922	85,397	79,755	83,091	103,289
Cost of revenues:					
Products	33,220	34,076	32,052	23,115	22,977
Services	33,362	32,143	29,136	43,780	57,586
Write down of inventory and impairment charges of long lived assets	-	5,763	3,500	-	-
Total cost of revenues	66,582	71,982	64,688	66,895	80,563
Gross profit	21,340	13,415	15,067	16,196	22,726
Operating expenses:					
Research and development, net	1,152	786	651	680	-
Selling and marketing expenses	3,426	3,439	3,475	3,719	4,369
General and administrative expenses	11,487	10,949	12,832	14,979	12,407
Impairment of goodwill and intangible assets	1,015	-	4,704	-	-
Other expenses (income)	9	(169)	-	-	-
Gain from sale of the propellers & parts businesses	-	-	-	(4,400)	-
Operating income (loss)	4,251	(1,590)	(6,595)	1,218	5,950
Financial income (expenses), net	(181)	(380)	(111)	149	1,174
Other expenses, net	-	-	(200)	-	(236)
Gain from dilution of interests in affiliated company	-	240	-	-	-
Income (loss) from operations before taxes on income	4,070	(1,730)	(6,906)	1,367	6,888
Taxes on income (tax benefit)	2,086	(316)	(4,153)	(765)	1,795
Share in results of affiliated company and impairment of share in affiliated company	(3,756)	331	(4,510)	(32)	674
Net income (loss)	(1,772)	(1,083)	(7,263)	2,100	5,767
Net loss (income) attributable to non controlling interest	58	53	(123)	(347)	(1,499)
Net income (loss) attributable to TAT Technologies' shareholders	\$ (1,714)	\$ (1,030)	\$ (7,386)	\$ 1,753	\$ 4,268
Basic and diluted net income (loss) per share attributable to controlling interest	\$ (0.19)	\$ (0.12)	\$ (0.84)	\$ 0.22	\$ 0.65
Weighted average number of shares used in computing basic and diluted net income (loss) per share	8,808,075	8,815,003	8,815,003	7,893,639	6,546,055
Cash dividend per share	\$ 0.28	\$ -	\$ -	\$ 0.85	\$ -



**Balance Sheet Data:**

	As of December 31,				
	2012	2011	2010	2009	2008
	(in thousands)				
Working capital	\$ 71,430	\$ 70,665	\$ 70,462	\$ 76,748	\$ 90,616
Total assets	107,511	115,318	121,427	124,491	135,930
Long-term liabilities, excluding current maturities	6,421	9,333	5,294	13,556	12,925
Shareholders' equity	\$ 82,233	\$ 86,370	\$ 88,059	\$ 94,866	\$ 76,077

**B. Capitalization and Indebtedness**

Not applicable.

**C. Reasons for the Offer and Use of Proceeds**

Not applicable.

**D. Risk Factors**

*Investing in our Ordinary shares involves certain risks and uncertainties. You should carefully consider the risks and uncertainties described below before investing in our Ordinary shares. Our business, prospects, financial condition and results of operations could be adversely affected due to any of the following risks. In that case, the value of our Ordinary shares could decline, and you could lose all or part of your investment.*

**Risks Related to Our Business and Our Industry**

***The aerospace industry is subject to significant government regulation and oversight, and TAT and its subsidiaries may incur significant additional costs to comply with these regulations.***

The aerospace industry is highly regulated in the United States and in other countries. TAT and its subsidiaries must be certified or accepted by the FAA, the United States Department of Defense, the European Aviation Safety Agency, or EASA, and similar agencies in foreign countries and by individual original equipment manufacturers, or OEMs, in order to manufacture, sell and service parts used in aircraft. If any of the material certifications, authorizations or approvals of TAT or its subsidiaries are revoked or suspended, then the operations of TAT or its subsidiaries, as the case may be, will be significantly curtailed and TAT and its subsidiaries could be subjected to significant fines and penalties. In the future, new and more demanding government regulations may be adopted or industry oversight may be increased. TAT and its subsidiaries may have to incur significant additional costs to achieve compliance with new regulations or to reacquire a revoked or suspended license or approval, which could materially reduce profitability.

*TAT competes with a number of established companies in all aspects of TAT's business, many of which have significantly greater resources or capabilities than TAT.*

For the OEM of heat management solutions, TAT's major competitors are other OEMs who manufacture heat transfer components, including manufacturers based in the U.S. such as the Hughes-Treidler division of Ametek Inc., Lytron Inc., Niagara Thermal, Hamilton Sundstrand, Honeywell International, Liebherr-Aerospace Toulouse S.A., Stewart Werner South Wind Corp., United Aircraft Products and Triumph Thermal Systems, manufacturers based in Europe such as I.M.I. Marston Ltd., Dunlop Aerospace (including Serck Aviation) and manufacturers based in Asia such as Sumitomo Precision Products from Japan. Many of TAT's competitors are far larger, have substantially greater resources, including technical, financial, research and development, marketing and distribution capabilities than TAT, and enjoy greater market recognition. These competitors may be able to achieve greater economies of scale and may be less vulnerable to price competition than TAT. TAT may not be able to offer its products as part of integrated systems to the same extent as its competitors or successfully develop or introduce new products that are more cost effective or offer better performance than those of its competitors. Failure to do so could adversely affect TAT's business, financial condition and results of operations.

For the OEM of electric motion systems, TAT's major competitors are mainly large companies that provide standard products and companies that provide special customized solutions. As the providers of the systems in which TAT's products are integrated usually tend to prefer local manufacturers for the purchase of the components, penetrating markets outside of Israel requires either high levels of product innovation or lower prices compared to the prices offered by such competitors or a local marketing and engineering presence in these countries.

For the Heat Transfer Services and Products, TAT's major competitors are the service divisions of OEMs, the in-house maintenance services of a number of commercial airlines and other independent service providers, including Triumph Accessories (Triumph Corporation), LORI Heat Transfer Center of Honeywell (Tulsa, Oklahoma), SECAN-Honeywell (France) and Drake Air – Ametek (Tulsa, Oklahoma).

For the MRO services for Aviation Components, TAT's major competitors are the service divisions of OEMs, the in-house maintenance services of a number of commercial airlines and other independent service providers, including Standard Aero Group Inc., Aerotech International Inc., Honeywell International, AAR Corp., Messier-Dowty Aerospace (MD), Hawker Pacific and APRO.

Competition in the MRO market is based on price, quality, engineered solutions, ability to provide a broad range of services, and the ability to perform repairs and overhauls rapidly. A number of our competitors have inherent competitive advantages. For example, we compete with the service divisions of large OEMs which are able to derive significant brand recognition from their OEM manufacturing activities. We also compete with the in-house service divisions of large commercial airlines and there is a strong incentive for an airline to fully-utilize the services of its maintenance employees and facilities.

Further, TAT's competitors may have additional competitive advantages, such as:

- The ability to adapt more quickly to changes in customer requirements and industry conditions or trends;
- Greater access to capital;
- Stronger relationships with customers and suppliers;
- Greater name recognition; and
- Access to superior technology and marketing resources.

If TAT is unable to overcome these competitive disadvantages, then TAT's business, financial condition and results of operations would be adversely affected.

***TAT derives a material part of its revenues from several major customers. If TAT loses any of these customers or they reduce the amount of business they do with TAT, TAT's revenues may be seriously affected.***

Five customers accounted for approximately 20.8%, 21.3% and 21.6% of TAT's revenues for the years ended December 31, 2012, 2011 and 2010, respectively. TAT's major customers may not maintain the same volume of business with TAT in the future. If TAT loses any of these customers or they reduce the amount of business they do with TAT, TAT's revenues may be seriously affected.

***A part of the revenues of TAT and its subsidiaries are from contracts with the U.S. and Israeli governments and are subject to special risks. A loss of all, or a major portion, of the revenues of TAT or any of its subsidiaries from government contracts could have a material adverse effect on TAT's operations.***

A portion of the revenues of TAT and its subsidiaries are from contracts with the U.S. and Israeli governments. Sales to the U.S. and Israeli governments accounted for approximately 4.4%, 7.3% and 7.3% of TAT's revenues on a consolidated basis for the years ended December 31, 2012, 2011 and 2010, respectively.

Business with the U.S. and Israeli governments, as well as with the governments of other countries, is subject to risks which are not as relevant in business with private parties. These risks include the ability of the governmental authorities to unilaterally:

- Suspend TAT or any of its subsidiaries from receiving new contracts pending resolution of alleged violations of procurement laws or regulations;
- Terminate existing contracts, with or without cause, at any time;
- Condition the receipt of new contracts on conditions which are beyond the control of TAT;
- Reduce the value of existing contracts;
- Audit the contract-related costs and fees of TAT and its subsidiaries, including allocated indirect costs; and
- Control or prohibit the export of the products of TAT and its subsidiaries.

A decision by a governmental authority to take any or all of the actions listed above could materially reduce the sales and profitability of TAT and its subsidiaries. Most of the U.S. Government contracts of TAT and its subsidiaries can be terminated by the U.S. Government either for its convenience or if TAT or any of its subsidiaries defaults by failing to perform under the contract. Termination for convenience provisions generally provide only for the recovery of costs incurred or committed, settlement expenses and profit on the work completed by TAT and its subsidiaries prior to termination.

Declines in military/defense budgets may result in reduced demand for the products and manufacturing services of TAT and its subsidiaries. Any decline could result in reduction in the business revenues of TAT and its subsidiaries and adversely affect their business, results of operations and financial condition.

***If TAT does not receive the governmental approvals necessary for the export of its products, TAT's revenues may decrease. Similarly if TAT's suppliers and partners do not receive their government approvals necessary to export their products or designs to TAT, TAT's revenues may decrease.***

Under Israeli law, the export of certain of the products and know-how of TAT is subject to approval by the Israeli Ministry of Defense. To initiate sales proposals with regard to exports of the products and know-how of TAT and to export such products or know-how, TAT must obtain permits from the Ministry of Defense. TAT may not be able to receive in a timely manner, or at all, all the required permits for which it may apply in the future.

Similarly, under foreign laws the export of certain military products, technical designs and spare parts require the prior approval of, or export license from, such foreign governments. In order to maintain the third party production, certain co-development activities and procurements required for the performance of certain contracts, TAT must receive detailed technical designs, products or product parts' samples from its strategic partners or suppliers. TAT may not be able to receive all the required permits and/or licenses in a timely manner, or at all. Consequently, TAT's revenues may decrease.

***TAT depends on a limited number of suppliers of components for certain of its products and if TAT or any of its subsidiaries is unable to obtain these components when needed, they would experience delays in manufacturing their products and TAT's financial results could be adversely affected.***

TAT relies on a limited number of key suppliers for parts for certain of its OEM and MRO services. Certain of these suppliers are currently the sole source of one or more components upon which TAT is dependent. Suppliers of some of these components require TAT to place orders with significant lead-time to assure supply in accordance with TAT's requirements. If TAT were to engage in a commercial dispute with or be unable to obtain adequate supplies of parts from these suppliers at commercially reasonable prices or required lead time, TAT's operations could be interrupted. Increased costs associated with supplied materials or components could increase TAT's costs and reduce TAT's profitability if TAT is unable to pass these cost increases on to its customers.

*TAT may face increased costs and a reduced supply of raw materials. TAT may not be able to recoup future increases in the cost of raw materials or in electric power costs for its operations through price increases for its products.*

In recent years, the cost of raw materials and components used by TAT has fluctuated significantly due to market and industry conditions. The cost of electric power used in TAT's operations has also fluctuated significantly in the last several years. TAT may not be able to recoup future increases in the cost of raw materials and components or electric power costs through price increases for its products.

*TAT faces special risks from international sales operations which may have a material adverse effect on TAT's business, operating results and financial condition.*

In the years ended December 31, 2012, 2011 and 2010, approximately 78.9%, 77.4% and 70.3% of TAT's sales, respectively, resulted from TAT's international operations (out of Israel). This source of revenue is subject to various risks, including:

- Governmental embargoes or foreign trade restrictions;
- Changes in U.S. and foreign governmental regulations;
- Changes in foreign exchange rates;
- Tariffs;
- Other trade barriers;
- Political, economic and social instability; and
- Difficulties collecting accounts receivable.

Accordingly, TAT and its subsidiaries may encounter significant difficulties in connection with the sale of its products in international markets.

*TAT may engage in future acquisitions that could dilute TAT's shareholders' equity and harm TAT's business, results of operations and financial condition.*

TAT has pursued, and will continue to pursue, growth opportunities through internal development and acquisition of complementary businesses, products and technologies. TAT is unable to predict whether or when any prospective acquisition will be completed. The process of integrating an acquired business may be prolonged due to unforeseen difficulties and may require a disproportionate amount of TAT's resources and management's attention. TAT may not be able to successfully identify suitable acquisition candidates, complete acquisitions, integrate acquired businesses into its operations, or expand into new markets. Further, once integrated, acquisitions may not achieve comparable levels of revenues, profitability or productivity as TAT's existing business or otherwise perform as expected. The occurrence of any of these events could harm TAT's business, financial condition or results of operations. Future acquisitions may require substantial capital resources, which may require TAT to seek additional debt or equity financing.

Future acquisitions by TAT could result in the following, any of which could materially harm TAT's results of operations or the price of TAT's Ordinary shares:

- Issuance of equity securities that would dilute TAT's shareholders' percentages of ownership;
- Large one-time write-offs;
- The incurrence of debt and contingent liabilities;
- Difficulties in the assimilation and integration of operations, personnel, technologies, products and information systems of the acquired companies;
- Diversion of management's attention from other business concerns;
- Contractual disputes;
- Risks of entering geographic and business markets in which TAT has no or only limited prior experience; and
- Potential loss of key employees of acquired organizations.

***Rapid technological changes may adversely affect the market acceptance of the products of TAT.***

The aerospace and defense markets in which TAT competes are subject to technological changes, introduction of new products, change in customer demands and evolving industry standards. The future success of TAT will depend upon its ability to keep pace with technological developments and to timely address the increasingly sophisticated needs of its customers by supporting existing and new technologies and by developing and introducing enhancements to its current products and new products. TAT may not be able to successfully develop and market enhancements to its products that will respond to technological change, evolving industry standards or customer requirements. TAT may experience difficulties that could delay or prevent the successful development, introduction and sale of such enhancements; and such enhancements may not meet the requirements of the market or achieve any significant degrees of market acceptance. If release dates of any new products or enhancements of TAT are delayed, or if when released, they fail to achieve market acceptance, TAT's business, operating results and financial condition would be materially adversely affected.

***TAT has fixed-price contracts with some of its customers and TAT bears the risk of costs in excess of its estimates. In addition, TAT may not be able to pass on increased costs to its customers.***

TAT has entered into multi-year, fixed-price contracts with some of its MRO and OEM customers. Pursuant to these contracts, TAT realizes all the benefits or costs resulting from any increases or decreases in the cost of providing services to these customers. Several of TAT's contracts do not permit TAT to recover for increases in raw material prices, taxes or labor costs and other contracts may permit, to a limited extent, periodic price adjustments. Any increase in these costs could increase the cost of operating the business of TAT and reduce its profitability. Factors such as inaccurate pricing and increases in the cost of labor, materials or overhead may result in cost over-runs and losses on those agreements. TAT may not succeed in obtaining the agreement of a customer to re-price a particular product, and may not be able to recoup previous losses resulting from incomplete or inaccurate engineering data. In addition, as costs increase, TAT may not be able to pass on such increased costs to its other customers. This could materially impact TAT's profitability.



***TAT depends on its key executives, and may not be able to hire and retain additional key employees or successfully integrate new members of its team and the loss of key employees could have a material adverse effect on TAT's business.***

TAT's success will depend largely on its continued reliance on the experience and expertise of its senior management. Any of the senior managers of TAT may terminate his employment with TAT and seek employment with others who may seek his expertise. The loss of the expertise of senior management of TAT through death, disability or termination of employment would have a material and adverse effect on TAT's business, financial condition and results of operations. TAT is not the beneficiary of life or disability insurance covering any of the executives, key employees or other personnel of TAT.

***TAT depends on its manufacturing and MRO facilities and any material damage to these facilities may adversely impact TAT's operations.***

TAT believes that its results of operations will be dependent in large part upon its ability to manufacture and deliver OEM products and to provide MRO services promptly upon receipt of orders and to provide prompt and efficient service to its customers. As a result, any material disruption of TAT's day-to-day operations could have a material adverse effect on their business, customer relations and profitability. TAT relies on its Gedera, Israel, Kibbutz Marom-Golan, Israel, Kernersville and Winston-Salem, North Carolina and Tulsa, Oklahoma facilities for the production of its OEM products and provision of its MRO services. A war, fire, flood, earthquake or other disaster or condition that significantly damaged or destroyed any of these facilities would have a material adverse effect on the operations of TAT.

***TAT uses equipment that is not easily repaired or replaced, and therefore material equipment failures could cause TAT or its subsidiaries to be unable to meet quality or delivery expectations of its customers.***

Many of the service and manufacturing processes of TAT are dependent on equipment that is not easily repaired or replaced. As a result, unexpected equipment failures could result in production delays or the manufacturing of defective products. The ability of TAT to meet the expectations of its customers with respect to on-time delivery of repaired components or quality OEM products is critical. The failure by TAT to meet the quality or delivery expectations of its customers could lead to the loss of one or more of its significant customers.

***TAT may fail to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act of 2002.***

The Sarbanes-Oxley Act of 2002 imposes certain duties on TAT and TAT's executives and directors. TAT's efforts to comply with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 governing internal controls and procedures for financial reporting have resulted in increased general and administrative expense and a diversion of management time and attention, and TAT expects these efforts to require the continued commitment of significant resources. TAT may identify material weaknesses or significant deficiencies in its assessments of its internal controls over financial reporting. Failure to maintain effective internal controls over financial reporting could result in investigation or sanctions by regulatory authorities and could have a material adverse effect on TAT's operating results, investor confidence in TAT's reported financial information and the market price of TAT's Ordinary shares.

***TAT has potential exposure to liabilities arising under environmental laws and regulations.***

The business operations and facilities of TAT are subject to a number of federal, state, and local laws and regulations that govern the discharge of pollutants and hazardous substances into the air and water as well as the handling, storage and disposal of such materials and other environmental matters. Compliance with such laws as they relate to the handling, storage and disposal of hazardous substances is a significant obligation for TAT at each of its facilities. TAT would be subject to serious consequences, including fines and other sanctions, and limitations on the operations of TAT due to changes to, or revocations of, the environmental permits applicable to its facilities if it fails to comply. The adoption of new laws and regulations, stricter enforcement of existing laws and regulations, the discovery of previously unknown contamination or the imposition of new cleanup requirements could require TAT to incur costs and become subject to new or increased liabilities that could increase the operating costs of TAT and adversely affect the manner in which TAT conducts its business.

Under certain environmental laws, liability associated with investigation or remediation of hazardous substances can arise at a broad range of properties, including properties currently or formerly operated by TAT or any of its predecessors, as well as properties to which TAT sent hazardous substances or wastes for treatment, storage, or disposal. Costs and other obligations can arise from claims for toxic torts, natural resource and other damages, as well as the investigation and clean-up of contamination at such properties. Under certain environmental laws, such liability may be imposed jointly and severally, so TAT may be responsible for more than its proportionate share and may even be responsible for the entire liability at issue. The extent of any such liability can be difficult to predict.

*TAT is exposed to potential liabilities arising from product liability and warranty claims.*

TAT's operations expose TAT to potential liabilities for personal injury or death as a result of the failure of an aircraft component that has been designed, manufactured, serviced or supplied by TAT. TAT believes that, in an effort to improve operating margins, some customers have delayed the replacement of parts beyond their recommended lifetime, which may undermine aircraft safety and increase the risk of liability of TAT and its subsidiaries.

There can be no assurance that TAT will not experience any material product liability losses in the future, that it will not incur significant costs to defend such claims, that its insurance coverage will be adequate if claims were to arise or that it would be able to maintain insurance coverage in the future at an acceptable cost. A successful claim brought against TAT or its subsidiaries in excess of its available insurance coverage may have a material adverse effect on TAT's business.

In addition, in the ordinary course of business of TAT, contractual disputes over warranties can arise. TAT may be subject to requests for cost sharing or pricing adjustments from its customers as a part of its commercial relationships with them, even though they have agreed to bear these risks.

#### **Risk Factors Related to Our Ordinary Shares**

*TAT's share price has been volatile in the past and may decline in the future.*

TAT's Ordinary shares have experienced significant market price and volume fluctuations in the past and may experience significant market price and volume fluctuations in the future in response to factors such as the following, some of which are beyond TAT's control:

- Quarterly variations in TAT's operating results;
- Operating results that vary from the expectations of securities analysts and investors;
- Changes in expectations as to TAT's future financial performance, including financial estimates by securities analysts and investors;

- Announcements of technological innovations or new products by TAT or TAT's competitors;
- Announcements by TAT or TAT's competitors of significant contracts, acquisitions, strategic partnerships, joint ventures or capital commitments;
- Announcements by third parties of significant claims or proceedings against us;
- Additions or departures of key personnel;
- Future sales of TAT's Ordinary shares;
- De-listing of TAT's shares from the NASDAQ Global Market;
- Stock market price and volume fluctuation; and
- Legal proceedings against TAT's controlling shareholders

Domestic and international stock markets often experience extreme price and volume fluctuations. Market fluctuations, as well as general political and economic conditions, such as a recession or interest rate or currency rate fluctuations or political events or hostilities in or surrounding Israel, could adversely affect the market price of TAT's Ordinary shares.

In the past, securities class action litigation has often been brought against companies following periods of volatility in the market price of its securities. TAT may in the future be the target of similar litigation. Securities litigation could result in substantial costs and divert management's attention and resources both of which could have a material adverse effect on TAT's business and results of operations.

***Substantial future sales of TAT's Ordinary shares by TAT's principal shareholders may depress TAT's share price.***

TAT's principal shareholder, Isal Amlat Investment (1993) Ltd., or Isal Amlat, beneficially owns (through its 94% interest in KMN Industries Ltd.) 54.00% of TAT's outstanding shares of which 43.7% of TAT's outstanding shares are held directly by its subsidiary, TAT Industries Ltd. Isal Amlat and its affiliates have defaulted under certain of their loans and a receiver has been appointed for the Ordinary shares held by Isal Amlat and its affiliates. Such shares are subject to sale by the receiver which sale would result in a change of control of TAT. As a result of the possibility of such a sale, the market price of TAT's Ordinary shares may fall. Any substantial sales of TAT's shares by the receiver in the public market also might make it more difficult for TAT to sell equity or equity-related securities in the future at a time, in a place and on terms TAT deems appropriate.

#### **Risks Relating to Our Location in Israel**

*Because TAT has significant operations in Israel, TAT may be subject to political, economic and other conditions affecting Israel that could increase TAT's operating expenses and disrupt TAT's business.*

TAT is incorporated under the laws of Israel, and TAT's executive offices, manufacturing plant and research and development facilities are located in the State of Israel. As a result, political, economic and military conditions affecting Israel directly influence TAT. Any major hostilities involving Israel, a full or partial mobilization of the reserve forces of the Israeli army, the interruption or curtailment of trade between Israel and its present trading partners, or a significant downturn in the economic or financial condition of Israel could have a material adverse effect on TAT's business, financial condition and results of operations.

Since the establishment of the State of Israel in 1948, Israel and its Arab neighbors have engaged in a number of armed conflicts. A state of hostility, varying from time to time in intensity and degree, has led to security and economic problems for Israel. Major hostilities between Israel and its neighbors may hinder Israel's international trade and lead to economic downturn. This, in turn, could have a material adverse effect on TAT's operations and business. Since June 2007, when Hamas effectively took control of the Gaza Strip, there have been extensive hostilities along the Gaza Strip. Ongoing violence between Israel and the Palestinians as well as tension between Israel and its Arab neighbors and Iran may have a material adverse effect on TAT's business, financial conditions and results of operations.

Furthermore, there are a number of countries, primarily in the Middle East, that restrict business with Israel or Israeli companies, and TAT is precluded from marketing its products to these countries. Restrictive laws or policies directed towards Israel or Israeli businesses may have an adverse impact on TAT's operations, TAT's financial results or the expansion of TAT's business.

*TAT may be adversely affected by a change in the exchange rate of the NIS against the dollar. Because exchange rates between the NIS and the dollar fluctuate continuously, exchange rate fluctuations, particularly larger periodic devaluations, may have an impact on TAT's profitability and period to period comparisons of TAT's results.*

TAT's financial statements are stated in dollars, while a portion of TAT's expenses, primarily labor expenses, are incurred in NIS and a part of TAT's revenues are quoted in NIS. Additionally, certain assets, as well as a portion of TAT's liabilities, are denominated in NIS. Because exchange rates between the NIS and the dollar fluctuate continuously, exchange rate fluctuations, particularly larger periodic devaluations, may have an impact on TAT's profitability and period to period comparisons of TAT's results. TAT's results may be adversely affected by the devaluation of the NIS in relation to the dollar (or if such devaluation is on a lagging basis), if TAT's revenues in NIS are higher than TAT's expenses in NIS and/or the amount of TAT's assets in NIS are higher than TAT's liabilities in NIS. Alternatively, TAT's results may be adversely affected by an appreciation of the NIS in relation to the dollar (or if such appreciation is on a lagging basis), if the amount of TAT's expenses in NIS are higher than the amount of TAT's revenues in NIS and/or the amount of TAT's liabilities in NIS are higher than TAT's assets in NIS.

*TAT's results of operations may be negatively affected by the obligation of its personnel to perform military service.*

Many of TAT's employees and some of TAT's directors and officers in Israel are obligated to perform annual reserve duty in the Israel Defense Forces and may be called for active duty under emergency circumstances at any time. If a military conflict or war arises, these individuals could be required to serve in the military for extended periods of time. TAT's operations could be disrupted by the absence for a significant period of one or more of TAT's executive officers or key employees or a significant number of other employees due to military service. Any disruption in TAT's operations could adversely affect TAT's business.

*Your rights and responsibilities as a shareholder will be governed by Israeli law and differ in some respects from the rights and responsibilities of shareholders under U.S. law.*

TAT is incorporated under Israeli law. The rights and responsibilities of holders of TAT's Ordinary shares are governed by TAT's memorandum of association, articles of association and by Israeli law. These rights and responsibilities differ in some respects from the rights and responsibilities of shareholders in typical U.S. corporations. In particular, each shareholder of an Israeli company has a duty to act in good faith and in a customary manner in exercising his or her rights and fulfilling his or her obligations toward the company and other shareholders and to refrain from abusing his power in the company, including, among other things, in voting at the general meeting of shareholders on certain matters. Israeli law provides that these duties are applicable in shareholder votes on, among other things, amendments to a company's articles of association, increases in a company's authorized share capital, mergers and interested party transactions requiring shareholder approval. In addition, a controlling shareholder of an Israeli company, or a shareholder who knows that he or she possesses the power to determine the outcome of a shareholder vote or who has the power to appoint or prevent the appointment of a director or officer in the company, has a duty of fairness toward the company. However, Israeli law currently does not define the substance of this duty of fairness. Because Israeli corporate law has undergone extensive revision in recent years, there is relatively little case law available to assist in understanding the implications of these provisions that govern shareholder behavior.

*Israeli law may delay, prevent or make difficult an acquisition of TAT, which could prevent a change of control and, therefore, depresses the price of TAT's shares.*

Israeli corporate law regulates mergers, requires tender offers for acquisitions of shares above specified thresholds, requires special approvals for transactions involving directors, officers or significant shareholders and regulates other matters that may be relevant to these types of transactions. Furthermore, Israeli tax considerations may make potential transactions unappealing to TAT or to some of TAT's shareholders. These provisions of Israeli law may delay, prevent or make difficult an acquisition of TAT, which could prevent a change of control and therefore depress the price of TAT's shares.

***Investors and TAT's shareholders generally may have difficulties enforcing a U.S. judgment against TAT, TAT's executive officers and directors or asserting U.S. securities laws claims in Israel.***

TAT is incorporated in Israel and the majority of TAT's executive officers and directors reside outside the United States. Service of process upon them may be difficult to effect within the United States. Furthermore, many of TAT's assets and most of the assets of TAT's executive officers and directors are located outside the United States. Therefore, a judgment obtained against TAT or certain of its executive officers and directors in the United States, including one based on the civil liability provisions of the U.S. federal securities laws, may not be collectible in the United States and may not be enforced by an Israeli court. It also may be difficult for you to assert U.S. securities law claims in original actions instituted in Israel. However, subject to certain time limitations and other conditions, Israeli courts may enforce final judgments of United States courts for liquidated amounts in civil matters, including judgments based upon the civil liability provisions of those and similar acts.

***As a foreign private issuer whose shares are listed on the NASDAQ Global Market, TAT may follow certain home country corporate governance practices instead of certain NASDAQ requirements.***

As a foreign private issuer whose shares are listed on the NASDAQ Global Market, TAT is permitted to follow certain home country corporate governance practices instead of certain requirements of the NASDAQ Marketplace Rules. A foreign private issuer that elects to follow a home country practice instead of such requirements must submit to NASDAQ in advance a written statement from an independent counsel in such issuer's home country certifying that the issuer's practices are not prohibited by the home country's laws. In addition, a foreign private issuer must disclose in its annual reports filed with the Securities and Exchange Commission or on its website each such requirement that it does not follow and describe the home country practice followed by the issuer instead of any such requirement. As a foreign private issuer listed on The NASDAQ Global Market, TAT may follow TAT's home country law, instead of the NASDAQ Marketplace Rules, which require that TAT obtain shareholder approval for certain dilutive events, such as for the establishment or amendment of certain equity based compensation plans, an issuance that will result in a change of control of TAT, certain transactions other than a public offering involving issuances of a 20% or more interest in TAT and certain acquisitions of the stock or assets of another company.



**Item 4. Information on the Company**

**History and Development of TAT**

TAT was incorporated under the laws of the State of Israel in April 1985 under the name Galaxy Graphics Ltd. TAT changed its name to Galagraph Ltd. in August 1986 and to TAT Technologies Ltd. in May 1992. TAT is a public limited liability company under the Israeli Companies Law 1999-5759, or the Israeli Companies Law, and operates under this law and associated legislation. TAT's registered offices and principal place of business are located at Re'em Industrial Park, Neta Boulevard, Bnei Ayish, Gedera 70750, Israel and its telephone number is +972-8-8268-500. TAT's address on the Internet is [www.tat-technologies.com](http://www.tat-technologies.com). The information on TAT'S website is not incorporated by reference into this annual report.

TAT was founded in 1985 to develop the computerized systems business of its parent company, TAT Industries Ltd. (or TAT Industries), a publicly held Israeli corporation then engaged in the manufacture and sale of aeronautical equipment. In December 1991, TAT acquired the heat exchange operations of TAT Industries and in 2000, TAT purchased the remaining operations of TAT Industries relating to the manufacture and maintenance of aviation accessories and leased certain of its properties.

In March 1987, TAT completed the initial public offering of its securities in the United States. TAT was listed on the NASDAQ Global Market (then known as the NASDAQ National Market) from its initial public offering until July 1998 when the listing of TAT's Ordinary shares was transferred to the NASDAQ Capital Market. On June 24, 2009 TAT's Ordinary shares resumed trading on the NASDAQ Global Market. Since August 2005 TAT's shares have been traded also on the Tel Aviv Stock Exchange (TASE).

TAT is a provider of a variety of services and products to the commercial and military aerospace and defense industries through its Gedera facility, as well as through its subsidiaries, Bental, in Israel, and Limco and Piedmont in the U.S (Limco and Piedmont are held by TAT through Limco-Piedmont Inc. ("Limco-Piedmont")).

Limco provides Heat Transfer MRO services and products to the aerospace industry. Limco's Federal Aviation Administration, or FAA, certified repair station (located in Oklahoma) provides aircraft with MRO services for airlines, air cargo carriers, maintenance service centers and the military, especially for heat transfer components. In addition to Limco's MRO services Limco is an OEM of heat transfer products for airplane manufacturers and other selected related products.

In July 2005, Limco acquired Piedmont Aviation Component Services, LLC ("Piedmont"), a company certified by the FAA to perform maintenance, repair and overhaul services on APUs and landing gears. Piedmont's FAA, certified repair station (located in North Carolina) provides MRO services for airlines, air cargo carriers, maintenance service centers and the military, especially for landing gear and auxiliary power units (APU).

In July 2007, Limco-Piedmont completed an initial public offering of its shares of Common stock and Limco-Piedmont's shares were listed on the NASDAQ Global Market (symbol: LIMC) until July 2, 2009, when TAT acquired all of the publicly held shares of Limco-Piedmont (approximately 32% of Limco-Piedmont's total shares) in a stock for stock merger. As a result of such merger, Limco-Piedmont again became a wholly-owned subsidiary of TAT.

On January 1, 2008, TAT established a wholly-owned subsidiary under the laws of the State of California, TAT-GAL Inc., which acts as purchasing agent for TAT's operations.

Following a series of transactions occurring between March 2008 and March 2009, TAT acquired 70% control of Bental. The acquisition of Bental shares (for an aggregate price of \$9,192) was financed by loans in a total amount of \$6.25 million received from Bank Mizrahi and TAT's internal resources.

On December 19 2007, Isal Amlat Industries (1993) Ltd., an Israeli company publicly traded on the Tel Aviv Stock Exchange ("**Isal Amlat**"), through KMN Industries Ltd. in which Isal Amlat holds 94% of the issued share capital ("**KMN Industries**"), purchased the controlling interests in TAT and in TAT Industries, TAT's controlling shareholder, by purchasing from Mr. Shlomo Ostersetzer, the former Chairman of TAT's Board of Directors and TAT's former President, Mr. Dov Zeelim, the former Vice Chairman of TAT's Board of Directors and TAT's former Chief Executive Officer, and FIMI Opportunity Fund, or FIMI, 10% of TAT's then outstanding Ordinary shares for consideration of NIS 50.4M, and 54% of TAT Industries' then outstanding Ordinary shares for consideration of NIS 105.3M.

The agreement between KMN Industries and Mr. Zeelim, as amended on January 31, 2008, provided KMN Industries with additional shares in TAT Industries purchased from Mr. Zeelim.

Pursuant to an agreement between KMN Industries and Mr. Zeelim entered into in May 2008, in connection with Mr. Zeelim's resignation from the office of Chief Executive Officer of TAT, Mr. Zeelim exercised his put option on June 12, 2008 and 4.17% of TAT Industries' then outstanding Ordinary shares were purchased by KMN Industries.

On July 17, 2008 KMN Industries and FIMI amended the terms of their agreement. Accordingly, 141,443 of TAT's Ordinary shares constituting then 2% of TAT's outstanding shares were purchased by KMN Industries in December 2008 at a price per share of \$19.343 and the remaining 100,000 of TAT's Ordinary shares constituting then 1.1% of TAT's outstanding shares were purchased by KMN Industries in November 2009 for a total consideration of \$2.0 million.

On March 11, 2009 and on August 13, 2009, TAT's board of directors authorized its management to enter into engagements with Oppenheimer Israel Investment House for the blind trust purchase of TAT's shares under rule 10b5-1 of the Securities Exchange Act of 1934. The first purchase plan was terminated on March 26, 2009, with TAT having purchased 4,650 Ordinary shares for an aggregate price of \$26,000. The second purchase plan authorized Oppenheimer Israel to purchase shares of TAT in the aggregate amount of up to \$2 million (approximately NIS 7.8 million) over a period of six months and at a price not exceeding \$9 per share. A total of 253,390 Ordinary shares were purchased, representing about 2.8% of the Company's share capital in consideration of approximately \$2 million (an average of \$7.90 per share). Both plans ended and the purchased shares became dormant as defined in the Israeli Companies Law.

In September, 2011 Isal Amlat purchased an aggregate of 18,600 Ordinary shares of TAT at an average price of 20.39 NIS per share (approximately \$5.54 per share). Such purchases were made on the Tel Aviv Stock Exchange. Following such purchases, Isal beneficially owned 4,750,951 Ordinary shares, representing 54.00% of TAT's Ordinary shares.

On May 21, 2012, TAT's Board of Directors approved a stock repurchase plan under Rule 10b5-1 of the Securities Exchange Act of 1934. The plan was for a period of 6 months (subject to extension) and provided for the purchase of shares in an aggregate amount of up to \$0.5 million U.S. dollars and for a price not exceeding \$7.5 per share. Such plan replaced and superseded a prior repurchase plan approved by TAT's Board of Directors' on February 21, 2012. On November 21, the term of such stock repurchase plan ended. As of such date, the Company had purchased 16,433 shares for approximately \$71,000 (average of \$4.32 per share) constituting less than 0.1% of TAT's issued shares. The purchased shares became dormant as defined in the Israeli Companies Law.

On December 4, 2009, TAT's indirect subsidiary, Piedmont, acquired 288,334 shares of Class B Common stock of First Aviation Services Inc., or FAvS, representing 37% of FAvS's then share capital and \$750,000 of FAvS Preferred Shares (entitling Piedmont to cash dividends at an annual rate of 12% payable quarterly or at the discretion of FAvS to PIK dividends payable in additional Preferred Shares at an annual rate of 15%). In consideration for such shares, Piedmont transferred to FAvS its propellers and parts businesses and guaranteed for a period of up to two years up to \$7 million of the bank debt incurred by FAvS to fund the transaction described in the next paragraph. FAvS is a provider of maintenance and repair services for various wheels, brakes and starter/generators.

As part of the transaction described above, FAvS also acquired all the assets and liabilities of Aerospace Turbine Rotables ("AeTR") for a cash consideration of \$7 million (guaranteed by Piedmont). AeTR specializes in renovation and repair of landing gear, safety equipment and hydraulic and electrical components for corporate, regional and military aircraft.

FAvS' shares are quoted over the counter (OTC). FAvS' share value as of the closing date (December 4, 2009) and as of December 31, 2009, 2010, 2011 and 2012 was \$17.8, \$15.0, \$12.4, \$5.45 and \$7.00, respectively (share value adjusted as result of a **1 for 20** reverse stock split).

TAT believes that the share value does not reflect the fair value of FAvS' share, because the extremely low trading volume in FAvS' shares does not reflect an active market. Therefore the fair value of FAvS, at the transaction date, was based on an appraisal performed by management, which included a number of factors, including the assistance of independent appraisers. According to the appraisal, FAvS' fair value amounted to \$22.549 million as of November 30, 2009. As a result of the sale of Piedmont's propellers and spare parts businesses, TAT recorded a capital gain in the amount of approximately \$4.4 million in its statement of income for the year ended December 31, 2009.

On October 1, 2010, Piedmont agreed to secure the guarantee mentioned above for \$6.6 million, by providing a letter of credit to the lender for FAvS. Such guaranty was for a period of 15 months ending December 31, 2011 and its amount was to be reduced as such debt amortized in increments of \$0.1 million per month. Piedmont was also granted a second lien on the assets of FAvS to secure the repayment obligations of FAvS in the event that the letter of credit is drawn upon. Piedmont also entered into an intercreditor agreement with the lender to FAvS which subordinated Piedmont's claims if the letter of credit is drawn upon to the obligations of FAvS to the lender. This guarantee was later terminated on March 2013, see below.

As of December 31, 2010, TAT recognized an impairment charge of \$1.8 million of its then 37% interest in FAvS that was based on an independent appraisal. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels.

A commercial dispute between Piedmont and FAvS relating to the propeller maintenance business which had been contributed to FAvS by Piedmont as part of the transaction discussed above arose in April 2010 when a customer of the propeller maintenance business requested reimbursement from FAvS for damages to certain propellers. FAvS then sought reimbursement from Piedmont for such amounts. Although Piedmont rejected all of FAvS' claims with regards to Piedmont's responsibility for the claimed damages, in July 2010, the parties reached an agreement pursuant to which Piedmont loaned \$700,000 to FAvS and agreed to bear a portion of the additional cost of the replacement of propeller blades that FAvS would be responsible for. In exchange FAvS agreed to waive all claims against Piedmont with respect to such customer. Such loan was subsequently forgiven.

Notwithstanding such waiver, in the last quarter of 2010, FAvS again asserted claims against Piedmont relating to the propeller maintenance business including claims not previously asserted. After reviewing this issue during the 2010 fourth quarter and thereafter, Piedmont estimated the additional liability it may bear and accordingly wrote off the loan and recorded an accrual, which it believed, covered its potential cost in connection with this matter.

In order to finally settle all disputes between them, on June 30, 2011 Piedmont and FAvS entered into a Settlement Agreement and Release (the "Settlement Agreement"). Pursuant to the Settlement Agreement, each party fully released the other party and acknowledged that the settlement was a compromise of disputed claims and was not to be construed as an admission of liability or wrongdoing. In addition, each party agreed not to disparage the other and Piedmont paid an aggregate of \$700,000 to FAvS.

Simultaneously with the execution of the Settlement Agreement, Mr. Hollander, the Chief Executive Officer and controlling stockholder of FAvS, purchased 166,113 shares of Class A Common Stock of FAvS at a price of \$18.06 per share (for an aggregate price of \$3 million) (share price and share amount adjusted as result of a **1 for 20** reverse stock split) following which Piedmont's interest in FAvS was diluted to 30.6% (29.64% as of December 31, 2012). In addition, Piedmont agreed to extend its guarantee of the bank debt incurred by FAvS to fund the AeTR transaction through June 30, 2013 and to continue to provide a letter of credit to secure such guarantee. The amortization schedule for such debt was revised so that no amortization would occur until June 30, 2012. Thereafter the debt amortized at the rate of \$200,000 per month. As of December 31, 2012, the guaranty amount was \$4.6 million. The guaranty was terminated in March 2013, see below.

The Stockholders Agreement entered into in 2009 between Piedmont and Mr. Hollander was also amended to delete the reciprocal drag along rights and to provide that Piedmont may designate one member to the Board of Directors of FAvS (rather than the two provided in the original agreement). Finally, the Rights Agreement entered into in 2009 between Piedmont and FAvS was amended so that Piedmont's right to approve certain material corporate actions by FAvS has been limited to the right to approve contracts or agreements with affiliates of FAvS. The amendment also provides that the approval of Piedmont will not be required if FAvS seeks to raise additional capital from Mr. Hollander so long as the consideration being paid by Mr. Hollander is not less than the consideration that would be paid by a third-party in an arms-length transaction and is fair, equitable and reasonable under the circumstances.

In connection with the Settlement Agreement and the dilution in Piedmont's interest in FAvS, Piedmont recorded, at June 30, 2011, a gain in the amount of \$0.24 million related to the \$3 million capital investment in FAvS.

In June, 2012, FAvS entered into a transaction with Mr. Hollander, pursuant to which FAvS borrowed \$3 million from Mr. Hollander, secured by a third lien on the assets of FAvS. The loan bears annual interest at 10% and in addition Mr. Hollander was issued warrants to purchase shares of Class A Common Stock of FAvS, representing 15% of FAvS post-exercise shareholders' equity, at an exercise price of \$7.00 per share.

Pursuant to the terms and conditions of the transaction, management believed that there were indicators of impairment with respect to TAT's investment in FAvS. Accordingly, the Company performed an impairment test of its investment in FAvS, with the assistance of a third party valuation. Based on the results of this test the Company determined that its investment in FAvS was impaired by \$3.3 million. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels which related to the business of API, one of FAvS subsidiaries, and approximates TAT's share in the loss resulting from the API Transaction discussed below.

On March 18, 2013 FAvS sold 97% of the stock of API for a total purchase price of \$16.5 million, of which \$15.9 million was used to repay debt (the "API Transaction"). The sale resulted in FAvS retaining a 3% equity interest in the API business. The API transaction resulted in a loss from discontinued operations and write-down of the API business of \$11.5 million which is included in the FAvS loss for the year ended December 31, 2012. Simultaneously with the transaction FAvS paid-off its Term Loan in the amount of \$4 million thereby terminating the guaranty and releasing the Letter of Credit provided by TAT to secure such guaranty. Accordingly the restricted deposit associated with the above Letter of Credit, was released as well.

In October 2012 two lenders to TAT's controlling stockholders, KMN Industries and TAT Industries (herein "Controlling Stockholders"), filed separate petitions to the court to enforce liens granted to such lenders by each of the Controlling Stockholders in certain collaterals including KMN Industries' holdings of an approximately 80% ownership interest in TAT Industries (which owns approximately 43% of TAT) and KMN Industries' direct holdings in TAT (which represents approximately 10% of TAT).

On December 18, 2012 the court appointed permanent receivers on behalf of the two lenders mentioned above for the purpose of jointly enforcing the liens granted to such lenders. Such collateral is subject to sale which will result in a change of control of TAT. On March 15, 2013 the receivers of TAT's shares mentioned above announced a tender to purchase such shares. Pursuant to the tender all proposals to acquire such shares must be submitted no later than April 25, 2013. As of the date hereof, the Company has no information with respect to any proposals received.

On January 3, 2013 the Israeli court appointed a temporary liquidator for Isal Amlet, the controlling shareholder of TAT Industries, following the request of the trustee to debentures issued by Isal Amlet. On January 28, 2013 such court has issued a Liquidation Order for Isal Amlet, effective as of end of May 2013.

**A. Business Overview**

**Overview**

TAT provides a variety of services and products to the commercial and military aerospace and defense industries and operates under four segments: (i) Original Equipment Manufacturing or "OEM" of Heat Management Solutions (ii) OEM of Electric Motion Systems (iii) Heat Transfer Services and Products, and (iv) Maintenance, Repair and Overhaul or "MRO" services for Aviation Components, each with the following characteristics.

TAT's activities in the field of OEM of Heat Management Solutions primarily relate to its Gedera facility and include (i) the design, development, manufacture and sale of a broad range of heat transfer components (such as heat exchangers, pre-coolers and oil/fuel hydraulic coolers) used in mechanical and electronic systems on-board commercial, military and business aircraft; (ii) the manufacture and sale of environmental control and cooling systems and (iii) a variety of other electronic and mechanical aircraft accessories and systems such as pumps, valves, power systems and turbines.

TAT's activities in the field of OEM of Electric Motion Systems primarily relate to its subsidiary, Bental, and include the design, development, manufacture and sale of a broad range of electrical motors, alternators, blowers' drivers and actuators for different applications for airborne and ground systems.

TAT's activities in the field of Heat Transfer services and products primarily relate to its subsidiary, Limco, and include the maintenance, repair and overhaul of heat transfer equipment and to a lesser extent, the manufacturing of certain heat transfer products. TAT's Limco subsidiary operates an FAA certified repair station, which provides heat transfer MRO services and products for airlines, air cargo carriers, maintenance service centers and the military. Limco is also certified by the European Aviation Safety Agency, or EASA, and the Civil Aviation Administration of Thailand (Thai).

TAT's activities in the field of MRO services for aviation components primarily relate to its subsidiary, Piedmont, and includes the maintenance, repair and overhaul of APUs, landing gear and other aircraft components. TAT's Piedmont subsidiary operates an FAA certified repair station, which provides aircraft component MRO services for airlines, air cargo carriers, maintenance service centers and the military.

As mentioned above under 'History and Development of TAT', Piedmont's Parts services division, was operated until December 4, 2009, when it was sold to FAvS, in which TAT now holds an equity interest of approximately 29.64%.

FAvS, together with its subsidiaries, offers maintenance, repair and overhaul services through three Federal Aviation Administration authorized facilities. Customers of FAvS include passenger and cargo airlines, general aviation, and military operators.

***OEM of Heat Management Solutions***

TAT is an OEM of Heat management solutions, primarily through its Gedera facility, to the aerospace and defense industries. The main OEM activity of Gedera is the design and manufacture of a complete line of heat transfer products, including heat exchangers, pre-coolers, oil coolers and cold plates, or heat transfer products. Heat transfer products facilitate the necessary removal and dissipation of heat generated during the operation of mechanical and electronic systems. Gedera's heat transfer products are generally integrated into a complete cooling system. Using Gedera's technological expertise, Gedera designs each of its heat transfer products to meet the specific space, power, performance and other needs of its customers. Gedera's heat transfer products are marketed worldwide for applications in commercial and military aircraft and electronic systems, the primary users of such equipment. Gedera's customers include Liebherr-Aerospace Toulouse S.A., or Liebherr, Boeing McDonnell Douglas Aerospace, or Boeing, Israel Aerospace Industries, or IAI, Cessna Aircraft Company, or Cessna, Cirrus Aircraft Inc., or Cirrus, Pilatus Aircraft Ltd, or Pilatus, Embraer Empresa Brasileira de Aeronáutica S.A., or Embraer, Eaton Aerospace LLC, or Eaton, Parker Hannifin Corporation, or Parker, as well as the United States Air Force, United States Army, and Navy. Such customers typically enter into supply contracts with Gedera pursuant to which Gedera manufactures specified heat transfer products in connection with the customers' production or retrofitting of particular aircraft equipment. Such supply contracts are generally long term engagements that may have terms of ten years or more.



As part of its OEM activities, Gedera is also engaged in the design, development and manufacture of complete environmental control systems and complete cooling systems. This product line principally includes cooling systems for electronic systems (used in airborne military platforms), ground cooling systems (used in military facilities, tents, vehicles and other military applications) and Vapor Cycle air conditioning systems (or ECS — Environmental Cooling Systems) used in light aircraft.

In addition, Gedera designs, develops and manufactures aviation and flow control accessories. These accessories include fuel components, such as valves and pumps, secondary power systems, and various instrumentation and electronic assemblies. Customers for Gedera's aviation accessories include Lockheed-Martin Corp, Teledyne Continental Motors, the Israeli Air Force, IAI, Elbit Systems, or Elbit, as well as the United States Air Force and Navy.

Gedera also provides limited MRO services for military customers, mainly for aviation accessories as well as for certain heat transfer products. Gedera currently overhauls emergency power systems, hydrazine tanks, jet fuel starters, and cooling turbines and valves for F-16s. In addition, Gedera overhauls anti-icing valves and starters for the Apache helicopter. Customers for Gedera's MRO services include the Israeli Air Force, IAI, NATO, as well as the United States Air Force, United States Army, and Navy.

Gedera relies on highly qualified personnel and strong engineering, development and manufacturing capabilities that enable it to support its customers from the early stages of development of their product and system specifications.

TAT estimates the size of the markets in which Gedera operates to be significant based on the scope of development projects and purchasing processes of its customers. Many of the projects Gedera is engaged in are lengthy and complex, which account for its long term supplier relationships and the customer loyalty it enjoys. TAT plans to expand its Gedera operations in the OEM segment, among other things, by transitioning from the manufacture of standalone components to the development and manufacture of complete systems/sub systems, and by targeting strategic territories with high commercial potential.

### ***OEM of Electric Motion Systems***

Through its subsidiary, Bental, TAT is an OEM of a wide range of innovative electric motion components and systems for the defense, aerospace and industrial markets. Bental designs and manufactures high performance, high precision motion systems and sub-systems that operate under challenging conditions. Bental specializes in innovative motion technologies such as brush and brushless motors, permanent magnet generators, electronic drivers and controllers, servo actuators, stabilized payload systems and more. Bental's products are integrated into various aviation and defense platforms and applications, including turret and gun control systems for armored fighting vehicles (AFVs), unmanned air, naval and ground vehicles (UAVs, USVs, UGVs), tanks and military vehicles, missiles, jet engines, cryogenic coolers for thermal imaging systems, optical systems, rotational drives for large antennae pedestals and more.

Bental's products have to comply with severe performance requirements, environmental conditions, quality assurance and industry standards. Bental usually manufactures relatively small series of products, custom designed for specific customer orders. Bental's products are designed either of its own initiatives or pursuant to customer specifications. Bental relies on highly qualified personnel and strong engineering, development and manufacturing capabilities that enable it to support its customers from the early stages of development of their product and system specifications. Bental targets customers mainly in the defense market and to a lesser extent, in the commercial market. Its customers include military forces, defense industries, commercial manufacturers of military equipment, commercial airlines, aircraft manufacturers, and other manufacturers of machinery. Bental is a certified supplier to IAI, Rafael, Israeli Ministry of Defense (MOD), Aeronautics, Raytheon, Elbit Systems, Pall Aeropower, Kodak (Creo), IBM, Galileo Avionica and others.

TAT estimates the size of Bental's market for its products to be significant based on the scope of development projects and purchasing processes of its customers. Many of the projects Bental is engaged in are lengthy and complex, which account for its long term supplier relationships and the customer loyalty it enjoys.

Bental plans to expand its OEM operations, among other things, by transitioning from the manufacture of standalone components to the development and manufacture of complete systems, by extending its operation towards commercial aviation market, by developing Product Manufacturing Authorization, or PMA products and by targeting international markets.

#### ***Heat Transfer Services and Products***

Through its subsidiary, Limco, TAT provides Heat Transfer services and products to the aerospace industry. Limco's FAA certified repair station provides aircraft component MRO services for airlines, air cargo carriers, maintenance service centers and the military. Limco is also certified by EASA, and the Civil Aviation Administration of Thailand (Thai). Limco specializes in MRO services for components of aircraft, such as heat transfer products and pneumatic ducting. Generally, manufacturer specifications, government regulations and military maintenance regimens require that aircraft components undergo MRO servicing at regular intervals or as necessary. Aircraft Heat Exchangers typically require MRO services, including repairs and installation of replacement units, after three to ten years of service or sooner if required. Aircraft manufacturers typically provide warranties on new aircraft and their components and subsystems, which may range from one to five years depending on the bargaining power of the purchaser. Warranty claims are generally the responsibility of the OEM during the warranty period. Limco's business opportunity usually begins upon the conclusion of the warranty period for these components and subsystems. Limco's customers include major US domestic and international airlines, air cargo carriers, maintenance service centers, OEMs such as commercial and military aircraft manufacturers and defense contractors, and the U.S. government (Army, Air Force and Coast Guard). Such customers typically enter into MRO contracts with Limco which are generally long term engagements that may have terms of one to ten years or more.

Limco is authorized by leading OEMs of aerospace products to provide MRO services for their systems. For example, Limco is a well recognized Hamilton Sundstrand repair center, providing MRO services for all of its air-to-air heat transfer products. Limco's repair station is certified by the FAA and EASA.

In addition to its MRO services, Limco also manufactures heat transfer products used in commercial, regional, business and military aircraft, complete environmental control systems and cooling systems for electronics. Customers for Limco's heat transfer products include the U.S. Army, Air Force and Navy, Raytheon, Boeing, Bell Helicopters, Vought Aircraft, Spirit and Gulfstream.

Limco relies on highly qualified personnel with strong manufacturing, engineering and development capabilities that enable it to provide excellent MRO services while supporting customers' specifications in the development of their new products and systems.

TAT estimates the size of the markets in which Limco operates to be significant based on the number of aircraft requiring MRO services provided by Limco along with the customer loyalty Limco enjoys. TAT plans to expand its Limco operations in the MRO segment, among other things, by developing MRO capabilities for additional types of heat transfer products with significant commercial potential.

***MRO services for Aviation Components***

Through its subsidiary, Piedmont, TAT provides MRO services for aviation components to the aerospace industry. Piedmont's FAA and EASA certified repair station provides aircraft component MRO services mainly for airlines, air cargo carriers and maintenance service centers. Piedmont specializes in MRO services for components of aircraft, such as APUs and landing gears. Generally, manufacturer specifications, government regulations and military maintenance regimens require that aircraft components undergo MRO servicing at regular intervals or as necessary. Aircraft components typically require MRO services, including repairs and installation of replacement units, after three to ten years of service or sooner if required. Aircraft manufacturers typically provide warranties on new aircraft and their components and subsystems, which may range from one to five years depending on the bargaining power of the purchaser. Warranty claims are generally the responsibility of the OEM during the warranty period. Piedmont's business opportunity usually begins upon the conclusion of the warranty period for these components and subsystems. Piedmont's customers mainly include US domestic and international airlines, air cargo carriers and maintenance service centers. Such customers typically enter into MRO contracts with Piedmont which are generally long term engagements that may have terms of one to ten years or more.

Piedmont is licensed by Honeywell as an authorized repair center, to provide MRO services for several of its APU models. Piedmont's repair station is certified by the FAA and EASA.

Piedmont relies on highly qualified personnel with strong manufacturing, engineering and development capabilities that enable it to provide excellent MRO services.

TAT estimates the size of the markets in which Piedmont operates to be significant based on the number of aircraft requiring MRO services provided by Piedmont. TAT plans to expand its Piedmont operations in the MRO segment, by using Piedmont's experience and reputation to develop MRO capabilities for additional types of APU and landing gear with significant commercial potential and by offering additional supplementary services such as machining, plating and grinding, or MPG.

## Business Strategy

TAT's principal strategy is as follows:

- **Enhancing OEM Capabilities** — TAT's goal through Gedera, Limco and Bental is to capitalize on its technical expertise, experience and reputation in the markets of heat management solutions and electrical motion systems, to expand the scope of its OEM offerings both in the airborne and ground segments, for the commercial and defense industries. TAT also intends to continue the transition from the development and manufacture of single components to the development and manufacture of complete systems.
- **Expand the scope of MRO services** - TAT's goal is to use its technical expertise, engineering resources and facilities to provide MRO services for additional types of aircraft and additional aircraft systems, subsystems and components and intends to develop the required technical expertise to provide these additional MRO services.
- **Increasing Market Share** — TAT plans to continue its aggressive marketing efforts for new customers as well as to expand its activities with its flagship customers. As part of TAT's efforts to achieve greater penetration in the international markets, TAT intends to expand its marketing presence in Western Europe, which is TAT's second largest market, and to substantially increase its presence in Asian, Far East, South American nations, East Europe and Africa, which are fast growing markets where TAT has had limited sales to date.
- **Penetrating the PMA Market** — TAT's goal, through Bental is to capitalize on its technical expertise, experience and reputation in the markets of electric motion systems, to expand the scope of its OEM offerings to the Product Manufacturing Authorization, or PMA as a supplier of off the shelf, cataloged electric motion motors for the commercial and defense industries.

- **Effective synergy among group members** — TAT plans to enhance the synergies between its various businesses by, among other things, using Gedera's OEM design capabilities to provide Limco enhanced capabilities to repair heat transfer systems and products, enabling Limco to compete more effectively in the industry and by supplying to Limco heat transfer components which should enable Limco to reduce prices on its MRO services. In addition, TAT believes that its acquisition of Bental provides growth potential and plans to capitalize on its affiliation with Bental by penetrating new markets such as the market for ground systems and introducing technologically innovative products to its existing customers.
- **Organic growth and M&A** — In addition to growing the existing businesses of Gedera, Limco and Bental, TAT also believes that additional acquisition opportunities exist that will complement its OEM and MRO businesses. TAT will continue to pursue targeted complementary business acquisitions which will broaden the scope and depth of its OEM and MRO operations and increase its market share.

## Products and Services

### *OEM of Heat Management Solutions*

Through its Gedera facility, TAT manufactures a wide range of heat transfer products used on board aircraft, air conditioning systems, environmental control systems and cooling systems for electronics for military use. These products/systems are manufactured in compliance with all of the stringent quality assurance standards that apply to the manufacture of aircraft parts. Gedera's quality systems comply with ISO 9001, AS9100, Boeing quality systems approval D6-82479 and FAR 21.303 (the FAA standard for Parts Manufacturer Approval).

### *Heat Transfer Products*

Gedera manufactures a wide range of heat transfer products. Gedera specializes in the design and manufacturing of highly efficient, compact and reliable heat transfer products that are designed to meet stringent constraints such as size, weight and applicable environmental conditions. Heat transfer products, such as heat exchangers, precoolers, evaporators, oil coolers and cold plates, are integral components of a wide variety of environmental control systems and mechanical and engine systems, as well as a wide range of electronic systems. These systems generate heat during operation that must be removed and dissipated. Heat transfer products facilitate the exchange of the heat created through the operation of these systems by transmitting the heat from a hot medium (air, oil or other fluids) to a cold medium for disposal.

In the aerospace industry, there is a constant need for improvements in performance, weight, cost and reliability. In addition, as electronic systems become smaller and more densely packed, the need for sophisticated and efficient heat transfer components to provide the cooling functions becomes more critical. Using Gedera's technological expertise, TAT believes it is well positioned to respond to these industry demands through continued new product development and product improvements.

Gedera's principal heat transfer products include air-to-air heat exchangers and precoolers and liquid-to-air heat exchangers. Typically, the air-to-air heat exchangers and precoolers cool a jet engine's hot "bleed air" which, when cooled, is then used in the aircraft's air conditioning, pressurization and pneumatic systems. The liquid-to-air heat exchangers cool liquids such as engine oil, hydraulic oil and other liquid coolants used in other systems.

Gedera provides one to all of the different types of heat transfer products in certain aircraft. Wide body planes generally require seven different types of heat transfer components, while regional aircraft and helicopters contain approximately three types. Gedera's heat exchangers and precoolers are generally sold for between \$2,000 and \$20,000 per unit. A significant portion of Gedera's heat transfer products are sold to customers in connection with the original manufacture or retrofitting of particular aircraft equipment. Gedera generally enters into long-term supply contracts with its customers, which require Gedera to supply heat transfer products as part of a larger project.

Gedera also manufactures heat dissipation equipment, such as evaporators, cold plates, cooling chests, heat sinks and old walls (which may be air-to-air, liquid-to-air or liquid-to-liquid), which control and dispose of heat emitted by the operation of various electronic systems. These heat dissipation products are currently utilized mainly in radar systems, avionics, electronic warfare systems and various pods for targeting, navigation and night vision.

Gedera's customers for heat transfer products/systems include: Liebherr, Boeing, IAI, Cessna, Bell Helicopter, Raytheon Aircraft Company, as well as the United States Air Force and Navy. As a result of the specialized nature of the systems in which Gedera's parts are included, spare and replacement parts for the original heat transfer products/systems are usually provided by Gedera.

#### *Aviation And Flow Control Accessories*

Gedera is also engaged in the design, development and manufacture of aviation and flow control accessories. These accessories include fuel component systems, such as valves and pumps, secondary power systems, various instrumentation and electronic assemblies. Gedera's customers for the design, development and manufacture of aviation and flow control accessories include Lockheed-Martin, Boeing, Teledyne, the Israeli Air Force, IAI, as well as the U.S. Air Force and Navy.

#### *Cooling And Air-Conditioning Systems*

Gedera is also engaged in the design, development and manufacture of complete environmental control systems and cooling systems. This product line includes ground cooling systems used in military facilities, tents, vehicles and other military applications. It also includes Vapor Cycle air conditioning systems (or ECS — Environmental Cooling Systems) used in light aircraft. Gedera offers mobile cooling and air conditioning solutions for military applications such as mobile command and control units, command and control vehicles, armored vehicles, mobile broadcast units, mobile hospitals, etc. In addition, Gedera offers a generic complete cooling systems for aircraft systems such as environmental control systems, engine starter systems and hydraulic systems and also offers air conditioning systems for light airplanes and helicopters, either as part of the development process of new aircraft or as an upgrade for existing aircraft. Gedera designs, develops and manufactures the air conditioning systems based on customer specifications, while providing a complete engineering solution in compliance with strict military and civil standards. Gedera's systems are used for military applications in Israel and abroad and are tested under strict standards and in battle field proven conditions.

#### *OEM of Electric Motion Systems*

Through its Bental subsidiary in Israel, TAT designs, develops and manufactures a wide range of innovative motion systems and other electro-mechanical solutions for the defense, aerospace and industrial markets. Bental's primary product lines are electric motors, actuators and alternators, and include the following list of products: customized electrical motors, alternators, drivers, actuators, stabilized payload control systems, propulsion motors, starter generators, blowers, turret & gun control system motors and more. Such products are integrated into various platforms and applications such as turret & gun control systems and other systems of military ground vehicles, unmanned aerial, naval and ground vehicles (UAV's, USVs, UGVs), missiles, jet engines, cryo-coolers for thermal imaging systems, optical systems, rotational drives for large antennae pedestals, medical equipment, semi conductor industry process, testing and quality assurance equipment, large printing machines and diamond polishing spindles. Bental's customers include IAI, Israeli MOD, Rafael, Raytheon, Elbit Systems, Pall Aeropower, Kodak (Creo), IBM, Galileo Avionica and others. Bental's products are manufactured based on customer specifications, often with special performance requirements which are suited for extreme environmental conditions for military and commercial applications. Bental's products are manufactured in compliance with ISO 9001 and are subject to strict quality control and inspection procedures that are carried out through all steps of design and manufacture.



#### *Electric Motors*

Bental develops, designs and manufactures different types of electric motors for use in an array of motion systems which are designed to comply with special performance requirements and be suitable for extreme environmental conditions for military ground equipment and remote-piloted vehicle applications. Bental also develops, designs and manufactures electric motors for special uses for customers in the commercial segment. In addition, Bental provides maintenance and repair services for the equipment manufactured by it. Bental also imports mass produced motors in large quantities pursuant to special orders from its customers in Israel.

#### *Actuators*

Bental develops, designs and manufactures an array of actuators for unmanned aerial vehicles and remote-piloted vehicle and other aerospace applications, to comply with special performance requirements and extreme environmental conditions.

Bental's Rotary Servo Actuator (RSA) systems are developed with tactical UAV manufacturers in mind. The RSA systems are high performance, low-weight compact servo actuators used for various aviation and UAV applications. The systems include motor, reduction gear, feedback sensor and electronic servo control & amplifier.

#### *Alternators*

Bental develops, designs and manufactures different types of alternators for automatic pilot and other military applications, to comply with special performance requirements and extreme environmental conditions.

The product line of brushless direct current alternators is based on rare earth magnet technology. The systems are capable of supplying very high power. The alternator product family is designed to serve aerospace and other defense applications. Bental's systems are comprised of the alternator and Generator Control Unit (GCU).

## ***Heat Transfer Services and Products***

### ***MRO Services For Heat Transfer Products***

Through its Limco subsidiary in the U.S., TAT provides MRO services for Heat Transfer products. The demand for MRO services is driven by the size and age of the aircraft fleet, aircraft utilization and regulations by the FAA and other governmental authorities.

Due to the increased maintenance costs of their aging fleets many carriers are seeking ways to reduce costs, minimize down-time, increase aircraft reliability and extend time between overhauls. One of the ways they are accomplishing these goals is through the outsourcing of more of their maintenance and support functions to reliable third parties. Limco also believes that commercial carriers who have made the decision to outsource their MRO requirements are searching for MRO service providers with a wide-range of service capabilities. These MRO service providers allow the carriers to concentrate their outsourcing of MRO services to a select group of third party providers. The global military aircraft fleet also presents similar opportunities for MRO service providers. Recent military operations around the world have significantly increased usage of the global military aircraft fleet and resulted in a higher rate of maintenance activity. Limco believes that an aging military fleet and the increased use of upgrade programs aimed at extending the useful life of aircraft will provide continued MRO growth opportunities.

Limco specializes in the repair and overhaul of heat transfer products. Heat transfer products are devices that efficiently transfer heat from one fluid to another or from hot air to colder air in various cooling systems and are essential components of an aircraft. These products include heat exchangers, oil coolers, pre-coolers, re-heaters, condensers, water separators and evaporators.

Limco is continually increasing its MRO capabilities based upon market need or customer request. Limco's capabilities include heat transfer components used in aircraft and systems manufactured by Airbus, Boeing, Bombardier, Cessna, Embraer, Lockheed Martin, Fokker, Fairchild, Gulfstream, British Aerospace and others.

One of Limco's operational strengths and competitive advantages is the close cooperation with TAT's Gedera facility. Through Gedera's core manufacturing capabilities and engineering expertise, Limco enjoys a constant supply source of cores of the highest quality necessary in order to perform its MRO services for Heat Transfer products. In addition, Limco benefits from Gedera's varying engineering and development capabilities relevant to Limco's Heat Transfer services.

Limco performs MRO services at its repair station in Tulsa, Oklahoma which is ISO9000 and AS9100 certified and licensed by the FAA and EASA, as well as by the Civil Aviation Administration of Thailand, to provide MRO services. Limco's Oklahoma facilities provided MRO services for heat transfer products.

Limco offers MRO services for heat transfer components to its customers on multiple levels. If the damage is significant, Limco will remanufacture the unit, which generally entails replacing the core matrix of the damaged or old heat transfer product in lieu of replacing the entire unit with a new one. Limco designs and develops these customized remanufactured units as a cost effective alternative to new part replacement. In the event of less severe damage, Limco will either overhaul or repair the unit as necessary. Re-manufactured units carry warranties similar to those provided to new units.

#### *OEM Authorizations And Licenses*

Limco believes that establishing and maintaining relationships with OEMs of aircraft systems and components, is an important factor in achieving sustainable success as an independent MRO service provider. OEMs grant participants in the overhaul and repair services market authorizations or licenses to perform repair and overhaul services on the equipment they manufacture. OEMs maintain tight controls over their authorized and licensed MRO service providers, in order to maintain high quality of service to their customers, and generally grant very few authorizations or licenses. Obtaining OEM authorizations requires sophisticated technological capabilities, experience-based industry knowledge and substantial capital investment. Limco believes that service providers that have received OEM authorizations and licenses gain a competitive advantage because they typically receive discounts on parts, technical information, OEM warranty support and use of the OEM name in marketing. Limco is an independent MRO service provider that is a well recognized repair center of Hamilton Sundstrand, the largest heat transfer equipment manufacturer, for its air-to-air heat transfer equipment in North America.

#### *OEM Capabilities*

In addition to its MRO services, Limco also acts as an OEM manufacturer of heat transfer products used mainly in military aircraft and also in commercial, regional and business aircraft. Limco specializes in the design and manufacturing of highly efficient heat transfer components, which are designed to meet stringent constraints such as size, weight and applicable environmental conditions. These units include heat exchangers, oil coolers, pre-coolers, re-heaters, condensers, fuel heaters and evaporators.

Limco also manufactures air conditioning systems, complete environmental control systems and cooling systems for electronics. Limco currently offers approximately 80 OEM parts to the aerospace industry. These parts are manufactured in compliance with the stringent quality assurance standards that apply to the manufacture of aircraft parts.

Limco's quality systems are ISO9000 and AS9100 certified and Limco has both Boeing quality systems approval D6-82479 and FAR 21.303 (the FAA standard for Parts Manufacturer Approval).

#### ***MRO Services for Aviation Components***

Through its Piedmont subsidiary in the U.S., TAT provides MRO services for aviation components, APUs and Landing Gear. As previously mentioned, the demand for MRO services is driven by the size and age of the aircraft fleet, aircraft utilization and regulations by the FAA and other governmental authorities.

Due to the increased maintenance costs of their aging fleets many carriers are seeking ways to reduce costs, minimize down-time, increase aircraft reliability and extend time between overhauls. One of the ways they are accomplishing these goals is through the outsourcing of more of their maintenance and support functions to reliable third parties. Piedmont also believes that commercial carriers who have made the decision to outsource their MRO requirements are searching for MRO service providers with a wide-range of service capabilities. These MRO service providers allow the carriers to concentrate their outsourcing of MRO services to a select group of third party providers. The global military aircraft fleet also presents similar opportunities for MRO service providers. Piedmont believes that an aging military fleet and the increased use of upgrade programs aimed at extending the useful life of aircraft will provide continued MRO growth opportunities.

Piedmont specializes in the repair and overhaul of APUs and landing gear. APUs are relatively small, self-contained generators used to start jet engines, usually with compressed air, and to provide electricity, hydraulic pressure and air conditioning while an aircraft is on the ground. In many aircraft, an APU can also provide electrical power during in-flight emergency situations. Landing gear are the structure that support an aircraft on the ground and allow it to taxi, takeoff and land.

Piedmont performs MRO services at its repair station in North Carolina, which is AS9001 certified and licensed by the FAA and EASA to provide MRO services.

Piedmont specializes in providing MRO services for APU models manufactured primarily by Honeywell, and in providing MRO services for landing gear for regional aircraft manufactured by Bombardier Canadair Regional Jet, ATR, British Aerospace Jet Stream and Bombardier Dash 8.

#### *OEM Authorizations And Licenses*

Piedmont believes that establishing and maintaining relationships with OEMs of aircraft systems and components is an important factor in achieving sustainable success as an independent MRO service provider. OEMs grant participants in the overhaul and repair services market authorizations or licenses to perform repair and overhaul services on the equipment they manufacture. OEMs maintain tight controls over their authorized and licensed MRO service providers, in order to maintain high quality of service to their customers, and generally grant few authorizations or licenses. Obtaining OEM authorizations requires sophisticated technological capabilities, experience-based industry knowledge and substantial capital investment. Piedmont believes that service providers that have received OEM authorizations and licenses gain a competitive advantage because they typically receive discounts on parts, technical information, OEM warranty support and use of the OEM name in marketing. Piedmont is an authorized repair station licensed by Honeywell, the largest manufacturer of APUs, for several of its APU models.

#### *Machining, Plating and Grinding, or MPG Services*

Piedmont extended the provision of MPG services, either as supplementary to its traditional MRO services or as stand-alone services. Piedmont believes that establishing and maintaining relationships with customers to its MPG shop is an important factor in achieving sustainable success as an independent MRO service provider and creates a competitive advantage.

Customers.

General

TAT targets both the commercial and defense markets for aviation and ground applications. Our customers include commercial manufacturers of military equipment, commercial airlines, aircraft manufacturers, military forces, defense industries, and other manufacturers of electronic systems, aviation units and machinery in the U.S., Europe, Asia, South America and Israel.

Major Customers

OEM Customers

TAT provides, primarily through Gedera and Bental, OEM services worldwide to customers in the commercial, defense and industrial markets. TAT currently sells its OEM products and systems to approximately 200 commercial and military aircraft manufacturers and defense contractors, and the U.S. and Israeli governments.

TAT's leading OEM customers are set in the following table:

Aircraft manufacturers	Boeing McDonnell Douglas Aerospace, Airbus, Cessna Aircraft Company, Bombardier, Cirrus Aircraft Inc., Pilatus Aircraft Ltd, Embraer Empresa Brasileira de Aeronáutica S.A, Bell Helicopters, Lockheed Martin,
System manufacturers/integrators and Defense Contractors	Liebherr-Aerospace, Thales Electron Devices, Honeywell International, Rafael, Elbit, IAI, LockheedAeronautics, Schiebel, Martin, Fairchild, British Aerospace, EADS, Eaton Aerospace, Parker Hannifin Corporation.
Industry players	Kodak (Creo), IBM

The development projects and purchasing processes of many of TAT's OEM customers are lengthy and complex and accordingly, involve long term supply contracts with several of its material customers. These agreements provide for delivery schedules that are customized for the relevant product or service. With some of its customers, TAT enters into master purchase orders in which the anticipated supply quantities as well as the prices for the supplied products are determined for a certain period, and the actual purchase orders are fulfilled based on customer demands from time to time. In addition, TAT also enters into master agreements that determine supply quantities and prices for a set period, but under which the customer is not obligated to purchase any quantity of products.

*MRO Customers*

TAT services approximately 200 MRO customers, primarily through Limco and Piedmont, including major U.S. domestic and international airlines, air cargo carriers, maintenance service centers, the U.S. military and navy and other military air forces. TAT is not a party to any OEM manufacturing contracts, and acts solely upon orders received from its MRO services' customers.

TAT's leading MRO customers are set in the following table:

Domestic and International Airlines and Air Cargo carriers	Lufthansa, , Singapore Airlines, Air France-KLM, SAS, Swiss, ELAL, Delta, United, US Airways, Air Canada Jazz, Air Wisconsin, Austrian Airlines
Maintenance Service Centers	Fokker, Honeywell International, Kellstrom Commercial, Aerokool
Government and Air forces	U.S. Army, Air Force and Navy; Israeli Air force; NATO Air-forces

Due to the long term relationships of TAT with many of its customers, their relative financial stability and their loyalty to TAT, TAT anticipates that the risk of major customer terminations is low. TAT also makes significant efforts to penetrate new markets and to broaden its customer base in order, among other things, to reduce the risk of relying on a small number of customers.

#### *Military Contracts*

Sales to the U.S. and Israeli governments accounted for approximately 3.6% and 0.7% of TAT's revenues for the year ended December 31, 2012, approximately 4.7% and 2.6% of its revenues for the year ended December 31, 2011 and approximately 3.7% and 3.6% of its revenues for the year ended December 31, 2010, respectively.

Many of TAT's contracts are competitively bid and awarded on the basis of technical merit, personnel qualifications, experience and price. TAT also receives some contract awards involving special technical capabilities on a negotiated, noncompetitive basis due to TAT's technical capabilities.

TAT provides products under government contracts that usually require performance over a period of several months to several years. Long-term contracts for the U.S. military may be conditioned upon continued availability of congressional appropriations. Variances between anticipated budget and congressional appropriations may result in a delay, reduction or termination of these contracts.

The vast majority of the governmental contracts to which TAT is party to are fixed-price contracts, some of which contain fixed price escalation mechanism. Under these contracts TAT agrees to perform specific work for a fixed price and, accordingly, realizes the benefit or detriment to the extent that the actual cost of performing the work differs from the contract price. The allowable government contract costs and fees of TAT are subject to audit and may result in non-reimbursement of some contract costs and fees. While governments reserve the right to conduct further audits, audits conducted for periods through fiscal year 2012 have resulted in no material cost recovery disallowances for TAT.

The eligibility of TAT to perform under their government contracts requires TAT to maintain adequate security measures. TAT have implemented security procedures that they believe adequately satisfies the requirements of their current government contracts.



## Sales and Marketing

### Gedera

Gedera derives its revenues mainly from sales to customers in the United States, Israel and Europe. The below tables detail Gedera's (i) geographic revenues; and (ii) revenues derived from commercial and defense customers, for the years ended December 31, 2012 and 2011, before elimination of intercompany sales of \$3.0 million and \$4.0 million, respectively.

Geographic Region	Year Ended December 31,			
	2012		2011	
	Revenues In Thousands	Percentage	Revenues In Thousands	Percentage
North America	\$ 11,064	35.7%	\$ 14,678	48.9%
Europe	6,570	21.2	5,771	19.2
Israel	9,326	30.1	8,218	27.4
Other	4,072	13.1	1,353	4.5
Total	\$ 31,032	100%	\$ 30,020	100%

	Year Ended December 31,			
	2012		2011	
	Revenues In Thousands	Percentage	Revenues In Thousands	Percentage
Commercial Customers	\$ 14,019	45.2%	\$ 10,040	33.4%
Defense Customers	17,013	54.8	19,980	66.6
Total	\$ 31,032	100%	\$ 30,020	100%

**Bental**

Bental derives its revenues mainly from sales to customers in Israel. The below tables detail Bental's (i) geographic revenues; and (ii) revenues driven from commercial and defense customers, for the years ended December 31, 2012 and 2011.

Sources of Revenues	Year Ended December 31,			
	2012		2011	
	Revenues in Thousands	Percentage	Revenues In Thousands	Percentage
North America	\$ 595	5.9%	\$ 480	4.1%
Europe	435	4.4	277	2.4
Israel	8,897	88.9	10,727	92.0
Other	80	0.8	174	1.5
Total	\$ 10,007	100%	\$ 11,658	100%

	Year Ended December 31,			
	2012		2011	
	Revenues In Thousands	Percentage	Revenues In Thousands	Percentage
Commercial Customers	\$ 440	4.4%	\$ 937	8.0%
Defense Customers	9,567	95.6	10,721	92.0
Total	\$ 10,007	100%	\$ 11,658	100%

**Limco**

Limco derives its revenues mainly from sales to customers in the US and Europe. The below tables details Limco's (i) geographic revenues and (ii) revenues derived from commercial and defense customers, for the years ended December 31, 2012 and 2011, respectively.

Sources of Revenues	Year Ended December 31,			
	2012		2011	
	Revenues in Thousands	Percentage	Revenues In Thousands	Percentage
North America	\$ 20,175	72.8%	\$ 22,583	81.8%
Europe	3,210	11.6	2,657	9.6
Israel	468	1.7	297	1.1
Other	3,856	13.9	2,066	7.5
Total	\$ 27,709	100%	\$ 27,603	100%

	Year Ended December 31,			
	2012		2011	
	Revenues In Thousands	Percentage	Revenues In Thousands	Percentage
Commercial Customers	\$ 15,240	55.0%	\$ 14,340	52.0%
Defense Customers	12,469	45.0	13,263	48.0
Total	\$ 27,709	100%	\$ 27,603	100%

**Piedmont**

Piedmont derives its revenues mainly from sales to customers in the US and Europe. The below tables details Piedmont's geographic revenues and (ii) revenues derived from commercial and defense customers, for the years ended December 31, 2012 and 2011, respectively.

Sources of Revenues	Year Ended December 31,			
	2012		2011	
	Revenues in Thousands	Percentage	Revenues In Thousands	Percentage
North America	\$ 16,442	73.3%	\$ 13,677	67.9%
Europe	4,717	21.0	5,596	27.8
Israel	-	-	90	0.4
Other	1,283	5.7	783	3.9
Total	\$ 22,442	100%	\$ 20,146	100%

	Year Ended December 31,			
	2012		2011	
	Revenues In Thousands	Percentage	Revenues In Thousands	Percentage
Commercial Customers	\$ 22,442	100%	\$ 20,146	100%
Defense Customers	-	-	-	-
Total	\$ 22,442	100%	\$ 20,146	100%

Gedera, Bental, Limco and Piedmont market their products and services through their respective marketing staffs and a worldwide network of independent representatives. Gedera's, Bental's, Limco's and Piedmont's representatives are strategically located near key customer sites in offices throughout the United States, Europe, the Middle East, Asia and South America. Their staff is in regular contact with engineering and procurement personnel and program managers of existing and target customers to identify new programs and needs for their products, obtain requests for quotations and identify new product opportunities. Gedera's, Bental's, Limco's and Piedmont's marketing activities also include advertising in technical publications which target heat transfer components and related markets, attending exhibitions, trade shows and professional conferences, organizing seminars and direct mailing of advertisements and technical brochures to current and potential customers and advertising in technical publications which target relevant products and related markets.

#### **Backlog**

At December 31, 2012, TAT had a backlog of approximately \$52.7 million for products and services. TAT anticipates that approximately \$31.8 million of such backlog will be delivered by December 31, 2013 and approximately \$20.9 million will be delivered by December 31, 2014 and thereafter. At December 31, 2011, TAT had a backlog of approximately \$55.4 million for products and services.

#### **Product and Service Warranties**

TAT provides warranties for its products and services ranging from one to three years, which vary with respect to each contract and in accordance with the nature of each specific product. To date, TAT's warranty costs have not been substantial. As of December 31, 2012, the combined warranty reserve for TAT was \$276 thousand.

## Competitive Environment

### *OEM of Heat Management Solutions*

The aerospace and defense OEM industries in general and specifically, the commercial and military aviation markets, are characterized by intense competition and the need to constantly be in the forefront of technological innovations in order to be able to offer advanced and attractive products. Competition in these OEM markets is also based on price, quality and turn-around time. TAT estimates the market size of heat management solutions to be significant based on the scope of development projects and purchasing processes of the potential customers. TAT estimates that due to the high barriers to enter the aerospace and defense OEM industries, which include the need for highly qualified and trained personnel, technologically advanced facilities and the need to obtain appropriate governmental approvals, there are a small number of competing suppliers in the markets in which it operates. The nature of the projects in the OEM industry, which are often time consuming and complex also require long term supplier relationships and customer loyalty in order to succeed.

TAT's competitors in the global OEM aerospace and defense industries can be divided into two main groups:

- Complete system manufacturers that either independently or through subcontractors, design, develop and manufacture complete systems (such as a manufacturer of a cooling system for aircraft hydraulic systems) directly for the platform manufacturer (i.e. hydraulic system; business jet). Although these companies have the capabilities to design and manufacture each standalone component in a complete system (i.e. a heat exchanger integrated in the cooling system for hydraulic systems) it is unlikely that such companies will compete with TAT in projects where there is a specific requirement for a stand-alone component. These companies will compete on complete systems and/or projects where the components/products TAT develops are part of the complete system. In such cases it is very likely that these companies will subcontract to companies such as TAT the design and manufacturing of one or a few components in the system.
- Component manufacturers for which the design and manufacture of components (such as heat exchangers) is the main business (and which are normally placed in the "value chain" one level below the system manufacturers, such as a manufacturer of a cooling system for aircraft's Hydraulic system and two levels below the platform manufacturer such as manufacturer of a new aircraft). For certain platform, although some of the Component manufacturers have the capabilities to design, develop and manufacture a complete system (i.e. environmental cooling system for business jet), these companies will usually not compete on projects for complete systems in which their manufactured component constitutes a small part of the complete system, mainly due to the extreme competitive barriers to entry and to their inability to move up the "value chain" from a component supplier to a whole system manufacturer. These companies are likely to compete in projects where there is a specific requirement for a standalone aviation component (such as a heat exchanger) and in tenders by manufacturers of complete systems or products for sub-contractors.

The major competitors of TAT in the area of OEM of Heat Management Solutions include manufacturers in the U.S. such as Honeywell International,, Hughes-Treidler division of Ametek Inc., Lytron Inc., Kintex, Niagra Thermal, Hamilton Sundstrand, Stewart Werner South Wind Corp., United Aircraft Products and Triumph Thermal Systems, manufacturers based in Europe such as I.M.I. Marston Ltd., Dunlop Aerospace (including Serck Aviation), Liebherr-Aerospace Toulouse S.A and manufacturers based in Asia such as Sumitomo Precision Products from Japan. Such competitors may enjoy competitive advantages over Gedera, such as:

- The ability to independently offer systems in addition to components;
- Greater access to capital;
- Stronger relationships with customers and suppliers;
- Better name recognition;
- Access to superior technology and marketing resources; and
- The ability to adapt more quickly to changes in customer requirements and industry conditions or trends.

#### ***Heat Transfer Services***

The market for Heat Transfer services and products is highly competitive. Competition in this market is based on quality, price, and the ability to provide a broad range of services and to perform repairs and overhauls rapidly. TAT's competitors in the global Heat Transfer Services can be divided into two main groups:

- Service Divisions of OEMs – generally, each OEM of products in the heat management solutions segment has the necessary capabilities to provide MRO services for products it designs and manufactures throughout their lifetime – commencing the initial production period and through the after-market period (service divisions of OEMs). These service divisions of OEMs may also acquire capabilities to service other OEM's products and to become a provider of MRO services.

- Service Centers – which provide MRO services for broad range of components and systems. These Service Centers can be either the in-house maintenance services of a number of commercial airlines or other independent service providers.

Accordingly, in the areas of OEM operations, manufacturers of components can compete with manufacturers of complete systems, mainly for small systems. Such OEM manufacturers can also compete for the provisions MRO services, with other providers of MRO service.

For heat transfer MRO services TAT's major competitors are the Triumph Accessories, Elite, Drake Air, LORI Heat Transfer Center of Honeywell and SECAN-Honeywell (France).

A number of Limco's competitors have inherent competitive advantages. For example, Limco competes with the service divisions of large OEMs who in some cases have design authority with respect to their OEM products and are able to derive significant brand recognition from their OEM manufacturing activities. Limco also competes with the in-house service divisions of large commercial airlines and there is a strong incentive for an airline to fully utilize the services of its maintenance employees and facilities. Further, Limco's competitors may have additional competitive advantages, such as:

- The availability of large quantities of expensive spare parts;
- Greater access to capital;
- Stronger relationships with customers and suppliers;
- Better name recognition;
- Access to superior technology and marketing resources; and
- The ability to adapt more quickly to changes in customer requirements and industry conditions or trends.



#### ***OEM of Electric Motion Systems***

The market in which Bental operates is highly competitive and is characterized by large customers that are related to the defense and/or aerospace governmental agencies in their countries. Bental's market is also subject to strict import and export regulations and to the budgetary constraints imposed by the governments of such countries. Bental is required to constantly be at the forefront of technological innovations in order to be able to offer advanced innovative products to its customers. Bental's operations require highly qualified and trained engineering, manufacturing, information and quality assurance personnel.

An analysis of the market participants in the global market of electric motion systems shows that it is comprised mainly of large companies that provide standard products and niche companies that provide special customized solutions. With respect to the markets outside Israel, the providers of the systems in which Bental's products are integrated tend to prefer local manufacturers for the purchase of the components and therefore, the penetration of these markets requires product innovation and local presence. In the Israeli market, the competition is mainly against imported components. Bental's major competitors in this segment are: for electric motors - Danaher Motion — Kollmorgen (USA), Artus Pacific Scientific (Europe), Moog Components Group (USA) Aveox (USA), Ametek (USA), ICPE (Europe); For actuators - Kearfott Corp. (USA), Moog Components Group (USA), Pegasus Actuators (Europe), M.T.C Ltd. (Israel); for alternators - Sullivan Products (USA), Prestolite (USA), Sernat (Europe).

#### ***MRO Services for Aviation Components***

The market for MRO services, in which Piedmont operates, is highly competitive. Competition in this market is based on quality, price, and the ability to provide a broad range of services and to perform repairs and overhauls rapidly. Piedmont's primary MRO services competitors are the service divisions of OEMs, the in-house maintenance services of a number of commercial airlines and other independent service providers. For APU and landing gear MRO services Piedmont's major competitors are Standard Aero Group Inc., Aerotech International Inc., Honeywell International, Chase Aerospace, Professional, Messier-Dowty Aerospace (MD), AAR Corp., Hawker Pacific and APRO.

A number of Piedmont’s competitors have inherent competitive advantages. For example, Piedmont competes with the service divisions of large OEMs who in some cases have design authority with respect to their OEM products and are able to derive significant brand recognition from their OEM manufacturing activities. Piedmont also competes with the in-house service divisions of large commercial airlines and there is a strong incentive for an airline to fully utilize the services of its maintenance employees and facilities. Further, Piedmont’s competitors may have additional competitive advantages, such as:

- The ability to adapt more quickly to changes in customer requirements and industry conditions or trends;
- Greater access to capital;
- Stronger relationships with customers and suppliers;
- Better name recognition; and
- Access to superior technology and marketing resources.

**Competitive Strengths**

We believe that TAT’s success can be attributed to several critical factors, including the following:

- Active efforts to preserve its customer base in existing projects, while actively making efforts to broaden and increase its engagements with such clients.
- Conducting marketing activities aiming at penetrating new geographical markets and obtaining new customers, while taking advantage of the unique knowledge and expertise that Gecera, Bental, Limco and Piedmont gained in various areas.
- Entering into additional related operating segments that will enable Gecera, Bental, Limco and Piedmont to fulfill its growth potential.
- Providing its customers with the best value, including competitive prices, by tailoring service packages that combine the design and planning of an OEM component, the manufacture of such component, and the provision of maintenance services.
- Extending MRO capabilities in order to establish a ‘one-stop-shop’ center for comprehensive MRO services for the types of aircraft Limco and Piedmont target.

- Enhancing its engineering capabilities in order to support customer needs related to new projects and in order to certify MRO services that differ from processes previously approved by the FAA or ESAA. This will allow shortening the long and complex approval process, streamlining the design and certification process, and reducing costs.
- Constant search for new technologies and manufacturing techniques in the heat management solutions line.
- Innovations and improvements aiming at enhancing the quality and performance of Gecera's, Bental's, Limco's and Piedmont's existing products.
- Cutting delivery times and reducing costs.
- Entrepreneurship and innovation in the development of new products in an effort to become a market leader and to enter into long term platforms.

#### **Engineering and Manufacturing**

As of December 31, 2012, TAT, had 493 employees engaged in manufacturing, repair, and testing of products and in engineering (out of a total of 575 employees). TAT believes that its engineering staff provides it with the ability to support its customers with innovative and efficient products while maintaining short product development cycles, high quality design and competitive pricing.

Gecera's engineering staff has extensive knowledge and experience related to its heat transfer components. Most of Gecera's product lines have a designated project manager who is an experienced engineer and is in charge of all the activities in his area. The product manager interfaces with the customer, engineering department, manufacturing department and vendors, and is responsible for all aspects of the program including scheduling, adherence to specifications, customer support and reporting.

In general, Gecera has manufacturing capabilities for most of the components of its heat transfer components. Gecera also manufactures the necessary tools, fixtures, test equipment and special jigs required to manufacture, assemble and test these products. Gecera developed proprietary design techniques which assist in the mechanical design and manufacturing of its products. All of Gecera's products are inspected and tested by trained inspectors using highly sophisticated test equipment in accordance with customer requirements.

Bental's engineering staff has extensive knowledge and experience related to its electric motion systems. Most of Bental's product lines have a designated project manager who is an experienced engineer and is in charge of all the activities in his area. The product manager interfaces with the customer, engineering department, manufacturing department and vendors, and is responsible for all aspects of the program including scheduling, adherence to specifications, customer support and reporting.

Limco's engineering department enhances its ability to provide its customers with high-end top quality MRO services, supports the provision of MRO services for new products with commercial potential and supports its OEM activity. Limco's engineering department employs several certified mechanical and aerospace engineers. Limco's multi-disciplinary team of engineers specializes, among others, in heat transfer components and supports all processes of thermal and structural analysis, mechanical and metallurgical research and development for manufacturing design. All of Limco's engineers have direct experience with aerospace component repair and have experience with the process of obtaining supplemental type certificates from the FAA and in obtaining FAA product manufacturing authorizations. Limco utilizes onsite DER at Piedmont facility who is certified by the FAA to approve the repair of engines, mechanical systems and equipment, which enables Limco to respond quickly to its customers' needs. Having a DER available on staff allows Limco to enter the market for a particular type of service more quickly than those of its competitors who do not have immediate access to a DER. Limco works directly with the FAA Aircraft Certification Office in obtaining approvals on projects that are outside its DER's authority.

Piedmont's engineering department enhances its ability to provide its customers with high-end top quality MRO services and supports the provision of MRO services for new products with commercial potential. Piedmont's engineering department employs several certified mechanical and aerospace engineers, including a Designated Engineering Representative, or DER, certified by the FAA. Piedmont's engineers have direct experience with aerospace component repair and have experience with the process of obtaining supplemental type certificates from the FAA and in obtaining FAA product manufacturing authorizations. Piedmont's onsite DER is certified by the FAA to approve the repair of APUs and equipment, which enables Piedmont to respond quickly to its customers' needs. Having a DER on staff allows Piedmont to enter the market for a particular type of service more quickly than its competitors who do not employ a DER. Piedmont works directly with the FAA Aircraft Certification Office in obtaining approvals on projects that are outside its DER's authority.

## **Research and Development**

The technological developments in the markets in which TAT operates, increase the need to constantly examine the use of new materials and technology in an effort to improve both the physical characteristics of the products (size, weight), as well as their performance (optimal heat transfer, higher reliability and increased lifespan). TAT also develops new products and enhanced functionalities to its existing products based on customer demands and by the competitive environment and market potential. TAT invests resources to attain such technological and product improvements in cooperation with its customers.

## **Source and Availability of Raw Materials and Spare Parts**

Gedera, Bental, Limco and Piedmont acquire most of the components for the manufacture of their products from a limited number of suppliers and subcontractors, most of whom are located in Israel and the United States. Certain of these suppliers are currently the sole source of one or more components upon which Gedera, Bental, Limco and Piedmont are dependent. Since many of Gedera's, Bental's, Limco's and Piedmont's purchases require long lead-times, a delay in the supply of an item can significantly delay the delivery of a product. Generally, Gedera, Bental, Limco and Piedmont have not experienced difficulty in obtaining timely deliveries of necessary components. The raw materials used in Gedera's, Bental's, Limco's and Piedmont's manufacturing programs are generally readily available metals and alloys. Gedera, Bental, Limco and Piedmont have not had any difficulty in obtaining such materials in the past and if they are unable to obtain these components when needed, Gedera, Bental, Limco and Piedmont would experience delays in manufacturing their products and their financial results could be adversely affected.

Gedera, Bental, Limco and Piedmont select their suppliers primarily based on their ability to ensure that their parts are serviceable and traceable to OEM-approved sources, their delivery performance and their ability to help reduce their total cost of procuring those parts. For quality control, cost and efficiency reasons, Gedera, Bental, Limco and Piedmont generally purchase supplies only from vendors with whom they have ongoing relationships or who their customers have previously approved.

Authorizations from OEMs often require that TAT purchases component parts that are needed for its MRO services from the OEM or its designated distributors. Gedera and Piedmont have separate agreements with Honeywell under which Honeywell has agreed to sell Gedera and Piedmont certain parts at a discount for a period of five years, ending August 28, 2017 and May 31, 2014, respectively.

When deemed essential, Gedera, Bental, Limco and Piedmont have been and are investing efforts in order to qualify second sources or have identified alternate sources for many of its parts needs.

#### **Israeli Export Policy**

Exports of military related products are subject to the military export policy of the State of Israel. Current Israeli Government policy encourages exports to approved customers, provided that such exports do not run counter to Israeli policy or national security considerations. Gedera and Bental must obtain a permit to initiate a sales proposal and ultimately an export license for the transaction required. Gedera and Bental may not be able to obtain export permits or licenses in the future. In addition, governmental policy with respect to military exports may be altered. However, to date Gedera and Bental have not encountered any significant difficulties in obtaining necessary permits or licenses for sale of their products.

#### **Proprietary Rights**

At the present time Gedera, Bental, Limco and Piedmont do not own any patents. Gedera, Bental, Limco and Piedmont rely on laws protecting trade secrets, and consider such items proprietary, but TAT believes that Gedera, Bental, Limco and Piedmont's success depends less on the ownership of such proprietary rights than on their innovative skills, technical competences marketing and engineering abilities. Gedera, Bental, Limco and Piedmont have no material registered trademarks.

#### **B. Government Regulations**

##### **Aerospace and Safety Regulations**

The commercial aerospace industry is highly regulated by the FAA in the United States, EASA in Europe, the Civil Aviation Authority in England and other governmental authorities elsewhere in the world, while the military aerospace industry is governed by military quality specifications established by the U.S. Department of Defense for the manufacturing and repair industries and ISO-9000. TAT is required to be certified by one or more of these entities and, in some cases, by individual OEMs. TAT must also satisfy the requirements of its customers, including OEMs and airlines that are subject to FAA regulations and to evolving industry standards, and provide these customers with products that comply with the government regulations applicable to commercial flight operations. TAT believes it currently satisfies or exceeds these FAA maintenance standards in its repair and overhaul activities. Each of its repair stations is approved by the FAA. TAT also believes it currently satisfies all industry standards in its facilities.

TAT's operations are also subject to a variety of worker and community safety laws including the Occupational Safety and Health Act of 1970, known as OSHA, which mandates general requirements for safe workplaces for all US employees. In addition, OSHA provides special procedures and measures for the handling of certain hazardous and toxic substances. TAT believes that its operations are in material compliance with OSHA's health and safety requirements.

TAT believes that it is in material compliance with US, European and other governmental regulations affecting the aerospace and defense industry.

#### **Israeli Regulations**

TAT's operations in Israel are subject to supervision by the Ministry of Defense and Civil Aviation Administration. Gedera and Bental are certified by the Israeli Air Force and the Ministry of Defense for both manufacturing and maintenance. Gedera is also licensed as a repair station for certain components by the Israeli Civil Aviation Administration. In addition, Gedera's and Bental's export of certain products and/or know-how is subject to approval by the Department for the Control of the Defense Export of the Israeli Ministry of Defense, known as API. Permits from API must be obtained for the initiation of sales proposals with regard to such exports, as well as for the actual export of such products.

#### **Environmental Matters**

TAT's operations are subject to a number of federal, state and local environmental laws in the United States and Israel, and to regulation by government agencies, including the U.S. Environmental Protection Agency. Among other matters, these regulatory authorities impose requirements that regulate the emission, discharge, generation, management, transportation and disposal of pollutants and hazardous substances. These authorities may require TAT to initiate actions to remediate the effects of hazardous substances which may be or have been released into the environment, and require TAT to obtain and maintain permits in connection with TAT's operations. This extensive regulatory framework imposes significant compliance burdens and risks.

Although TAT seeks to maintain its operations and facilities in compliance with applicable environmental laws, there can be no assurance that TAT has no violations, or that change in such laws, regulations or interpretations of such laws or in the nature of TAT's operations will not require TAT to make significant additional expenditures to ensure compliance in the future. Currently, TAT does not believe that it will have to make material capital expenditures for its operations to comply with environmental laws or regulations, or to incur material costs for environmental remediation during the 2013 fiscal year.

TAT has received no material third party environmental claims relating to its facilities, and TAT believes that it has all material licenses and certifications that are required in the jurisdictions in which it operates.

**C. Property, Plants and Equipment**

The Gedera facility is located in Park Re'em near Gedera. The Park Re'em's location houses TAT's executive offices, Gedera's research and development and manufacturing operations and includes approximately 344,000 square feet facility. The land of this facility is leased by TAT Industries from the Israel Land Authority, or ILA pursuant to a lease that expires in 2016 with respect to one plot (237,000 square feet) and 2020 with respect the other plot (107,000 square feet). The leases term may be extended for a subsequent period of up to 49 years, subject to payment to be calculated according to the ILA's rules. Approximately 43,000 square feet of the facility was sub-leased to TAT in 1991 until 2020 for rental fees which were paid in advance for the whole sub-lease period. TAT sub-leases the remaining 301,000 square feet of the facility from TAT Industries pursuant to an agreement TAT entered into in connection with the purchase of the operations relating to the manufacture of aviation accessories of TAT Industries in February 2000. The agreement is for a period of 24 years and 11 months and the rental fee is subject to revaluation every fifth year. From 2000 to 2004, TAT paid TAT Industries annual rental fees of approximately \$300,000 per year, with an additional incremental payment of 2% per year. In 2005 the rental fee was reviewed by a real estate appraiser, and as a result was increased to \$310,000 per year with an additional incremental payment of 2% per year. In 2010 the rental fee was reviewed again by a real estate appraiser, and as a result was increased to \$400,000 per year with an additional incremental payment of 2% per year. Total rental payment TAT paid to TAT Industries during 2012 and 2011 were \$416,000 and \$408,000, respectively. See also Item 7.B "Major Shareholders and Related Party Transactions – Related Party Transactions – Management and Services Agreement with TAT Industries."



The operations of Bental are conducted in Kibbutz Marom-Golan. The Marom-Golan facility is located on a 54,000 square feet land, that houses Bental's offices, research and development and manufacturing operations that include all together approximately 18,500 square feet. The facility is leased from Bental Investments Cooperative Agricultures Society Ltd. and from Kibbutz Marom-Golan pursuant to a lease that expires in December 2013 (for a 14,500 square feet plot) and June 2027 (for a 4,000 square feet plot), respectively. The lease agreement may be extended for subsequent periods upon terms. Total rental payment Bental paid in 2012 and 2011 was \$51,000 and \$53,000, respectively.

Limco owns and operates a 55,000 square feet manufacturing plant in Tulsa, Oklahoma which has historically supported all its business, including its aftermarket heat transfer component repair station. This facility also has housed Limco's administration, engineering, quality control and support services. Limco also leases an additional 9,000 square feet repair station adjacent to its Tulsa manufacturing plant which has supported its heat transfer component and pneumatic ducting MRO services.

Piedmont leases approximately 56,000 square feet space for its facility in Kernersville, North Carolina to support its aftermarket APU, Landing Gear and related component repair station. In 2012 and 2011, the annual rental expense for this property was \$78,000 and \$70,000 , respectively for each one of these years. The lease, expires on October 31, 2016. Piedmont also leases approximately 32,000 square feet for its facility in Winston Salem, North Carolina to support its plating and machining shop as well as related component repairs. In 2012 and 2011, the annual rental expense for this property was \$48,000 for each one of these years. The lease expires on December 31, 2017.

**Item 4A. Unresolved Staff Comments**

Not applicable.

**Item 5. Operating and Financial Review and Prospects**

**Operating Results**

*The following discussion of our results of operations should be read together with our consolidated financial statements and the related notes, which appear elsewhere in this annual report. The following discussion contains forward-looking statements that reflect our current plans, estimates and beliefs and involve risks and uncertainties. Our actual results may differ materially from those discussed in the forward-looking statements. Factors that could cause or contribute to such differences include those discussed below and elsewhere in this annual report.*

**Overview**

TAT provides a variety of services and products to the aerospace and defense industries under four segments: (i) OEM of Heat Management Solutions; (ii) OEM of Electric Motion Systems; (iii) Heat Transfer Services and Products; and (iv) MRO services for Aviation Components.

TAT's activities in the field of OEM of Heat Management Solutions primarily relate to its Gedera facility and include the (i) design, development, manufacture and sale of a broad range of heat transfer products (such as heat exchangers, pre-coolers and oil/fuel hydraulic coolers) used in mechanical and electronic systems on-board commercial, military and business aircraft; and (ii) manufacture and sale of environmental control and cooling systems and (iii) a variety of other electronic and mechanical aircraft accessories and systems such as pumps, valves, power systems and turbines. It also includes, to a lesser extent, the maintenance services for heat transfer products and flow control accessories.

TAT's activities in the field of OEM of Electric Motion Systems primarily relate to its subsidiary, Bental, and include the design, development, manufacture and sale of a broad range of electrical motor applications for airborne and ground systems.

TAT's activities in the field of Heat Transfer Services and Products primarily relate to its subsidiary, Limco, and include the maintenance, repair and overhaul of heat transfer products and other aircraft component. Limco operates an FAA certified repair station, which provides aircraft component MRO services for airlines, air cargo carriers, maintenance service centers and the military. In addition to its MRO services, Limco also manufactures heat transfer products used in commercial, regional, business and military aircraft.

TAT's MRO services for Aviation Components primarily relate to its subsidiary, Piedmont, and include the maintenance, repair and overhaul of APUs, and landing gear. Piedmont operates an FAA certified repair station, which provides aircraft component MRO services for airlines, air cargo carriers, maintenance service centers and the military.

TAT is reliant on the commercial and military aviation and defense industries. Any downturn in these industries could decrease demand for its services and products and negatively impact its financial condition. The commercial airline industry is cyclical and has historically been subject to fluctuations due to general economic and political conditions, such as fuel and labor costs, price competition, downturns in the global economy and national and international events.

TAT's revenues from OEM operations generally have higher gross margins than from MRO services. Respectively, the manufacture of OEM products require higher level of expertise, associated labor and initial investments than does the provision of MRO services.

TAT's cost of revenues for OEM operations and MRO services consists of component and material costs, direct labor costs, shipping expenses, royalties, overhead related to manufacturing and depreciation of manufacturing equipment. TAT's gross margin is affected by the proportion of its revenues generated from each of its operational segments.

The principal factors that affect the operating income of TAT's four segments in addition to their gross profit, is the amount TAT expends for selling and marketing expenses and general and administrative expenses. While TAT plans to tightly monitor and save on its operating expenses, TAT believes that these operating expenses may increase in the future in accordance with its plans to grow the business of these segments.

TAT's research and development expenses are related to new products and technologies or significant improvement in existing products and technologies, primarily within the OEM operations in Israel and in the Heat Transfer Services and Products operating segment in the U.S.

TAT's selling and marketing expenses during the past year were similar to previous year. While TAT plans to tightly monitor and save on its operating expenses, TAT believes that its selling and marketing expenses may increase in the future in accordance with its plans to grow the business of these segments.

TAT's general and administrative expenses have increased during 2012, following a decrease in 2011 compared to the previous year. The increase in 2012 was primarily as result of a provision recorded for a doubtful debt and a decrease in FavS participation in certain operating expenses during year 2012 in the MRO services for aviation components operating segment. The decrease in 2011 was primarily as result of \$1.8 million non-recurring expense recorded in the fourth quarter of 2010 related to the Parts services operations and the Propellers MRO operations contributed to FavS. While TAT plans to tightly monitor and save on its operating expenses, TAT believes that its general and administration expenses may increase in the future in accordance with its plans to grow the business of these segments.

In July 2005, Limco acquired Piedmont for approximately \$20.2 million, which included \$5.3 million in cash and the assumption of approximately \$8.7 million of bank indebtedness and \$5.6 million of other liabilities of Piedmont. The acquisition was accounted for using the purchase method of accounting as determined in the relevant accounting standards and accordingly, the purchase price was allocated to the assets acquired and the liabilities assumed based on the estimated fair value at the date of acquisition.

In July 2007, Limco completed an initial public offering of its shares of Common stock. In connection with the initial public offering, Limco sold an aggregate amount of 4,205,000 shares of its Common stock (including over allotment option shares) and TAT sold an aggregate amount of 855,000 shares of Limco's Common stock held by TAT (including over allotment option shares), at a price to the public of \$11.00 per share. Net proceeds to Limco from the offering were approximately \$41.2 million and net proceeds to TAT from the offering were approximately \$8.7 million. As a result, TAT recognized a net capital gain of approximately \$26.4 million net of taxes of \$1.2 for the year ended December 31, 2007.

In July 2009, TAT acquired all of the publicly held shares of Limco (approximately 32% of Limco's total shares). Under the terms of the merger agreement, Limco's stockholders received one half of an Ordinary share of TAT for each share of Limco Common stock they own following which they held approximately 27.8% of the then share capital of TAT. As a result of such merger, Limco again became a wholly-owned subsidiary of TAT.

On December 4, 2009, TAT's indirect subsidiary, Piedmont, acquired 288,334 shares of Class B Common stock of First Aviation Services Inc., or FAvS, representing 37% of FAvS's then share capital (total number of shares acquired is adjusted to reflect of a 1 for 20 reverse stock split) and \$750,000 of FAvS' Preferred Shares (entitling Piedmont to cash dividends at an annual rate of 12% payable quarterly or at the discretion of FAvS to PIK dividends payable in additional Preferred Shares at an annual rate of 15%). In consideration for such shares, Piedmont transferred to FAvS its propellers and parts businesses and guaranteed for a period of up to two years up to \$7 million of the bank debt incurred by FAvS to fund the transaction described in the next paragraph. FAvS is a provider of maintenance and repair services for various wheels, brakes and starter/generators.

On December 4, 2009 and as part of the above mentioned transaction, FAvS also acquired all the assets and liabilities of Aerospace Turbine Rotables ("AcTR"). AcTR specializes in renovation and repair of landing gear, safety equipment and hydraulic and electrical components for corporate, regional and military aircraft.

FAvS' shares are quoted over the counter (OTC) at the NASDAQ stock market. FAvS' share value as of the closing date (December 4, 2009) and as of December 31, 2009, 2010, 2011 and 2012 was \$17.8, \$15.0, \$12.4, \$5.45, and \$7.00, respectively (share value adjusted as result of a 1 for 20 reverse stock split). TAT believes that the share value does not reflect the fair value of FAvS shares, because the extremely low trading volume in FAvS' shares does not reflect an active market. Therefore the fair value of FAvS was based on an appraisal performed by management, which included a number of factors, including the assistance of independent appraisers. According to the appraisal, FAvS' fair value amounted to \$22.549 million as of November 30, 2009. As a result of the sale of Piedmont's propellers and spare parts businesses, TAT recorded a capital gain in the amount of \$4.4 million in its statement of income.

During the year ended December 31, 2010, TAT recorded write down of inventory in the amount of \$3.5 million attributable to inventory of the MRO segment. In 2010 management recognized that the aviation industry is not recovering quickly enough, as it previously estimated, from year 2009 recession and that the industry does not pick up growth rates as were in prior years. As a result management estimated a decline in future forecasted sales levels and profitability margins resulting from the said anticipated weakness in the global aviation industry in general and to a greater extent in the U.S., where the MRO segment is operated under Limco and Piedmont.

During the year ended December 31, 2010, the Company performed its annual impairment test of goodwill. Based on the results of this test, the Company encountered adverse changes in the business climate including a weak U.S. and global economy which resulted in a reduction in demand for the MRO services. In year 2010 management also recognized that the aviation industry is not recovering quickly enough, as it previously estimated, from year 2009 recession and that the industry does not pick up growth rates as were in prior years. As a result management estimated a decline in future forecasted sales levels and profitability margins resulting from the said anticipated weakness in the global aviation and revised its future cash flow expectations, which lowered the fair value estimates of a certain reporting unit. The Company determined under the second step of its annual test that the fair value of goodwill at its MRO reporting unit was less than the carrying value for this reporting unit. The Company recorded a \$4.2 million impairment charge in the third quarter of 2010 to reflect the implied fair value of goodwill for the MRO reporting unit

During 2010, the Company also reviewed its other intangible assets for impairment, in accordance with ASC 360. The Company estimated the fair value of its other intangible assets using a discounted cash flow analysis and compared those values to the carrying value of the assets. The Company concluded, based on this comparison, that customer relations were impaired at its MRO reporting unit. The Company recorded a \$0.48 million impairment charge during the year ended December 31, 2010 to reflect the fair value of those customer relations for the MRO reporting unit.

As of December 31, 2010, TAT recognized an impairment charge of \$1.8 million of its 37% interest in FAvS, which was performed with the assistance of an independent appraisal.

During the year ended December 31, 2011, the Company recorded a write down of inventory in the amount of \$2.5 million under cost of revenues, attributable to inventory of the MRO for Aviation Components operating segment. The write down was due to management's estimate of the continued decline in future forecasted sales levels and profitability margins in certain product lines in this operating segment resulting from the weakness in these areas of business.

In addition, although revenues in the MRO for Aviation Components operating segment have increased in 2011 compared to 2010, profit margins were lower than anticipated. Accordingly, the Company reviewed the MRO for Aviation Components' long lived assets for impairment by estimating the fair value of this segment's operations and the fair value of its specific long lived assets, and comparing those values to the carrying value of the assets.

The Company concluded, based on this valuation, that certain fixed assets and intangible asset amounting to \$1.9 million and \$1.1 million, respectively at its MRO for Aviation Components operating segment were impaired.

Due to management estimates of a continuing decline in sales levels in the OEM of Electric Motion Systems operating segment, resulting from the weakness in the Israeli defense market, the Company reviewed indications for impairment of certain identifiable assets in this segment. Accordingly, the Company reviewed these assets for impairment by estimating their fair value based on their net selling price and comparing those values to the carrying value of the assets. As a result the Company concluded that the intangible asset 'Customer Relations' at its OEM of Electric Motion Systems operating segment in the amount of \$0.3 million was impaired.

Accordingly, the Company recorded a \$3.3 million impairment charges during the quarter ended September 30, 2011 to reflect the fair value of the long lived assets mention above.

During the second quarter ended June 30, 2012, management believed that there were indicators of impairment of goodwill in its OEM of Electric Motion System reporting unit, primarily due to a decline in future forecasted sales levels and profitability margins resulting from the continued weakness in the defense industry. Accordingly, the Company performed an impairment test of goodwill, as of June 30, 2012, for this reporting unit, with the assistance of a third party valuation. Based on the results of this test, the Company determined that the entire balance of goodwill included in this reporting unit was impaired and recorded an impairment charge of \$1.0 million

In addition, in June 2012, FAvS entered into a transaction with its controlling stockholder, Mr. Hollander, pursuant to which FAvS borrowed \$3 million from Mr. Hollander, secured by a third lien on the assets of FAvS. The loan bears interest at 10% and in addition Mr. Hollander was issued warrants to purchase shares of Class A Common Stock of FAvS, representing 15% of FAvS post-exercise shareholders' equity, at an exercise price of \$7.00 per share. Pursuant to the terms and conditions of the transaction, management believed that there were indicators of impairment with respect to TAT's investment in FAvS. Accordingly, the Company performed an impairment test of its investment in FAvS, with the assistance of a third party valuation. Based on the results of this test the Company determined that its investment in FAvS was impaired by \$3.3 million. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels which related to the business of API, one of FAvS subsidiaries, and approximates TAT's share in the loss resulting from the API Transaction discussed below.

On March 18, 2013 FAvS sold 97% of the stock of API for a total purchase price of \$16.5 million, out of which \$15.9 million was used to repay debt (the "API Transaction"). The sale resulted in FAvS retaining a 3% equity interest in the API business. The API transaction resulted in a loss from discontinued operations and write-down of the API business of \$11.5 million which is included in the FAvS loss for the year ended December 31, 2012. Simultaneously with the transaction FAvS paid-off its Term Loan in the amount of \$4 million thereby terminating the guaranty and releasing the Letter of Credit provided by TAT to secure such guaranty. Accordingly the restricted deposit associated with the above Letter of Credit, was released as well.

## Sources of Revenues

TAT, directly and through its subsidiaries, provides a variety of services and products to the commercial and military aerospace and defense industries, such as the manufacture, maintenance and repair of a broad range of heat transfer components (such as heat exchangers, pre-coolers and oil/fuel hydraulic coolers) used in mechanical and electronic systems on-board commercial, military and business aircraft; other environmental control and cooling systems a variety of other electronic and mechanical aircraft accessories and a wide range of electric motion systems.

TAT specializes in the repair and overhaul of heat transfer products, APUs, landing gear and pneumatic ducting. TAT is a well recognized repair center for heat transfer products of Hamilton Sundstrand, a leading provider of aerospace products, to provide MRO services for all of its air-to-air heat transfer products, and an authorized repair center by Honeywell, a leading manufacturer of aerospace products and aerospace services provider, to provide MRO services for several of their APU models. TAT's repair stations are certified by the FAA and the EASA as well as by the Civil Aviation Administration of Vietnam (CAAV) and Thailand (Thai).

The following table reflects the geographic breakdown of TAT's revenues for each of the three years ended December 31, 2012:

	Years Ended December 31,					
	2012		2011		2010	
	Revenues in Thousands	% of Total Revenues	Revenues in Thousands	% of Total Revenues	Revenues in Thousands	% of Total Revenues
<b>Sale of products</b>						
North America	\$ 17,068	34.7%	\$ 20,988	29.6%	\$ 7,531	19.3%
Europe	9,828	19.9%	6,048	16.1%	5,567	14.3%
Israel	18,223	37.0%	18,945	50.3%	23,223	59.6%
Other	4,151	8.4%	1,527	4.0%	2,633	6.8%
Total	\$ 49,270	100.00%	\$ 47,508	100.00%	\$ 38,954	100.00%



	Years Ended December 31,					
	2012		2011		2010	
	Revenues in Thousands	% of Total Revenues	Revenues in Thousands	% of Total Revenues	Revenues in Thousands	% of Total Revenues
<b>Services</b>						
North America	\$ 28,120	72.8%	\$ 26,403	75.9%	\$ 25,607	62.8%
Europe	5,105	13.2%	8,253	17.3%	8,573	21.0%
Israel	288	0.7%	384	0.8%	410	1.0%
Other	5,139	13.3%	2,849	6.0%	6,211	15.2%
Total	\$ 38,652	100.00%	\$ 37,889	100.00%	\$ 40,801	100.00%

TAT's revenues from its four operational segments for the three years ended December 31, 2012 were as follows:

	Year Ended December 31,					
	2012		2011		2010	
	Revenues in Thousands	% of Total Revenues	Revenues in Thousands	% of Total Revenues	Revenues in Thousands	% of Total Revenues
<b>Revenues</b>						
OEM of Heat Management Solutions	\$ 31,032	35.3%	\$ 30,020	35.2%	\$ 29,651	37.2%
Heat Transfer Services and Products *	27,709	31.5%	27,603	32.3%	24,468	30.7%
MRO services for Aviation Components *	22,442	25.5%	20,146	23.6%	16,333	20.4%
OEM of Electric Motion Systems	10,007	11.4%	11,658	13.6%	13,046	16.4%
Eliminations	(3,268)	(3.7)%	(4,030)	(4.7)%	(3,743)	(4.7)%
Total revenues	\$ 87,922	100.00%	\$ 85,397	100.00%	\$ 79,755	100.00%

\* As of January 1, 2011, TAT began reporting its operations based on four operating segments, after dividing its MRO Services operating segment into two separate segments: Heat Transfer Services and Products and MRO services for Aviation Components. Accordingly, the revenues and costs reported for the twelve month period ended December 31, 2010 for MRO Services operating segment were divided between these two new operating segments. Additionally, the operating segment name of 'OEM of Heat Transfer Products' was changed to 'OEM of Heat Management Solutions'.

## Costs and Expenses

**Cost of revenues** TAT's cost of revenues for OEM operations and MRO services consist of component and material costs, direct labor costs, royalties, shipping expenses, overhead related to manufacturing and depreciation of manufacturing equipment. Cost of revenues for 2011 also included non-recurring expenses associated with a write down of inventory and impairment charges of long lived assets.

TAT's gross margin was affected by the proportion of TAT's revenues generated from OEM operations and MRO services in each of the reported years, as well as by non-recurring expenses associated with a write down of inventory and impairment charges of long lived assets recorded in 2011.

**Research and development expenses, net.** Research and development expenses, net are related to new products and technologies or to a significant improvement of products and technologies, net of grants and participations received.

**Selling and marketing expenses.** Selling and marketing expenses consist primarily of commission payments, compensation and related expenses of TAT's sales teams, attendance at trade shows, advertising expenses and related costs for facilities and equipment.

**General and administrative expenses.** General and administrative expenses consist of compensation and related expenses for executive, finance and administrative personnel, professional fees, other general corporate expenses and related costs for facilities and equipment.

**Impairment of goodwill and intangible assets.** During the second quarter ended June 30, 2012, management believed that there were indicators of impairment of goodwill in its OEM of Electric Motion System reporting unit, primarily due to a decline in future forecasted sales levels and profitability margins resulting from the continued weakness in the defense industry. Accordingly, the Company performed an impairment test of goodwill, as of June 30, 2012, for this reporting unit, with the assistance of a third party valuation. Based on the results of this test, the Company determined that the entire balance of goodwill included in this reporting unit was impaired and recorded an impairment charge of \$1.0 million. During the quarter ended September 30, 2010, TAT performed its annual impairment test of goodwill. Based on the results of this test TAT recorded goodwill impairment charge for the goodwill included in the MRO Services segment. In addition, the Company recorded an impairment charge related to Intangible assets 'Customer Relations' in the MRO Services segment.

**Financial income (expense), net.** Financial income (expense), net consists of income and interest expense. Interest expense relates to the interest paid to banks and changes in the rate of the NIS against the U.S. dollar.

**Other income (expense).** Other income (expense) results from capital gain on sale of property and equipment and from other-than-temporary impairment loss on auction rate securities recorded in 2010.

**Tax expense (income).** Tax expense consists of Israeli, U.S. federal, state and local taxes on the income of TAT's business and changes in deferred tax assets (liabilities).

**Impairment of share in associated company.** During the quarter ended June 30, 2012 TAT recognized an impairment with respect to its approximately 30% interest in FAvS', which was based on an independent appraisal. During the quarter ended December 31, 2010, TAT performed an impairment testing of its investment in FAvS, due to certain indicators suggesting such test. Based on the results of this test the Company determined that its investment in FAvS was impaired due to a decline in FAvS' profitability margins and future forecasted sales levels.

#### **Impact of Critical Accounting Policies**

TAT's consolidated financial statements are prepared in accordance with U.S. GAAP. These accounting principles require management to make certain estimates, judgments and assumptions based upon information available at the time that they are made, historical experience and various other factors that are believed to be reasonable under the circumstances. These estimates, judgments and assumptions can affect the reported amounts of assets and liabilities as of the date of the financial statements, as well as the reported amounts of revenues and expenses during the periods presented. While all the accounting policies impact the financial statements, certain policies may be viewed to be critical. These policies are those that are both most important to the portrayal of TAT's financial condition and results of operations and require management's most difficult, subjective and complex judgments and estimates. Actual results could differ from those estimates.

In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles in the United States and does not require management's judgment in its application. There are also areas in which management's judgment in selecting among available alternatives would not produce a materially different result. Management has reviewed these critical accounting policies and related disclosures with TAT's Audit Committee.

TAT's management believes the significant accounting policies which affect management's more significant judgments and estimates used in the preparation of TAT's consolidated financial statements and which are the most critical to aid in fully understanding and evaluating the reported financial results include the following:

- Revenue recognition
- Inventory valuation
- Goodwill, Intangible assets and Long-lived assets
- Income taxes
- Doubtful debts
- Fair value estimation of TAT's investment in FavS, performed by management with the assistance of a third party valuation.

#### **Segments**

TAT operates under four segments: (i) Original Equipment Manufacturing or "OEM" of Heat Management Solutions (ii) OEM of Electric Motion Systems (iii) Heat Transfer Services and Products, and (iv) Maintenance, Repair and Overhaul or "MRO" services for Aviation Components.

Until December 31, 2010, TAT operated under three segments. Commencing January 1, 2011, TAT began reporting its operations based on four operating segments, after dividing its MRO Services operating segment into two separate segments: Heat Transfer Services and Products; and MRO services for Aviation Components. Additionally, the operating segment name of 'OEM of Heat Transfer Products' was changed to 'OEM of Heat Management Solutions'.

TAT's activities in the area of OEM of Heat Management Solutions primarily relate to its Gedera facility and include (i) the design, development, manufacture and sale of a broad range of heat transfer products (such as heat exchangers, pre-coolers and oil/fuel hydraulic coolers) used in mechanical and electronic systems on-board commercial, military and business aircraft; (ii) the manufacture and sale of environmental control and cooling systems and (iii) a variety of other electronic and mechanical aircraft accessories and systems such as pumps, valves, power systems and turbines. It also includes, to a lesser extent, the maintenance services for heat transfer products and flow control accessories.

TAT's activities in the area of OEM of Electric Motion Systems primarily relate to its subsidiary, Bental, and include the design, development, manufacture and sale of a broad range of electrical motor applications for airborne and ground systems.

TAT's activities in the field of Heat Transfer Services and Products primarily relate to its subsidiary, Limco, and include the maintenance, repair and overhaul of heat transfer equipment and in a lesser extent, the manufacturing of certain heat transfer products. TAT's Limco subsidiary operates an FAA certified repair station, which provides heat transfer MRO services and products for airlines, air cargo carriers, maintenance service centers and the military.

TAT's activities in the field of MRO services for Aviation Components primarily relate to its subsidiary, Piedmont, and includes the maintenance, repair and overhaul of APUs, landing gear and other aircraft components. TAT's Piedmont subsidiary operates an FAA certified repair station, which provides aircraft component MRO services for airlines, air cargo carriers, maintenance service centers and the military.

#### **Revenue Recognition**

TAT generates its revenues from the sale of products and systems (the OEM segments) and from providing MRO Services (remanufacture, repair and overhaul services and long-term service contracts).

Revenues from the sale of products and services are recognized in accordance with ASC 605-10-S99 when persuasive evidence of an arrangement exists, delivery of the product has occurred, provided the collection of the resulting receivable is probable, the price is fixed or determinable and no significant obligation exists. TAT does not grant a right of return.

Revenues from product sales are recognized when product is shipped to the customer and title passes to the customer.

Revenues from multi-year, fixed price contracts for OEM customers are recognized when a product is shipped (and title passes) to the customer. Management provides for losses, if expected for the remaining portion of such contracts. For the years ended December 31, 2012, 2011 and 2010, no losses have been recognized for such fixed price contracts.

Revenues from MRO services are recognized as services are performed, at the time when the customer-owned material is shipped back to the customer.

Revenue from maintenance contracts are accounted according to ASC 605-10-S99. Accordingly, revenues from maintenance contracts are recognized over the contract period in proportion to the costs expected to be incurred in performing services under the contract. TAT estimates the costs that are expected to be incurred based on its experience with the aggregate costs incurred and to be incurred on contracts of this nature. The cost incurred related to the maintenance contracts are not incurred on a straight-line basis, as the timing to provide the maintenance services is dependent on when parts under these contracts require maintenance, therefore TAT accrues revenue based on anticipated costs per contract as costs are incurred. These revenues are then compared to actual results and adjusted to either deferred revenue for results greater than historical estimates or expensed in those cases of performances less than historical estimates. These accounts are reviewed monthly and adjusted as needed based on cost structures.

Revenues from royalties from sales of products developed with TAT's intellectual property, technology and technical assistance are recognized when the related sales are made.

#### **Valuation of Goodwill, Intangible Assets and Long-Lived Assets**

Goodwill represents the excess of the purchase price over the fair value of identifiable net assets acquired in business combinations.

In conjunction with acquisitions of assets, we allocate the purchase price based upon the relative fair values of the assets acquired and liabilities assumed. In connection with a business combination, amounts assigned to intangible assets are based upon fair value. We regularly assess whether indefinite life intangibles and goodwill have been impaired and will adjust the carrying values of these assets whenever events or changes in circumstances indicate that some or all of the carrying value of the assets may not be recoverable. Our judgments regarding the existence of impairment indicators are based on legal factors, market conditions and operating performances of our businesses and products. Future events could cause us to conclude that impairment indicators exist and that the carrying values of our intangible assets or goodwill are impaired. Any resulting impairment loss could have a material adverse impact on our financial position and results of operations.

We evaluate the recoverability and measure the possible impairment of goodwill. The impairment test is a two-step process that begins with the estimation of the fair value of the reporting unit. The first step screens for potential impairment, and the second step measures the amount of the impairment, if any. Our estimate of fair value considers publicly available information regarding the market capitalization of the company, as well as (1) publicly available information regarding comparable publicly traded companies in the aviation industry, (2) the financial projections and future prospects of our business, including its growth opportunities and likely operational improvements, and (3) comparable sales prices, if available. As part of the first step to assess potential impairment, we compare, on an operating unit level, our estimate of fair value for such operating unit to the book value of the operating unit. If the book value of any of the operating units is greater than the estimate of its fair value, we would then proceed to the second step to measure the impairment, if any. The second step measures the amount of impairment by comparing the implied fair value of goodwill with its carrying value. Such implied fair value is determined by allocating the fair value of the operating unit to all of the assets and liabilities of that unit as if the operating unit had been acquired in a business combination and the fair value of the reporting unit was the purchase price paid to acquire the operating unit. The excess of the fair value of the operating unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. If the carrying amount of the operating unit's goodwill is greater than its implied fair value, an impairment loss will be recognized in the amount of the excess.

We have determined September 30 of each year as the date of the annual impairment test for goodwill and other indefinite life intangible assets.

During the second quarter ended June 30, 2012, management believed that there were indicators of impairment of goodwill in its OEM of Electric Motion System reporting unit, primarily due to a decline in future forecasted sales levels and profitability margins resulting from the continued weakness in the defense industry. Accordingly, the Company performed an impairment test of goodwill, as of June 30, 2012, for this reporting unit, with the assistance of a third party valuation. Based on the results of this test, the Company determined that the entire balance of goodwill included in this reporting unit was impaired and recorded an impairment charge of \$1.0 million.

During the quarter ended September 30, 2011, although revenues in the MRO for Aviation Components operating segment have increased in 2011 compared to 2010, profit margins for this operating segment were lower than anticipated. Accordingly, the Company reviewed certain of its long lived assets for impairment by estimating their fair value based on their net selling price and comparing those values to the carrying value of the assets. The Company concluded, based on this valuation, that certain fixed assets and intangible assets amounting to \$1.9 million and \$1.1 million, respectively at its MRO for Aviation Components operating segment were impaired.

Due to management estimates of a continuing decline in sales levels in the OEM of Electric Motion Systems operating segment resulting from the weakness in the Israeli defense market, the Company reviewed indications for impairment of certain identifiable assets in this segment. Accordingly, the Company reviewed these assets for impairment by estimating their fair value based on their net selling price and comparing those values to the carrying value of the assets. As a result the Company concluded that the intangible asset 'Customer Relations' at its OEM of Electric Motion Systems operating segment in the amount of \$0.3 million was impaired.

Accordingly, the Company recorded a \$3.3 million impairment charges during the quarter ended September 30, 2011 to reflect the fair value of the long lived assets mentioned above.

As of December 31, 2012, there are no goodwill or other remaining identifiable intangible assets included on the balance sheet.

#### **Investment in Company Accounted for using the Equity Method**

Investment in which the Company exercises significant influence, which is not considered subsidiary ("associate"), is accounted for the equity method, whereby the Company recognizes its proportionate share of the company's net income or loss after the date of investment. The Company reviews this investment for impairment whenever events indicate the carrying amount may not be recoverable.



On December 4, 2009, the Company, through its subsidiary Piedmont, signed an investment agreement with FAvS. According to the agreement Piedmont was issued 288,334 shares of Class B Common stock of First Aviation Services Inc., or FAvS, represented 37% of FAvS's then share capital (total number of shares acquired is adjusted as result of a 1 for 20 reverse stock split) and \$ 750 thousand of FAvS Preferred shares (entitlement to cash dividends at an annual rate of 12% payable quarterly or to additional Preferred shares at an annual rate of 15%) in return for Piedmont's propeller and parts businesses. The net assets value as of December 4, 2009, of the propeller and parts businesses was \$4,325 thousand, the fair value of FAvS' Ordinary shares and Preferred shares was \$8,931 thousand (including businesses' acquisition expenses of \$200 thousand). Accordingly, the Company recorded \$4.4 million of capital gain.

As of December 31, 2010, the Company recorded a \$4.5 million loss from its share in the loss and impairment of its 37% interest in FAvS.

In June, 2012, FAvS entered into a transaction with its controlling stockholder, Mr. Hollander, pursuant to which FAvS borrowed \$3 million from Mr. Hollander, secured by a third lien on the assets of FAvS. The loan bears interest at 10% and in addition Hollander was issued warrants to purchase shares of Class A Common Stock of FAvS, representing 15% of FAvS post-exercise shareholders' equity, at an exercise price of \$7.00 per share.

Pursuant to the terms and conditions of the transaction, management believed that there were indicators of impairment with respect to TAT's investment in FAvS. Accordingly, the Company performed an impairment test of its investment in FAvS, with the assistance of a third party valuation. Based on the results of this test the Company determined that its investment in FAvS was impaired by \$3.3 million. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels which related to the business of API, one of FAvS subsidiaries, and approximates TAT's share in the loss resulting from the API Transaction discussed below.

On March 18, 2013 FAvS sold 97% of the stock of API for a total purchase price of \$16.5 million, of which \$15.9 million was used to repay debt (**the "API Transaction"**). The sale resulted in FAvS retaining a 3% equity interest in the API business. The **API** transaction resulted in a loss from discontinued operations and write-down of the API business of \$11.5 million which is included in the FAvS loss for the year ended December 31, 2012. Simultaneously with the transaction FAvS paid-off its Term Loan in the amount of \$4 million thereby terminating the guaranty and releasing the Letter of Credit provided by TAT to secure such guaranty. Accordingly the restricted deposit associated with the above Letter of Credit, was released as well.

FAvS audited consolidated financial statements for the year ended December 31, 2012, which were signed on March 20, 2013, included a restatement of 2011 consolidated results to correct errors in previously reported amounts. TAT's management reviewed the restatement and its effect on the consolidated financial statements of the Company and found it to be immaterial. Accordingly, no restatement was recorded in the Company's consolidated financial statements.

#### **Income Taxes**

TAT operates within multiple taxing jurisdictions and is subject to audits in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve. In management's opinion, adequate provisions for income taxes have been made for all years. Although management believes that its estimates are reasonable, no assurance can be given that the final tax outcome of these issues will not be different than those that are reflected in its historical income tax provisions.

TAT accounts for income taxes in accordance with ASC 740-10. TAT uses the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on temporary differences between the financial statement and tax bases of assets and liabilities and net operating loss and credit carry forwards using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established when it is more likely than not that some portion of the deferred tax assets will not be realized. To the extent that TAT's decisions and assumptions and historical reporting are determined not to be compliant with applicable tax laws TAT may be subject to adjustments in its reported income for tax purposes as well as interest and penalties.

Interpretation ASC 740-10 prescribes a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. ASC 740-10 also provides guidance on derecognition of tax positions, classification on the balance sheet, interest and penalties, accounting in interim periods, disclosure and transition. In addition, ASC 740-10 requires significant judgment in determining what constitutes an individual tax position as well as assessing the outcome of each tax position. Changes in judgment as to recognition or measurement of tax positions can materially affect the estimate of the effective tax rate and consequently, affect our operating results.

#### **Allowances for Doubtful Accounts**

TAT performs ongoing credit evaluations of its customers' financial condition and requires collateral as deemed necessary. Allowances for doubtful accounts are maintained for estimated losses resulting from the inability of TAT's customers to make payments. In judging the adequacy of the allowance for doubtful accounts, TAT considers multiple factors including the aging of receivables, historical bad debt experience and the general economic environment. Management applies considerable judgment in assessing the realization of receivables, including assessing the probability of collection and the current credit worthiness of each customer. If the financial condition of TAT's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

#### **Inventories**

Inventories are stated at the lower of cost or market. Cost is determined by the basis of actual cost or by the average cost method. TAT's policy for valuation of inventory and commitments to purchase inventory, including the determination of obsolete or excess inventory, requires it to perform a detailed assessment of inventory at each balance sheet date which includes a review of, among other factors, an estimate of future demand for products within specific time frames, valuation of existing inventory, as well as product lifecycle and product development plans. The business environment in which TAT operates, the wide range of products that TAT offers and the relatively short sales-cycles TAT experiences, all contribute to the exercise of judgment relating to maintaining and writing-off of inventory levels. The estimates of future demand that TAT uses in the valuation of inventory are the basis for its revenue forecast, which is also consistent with its short-term manufacturing plan. Inventory reserves are also provided to cover risks arising from non-moving items. Inventory management remains an area of management focus as TAT balances the need to maintain strategic inventory levels to ensure competitive lead times against the risk of inventory obsolescence because of changing technology and customer requirements. TAT writes down obsolete or slow moving inventory in an amount equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand, market conditions and sale forecasts.

During the quarter ended September 30, 2011, we recorded a write down of inventory in the amount of \$2.5 million under cost of revenues, attributable to inventory of the MRO services for Aviation Components operating segment. Although revenues in the MRO for Aviation Components operating segment increased in the three and nine month periods of year 2011 compared to year 2010, profit margins were lower than anticipated. Accordingly, the write down was due to management's estimation of the continued decline in future forecasted sales levels and profitability margins in certain product lines in this operating segment resulting from the weakness in these areas of business.

If actual market conditions are less favorable than TAT anticipates, additional inventory write-downs may be required.

#### Key Indicators

TAT's management evaluates its performance by focusing on its key performance indicators, which are revenues, sources of revenues, gross profit and operating income. These key performance indicators are primarily affected by the competitive landscape in which TAT operates and its ability to meet the challenges posed.

The following table presents, for the periods indicated, information concerning TAT's results of operations:

	Year Ended December 31		
	2012	2011	2010
	(in thousands)		
Revenues			
OEM of Heat Management Solutions	\$ 31,032	\$ 30,020	\$ 29,651
Heat Transfer Services and Products *	27,709	27,603	* 24,468
MRO services for Aviation Components *	22,442	20,146	* 16,333
OEM Electric Motion Systems	10,007	11,658	13,046
Eliminations	(3,268)	(4,030)	(3,743)
Total revenues	87,922	85,397	79,755
Cost of revenues			
OEM of Heat Management Solutions	23,105	22,660	22,425
Heat Transfer Services and Products	19,671	20,173	* 18,005
MRO services for Aviation Components	19,044	17,882	* 14,631
OEM Electric Motion System	8,043	9,388	10,092
Write down of inventory and impairment charges of long lived assets	-	5,763	3,500
Eliminations	(3,281)	(3,884)	(3,965)
Total cost of revenues	66,582	71,982	64,688
Research and development costs, net	1,152	786	651
Selling and marketing expenses	3,426	3,439	3,475
General and administrative expenses	11,487	10,949	12,832
Impairment of goodwill and intangible assets	1,015	-	4,704
Other expenses (income)	9	(169)	-
Operating income (loss)	4,251	(1,590)	(6,595)
Financial expense, net	(181)	(380)	(111)
Other expenses	-	-	(200)
Gain from dilution of interests in affiliated company	-	240	-
Income (loss) before taxes on income	4,070	(1,730)	(6,906)
Taxes on income (tax benefit)	2,086	(316)	(4,153)
Net income (loss) after taxes on income	1,984	(1,414)	(2,753)
Share in results of affiliated company and impairment of share in affiliated company	(3,756)	331	(4,510)
Net loss (income) attributable to non controlling interest	58	53	(123)
Net loss attributable to TAT Technologies' Shareholders	\$ (1,714)	\$ (1,030)	\$ (7,386)

\* As of January 1, 2011, TAT began reporting its operations based on four operating segments, after dividing its MRO Services operating segment into two separate segments: Heat Transfer Services and Products and MRO services for Aviation Components. Accordingly, the revenues and costs reported for the twelve month period ended December 31, 2010 for MRO Services operating segment were divided between these two new operating segments. Additionally, the operating segment name of 'OEM of Heat Transfer Products' was changed to 'OEM of Heat Management Solutions'.

The following table presents, for the periods indicated, information concerning TAT's results of operations as a percentage of revenues:

	Year Ended December 31,		
	2012	2011	2010
Revenues			
OEM of Heat Management Solutions	35%	35%	37%
Heat Transfer Services and Products	32	32	31
MRO services for Aviation Components	26	24	20
OEM Electric Motion Systems	11	14	17
Eliminations	(4)	(5)	(5)
Total revenues	100	100	100
Cost of revenues			
OEM of Heat Management Solutions	27	27	28
Heat Transfer Services and Products	22	24	23
MRO services for Aviation Components	22	21	18
OEM Electric Motion Systems	9	11	13
Write down of inventory and impairment charges of long lived assets	-	7	4
Eliminations	(4)	(5)	(5)
Cost of revenues	76	84	81
Research and development costs, net	1	1	1
Selling and marketing expenses	4	4	4
General and administrative expenses	13	13	16
Impairment of goodwill and intangible assets	1	-	6
Other expenses (income)	-	*	-
Operating income (loss)	5	(2)	(8)
Financial expense, net	*	*	*
Other expenses	*	-	*
Gain from dilution of interests in affiliated company	*	*	-
Income (loss) before taxes on income	5	(2)	(9)
Taxes on income (tax benefit)	3	*	(5)
Net income (loss) after taxes on income	2	(2)	(4)
Share in results of affiliated company and impairment of share in affiliated company	(4)	(*)	(6)
Net loss (income) attributable to non controlling interest	*	*	*
Net income (loss) attributable to TAT Technologies' Shareholders	(2)%	(1)%	(10)%

\* Less than one percent.

***Year ended December 31, 2012 compared with Year ended December 31, 2011***

*Revenues.* Total revenues were \$87.9 million for the twelve months ended December 31, 2012, compared to \$85.4 million for the twelve months ended December 31, 2011, an increase of 3.0%. This reflects the increase in revenues in all our significant operating segments - the OEM of Heat Management Solutions segment, the Heat Transfer Services and Products segment and the MRO Services for Aviation Components segment; while revenues in the OEM of Electric Motion Systems operating segment significantly decreased due to growing weakness in the relevant defense markets. This decrease is a continuation of the decrease in revenues this segment had experienced during 2011.

*Revenues from OEM of Heat Management Solutions.* Revenues from OEM of Heat Management Solutions operating segment increased to \$31.0 million for the year ended December 31, 2012 from \$30.0 million for the year ended December 31, 2011, an increase of 3.4%.

*Revenues from OEM of Electric Motion Systems.* Revenues from OEM of Electric Motion Systems operating segment decreased to \$10.0 million for the year ended December 31, 2012, from \$11.7 million for the year ended December 31, 2011, a decrease of 14.2%. During 2012 and 2011 this segment experienced a gradual decrease in revenues due to growing weakness in the relevant defense markets.

*Revenues from Heat Transfer Services and Products.* Revenues from Heat Transfer Services and Products operating segment increased to \$27.7 million for the year ended December 31, 2012, from \$27.6 million for the year ended December 31, 2011, an increase of 0.4%.

*Revenues from MRO services for Aviation Components.* Revenues from MRO services for Aviation Components operating segment increased to \$22.4 million for the year ended December 31, 2012, from \$20.1 million for the year ended December 31, 2011, an increase of 23.6%. The increase was attributable to increased sales both to existing and new customers.

*Cost of revenues.* Cost of revenues was \$66.6 million for the twelve months ended December 31, 2012, compared to \$66.2 million for the twelve months ended December 31, 2011 (excluding a \$5.76 million write down of inventories and impairment charges of long lived assets recorded in the 2011 third quarter), an increase of 0.5%. This reflects (i) the increase in cost of revenues in the OEM of Heat Management Solutions operating segment and in the MRO Services for Aviation Components operating segment, which is primarily attributable to the increase in revenues in these operating segments; partially offset by (ii) the decrease in cost of revenues in the Heat Transfer Services and Products operating segment which is primarily attributable to decreased material costs; and (iii) the decrease in cost of revenues in the OEM of Electric Motion Systems operating segment, which is primarily attributable to the decrease in revenues in this operating segment.

Cost of revenues as a percentage of revenues was 75.7% for the twelve months ended December 31, 2012, compared to 77.5% for the twelve months ended December 31, 2011 (excluding a \$5.76 million write down of inventories and impairment charges of long lived assets recorded in the 2011 third quarter). This decrease is primarily attributable to (i) product mix with higher margin products sold during this period along with lower rate of fixed production costs in the MRO Services for Aviation Components operating segment (partially effected by the sale of inventory items that were impaired in approximately \$0.6 million in previous years) and in the OEM of Heat Management Solutions operating segments; (ii) product mix with higher margin products in the Heat Transfer Services and Products operating segment; and (iii) similar cost of revenues as a percentage of revenues in the OEM of Electric Motion Systems operating segment.

*Cost of revenues for OEM of Heat Management Solutions.* Cost of revenues for OEM of Heat Management Solutions operating segment increased to \$23.1 million for the year ended December 31, 2012, from \$22.6 million for the year ended December 31, 2011, an increase of 2.0%. This increase is mainly attributable to the increase in revenues in 2012.

Cost of revenues as a percentage of revenues in this segment decreased to 74.5% in the year ended December 31, 2012, from 75.5% for the year ended December 31, 2011. Primarily as a result of product mix with higher margin products sold during year 2012 along with lower rate of fixed production costs in 2012 compared with 2011.

*Cost of revenues for OEM of Electric Motion Systems.* Cost of revenues for OEM of Electric Motion Systems operating segment decreased to \$8.0 million for the year ended December 31, 2012, from \$9.4 million for the year ended December 31, 2011, a decrease of 14.3%. This decrease is mainly attributable to the decrease in revenues in 2012.

Cost of revenues as a percentage of revenues in this segment was 80.4% in the year ended December 31, 2012, similar to 80.5% in the year ended December 31, 2011.

*Cost of revenues for Heat Transfer Services and Products.* Cost of revenues for Heat Transfer Services and Products operating segment decreased to \$19.7 million for the year ended December 31, 2012 from \$20.2 million for the year ended December 31, 2011, a decrease of 2.5%. This decrease is mainly attributable to the decrease in material costs in 2012 compared with 2011.

Cost of revenues as a percentage of revenues in this segment decreased to 71.0% in the year ended December 31, 2012 from 73.1% for the year ended December 31, 2011, primarily as a result of product mix with higher margins sold during year 2012.

*Cost of revenues for MRO services for Aviation Components.* Cost of revenues for MRO services for Aviation Components operating segment increased to \$19.0 million for the year ended December 31, 2012 from \$17.9 million for the year ended December 31, 2011, an increase of 6.5%. This increase is mainly attributable to the increase in revenues in 2012.

Cost of revenues as a percentage of revenues in this segment decreased to 84.9% in the year ended December 31, 2012 from 88.8% for the year ended December 31, 2011, Primarily as a result of product mix with higher margin products sold during year 2012 along with lower rate of fixed production costs in 2012 compared with 2011.

*Write down of inventory and impairment of long lived assets.* For the twelve months ended December 31, 2011, charges under this item were \$5.46 million attributable to a write down of inventory and impairment charges of intangible assets and fixed assets in the MRO Services for Aviation Components operation and \$0.3 million attributable to impairment of intangible asset 'Customer Relations' in the OEM of Electric Motion Systems operating segment.



*Research and development, net.* Research and Development expenses were \$1.2 million for the twelve months ended December 31, 2012, compared to \$0.8 million for the twelve months ended December 31, 2011, an increase of 46.6%, and are related to new products and technologies within the OEM operations in Israel and the Heat Transfer Services and Products operating segment.

Research and Development expenses as a percentage of revenues were 1.3% for the twelve months ended December 31, 2012 compared to 0.9% for the twelve months ended December 31, 2011. TAT expects to invest additional resources in research and development activities, and accordingly will continue to incur and record additional research and development expenses in coming years.

*Selling and marketing expenses.* Selling and marketing expenses were \$3.4 million for the twelve months ended December 31, 2012, similar to \$3.4 million for the twelve months ended December 31, 2011. This was impacted by (i) the increased expenses in the OEM of Heat Management Solutions operating segment, primarily attributable to increased payroll costs, commissions and exhibition expenses; (ii) similar expenses in the Heat Transfer Services and Products operating segment; offset by (iii) the decreased expenses in the MRO Services for Aviation Components operating segment, attributable to decreased payroll costs, commissions and exhibition expenses; and (iv) the decreased expenses in the OEM of Electric Motion Systems operating segments, primarily attributable to a decrease in exhibition expenses.

Selling and marketing expenses as a percentage of revenues were 3.9 % for the twelve months ended December 31, 2012, similar to 4.0% for the twelve months ended December 31, 2011. TAT expects to continue to invest additional resources in selling and marketing activities in coming years.

*General and administrative expenses.* General and administrative expenses were \$11.5 million for the twelve months ended December 31, 2012, compared to \$10.9 million for the twelve months ended December 31, 2011, an increase of 4.9%. The increase in general and administrative expenses was impacted by (i) the increased expenses in the MRO Services for Aviation Components operating segment primarily attributable to a provision recorded for doubtful debt in the first quarter and to a decrease in FAVS' participation in certain operating expenses; (ii) the increased expenses in the Heat Transfer Services and Products operating segment, primarily attributable to the increase in payroll costs and employee related expenses; partially offset by (iii) the decreased expenses in the OEM of Heat Management Solutions operating segment primarily attributable to decreased payroll costs; and (iv) the decreased expenses in the OEM of Electric Motion Systems operating segment attributable to the increase in exchange rates between the U.S. dollar and the Israeli Shekel.

General and administrative expenses as a percentage of revenues were 13.1% for the twelve months ended December 31, 2012, compared to 12.8% for the twelve months ended December 31, 2011.

*Impairment of Goodwill.* During the twelve months ended December 31, 2012, the Company recorded an impairment charge of \$1.0 million to reflect the impairment of the entire balance of the goodwill included in the OEM of Electric Motion Systems operating segment. This was based on an impairment test performed by the Company, with the assistance of an independent appraisal.

*Operating income (loss).* For the twelve months ended December 31, 2012, TAT reported operating income of \$5.3 million compared to operating income of \$4.2 million for the twelve months ended December 31, 2011 (excluding the above mentioned impairment charge of goodwill recorded in 2012 second quarter and non-recurring write down of inventories and impairment charges of long lived assets recorded in 2011 third quarter), an increase of 26.2%. The increase in operating income is attributable to (i) the increase in operating income in the OEM of Heat Management Solutions operating segment; (ii) the decrease in operating loss in the MRO Services for Aviation Components and the OEM of Electric Motion Systems operating segments; partially offset by (iii) the moderate decrease in operating income in the Heat Transfer Services and Products operating segment.

*Financial expenses.* Financial expenses for the twelve months ended December 31, 2012 were \$2.2 million, similar to \$2.2 for the twelve months ended December 31, 2011. Financial expenses during the twelve months ended December 31, 2012 primarily resulted from changes in exchange rates between the U.S. dollar and the Israeli Shekel, realized losses from hedging transactions, bank fees and interest payments on short-term credit and long-term loans.

*Financial income.* Financial income for the twelve months ended December 31, 2012 was \$2.0 million, compared to \$1.8 million for the twelve months ended December 31, 2011. Financial income during the twelve month period ended on December 31, 2012 primarily resulted from changes in exchange rates between the U.S. dollar and the Israeli Shekel and between the U.S. dollar and the Euro, change in fair value of unrealized hedging transactions profits, interest received from the Israeli tax authorities for excess payments made in previous years and from interest received on short-term investments.

*Taxes on income (tax benefit).* Taxes on income for the twelve months ended December 31, 2012, amounted to \$2.1 million, compared to a tax benefit of \$0.3 million for the twelve months ended December 31, 2011. Taxes on income for the twelve months ended December 31, 2012, were impacted by (i) the decrease in pre-tax loss incurred in 2012 compared to the pre-tax loss incurred in 2011 in the MRO Services for Aviation Components operating segment; partially offset by (ii) the decrease in tax expenses in the OEM of Heat Management Solutions operating segment, mainly due to the adoption of a new tax regulation under the Law for the Encouragement of Capital Investments in 2011; (iii) the decrease in pre-tax income in the Heat Transfer Services and Products operating segment; and (iv) similar tax expense in the OEM of Electric Motion Systems operating segment.

*Share in Results of affiliated company.* TAT recognized a loss of \$0.45 million from its approximately 30% interest in FAvS's results for the twelve months ended December 31, 2012 compared to income of \$0.3 million for the twelve months ended December 31, 2011. Additionally, during the twelve months ended December 31, 2012 TAT recognized an impairment of \$3.3 million with respect to its approximately 30% interest in FAvS. This was based on an impairment test performed by the Company, with the assistance of an independent appraisal.

*Net loss attributable to noncontrolling interest.* TAT recognized net loss of \$0.1 million attributable to noncontrolling interest for the twelve months ended December 31, 2012, similar to the net loss attributable to noncontrolling interest for the twelve months ended December 31, 2011. In both periods net loss attributable to noncontrolling interest was attributable to our 70% held Bental subsidiary.

*Net loss attributable to controlling interest.* TAT recognized net loss of \$1.7 million for the twelve months ended December 31, 2012 compared to net loss of \$1.0 million for the twelve months ended December 31, 2011. The net loss reported for the twelve months ended December 31, 2012 is the result of a \$1.0 million impairment charge of goodwill, recorded in the second quarter of 2012, in TAT's OEM for Electric Motion Systems operating segment and the \$3.3 million impairment charge, also recorded in the second quarter of 2012, with respect to TAT's investment in FAvS. The net loss reported for the twelve months ended December 31, 2011 was the result of a \$5.76 million (before taxes) write down of inventories and impairment charges of long lived assets (\$3.61 million, net of taxes). Excluding these impairment charges net income for the twelve month period ended December 31, 2012, was \$2.6 million similar to net income of \$2.6 million for twelve month period ended December 31, 2011.

***Year ended December 31, 2011 compared with Year ended December 31, 2010***

*Revenues.* Total revenues were \$85.4 million for the twelve months ended December 31, 2011, compared to \$79.8 million for the twelve months ended December 31, 2010, an increase of 7.1%. This reflects (i) the increase in revenues in the Heat Transfer Services and Products operating segment; (ii) the increase in revenues in the MRO Services for Aviation Components operating segment; and (iii) the increase in revenues in the OEM of Heat Management Solutions operating segment. This was partially offset by decreased revenues in the OEM of Electric Motion Systems operating segment for the twelve months ended December 31, 2011 compared to the twelve months ended December 31, 2010 due to growing weakness in the relevant markets.

*Revenues from OEM of Heat Management Solutions.* Revenues from OEM of Heat Management Solutions segment increased to \$30.0 million for the year ended December 31, 2011 from \$29.7 million for the year ended December 31, 2010, an increase of 1.2%.

*Revenues from OEM of Electric Motion Systems.* Revenues from OEM of Electric Motion Systems segment decreased to \$11.7 million for the year ended December 31, 2011, from \$13.0 million for the year ended December 31, 2010, a decrease of 10.6%. During 2011 this segment experienced a gradual decrease in revenues due to growing weakness in the relevant markets

*Revenues from Heat Transfer Services and Products.* Revenues from Heat Transfer Services and Products increased to \$27.6 million for the year ended December 31, 2011, from \$24.5 million for the year ended December 31, 2010, an increase of 12.8%. The increase was attributable to increased sales both to existing and new customers.

*Revenues from MRO services for Aviation Components.* Revenues from MRO services for Aviation Components increased to \$20.1 million for the year ended December 31, 2011, from \$16.3 million for the year ended December 31, 2010, an increase of 23.4%. The increase was attributable to increased sales both to existing and new customers.

*Cost of revenues.* Cost of revenues was \$66.2 million for the twelve months ended December 31, 2011 compared to \$61.2 million for the twelve months ended December 31, 2010 (excluding write down of inventories and impairment charges of long lived assets), an increase of 8.2%. This primarily reflects (i) the increase in cost of revenues in the Heat Transfer Services and Products operating segment; and (ii) the increase in cost of revenues in the MRO Services for Aviation Components operating segment, attributable to the increase in revenues in these operating segments; partially offset by (iii) the decrease in cost of revenues in the OEM of Electric Motion Systems operating segment attributable to the decrease in revenues in this operating segment.

Cost of revenues as a percentage of revenues was 77.5% for the twelve months ended December 31, 2011, similar to 76.7% for the twelve months ended December 31, 2010 (excluding write down of inventories and impairment charges of long lived assets). This increase is primarily attributable to product mix with higher margin products sold during the twelve months ended December 31, 2011, in the Heat Transfer Services and Products and MRO Services for Aviation Components operating segments; partially offset by product mix with lower margin products sold during the twelve months ended December 31, 2011 in the OEM of Electric Motion Systems operating segment.

All of the following cost of revenues' data for the operational segments does not reflect the elimination of inter-company transactions.

*Cost of revenues for OEM of Heat Management Solutions.* Cost of revenues for OEM of Heat Management Solutions was \$22.7 million for the year ended December 31, 2011, similar to \$22.4 million for the year ended December 31, 2010.

Cost of revenues as a percentage of revenues in this segment was 75.5% in the year ended December 31, 2011, similar to 75.6% for the year ended December 31, 2010.

*Cost of revenues for OEM of Electric Motion Systems.* Cost of revenues for OEM of Electric Motion Systems segment decreased to \$9.4 million for the year ended December 31, 2011, from \$10.1 million for the year ended December 31, 2010, a decrease of 7.0%. This decrease is mainly attributable to the decrease in revenues in these operating segments.

Cost of revenues as a percentage of revenues in this segment increased to 80.5% in the year ended December 31, 2011, from 77.4% in the year ended December 31, 2010, primarily as a result of product mix with lower margin products sold during year 2011 and of the higher rate of fixed costs to total costs resulting from the lower revenues in 2011 compared with 2010.

*Cost of revenues for Heat Transfer Services and Products.* Cost of revenues for Heat Transfer Services and Products increased to \$20.2 million for the year ended December 31, 2011 from \$18.0 million for the year ended December 31, 2010, an increase of 12.0%. This increase is mainly attributable to the increase in revenues in 2011.

Cost of revenues as a percentage of revenues in this segment decreased to 73.1% in the year ended December 31, 2011 from 73.6% for the year ended December 31, 2010, primarily as a result of product mix with higher margins sold during year 2011.

*Cost of revenues for MRO services for Aviation Components.* Cost of revenues for MRO services for Aviation Components increased to \$17.9 million for the year ended December 31, 2011 from \$14.6 million for the year ended December 31, 2010, an increase of 22.2%. This increase is mainly attributable to the increase in revenues in 2011.

Cost of revenues as a percentage of revenues in this segment decreased to 88.8% in the year ended December 31, 2011 from 89.6% for the year ended December 31, 2010, primarily as a result of product mix with higher margins sold during year 2011.

*Write down of inventory and impairment charges of long lived assets.* For the year ended December 31, 2011, charges under this item were \$5.5 million attributable to a non-recurring write down of inventory and impairment charges of intangible assets and fixed assets in the MRO Services for Aviation Components operation and \$0.3 million attributable to impairment of intangible asset 'Customer Relations' in the OEM of Electric Motion Systems operating segment. For the year ended December 31, 2010, charges under this item were \$3.5 million attributable to a non-recurring write down of inventory in the MRO Services operation.

*Research and development, net.* Research and Development expenses were \$0.8 million for the twelve months ended December 31, 2011, similar to \$0.7 million for the twelve months ended December 31, 2010, and are related to new products and technologies within the OEM operations in Israel. Research and Development expenses as a percentage of revenues were 1% in the twelve months ended December 31, 2011 and in the twelve months ended December 31, 2010. TAT does expect to continue to incur research and development expenses in coming years.

*Selling and marketing expenses.* Selling and marketing expenses were \$3.4 million for the twelve months ended December 31, 2011, similar to \$3.5 million for the twelve months ended December 31, 2010. This reflects an increase in selling and marketing expenses in the OEM of Electric Motion Systems operating segment; partially offset by the decrease in selling and marketing expenses in the MRO Services for Aviation Components operating segment. Selling and marketing expenses as a percentage of revenues were 4.0 % for the twelve months ended December 31, 2011, compared to 4.4% for the twelve months ended December 31, 2010 due to the higher revenues in 2011.

*General and administrative expenses.* General and administrative expenses decreased to \$10.9 million for the twelve months ended December 31, 2011, from \$12.8 million for the twelve months ended December 31, 2010, a decrease of 14.7%. This reflects (i) a decrease in the MRO Services for Aviation Components operating segment due to a \$1.8 million non-recurring expense recorded in the fourth quarter of 2010 related to the Parts services operations and the Propellers MRO operations contributed to FAvS (see also "FavS Transaction" below); and (ii) a decrease in the OEM of Electric Motion Systems operating segment; offset by (iii) an increase in the Heat Transfer Services and Products operating segment; and (iv) an increase in the OEM of Heat Management Solutions.

General and administrative expenses as a percentage of revenues were 12.8% for the twelve months ended December 31, 2011, compared to 16.1% for the twelve months ended December 31, 2010 primarily due to the non-recurring expense recorded in the fourth quarter of 2010 and to the higher revenues in 2011.

*Impairment of Goodwill and Intangible assets.* For the year ended December 31, 2010, charges under this item were \$4.7 million primarily attributable a \$4.2 million impairment of goodwill in the MRO reporting unit and a \$0.48 million impairment of 'Customer Relations' in the same reporting unit, during the quarter ended September 30, 2010. These impairments were related to adverse changes in the future outlook for MRO services business including a weak U.S. and global economy which resulted in a reduction in projected future demand for the MRO services.

*Operating loss.* TAT reported an operating loss of \$1.6 million for the twelve months ended December 31, 2011, compared to an operating loss of \$6.6 million for the twelve months ended December 31, 2010 – a decrease of \$5.0 million in operating loss. Excluding the said write down of inventory and impairment charges of long lived assets and goodwill, operating income for the twelve months ended December 31, 2011 was \$4.2 million compared to operating income of \$1.6 million for the twelve months ended December 31, 2010, an increase of 159%. The increase in operating income (excluding these write downs) is primarily attributable to the increase in income from operations in the Heat Transfer Services and Products operating segment and a decrease in operating loss in the MRO Services for Aviation Components operating segment; partially offset by the decrease in income from operations in the OEM of Heat Management Solutions operating segment and the operating loss in the OEM of Electric Motion Systems operating segment.

*Financial expenses.* Financial expenses were \$2.2 million for the twelve months ended December 31, 2011, compared to \$1.7 for the twelve months ended December 31, 2010. Financial expenses during the twelve months ended December 31, 2011 primarily resulted from changes in exchange rates between the U.S. dollar and the Israeli Shekel, change in the fair value of unrealized hedging transactions profits, and interest payments on short-term credit and long-term loans.

*Financial income.* Financial income for the twelve months ended December 31, 2011 was \$1.8 million, compared to \$1.6 million for the twelve months ended December 31, 2010. Financial income during the twelve months period ended on December 31, 2011 primarily resulted from changes in exchange rates between the U.S. dollar and the Israeli Shekel and between the U.S. dollar and the Euro, realized profits from hedging transactions, interest received from the Israeli tax authorities for excess payments made in previous years and from interest received on short-term investments.

*Other expense, net.* Other expense for the twelve months ended December 31, 2010, was \$0.2 million and is attributable to other-than-temporary impairment loss on auction rate securities based on fair value estimation.

*Taxes.* income for the twelve months ended December 31, 2011, amounted to \$0.3 million, compared to tax income of \$4.1 million for the twelve months ended December 31, 2010. Tax income for the twelve months ended December 31, 2011, is primarily attributable to (i) an increase in pre-tax income in the Heat Transfer Services and Products operating segment; (ii) a decrease in pre-tax loss in the MRO Services for Aviation Components operating segment; (iii) increase in tax expenses in the OEM of Heat Management Solutions operating segment, due to higher income before tax for Israeli tax purposes that was impacted by changes in exchange rates between U.S. dollar and the Israeli Shekel. The increase in the tax expenses was partially offset by the pre-tax losses incurred in the OEM of Electric Motion Systems operating segment.



*Share in results of affiliated company and impairment of share in affiliated Company.* TAT recognized income of \$0.33 million from its interest in FAvS's results for the twelve months ended December 31, 2011 compared to loss of \$4.5 million from its interest in FAvS's results and impairment of its share in FAvS (with the assistance of an independent appraisal) for the twelve months ended December 31, 2010.

On June 30, 2011 TAT's interests in FAvS were diluted from 36.6% to 30.3% (30.02% as of December 31, 2011) (see also "FavS Transaction" below).

*Net loss (income) attributable to noncontrolling interest.* TAT recognized an immaterial amount of net loss attributable to noncontrolling interest for the twelve months ended December 31, 2011 compared with net income attributable to noncontrolling interest of \$0.1 million for the twelve months ended December 31, 2010, primarily attributable to our 70% held Bental subsidiary.

*Net loss attributable to controlling interest.* TAT recognized a net loss of \$1.0 million for the twelve months period ended on December 31, 2011 compared to net loss of \$7.4 million for the twelve months ended on December 31, 2010.

#### **Quarterly Results Of Operations (UNAUDITED)**

The following table presents the unaudited consolidated statements of operations data for each of the eight fiscal quarters ended December 31, 2012, in dollars and as a percentage of revenues. In the opinion of TAT's management, this unaudited information has been prepared on the same basis as TAT's audited consolidated financial statements and includes all adjustments, consisting only of normal recurring adjustments, necessary for fair statement of the unaudited information for the quarters presented. The results of operations for any quarter are not necessarily indicative of results that TAT might achieve for any subsequent periods.

	Three months ended							
	2012				2011			
	Dec. 31,	Sept. 30,	June 30,	Mar. 31,	Dec. 31,	Sept. 30,	June 30,	Mar. 31,
	(\$ in thousands)							
Revenues	\$ 23,039	\$ 22,079	\$ 22,127	\$ 20,677	\$ 23,391	\$ 20,710	\$ 19,894	\$ 21,402
Cost of revenues	17,779	16,279	16,421	16,103	18,442	16,284	15,801	15,692
Write down of inventory and impairment charges of long lived assets	-	-	-	-	-	5,763	-	-
Gross profit (loss)	5,260	5,800	5,706	4,574	4,949	(1,337)	4,093	5,710
Research and Development, net	313	164	501	174	143	180	198	265
Selling and marketing expenses	830	783	924	889	957	715	885	882
General and administrative expenses	3,233	2,504	2,755	2,995	2,940	2,985	2,555	2,469
Impairment of goodwill and intangible assets	-	-	1,015	-	-	-	-	-
Other expenses (income)	(1)	-	(4)	14	(44)	(125)	-	-
Operating income (loss)	885	2,349	515	502	953	(5,092)	455	2,094
Financial income (expenses), net	(18)	(40)	(383)	260	(334)	(377)	122	209
Gain from dilution of interests in affiliated company	-	-	-	-	-	-	240	-
Income (loss) before taxes on income	867	2,309	132	762	619	(5,469)	817	2,303
Taxes on income (tax benefit)	190	565	1,063	268	363	(1,948)	489	780
Share in results of affiliated company and impairment of share in affiliated company	(540)	136	(3,312)	(40)	(119)	167	197	86
Net income (loss)	137	1,880	(4,243)	454	137	(3,354)	525	1,609
Net loss (income) attributable to non controlling interest	(8)	(108)	44	130	(20)	70	110	(107)
Net income (loss) attributable to TAT Technologies' Shareholders	\$ 129	\$ 1,772	\$ (4,199)	\$ 584	\$ 117	\$ (3,284)	\$ 635	\$ 1,502
Revenues	100.0%	100.0%	100.0%	100.0	100.0%	100.0%	100.0%	100.0%
Cost of revenues	77.2	73.7	74.2	77.9	78.8	78.6	79.4	73.3
Write down of inventory and impairment charges of long lived assets	-	-	-	-	-	27.8	-	-
Gross profit (loss)	22.8	26.3	25.8	22.1	21.2	(6.4)	20.6	26.7
Research and Development, net	1.4	0.7	2.3	0.8	0.6	0.9	1.0	1.2
Selling and marketing expenses	3.6	3.6	4.2	4.3	4.1	3.5	4.4	4.1
General and administrative expenses	14.0	11.4	12.4	14.5	12.6	14.4	12.9	11.6
Write off of goodwill and intangible assets	-	-	4.6	-	-	-	-	-
Other expenses (income)	-	*	*	0.1	(0.2)	(0.6)	-	-
Operating income (loss)	3.8	10.6	2.3	2.4	4.1	(24.6)	2.3	9.8
Financial income (expenses), net	(0.1)	(0.1)	(1.7)	1.3	(1.4)	(1.8)	0.6	0.9
Gain from dilution of interests in affiliated company	-	-	-	-	-	-	1.2	-
Income (loss) before taxes on income	3.7	10.5	0.6	3.7	2.7	(26.4)	4.1	10.7
Taxes on income (tax benefit)	0.8	2.6	4.8	1.3	(1.6)	(9.4)	2.5	3.6
Share in results of affiliated company and impairment of share in affiliated company	(2.3)	0.6	(15.0)	-	(0.5)	(0.8)	1.0	*
Net income (loss)	0.6	7.3	(19.2)	2.4	0.6	(16.2)	2.6	7.1
Net loss (income) attributable to non controlling interest	*	(0.5)	0.2	(0.2)	(0.1)	0.3	0.6	(0.5)
Net income (loss) attributable to TAT Technologies' Shareholders	0.6%	7.8%	(19.0)%	2.6%	0.5%	(15.9)%	3.2%	7.0%

TAT expects its operating results may fluctuate in the future as a result of various factors, many of which are outside of TAT's control, including the timing of orders, the provision of services and deliveries. Consequently, TAT believes that period-to-period comparisons of its operating results may not necessarily be meaningful, and as a result, you should not rely on them as an indication of future performance.

#### **Seasonality**

In the OEM industry in general and in TAT's OEM businesses in particular, the majority of customers operate based on annual budgets and tend to utilize during the fiscal fourth quarter the remaining balance of any un-used budgets. This trend is more typical with customers from the defense industry. Accordingly, TAT is more likely to generate increased revenues in the OEM businesses (such as TAT's OEM of Heat Management Solutions and OEM of Electric Motion Systems) during the fiscal fourth quarter. The aviation industry is known for its highest traffic in the third quarter, primarily attributable to summer vacations. As a result, during the fiscal third quarter, airlines tend to postpone, to the extent possible, maintenance and repair of their aircraft to minimize aircraft grounding. Accordingly, TAT is more likely to notice decreased revenues in the MRO businesses (such as TAT's MRO for Aviation Components and Heat Transfer Services and Products) during the fiscal third quarter with recovery during subsequent quarters. Notwithstanding the above, the seasonality trends do not necessarily have a material impact on the over whole revenues of TAT.

**Conditions in Israel**

TAT is incorporated under the laws of, and its principal executive offices and manufacturing and research and development facilities are located in, the State of Israel. See “RISK FACTORS” for a description of governmental, economic, fiscal, monetary or political policies or factors that have materially affected or could materially affect TAT’s operations.

**Trade Relations**

Israel is a member of the United Nations, the International Monetary Fund, the International Bank for Reconstruction and Development and the International Finance Corporation. Israel is a member of the World Trade Organization and is a signatory to the General Agreement on Tariffs and Trade. In addition, Israel has been granted preferences under the Generalized System of Preferences from the United States, Australia, Canada and Japan. These preferences allow Israel to export the products covered by such programs either duty-free or at reduced tariffs.

Israel and the European Union Community, known now as the “European Union,” concluded a Free Trade Agreement in July 1975 that confers some advantages with respect to Israeli exports to most European countries and obligates Israel to lower its tariffs with respect to imports from these countries over a number of years. In 1985, Israel and the United States entered into an agreement to establish a Free Trade Area. The Free Trade Area has eliminated all tariff and some non-tariff barriers on most trade between the two countries. On January 1, 1993, an agreement between Israel and the European Free Trade Association, known as the “EFTA,” established a free-trade zone between Israel and the EFTA nations. In November 1995, Israel entered into a new agreement with the European Union, which includes a redefinition of rules of origin and other improvements, such as allowing Israel to become a member of the Research and Technology programs of the European Union. In recent years, Israel has established commercial and trade relations with a number of other nations, including Russia, China, India, Turkey and other nations in Eastern Europe and the Asia-Pacific region.

## Impact of Currency Fluctuation and of Inflation

TAT reports its financial results in dollars and receives payment primarily in dollars or dollar-linked NIS for all of its sales while it incurs a portion of its expenses, principally salaries and related personnel expenses in Israel, in NIS. Additionally, certain assets, as well as a portion of its liabilities, are denominated in NIS. Therefore, the dollar cost of its operations is influenced by the extent to which any inflation in Israel is offset on a lagging basis, or is not offset by the devaluation of the NIS in relation to the U.S. dollar. When the rate of inflation in Israel exceeds the rate of devaluation of the NIS against the U.S. dollar, the dollar cost of operations in Israel increases. If the dollar cost of operations in Israel increases, its dollar-measured results of operations will be adversely affected. TAT cannot assure you that TAT will not be materially and adversely affected in the future if inflation in Israel exceeds the devaluation of the NIS against the dollar or if the timing of the devaluation lags behind inflation in Israel.

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

Year ended December 31,	Israeli inflation rate%	NIS appreciation (devaluation) to the US dollar rate%	Israeli inflation adjusted for appreciation (devaluation) %
2003	(1.9)	7.6	5.7
2004	1.2	1.6	2.8
2005	2.4	(6.8)	(4.4)
2006	(0.1)	8.2	8.1
2007	3.4	9.0	12.4
2008	3.8	1.1	4.9
2009	3.9	0.7	4.6
2010	2.7	6.4	9.1
2011	2.2	(7.7)	(5.5)
2012	1.4	2.3	3.7

A devaluation of the NIS in relation to the U.S. dollar has the effect of reducing the U.S. dollar amount of any of its expenses or liabilities which are payable in NIS, unless these expenses or payables are linked to the U.S. dollar. This devaluation also has the effect of decreasing the U.S. dollar value of any asset which consists of NIS or receivables payable in NIS, unless the receivables are linked to the U.S. dollar. Conversely, any increase in the value of the NIS in relation to the U.S. dollar has the effect of increasing the U.S. dollar value of any unlinked NIS assets and the U.S. dollar amounts of any unlinked NIS liabilities and expenses. During the years 2010 and 2009 the NIS appreciated against the U.S. dollar, which resulted in a significant increase in the U.S. dollar cost of TAT's NIS expenses. Such trend was reversed during the first half of 2011 and by the end of the year the NIS depreciated against the U.S. dollar by 7.7%. Such trend was continued through the end of September 2012, during which the NIS depreciated by additional 2.4%. By the end of 2012 this trend had reversed and the NIS was appreciated by 4.6%. During the first four months of 2012 NIS further appreciated against the U.S. dollar by approximately additional 2.8%.

Because exchange rates between the NIS and the dollar fluctuate continuously, exchange rate fluctuations and especially larger periodic devaluations will have an impact on TAT's profitability and period-to-period comparisons of its results. The effects of foreign currency re-measurements are reported in TAT's consolidated financial statements in current operations. TAT cannot assure you that in the future its results of operations may not be materially adversely affected by currency fluctuations.

#### **Corporate Tax Rate**

Israeli companies are generally subject to income tax on their taxable income. The applicable rate for 2011 was 24% and was due to further gradually reduce to 18% in 2016 and thereafter. Nevertheless, on December 5, 2011, the Knesset (Israel's Parliament) passed a law for changing the tax burden (Legislative Amendments), which canceled, among others, the gradual reduction in the corporate tax rates in Israel. In addition, the corporate tax in Israel increased to 25% starting in 2012. However, the rate is effectively reduced for income derived from an approved enterprise and beneficiary enterprise. Until December 31, 2010, TAT and Bental have elected to participate in the alternative package of tax benefits for its current approved enterprise and beneficiary enterprise under the Law for the Encouragement of Capital Investments, 1959, as amended, the income derived from those enterprises will be exempt from Israeli corporate tax for a specified benefit period (except to the extent that dividends are distributed during the tax-exemption period other than upon liquidation) and subject to reduced corporate tax rates for an additional period.

Additional amendments to the Approved Enterprise Law became effective in January 2011 (the “2011 Amendment”). Under the 2011 Amendment, income derived by ‘Preferred Companies’ from ‘Preferred Enterprises’ (both as defined in the 2011 Amendment) would be subject to a uniform rate of corporate tax as opposed to the current incentives that are limited to income from Approved or Benefiting Enterprises during their benefits period. According to the 2011 Amendment, the uniform tax rate on such income, referred to as ‘Preferred Income’, would be 10% in areas in Israel that are designated as Development Zone A and 15% elsewhere in Israel during 2011-2012, 7% and 12.5%, respectively, in 2013-2014, and 6% and 12%, respectively, thereafter. Income derived by a Preferred Company from a ‘Special Preferred Enterprise’ (as defined in the Approved Enterprise) would enjoy further reduced tax rates for a period of ten years of 5% in Zone A and 8% elsewhere. As with dividends distributed from taxable income derived from an Approved Enterprise or Benefiting Enterprise during the applicable benefits period, dividends distributed from Preferred Income would be subject to a 15% tax (or lower, if so provided under an applicable tax treaty), which would generally be withheld by the distributing company. While the Company may incur additional tax liability in the event of distribution of dividends from tax exempt income generated from its Approved and Benefiting Enterprises, no additional tax liability will be incurred by the Company in the event of distribution of dividends from income taxed in accordance with the 2011 Amendment.

Under the transitional provisions of the 2011 Amendment, the Company and Bental elected to irrevocably implement the 2011 Amendment with respect to its existing Approved and Benefiting Enterprises while waiving benefits provided under the legislation prior to the 2011 Amendment.

Certain investment income derived by TAT from investments may not be regarded by the Israeli tax authorities as income from TAT’s approved and beneficiary enterprises and consequently may be taxed at the regular statutory rate in Israel.

Certain of TAT’s subsidiaries operate in and are subject to the tax laws of various other jurisdictions, primarily the United States. TAT’s U.S. subsidiaries are taxed based on federal and state tax laws. The effective tax of TAT’s U.S. subsidiaries was 38% in the years ended December 31, 2012, 2011 and 2010, respectively.

**Recently Issued Accounting Standards**

In December 2011, the FASB amended its guidance on disclosures about offsetting assets and liabilities. The amendment enhances disclosures regarding financial instruments and derivative instruments that are either (1) offset in accordance with GAAP or (2) subject to an enforceable master netting arrangement. This information will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments.

The amendments in ASU 2011-11 will be applied for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented.

The Company does not expect ASU 2011-11, which relates to disclosure matters only, to have an impact on the Company's consolidated financial position, results of operations or cash flows.

**Liquidity and Capital Resources**

As of December 31, 2012, TAT had cash and cash equivalents and short-term bank deposits of \$26.6 million and restricted cash of \$2.3 million (such restricted cash was released on March 18, 2013, following the API Transaction), which equals \$28.9 million of financial assets, compared with cash and cash equivalents \$26.2 million, marketable securities of \$1.9 million and restricted cash of \$3.3 million, which equals \$31.4 million of financial assets as of December 31, 2011. Financial assets, net of debt were \$24.5 million in December 31, 2012 compared to \$22.0 million in December 31, 2011

On November 15, 2011, TAT's subsidiary, Limco-Piedmont renewed its credit facility with a U.S bank for an additional 21 month period ending on August 31, 2013 for borrowings of up to \$10 million under certain conditions, of which, as of December 31, 2012, Limco-Piedmont had utilized \$0.7 million. As of December 31, 2012 the Company met all financial covenants related to such credit facility.



With regards to loans balance in the total amount of \$5.5 million received by TAT from an Israeli bank, in September, 2011 TAT reached agreement with its lending bank to adjust certain financial covenants related to the said loans. Accordingly, as of December 31, 2012 and 2011 the Company met all financial covenants related to such loans. On November 7, 2011, the Company made a prepayment of \$2.25 million, and on November 6, 2012, additional prepayment of \$0.8 million following which its remaining balance was \$2.5 million.

On September 7, 2011 TAT received a loan from its Bental subsidiary for the total amount of NIS2.5 million (approximately \$0.7 million), to be repaid in whole at the end of a 24 month period (the "Term"). The principle amount bears interest of Prime +1% payable on a quarterly basis and may be repaid at any time during the Term upon TAT's discretion. Simultaneously with such loan, Bental received a loan from an Israeli bank for similar amount under similar terms and conditions.

Capital expenditures for the years ended December 31, 2012, 2011 and 2010 were approximately \$2.4 million, \$3.3 million and \$2.9 million, respectively. These capital expenditures were principally for the purchase of equipment for the OEM and MRO facilities. TAT funded these expenditures from cash flows from operations and also from financing activities. TAT expects that its available cash and cash equivalents and cash flow that will be generated from operations will be sufficient to enable it fund its capital expenditures.

TAT believes that anticipated cash flow from operations and its current cash balances will be sufficient to meet its cash requirements for at least 12 months. TAT's future capital requirements will depend on many factors, including its rate of revenue growth, the expansion of its selling and marketing activities, costs associated with expansion into new markets and the timing of the introduction of new products and services.

On April 22, 2012, subsequent to the balance sheet date, TAT's Board declared a cash dividend in the total amount of \$2.5M' (approximately NIS9.4 million), or \$0.283 per share (approximately NIS1.065 per share), for all of the shareholders of TAT. The dividend was paid on May 17, 2012 to shareholders of record on May 3, 2012.

TAT's Israeli operations are profitable and expected to continue to be profitable. Accordingly there are no liquidity constraints that require the distribution of retain earnings from TAT's U.S. subsidiaries.

## Cash Flows

The following table summarizes TAT's cash flows for the periods presented:

	Year Ended December 31,		
	(in thousands)		
	2012	2011	2010
Net cash provided by (used in) operating activities	\$ 7,738	\$ 698	\$ 3,038
Net cash provided by (used in) investing activities	(9,912)	(602)	(2,986)
Net cash provided by (used in) financing activities	(7,545)	850	1,358
Effect of changes in exchange rate on cash and cash equivalents of foreign currency subsidiary company	68	(51)	59
Net increase (decrease) in cash and cash equivalents	(9,651)	(805)	1,469
Cash and cash equivalents at beginning of the year	26,232	27,037	25,568
Cash and cash equivalents at end of the year	\$ 16,581	\$ 26,232	\$ 27,037

The net cash provided by operating activities for the year ended December 31, 2012 amounted to approximately \$7.7 million, compared to \$0.7 million for the year ended December 31, 2011 and \$3.0 for the year ended December 31, 2010.

Net cash provided by operating activities for the year ended December 31, 2012 was principally derived from \$1.8 million of net loss and from the following adjustments for the following non-cash line items: an upwards adjustment of \$2.4 million for depreciation and amortization; an upwards adjustment of \$1.0 million for impairment of goodwill; an upwards adjustment of \$3.8 million for share in results of affiliated company and impairment of share in affiliated company; an upwards adjustment of \$1.7 million for decrease in net deferred income tax asset; an upwards adjustment of \$0.7 million for decrease in amounts due from related parties; an upwards adjustment of \$0.5 million for decrease in other accounts receivable and prepaid expenses and an upwards adjustment of \$1.3 million for increase in trade accounts payable and other accounts payable and accrued expenses. This was offset with a downward adjustment of \$0.5 million for increase in trade accounts receivable, downward adjustment of \$0.4 million from change in fair value of derivatives and a downward adjustment of \$1.7 million for increase in inventories.

Net cash provided by operating activities for the year ended December 31, 2011 was principally derived from \$1.1 million of net loss adjusted for the following non-cash line items: an upwards adjustment of \$3.3 million for depreciation and amortization; an upwards adjustment of \$2.5 million for write down of inventory, an upwards adjustment of \$3.3 million for impairment of long lived assets; an upwards adjustment of \$1.3 million for decrease in other accounts receivable and prepaid expenses. This was offset with a downward adjustment of \$0.9 million for increase in deferred income taxes net, a downward adjustment of \$1.2 million for increase in related parties, net and trade accounts receivable, a downward adjustment of \$2.0 million for increase in inventories (excluding the above write down), a downward adjustment of \$2.5 million for decrease in trade accounts payable and a downward adjustment of \$1.6 million for decrease in other accounts payable and accrued expenses.

Net cash provided by operating activities for the year ended December 31, 2010, was principally derived from \$7.3 million of net loss and from the following adjustments for the following non-cash line items: an upwards adjustment of \$3.4 million for depreciation and amortization; an upwards adjustment of \$3.5 million for write down of inventory, an upwards adjustment of \$4.7 million for impairment of goodwill and long lived assets; an upwards adjustment of \$4.5 million for share in loss and impairment of investment of an affiliated company, an upwards adjustment of \$1.8 million for increase in trade accounts payable, an upwards adjustment of \$1.6 million for increase in other accounts payable and accrued expenses. This was offset with a downward adjustment of \$3.0 million for increase in deferred income taxes, net, a downward adjustment of \$4.7 million for increase in trade accounts receivable, a downward adjustment of \$1.6 million for increase in inventories (excluding the above write down), a downward adjustment of \$1.0 million for increase in other accounts receivable and prepaid expenses.

The increase in trade receivables in 2010 resulted primarily from the increased revenues, excluding revenues of the Parts services and Propellers MRO operations contributed to FAvS on December 4, 2009. The increase in inventories in 2011 and 2010 resulted from purchases of inventories in relatively large quantities sufficient to support long term contracts, enabling TAT to enjoy relatively lower prices.

Net cash used in investing activities was approximately \$9.9 million for the year ended December 31, 2012, compared to net cash used in investing activities of \$0.6 million for the year ended December 31, 2011 and net cash used in investing activities of approximately \$3.0 million for the year ended December 31, 2010.

Of the cash used in investing activities in the year ended December 31, 2012 approximately \$2.4 million was used for the purchase of property and equipment, primarily production equipment and building improvements and \$10.0 million used for investment in short-term deposit, partially offset by \$1.9 million of proceeds received from selling marketable securities and \$0.9 million from the release of restricted deposit.

Of the cash used in investing activities in the year ended December 31, 2011 approximately \$3.3 million was used for the purchase of property and equipment, primarily production equipment and building improvements and \$0.6 million used for the purchase of marketable securities, partially offset by \$1.2 million of proceeds received from selling marketable securities and \$1.8 million from the exercise of restricted deposit.

Of the cash used in investing activities in the year ended December 31, 2010 approximately \$3.0 million was used for the purchase of property and equipment, primarily production equipment and building improvements and \$0.6 million used for the purchase of marketable securities, partially offset by \$0.9 million of proceeds received from selling marketable securities.

Net cash used in financing activities was approximately \$7.5 million for the year ended December 31, 2012, compared to net cash used in financing activities of approximately \$0.8 million for the year ended December 31, 2011 and net cash provided by financing activities of approximately \$1.4 million for the year ended December 31, 2010.

In the year ended December 31, 2012, the net cash used in financing activities was primarily attributable to repayments of \$4.5 million of short-term credit, repayments of \$1.0 million of long-term loans and payment of \$2.5 million of cash dividend.

In the year ended December 31, 2011, the net cash used in financing activities was primarily attributable to repayments of \$3.4 million of long term loan, partially offset by proceeds of \$2.6 million short term credit received from a bank.

In the year ended December 31, 2010, the net cash provided by financing activities was primarily attributable to proceeds of \$1.7 million short term credit received from a bank and proceeds of \$1.2 million from long-term loans received, partially offset by \$1.6 million of repayments of long term loans.

**A. Research and Development, Patents and Licenses**

Not applicable.

**B. Trend Information**

Our revenues in the US in fiscal 2013 are expected to be impacted by global trends of increased traffic reported by airlines, by the increasing fuel costs that continue to impact the commercial airlines business environment by reducing airlines' profitability and offsetting the positive impact of growing air traffic, by the expected slowdown in the demand for MRO services as a result of airlines deferring MRO activities and utilizing existing stock (destocking) rather than maintaining inventory levels, by the fact that we continue to witness positive indications from commercial OEMs in the aerospace industry that increase backlog of new airplanes and/or airborne platforms/systems and by the fact that the defense market shows growing weakness and is impacted by budget constraints. We also expect that as soon as the aerospace and defense industries recover, our revenues will continue to trend upward.

**C. Off-Balance Sheet Arrangements**

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

#### D. Tabular Disclosure of Contractual Obligations

The following table summarizes our minimum contractual obligations and commercial commitments as of December 31, 2012 and the effect we expect them to have on our liquidity and cash flow in future periods.

Contractual Obligations	Payments due by Period				
	Total	Less than 1 year	1-3 Years	3-5 Years	More than 5 years
Debt obligations	\$ 4,380,000	\$ 3,265,000	\$ 1,115,000	\$ -	\$ -
Operating lease obligations (1)	3,295,000	904,000	1,580,000	352,000	495,000
Purchase commitments	5,471,000	5,471,000	-	-	-
Estimated loan interest (2)	170,000	124,000	46,000	-	-
Total	\$ 13,316,000	\$ 9,764,000	\$ 2,741,000	\$ 352,000	\$ 459,000

- (1) Pursuant to the terms of the agreement we entered into with TAT Industries in 2000 to purchase its operations relating to the manufacture of aviation accessories, we rent from TAT Industries the real estate and buildings encompassing an area of approximately 302,000 square feet for a period of 24 years and eleven months. In consideration we agreed to pay TAT Industries annual rental payments of approximately \$416,000 for the year ended December 31, 2012 with an additional incremental payment of 2% per year. Such rental rates are subject to revaluation every fifth year.
- (2) Interest related to (i) a loan in the amount of \$523,000 which bears annual fixed interest of 5.25% and will be repaid in August 2014; and (ii) loans in the total amount of \$2,477,000 which will be repaid in four annual installments commencing 2011. These loans bear quarterly interest of Libor + 3.5% and Libor + 1.8%.

In addition, we have long-term liabilities for severance pay that are calculated pursuant to Israeli severance pay law generally based on the most recent salary of the employees multiplied by the number of years of employment, as of the balance sheet date. Employees are entitled to one month's salary for each year of employment or a portion thereof. As of December 31, 2012, our severance pay liability, net was \$497,000.

**Item 6. Directors, Senior Management and Employees**

**A. Directors and Senior Management**

Set forth below are the name, age, principal position and a biographical description of each of our directors and executive officers, as of the date hereof:

<b>Name</b>	<b>Age</b>	<b>Position</b>
Zeev Birnboim	63	Chairman of the Board of Directors *
Itzik Maaravi	53	Chief Executive Officer
Todd Schwartz	45	Chief Executive Officer of Piedmont
Yair Raz	57	Chief Executive Officer of Limco
Shmuel Mendel	61	Chief Executive Officer of Bental
Yaron Shalem	40	Chief Financial Officer
Shlomi Karako	54	Vice President Operations
Avi Shani	65	Independent outside Director **
Iris Shapira	46	Independent Director **
Jan Loeb	54	Director
Yankale Shahar	51	Independent outside Director **

(\*) Chairman of Bental's board of directors

(\*\*) Member of the audit committee and member of the committee that examines the financial statements, prior to the Board of Directors' approval; also a member of the compensation committee.

**Zeev Birnboim** was elected as the Chairman of TAT's Board of Directors in March 2013. Mr. Birnboim served from 2009 to 2012, as the Vice President of Business Development, Sales and Marketing of Krausz Industries Ltd. Prior to that, Mr. Birnboim served, inter alia, as the President & CEO of Vita Pri Hagalil Ltd (2004-2009), as the President & CEO of Smart Storage Ltd. (2002-2004) and as the President & CEO of Tadiran-Ampa Ltd. (1998-2002). Mr. Birnboim holds a B.A. in economics and MBA from Hebrew University and has completed the International Senior Management Program at Harvard University.

**Avi Shani** has served as an outside director (within the meaning of the Israeli Companies Law) since August 2008 and is a member of TAT's Audit Committee; in August 2011, Mr. Shani was re-elected to serve as an outside director for a second three-year term. Mr. Shani is also serving as a director of Psagot Providence Funds and of Psagot Pensions Funds. From 2005 until 2008 Mr. Shani served as the CEO of TCM Mobile, a start up company, and prior to that, during years 2000 - 2004 he served as Executive Vice President Investments and Chief Economist of IDB Development, a leading Israeli holding company, in charge of new Investments. Mr. Shani holds a B.A degree in Economics and an MBA, both from Tel Aviv University.

**Iris Shapira** was elected as a director and as a member of TAT's Audit Committee in January 2012. The Audit Committee also determined that Ms. Shapira is qualified as a "director with accounting and financial expertise". Ms. Shapira has served, since February 2010, as the CFO of Haldor Advanced Technologies Ltd. and, since 2010, as an outside director of Computer Direct Group Ltd. During 2010-2011, she served as an outside director of E.T. View Ltd, and during 2003-2007 as the CFO of Cloverleaf Communications Inc. Prior to that, Ms. Shapira served, inter alia, as the CFO of Emblaze Mobile Technologies Ltd. and of Mofet Venture Capital Fund. Ms. Shapira holds a B.A. in accounting and economics from Tel Aviv University and is a certified CPA (Israel).

**Jan Loeb** was elected as a director by our Board of Directors in August 2009. Mr. Loeb has served as President of Leap Tide Capital Management, Inc., a capital investment firm, since 2007. From February 2005 through January 2007, he served as a portfolio manager of Amtrust Capital Management, Inc. From February 2004 through January 2005, Mr. Loeb was a Portfolio Manager for Chesapeake Partners, a capital investment firm. From January 2002 through December 2004, Mr. Loeb was a Managing Director of Jefferies & Company, Inc., an investment banking firm based in New York City. From 1994 through 2001, Mr. Loeb was a Managing Director of Dresdner Kleinwort and Wasserstein, Inc., an investment banking firm based in New York City, which was formerly known as Wasserstein Perella & Co., Inc. Mr. Loeb is also a director of American Pacific Corp and was a director of Pernix Therapeutics Holdings, Inc. until September 2011. Mr. Loeb graduated from Baruch College – City University of New York with a baccalaureate in Finance and Investments.

**Mr. Yacov Shazar** had served as an outside director (within the meaning of the Israeli Companies Law) since August 2010 and is a member of TAT's Audit Committee. Mr. Shazar served as the Chief Financial Officer and Vice President of Elad Group, Canada, from 2004 through 2005, and between years 1990-2004 he served as a customer relations manager in the business division at Bank Hapoalim. Mr. Shazar holds a B.A. degree in Economics and Mathematics from the Hebrew University of Jerusalem.

**Mr. Itsik Maaravi** has served as TAT's Chief Executive Officer since January 2012. Prior to that, Mr. Maaravi served as President of TAT's Piedmont subsidiary, a position he held since July 2011. From July 2009 through June 2011 Mr. Maaravi was Chief Marketing Officer for Piedmont as well as for the Company's Limco subsidiary. Between 2000 and June 2009 Mr. Maaravi held senior marketing positions at Kamor Aviation and Israel Aerospace Industries.



**Mr. Todd Schwarz** has served as Chief Executive Offices of Piedmont since October 2012 and prior thereto as its Chief Financial Officer since January 2011. He began his career with Ernst& Young as a tax specialist in 1989 and immediately before joining Piedmont was the Vice President of Finance and Administration for a regional real estate developer. Mr. Schwarz holds a MBA from the University of Virginia's Darden School of Business and a B.A. in Accountancy from North Carolina State University.

**Dr. Yair Raz** has served as Chief Executive Offices of Limco since November 2012. Prior to that, Dr. Raz served as the Chief Operating Officer of Piedmont Aviation, a position he held since April 2012. From January 2011 to January 2012 Dr. Raz was the BTI Vice President Marketing and Business Development for North America. Between August 2005 and December 2011 Dr. Raz served as General Manager of PCI, a PWA and BTI Joint Venture in the US. Between 1995 and July 2005 Dr. Raz held a growing responsibility Leadership Positions with PCI in the US including Operation Manager, Engineering, Procurement and President Assistant. Between 1998 and 2012 Dr. Raz was also involved with the JV of BTI and PWA in Xian China. Between 1983 and 1995 Dr. Raz held growing leadership positions with BTL in Israel. Those positions included Quality and Plant Management. Dr. Raz holds a B.Sc degree in Mechanical Engineering and a M.Sc degree in Material science from the Technion in Haifa and a Phd. degree from La Salle University in the US.

**Mr. Shmulik Mandel** has served as Bental's Chief Executive Officer since June 2006. Between the years 1998-2006, Mr. Mandel served as the Chairman of the Board of Bental. From 1995 to 1998 Mr. Mandel served as the director of economic affairs for the United Kibutzim Movement in Israel. From 1993 to 2006 Mr. Mandel served as Chairman of the Board of Director of different corporations, among them Atudot Pension Fund Ltd., Lehavot Production and Shield Ltd., Lordan Ltd. and The Investment Company of the Bank for Industrial Development. Mr. Mandel holds a B.S degree in Computer Sciences from the Technion.

**Mr. Yaron Shalem** has served as TAT's Chief Financial Officer since August 2008. Prior to that, between the years 2006 and 2008 Mr. Shalem served as the CFO of OrganiTech USA Inc. - a provider of high-tech hydroponics factories. Prior to that, during years 2003-2005 Mr. Shalem served as the CFO of Arelnet Ltd. - a provider of IP based telecom switches. Before that Mr. Shalem was the CFO of CellPay Ltd, an Israeli start-up provider in the Mobile Payment arena. Mr. Shalem is a CPA and holds a B.A. in Economy & Accounting from Tel Aviv University and an MBA degree from Bar-Ilan University.

*Mr. Shlomi Karako* has served as TAT’s VP Operations since June 2011. Prior to that, between the years 2009 and 2011 Mr. Karako served as an Executive Vice President at Spectronix Ltd. From 2005 through 2009 Mr. Karako served as the General Manager of the business jets division of the Israel Aerospace Industry (IAI). Prior to that, Mr. Karako served in the Israeli Air Force (IAF) for 27 years and retired as Colonel – his last position was managing the aircraft department, with responsibility for engineering, maintenance and logistics for all IAF aircraft. Mr. Karako holds a B.Sc in mechanical engineering from Beer-Shiva University and an M.B.A. from Tel Aviv University.

**Compensation**

The following table sets forth all the compensation TAT paid with respect to all of its directors and executive officers as a group for the year ended December 31, 2012.

	Salaries, fees, Commissions and bonuses	Other benefits
All directors and executive officers as a group (10 persons)	\$ 1,249,000	\$ 340,000

During the year ended December 31, 2012, TAT paid its directors, the determined medium amounts permitted by law to an outside director (within the meaning of the Israeli companies Law) which was: a per meeting attendance fee of NIS 2,540 (approximately \$658), plus an annual fee of NIS 68,005 (approximately \$17,627).

**B. Board Practices**

**Introduction**

According to the Israeli Companies Law and our articles of association, 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 another organ in the company (including our shareholders). Our executive officers are responsible for our day-to-day management. Our executive officers have individual responsibilities established by our chief executive officer and board of directors.

## **Election of Directors**

Our articles of association provide for a board of directors consisting of such number of directors as may be determined from time to time at a general meeting of shareholders, provided that it shall be no less than two or more than eleven. Our board of directors is currently composed of five directors, including three independent directors, two of whom also qualify as outside directors within the meaning of the Israeli Companies Law.

Pursuant to our articles of association and in accordance with the Israeli Companies Law, our directors (except the outside directors) are elected at our annual general meeting of shareholders by a vote of the holders of a majority of the voting power represented and voting at such meeting; in addition, directors (except the outside directors) may be appointed by a vote of a majority of directors then in office. All our directors (except the outside directors) hold office until the annual general meeting of shareholders succeeding their election (provided that if no directors are elected at the annual general meeting, the directors in office at the time such meeting was convened shall continue to hold their office) or until their earlier death, resignation, removal or other circumstances as set forth in the Israeli law. All the members of our Board of Directors (except the outside directors) may be reelected upon completion of their term of office.

The Israeli Companies Law requires the board of directors of a public company to determine a minimum number of directors with “accounting and financial expertise.” Our board of directors determined, accordingly, that at least two directors must have “accounting and financial expertise,” as such term is defined by regulations promulgated under the Israeli Companies Law.

We are exempt from the requirements of the NASDAQ Marketplace Rules with regard to the nomination process of directors since we are a controlled company within the meaning of NASDAQ Marketplace Rule 5615(c)(2). See below in this Item 6. “Directors, Senior Management and Employees - Board Practices - NASDAQ Exemptions for a Controlled Company.”

## Outside and Independent Directors

*Outside Directors.* Under the Israeli Companies Law, Israeli companies whose shares have been offered to the public or whose shares are listed in an authorized stock exchange (accordingly, such shares are considered as held by "the public") are required to appoint at least two outside directors who meet the independence criteria set by the Israeli Companies Law.

A person is qualified to serve as an outside director only if he or she has "accounting and financial expertise" or "professional qualifications," as such terms are defined by the Israeli Companies Regulations (Conditions and Criteria for a Director Who Possesses Accounting Expertise and a Director Who Possesses Professional Competence), 2005. At least one of the outside directors must have "accounting and financial expertise." Each of our outside directors has "accounting and financial expertise."

The outside directors are elected by a special majority vote at a shareholders meeting as specified hereinafter. The shareholders voting in favor of their initial election must include at least a majority of the shares (i) of the non-controlling shareholders of the company and (ii) which do not have a personal interest in the approval of the election, as a result of their relationships with the controlling shareholders - who actually voted on the matter (not including abstentions). This minority approval requirement need not be met if the total shareholdings of those non-controlling shareholders and shareholders who do not have a personal interest in the matter as a result of their relationships with the controlling shareholders - who actually vote against their election represent 2% or less of all of the voting rights in the company.

In general, outside directors serve for a three-year term and may be reelected to two additional three-year terms by one of the following mechanisms: (1) the board of directors proposed the re-election of the nominee and the re-election was approved by the majority required for appointment of outside directors for their initial term; or (2) a shareholder holding 1% or more of the company's voting rights proposed the re-election of the nominee, and the re-election was approved by a majority of the votes cast by the shareholders of the company, excluding the votes of controlling shareholders or those who have a personal interest in the matter as a result of their relationships with the controlling shareholders, provided that the aggregate votes cast in favor of the re-election by shareholders who are not controlling shareholders and do not have a personal interest in the matter as a result of their relationships with the controlling shareholders constitute more than 2% of the company's voting rights. An outside director may be removed from office at the initiative of the board of directors at a special general meeting of shareholders, if the board resolves that the statutory requirements for that person's appointment as outside director no longer exist, or that the outside director has violated his or her duty of loyalty to the company. The resolution of the special general meeting of shareholders regarding the termination of office of an outside director requires the same majority that is required for the election of an outside director. The court may order the termination of the office of an outside director on the same grounds, following a motion filed by a director or a shareholder. If an outside directorship becomes vacant and as result, there is less than two directors who serve as outside directors in the company, the board of directors is required under the Israeli Companies law to convene a shareholders meeting immediately to appoint a new outside director.

Each committee of the board of directors that is authorized to exercise powers vested in the board of directors must include at least one outside director and the audit committee must include all of the outside directors. An outside director is entitled to compensation as provided in regulations adopted under the Israeli Companies Law and is otherwise prohibited from receiving any other compensation, directly or indirectly, in connection with such service.

Until the lapse of two years from termination of office, we may not engage an outside director or his spouse or child, to serve as an office holder and cannot employ or receive services from these persons, either directly or indirectly, including through a corporation controlled by that person; and with regards to a related person (to a such outside director) as defined in the Israeli Companies law which is not a spouse or child – until the lapse of one year from termination of office.

*Independent Directors.* As a controlled company, within the meaning of NASDAQ Marketplace Rule 5615(c)(2), we are exempt from the NASDAQ Marketplace Rule which requires that a majority of our board of directors qualify as independent directors, within the meaning of the NASDAQ Marketplace Rules. See Item 6. “Directors, Senior Management and Employees - Board Practices - NASDAQ Exemptions for a Controlled Company”.

#### **Audit Committee**

Under the Israeli Companies Law, the board of directors of any public company must establish an audit committee. In general, the audit committee must consist of at least three directors and must include all of the outside directors; the majority of the audit committee members must be independent directors within the meaning of the Israeli Companies Law. The audit committee may not include (i) the chairman of the board of directors, (ii) any director employed by the company or by a controlling shareholder of the company (including a company which is controlled by him), (iii) any director providing services to the company or to a controlling shareholder of the company (including to a company which is controlled by him) on an ongoing basis, or (iv) a controlling shareholder or any of the controlling shareholder's relatives.

In addition, the NASDAQ Marketplace Rules require us to establish an audit committee comprised of at least three members, all of whom must be independent directors, each of whom is financially literate and satisfies the respective “independence” requirements of the Securities and Exchange Commission and NASDAQ and one of whom has accounting or related financial management expertise at senior levels within a company.

Our audit committee acts also as a committee for the review and the approval of our financial statements, and as such, assists our board of directors in overseeing the accounting and financial reporting processes of our company and audits of our financial statements, including the integrity of our financial statements, compliance with legal and regulatory requirements, our independent registered public accountants’ qualifications and independence, the performance of our internal audit function and independent registered public accountants, finding any defects in the business management of our company and proposing to our board of directors ways to correct such defects, approving related-party (officers, directors, controlling shareholder, etc.) transactions with the company as required by Israeli law, examining the scope of work and the payment to our independent auditors and such other duties as may be directed by our board of directors. The audit committee may consult from time to time with our independent auditors and internal auditor with respect to matters involving financial reporting and internal accounting controls.

Our audit committee consists of three members of our board of directors (including two outside directors and one independent director) who satisfy the respective “independence” requirements of the Securities and Exchange Commission, NASDAQ and Israeli law for audit committee members. Our board of directors has determined that each member of our audit committee qualifies as an audit committee financial expert, as defined by rules of the Securities and Exchange Commission. The audit committee meets at least once each quarter.

#### **Internal Audit**

The Israeli Companies Law requires the board of directors of a public company to appoint an internal auditor following a recommendation by the audit committee. The role of the internal auditor is to examine, among other things, the compliance of the Company’s conduct with applicable law and orderly business practice. The internal auditor must meet certain statutory requirements of independence. Mr. Doron Cohen has served as our internal auditor since December 24, 2008.

## **Directors' Service Contracts**

There are no arrangements or understandings between us and any of our subsidiaries, on the one hand, and any of our directors, on the other hand, providing for benefits upon termination of their employment or service as directors of our company or any of our subsidiaries.

## **Approval of Related Party Transactions under Israeli Law**

### *Fiduciary Duties of Office Holders*

The Israeli Companies Law codifies the fiduciary duties that “office holders,” including directors and executive officers, owe to a company. An office holder’s fiduciary duties consist of a duty of care and a duty of loyalty. The duty of care requires an office holder to act at a level of care that a reasonable office holder in the same position would employ under the same circumstances. This includes the duty to utilize reasonable means to obtain (i) information regarding the business feasibility of a given action brought for his approval or performed by him by virtue of his position and (ii) all other information of importance pertaining to the foregoing actions. The duty of loyalty requires that an office holder acts in good faith and for the benefit of the company, including (i) avoiding any conflict of interest between the office holder’s position in the company and any other position he holds or his personal affairs, (ii) avoiding any competition with the company’s business, (iii) avoiding exploiting any business opportunity of the company in order to receive personal gain for the office holder or others, and (iv) disclosing to the company any information or documents relating to the company’s affairs that the office holder has received by virtue of his position as an office holder. Such disclosure is not a breach of the fiduciary duty of the officer to the Company.

### *Disclosure of Personal Interests of an Office Holder; Approval of Transactions with Office Holders*

The Israeli Companies Law requires that an office holder promptly, and no later than the first board meeting at which such transaction is considered, disclose any personal interest that he or she may have and all related material information known to him or her and any documents in their position, in connection with any existing or proposed transaction by us. An office holder who did not disclose his personal Interests, will be observed as breached his Fiduciary Duties. In addition, if the transaction is an extraordinary transaction, that is, a transaction other than in the ordinary course of business or other than on market terms, or likely to have a material impact on the company’s profitability, assets or liabilities,. The Office Holder must also disclose any personal interest held by the office holder’s spouse, brother or sister, parent, grandparent, child as well as brother, sister or parent of such person's spouse or the spouse of any of the above, or by any corporation in which the office holder or his relative (as defined in the Israeli Companies Law) is a 5% or greater shareholder, director or general manager or in which he or she has the right to appoint at least one director or the general manager.

Under the Israeli Companies Law, in general all arrangements as to compensation of office holders who are not directors require the approval of the compensation committee and the board of directors, including and exculpation, insurance and indemnification of, or an undertaking to, indemnify an office holder who is not a director. The compensation of office holders who are directors must be approved by our compensation committee, board of directors and the general meeting of our shareholders.

Some transactions, actions and arrangements involving an office holder (or a third party in which an office holder has an interest) must be approved by the board of directors or as otherwise provided for in a company's articles of association. If the transaction is an extraordinary transaction (which defined as a transaction not in the ordinary course of business and for a material value) such a transaction must be approved by the audit committee and by the board of directors itself, and under certain circumstances shareholders' approval may be required. A director who has a personal interest in a transaction that is considered at a meeting of the board of directors or the audit committee may not be present during the board of directors or audit committee discussions and may not vote on the transaction, unless the transaction is not an extraordinary transaction or the majority of the members of the board or the audit committee have a personal interest, as the case may be. In the event the majority of the members of the board of directors or the audit committee have a personal interest, then the approval of the general meeting of shareholders is also required.

*Disclosure of Personal Interests of a Controlling Shareholder; Approval of Transactions with Controlling Shareholders*

The disclosure requirements that apply to an office holder also apply to a transaction in which a controlling shareholder of the company has a personal interest. The Israeli Companies Law provides that an extraordinary transaction with a controlling shareholder or an extraordinary transaction with another person in whom the controlling shareholder has a personal interest or a transaction with a controlling shareholder or his relative regarding terms of service and employment, must be approved by the audit committee (or the compensation committee, as the case may be), the board of directors and the shareholders by a special majority, as follows. The shareholders's general meeting approval for such a transaction must include the majority of the shareholders who have no personal interest in the transaction who voted on the matter (not including abstentions). The transaction can be approved by shareholders' general meeting without this majority approval if the total shareholdings of those shareholders who have no personal interest and voted against the transaction do not represent more than two percent of the voting rights in the company.



Under the regulations promulgated under the Israeli Companies Law, certain extraordinary transactions between a public company and its controlling shareholder(s) do not require shareholder approval. In addition, under such regulations, directors' compensation and employment arrangements in a public company do not require the approval of the shareholders if both the audit committee and the board of directors agree that such arrangements are solely for the benefit of the company or if the directors' compensation does not exceed the maximum amount of compensation for outside directors determined by applicable regulations. Also, employment and compensation arrangements for an office holder that is a controlling shareholder of a public company do not require shareholder approval if certain criteria are met. The foregoing exemptions from shareholder approval will not apply if one or more shareholders holding at least 1% of the issued and outstanding share capital of the company or of the company's voting rights, objects to the use of these exemptions provided that such objection is submitted to the company in writing not later than fourteen days from the date of the filing of a report regarding the adoption of such resolution by the company. If such objection is duly and timely submitted, then the transaction or compensation arrangement of the directors will require shareholders' approval as detailed above.

In addition, a private placement of securities that will (i) cause a person to become a controlling shareholder or (ii) increase the relative holdings of a shareholder that holds 5% or more of the company's outstanding share capital, or (iii) will cause any person to become, as a result of the issuance, a holder of more than 5% of the company's outstanding share capital in a private placement in which 20% or more of the company's outstanding share capital prior to the placement are offered, the payment for which (in whole or in part) is not in cash or not under market terms, requires approval by the board of directors and the shareholders of the company.

## **Exculpation, Indemnification and Insurance of Directors and Officers**

### *Exculpation of Office Holders*

The Israeli Companies Law provides that an Israeli company cannot exculpate an office holder from liability with respect to a breach of his duty of loyalty, but may, if permitted by its articles of association, exculpate in advance an office holder from his liability to the company, in whole or in part, with respect to a breach of his or her duty of care. However, a company may not exculpate in advance a director from his or her liability to the company with respect to a breach of his duty of care in the event of distributions.

### *Insurance for Office Holders*

The Israeli Companies Law provides that a company may, if permitted by its articles of association, enter into a contract to insure an office holder for acts or omissions performed by the office holder in such capacity for:

- Breach of his or her duty of care to the company or to another person;
- Breach of his or her duty of loyalty to the company, provided that the office holder acted in good faith and had reasonable cause to assume that his act would not prejudice the company's interests;
- Monetary liability imposed upon the office holder in favor of another person;
- A monetary obligation imposed on the office holder in favor of another person who was injured by a violation, as this term is defined in section 52(54)(a)(1)(a) of the Israeli Securities Law; and
- Expenses expended by the office holder, including reasonable litigation expenses, and including attorney's fees, in respect of any proceeding under chapters 8-C, 8-D or 9-A of the Israeli Securities Law or in respect to any monetary sanction.

### *Indemnification of Office Holders*

The Israeli Companies Law provides that a company may, if permitted by its articles of association, indemnify an office holder for acts or omissions performed by the office holder in such capacity for:

- Monetary liability imposed on the office holder in favor of another person by any judgment, including a settlement or an arbitrator's award approved by a court;
- Reasonable litigation expenses, including attorney's fees, actually incurred by the office holder as a result of an investigation or proceeding instituted against him or her by a competent authority, provided that such investigation or proceeding concluded without the filing of an indictment against the office holder or the imposition of any monetary liability in lieu of criminal proceedings, or concluded without the filing of an indictment against the office holder and a monetary liability was imposed on the officer holder in lieu of criminal proceedings with respect to a criminal offense that does not require proof of criminal intent;

- A monetary obligation imposed on the office holder in favor of another person who was injured by a violation, as this term is defined in section 52(54)(a)(1)(a) of the Israeli Securities Law;
- Expenses expended by the office holder, including reasonable litigation expenses, and including attorney's fees, in respect of any proceeding under chapters 8-C, 8-D or 9-A of the Israeli Securities Law or in respect to any monetary sanction
- Reasonable litigation expenses, including attorneys' fees, incurred by such office holder or which were imposed on him by a court, in proceedings the company instituted against the office holder or that were instituted on the company's behalf or by another person, or in a criminal charge from which the office holder was acquitted, or in a criminal proceeding in which the office holder was convicted of a crime which does not require proof of criminal intent; or
- Any other liability, payment or expense which the Company may indemnify its office holders under the Israeli Company Law, the Israeli Securities Law or other Israeli law.

In accordance with the Israeli Companies Law, a company's articles of association may permit the company to:

- Undertake in advance to indemnify an office holder, except that with respect to a financial liability imposed on the office holder by any judgment, settlement or court-approved arbitration award, the undertaking must be limited to types of occurrences, which, in the opinion of the company's board of directors, are, at the time of the undertaking, foreseeable due to the company's activities and to an amount or standard that the board of directors has determined is reasonable under the circumstances; and
- Undertake in advance to indemnify an office holder for reasonable litigation expenses, including attorney's fees, actually incurred by the office holder as a result of an investigation or proceeding instituted against him or her by a competent authority, provided that such investigation or proceeding concluded without the filing of an indictment against the office holder or the imposition of any monetary liability in lieu of criminal proceedings, or concluded without the filing of an indictment against the office holder and a monetary liability was imposed on the officer holder in lieu of criminal proceedings with respect to a criminal offense that does not require proof of criminal intent.
- Undertake in advance to indemnify an office holder for reasonable litigation expenses, including attorneys' fees, incurred by such office holder or which were imposed on him by a court, in proceedings the company instituted against the office holder or that were instituted on the company's behalf or by another person, or in a criminal charge from which the office holder was acquitted, or in a criminal proceeding in which the office holder was convicted of a crime which does not require proof of criminal intent.

- Retroactively indemnify an office holder of the company.

*Limitations on Exculpation, Insurance and Indemnification*

The Israeli Companies Law provides that neither a provision of the articles of association permitting the company to enter into a contract to insure the liability of an office holder, nor a provision in the articles of association or a resolution of the board of directors permitting the indemnification of an office holder, nor a provision in the articles of association exempting an office holder from duty to the company shall be valid, where such insurance, indemnification or exemption relates to any of the following:

- Breach by the office holder of his duty of loyalty, except with respect to insurance coverage or indemnification if the office holder acted in good faith and had reasonable grounds to assume that the act would not prejudice the company;
- Breach by the office holder of his duty of care if such breach was committed intentionally or recklessly, unless the breach was committed only negligently;
- Any act or omission committed with intent to derive an unlawful personal gain; and
- Any fine or forfeiture imposed on the office holder.

In addition, pursuant to the Israeli Companies Law, exemption of, procurement of insurance coverage for, an undertaking to indemnify or indemnification of an office holder must be approved by the compensation committee (with regards to a "Public Company" or to a "Bond Company", as determined in the Israeli Companies Law), and the board of directors and, if such office holder is a director or a controlling shareholder or a relative of the controlling shareholder, also by the shareholders general meeting. A special majority at the general meeting is required if a controlling shareholder is interested in such transaction as an office holder or as a relative of an office holder, as described above.

Our articles of association include provisions which allow us to insure, indemnify and exempt our office holders, subject to the provisions of the Israeli Companies Law. We currently maintain directors' and officers' liability insurance to cover liabilities of up to \$25 million per claim and in the aggregate; following the approvals by our audit committee and the board of directors in accordance with the conditions of a "framework transaction" approved by the general meeting of shareholders on August 30, 2010, such insurance has been recently renewed twice for additional periods of one year on March 15, 2012 and on March 15, 2013 through March 15, 2014. In July 2004, our shareholders approved a form of directors and officers letter of indemnification and exemption for liabilities and expenses incurred as a result of their acts in their capacity as directors and officers of our company, in an aggregate amount not to exceed \$5.0 million or 25% of our equity capital (net worth).

On February 8, 2009, following the approval by our board of directors and audit committee, our shareholders approved the purchase of a tail (runoff) policy insuring the directors and officers of our company in office prior to the acquisition of the control by Isal Amlat, as part of Isal Amlat's obligations under the purchase agreement. The resolution to obtain such policy was adopted by a super majority vote, as required for the approval of transactions with related parties under Israeli law. The policy will be in effect for 7 years, until January 1, 2015. The coverage limit under such policy is 10 million dollars and the premium for such policy is 115,000 dollars for the term of the policy.

Following our acquisition of the shares of Limco-Piedmont held by the public in July 2009 we purchased a tail policy insuring the former directors and officers of Limco-Piedmont. The coverage limit under the policy is \$25 million and the premium for such policy is \$190,000 dollars for the term of the policy.

In March 2012 our board of directors and audit committee approved the purchase of a directors and officers insurance policy for the directors and officers of our company and its subsidiaries, Limco-Piedmont and Bental, and its controlling shareholder TAT Industries. The coverage limit under the policy is 25 million dollars and the premium for the insurance term (one year) is approximately \$100,000.

In March 2013 our board of directors and audit committee approved the purchase of a directors and officers insurance policy for one year for the directors and officers of our company, its subsidiaries (Limco-Piedmont and Bental) and its controlling shareholder (TAT Industries). The coverage limit under the policy is 25 million dollars and the premium for the insurance term (one year) is approximately \$112,000 out of which approximately \$7,500 are charged to TAT Industries.

The 2012 Annual and Extraordinary General Meeting of shareholders of TAT was held on Thursday, June 28, 2012 (the "Meeting"). Among other topics in the meeting, there was also a proposal to amend the Articles of Association of the Company to reflect recent amendments to the Israeli Companies Law and Israeli Securities Law and subject to this approval, to modify certain amendments to the form of indemnification and exemption undertaking by the Company to its directors and officers (the "Form"). Those two aforementioned decisions were not approved in the Meeting and therefore the original Articles of Association and Form are still binding the Company, also with regards to insurance, indemnification and exemption of our office holders, and the Form, provided that they do not contradict provisions in the Israeli Companies Law and Israeli Securities Law which cannot be prescribed. For further details see TAT immediate reports on Form 6K dated May 23, 2012 (TASE reference number 2012-02-133929) and June 28, 2012 (TSAE reference number 2012-02-170526). Subject to the approval of our audit committee, board of directors and shareholders, TAT intends to modify its Articles of Association in order to adjust them to the Israeli Companies Law and Israeli Securities Law.

#### **NASDAQ Exemptions for a Controlled Company**

We are a controlled company within the meaning of NASDAQ Marketplace Rule 5615(c)(2), or Rule 5615(c)(2), because KMN beneficially owns more than 50% of our voting shares.

Under Rule 5615(c)(2), a controlled company is exempt from the following requirements of NASDAQ Marketplace Rules 5605(b)(1), 5605(d) and 5605(e) that would otherwise require that:

- The majority of the company's board of directors qualifies as independent directors, as defined under NASDAQ Marketplace Rules.
- The compensation of the chief financial officer and all other executive officers be determined, or recommended to the board of directors for determination, either by (i) a majority of the independent directors or (ii) a compensation committee comprised solely of independent directors.
- Director nominees must either be selected or recommended for the board of directors, either by (a) a majority of independent directors or (b) a nominations committee comprised solely of independent directors.

We intend to continue to rely on these exemptions provided under Rule 5615(c)(2).

#### **C. Employees**

As of December 31, 2012, we and our subsidiaries employed 575 employees, of whom 439 were employed in manufacturing and quality control, 54 were employed in engineering and research and development and 82 were employed in administration, sales and marketing. Of such employees, 298 were located in Israel and 277 were employed by Limco and Piedmont and located in the United States.

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 Association) are applicable to our Israeli employees by order of the Israeli Ministry of Labor. These provisions concern mainly the length of the workday, minimum daily wages for professional workers, contributions to a pension fund, insurance for work-related accidents, procedures for dismissing employees, determination of severance pay and other conditions of employment. We generally provide our employees with benefits and working conditions beyond the required minimums. Furthermore, under the collective bargaining agreements, the wages of most of our employees are linked to the Consumer Price Index, although the extent of the linkage is limited.

In addition, Israeli law generally requires severance pay upon the retirement or death of an employee or termination of employment without due cause. Furthermore, Israeli employees and employers are required to pay predetermined sums to the National Insurance Institute which is similar to the United States Social Security Administration. The payments thereto amount to approximately 12% of wages, with the employee contributing approximately 43% and the employer approximately 56%.

A general practice followed by us, although not legally required, is the contribution of monies on behalf of its senior employees to a fund known as “Management Insurance.” This fund provides a combination of savings plan, insurance and severance pay benefits to the employee, giving the employee a lump sum payment upon retirement and securing his right to receive severance pay, if legally entitled, upon termination of employment. The employee contributes an amount equal to approximately 5%-6% of his wages and the employer contributes an additional amount of approximately 13-1/3% - 16% of such wages.

**D. Share Ownership**

**Beneficial Ownership of Executive Officers and Directors**

Except as set forth under ‘Stock Option Plans’ and in item 7A below, none of our directors and executive officers beneficially owns more than 1% of our outstanding shares.

## Stock Option Plans

In November 2011, our audit committee and board of directors approved a stock option plan (the “Plan”), which was subsequently approved by the Company’s shareholders, on June 28, 2012. According to the plan an aggregate of 380,000 options (“Options”) exercisable into up to 380,000 Ordinary shares, 0.9 NIS par value, of the Company will be granted to certain members of our board of directors and certain senior executives in TAT, Limco and Piedmont, at an exercise price of \$6.5 per share. The Options vest over a three-year period (one-third each year with the first one-third vesting on June 28, 2013), but the vesting of 50% of the Options is subject, in addition, to certain minimum shareholders’ equity during a period of 4 years from the grant date. On August 21, 2012, pursuant to the Plan, TAT’s Board of Directors approved the grant of 330,000 Options, which were granted on October 4, 2012 (out of which 45,000 options were forfeited on October 30, 2012 and an additional 100,000 were forfeited in 2013 through the date of this report).

### Item 7. Major Shareholders and Related Party Transactions

#### A. Major Shareholders

On October 2012 two Israeli lenders to TAT’s controlling stockholders, KMN Industries and TAT Industries (herein “Controlling Stockholders”), filed separate petitions to the court to enforce liens granted to such lenders by each of the Controlling Stockholders in certain collateral including KMN Industries’ holdings of an approximately 80% ownership interest in TAT Industries (which owns approximately 43% of TAT) and KMN Industries’ direct holdings in TAT (which represents approximately 10% of TAT).

On December 18, 2012 the court appointed permanent receivers on behalf of the two lenders mentioned above for the purpose of jointly enforcing the liens granted to such lenders. If such liens are enforced, such collateral is subject to sale which would result in a change of control of TAT. On March 15, 2013 the receivers of TAT’s shares mentioned above announced a tender to purchase such shares. Pursuant to the tender all proposals to acquire such shares must be submitted no later than April 25, 2013.

As of the date hereof, the Company has no information with respect to any proposals received.

In addition on January 3, 2013 the Israeli court appointed a temporary liquidator for Isal Amlet, the controlling shareholder of TAT Industries, following the request of the trustee to debentures issued by Isal Amlet. On January 28, 2013 such court has issued a Liquidation Order for Isal Amlet, effective as of end of May 2013.



Subject to the appointed of liquidator mentioned above, Isal Amlat, a Tel Aviv Stock Exchange publicly traded company, organized under the laws of the State of Israel, is the beneficial holder of 53.89% of TAT's outstanding shares (4,750,951 shares), of which 10.27% (905,043 shares) are held by Isal Amlet and 43.6% (3,845,908 shares) are held directly by TAT's parent company TAT Industries. 79.33% of TAT Industries' outstanding share capital is held by KMN Industries (KMN). 94% of KMN Industries' outstanding share capital is held by Isal Amlat. 81.68% of Isal Amlat's outstanding share capital is held by KMN Holdings Ltd., an Israeli company publicly traded on the Tel Aviv Stock Exchange, of which 58.63% of its outstanding share capital is held by Ron Elroy. Leap-Tide Capital Management Inc., which is controlled by Mr. Jan Loeb, a member of our board of directors, is the beneficial holder of 5.9% of TAT's Ordinary shares (522,607 shares). No other shareholder is known to us to be a beneficial owner of 5% or more of TAT's Ordinary shares.

The following table sets forth certain information as of April 5, 2013, regarding the beneficial ownership by all shareholders known to us to own beneficially 5% or more of our Ordinary shares:

Name	Number of Ordinary Shares Beneficially Owned (1)	Percentage of Ownership(2)
Isal Amlat Investments (1993) Ltd. (3)	4,750,951	54.00%
TAT Industries (4)	3,845,908	43.71%
Leap-Tide Capital Management Inc.,	522,607	6.28%

- (1) Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission and generally includes voting or investment power with respect to securities. Ordinary shares relating to options and warrants currently exercisable or exercisable within 60 days of the date of this table are deemed outstanding for computing the percentage of the person holding such securities but are not deemed outstanding for computing the percentage of any other person. Except as indicated by footnote, and subject to community property laws where applicable, the persons named in the table above have sole voting and investment power with respect to all shares shown as beneficially owned by them.

- (2) The percentages shown are based on 8,798,570 Ordinary shares issued and outstanding as of April 5, 2013 (net of 274,473 dormant shares).
- (3) Subject to the appointed of liquidator mentioned above, includes 905,043 Ordinary shares held by Isal Amlat (through KMN Industries) and 3,845,908 Ordinary shares held directly by TAT Industries, which is 79.33% held by Isal Amlat. As such, Isal Amlat may be deemed to be the beneficial owner of the aggregate 4,750,951 Ordinary shares held directly by itself and TAT Industries. 81.68% of Isal Amlat's outstanding share capital is held by KMN Holdings Ltd., an Israeli company publicly traded on the Tel Aviv Stock Exchange, which 58.63% of its outstanding share capital is held by Ron Elroy.
- (4) Subject to the appointed of permanent receivers as mentioned above, 79.33% of TAT Industries' outstanding share capital is held by KMN Industries (KMN) and 94% of KMN Industries' outstanding share capital is held by Isal Amlat. As such, MKN Industries (KMN) and Isal Amlat may be deemed to be the beneficial owner of the aggregate 3,845,908 Ordinary shares held directly by TAT Industries. 81.68% of Isal Amlat's outstanding share capital is held by KMN Holdings Ltd., an Israeli company publicly traded on the Tel Aviv Stock Exchange, which 58.63% of its outstanding share capital is held by Ron Elroy.

#### **Significant Changes in the Ownership of Major Shareholders**

On March 11, 2009 and on August 13, 2009, TAT's board of directors authorized its management to engage Oppenheimer Israel Investment House for the blind trust purchase of TAT's shares under rule 10b5-1 of the Securities Exchange Act of 1934. The first purchase plan, which was discontinued on March 26, 2009, resulted on the purchase of 4,650 shares for a cumulative amount of \$ 26 thousand. The second purchase plan, which was discontinued on November 21, 2009, included licensing Oppenheimer Israel to purchase shares of TAT on a foreign stock exchange in an aggregate amount of up to \$2 million (approximately NIS 7.8 million) for a period of six months and at a price not exceeding \$9 per share. As of December 31, 2010, 253,390 shares were purchased, representing about 2.8% of the Company's share capital in consideration of approximately \$2 million (an average of \$7.90 per share). The purchased shares became dormant as defined in the Companies Law.

In September, 2011 Isal Amlat purchased an aggregate of 18,600 Ordinary shares of TAT at an average price of 20.39 NIS per share (approximately \$5.54 per share). Such purchases were made on the Tel Aviv Stock Exchange. Following such purchases, Isal beneficially owns 4,750,951 Ordinary shares, representing 54.00% of TAT's Ordinary shares.

On May 21, 2012, TAT's Board of Directors authorized a share repurchase plan (the "**Plan**"), under Rule 10b5-1 of the Securities Exchange Act of 1934. The plan was for a period of 6 months (subject to extension) and provided for the purchase of shares in an aggregate amount of up to \$0.5 million U.S. dollars. Such plan replaced and superseded a prior repurchase plan approved by TAT's Board of Directors, on February 21, 2012. On November 21, the term of such stock repurchase plan ended. As of such date, the Company had purchased 16,433 shares for approximately \$71 thousands (average of \$4.32 per share) constituting less than 0.1% of TAT's issued shares.

On October 2012 two lenders to TAT's controlling stockholders, KMN Industries and TAT Industries (herein "Controlling Stockholders"), filed separate petitions to the court to enforce liens granted to such lenders by each of the Controlling Stockholders in certain collateral including KMN Industries' holdings of an approximately 80% ownership interest in TAT Industries (which owns approximately 43% of TAT) and KMN Industries' direct holdings in TAT (which represents approximately 10% of TAT).

On December 18, 2012 the court appointed permanent receivers on behalf of the two lenders mentioned above for the purpose of jointly enforcing the liens granted to such lenders. If such liens are enforced, such collateral is subject to sale which would result in a change of control of TAT. On March 15, 2013 the receivers of TAT's shares mentioned above announced a tender to purchase such shares. Pursuant to the tender all proposals to acquire such shares must be submitted no later than April 25, 2013.

As of the date hereof, the Company has no information with respect to any proposals received.

On January 3, 2013 the Israeli court appointed a temporary liquidator for Isal Amlat, the controlling shareholder of TAT Industries, following the request of the trustee to debentures issued by Isal Amlat. On January 28, 2013 such court has issued a Liquidation Order for Isal Amlat, effective as of end of May 2013.

## Major Shareholders Voting Rights

Our major shareholders do not have different voting rights.

## Record Holders

Based on a review of the information provided to us by our transfer agent, as of April 5, 2013, there were 43 holders of record of our Ordinary shares, of which 40 record holders holding less than 1.0% of our Ordinary shares had registered addresses in the United States. These numbers are not representative of the number of beneficial holders of our shares nor is it representative of where such beneficial holders reside since many of these Ordinary shares were held of record by brokers or other nominees including CEDE & Co., the nominee for the Depositary Trust Company (the central depository for the U.S. brokerage community), which held approximately 70% of our outstanding Ordinary shares as of such date.

## B. Related Party Transactions

### *Management and Services Agreement with TAT Industries*

In February 2000, TAT entered into an agreement with TAT Industries, TAT'S controlling shareholder, to purchase operations of TAT Industries relating to the manufacture of aviation accessories and the lease of certain real estate and buildings. Pursuant to the terms of this agreement, all of the employees of TAT Industries were transferred to TAT effective as of January 1, 2000, without any change in the conditions of their employment. TAT Industries pays TAT \$50,000 per year for administrative, accounting and secretarial services provided by TAT to TAT Industries. According to the requirements of the Israeli Companies Law, as amended in 2011, in January 2012 our audit committee has reapproved the terms of these services for an additional three years, commencing retroactively as of November 14, 2011.

In addition, pursuant to the terms of the agreement, TAT sub-leases from TAT Industries approximately 301,000 square foot of the Gedera facility until the end of the respective lease agreements TAT Industries has with the Israel Land Authority (see also under Item 4. Information of the Company, C. Property, Plants and) for a period of 24 years and eleven months, for rental fee which is subject to revaluation every fifth year, with an additional incremental payment of 2%. In 2010 the rental fee was revaluated by a real estate appraiser, and as a result was increased to \$400,000 per year with an additional incremental payment of 2% per year. Total rental payment TAT paid to TAT Industries during 2012 and 2011 were \$416,000 and \$408,000, respectively. See item 4.D "Information on the Company- Property, Plants and Equipment". According to the requirements of the Israeli Companies Law, as amended in 2011, in January 2012 our audit committee has reapproved the terms of the sub-lease until the next revaluation by a real appraiser, due in 2015.

On April 22, 2012, the Board of Directors of the Company approved and ratified payments made by the Company to certain third parties on account of debts of TAT Industries Ltd., the Company's controlling shareholder ("TAT Industries"), to such third parties. As of December 31, 2012 TAT Industries does not have any outstanding debt to TAT (other than a current VAT balance in the amount of \$54,000 resulted from the two companies' consolidated Tax Return.

TAT Industries and TAT are reporting to the Value Added Tax Authorities on a consolidated basis.

*Management Agreement with ISAL*

In March 2012, the audit committee and the board of directors of TAT approved a new three-year management agreement with Isal Amlat, commencing as of February 8, 2012 (the "**New Management Agreement**"). Each of TAT and Isal Amlat shall be entitled to terminate the New Management Agreement subject to a prior written notice of 4 months. Pursuant to the New Management Agreement, in consideration of the management services provided by Isal Amlat, TAT pays Isal Amlat management fees in a total annual amount of NIS1,500,000, linked to the Consumers Price Index to be paid on a monthly basis, plus VAT. In addition, Isal Amlat is entitled to repayment of expenses actually borne as part of providing the management services. The audit committee and board of directors of the Company will examine on a yearly basis, and for the first time in close proximity to the date of publication of the financial reports for the year 2012, the management services actually provided to the Company, and shall examine whether a material change has occurred justifying the update of the management fees and/or the conditions of the New Management Agreement. The New Management Agreement was approved by the shareholders of TAT on June 28, 2012.

On August 21, 2012 the board of directors of TAT approved, following an approval of TAT's audit committee, a change to the New Management Agreement with Isal Amlat, effective from such date according to which the scope of the services provided by Isal Amlat to TAT were reduced and the annual management fees were also reduced by a total amount of NIS570,000 ("reduced amount") following such a reduction such annual management fee was NIS 930,000.

In addition, the Company will receive management services from a private company ("Management company") controlled by Mr. Nathan Galili ("Galili"), CEO of KNM Industries Ltd. (a private company through which Isal Amlat indirectly holding control in the Company). The management services will consist of a half-time of Galili, which value is more than the reduced amount, and will additionally includes its services as active chairman of Bental. For those services the Company will pay the management company annual management fees equal to the reduced amount, in addition to NIS7,000 (plus VAT), as a monthly remuneration for travelling expenses to Bental. In addition, if during the service period or within a twelve month period from the end of the service period the Company will sell its holding in Bental, for more than \$6.6 million ("low threshold"), then the management company will be eligible for a bonus which will be determined as follows:

- 2% out of the 1<sup>st</sup> million above the low threshold, the Company will receive for its holding in Bental, plus
- Additional 3% out of the 2<sup>nd</sup> million above the low threshold the Company will receive for its holding in Bental, plus
- Additional 5% out of the 3<sup>rd</sup> million above the low threshold the Company will receive for its holding in Bental.
- It is clarified that in any event the amount of the bonus shall not exceed \$100 thousand.
- Such management services will be provided until February 8, 2015 (the end of term of the new management agreement with Isal Amlat). Each of the parties (TAT and the management company) may terminate the agreement with a prior written notice of four months.

On January 27, 2013 TAT informed Isal Amlat that no management services had been provided by Isal Amlat to TAT during the preceding months, TAT decided to immediately terminate the Management Agreement. At that date TAT ceased paying management fees.

On February 8, 2013 Mr. Galili informed TAT on the termination of the engagement with TAT, effectively immediately while management fees will be paid throughout June 8, 2013 at the end of the four-month notice period. Mr. Galili ceased providing management services on February 8, 2013.

#### *Inclusion of TAT Industries in a Directors' and Officers' Liability Insurance Policies*

Our directors' and officers' liability insurance policy (see Item 6.B "Board Practices- Exculpation, Indemnification and Insurance of Directors and Officers") includes our parent company, TAT Industries, which bears \$7,500 out of the total \$112,000 annual premium with respect to the insurance.

#### *Management Agreement with Bental*

On June 14, 2010, following the approval of TAT's Board of Directors and audit committee, TAT and Bental entered into a management agreement pursuant to which in consideration of management services provided by TAT, Bental will pay to TAT an amount of \$120,000 plus VAT per fiscal year, commencing June 2010. The agreement will be in effect until otherwise terminated by the parties

#### *Loan from Bental*

On September 7, 2011 TAT received a loan from its subsidiary, Bental, in the total amount of NIS2.5 million (approximately \$0.7 million), to be repaid in whole at the end of a 24 month period (the "Term"). The principle amount bears interest of Prime +1% payable on a quarterly basis and may be repaid at any time during the Term upon TAT's discretion. Simultaneously with such loan, Bental received a loan from an Israeli bank for a similar amount under similar terms and conditions.

#### *Other Transactions*

TAT has commercial relationships in the ordinary course of business, with certain companies that are controlled by KMN Holdings, TAT's indirect controlling shareholder: KMN Trades and Metals, Ika Laboratories Ltd., Alexandrovitzh Ltd. and Haglil Industries Ltd. During fiscal year 2012, TAT purchased from such companies raw materials and services in an aggregate amount of \$348,000, all in arms length transactions.

#### *Other Relationships*

Mr. Itsik Maaravi, TAT's Chief Executive Officer and Mr. Yaron Shalem, TAT's Chief Financial Officer, also serve in the same positions in TAT Industries.

Mr. Maaravi, , TAT's Chief Executive Officer also serves as a director of FAvS.

**C. Interests of Experts and Counsel**

Not applicable.

**Item 8. Financial Information**

**A. Consolidated Statements and Other Financial Information**

See the consolidated financial statements, including the notes thereto, included in Item 18.

**Legal Proceedings**

On November 29, 2011, a Factoring company ("the plaintiff"), filed a claim with the magistrates court in Tel-Aviv against the Company, Bental and ten others ("the respondents"), jointly and severally, for the amount of 6,151 thousand NIS (approximately \$1,620). The plaintiff's case against the Company is based on invoices that were presented to the plaintiff by supplier of the Company ("the supplier"), by virtue of assignment of rights, which were originally issued to the Company by the supplier for certain alleged services. On February 5, 2012 the Company filed for its statement of defense, in which it denied the plaintiff's claims and clarified that it acted according to the deed of assignment of rights, and that the invoices neither represent nor reflect real transactions and/or real services which were rendered. The Company is of the opinion that its exposure due to the claim filed is not probable to be materialized and thus no provision was recorded in regard of that claim of December 31, 2012.

**Dividend Distribution Policy**

The Israel Companies Law also restricts our ability to declare dividends in a way that we can only distribute dividends from profits (as defined in the law), provided that there is no reasonable suspicion that the dividend distribution will prevent us from meeting our existing and future expected obligations as they come due.

**B. Significant Changes**

Since the date of the annual consolidated financial statements included in this annual report, no significant change has occurred.



**Item 9. The Offer and Listing****A. Offer and Listing Details****Annual Stock Information**

The following table sets forth, for each of the years indicated, the high and low sales prices of our Ordinary shares on the NASDAQ Global Market and the TASE:

	NASDAQ Global Market <sup>(1)</sup>		Tel Aviv Stock Exchange	
	High	Low	High	Low
Fiscal Year Ended December 31, 2004	9.80	6.21	—	—
Fiscal Year Ended December 31, 2005	9.35	5.25	NIS 35.50	NIS 29.70
Fiscal Year Ended December 31, 2006	19.52	5.92	82.10	30.25
Fiscal Year Ended December 31, 2007	28.18	11.37	116.70	47.68
Fiscal Year Ended December 31, 2008	12.24	3.62	53.00	15.52
Fiscal Year Ended December 31, 2009	9.13	3.95	33.90	16.53
Fiscal Year Ended December 31, 2010	9.38	5.19	37.36	18.30
Fiscal Year Ended December 31, 2011	6.32	4.20	22.19	15.68
Fiscal Year Ended December 31, 2012	6.05	3.64	23.42	14.81

(1) On June 24, 2009 TAT's Ordinary shares began trading on the NASDAQ Global Market.

## Quarterly Stock Information

The following table sets forth, for each of the full financial quarters in the two most recent full financial years and any subsequent period, the high and low sales prices of our Ordinary shares on the NASDAQ Global Market and the TASE:

	NASDAQ Global Market <sup>(1)</sup>		Tel Aviv Stock Exchange	
	High	Low	High	Low
<b>2011</b>				
First Quarter	5.99	5.20	NIS 20.84	NIS 18.90
Second Quarter	6.08	5.25	20.00	19.01
Third Quarter	6.32	3.67	21.48	18.49
Fourth Quarter	5.55	4.20	19.63	15.68
<b>2012</b>				
First Quarter	4.58	4.12	NIS 17.50	NIS 15.31
Second Quarter	4.80	4.12	17.96	15.26
Third Quarter	4.47	3.64	17.15	14.84
Fourth Quarter	6.04	3.66	23.42	14.81
<b>2013</b>				
First Quarter	7.22	5.58	NIS 26.93	NIS 20.60
Second Quarter (through April 22, 2013)	4.38	4.15	NIS 15.92	NIS 15.37

(1) On June 24, 2009 TAT's Ordinary shares began trading on the NASDAQ Global Market.

## Monthly Stock Information

The following table sets forth, for the most recent six months, the high and low sales prices of our Ordinary shares on the NASDAQ Global Market and the TASE:

	NASDAQ Global Market		Tel Aviv Stock Exchange	
	High	Low	High	Low
October 2012	4.69	3.66	18.21	14.81
November 2012	6.05	5.54	23.02	18.28
December 2012	6.00	5.54	NIS 23.42	NIS 20.58
January 2013	6.38	5.58	23.95	20.60
February 2013	7.22	6.41	26.93	24.38
March 2013	6.75	6.20	24.90	23.39

**B. Plan of Distribution**

Not applicable.

**C. Markets**

Our Ordinary shares are traded on the NASDAQ Global Market under the symbol “TATT”. On August 16, 2005, we listed our shares for trade on the TASE as a dual listed company.

**D. Selling Shareholders**

Not applicable.

**E. Dilution**

Not applicable.

**F. Expense of the Issue**

Not applicable.

**Item 10. Additional Information**

**A. Share Capital**

Not applicable.

**B. Memorandum and Articles of Association**

Set out below is a description of certain provisions of our Memorandum of Association, Articles of Association and of the Israeli Companies Law related to such provisions. This description is only a summary and does not purport to be complete and is qualified by reference to the full text of the Memorandum of Association and Articles of Association, which are incorporated by reference as exhibits to this Annual Report, and to Israeli law.

**Purposes and Objects of the Company**

We are a public company registered with the Israeli Companies Registry and have been assigned company number 52-0035791. Section 2 of our memorandum of association provides that we were established for the purpose of engaging in the business of providing services of planning, development, consultation and instruction in the electronics field. In addition, the purpose of our company is to perform various corporate activities permissible under Israeli law.

On February 1, 2000, the Israeli Companies Law came into effect and superseded most of the provisions of the Israeli Companies Ordinance (New Version), 5743-1983, except for certain provisions which relate to liens, bankruptcy, dissolution and liquidation of companies. Under the Israeli Companies Law, various provisions, some of which are detailed below, overrule the current provisions of our articles of association.

**The Powers of the Directors**

Under the provisions of the Israeli Companies Law which prevails over our Articles of Association in certain issues, a director cannot participate in a meeting nor vote on a proposal, arrangement or contract in which he or she is materially interested except in cases where a majority of the directors are materially interested in the same transaction. In addition, our directors cannot vote compensation to themselves or any members of their body without the approval of our compensation committee and our shareholders at a general meeting, except for certain cases in which there is no need for the approval of the general meeting in accordance with the regulations promulgated under the Israeli Companies Law. See Item 6. "Directors, Senior Management and Employees – Board Practices – Approval of Related Party Transactions Under Israeli Law."

The authority of our directors to enter into borrowing arrangements on our behalf is not limited, except in the same manner as any other transaction by us.

Our articles of association do not impose any mandatory retirement or age-limit requirements on our directors and our directors are not required to own shares in our company in order to qualify to serve as directors.

## Rights Attached to Shares

Our authorized share capital consists of 10,000,000 Ordinary shares of a nominal value of NIS 0.90 each. All outstanding Ordinary shares are validly issued, fully paid and non-assessable.

The rights attached to the Ordinary shares are as follows:

**Dividend rights.** Holders of our Ordinary shares are entitled to the full amount of any cash or share dividend subsequently declared. The board of directors may declare dividends in accordance with the provisions of the Israeli Companies Law as mentioned above. See Item 8.A. “Financial Information – Consolidated and Other Financial Information – Dividend Distribution Policy”. If after one year a dividend has been declared and it is still unclaimed, the board of directors is entitled to invest or utilize the unclaimed amount of dividend in any manner to our benefit until it is claimed. We are not obligated to pay interest or linkage differentials on an unclaimed dividend.

**Voting rights.** Holders of Ordinary shares have one vote for each Ordinary share held on all matters submitted to a vote of shareholders. Such 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.

The quorum required for any meeting of shareholders consists of at least two shareholders present in person or represented by proxy who hold or represent, in the aggregate, at least one third of the voting rights of the issued share capital. A meeting adjourned for lack of a quorum generally is adjourned to the same day in the following week at the same time and place or any time and place as the directors designate in a notice to the shareholders. At the reconvened meeting, the required quorum consists of any two members present in person or by proxy.

Under our Articles of Association, any resolution, including resolutions amending our memorandum of association or articles of association, winding-up, authorization of a class of shares with special rights, or other changes as specified in our Articles of Association, requires approval of the holders of a majority of the voting rights represented at the meeting, in person, by proxy or by written ballot, and voting thereon.

Pursuant to the Israeli Companies Law and our articles of association, our directors (other than outside directors) are elected at our annual general meeting of shareholders by a vote of the holders of a majority of the voting power represented and voting at such meeting and hold office until the next annual general meeting of shareholders and until their successors have been elected. All the members of our Board of Directors (except the outside directors) may be reelected upon completion of their term of office. For information regarding the election of outside directors, see Item 6. “Directors, Senior Management and Employees – Board Practices — Election of Directors.”

***Rights to share in our company's profits.*** Our shareholders have the right to share in our profits distributed as a dividend and any other permitted distribution. See this Item 10B. "Additional Information – Memorandum and Articles of Association – Rights Attached to Shares – Dividend rights."

***Rights to share in surplus in the event of liquidation.*** In the event of our liquidation, after satisfaction of liabilities to creditors, our assets will be distributed to the holders of Ordinary shares in proportion to the nominal value of their holdings. This right may be affected by the grant of preferential dividend or distribution rights to the holders of a class of shares with preferential rights that may be authorized in the future.

***Liability to capital calls by our company.*** Under our memorandum of association and the Israeli Companies Law, the liability of our shareholders is limited to the par value of the shares held by them.

***Limitations on any existing or prospective major shareholder.*** See Item 6. "Directors and Senior Management – Board Practices - Approval of Related Party Transactions Under Israeli Law."

#### **Changing Rights Attached to Shares**

According to our Articles of Association, in order to change the rights attached to any class of shares, unless otherwise provided by the terms of the class, such change must be adopted by a general meeting of the shareholders and by a separate general meeting of the holders of the affected class with a majority of the voting rights represented at the meeting, in person, by proxy or by written ballot, and voting thereon.

#### **Annual and Extraordinary Meetings**

Under the Israeli Companies Law a company must convene an annual meeting of shareholders at least once every calendar year and within fifteen months of the last annual meeting. The agenda of the annual meeting includes discussing the financial statements and the report of the board of directors and may also include the appointment of directors and independent auditors as well as other issues. Depending on the matter to be voted upon, notice of at least 21 days or 35 days prior to the date of the meeting is required. Our board of directors may, in its discretion, convene additional meetings as "special general meetings." With respect to "special general meetings notice of at least 35 days prior to the date of the meeting is required. In addition, the board must convene a special general meeting upon (1) the demand of two of the directors or 25% of the nominated directors, and (2) one or more shareholders having at least 5% of the outstanding share capital and at least 1% of the voting power in the company, or one or more shareholders having at least 5% of the voting power in the company. See Item 10B. "Additional Information - Memorandum and Articles of Association - Rights Attached to Shares - Voting Rights."

**Limitations on the Rights to Own Securities in Our Company**

Neither our memorandum of association or our articles of association nor the laws of the State of Israel restrict in any way the ownership or voting of shares by non-residents, except with respect to subjects of countries which are in a state of war with Israel.

**Provisions Restricting Change in Control of Our Company**

The Israeli Companies Law requires that mergers between Israeli companies be approved by the board of directors and general meeting of shareholders of both parties to the merger transaction. The approval of the board of directors of both companies is subject to such boards' confirmations that there is no reasonable doubt that after the merger the surviving company will be able to fulfill its obligations towards its creditors. Each company must notify its creditors about the contemplated merger. Under the Israeli Companies Law, our Articles of Association are deemed to include a requirement that such merger be approved by an extraordinary resolution of the shareholders, as explained above. The approval of the merger by the general meetings of shareholders of the companies is also subject to additional approval requirements as specified in the Israeli Companies Law and regulations promulgated there under. See also Item 6. "Directors, Senior Management and Employees – Board Practices – Approval of Related Party Transactions Under Israeli Law."

**Disclosure of Shareholders Ownership**

The Israeli Securities Law, 5728-1968 and regulations promulgated there under contain various provisions regarding the ownership threshold above which shareholders must disclose their share ownership. However, these provisions do not apply to companies, such as ours, whose shares are publicly traded in Israel as well on the NASDAQ Global Market. We are required pursuant to the Israeli Securities Law and the regulations promulgated thereunder to submit to the Israeli Securities Authority and the TASE, through a public immediate report, among other things, all information that we receive from our shareholders regarding their shareholdings in our company, provided that such information was published or is required to be published under applicable foreign law.

## Changes in Our Capital

The Board has the right to issue shares. Changes in our capital are subject to the approval of the shareholders at a general meeting by a majority of the voting rights represented at the meeting, in person, by proxy or by written ballot, and voting thereon.

There are no restrictions on the rights of nonresident or foreign shareholders to hold or vote the Ordinary Shares.

### C. Material Contracts

#### *Bental Acquisition*

Following a series of transactions occurring between March 2008 and March 2009, TAT acquired 70% control of Bental. The acquisition of the Bental shares (for an aggregate price of \$9,192) was financed by loans in a total amount of \$6.25 million received from Bank Mizrahi and TAT's internal resources.

#### *Plan of Merger with Limco-Piedmont*

On April 3, 2009 we entered into an Agreement and Plan of Merger with Limco-Piedmont and LIMC Acquisition Company, a Delaware corporation and our wholly-owned subsidiary, pursuant to which we acquired on July 2, 2009, all of the publicly held shares of Common stock of Limco pursuant to a stock for stock merger. Under the terms of the merger agreement, Limco-Piedmont's stockholders received one half of an Ordinary share of TAT for each share of Limco-Piedmont Common stock they own. Following the merger, Limco-Piedmont became our wholly owned subsidiary.

#### *FAvS Transaction*

Pursuant to a Stock Purchase Agreement dated November 9, 2009 with FAvS, TAT's subsidiary, Piedmont, acquired on December 4, 2009, 288,334 shares of Class B Common stock of First Aviation Services Inc., or FAvS, representing 37% of FAvS' then share capital (total number of shares acquired is adjusted as result of a 1 for 20 reverse stock split) and \$750,000 of newly issued shares of Class A Preferred Stock of FAvS (with quarterly dividends at the rate of 12% per annum if paid in cash and 15% per annum if paid in additional shares of Series A Preferred Stock) in exchange for Piedmont's wholly-owned subsidiary, Piedmont Propulsion Systems, which was engaged in the business of providing maintenance, repair and overhaul services for propellers for fixed wing aircraft as well as aircraft parts distribution and trading.



The shares of FAvS Class B Common Stock acquired by Piedmont are non-voting. While Piedmont will have the option, at any time, to convert such shares into shares of Class A Common Stock of FAvS (which have full voting rights), Piedmont has granted to First Equity Group, Inc. ("**FEG**"), a proxy to act for Piedmont in connection with all votes to be taken by the stockholders of FAvS. Mr. Hollander, who is the Chief Executive Officer of FAvS, controls FAvS through his ownership of FEG. The proxy is for a period of five years (subject to earlier termination upon the occurrence of certain events (including an IPO meeting certain criteria, a material default by FAvS under its loan agreement or Mr. Hollander ceasing to serve as Chief Executive Officer of FAvS). In addition, Piedmont and FEG have each agreed not to sell any shares of stock of FAvS for a two-year period commencing on the third anniversary of the closing unless the selling party obtains from the purchaser a proxy (terminating on the fifth anniversary of the closing) in favor of the non-selling party.

Mr. Hollander, FEG and Piedmont also entered into a stockholders agreement which, among other things, restricts each party's ability to dispose of its shares in FAvS and provides for reciprocal rights of first offer, tag along rights and drag along rights. The stockholders agreement also provides that, so long as Piedmont owns at least 10% of the equity of FAvS, it shall have the right to have two designees serve on the six-member Board of Directors of FAvS. Piedmont and FAvS have additionally entered into a rights agreement pursuant to which, among other things, FAvS granted to Piedmont pre-emptive rights, information and access rights and the right to approve certain material corporate actions. The stockholders agreement and rights agreement were amended on June 30, 2011 in connection with the settlement of the dispute described further below.

Piedmont agreed to guaranty \$7 million of the debt incurred by FAvS in connection with the AeTR acquisition by providing a letter of credit to the lender for FAvS. The guaranty was for a period of up to two years and reduced as such debt amortized. Piedmont was granted a second lien on the assets of FAvS to secure the repayment obligations of FAvS in the event the letter of credit is drawn upon. Piedmont also entered into an intercreditor agreement with the lender to FAvS which subordinated Piedmont's claims if the letter of credit is drawn upon to the obligations of FAvS to the lender.

On October 1, 2010, Piedmont agreed to secure the guarantee for \$6.6 million, by providing a new letter of credit to the lender for FAvS. Such guaranty was for a period of 15 months ending December 31, 2011 and its amount was reduced as such debt amortizes in increments of \$0.1 million per month. Piedmont was also granted a second lien on the assets of FAvS to secure the repayment obligations of FAvS in the event that the letter of credit is drawn upon. Piedmont also entered into an intercreditor agreement with the lender to FAvS which subordinated Piedmont's claims if the letter of credit is drawn upon to the obligations of FAvS to the lender.

FAvS and Piedmont also entered into a one-year services agreement pursuant to which Piedmont provided certain finance, human resources, IT and quality control services to FAvS and a multi-year services agreement pursuant to which a subsidiary of Piedmont provides certain plating, machining and grinding services to FAvS.

A commercial dispute arose between Piedmont and FAvS relating to the propeller maintenance business which had been contributed to FAvS by Piedmont as part of the transaction discussed above. The commercial dispute began in April 2010 when a customer of the propeller maintenance business requested reimbursement from FAvS for damages to certain propellers. FAvS then sought reimbursement from Piedmont for such amounts. Although Piedmont rejected all of FAvS' claims with regards to Piedmont's responsibility for the claimed damages, the parties reached an agreement pursuant to which Piedmont loaned \$700,000 to FAvS and agreed to bear a portion of the additional cost of the replacement of propeller blades that FAvS would be responsible for. In exchange FAvS agreed to waive all claims against Piedmont with respect to such customer. Such loan was subsequently forgiven.

Notwithstanding such waiver, in the last quarter of 2010, FAvS again asserted claims against Piedmont relating to the propeller maintenance business, including claims not previously asserted. After reviewing this issue during the 2010 fourth quarter and thereafter, the company estimated the additional liability it may bear and accordingly wrote off the payment and recorded an accrual, which it believed, covered its potential cost in connection with this matter.

In order to finally settle all disputes between them, on June 30, 2011 Piedmont and FAvS entered into a Settlement Agreement and Release (the "Settlement Agreement"). Pursuant to the Settlement Agreement, each party fully released the other party and acknowledged that the settlement was a compromise of disputed claims and was not to be construed as an admission of liability or wrongdoing. In addition, each party agreed not to disparage the other and Piedmont paid an aggregate of \$700,000 to FAvS.

Simultaneously with the execution of the Settlement Agreement, Mr. Hollander, the Chief Executive Officer and controlling stockholder of FAvS, purchased 166,113 shares of Class A Common Stock of FAvS at a price of \$18.06 per share (for an aggregate price of \$3 million). In addition, Piedmont agreed to extend its guarantee of the bank debt incurred by FAvS to fund the AeTR transaction through June 30, 2013 and to continue to provide a letter of credit to secure such guarantee. The amortization schedule for such debt was revised so that no amortization will occur until June 30, 2012. Thereafter the debt amortized at the rate of \$200,000 per month. The guarantee was terminated on March 2013, see below.

The Stockholders Agreement entered into in 2009 between Piedmont and Mr. Hollander was also amended to delete the reciprocal drag along rights and to provide that Piedmont may designate one member to the Board of Directors of FAvS (rather than the two provided in the original agreement). Finally, the Rights Agreement entered into in 2009 between Piedmont and FAvS was amended so that Piedmont's right to approve certain material corporate actions by FAvS has been limited to the right to approve contracts or agreements with affiliates of FAvS. The amendment also provides that the approval of Piedmont will not be required if FAvS seeks to raise additional capital from Mr. Hollander so long as the consideration being paid by Mr. Hollander is not less than the consideration that would be paid by a third-party in an arms-length transaction and is fair, equitable and reasonable under the circumstances.

In connection with the Settlement Agreement and the dilution in Piedmont's interest in FAvS, the Company recorded, at June 30, 2011, a gain in the amount of \$0.24 million related to the \$3 million capital investment in FAvS by Mr. Hollander.

In June, 2012, FAvS entered into a transaction with Mr. Hollander, pursuant to which FAvS borrowed \$3 million from Mr. Hollander, secured by a third lien on the assets of FAvS. The loan bears interest at 10% and in addition Mr. Hollander was issued warrants to purchase shares of Class A Common Stock of FAvS, representing 15% of FAvS post-exercise shareholders' equity, at an exercise price of \$7.00 per share.

Pursuant to the terms and conditions of the transaction, management believed that there were indicators of impairment with respect to TAT's investment in FAvS. Accordingly, the Company performed an impairment test of its investment in FAvS, with the assistance of a third party valuation. Based on the results of this test the Company determined that its investment in FAvS was impaired by \$3.3 million. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels which related to the business of API, one of FAvS subsidiaries, and approximates TAT's share in the loss resulting from the API Transaction discussed below.

On March 18, 2013 FAvS sold 97% of the stock of API for a total purchase price of \$16.5 million, of which \$15.9 million was used to repay debt (the “API Transaction”). The sale resulted in FAvS retaining a 3% equity interest in the API business. The API transaction resulted in a loss from discontinued operations and write-down of the API business of \$11.5 million which is included in the FAvS loss for the year ended December 31, 2012. Simultaneously with the transaction FAvS paid-off its Term Loan in the amount of \$4 million thereby terminating the guarantee and releasing the Letter of Credit provided by TAT to secure such guarantee. Accordingly the restricted deposit associated with the above Letter of Credit, was released as well.

*Market Maker (TASE) Agreement*

On August 15, 2011, TAT entered into a Market Making agreement for its shares traded on the Tel Aviv Stock Exchange (TASE) with Harel Finance Trade & Securities Ltd. for the purpose of improving liquidity of TAT shares. The agreement is for a 12 month period, subject for TASE’s approval. The agreement will be automatically extended in 12 month periods, unless otherwise terminated by either of the parties giving 30 days notice or in accordance with certain regulatory circumstances. TAT will pay an immaterial fee in connection with the said agreement.

**D. Exchange Controls**

Israeli law and regulations do not impose any material foreign exchange restrictions on non-Israeli holders of our Ordinary shares. In May 1998, a new “general permit” was issued under the Israeli Currency Control Law, 1978, which removed most of the restrictions that previously existed under such law, and enabled Israeli citizens to freely invest outside of Israel and freely convert Israeli currency into non-Israeli currencies.

Non-residents of Israel who purchase our Ordinary shares will be able to convert dividends, if any, thereon, and any amounts payable upon our dissolution, liquidation or winding up, as well as the proceeds of any sale in Israel of our Ordinary shares to an Israeli resident, into freely repatriable dollars, at the exchange rate prevailing at the time of conversion, provided that the Israeli income tax has been withheld (or paid) with respect to such amounts or an exemption has been obtained.

## **E. Taxation**

The following is a discussion of Israeli and United States tax consequences material to our shareholders. To the extent that the discussion is based on new tax legislation which has not been subject to judicial or administrative interpretation, the views expressed in the discussion might not be accepted by the tax authorities in question. The discussion is not intended, and should not be construed, as legal or professional tax advice and does not exhaust all possible tax considerations.

You are urged to consult your own tax advisor as to the Israeli, United States and other tax consequences of the purchase, ownership and disposition of our Ordinary shares, including, in particular, the effect of any non-Israeli, state or local taxes.

### **Israeli Tax Considerations**

The following is a summary of the principal Israeli tax laws applicable to us, of the Israeli Government programs from which we benefit and of the Income Tax Law (Inflationary Adjustments), 1985. This section also contains a discussion of material Israeli tax consequences to our shareholders who are not residents or citizens of Israel. This summary does not discuss all aspects of Israeli tax law that may be relevant to a particular investor in light of his or her personal investment circumstances, or to some types of investors subject to special treatment under Israeli law. Examples of investors subject to special treatment under Israeli law include residents of Israel, traders in securities, or persons who own, directly or indirectly, 10% or more of our outstanding voting capital, all of whom are subject to special tax regimes not covered in this discussion. Some parts of this discussion are based on new tax legislation that has not been subject to judicial or administrative interpretation. The discussion should not be construed as legal or professional tax advice and does not cover all possible tax consequences.

### **General Corporate Tax Structure**

Israeli companies were generally subject to corporate tax at the rate of 25% in 2010, which was reduced to 24% in 2011, and was due to further gradually reduced to 18% in 2016 and thereafter. On December 5, 2011, the Knesset (Israel's Parliament) passed a law for changing the tax burden (Legislative Amendments), which cancels, among others, the gradual reduction in the corporate tax rates in Israel. In addition, the corporate tax in Israel increased to 25% starting in 2012.

However, the rate is effectively reduced for income derived from an approved enterprise and beneficiary enterprise, as discussed below.

We do not expect that the October 2011 Amendment to have a material effect on the tax payable in respect of its Israeli operations.

#### **Tax Benefits under the Law for the Encouragement of Capital Investments, 1959**

We have one capital investment program that has been granted "approved enterprise" status under the Law for the Encouragement of Capital Investments, 1959, commonly referred to as the Investment Law, and one program that qualify as a "beneficiary enterprise" pursuant to an amendment to the Investment Law that came into effect on April 1, 2005. These programs were waived as part of the "Preferred enterprise" which is part of the "2011 Amendment" mentioned below.

Prior to the April 2005 amendment, the Investment Law provided that capital investments in a production facility (or other eligible assets) may be designated as an approved enterprise upon prior approval from the Investment Center of the Israel Ministry of Industry, Trade and Labor, or the Investment Center.

On April 1, 2005, an amendment to the Investment Law came into effect, which revised the criteria for investments qualified to receive tax benefits. An eligible investment program under that amendment provided for benefits as a beneficiary enterprise (rather than the previous terminology of approved enterprise). Among other things, the April 2005 amendment provided tax benefits to both local and foreign investors. Companies that meet the specified criteria received the tax benefits without need for prior approval and instead, a company was to claim the tax benefits offered by the Investment Law directly in its tax returns.

The period of tax benefits for the then new beneficiary enterprise commences in the year that is the later of: (i) the year in which taxable income is first generated by a company, or (ii) a year selected by the company for commencement, on the condition that the company meets certain provisions provided by the Investment Law. The amendment does not apply to investment programs approved prior to December 31, 2004 and applies only to new investment programs. We began to generate income under the provision of the new amendment as of the beginning of 2006.

After expiration of the initial tax exemption period, the company is eligible for what was considered then a reduced corporate tax rate of 10% to 25% for the following five to eight years, depending on the extent of foreign investment in the company. The benefits period was limited to 12 years from completion of the investment under the approved plan or 14 years from the date of the approval, whichever is earlier. A company in which more than 25% of the shareholders are non-residents of Israel, defined under the Investment Law as a Foreign Investors Company, may be eligible for benefits for an extended period of up to ten years.

If a company distributes dividends from tax-exempt approved enterprise and/or beneficiary enterprise income, the company will be taxed on the otherwise exempt income at the same reduced corporate tax rate that applies to it after the initial exemption period. Distribution of dividends derived from approved enterprise and beneficiary enterprise income that was taxed at reduced rates, but not tax exempt, does not result in additional tax consequences to the company. Shareholders who receive dividends derived from approved enterprise and beneficiary enterprise income are generally taxed at a rate of 15%, which is withheld and paid by the company paying the dividend, if the dividend is distributed during the benefits period or within the following 12 years.

The benefits available to an approved enterprise and beneficiary enterprise were conditioned upon terms stipulated in the Investment Law and the related regulations (which include making specified investments in property and equipment, and financing a percentage of these investments with share capital), and, for an approved enterprise, the conditions contained in the certificate of approval from the Investment Center. If we do not fulfill these conditions, in whole or in part, the benefits can be cancelled and we may be required to refund the amount of the benefits, linked to the Israeli consumer price index plus interest. We believe that our approved enterprise and beneficiary enterprise programs currently operate in compliance with all applicable conditions and criteria, but we cannot assure you that they will continue to do so.

We have derived, a material portion of our operating income from our approved enterprise and beneficiary enterprise facilities. We were therefore eligible for a tax exemption for a limited period on undistributed approved enterprise and beneficiary enterprise income. We intend to reinvest the entire amount of our tax-exempt income and not to distribute this income as a dividend.

#### **Tax Benefits and Grants for Research and Development**

Israeli tax law allows, under specific conditions, a tax deduction in the year incurred for expenditures, including capital expenditures, relating to scientific research and development projects, if the expenditures are approved by the relevant Israeli government ministry, determined by the field of research, and the research and development is for the promotion of the company and is carried out by or on behalf of the company seeking such deduction. Expenditures not so approved are deductible over a three-year period. However, expenditures from proceeds made available to us through government grants are not deductible according to Israeli law.

#### **Tax Benefits under the Law for the Encouragement of Industry (Taxes), 1969**

According to the Law for the Encouragement of Industry (Taxes), 1969, or the Industry Encouragement Law, an Industrial Company is a company resident in Israel, at least 90% of the income of which, in a given tax year, determined in Israeli currency (exclusive of income from some government loans, capital gains, interest and dividends), is derived from an industrial enterprise owned by it. An “industrial enterprise” is defined as an enterprise whose major activity in a given tax year is industrial production activity.

Under the Industry Encouragement Law, Industrial Companies are entitled to the following preferred corporate tax benefits:

- Amortization of purchases of acquired technology and patents over an eight-year period for tax purposes;
- Amortization of specified expenses incurred in connection with a public issuance of securities over a three-year period for tax purposes;
- Right to elect, under specified conditions, to file a consolidated tax return with additional related Israeli Industrial Companies; and
- Accelerated depreciation rates on equipment and buildings.

Eligibility for benefits under the Industry Encouragement Law is not subject to receipt of prior approval from any governmental authority.



Additional amendments to the Approved Enterprise Law became effective in January 2011 (the “2011 Amendment”). Under the 2011 Amendment, income derived by ‘Preferred Companies’ from ‘Preferred Enterprises’ (both as defined in the 2011 Amendment) would be subject to a uniform rate of corporate tax as opposed to previous years’ incentives that were limited to income from Approved or Benefiting Enterprises during their benefits period. According to the 2011 Amendment, the uniform tax rate on such income, referred to as ‘Preferred Income’, would be 10% in areas in Israel that are designated as Development Zone A and 15% elsewhere in Israel during 2011-2012, 7% and 12.5%, respectively, in 2013-2014, and 6% and 12%, respectively, thereafter. Income derived by a Preferred Company from a ‘Special Preferred Enterprise’ (as defined in the Approved Enterprise) would enjoy further reduced tax rates for a period of ten years of 5% in Zone A and 8% elsewhere. As with dividends distributed from taxable income derived from an Approved Enterprise or Benefiting Enterprise during the applicable benefits period, dividends distributed from Preferred Income would be subject to a 15% tax (or lower, if so provided under an applicable tax treaty), which would generally be withheld by the distributing company. While the Company may incur additional tax liability in the event of distribution of dividends from tax exempt income generated from its Approved and Benefiting Enterprises, no additional tax liability will be incurred by the Company in the event of distribution of dividends from income taxed in accordance with the 2011 Amendment.

Under the transitional provisions of the 2011 Amendment, the Company elects to irrevocably implement the 2011 Amendment with respect to its existing Approved and Benefiting Enterprises while waiving benefits provided under the legislation prior to the 2011 Amendment.

We cannot assure you that we will continue to qualify as an Industrial Company or that the benefits described above will be available to us in the future, which would entail the loss of the benefits that relate to this status.

#### **Special Provisions Relating to Taxation under Inflationary Conditions**

The Income Tax Law (Inflationary Adjustments), 1985, referred to as the Inflationary Adjustments Law, which attempts to overcome the problems presented to a traditional tax system by an economy undergoing rapid inflation. The Inflationary Adjustments Law is highly complex.

On February 26, 2008, the Israeli Parliament (the Knesset) enacted the Income Tax Law (Inflationary Adjustments) (Amendment No. 20) (Restriction of Effective Period), 2008, which we refer to as the Inflationary Adjustments Amendment. In accordance with the Inflationary Adjustments Amendment, the effective period of the Inflationary Adjustments Law will cease at the end of the 2007 tax year and as of the 2008 tax year the provisions of the law shall no longer apply, other than the transitional provisions intended at preventing distortions in the tax calculations. In accordance with the Inflationary Adjustments Amendment, commencing the 2008 tax year, income for tax purposes will no longer be adjusted to a real (net of inflation) measurement basis. Furthermore, the depreciation of inflation immune assets and carried forward tax losses will no longer be linked to the Israeli consumer price index.

## **Taxation of Dividends Paid on our Ordinary Shares**

### *Taxation of Israeli Shareholders*

Israeli resident individuals are generally subject to Israeli income tax on the receipt of dividends paid on our Ordinary shares, other than bonus shares (share dividends) or stock dividends, at the rate of 20%, or 25% for a shareholder that is considered a material shareholder (within the meaning of the Israeli Income Tax Ordinance) at any time during the 12-month period preceding such distribution. Dividends paid on our Ordinary shares to Israeli companies are exempt from such tax, except for dividends distributed from income derived outside of Israel, which are subject to the 25% tax rate.

Dividends paid from income derived from any of our approved enterprises or beneficiary enterprises are subject to tax, which is withheld at the source, at the rate of 15%, although we cannot assure you that we will designate the profits that are being distributed in a way that will reduce shareholders' tax liability to this tax rate.

### *Taxation of Non-Israeli Shareholders*

Non-residents of Israel are subject to Israeli income tax on income accrued or derived from sources in Israel, including passive income such as dividends. As of January 1, 2012, on distributions of dividends by an Israeli company to non Israeli shareholders, other than bonus shares and stock dividends, income tax is applicable at the rate of 25%, or 30% for a shareholder that is considered a significant shareholder at any time during the 12-month period preceding such distribution, unless a different rate is provided in a treaty between Israel and the shareholder's country of residence. As aforesaid, dividends of income generated by an Approved Enterprise (or Benefited Enterprise) are subject to withholding tax at a rate of 15%.

Under the U.S.-Israel Tax Treaty, the maximum tax on dividends paid to a holder of shares who is a treaty U.S. resident is 25%, or 15% if the dividends are generated by an Approved Enterprise (or Benefited Enterprise). However, if the income out of which the dividend is being paid is not attributable to an Approved Enterprise (or Benefited Enterprise) and not more than 25% of our gross income consists of interest or dividends, then such tax rate is reduced to 12.5% for a non-resident that is a U.S. corporation and holds 10% or more of our issued voting power during the part of the tax year that precedes the date of payment of the dividend and during the whole of its prior tax year.

#### Capital gains taxes applicable to non-Israeli shareholders

Capital gains from the sale of our Ordinary shares by non-Israeli shareholders are exempt from Israeli taxation, provided that the capital gain is not derived from a permanent establishment in Israel. In addition, the U.S.-Israel tax treaty exempts U.S. residents who hold less than 10% of our voting rights, and who held less than 10% of our voting rights during the 12 months prior to a sale of their shares, from Israeli capital gains tax in connection with such sale.

#### UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

*The following discussion summarizes the material U.S. federal income tax considerations generally applicable to the purchase, ownership and disposition of our Ordinary shares. Unless otherwise stated, this summary deals only with shareholders that are U.S. Holders (as defined below) who hold their Ordinary shares as capital assets.*

As used in this section, the term “U.S. Holder” means a beneficial owner of an Ordinary share who is:

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

The term “Non-U.S. Holder” means a beneficial owner of an Ordinary share that is an individual, corporation, estate or trust and is not a U.S. Holder. The tax consequences to a Non-U.S. Holder may differ substantially from the tax consequences to a U.S. Holder. Certain aspects of U.S. federal income tax relevant to a Non-U.S. Holder are discussed below.

This description is based on provisions of the U.S. Internal Revenue Code of 1986, as amended (the "Code"), existing and proposed U.S. Treasury regulations promulgated thereunder, administrative and judicial interpretations thereof, and the US-Israel Tax Treaty, each as in effect as of the date of this prospectus. These sources may change, possibly with retroactive effect, and are open to differing interpretations. This description does not discuss all aspects of U.S. federal income taxation that may be applicable to investors in light of their particular circumstances or to investors who are subject to special treatment under U.S. federal income tax law, including:

- Insurance companies;
- Dealers in stocks, securities or currencies;
- Financial institutions and financial services entities;
- Real estate investment trusts;
- Regulated investment companies;
- Persons that receive Ordinary shares in connection with the performance of services;
- Tax-exempt organizations;
- Persons that hold Ordinary shares as part of a straddle or appreciated financial position or as part of a hedging, conversion or other integrated instrument;
- Persons who hold the Ordinary shares through partnerships or other pass-through entities;
- Individual retirement and other tax-deferred accounts;
- Expatriates of the United States and certain former long-term residents of the United States;
- Persons liable for the alternative minimum tax;
- Persons having a "functional currency" other than the U.S. dollar; and
- Direct, indirect or constructive owners of 10% or more, by voting power or value, of our company.

If a partnership or an entity treated as a partnership for U.S. federal income tax purposes owns Ordinary shares, the U.S. federal income tax treatment of a partner in such a partnership will generally depend upon the status of the partner and the activities of the partnership. A partnership that owns Ordinary shares and the partners in such partnership should consult their tax own advisors about the U.S. federal income tax consequences of holding and disposing of Ordinary shares.

This discussion does not consider the possible application of U.S. federal gift or estate tax or alternative minimum tax.

All investors are urged to consult their own tax advisors as to the particular tax consequences to them of an investment in our Ordinary shares, including the effect and applicability of United States federal, state, local and foreign income and other tax laws (including estate and gift tax laws) and tax treaties.

**Distributions Paid on the Ordinary Shares**

Subject to the discussion below under “Passive Foreign Investment Company Considerations,” a U.S. Holder generally will be required to include in his or her gross income as ordinary dividend income the amount of any distributions paid on the Ordinary shares, including the amount of any Israeli taxes withheld, to the extent that those distributions are paid out of our current or accumulated earnings and profits, as determined for U.S. federal income tax purposes. Subject to the discussion below under “Passive Foreign Investment Company Considerations,” distributions in excess of our earnings and profits will be applied against and will reduce the U.S. Holder’s tax basis in its Ordinary shares and, to the extent they exceed that tax basis, will be treated as gain from a sale or exchange of those Ordinary shares. Our dividends will not qualify for the dividends-received deduction applicable in some cases to U.S. corporations.

Dividends that we pay in NIS, including the amount of any Israeli taxes withheld therefrom, will be included in your income in a U.S. dollar amount calculated by reference to the exchange rate in effect on the day such dividends are received, regardless of whether the payment is in fact converted into U.S. dollars. A U.S. Holder who receives payment in NIS and converts NIS into U.S. dollars at an exchange rate other than the rate in effect on such day will have a foreign currency exchange gain or loss that would be treated as ordinary income or loss. U.S. Holders should consult their own tax advisors concerning the U.S. tax consequences of acquiring, holding and disposing of NIS.

Subject to certain limitations, “qualified dividend income” received by a noncorporate U.S. Holder in tax years beginning on or before December 31, 2010 will be subject to tax at a reduced maximum tax rate of 15%. Distributions taxable as dividends paid on the Ordinary shares should qualify for the 15% rate provided that we are not a passive foreign investment company (as described below) for U.S. tax purposes and that either: (i) we are entitled to benefits under the income tax treaty between the United States and Israel (the “U.S.-Israel Tax Treaty”) or (ii) the Ordinary shares are readily tradable on an established securities market in the United States and certain other requirements are met. We believe that we are entitled to benefits under the U.S.-Israel Tax Treaty and that the Ordinary shares currently will be readily tradable on an established securities market in the United States. However, no assurance can be given that the Ordinary shares will remain readily tradable. The rate reduction does not apply unless certain holding period requirements are satisfied. With respect to the Ordinary shares, the U.S. Holder must have held such shares for at least 61 days during the 121-day period beginning 60 days before the ex-dividend date. The rate reduction also does not apply to dividends received from passive foreign investment companies, see discussion below, or in respect of certain hedged positions or in certain other situations. The legislation enacting the reduced tax rate contains special rules for computing the foreign tax credit limitation of a taxpayer who receives dividends subject to the reduced tax rate. U.S. Holders of Ordinary shares should consult their own tax advisors regarding the effect of these rules in their particular circumstances.

Subject to the discussion below under “Information Reporting and Back-up Withholding,” a Non-U.S. Holder generally will not be subject to U.S. federal income or withholding tax on dividends received on Ordinary shares unless that income is effectively connected with the conduct by that Non-U.S. Holder of a trade or business in the United States, in which case a corporate Non-U.S. Holder may also be subject to the U.S. branch profits tax.

#### **Foreign Tax Credit**

Any dividend income resulting from distributions we pay to a U.S. Holder with respect to the Ordinary shares generally will be treated as foreign source income for U.S. foreign tax credit limitation purposes. Subject to certain conditions and limitations, Israeli tax withheld on dividends may be deducted from taxable income or credited against a U.S. Holder’s U.S. federal income tax liability. The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For this purpose, any dividend that we distribute generally will constitute “passive category income,” or, in the case of certain U.S. Holders, “general category income.” The rules relating to the determination of foreign source income and the foreign tax credit are complex, and the availability of a foreign tax credit depends on numerous factors. Each investor who is a U.S. Holder should consult with its own tax advisor to determine whether its income with respect to the Ordinary shares would be foreign source income and whether and to what extent that investor would be entitled to a foreign tax credit.

## **Disposition of Ordinary Shares**

Upon the sale or other disposition of Ordinary shares, subject to the discussion below under “Passive Foreign Investment Company Considerations,” a U.S. Holder generally will recognize capital gain or loss equal to the difference between the amount realized on the disposition and the holder’s adjusted tax basis in the Ordinary shares. U.S. Holders should consult their own advisors with respect to the tax consequences of the receipt of a currency other than U.S. dollars upon such sale or other disposition.

Gain or loss upon the disposition of the Ordinary shares will be treated as long-term if, at the time of the sale or disposition, the Ordinary shares were held for more than one year. The deductibility of capital losses by a U.S. Holder is subject to limitations. In general, any gain or loss recognized by a U.S. Holder on the sale or other disposition of Ordinary shares will be U.S. source income or loss for U.S. foreign tax credit purposes. U.S. Holders should consult their own tax advisors concerning the source of income for U.S. foreign tax credit purposes and the effect of the U.S.-Israel Tax Treaty on the source of income.

Subject to the discussion below under “Information Reporting and Back-up Withholding,” a Non-U.S. Holder generally will not be subject to U.S. federal income or withholding tax on any gain realized on the sale or exchange of Ordinary shares unless:

- that gain is effectively connected with the conduct by the Non-U.S. Holder of a trade or business in the United States, and, if a tax treaty applies, is attributable to a permanent establishment or fixed base of the Non-U.S. Holder in the United States; or
- in the case of any gain realized by an individual Non-U.S. Holder, that holder is present in the United States for 183 days or more in the taxable year of the sale or exchange, and other conditions are met.

## **Passive Foreign Investment Company Considerations**

Special U.S. federal income tax rules apply to U.S. Holders owning shares of a passive foreign investment company. A non-U.S. corporation will be considered a passive foreign investment company for any taxable year in which, after applying certain look-through rules, 75% or more of its gross income consists of specified types of passive income, or 50% or more of the average value of its assets consists of assets that 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.

If we were classified as a passive foreign investment company, a U.S. Holder could be subject to increased tax liability upon the sale or other disposition of Ordinary shares or upon the receipt of amounts treated as “excess distributions.” Under these rules, the excess distribution and any gain would be allocated ratably over the U.S. Holder’s holding period for the Ordinary shares, and the amount allocated to the current taxable year and any taxable year prior to the first taxable year in which we were a passive foreign investment company would be taxed as ordinary income. The amount allocated to each of the other taxable years would be subject to tax at the highest marginal tax rate in effect for the applicable class of taxpayer for that year, and an interest charge for the deemed deferral benefit would be imposed on the resulting tax allocated to such other taxable years. The tax liability with respect to the amount allocated to years prior to the year of the disposition, or “excess distribution,” cannot be offset by any net operating losses. In addition, holders of stock in a passive foreign investment company may not receive a “step-up” in basis on shares acquired from a decedent. If we are a passive foreign investment company in any year, a U.S. Holder would be required to file an annual return on IRS Form 8621 regarding distributions received with respect to Ordinary shares and any gain realized on the disposition of Ordinary shares.

Based on our current and projected income, assets and activities, we do not believe that we will be a passive foreign investment company for our current taxable year. However, because the determination of whether we are a passive foreign investment company is based upon the composition of our income and assets from time to time, we cannot be certain that we will not be considered a passive foreign investment company for the current taxable year or any future taxable year.

The passive foreign investment company tax consequences described above will not apply to a U.S. Holder if the U.S. Holder makes an election to treat us as a qualified electing fund, or QEF. If a U.S. Holder makes a timely QEF election, the U.S. Holder would be required to include in income for each taxable year its pro rata share of our ordinary earnings as ordinary income and its pro rata share of our net capital gain as long-term capital gain, whether or not such amounts are actually distributed to the U.S. Holder. However, a U.S. Holder would not be eligible to make a QEF election unless we comply with certain applicable information reporting requirements. We will provide U.S. Holders with the information needed to report income and gain under a QEF election should we become a passive foreign investment company.



As an alternative to making a QEF election, a U.S. Holder of passive foreign investment company stock which is publicly traded may in certain circumstances avoid certain of the tax consequences generally applicable to holders of a passive foreign investment company by electing to mark the stock to market annually and recognizing as ordinary income or loss each year an amount equal to the difference as of the close of the taxable year between the fair market value of the passive foreign investment company stock and the U.S. Holder's adjusted tax basis in the passive foreign investment company stock. Losses would be allowed only to the extent of net mark-to-market gain previously included by the U.S. Holder under the election for prior taxable years. Income recognized and deductions allowed under the mark-to-market provisions, as well as any gain or loss on the disposition of Ordinary shares with respect to which the mark to market election is made, are generally treated as ordinary income or loss (except that loss is treated as capital loss to the extent the loss exceeds the net mark-to-market gains, if any, that a U.S. Holder included in its income with respect to such Ordinary shares in prior years). However, gain or loss from the disposition of Ordinary shares (as to which a "mark-to-market" election was made) in a year in which we are no longer a passive foreign investment company, will be capital gain or loss. The mark-to-market election is available for so long as our Ordinary shares constitute "marketable stock," which includes stock of a passive foreign investment company that is "regularly traded" on a "qualified exchange or other market." Generally, a "qualified exchange or other market" includes a national securities exchange that is registered with the Securities and Exchange Commission or the national market system established pursuant to Section 11A of the Securities Exchange Act of 1934. A class of stock that is traded on one or more qualified exchanges or other markets is "regularly traded" on an exchange or market for any calendar year during which that class of stock is traded, other than in the minimized quantities, on at least 15 days during each calendar quarter. We believe that The NASDAQ Global Market will constitute a qualified exchange or other market for this purpose. However, we can not be certain that our Ordinary shares will continue to trade on The NASDAQ Global Market or that the Ordinary shares will be regularly traded for this purpose.

The rules applicable to owning shares of a passive foreign investment company are complex, and each holder who is a U.S. Holder should consult with its own tax advisor regarding the consequences of investing in a passive foreign investment company.

#### **Information Reporting and Backup Withholding**

Payments in respect of Ordinary shares may be subject to information reporting to the U.S. Internal Revenue Service and to U.S. backup withholding tax at a rate equal to the fourth lowest income tax rate applicable to individuals (which, under current law, is 28%). Backup withholding will not apply, however, if you (i) are a corporation or come within certain exempt categories, and demonstrate the fact when so required, or (ii) furnish a correct taxpayer identification number and make any other required certification. U.S. Holders who are required to establish their exempt status generally must provide such certification on IRS Form W-9.

Backup withholding is not an additional tax. Amounts withheld under the backup withholding rules may be credited against a U.S. Holder's U.S. tax liability, and a U.S. Holder may obtain a refund of any excess amounts withheld under the backup withholding rules by filing the appropriate claim for refund with the IRS.

Any U.S. holder who holds 10% or more in vote or value of our Ordinary shares will be subject to certain additional United States information reporting requirements.

**U.S. Gift and Estate Tax**

An individual U.S. Holder of Ordinary shares will generally be subject to U.S. gift and estate taxes with respect to Ordinary shares in the same manner and to the same extent as with respect to other types of personal property.

**F. Dividends and Paying Agents**

Not applicable.

**G. Statement by Experts**

Not applicable.

**H. Documents on Display**

We are subject to the reporting requirements of the United States Securities Exchange Act of 1934, as amended, as applicable to "foreign private issuers" as defined in Rule 3b-4 under the Exchange Act, and in accordance therewith, we file annual and interim reports and other information with the Securities and Exchange Commission.

As a foreign private issuer, we are exempt from certain provisions of the Exchange Act. Accordingly, our proxy solicitations are not subject to the disclosure and procedural requirements of Regulation 14A under the Exchange Act and transactions in our equity securities by our officers and directors are exempt from reporting and the “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 as frequently or as promptly as United States companies whose securities are registered under the Exchange Act. However, we make available on our website [www.tat-technologies.com](http://www.tat-technologies.com), our annual audited financial statements, which have been examined and reported on, with an opinion expressed by, an independent public accounting firm, and we intend to file reports with the Securities and Exchange Commission on Form 6-K containing unaudited financial information for the first three quarters of each fiscal year.

This annual report on Form 20-F and the exhibits thereto and any other document we file pursuant to the Exchange Act may be inspected without charge and copied at prescribed rates at the following Securities and Exchange Commission public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549; and on the Securities and Exchange Commission Internet site (<http://www.sec.gov>) and on our website [www.tat-technologies.com](http://www.tat-technologies.com). You may obtain information on the operation of the Securities and Exchange Commission’s public reference room in Washington, D.C. by calling the Securities and Exchange Commission at 1-800-SEC-0330. The Exchange Act file number for our Securities and Exchange Commission filings is 0-16050.

In addition, since August 16, 2005 we are also listed on the TASE. From such date we submit copies of all our filings with the SEC to the Israeli Securities Authority and TASE. Such copies can be retrieved electronically through the TASE internet messaging system ([www.maya.tase.co.il](http://www.maya.tase.co.il)) and, in addition, through the MAGNA distribution site of the Israeli Securities Authority ([www.magna.isa.gov.il](http://www.magna.isa.gov.il)).

The documents concerning our company which are referred to in this annual report may also be inspected at our offices located at Re'em Industrial Park Neta, Boulevard Bnei Ayish, Gedera, Israel.

**I. Subsidiary Information**

Not applicable.

**Item 11. Quantitative and Qualitative Disclosures about Market Risk**

We do not own and have not issued any market risk sensitive instruments about which disclosure is required to be provided pursuant to this Item.

#### Effects of Changes in Interest Rates

We pay interest on our long-term loans facilities in accordance with the nature of each loan. For loans that bear Libor Rate, we pay interest at a rate per annum equal to up to 3.5% in excess of the Libor Rate. As a result, changes in the general level of interest rates directly affect the amount of interest payable by us under these facilities. For loans that bear fixed interest rate, we pay interest at a rate per annum equal to up to 5.25%. As of December 31, 2012 we do not have any loans that linked to the Consumer Price Index (the “CPI”).

#### Effects of Currency Exchange Fluctuations

Our financial statements are stated in dollars, while a portion of our expenses, primarily labor expenses, is incurred in NIS and a part of our revenues are quoted in NIS. Additionally, certain assets, as well as a portion of our liabilities, are denominated in NIS. As a result, our operations may be affected by fluctuations of the U.S. dollar/NIS exchange rate. In 2012, the NIS appreciated against the U.S. dollar by 2.3%, while in 2011 the NIS depreciated against the U.S. dollar by 7.7%. We estimate that a devaluation of 1% of the U.S. dollar against the NIS would result in a decrease of approximately \$150,000 in our operating income.

#### Item 12. Description of Securities Other than Equity Securities

Not Applicable.

#### PART II

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

None.

#### Item 14. Material Modifications to the Rights of Security Holders

None.

**Item 15. Controls and Procedures**

Not applicable.

**Item 15T. Controls and Procedures**

**Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in its Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our chief executive officer and chief financial officer to allow timely decisions regarding required disclosure. Our management, including our chief executive officer and chief financial officer, conducted an evaluation of our disclosure controls and procedures, as defined under Exchange Act Rule 13a-15(e), as of the end of the period covered by this Annual Report on Form 20-F. Based upon that evaluation, our chief executive officer and chief financial officer have concluded that, as of such date, our disclosure controls and procedures were effective.

**Management's Annual Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) promulgated under the Securities Exchange Act of 1934 as a process designed by, or under the supervision of, the company's principal executive and principal financial officers and effected by the company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transaction and dispositions of the assets of the company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2012. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. Based on that assessment, our management concluded that as of December 31, 2012, our internal control over financial reporting is effective.

This annual report does not include an attestation report of our independent registered public accounting firm regarding internal control over financial report. Management's report was not subject to attestation by our independent registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit us to provide only management's report in this annual report.

#### **Changes in Internal Control over Financial Reporting**

There was no change in our internal control over financial reporting that occurred during the period covered by this annual report that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

**Item 16.** [Reserved]

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

Our board of directors has determined that each member of our audit committee each of whom also qualifies as independent director, meets the definition of an audit committee financial expert, as defined by rules of the Securities and Exchange Commission. For a brief listing of the relevant experience of the member of our audit committee, see Item 6.A. "Directors, Senior Management and Employees — Directors and Senior Management."

**Item 16B. Code of Ethics**

We have adopted a code of ethics that applies to our chief executive officer and all senior financial officers of our company, including the chief financial officer, chief accounting officer or controller, or persons performing similar functions. The code of ethics is publicly available on our website at [www.tat-technologies.com](http://www.tat-technologies.com). Written copies are available upon request. If we make any substantive amendment to the code of ethics or grant any waivers, including any implicit waiver, from a provision of the codes of ethics, we will disclose the nature of such amendment or waiver on our website.

**Item 16C. Principal Accountant Fees and Services****Fees Paid to Independent Public Accountant**

The following table sets forth, for each of the years indicated, the fees paid to our principal independent registered public accounting firm. All of such fees were pre-approved by our Audit Committee.

<b>Services Rendered</b>	<b>Year Ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Audit (1)	\$ 257,000	\$ 291,000
Tax (2)	47,000	31,600
<b>Total</b>	<b>\$ 304,000</b>	<b>\$ 322,600</b>

- (1) Audit fees are for audit services for each of the years shown in the table, including fees associated with the annual audit and reviews of our quarterly financial results, consultations on various accounting issues and audit services provided in connection with other statutory or regulatory filings.
- (2) Tax fees relate to professional services rendered for tax compliance and tax advice. These services include assistance regarding international and Israeli taxation.

## Pre-Approval Policies and Procedures

Our Audit Committee has adopted a policy and procedures for the pre-approval of audit and non-audit services rendered by our independent public accounting firm Kesselman & Kesselman, a member of PriceWaterhouseCoopers International Ltd. Pre-approval of an audit or non-audit service may be given as a general pre-approval, as part of the audit committee's approval of the scope of the engagement of our independent auditor, or on an individual basis. Any proposed services exceeding general pre-approved levels also require specific pre-approval by our audit committee. The policy prohibits retention of the independent public accountants to perform the prohibited non-audit functions defined in Section 201 of the Sarbanes-Oxley Act or the rules of the SEC, and also requires the Audit Committee to consider whether proposed services are compatible with the independence of the public accountants.

### Item 16D. Exemptions from the Listing Standards for Audit Committee

Not Applicable.

### Item 16E. Purchase of Equity Securities By The Issuer and Affiliated Purchasers

Not Applicable.

### Item 16F. Change in Registrant's Certifying Accountant.

Not Applicable.

### Item 16G. Corporate Governance

The following are the significant ways in which our corporate governance practices differ from those followed by domestic companies under the Nasdaq Rules:

*Shareholder Approval.* Although the Nasdaq Rules generally require shareholder approval of equity compensation plans and material amendments thereto, we follow Israeli Companies Law, which is to have such plans and amendments approved only by the board of directors, unless such arrangements are for the compensation of directors or a transaction with the controlling shareholder, in which case they also require the approval of the audit committee and the shareholders.



In addition, rather than follow the Nasdaq Rules requiring shareholder approval for the issuance of securities in certain circumstances, we follow Israeli law, under which a private placement of securities requires approval by our board of directors and shareholders if it will cause a person to become a controlling shareholder (generally presumed at 25% ownership) or if:

- o The securities issued amount to 20% or more of our outstanding voting rights before the issuance;
- o Some or all of the consideration is other than cash or listed securities or the transaction is not on market terms; and
- o The transaction will increase the relative holdings of a shareholder that holds 5% or more of our outstanding share capital or voting rights or that it will cause any person to become, as a result of the issuance, a holder of more than 5% of our outstanding share capital or voting rights.

Annual Reports. While the Nasdaq Rules generally require that companies send an annual report to shareholders prior to the annual general meeting, we follow the generally accepted business practice for companies in Israel. Specifically, we file annual reports on Form 20-F, which contain financial statements audited by an independent accounting firm, electronically with the SEC and post a copy on our website.

### **PART III**

#### **Item 17. Financial Statements**

We have elected to furnish financial statements and related information specified in Item 18.

#### **Item 18. Financial Statements**

##### **Consolidated Financial Statements of the Company**

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#### **Item 19. Exhibits**

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

- |     |  |
|-----|--|
| 1.1 | Memorandum of Association of the Registrant (1)  |
| 1.2 | Articles of Association of the Registrant (1)  |
| 2.1 | Specimen Certificate for Ordinary Shares (1)   |
| 4.1 | 2012 Stock Option Plan (filed herewith)  |
| 4.2 | Agreement dated February 10, 2000, by and between the Registrant and TAT Industries Ltd. (English summary translation) (2)   |
| 4.3 | English translation of Share Sales Agreement, dated March 27, 2008, by and between the Registrant and Bental Investments Cooperative Agricultures Society Ltd. (5) |

- 4.4 English translation of Shareholders' Agreement, dated May 21, 2008, by and between the Registrant, Tat Industries Ltd. and Bental Investments Cooperative Agriculture Society Ltd. (5)
- 4.5 English translation of Amendment to the Share Sales and Options Agreement and the Shareholders' Agreement, dated May 21, 2008, by and between the Registrant, Tat Industries Ltd. and Bental Investments Cooperative Agriculture Society Ltd. (5)
- 4.6 English translation of Share Sales Agreement dated April 15, 2008, by and between the Registrant and Mivtach Shamir Investments (1993) Ltd. (5)
- 4.7 Agreement and Plan of Merger dated April 3, 2009 by and between the Registrant, Limco-Piedmont, Inc. and LIMC Acquisition Company (4)
- 5.0 Reports of Other Certified Public Accountants filed: First Aviation Services Inc.
- 8 List of Subsidiaries of the Registrant
- 12.1 Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
- 12.2 Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended
- 13.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 13.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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(1) Filed as an exhibit to the Registrant's Annual Report on Form 20-F for the year ended December 31, 1992, and incorporated herein by reference.

(2) Incorporated by reference to the Registrant's Annual Report on Form 20-F for the year ended December 31, 1999, and incorporated herein by reference.

- (3) Incorporated by reference to the Registrant's Annual Report on Form 20-F for the year ended December 31, 2006, and incorporated herein by reference.
- (4) Filed as an exhibit to the Registrant's Registration Statement on Form F-4 filed on May 7, 2009 and incorporated herein by reference.
- (5) Filed as an exhibit to the Registrant's Annual Report on Form 20-F for the year ended December 31, 2007, and incorporated herein by reference.
- (6) Filed as an exhibit to the Registrant's Annual Report on Form 20-F for the year ended December 31, 2010, and incorporated herein by reference.

#### SIGNATURES

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

TAT TECHNOLOGIES LTD.

By: /s/ Yaron Shalem

Yaron Shalem  
Chief Financial Officer  
(Principal Accounting Officer)

Date: April 25, 2013

TAT TECHNOLOGIES LTD. AND ITS SUBSIDIARIES  
CONSOLIDATED FINANCIAL STATEMENTS  
AS OF DECEMBER 31, 2012

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TAT TECHNOLOGIES LTD. AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2012

IN U.S. DOLLARS

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the shareholders of  
TAT Technologies Ltd.

We have audited the accompanying consolidated balance sheets of TAT Technologies Ltd. and its subsidiaries (the "Company") as of December 31, 2012 and 2011, and the related consolidated statements of operations, comprehensive income, changes in equity and cash flows for each of the three years in the period ended December 31, 2012. These consolidated 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 did not audit the financial statements of First Aviation Services Inc., an equity method investee, as of and for the years ended December 31, 2012 and 2011. The First Aviation Services Inc. financial statements audited by other auditors were prepared on a "historical" basis (prior to basis adjustments primarily related to impairment charges recorded by the Company) and reflect total net assets of \$5,160,000 and \$17,590,000 as of December 31, 2012 and 2011, respectively, and total net loss of (\$12,979,000) and (\$94,000) for the years ended December 31, 2012 and 2011, respectively (subsequently adjusted by the Company to net assets of \$1,264,000 and \$5,020,000, and net (loss)/income of (\$3,756,000) and \$331,000, respectively, to reflect the share in the results of First Aviation Services Inc. and other adjustments primarily related to impairment charges recorded by the Company). We audited the adjustments necessary to convert the "historical" basis financial statements of First Aviation Services Inc. to the basis reflected in the Company's consolidated financial statements. The First Aviation Services Inc. financial statements were audited by other auditors (whose report thereon dated March 20, 2013 expressed an unqualified opinion on those financial statements and included a paragraph with respect to the restatement of the 2011 financial statements to correct an error) has been furnished to us, and our opinion expressed herein, insofar as it relates to the historical amounts included for First Aviation Services Inc., is based solely on the report of the other auditors.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated 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 statements presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits and the report of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2012 and 2011 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2012, in conformity with accounting principles generally accepted in the United States of America.

Tel-Aviv, Israel  
April 25, 2013

/s/ Kesselman & Kesselman  
Certified Public Accountants (Isr.)  
A member firm of PricewaterhouseCoopers International Limited



## CONSOLIDATED BALANCE SHEETS

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

	December 31,	
	2012	2011
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 16,581	\$ 26,232
Short-term bank deposits	10,048	-
Marketable securities at fair value	-	1,900
Short-term restricted deposits	2,307	954
Trade accounts receivable, net	20,930	20,621
Other accounts receivable and prepaid expenses	4,533	5,661
Amounts due from related parties	54	818
Inventories, net	33,031	31,303
Total current assets	87,484	87,489
INVESTMENT AND OTHER NON CURRENT ASSETS:		
Long-term restricted deposits	-	2,300
Investment in an affiliated company	1,264	5,020
Funds in respect of employee rights upon retirement	3,318	2,859
Deferred income taxes	2,535	3,669
	7,117	13,848
PROPERTY, PLANT AND EQUIPMENT, NET	12,910	12,939
GOODWILL, NET	-	1,042
Total long-term assets	20,027	27,829
Total assets	\$ 107,511	\$ 115,318

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

## CONSOLIDATED BALANCE SHEETS

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

	December 31,	
	2012	2011
<b>LIABILITIES AND EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Short term bank loan and current maturities of long-term loans	\$ 3,274	\$ 4,916
Trade accounts payable	5,373	5,073
Amounts due to related parties	112	165
Other accounts payable and accrued expenses	7,295	6,670
Total current liabilities	16,054	16,824
<b>NON CURRENT LIABILITIES:</b>		
Long-term loans, net of current maturities	1,116	4,420
Other long-term liabilities	-	86
Liability in respect of employee rights upon retirement	3,815	3,414
Deferred income taxes	1,490	1,413
Total long-term liabilities	6,421	9,333
<b>COMMITMENTS AND CONTINGENT LIABILITIES</b>		
Total liabilities	22,475	26,157
<b>EQUITY:</b>		
Ordinary shares of NIS 0.9 par value :		
Authorized: 10,000,000 shares at December 31, 2012 and 2011;		
Issued: 9,073,043 shares at December 31, 2012 and 2011;		
Outstanding: 8,798,570 and 8,815,003 shares at December 31, 2012 and 2011, respectively	2,790	2,790
Additional paid-in capital	64,410	64,402
Treasury shares at cost - 274,473 and 258,040 shares, at December 31, 2012 and 2011, respectively	(2,088)	(2,018)
Accumulated other comprehensive loss	(897)	(1,036)
Retained earnings	18,018	22,232
Total TAT Technologies Ltd. shareholders' equity	82,233	86,370
Non controlling interest	2,803	2,791
Total equity	85,036	89,161
Total liabilities and equity	\$ 107,511	\$ 115,318

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

## CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Year ended December 31,		
	2012	2011	2010
Revenues:			
Products	\$ 46,270	\$ 47,508	\$ 38,954
Services	41,652	37,889	40,801
	<u>87,922</u>	<u>85,397</u>	<u>79,755</u>
Cost of revenues:			
Products	33,220	34,076	32,052
Services	33,362	32,143	29,136
Write down of inventory and impairment charges of long lived assets	-	5,763	3,500
	<u>66,582</u>	<u>71,982</u>	<u>64,688</u>
Gross profit	<u>21,340</u>	<u>13,415</u>	<u>15,067</u>
Operating expenses:			
Research and development, net	1,152	786	651
Selling and marketing expenses	3,426	3,439	3,475
General and administrative expenses	11,487	10,949	12,832
Impairment of goodwill and other intangible assets	1,015	-	4,704
Other expenses (income)	9	(169)	-
	<u>17,089</u>	<u>15,005</u>	<u>21,662</u>
Operating income (loss)	4,251	(1,590)	(6,595)
Financial expenses, net	(181)	(380)	(111)
Other expenses	-	-	(200)
Gain from dilution of interests in affiliated company	-	240	-
Income (loss) before taxes on income	4,070	(1,730)	(6,906)
Taxes on income (tax benefit)	2,086	(316)	(4,153)
Net income (loss) after taxes on income	1,984	(1,414)	(2,753)
Share in results of affiliated company and impairment of share in affiliated company	(3,756)	331	(4,510)
Net loss	(1,772)	(1,083)	(7,263)
Net loss (income) attributable to non controlling interest	58	53	(123)
Net loss attributable to TAT Technologies Ltd. shareholders	<u>\$ (1,714)</u>	<u>\$ (1,030)</u>	<u>\$ (7,386)</u>

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

## CONSOLIDATED STATEMENTS OF OPERATIONS

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

	Year ended December 31,		
	2012	2011	2010
Loss per share			
Basic and diluted net loss per share attributable to controlling interest	\$ (0.19)	\$ (0.12)	\$ (0.84)
Weighted average number of shares - basic and diluted	8,808,075	8,815,003	8,815,003

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

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

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

	Year ended December 31,		
	2012	2011	2010
Net loss	\$ (1,772)	\$ (1,083)	\$ (7,263)
Other comprehensive income (loss):			
Foreign currency translation adjustments	209	(819)	708
Unrealized gain (loss) on marketable securities, net of tax	-	(11)	11
Total other comprehensive income (loss)	209	(830)	719
Comprehensive loss	\$ (1,563)	\$ (1,913)	\$ (6,544)
Comprehensive loss (income) attributable to non controlling interest	(12)	261	(312)
Comprehensive loss attributable to TAT Technologies' Ltd. shareholders	<u>\$ (1,575)</u>	<u>\$ (1,651)</u>	<u>\$ (6,856)</u>

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

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

U.S dollars in thousands, except share data

	TAT Technologies Ltd. Shareholders							Non controlling interest	Total equity
	Share capital		Additional paid-in capital	Accumulated other comprehensive income (loss)	Treasury shares	Retained earnings			
	Number of shares	Amount							
BALANCE AT JANUARY 1, 2010	9,073,043	\$ 2,790	\$ 64,390	\$ (944)	\$ (2,018)	\$ 30,648	\$ 2,740	\$ 97,606	
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2010:									
Net income (loss)	-	-	-	-	-	(7,386)	123	(7,263)	
Foreign currency translation	-	-	-	522	-	-	186	708	
Adjustment on marketable securities	-	-	-	8	-	-	3	11	
Share based compensation expenses	-	-	49	-	-	-	-	49	
BALANCE AT DECEMBER 31, 2010	9,073,043	2,790	64,439	(414)	(2,018)	23,262	3,052	91,111	
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2011:									
Net loss	-	-	-	-	-	(1,030)	(53)	(1,083)	
Foreign currency translation	-	-	-	(614)	-	-	(205)	(819)	
Adjustment on marketable securities	-	-	-	(8)	-	-	(3)	(11)	
Share based compensation income	-	-	(37)	-	-	-	-	(37)	
BALANCE AT DECEMBER 31, 2011	9,073,043	2,790	64,402	(1,036)	(2,018)	22,232	2,791	89,161	
CHANGES DURING THE YEAR ENDED DECEMBER 31, 2012:									
Net loss	-	-	-	-	-	(1,714)	(58)	(1,772)	
Foreign currency translation	-	-	-	139	-	-	70	209	
Dividend distributed	-	-	-	-	-	(2,500)	-	(2,500)	
Purchase of treasury shares	-	-	-	-	(70)	-	-	(70)	
Share based compensation expenses	-	-	8	-	-	-	-	8	
BALANCE AT DECEMBER 31, 2012	9,073,043	\$ 2,790	\$ 64,410	\$ (897)	\$ (2,088)	\$ 18,018	\$ 2,803	\$ 85,036	

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

## CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2012	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	\$ (1,772)	\$ (1,083)	\$ (7,263)
Adjustments to reconcile net loss to net cash provided by operating activities:			
Depreciation and amortization	2,403	3,271	3,382
Exchange differentials of long-term loans	22	(13)	7
Write down of inventory	-	2,500	3,500
Impairment of goodwill, intangible assets and long lived assets	1,015	3,263	4,704
Loss (gain) on sale of property and equipment	9	(169)	149
Loss (gain) on sale and impairment loss on marketable securities	-	(9)	196
Loss (gain) from change in fair value of derivatives	(399)	372	(100)
Interest from short-term bank deposits and restricted deposits	(55)	-	-
Provision for doubtful accounts	258	31	259
Share in results of affiliated company and impairment of share in affiliated company	3,756	(331)	4,510
Gain from dilution of interests in affiliated company	-	(240)	-
Share based compensation expenses (income)	8	(37)	49
Liability in respect of employee rights upon retirement	379	28	248
Deferred income taxes, net	1,599	(868)	(2,973)
Changes in operating assets and liabilities:			
Amounts due to (from) related parties, net	711	(674)	213
Increase in trade accounts receivable	(478)	(544)	(4,689)
Decrease (increase) in other accounts receivable and prepaid expenses	611	1,283	(993)
Increase in inventories, net	(1,673)	(1,959)	(1,643)
Increase (decrease) in trade accounts payable	287	(2,545)	1,775
Increase (decrease) in other accounts payable and accrued expenses	1,059	(1,580)	1,623
Increase (decrease) in other long-term liabilities	(2)	2	84
Net cash provided by operating activities	7,738	698	3,038
CASH FLOWS FROM INVESTING ACTIVITIES:			
Proceeds from sale of marketable securities	1,900	1,215	854
Purchase of marketable securities	-	(578)	(616)
Funds in respect of employee right upon retirement	(443)	(3)	(313)
Proceeds from sale of property and equipment	71	247	189
Purchase of intangible assets	-	-	(136)
Purchase of property and equipment	(2,394)	(3,305)	(2,950)
Investment in short-term deposit	(10,000)	-	-
Proceeds released from restricted deposits	954	2,172	-
Deposit of restricted deposits	-	(350)	(14)
Net cash used in investing activities	\$ (9,912)	\$ (602)	\$ (2,986)

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

## CONSOLIDATED STATEMENTS OF CASH FLOWS

U.S. dollars in thousands

	Year ended December 31,		
	2012	2011	2010
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Repayments of long-term loans	\$ (1,060)	\$ (3,374)	\$ (1,551)
Proceeds from long-term loans received	-	673	1,185
Dividend paid	(2,500)	-	-
Repayments of short-term loans	(4,542)	(795)	-
Short-term credit received from a bank	627	2,646	1,724
Repurchase of treasury shares	(70)	-	-
Net cash provided by (used in) financing activities	(7,545)	(850)	1,358
Translation adjustment on cash and cash equivalents	68	(51)	59
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(9,651)	(805)	1,469
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	26,232	27,037	25,568
<b>BALANCE OF CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b>\$ 16,581</b>	<b>\$ 26,232</b>	<b>\$ 27,037</b>
<u>Supplemental disclosure of cash flow information:</u>			
Interest paid	\$ (255)	\$ (247)	\$ (245)
Income taxes paid	\$ (836)	\$ (1,213)	\$ (1,845)
Income taxes refunds	\$ 978	\$ 2,145	\$ 2,480

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



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 1 - GENERAL

- a. TAT Technologies Ltd., ("TAT" or the "Company") an Israeli corporation, incorporated in 1985, is a leading provider of services and products to the commercial and military aerospace and ground defense industries. Together with its subsidiaries, 100% held, Limco-Piedmont Inc. ("Limco-Piedmont"), 70% held, Bental Industries Ltd. ("Bental") and 100% held, TAT Gal Inc. ("TAT Gal") hereinafter collectively referred to as the "Group", it is principally engaged in the following activities:

- Design, development, manufacture and sale of a broad range of heat transfer equipment and solutions;
- Remanufacture, overhaul and repair of heat transfer equipment;
- Maintenance, repair and overhaul of auxiliary power units, landing gears and related components;
- Design, development and manufacture of aviation and flow control accessories including fuel components, secondary power systems, and various instrumentation and electronic assemblies;
- Design, development and manufacture of environmental control and cooling systems; and
- Production and development of precision electric motion systems, mainly earmarked for the defense industries.

The products developed, repaired, and maintained by the Group are primarily used for airborne systems on commercial and military aircrafts as well as for defense ground systems. The principal markets of TAT are in Israel, Europe and the United States.

As of December 31, 2012, Limco-Piedmont holds 100% of Limco-Airepair Inc. ("Limco") and of Piedmont Aviation Component Services LLC. ("Piedmont") and also holds, through Piedmont, 29.64% in First Aviation Services Inc. ("FAvS"), a world-wide distributor of products and services to the aerospace industry and a one-stop-shop for maintenance, repair and overhaul services (for wheels, breaks, propellers and landing gear) for the General Aviation Industry.

- b. TAT's shares are listed on both the NASDAQ (TATT) and Tel-Aviv stock exchange.
- c. TAT Industries Ltd., an Israeli corporation whose shares are listed on the Tel-Aviv Stock Exchange ("TAT Industries") holds 43.71% of TAT's shares, as of December 31, 2012.
- d. On July 2, 2009, TAT Industries Audit Committee and Board of Directors approved an agreement with the controlling shareholder of TAT Industries, KMN Industries Ltd. (formerly: Isal Amlat Industries (1994) Ltd.) ("KMN Industries"), according to which KMN Industries is empowering TAT Industries, or anyone on its behalf, to attend and vote at any meeting of TAT shareholders, with its discretion, KMN Industries' shares of TAT. This agreement shall remain in effect as long as KMN Industries remains the controlling shareholder, as the term "control" is defined in the Israeli Securities Law, 1968. As of December 31, 2012, KMN Industries holds directly an additional 10.29% of TAT's shares.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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U.S. dollars in thousands

## NOTE 1 - GENERAL (CONT)

- e. In October 2012, two lenders to TAT's controlling shareholders, KMN Industries and TAT Industries ("Controlling Shareholders"), filed separate petitions to the District court to enforce liens granted to such lenders by each of the Controlling Shareholders in certain collaterals including KMN Industries' holdings of an approximately 80% ownership interest in TAT Industries (which owns 43.71% of TAT) and KMN Industries' direct holdings in TAT (which represents 10.29% of TAT). On December 18, 2012, the District court appointed permanent receivers on behalf of the two lenders mentioned above for the purpose of jointly enforcing the liens granted to such lenders. If such liens are enforced, such collateral is subject to sale which would result in the sale of TAT's shares, currently owned by TAT Industries, and/or KMN Industries. On March 15, 2013, the receivers of TAT's shares mentioned above announced a tender to purchase such shares. Pursuant to the tender all proposals to acquire such shares must be submitted no later than April 18, 2013.

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

**Accounting principles**

The consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"), applied on a consistent basis, unless otherwise indicated below.

**a. Use of estimates in the preparation of financial statement**

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

As applicable to these financial statements, the most significant estimates and assumptions relate to: revenue recognition, recoverability of inventory, provision for doubtful accounts, fair value measurement of available for sale marketable securities, impairment of goodwill, intangible assets and long lived assets, impairment of investment in affiliated company, contingencies, provision for taxes and the realizability of deferred tax assets.

**b. Functional currency**

The majority of the TAT's revenues are generated in U.S. dollars ("dollars") and a substantial portion of TAT's costs are incurred in dollars. In addition, a significant portion of the TAT's financings has been obtained in dollars. Accordingly, the dollar is the currency of the primary economic environment in which TAT operates and accordingly its functional and reporting currency is the dollar.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

b. **Functional currency (cont)**

Limco's and Piedmont's ("U.S. subsidiaries") revenues are generated in dollars and its costs are incurred in dollars. In addition, the U.S. subsidiaries financing has been obtained in dollars. Accordingly, the dollar is the currency of the primary economic environment in which the U.S. subsidiaries operate and accordingly its functional and reporting currency is the dollar.

Monetary accounts maintained in currencies other than the dollar are re-measured using the representative foreign exchange rate at the balance sheet date. Operational accounts and non-monetary balance sheet accounts are measured and recorded at the rate in effect at the date of the transaction. The effects of foreign currency re-measurement are recorded in financial income (expenses), net.

Most of Bental's revenues are generated in New Israeli Shekel ("NIS") and a substantial portion of Bental's costs are incurred in NIS. In addition, Bental's financing has been obtained in NIS. Accordingly, the NIS is the currency of the primary economic environment in which Bental operates and accordingly its functional and reporting currency is the NIS. For Bental whose functional currency has been determined to be the NIS, assets and liabilities are translated at year-end exchange rates, and statement of operations items are translated at average exchange rates prevailing during the year. Resulting translation differences are recorded as a separate component of accumulated other comprehensive income (loss) in equity.

c. **Principles of consolidation**

The consolidated financial statements include the accounts of TAT and its subsidiaries. In these financial statements, "subsidiaries" are companies over which TAT has over 50% voting control and the financial statements of which are consolidated with those of the Company.

Intercompany balances and transactions, including profits from intercompany sales not yet realized outside the Group, have been eliminated upon consolidation. Non-controlling interests are included in equity.

d. **Cash and Cash equivalents**

All highly liquid investments, which include short-term bank deposits and money market accounts, that are not restricted as to withdrawal or use, and short-term debentures, the period to maturity of which do not exceed three months at the time of investment, are considered to be cash equivalents.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

e. **Restricted deposits**

Restricted deposits primarily consist of cash deposits securing a guarantee provided by the Group to an affiliated company and securing a loan provided to the Company by a financial institution; see note 13(f)(2) and 13(f)(5) for additional information. Classification of restricted deposits as current or non current assets takes into consideration the expected release date.

f. **Marketable securities**

Marketable securities consist of debt securities classified as available-for-sale and are recorded at fair value. The fair value of quoted securities is based on current market value. When securities do not have an active market, fair value is determined using a valuation model. This model is based on reference to other instruments with similar characteristics, or a discounted cash flow analysis, or other pricing models making use of market inputs and relying as little as possible on entity-specific inputs. Changes in fair value, net of taxes, are reflected in other comprehensive income (loss).

Realized gains and losses on sale of the securities are included in the consolidated statements of operations as financial income (expenses).

An other-than-temporary impairment has occurred if the Group does not expect to recover the entire amortized cost basis of the debt security. If the Group does not intend to sell the impaired debt security, and it is not more likely than not it will be required to sell the debt security before the recovery of its amortized cost basis, the amount of the other-than-temporary impairment recognized in earnings, recorded in financial expense, net, is limited to the portion attributed to credit loss. The remaining portion of the other-than-temporary impairment related to other factors is recognized in other comprehensive income (loss).

g. **Trade accounts receivable, net**

The Group's accounts receivable balances are due from companies primarily in the airline and defense industries. Credit is extended based on evaluation of a customer's financial condition and generally, collateral is not required. Trade accounts receivable from sales of services and products are typically due from customers within 30 - 90 days. Trade accounts receivable balances are stated at amounts due from customers net of an allowance for doubtful accounts. Accounts outstanding longer than their original contractual payment terms are considered past due. The Group determines its allowance by considering a number of factors, including the length of time accounts receivable are past due, the Group's previous loss history from such customers, customer's current ability to pay its obligation to TAT and the condition of the general economy and the industry as a whole. The Group writes-off accounts receivable when they become uncollectible. Payments subsequently received on such receivables are credited to the allowance for doubtful accounts. The allowance for doubtful accounts is determined with respect to specific debts that are doubtful of collection.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

## h. Inventories

Inventories are measured at the lower of cost or market.

Cost of inventories is determined as follows:

Raw materials and parts	-	On the basis of actual cost or standard cost.
Work in progress	-	On the basis of actual cost or standard cost which takes into account materials, labor and other direct and indirect manufacturing costs, or identifiable direct costs.
Finished goods	-	On the basis of actual cost or standard cost which takes into account materials, labor and other direct and indirect manufacturing costs, or identifiable direct costs.

Since the Group sells products and services related to airplane accessories (heat transfer equipment, defined in note 1, APU's, landing gears etc.) for airplanes that can be in service for 20 to 50 years, it must keep a supply of such products and parts on hand while the airplanes are in use. The Group writes down its inventory for estimated obsolescence and unmarketable inventory equal to the difference between the cost of inventory and estimated market value based upon assumptions for future demand and market conditions.

## i. Property, plant and equipment

Property, plant and equipment are stated at cost, after deduction of investment grants from Israel, net of accumulated depreciation. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, as follows:

	years
Buildings	25
Machinery and equipment	4 - 10 (mainly 10)
Motor vehicles	6 - 7
Office furniture and equipment	3 - 17 (mainly 7)
Software	3

Leasehold improvements are included in buildings and amortized using the straight line method over the period of the lease contract, or the estimated useful life of the asset, whichever is shorter.

## j. Grants from Office of the Chief Scientist of Israel ("OCS"):

Grants received from the OCS for approved research and development projects are recognized at the time the Company is entitled to such grants, on the basis of the costs incurred and included as a deduction from research and development expenses. Due to the fact that the Company is defined as "Traditional Industry Company", under the OCS regulations, these grants are non-royalty bearing.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

**k. Investment in Company Accounted for using the Equity Method**

Investment in which the Group exercises significant influence and which is not considered a subsidiary ("affiliate") is accounted for using the equity method, whereby the Group recognizes its proportionate share of the affiliated company's net income or loss after the date of investment. Significant influence is presumed to exist when the Group holds between 20%-50% of an affiliated company's voting instruments.

The Group reviews this investment for impairment whenever events indicate the carrying amount may not be recoverable. See note 3(b).

**l. Goodwill**

Goodwill reflects the excess of the consideration paid or transferred plus the fair value of any non-controlling interest in the acquired entity at the acquisition date over the fair values of the identifiable assets acquired and liabilities assumed.

Goodwill is not amortized, but rather tested for impairment by assessing the fair value of the Group's various reporting units, annually on September 30, or whenever events or circumstances present an indication of potential impairment.

Goodwill impairment testing is a two-step process. The first step involves comparing the fair value of a company's reporting units to their carrying amount. If the fair value of the reporting unit is determined to be greater than its carrying amount, there is no impairment. If the reporting unit's carrying amount is determined to be greater than the fair value, the second step must be completed to measure the amount of impairment, if any. Step two calculates the implied fair value of goodwill by deducting the fair value of all tangible and intangible assets, excluding goodwill, of the reporting unit from the fair value of the reporting unit as determined in step one. The implied fair value of the goodwill in this step is compared to the carrying value of goodwill. If the implied fair value of the goodwill is less than the carrying value of the goodwill, an impairment loss equivalent to the difference is recorded.

Determining the fair value of a reporting unit requires the exercise of judgment on the part of management and involves the use of estimates and assumptions, including with respect to: (i) future revenues and operating margins used in order to calculate projected future cash flows; (ii) discount rates reflecting the relevant risks associated with companies comparable to the applicable reporting unit; (iii) competitive and economic environments; and (iv) appropriate industry comparables. There are a number of generally accepted methods used for valuing a business. These methods may be used alone or in combination with one another. The 'income method' uses forecasted cash flows as a basis to value the business. An aggregate present value is calculated for future cash flows using a separately computed discount rate. The advantage of this method is that it facilitates an analysis of company-specific forecasted operating data and their impact upon the value of a business. The 'market-based' method identifies business entities with publicly traded securities whose business and financial risks are comparable to those of the business being valued. The pricing multiple of the companies selected are used to derive the market value of the business under analysis. This method has the advantage of objectivity since it is based upon external, publicly-available data.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

**l. Goodwill (cont)**

During the year ended December 31, 2012, management concluded that the carrying value of goodwill of the OEM of Electric Motion Systems reporting unit, exceeded its implied fair value and, accordingly, recorded an impairment charge in the amount of \$1,015 (which was the entire balance of goodwill included in this reporting unit). See note 8 for additional information.

For the year ended December 31, 2011, no goodwill impairment charges were recorded.

During the year ended December 31, 2010, management concluded that the carrying value of goodwill of the MRO services for aviation components reporting unit, exceeded its implied fair value and, accordingly, recorded an impairment charge in the amount of \$4,223. See note 8 for additional information.

**m. Impairment of long-lived assets**

The Group tests long-lived assets for impairment, whenever events or changes in circumstances indicate that the carrying amount of the asset (asset group) may not be recoverable. When required, the Group records charges for impairment of long-lived assets for the amount by which the present value of future cash flows, or some other fair value measure, is less than the carrying value of these assets (see also notes 7 and 8).

As of December 31, 2012 and 2011, all the Group's identifiable intangible assets have been amortized or written off.

**n. Treasury Shares**

Company shares held by the Company are presented as a reduction of TAT's shareholders' equity at their cost to the Company.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

o. **Revenue recognition**

The Group generates its revenues from the sale of its OEM products and systems and from providing MRO services (remanufacture, maintenance, repair and overhaul services and long-term service contracts) and parts services.

Revenues from the sale of products are recognized when persuasive evidence of an arrangement exists, delivery of the product has occurred, provided the collection of the resulting receivable is reasonably assured, the price is fixed or determinable and no significant obligation exists. The Group does not grant a right of return.

Revenues from product sales are recognized when the product is shipped to the customer and title passes to the customer.

Revenues from multi-year, fixed price contracts for OEM customers are recognized when a product is shipped (and title passes) to the customer. Management provides for losses as soon as a loss is expected for the remaining portion of such contracts. For the years ended December 31, 2012, 2011 and 2010, no losses have been recognized for such fixed price contracts.

Revenues from MRO services are recognized as services are performed, at the time when the customer-owned material is shipped back to the customer.

Revenues from some maintenance contracts are recognized over the contract period in proportion to the costs expected to be incurred in performing services under the contract. The Group estimates the costs that are expected to be incurred based on its experience with the aggregate costs incurred and to be incurred on contracts of this nature. The costs incurred related to the maintenance contracts are not incurred on a straight-line basis, as the timing to provide the maintenance services is dependent on when parts under these contracts require maintenance. Therefore, the Group accrues revenue as costs are incurred. These revenues are then compared to actual results and adjusted to either deferred revenue for results greater than historical estimates or expensed in those cases of performance less than historical estimates. These accounts are reviewed on a timely basis and adjusted (if required) based on cost structures.

Revenues from royalties from sales of products developed with the Group's intellectual property, technology and technical assistance are recognized when the related sales are made.

p. **Shipping and handling costs**

Shipping and handling costs billed to customers are included in revenue. The cost of shipping and handling products is included in costs of revenues.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

q. **Warranty costs**

The Group provides warranties for its products and services ranging from one to three years, which vary with respect to each contract and in accordance with the nature of each specific product.

The Group estimates the costs that may be incurred under its warranty and records a liability in the amount of such costs at the time the product is shipped. The Group periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

r. **Research and development**

Research and development costs, net of grants, are charged to expenses as incurred.

s. **Fair value measurement**

The Group measures fair value and discloses fair value measurements for financial and non-financial assets and liabilities. Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The accounting standard establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable prices that are based on inputs not quoted on active markets, but corroborated by market data or active market data for similar but not identical assets or liabilities.

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

In determining fair value, the Group utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers credit risk in its assessment of fair value.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

## t. Concentrations of credit risk

Financial instruments that potentially subject the Group to concentrations of credit risk consist principally of cash and cash equivalents, restricted deposits, marketable securities and accounts receivable.

Cash, cash equivalents and restricted deposits are deposited with major banks in Israel and the United States. Such deposits in the United States may be in excess of insured limits and are not insured in other jurisdictions. Management believes that the financial institutions that hold Group's cash, cash equivalents and restricted deposits are financially sound. Accordingly, minimal credit risk exists with respect to these financial instruments.

The Group's marketable securities include investments in debentures. Management believes that the companies that issued the debentures are financially sound, the portfolio is well diversified, and accordingly, minimal credit risk exists with respect to the marketable securities. See also note 4 for details about the auction rate securities impairment loss in 2011.

The Group's accounts receivable are derived mainly from sales to customers in the United States, Israel and Europe. The Group generally does not require collateral; however, in certain circumstances the Group may require letters of credit. Management believes that credit risks relating to accounts receivable are minimal since the majority of the Group's customers are world-leading manufacturers of aviation systems and aircrafts, international airlines, governments and air-forces, and world-leading manufacturers and integrators of defense and ground systems. In addition the Group has relatively a large number of customers with wide geographic spread which mitigates the credit risk. The Group performs ongoing credit evaluation of its customers' financial condition.

## u. Income taxes

Income taxes are accounted for in accordance with ASC 740 "Income Taxes". This statement prescribes the use of the asset and liability method, whereby deferred tax assets and liabilities account balances are determined based on temporary differences between financial reporting and tax basis of assets and liabilities and for tax loss carry-forwards. Deferred taxes are measured using the enacted laws and tax rates that will be in effect when the differences are expected to reverse. The Group provides a valuation allowance, if necessary, to reduce deferred tax assets to their estimated realizable value, see note 15 (i).

Deferred tax liabilities and assets are classified as current or noncurrent based on the classification of the related asset or liability for financial reporting or, if not related to an asset or liability for financial reporting, according to the expected reversal dates of the specific temporary differences.

Taxes which would apply in the event of disposal of investments in subsidiaries have not been taken into account in computing the deferred taxes, as it is the Group's intention to hold, and not to realize these investments.

The Group records deferred taxes related to its share in results of its affiliated company.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

With regard to dividends distributable from the income of non-Israeli subsidiaries: as the Group intends to permanently reinvest retained earnings and has no intention to declare dividends out of such earnings in the foreseeable future it does not record deferred taxes in respect of taxes that would have been paid in such event.

The Group did not provide for deferred taxes attributable to dividend distribution out of retained tax-exempt earnings from "Approved/Benefited Enterprise" plans (see note 15b), since it intends to permanently reinvest them and has no intention to declare dividends out of such tax exempt income in the foreseeable future. Management considers such retained earnings to be essentially permanent in duration.

Results for tax purposes for the Company and TAT's Israeli subsidiary are measured and reflected in NIS and for TAT's U.S. subsidiaries are measured and reflected in dollars. As explained in (b) above, the consolidated financial statements are presented in dollars. In accordance with ASC 740, TAT has not provided deferred income taxes on the differences resulting from changes in exchange rate and indexation.

The Group follows a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon ultimate resolution. The Group's policy is to include interest and penalties related to unrecognized tax benefits within income tax expense. Such liabilities are classified as long-term, unless the liability is expected to be resolved within twelve months from the balance sheet date.

v. **Derivative financial instruments**

TAT enters into forward exchange contracts and options strategies in order to limit the exposure to exchange rate fluctuation associated with payroll expenses mainly incurred in NIS.

Since the contracts do not qualify under ASC 815 "Derivative and Hedging", any gain or loss derived from such instruments is recognized immediately as financial income (expenses). All forward exchange contracts and options are recognized on the balance sheet at their fair value within other receivables or other payables.

As of December 31, 2012, TAT had U.S. Dollar-NIS derivative contracts with a notional amount of approximately \$2,700 to purchase and sell Dollars. The fair value of the foreign exchange contracts and the options was \$27 and \$(372) as of December 31, 2012 and 2011, respectively. The cash flows associated with the contracts are reflected as cash flows from operating activities in the statements of cash flows.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

w. **Basic and diluted net loss per share**

Loss per share is computed based on the weighted average number of ordinary shares outstanding during each year. Diluted loss per share includes the potential effect of stock options outstanding during the year, in accordance with ASC 260 "Earnings per Share", using the treasury stock method.

In 2012, 2011 and 2010, outstanding equity awards were not taken into account due to their anti-dilutive effect.

x. **Share-based compensation**

The Group applies ASC 718 "Stock Based Compensation" with respect to employees options, which requires awards classified as equity awards to be accounted for using the grant-date fair value method. The fair value of share-based awards is estimated using the Black-Scholes valuation model, the payment transaction is recognized as expense over the requisite service period, net of estimated forfeitures. The Group estimates forfeitures based on historical experience and anticipated future conditions.

The Group recognizes compensation cost for an award with only service conditions that has a graded vesting schedule using the accelerated method over the requisite service period for the entire award. For an award with performance conditions that has a graded vesting schedule, compensation cost is recognized upon meeting such conditions, using the accelerated method over the requisite service period for the entire award.

The total share-based compensation expenses (income) recognized in the years ended December 31, 2012, 2011 and 2010 in the statements of operations were \$8, \$(37) and \$49, respectively.

y. **Comprehensive income (loss)**

Other comprehensive income (loss), net of related taxes where applicable, includes, in addition to net income (loss): (i) currency translation adjustments; and (ii) unrealized holding gains and losses on available-for-sale securities.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONT)

## z. Contingencies

Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Group but which will only be resolved when one or more future events occur or fail to occur. The Group's management assesses such contingent liabilities and estimated legal fees, if any, and accrues for these costs. Such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Group or unasserted claims that may result in such proceedings, the Group's management evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought.

Management applies the guidance in ASC 450-20-25 "Loss Contingencies", when assessing losses resulting from contingencies. If the assessment of a contingency indicates that it is probable that a loss has been incurred and the amount of the liability can be estimated, then the estimated liability would be recorded as accrued expenses in the Company's financial statements. If the assessment indicates that a potential material loss contingency is not probable but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material would be disclosed.

Loss contingencies considered to be remote by management are generally not disclosed unless they involve guarantees, in which case the guarantee would be disclosed.

## aa. Recently Issued Accounting Principles Not Yet Adopted

In December 2011, the FASB amended its guidance on disclosures about offsetting assets and liabilities. The amendment enhances disclosures regarding financial instruments and derivative instruments that are either (1) offset in accordance with GAAP or (2) subject to an enforceable master netting arrangement. This information will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position, including the effect or potential effect of rights of setoff associated with certain financial instruments and derivative instruments.

The amendments in ASU 2011-11 will be applied for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. An entity should provide the disclosures required by those amendments retrospectively for all comparative periods presented.

The Company does not expect ASU 2011-11, which relates to disclosure matters only, to have a material impact on the Company's consolidated financial statements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 3 - INVESTMENT IN AN AFFILIATED COMPANY

## a. Acquisition of stocks of FAvS

On December 4, 2009, the Company, through its subsidiary Piedmont, signed an investment agreement with FAvS. According to the agreement Piedmont was issued 288,334 shares of Class B Common stock of FAvS representing 37% of FAvS' then share capital and \$ 750 of FAvS Preferred stocks (entitled to cash dividends at an annual rate of 12% payable quarterly or to additional Preferred stocks at an annual rate of 15%) in return for Piedmont's propeller and parts businesses.

On the date of the above mentioned transaction, FAvS also signed an agreement to purchase all the assets and liabilities of Aerospace Turbine Rotables ("AeTR"). AeTR specializes in renovation and repair of landing gear, safety equipment and hydraulic and electrical components for corporate, regional and military aircraft. Piedmont also provided a guarantee for a period of one year (later renewed for additional periods until finally released on March 2013 as described further below) of up to \$ 7,000 with respect to FAvS' debt in connection with the acquisition of AeTR (see also note 13(e)).

On October 1, 2010, Piedmont agreed to extend the guarantee for \$6,600, by renewing the guarantee to the lender of FAvS. The renewed guarantee was for a period of 15 months that ended on December 31, 2011, and Piedmont was also granted a second lien on the assets of FAvS to secure the repayment obligations of FAvS in the event that the letter of credit is drawn upon. Piedmont also entered into an inter creditor agreement with the lender to FAvS which subordinated Piedmont's claims if the letter of credit is drawn upon to the obligations of FAvS to the lender.

FAvS' shares are quoted over the counter (OTC) at the PINKSHEET stock market (PINKSHEET: FAVS.PK). FAvS' share value as of December 31, 2012, 2011 and 2010 was \$7.0, \$5.45 and \$12.4, respectively. The Company believes that the share value does not reflect the fair value of FAvS' share, due to very low trading volume in FAvS' shares that do not comprise an active market.

A commercial dispute existed between Piedmont and FAvS relating to the propeller maintenance business which had been contributed to FAvS by Piedmont, as part of the transaction discussed above. The commercial dispute began in April 2010 when a customer of the propeller maintenance business requested reimbursement from FAvS for damages to certain propellers. FAvS then sought reimbursement from Piedmont for such amounts.

In order to settle the commercial dispute that existed between TAT's subsidiary, Piedmont and FAvS, on June 30, 2011, Piedmont and FAvS entered into a Settlement Agreement and Release (the "Settlement Agreement"). Pursuant to the Settlement Agreement, each party fully released the other party and acknowledged that the settlement was a compromise of disputed claims and was not to be construed as an admission of liability or wrongdoing. In addition, each party agreed not to disparage the other and Piedmont paid an aggregate amount of \$1,400 to FAvS (which amount had been fully reserved during 2010).

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 3 - ACQUISITION (CONT)

## a. Acquisition of stocks of FAvS (cont)

Simultaneously with the execution of the Settlement Agreement, the Chief Executive Officer and controlling stockholder of FAvS ("FAvS CEO"), purchased 166,113 shares of Class A Common Stock of FAvS at a price of \$18.06 per share, for an aggregate amount of \$3,000, while diluting Piedmont's interest in FAvS from 36.6% to 30.3% (29.64% as of December 31, 2012). In addition, Piedmont agreed to extend its guarantee to the bank debt incurred by FAvS to fund the AeTR transaction through June 30, 2013 and to continue to provide a letter of credit to secure such guarantee. The amortization schedule for such debt was revised so that no amortization will occur until June 30, 2012. Thereafter the debt will amortize at the rate of \$200 per month. As of December 31, 2012, the guarantee amount was \$4,600. Piedmont secured an amount of \$2,300 as of December 31, 2012, in respect of this guarantee. On March 18, 2013, the guarantee was released with the completion of the transaction, as described further below.

The Stockholders Agreement initially entered into in 2009 between Piedmont and FAvS CEO was also amended to delete the reciprocal drag along rights and to provide that Piedmont may designate one member to the Board of Directors of FAvS (rather than the two members provided in the original agreement). Finally, the Rights Agreement entered into in 2009 between Piedmont and FAvS was amended so that Piedmont's right to approve certain material corporate actions by FAvS has been limited to the right to approve contracts or agreements with affiliates of FAvS. The amendment also provided that the approval of Piedmont would not be required if FAvS seeks to raise additional capital from FAvS CEO as long as the consideration that was paid by FAvS CEO was not less than the consideration that would have been paid by a third-party in an arms-length transaction and would have been a fair, equitable and reasonable consideration under the circumstances.

In connection with the Settlement Agreement and the dilution in Piedmont's interest in FAvS, the Company recorded, on June 30, 2011, a gain in the amount of \$240 related to the \$3,000 capital investment in FAvS by FAvS CEO which was at a higher share price than recorded at Piedmont books.

In June 2012, FAvS entered into another transaction with FAvS CEO, pursuant to which FAvS borrowed \$3,000 from FAvS CEO, secured by a third lien on the assets of FAvS. The loan bears interest at 10% and in addition FAvS CEO was issued warrants to purchase shares of Class A Common Stock of FAvS, representing 15% of FAvS post-exercise shareholders' equity, at an exercise price of \$7.00 per share. Pursuant to the terms and conditions of the transaction, management believed that there were indicators of impairment with respect to TAT's investment in FAvS. Accordingly, the Company performed an impairment test of its investment in FAvS, with the assistance of a third party valuation. Based on the results of this test, the Company determined that its investment in FAvS was impaired by \$3,300. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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U.S. dollars in thousands

## NOTE 3 - ACQUISITION (CONT)

## a. Acquisition of stocks of FAvS (cont)

On March 18, 2013, FAvS closed a transaction according to which it sold the majority of the stock of API, one of its subsidiaries, for a total purchase price of \$16,500, out of which \$15,900 was used to pay-off the outstanding balance of the FAvS Revolving Line of Credit as of the transaction date. The sale resulted in FAvS retaining a 3% equity interest in the API business. The transaction resulted in a loss from discontinued operations on FAvS books and a write-down of the API business of \$11,500 (the "Write Down") which is included in the FAvS loss for the year ended December 31, 2012. As mentioned above, on June 30, 2012, as a result of certain indications of impairment, the Company recorded an impairment charge of \$3,300 in its investment in FAvS (which approximates its share in the said Write-Down). The Company also recorded its share in the losses of FAvS for the year ended on December 31, 2012 in the amount of \$456. As such, the transaction on March 18, 2013, did not require an additional impairment by Piedmont. Simultaneously with the transaction, FAvS paid-off its Term Loan in the amount of \$4,000 on March 18, 2013, thereby releasing the guarantee issued to the lending bank by the Piedmont. Accordingly the restricted deposit associated with the above guarantee, was released as well as of March 18, 2013.

## b. Financial information

The FAvS audited consolidated financial statements as of December 31, 2012, which were signed on March 20, 2013, included a restatement for their 2011 consolidated financial statements for the correction of errors in its previously reported amounts.

Company's management reviewed the restatement and its affect on the consolidated financial statements of the Company and found it to be immaterial. Accordingly, no restatement was recorded in the Company's consolidated financial statements.

Due to losses incurred on maintenance contracts in 2010, Company's management performed an impairment test, as of December 31, 2010, on its investment in FAvS. As a result, the Company recorded an impairment charge of \$1,813 on its investment in FAvS as of December 31, 2010, based on this impairment test, which was performed by management with the assistance of a third party valuation firm.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 3 - ACQUISITION (CONT)

## b. Financial information (cont)

Condensed financial information from FAvS consolidated balance sheets as of December 31, 2012 and 2011:

	December 31,	
	2012	2011
Current assets	\$ 31,090	\$ 51,973
Long-term assets	9,742	10,080
Total assets	40,832	62,053
Current liabilities	31,476	38,432
Long-term liabilities	35,672	44,463
Total liabilities	\$ 67,148	\$ 82,895

Condensed financial information from FAvS consolidated statements of operations for each of the two years in the period ended December 31, 2012:

	Year ended December 31,	
	2012	2011
Net sales	\$ 21,579	\$ 20,515
Gross profit	9,202	8,626
Income (loss) from continuing operations	(1,476)	630
Net loss	(12,979)	(94)
Loss attributable to common stockholders	\$ (13,271)	\$ (345)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 3 - ACQUISITION (CONT)

## b. Financial information (cont)

A reconciliation of the share in results of affiliated company, impairment of share in affiliated company and gain from dilution of interests in affiliated company for each of the years ended December 31, 2012 and 2011:

	Year ended December 31,	
	2012	2011
Share in income (loss) related to common stockholders	\$ (653)	\$ 192
Share in income related to preferred stock	197	139
Impairment of in affiliated company	(3,300)	-
Gain from dilution of interests in affiliated company	-	240
	<u>\$ (3,756)</u>	<u>\$ 571</u>

## NOTE 4 - AVAILABLE-FOR-SALE - MARKETABLE SECURITIES

	December 31, 2012		
	Amortized Cost	Gross Unrealized Gains	Fair Value
<b>Available-for-sale:</b>			
Money Market	<u>\$ 3,341</u>	<u>\$ -</u>	<u>\$ 3,341</u>
	December 31, 2011		
	Amortized Cost	Gross Unrealized Gains	Fair Value
<b>Available-for-sale:</b>			
Money Market	<u>\$ 1,025</u>	<u>\$ -</u>	<u>\$ 1,025</u>
Auction Rate Securities (1)	<u>1,900</u>	<u>-</u>	<u>1,900</u>
	<u>\$ 2,925</u>	<u>\$ -</u>	<u>\$ 2,925</u>

- (1) Auction Rate Securities ("ARS") are a type of long-term bonds (usually issued for a period longer than ten years) issued by corporates, local authorities, institutions of higher education and others for securitization of assets. The ARS bear a variable interest rate, re-determined by an auction held every short period. The ARS interest held by the Company was re-determined every 7, 28 or 35 days and will mature on 2019. The ARS held by the Group were issued by SSM Health Care of Oklahoma City, Illinois and Wisconsin municipalities.

In 2012, the Group realized \$100 of the ARS held for its par value and later in the year realized its entire investment for a consideration of \$1,800 which approximated its book value.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 4 - AVAILABLE-FOR-SALE - MARKETABLE SECURITIES (CONT)

In the year 2011, the Company realized \$50 of the ARS held for its par value.

During the year ended December 31, 2010, the Company recorded an other-than-temporary impairment loss of \$200 on Auction Rate Securities based on its estimated fair value.

## NOTE 5 - FAIR VALUE MEASUREMENT

## Recurring Fair Value Measurements

The Group measures fair value and discloses fair value measurements for financial assets and liabilities. Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Company's financial assets measured at fair value on a recurring basis, consisted of the following types of instruments:

	December 31, 2012			
	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Money Market	\$ 3,341	\$ -	\$ -	\$ 3,341
Derivatives	-	27	-	27
Total	<u>\$ 3,341</u>	<u>\$ 27</u>	<u>\$ -</u>	<u>\$ 3,368</u>
	December 31, 2011			
	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Money Market	\$ 1,025	\$ -	\$ -	\$ 1,025
Auction Rate Securities	-	-	1,900	1,900
Total	<u>1,025</u>	<u>-</u>	<u>1,900</u>	<u>2,925</u>
<b>Liabilities:</b>				
Derivatives	<u>\$ -</u>	<u>\$ 372</u>	<u>\$ -</u>	<u>\$ 372</u>

Consistent with the Company's investment policy guidelines, the ARS investments held by the Company all had AA credit ratings at the time of purchase.

The carrying amounts of financial instruments, include cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, approximate fair value because of their generally short maturities.

The fair values of long-term liabilities were estimated by using level 3 inputs based on discounted future cash flows, using the rate currently available for liabilities of similar terms and maturity. The carrying amount of the Group's long-term liabilities approximates their fair value since interest rate reflects current market rates.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 5 - FAIR VALUE MEASUREMENT (CONT)

The following table includes a roll-forward of the amounts in the balance sheets for the years ended December 31, 2012 and 2011 (including the change in fair value) for auction rate securities classified within level 3 of the fair value hierarchy.

Balance as of January 1, 2011	\$ 1,950
Realized	(50)
Balance as of December 31, 2011	1,900
Realized	(1,900)
Balance as of December 31, 2012	\$ -

## Non-Recurring Fair Value Measurements

The following table presents the Group's assets measured at fair value on a non-recurring basis for the years ended December 31, 2012 and 2011:

	As of December 31, 2012	Fair value measurements using			Total losses for the year ended December 31, 2012
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
Goodwill (1)	\$ -	\$ -	\$ -	\$ -	\$ 1,015
Investment in affiliated company (2)	\$ 1,264	\$ -	\$ -	\$ 1,264	\$ 3,300

	As of December 31, 2011	Fair value measurements using			Total losses for the year ended December 31, 2011
		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
Property and equipment (3)	\$ 1,325	\$ -	\$ -	\$ 1,325	\$ 1,865
License for service center (3)	\$ -	\$ -	\$ -	\$ -	\$ 1,100
Customer relationships (3)	\$ -	\$ -	\$ -	\$ -	\$ 298

- (1) During the second quarter ended June 30, 2012, management believed that there were indicators of impairment of goodwill in its OEM of Electric Motion System reporting unit and accordingly performed interim goodwill impairment testing as of June 30, 2012, primarily due to a decline in future forecasted sales levels and profitability margins resulting from the continued weakness in the defense industry. Accordingly, the Company performed an impairment test of goodwill for this reporting unit, with the assistance of a third party valuation firm. Based on the results of this test, the Company determined that the entire balance of goodwill included in this reporting unit was impaired and recorded an impairment charge of \$1,015.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 5 - FAIR VALUE MEASUREMENT (CONT)

- (2) In June 2012, FAvS entered into a transaction with its CEO, pursuant to which FAvS borrowed \$3 million from FAvS CEO, secured by a third lien on the assets of FAvS. The loan bears interest at 10% and in addition FAvS CEO was issued warrants to purchase shares of Class A Common Stock of FAvS, representing 15% of FAvS post-exercise shareholders' equity, at an exercise price of \$7.00 per share.

Pursuant to the terms and conditions of the transaction, management believed that there were indicators of impairment with respect to TAT's investment in FAvS. Accordingly, the Company performed an impairment test of its investment in FAvS, with the assistance of a third party valuation firm. Based on the results of this test the Company determined that its investment in FAvS was impaired by \$3,300. The impairment was due to a decline in FAvS' profitability margins and future forecasted sales levels.

- (3) During the year ended December 31, 2011, the Company reviewed the MRO services for Aviation Components' long lived assets for impairment by estimating the fair value of the operations and the fair value of its specific long lived assets, and comparing those values to the carrying value of the assets. The Company concluded, based on this valuation, that certain fixed assets and intangible asset 'License for Service Center' amounting to \$1,865 and \$1,100, respectively at its MRO services for Aviation Components operating segment were impaired. In addition, due to management estimates of a continuing decline in sales levels in the OEM of Electric Motion Systems operating segment, resulting from the weakness in the Israeli defense market, the Company reviewed indications for impairment of certain identifiable assets in this segment. Accordingly, the Company reviewed these assets for impairment by estimating their fair value based on their net selling price and comparing those values to the carrying value of the assets. As a result the Company concluded that the intangible asset 'Customer Relations' at its OEM of Electric Motion Systems operating segment in the amount of \$298 was impaired.

Accordingly, the Company recorded a total of \$3,263 impairment charges in the year ended December 31, 2011 to reflect the fair value of the long lived assets mention above.

## NOTE 6 - INVENTORIES, NET

Inventories are composed of the following:

	December 31,	
	2012	2011
Raw materials and components	\$ 12,321	\$ 11,832
Work in process	16,145	16,652
Spare parts	3,897	2,243
Finished goods	668	576
	<u>\$ 33,031</u>	<u>\$ 31,303</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 6 - INVENTORIES, NET (CONT)

Inventories are net of reserve for slow moving and surplus production and write down of inventory (as mentioned below) in the amount of \$6,569 and \$6,589 at December 31, 2012 and 2011, respectively.

During the year ended December 31, 2011, the Company recorded a write down of inventory in the amount of \$2,500 attributable to inventory of the MRO services for aviation components segment. The write down was due to management's estimation of the continued decline in future forecasted sales levels and decline in profitability margins in certain product lines in this operating segment, which were lower than previously anticipated, resulting from the weakness in these areas of business, and was recorded under cost of revenues.

During the year ended December 31, 2010, the Company recorded a write down of inventory in the amount of \$3,500 attributable to inventory of the MRO services for aviation components segment. The write down was due to a decline in future forecasted sales levels, and was recorded under cost of revenues.

In 2012 and 2011, approximately \$669 and \$844, respectively, of inventory previously written-down were used or sold in the course of providing MRO services.

## NOTE 7 - PROPERTY, PLANT AND EQUIPMENT, NET

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

	December 31,	
	2012	2011
Cost:		
Land and buildings	\$ 6,929	\$ 6,518
Machinery and equipment (1)	36,849	35,176
Motor vehicles	676	869
Office furniture and equipment	2,293	2,189
Software	1,166	955
	<u>47,913</u>	<u>45,707</u>
Less: Accumulated depreciation	<u>35,003</u>	<u>32,768</u>
Depreciated cost	<u>\$ 12,910</u>	<u>\$ 12,939</u>

(1) The cost is net of investment grants received by Bental in the amount of \$274 and \$326 as of December 31, 2012 and 2011.

Depreciation and amortization expenses amounted to \$2,403, \$2,732 and \$2,719 for the years ended December 31, 2012, 2011 and 2010, respectively (depreciation and amortization expenses do not include impairment charges).

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 7 - PROPERTY, PLANT AND EQUIPMENT, NET (CONT)

During the year ended December 31, 2011, the Company recorded impairment of property, plant and equipment in the amount of \$1,865, attributable to certain property and equipment items of the MRO services for aviation components segment, based on estimations of the fair value of these assets. The impairment charge was recorded under the cost of revenues item in the consolidated statements of operations.

During the year ended December 31, 2010, the Company recorded impairment of property, plant and equipment in the amount of \$183 attributable to certain machinery and equipment items of the MRO services for aviation components segment based on the reduced forecasted usage of these items, and was recorded as an expense under the cost of revenues item in the consolidated statements of operations.

Liens on property, plant and equipment are discussed at note 13(f).

## NOTE 8 - GOODWILL AND INTANGIBLE ASSETS

## a. Intangible assets:

	December 31,	
	2012	2011
Cost:		
Customer relationships	\$ 865	\$ 865
License for service center	2,050	2,050
Others	136	136
	3,051	3,051
Accumulated amortization and impairment charges:		
Customer relationships	865	865
License for service center	2,050	2,050
Others	136	136
	3,051	3,051
Amortized cost	\$ -	\$ -

Amortization expenses amounted to \$539 and \$663 for the years ended December 31, 2011 and 2010, respectively (amortization expenses do not include impairment charges).

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 8 - GOODWILL AND INTANGIBLE ASSETS (CONT)

## a. Intangible assets (cont):

For the year ended December 31, 2011, due to decrease in the anticipated profit margins the Company recorded an impairment charge for its intangible assets in the total amount of \$1,398, under cost of revenues. This amount is comprised of impairment charge in the amount of \$1,100 (the entire asset was written off) in connection with the "Authorized service center" intangible asset at the MRO services for Aviation Components operating segment and \$298 (the entire asset was written off) in connection with the 'Customer Relations' intangible asset at its OEM of Electric Motion Systems operating segment (see also note 5(3)).

For the year ended December 31, 2010 the Company recorded an impairment charge in the amount of \$481 of customer relationship, at the MRO services for Aviation Components operating segment, under operating expenses. The Company estimated the fair value of its intangible assets using a discounted cash flow analysis and compared those values to the carrying value of the assets. The Company concluded, based on this comparison, that Customer relationship intangible asset was impaired at its MRO services reporting unit. The Company recorded a \$481 impairment charge and wrote off this asset in the year ended December 31, 2010.

## b. The changes in the carrying amounts of goodwill by reportable segment for the fiscal years ended December 31, 2012 and 2011 are as follows:

	<b>OEM - Electric Motion Systems</b>	<b>Heat Transfer Services and Products</b>	<b>MRO services for Aviation Components</b>	<b>Total</b>
Balance as of January 1, 2011	\$ 1,156	\$ -	\$ -	\$ 1,156
Effect of changes in exchange rate	(114)	-	-	(114)
Balance as of December 31, 2011	1,042	-	-	1,042
Effect of changes in exchange rate	(27)	-	-	(27)
Goodwill impairment	(1,015)	-	-	(1,015)
Balance as of December 31, 2012	-	-	-	-
Goodwill, gross, at December 31, 2012	1,015	456	4,091	5,562
Accumulated impairment losses	(1,015)	(456)	(4,091)	(5,562)
Goodwill, net, at December 31, 2012	\$ -	\$ -	\$ -	\$ -



NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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U.S. dollars in thousands

## NOTE 8 - GOODWILL AND INTANGIBLE ASSETS (CONT)

## c. Impairment Assessments

During the quarter ended June 30, 2012, management believed that there were indicators of impairment of goodwill in its OEM of Electric Motion System reporting unit as of June 30, 2012, primarily due to a decline in future forecasted sales levels and profitability margins resulting from the continued weakness in the defense industry. Accordingly, the Company performed an impairment test of goodwill for this reporting unit, with the assistance of a third party valuation firm. Based on the results of this test, the Company determined that the entire balance of goodwill included in this reporting unit was impaired and recorded an impairment charge of \$1,015.

The Company determined the fair value of the OEM of Electric Motion Systems reporting unit using the discounted cash flows method. The material assumptions used for 2012 annual test were five years of projected net cash flows (in accordance with the Company's budget), a discount rate of 17.72% and a long-term growth rate of 2.0%. The Company considered historical rates and current market conditions when determining the discount and growth rates to use in its analyses.

During the year ended December 31, 2011, the Company determined under the first step of its annual test that the fair value of the OEM of Electric Motion Systems reporting unit is greater than its carrying amount. Based on the results of this test the Company determined that the goodwill related to the said reporting unit was not impaired.

In 2011, the fair value of the OEM of Electric Motion Systems reporting unit exceeded its carrying value by approximately \$100, or 1.1% and thus was at risk of failing step one of the goodwill impairment test, and was therefore at risk of a future impairment in the event of unfavorable changes in the forecasted cash flows or the key assumptions used in the analysis, including the weighted average cost of capital (discount rate) and growth rates utilized in the discounted cash flow analysis.

The Company determined the fair value of the OEM of Electric Motion Systems reporting unit using the discounted cash flows method. The material assumptions used for 2011 annual test were three years of projected net cash flows (in accordance with the Company's budget), a discount rate of 18% and a long-term growth rate of 1.95%. The Company considered historical rates and current market conditions when determining the discount and growth rates to use in its analyses.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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## U.S. dollars in thousands

## NOTE 8 - GOODWILL AND INTANGIBLE ASSETS (CONT)

## c. Impairment Assessments (cont):

During the year ended December 31, 2010, the Company performed its annual impairment test of goodwill. During this year, the Company encountered adverse changes in the business climate including a weak U.S. and global economy which resulted in a reduction in demand for the MRO services. As a result of these factors, management revised its future cash flow expectations, which lowered the fair value estimates of a certain reporting unit. The Company determined under the first step of its annual test that the fair value of goodwill at its MRO services reporting unit was less than the carrying value for this reporting unit. The Company recorded a \$4,223 impairment charge (which was the entire remaining goodwill for this reporting unit) in the third quarter of 2010, to reduce the carrying value of goodwill down to the implied fair value of goodwill for the MRO services reporting unit.

The Company determined the fair value of the MRO services reporting unit using the discounted cash flows method. The material assumptions used for 2010 annual test were four years of projected net cash flows (in accordance with the Company's budget), a discount rate of 20.0% and a long-term growth rate of 2.79%. The Company considered historical rates and current market conditions when determining the discount and growth rates to use in its analyses.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 9 - OTHER BALANCE SHEETS SUPPLEMENTALS

## a. Other accounts receivable and prepaid expenses:

	December 31,	
	2012	2011
Deferred tax asset	\$ 2,122	\$ 2,564
Government authorities	1,424	1,818
Prepaid expenses	831	809
Income receivables and grants	33	254
Derivatives	27	-
Other	96	216
	<u>\$ 4,533</u>	<u>\$ 5,661</u>

## b. Other account payable and accrued expenses:

	December 31,	
	2012	2011
Employees and payroll accruals	\$ 3,358	\$ 3,608
Accrued expenses (1)	1,757	688
Government authorities	673	570
Advances from customers	731	557
Warranty provision	276	288
Accrued royalties	268	316
Derivatives	-	372
Deferred tax liability	126	179
Other accrued expenses	106	92
	<u>\$ 7,295</u>	<u>\$ 6,670</u>

- (1) Includes \$750 royalties payable to a supplier in the MRO business, following the reconciliation of an audit.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 10 - TRANSACTIONS WITH RELATED PARTIES

## a. Transactions with TAT Industries:

	Year ended December 31,		
	2012	2011	2010
Management fees (1)	\$ 50	\$ 50	\$ 50
Lease expenses (2)	\$ 416	\$ 408	\$ 371

- (1) According to the agreement between TAT and TAT Industries, TAT Industries will pay the Company an annual management fee in the amount of \$50. The management fees are recorded as a reduction of general and administration expenses.
- (2) During 2000, TAT entered into a lease agreement with TAT Industries, pursuant to which the Company leases from TAT Industries approximately 344,000 square feet, including 90,000 square feet of manufacturing, office and storage space, for a period of 24 years and eleven months for an annual rental fee which is subject to revaluation every fifth year by a real estate appraiser, with an additional incremental payment of 2% per year.

In 2010, following a revaluation by a real estate appraiser, the rental fee was increased to \$400 per year with an additional incremental payment of 2% per year. The rental fee will be revaluated again in 2015 (the "Next Revaluation"). The Company's Audit Committee has reapproved the said agreement until the Next Revaluation.

## b. Balances with related parties:

	December 31,	
	2012	2011
KMN Capital (USA) Inc. - current asset	\$ -	\$ 94
TAT Industries - current asset (1)	54	724
Total asset	\$ 54	\$ 818
Bental Non controlling interest - current liability	\$ (60)	\$ (85)
FAVS - current liability	(29)	(80)
Isal Amlat Investment (1993) Ltd.	(23)	-
Total liability	\$ (112)	\$ (165)

- (1) Results from certain expenses incurred by TAT Industries and borne by the Company. The debt bears interest at the rate equal to the interest rate agreed between TAT Industries and its lending banks.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 10 - TRANSACTIONS WITH RELATED PARTIES (CONT)

- c. Transactions with related parties:

	Year ended December 31,		
	2012	2011	2010
Management fees to shareholders (see item e below)	\$ 359	\$ 400	\$ 400

- d. Bental is engaged in various agreements with the Non controlling interest and other related parties for the rental, maintenance and other services provided to it, in connection with its plant and operations. Total amount paid by Bental for these services in 2012 and 2011 was \$505 and \$526, respectively.
- e. In March 2012, the audit committee and the board of directors of TAT approved a new three-year management agreement with Isal Amlat Investment (1993) Ltd. ("Isal Amlat") commencing as of February 8, 2012 (the "New Management Agreement"). Each of TAT and Isal Amlat shall be entitled to terminate the New Management Agreement subject to a prior written notice of 4 months. Pursuant to the New Management Agreement, in consideration of the management services provided by Isal Amlat, TAT pays Isal Amlat management fees in a total annual amount of NIS 1,500,000 (approximately \$400), linked to the Consumer Price Index to be paid on a monthly basis, plus VAT. In addition, Isal Amlat is entitled to repayment of expenses actually borne as part of providing the management services. The audit committee and board of directors of the Company will examine on a yearly basis, the management services actually provided to the Company, and shall examine whether a material change has occurred justifying the update of the management fees and/or the conditions of the New Management Agreement. The New Management Agreement was approved by the shareholders of TAT on June 28, 2012.

On August 21, 2012, the board of directors of TAT approved, following an approval of TAT's audit committee, a change to the New Management Agreement with Isal Amlat, effective from such date according to which the scope of the services provided by Isal Amlat to TAT were reduced and the annual management fees were also reduced by a total amount of NIS 570,000 (approximately \$150 - the "reduced amount").

Total amount paid by TAT for the management services in 2012, 2011 and 2010, was \$359, \$397 and \$408, respectively. The Agreement is subject to the approval of the Company's shareholders.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 10 - TRANSACTIONS WITH RELATED PARTIES (CONT)

In addition, the Company will receive management services from a private company ("Management company") controlled by Mr. Nathan Galili ("Galili"), CEO of KNM Industries Ltd. (a private company through which Isal Amlat indirectly holding control in the Company). The management services will consist of a half-time of Galili, which value is more than the reduced amount, and will additionally include its services as active chairman of Bental. For those services the Company will pay the Management company annual management fees equal to the reduced amount, in addition to NIS 7,000 (approximately \$2, plus VAT), as a monthly remuneration for travelling expenses to Bental. In addition, if during the service period or within a twelve month period from the end of the service period the Company will sell its holding in Bental, for more than \$6,600 ("low threshold"), then the Management company will be eligible for a bonus which will be determined as follows:

2% out of the 1st million above the low threshold, the Company will receive for its holding in Bental, plus an additional 3% out of the 2nd million above the low threshold the Company will receive for its holding in Bental, plus an additional 5% out of the 3rd million above the low threshold the Company will receive for its holding in Bental. It is clarified that in any event the amount of the bonus shall not exceed \$100.

Such management services will be provided until February 8, 2015 (the end of term of the new management agreement with Isal Amlat). Each of the parties (TAT and the Management company) may terminate the agreement with a prior written notice of four months.

On January 27, 2013, TAT informed Isal Amlat that no management services had been provided by Isal Amlat to TAT during the preceding months, and that TAT decided to immediately terminate the Management Agreement. At that date TAT ceased paying management fees.

On February 8, 2013, Mr. Galili informed TAT on the termination of the engagement with TAT, effectively immediately while management fees will be paid throughout June 8, 2013 at the end of the four-month notice period.

- f. On August 13, 2009, TAT's Audit Committee and Board of Directors approved the appointment of Mr. Avi Ortal as CEO of TAT's subsidiary, Limco-Piedmont simultaneously with serving as CEO of KMN Capital (USA) Inc., Mr. Ortal relocated to the U.S. and devoted his time to serving as CEO of the said companies. Mr. Ortal received a salary of approximately \$180 a year including a car and an insurance policy for his office as CEO of Limco-Piedmont. Furthermore, Mr. Ortal was entitled to a sum of approximately \$180 for his office as CEO of KMN Capital (USA) Inc., Limco-Piedmont bore the actual overall employment costs of Mr. Ortal as CEO of Limco-Piedmont and as CEO of KMN Capital (USA) Inc., KMN Capital (USA) Inc., reimbursed Limco-Piedmont for 50% of said costs. In April 2011, Mr. Ortal advised TAT's Board of Directors of his intention to terminate his employment with Limco-Piedmont on July 31, 2011. On May 18, 2011, Mr. Ortal entered into a Consulting Agreement with TAT, effective for a period of eight months following the termination of his employment, to provide part-time consulting services to TAT with respect to its U.S. based subsidiaries. Mr. Ortal will receive consulting fees of \$20 per month for such services. A total of \$180 was paid to Mr. Ortal upon his termination of employment. As of December 31, 2011, no further obligations remain to be provided by the Company to Mr. Ortal.
- g. On June 14, 2010, TAT and Bental signed a management services agreement. TAT agreed to provide Bental with various services including investor relations, business development, marketing and advertising consulting, legal services and the appointing of TAT personnel in Bental board of directors. The agreement is effective as of January 1, 2010 and the annual management fees are in the amount of \$120.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 10 - TRANSACTIONS WITH RELATED PARTIES (CONT)

- h. In December 2009, Piedmont provided a guarantee for a period of one year up to \$ 7,000 in respect of FAvS' debt taken in connection with the acquisition of AeTR. As of December 31, 2012, the guarantee amount is \$4,600 (such guarantee was released on March 18, 2013, see also note 3(a)).
- i. On September 7, 2011, TAT received a loan from Bental for the total amount of NIS 2.5 million (approximately \$700), to be repaid in whole at the end of a 24 month period (the "Term"). The principal amount bears interest of Prime + 1% payable on a quarterly basis and may be repaid at any time during the term upon TAT's discretion. Simultaneously with such loan, Bental received a loan from an Israeli bank for similar amount under similar terms and conditions.

## NOTE 11 - SHORT TERM BANK CREDIT AND LONG TERM LOANS

- a. Terms of the loans and balances:

	Currency of loan	Interest Rate December 31, 2012	Years of Maturity	December 31, 2012
Long-term loan (1)	NIS	5.25%	2012-2014	\$ 523
Long-term loan (2)	\$	2.50%-3.50%	2009-2014	2,477
Long-term loan (3)	NIS	Prime + 1%	2013	670
				3,670
Less - current maturities (1)				(290)
Less - current maturities (2)				(1,594)
Less - current maturities (3)				(670)
				\$ 1,116
	Currency of loan	Interest Rate December 31, 2011	Years of Maturity	December 31, 2011
Long-term loan (1)	NIS	5.25%	2012-2014	\$ 795
Long-term loan (2)	\$	2.50%-3.50%	2009-2014	3,252
Long-term loan (3)	NIS	Prime + 1%	2013	655
				4,702
Less - current maturities (1)				(282)
				\$ 4,420

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 11 - SHORT TERM BANK CREDIT AND LONG TERM LOANS (CONT)

Required principal payments (including current maturities) as of December 31, 2012, are as follows:

Year	Amount
2013	\$ 2,554
2014	1,116
	<u>\$ 3,670</u>

- (1) The original loan was received by Bental in 2009 from an Israeli bank in the amount of \$1,400 to be repaid in quarterly installments over a five years period, commencing 2010. On June 30, 2010, the remaining balance of the original loan, in the amount of \$1,185, was repaid and a new loan in the same amount was taken. This new loan bears annual fixed interest of 5.25% and will be repaid until August 2014 in quarterly installments. The loan balance as of December 31, 2012 and 2011 was \$523 and \$795, respectively (with regard to covenants related to such loan see note 13(f)(3)).
- (2) Loans received by TAT from an Israeli bank in a total amount of \$6,250 out of which \$5,000 were received during year 2008 and additional \$1,250 were received during year 2009. The loans amount was to be repaid in four annual installments commencing 2011. These loans bear quarterly interest of Libor + 3.5% and Libor + 1.85%, respectively. In May 2011, TAT repaid \$750 of principal, in accordance with the original installments schedule. On November 7, 2011, TAT prepaid \$2,250. On November 6, 2012, TAT prepaid \$775, following which the remaining balance was \$2,477. In September, 2011, TAT reached agreement with its lending bank to adjust certain financial covenants related to the said loans it was failing to meet at the time. Accordingly, as of December 31, 2012 the Company meets all financial covenants related to such loans (see also note 13(f)(2)).
- (3) On September 7, 2011, Bental received a loan from an Israeli bank in a total amount of NIS2.5 million (approximately \$700), to be repaid in whole at the end of a 24 month period (the "Term"). The principal amount bears interest of Prime + 1% payable on a quarterly basis and may be repaid at any time during the term upon Bental's discretion. The loan balance as of December 31, 2012 and 2011 was \$670 and \$655, respectively (see also note 10(i)).
- (4) In addition, as of December 31, 2012 Piedmont's bank credit balance amounted to \$32.

Group provided certain guarantees and covenants, to secure its long-term loans, see note 13(e) and 13(f).



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 11 - SHORT TERM BANK CREDIT AND LONG TERM LOANS (CONT)

## b. Line of credit

On November 15, 2011, Limco-Piedmont renewed its line of credit with a U.S bank for an additional 21 month period ending on August 31, 2013, for borrowings of up to \$10,000 under certain conditions. \$5,000 of this amount will stand for Limco and \$5,000 will stand for Piedmont. The line of credit bears interest of Libor + 1.5%, and its utilization is subject to compliance with financial covenants agreed between the parties. As of December 31, 2012 and 2011, approximately \$688 and \$4,340, respectively of the total line of credit was utilized by Limco and Piedmont. In addition, as of December 31, 2012 and 2011, Limco-Piedmont met all financial covenants related to such line of credit (see also note 13(f)(1)).

## NOTE 12 - LONG-TERM EMPLOYEE-RELATED OBLIGATIONS

## Severance pay:

TAT's and Bental's (the "Israeli companies") liability for severance pay, for their Israeli employees, is calculated pursuant to Israeli Severance Pay Law based on the most recent salary of the employees multiplied by the number of years of employment as of the balance sheet date. The liability is presented on the undiscounted basis. The Israeli companies record an expense for the net increase in its severance liability.

TAT's liability for all of its Israeli employees is fully covered for by monthly deposits with severance pay funds, insurance policies, Mivtahim Social Insurance Institution Ltd. ("Mivtahim") and by an accrual. The liability covered by deposits with Mivtahim is irrevocably transferred to Mivtahim. Accordingly, neither the amounts accumulated with Mivtahim, nor the corresponding liabilities for severance pay are reflected in the consolidated balance sheet.

The deposited funds include profits accumulated up to the balance sheet date. The deposited funds may be withdrawn only upon the fulfillment of the obligation pursuant to Israeli Severance Pay Law or labor agreements. The value of the deposited funds is based on the cash surrender value of these policies and includes profits (or loss) accumulated through the balance sheet date.

Severance pay expenses for the Israeli companies were \$501, \$495 and \$425 for the years ended December 31, 2012, 2011 and 2010, respectively.

Limco-Piedmont sponsors a 401(K) profit sharing plan covering substantially all of its employees. The plan permits the employer to contribute a discretionary amount for a plan year, which the employer designates a qualified non-elective contribution. Contributions to plan by Limco-Piedmont were \$209, \$188 and \$167 for the years ended December 31, 2012, 2011 and 2010, respectively.

The Group expects to contribute approximately \$730 in 2013 to the pension funds and insurance companies in respect of their severance and pension pay obligations.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 12 - LONG-TERM EMPLOYEE-RELATED OBLIGATIONS (CONT)

The Israeli companies are required to make severance payment upon dismissal of an employee or upon termination of employment in certain circumstances. The severance payment liability to the employees (based upon length of service and the latest monthly salary - one month's salary for each year employed) is recorded on the Company's balance sheets under "Employee rights upon retirement." The liability is recorded as if it were payable at each balance sheet date on an undiscounted basis.

The liability is funded in part from the purchase of insurance policies or by the establishment of pension funds with dedicated deposits in the funds. The amounts used to fund these liabilities are included in the balance sheets under "Liability in respect of employee rights upon retirement." These policies are the Company's assets. However, under employment agreements and subject to certain limitations, any policy may be transferred to the ownership of the individual employee for whose benefit the funds were deposited. In the years ended December 31, 2012, 2011 and 2010, the Israeli companies deposited \$292, \$313 and \$281, respectively, with insurance companies in connection with its severance payment obligations.

In accordance with the current employment agreements with certain employees, the Israeli companies make regular deposits with certain insurance companies for accounts controlled by each applicable employee in order to secure the employee's rights upon retirement. The Israeli companies are fully relieved from any severance pay liability with respect to each such employee after they make the payments on behalf of the employee. The liability accrued in respect of these employees and the amounts funded, as of the respective agreement dates, are not reflected in the Israeli Companies balance sheets, as the amounts funded are not under the control and management of the Israeli companies and the pension or severance pay risks have been irrevocably transferred to the applicable insurance companies (the "Contribution Plans").

The amounts of severance payments, actually paid to retired employees, by the Israeli companies were \$109, \$43 and \$253 for the years ended December 31, 2012, 2011 and 2010.

The Israeli companies expect to pay \$2,513 in future benefits to their employees during 2012 to 2021 upon their normal retirement age - see breakdown below. The amount was determined based on the employee's current salary rates and the number of service years that will be accumulated upon the retirement date. These amounts do not include amounts that might be paid to employees that will cease working for the Israeli companies before their normal retirement age.

Year	Amount
2013	\$ 458
2014	211
2015	298
2016	299
2017	182
Thereafter (through 2021)	1,065
	<u>\$ 2,513</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 13 - COMMITMENTS AND CONTINGENT LIABILITIES

## a. Commissions arrangements:

The group is committed to pay marketing commissions to sale agents at a range of 1% to 12% of total sales contracts which were received through promotion and distribution carried out by them. Commission expenses were \$701, \$626 and \$750 for the years ended December 31, 2012, 2011 and 2010, respectively. The commissions were recorded as part of the selling and marketing expenses.

## b. Royalty commitments:

- (1) TAT is committed to pay royalties to third parties through 2012, of ranging between 9% to 17% of sales of products developed by the third parties. Royalty expenses were \$202, \$460 and \$328 for the years ended December 31, 2012, 2011 and 2010, respectively. The royalties were recorded as part of the cost of revenues.
- (2) Limco-Piedmont is committed to pay royalties to a third party, ranging between 3% to 5% of sales of products purchased from the third party, after deducting related costs incurred by Limco-Piedmont. That third party is the exclusive manufacturer of the products for which Limco-Piedmont provide MRO services. In addition, Limco-Piedmont is committed to pay said third party royalties, ranging between 1.5% to 10% of sales of additional products exclusively manufactured by the third party. Royalty expenses were \$232, \$201 and \$111 for the years ended December 31, 2012, 2011 and 2010, respectively. The royalties were recorded as part of the cost of revenues.
- (3) Bental is committed to pay royalties to the Israeli government on proceeds from the sales of products, in the research and development of which the Israeli government participated by way of grants. Under the terms of Bental's funding from the Office of the Chief Scientist, royalty payments are computed on the portion of sales from such products at a rate of 2% and 3.5%. The commitment to the Chief Scientist is limited to the amount of the received participation (U.S. dollar linked), with the addition of an annual interest rate based on Libor. As of December 31, 2012 and 2011, the total amount of royalty bearing grants due by Bental to the Chief Scientist was approximately \$86 and \$82, respectively.

## c. Lease commitments:

Limco-Piedmont leases some of its operating and office facilities for various terms under long-term, non-cancelable operating lease agreements. The leases expire at various dates through 2017. The monthly rental expense ranges from approximately \$3.5 to \$8. Certain leases contain renewal options as defined in the agreements. Lease expense (excluding related parties) totaled \$126, \$258 and \$246 for the years ended December 31, 2012, 2011, and 2010 respectively.

TAT leases its factory from its TAT Industries until 2020; (416\$ for the year ended December 31, 2012, see also note 10(a)).

Bental leases an area of its plant from a related party for \$50 per annum, under a long-term lease until 2013.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 13 - COMMITMENTS AND CONTINGENT LIABILITIES

## c. Lease commitments (cont):

As of December 31, 2012, future minimum rental payments under non-cancelable operating leases are as follows:

Year	Amount
2013	\$ 601
2014	610
2015	618
2016	627
2017	559
Total	\$ 3,015

## d. Legal claims contingencies

- (1) For details about the settlement of the commercial dispute between Piedmont and FAvS See note 3(a).
- (2) On November 29, 2011, a Factoring company ("the plaintiff"), filed a claim with the magistrates court in Tel-Aviv against the Company, Bental and ten others ("the respondents"), jointly and severally, for the amount of 6,151 thousand NIS (approximately \$1,620). The plaintiff's case against the Company and Bental is based on invoices that were presented to the plaintiff by supplier of the Company and Bental ("the supplier"), by virtue of assignment of rights, which were originally issued to the Company and Bental by the supplier for certain alleged services. On February 5, 2012, the Company and Bental filed for its statement of defense, in which it denied the plaintiff's claims and clarified that it acted according to the deed of assignment of rights, and that the invoices neither represent nor reflect real transactions and/or real services which were rendered. The Company and Bental and their legal advisor are of the opinion that their exposure due to the claim filed is not probable to be materialized and thus no provision was recorded in regard of that claim of December 31, 2012.

## e. Guarantees:

- (1) Bental provides bank guarantees to third parties, in the ordinary course of business, mainly in order to secure certain advances from customers. The maximum credit risk for these guarantees totaled approximately \$97 as of December 31, 2012.
- (2) In order to secure TAT's liability to the Israeli customs, the Company provided a bank guarantee in the amount of \$157. The guarantee is linked to the consumer price index and is valid until December 2013.
- (3) See also note 13(f) for restricted cash deposit against certain loans and guarantees.
- (4) See also note 10(h) for details of a guarantee provided by Piedmont in respect of FAVS debt. As of December 31, 2012, the amount of this guarantee is \$4,600 (such guarantee was released on March 18, 2013, see also note 3(a)).

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 13 - COMMITMENTS AND CONTINGENT LIABILITIES (CONT)

## f. Covenants and liens on assets:

- 1) In connection with its line of credit, Limco-Piedmont is obligated to meet minimal borrowing base and certain financial covenants. The utilization of the credit line is subject to compliance with the following financial covenants as agreed with the lending U.S bank:
  - (i) Tangible net worth of not less than \$51,500 (on August 20, 2012 concluded with the U.S bank to set this covenant at \$49,500). As of December 31, 2012 and 2011 Limco-Piedmont's tangible net worth was \$51,533 and \$53,879, respectively;
  - (ii) Total liabilities to tangible net worth ratio of less than 1.0. As of December 31, 2012 and 2011 Limco-Piedmont's leverage was 0.18 and 0.25, respectively; and
  - (iii) Net financial assets of not less than \$10,000. As of December 31, 2012 and 2011 Limco-Piedmont's net financial assets amount was \$20,667 and \$24,554, respectively.

Accordingly, as of December 31, 2012 and 2011 Limco-Piedmont met all financial covenants.

- 2) In order to secure bank loans in the remaining amount of \$2,477 as of December 31, 2012, TAT granted a specific lien on Bental's shares held by TAT and designated certain deposit in the amount of \$350 for pledge upon request from the bank (such amount was released on November 7, 2012 together with the prepayment of \$775 - see also note 11 (a)(2)). In addition, TAT is obligated to meet certain covenants including:
  - (i) TAT's shareholders' equity will not be less than \$30,000 and 30% out of its total assets. As of December 31, 2012 and 2011 TAT's shareholders' equity was \$82,233 and \$86,370, representing 76% and 75%, respectively of its total assets);
  - (ii) Bental's net debt (less cash and designated certain deposit) to its operational profit ratio will be less than 4.0. As of December 31, 2012 Bental has net financial assets. As of December 31, 2011 the ratio was 1.1.
  - (iii) Bental's shareholders' equity will not be less than NIS 25 million (approximately \$6,550) and 50% of its total assets (as of December 31, 2012 and 2011 Bental's shareholders' equity was NIS34.8 million (approximately \$9,335) and NIS 35.5 million (approximately \$9,300), representing 70% and 68%, respectively of its total assets); and
  - (iv) TAT's holding interest in Bental will not be less than 70% (as of December 31, 2012 and 2011 TAT's holding interest in Bental is 70%).

Accordingly, as of December 31, 2012 and 2011, TAT met all financial covenants as agreed.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 13 - COMMITMENTS AND CONTINGENT LIABILITIES (CONT)

## f. Covenants and liens on assets (cont):

- 3) In order to secure bank loans in the amount of \$1,185 (remaining balance of \$523 as of December 31, 2012), Bental granted floating liens on all of its property and assets, fixed lien on its unpaid share capital and goodwill and first priority liens on its property, plant and equipment, checks and other trading instruments. In addition, Bental is obligated to certain covenants including:
  - (i) Bental's debt to EBITDA ratio will be less than 3.0. As of December 31, 2012 and 2011 the ratio was (2.4) and 2.1, respectively; and
  - (ii) Bental's tangible shareholders' equity will not be less than NIS 20 million (approximately \$5,300) and not less than 30% of its total assets. As of December 31, 2012 and 2011 Bental's tangible shareholders' equity was NIS 34.8 million (approximately \$9,335) and NIS 35.5 million (approximately \$9,300), representing 70% and 69%, respectively of its total assets.

Accordingly, as of December 31, 2012, Bental met all financial covenants as agreed.

- 4) A lien on Bental Approved Enterprise has been registered in favor of the State of Israel (see note 15(b) below).
- 5) In order to secure the guarantee Piedmont provided to FAvS as mentioned on note 10(h), Piedmont granted a lien on a bank deposit in the amount of \$2,300, which is recorded as restricted deposit in the balance sheet as of December 31, 2012.

## NOTE 14 - SHAREHOLDERS' EQUITY

- a. TAT's Ordinary shares confer upon their holders voting rights, the right to receive dividends, if declared, and any amounts payable upon the dissolution, liquidation or winding up of the affairs of TAT.
- b. Treasury purchase plan

On May 21, 2012, TAT's Board of Directors approved a stock repurchase plan under Rule 10b5-1 of the Securities Exchange Act of 1934. The plan was for a period of 6 months and provided for the purchase of shares in an aggregate amount of up to \$0.5 million dollars. Such plan replaced and superseded a prior repurchase plan approved by TAT's Board of Directors on February 21, 2012. On November 21, 2012, the term of such stock repurchase plan ended. As of such date, the Company had purchased 16,433 shares for approximately \$70 thousands (average of \$4.29 per share) constituting less than 0.1% of TAT's issued shares.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 14 - SHAREHOLDERS' EQUITY (CONT)

The repurchased shares became dormant as defined in the Israeli Companies Law.

A reconciliation of opening and closing balances of the number of ordinary shares is presented below:

	2012	2011
Balance outstanding at beginning of year	8,815,003	8,815,003
Purchase of treasury shares	(16,433)	-
Balance outstanding at end of year	8,798,570	8,815,003

## c. Stock option plans

- (1) On August 14, 2008, TAT's Board of Directors approved the grant of 65,477 unregistered options in three Series A, B and C to its Chief Executive Officer. Each option of Series A, B and C vests over two, three and four years commencing May 19, 2008, respectively, and expires three years after vesting. Each Series A, B and C option can be exercised into one Ordinary share NIS 0.9 par value, for an exercise price of \$6.15 (adjusted for dividend distribution and other equity changes as defined in the option grant terms). Alternatively, the Chief Executive Officer can opt to receive TAT's Ordinary shares based on the value of the appreciation over the exercise price.

The weighted average fair value of stock options granted at the grant date, is \$2.69, \$2.9 and \$3.15, for Series A, B and C, respectively, based on the Black-Scholes option-pricing model with the following weighted average assumptions:

	Series A	Series B	Series C
Number of options	21,826	21,826	21,825
Weighted average expected stock price volatility	60.05%	55.96%	54.57%
Weighted average expected option life (in years)	3.25	4.25	5.25
Average risk free interest rate	2.72%	2.94%	3.15%
Dividend yield	0%	0%	0%

The expected volatility is based on the historical volatility of the Company's stock. The risk-free interest rate assumption is based on observed interest rates appropriate for the expected term of the stock options granted. The expected term of options is based on the simplified method as allowed under and ASC 718-10-S99 and 110 issued by the SEC (the "simplified method"). The simplified method assumes the option will be exercised midway between the vesting date and the contractual term of the option. The Company is able to use the simplified method as the options qualify as "plain vanilla" options as defined by ASC 718-10-S99 and since the Company does not have sufficient historical exercise data to provide a reasonable basis to estimate expected term. The dividend yield is derived from the absence of formal dividend distribution plan.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 14 - SHAREHOLDERS' EQUITY (CONT)

## c. Stock option plans (cont)

- (2) Following the approval of TAT's Audit committee and Board of Directors, on June 28, 2012, the Company's shareholders approved the 2012 stock option plan (the "2012 Plan") to grant up to 380,000 options to purchase Ordinary shares, 0.9 NIS par value, of the Company to senior executives and certain members of the Board of Directors, at an exercise price of \$6.5 per share. The Options vest over a three-year period (one-third each year), the vesting of 50% of the Options is subject, in addition, to certain minimum shareholders' equity during a period of 4 years from the grant date, unless the optionee is no longer employed by the Company, in which case the options will be considered forfeited within 30 days. On August 21, 2012, pursuant to the 2012 Plan, TAT's Board of Directors approved the grant of 330,000 Options, which were granted on October 4, 2012 (out of which 45,000 options were forfeited on October 30, 2012).

The fair value of the Company's stock options granted under the 2012 plan for the year ended December 31, 2012 was estimated using the following assumptions:

	2012
Expected stock price volatility	41.57% - 43.4%
Expected option life (in years)	2.23 - 3.23
Risk free interest rate	0.23% - 0.32%
Dividend yield	9.8%

The Company uses the Black-Scholes option pricing model to determine the weighted average fair value of options. The volatility factor used in the Black-Scholes option pricing model is based on historical stock price fluctuations. The expected term of options is based on the simplified method. The Company is able to use the simplified method as the options qualify as "plain vanilla" options as defined by ASC 718-10-S99 and since the Company does not have sufficient historical exercise data to provide a reasonable basis to estimate expected term. Expected dividend yield is based upon historical and projected dividend activity and the risk-free interest rate assumption is based on observed interest rates appropriate for the expected term of the stock options granted.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 14 - SHAREHOLDERS' EQUITY (CONT)

## d. Stock option plans (cont)

(3) The following table is a summary of the activity of TAT's stock Option plan:

	Year ended December 31,					
	2012		2011		2010	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at the beginning of the year	43,652	\$ 6.15	65,477	\$ 6.15	65,477	\$ 6.15
Granted	330,000	6.50	-	-	-	-
Expired	(43,652)	6.15	-	-	-	-
Forfeited	(45,000)	6.50	(21,825)	6.15	-	-
Outstanding at the end of the year	285,000	\$ 6.50	43,652	\$ 6.15	65,477	\$ 6.15
Exercisable options	-	\$ -	43,652	\$ 6.15	21,826	\$ 6.15

The weighted-average grant-date fair value of options granted in 2012 was \$0.19. There was no aggregate intrinsic value for the options outstanding for the years ended December 31, 2012, 2011 and 2010.

Compensation expenses (income) attributable to outstanding stock options were \$8, \$(37) and \$49 for the years ended December 31, 2012, 2011 and 2010, respectively. Compensation expense is recognized in the statement of income as an operating expense based on the fair value of the option over the requisite service period. As of December 31, 2012, there was \$ 19.4 of total unrecognized compensation cost related to nonvested Share based compensation arrangements granted under the Company's 2012 plan. That cost is expected to be recognized over a weighted-average period of 1.44 years.

Following the resignation of Mr. Fledel, the Company's Chief Executive Officer on December 7, 2011 the 21,825 unvested stock options forfeited and the remaining 43,652 stock options expired on March 6, 2012. As result, the Company recorded for the year ended December 31, 2011 an income from the expiration of such options, in the total amount of \$37.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 14 - SHAREHOLDERS' EQUITY (CONT)

- e. Market Maker for TAT shares traded in Tel Aviv Stock Exchange

On August 15, 2011, TAT entered into a Market Making agreement for its shares traded on the Tel Aviv Stock Exchange (TASE) with Harel Finance Trade & Securities Ltd. for the purpose of improving liquidity of TAT shares. The agreement is for a 12 month period, subject for TASE's approval. The agreement will be automatically extended in 12 month periods, unless otherwise terminated by either of the parties giving 30 days notice or in accordance with certain regulatory circumstances. TAT will pay an immaterial fee in connection with the said agreement.

- f. Dividends

On April 22, 2012, TAT's Board declared a cash dividend in the total amount of \$2.5 million (approximately NIS 9.4 million), or \$0.283 per share (approximately NIS 1.065 per share), for all of the shareholders of TAT. The dividend was paid on May 17, 2012 to shareholders of record on May 3, 2012.

- g. Accumulated other comprehensive loss

As of December 31, 2012, the entire amount of accumulated other comprehensive loss consists of amounts derived from foreign currency translation.

## NOTE 15 - TAXES ON INCOME

- a. Measurement of taxable income under the Income Tax (Inflationary Adjustments) Law, 1985 (the "Inflationary Adjustments Law")

In accordance with the Inflationary Adjustments Law, the results for tax purposes have been measured through 2007, and reflected in real terms in accordance with the changes in the Israeli Consumer Price Index (CPI). Under the Inflationary Adjustments Law (Amendment No. 20, 2008, ("the amendment"), that was enacted in the Israeli Parliament on February 26, 2008, the provisions of the Inflationary adjustments law will no longer apply to the Company and Bental in 2008 and thereafter. The amendment specifies transitional provisions regarding the discontinuance of the provisions of the Inflationary adjustments law that have applied to the Company and Bental through the end of 2007.

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

Some facilities of the Israeli companies in Israel have been granted approved enterprise status under the above law.

The main tax benefits available are:

In respect of income derived from the approved enterprise, the Israeli companies were entitled to reduced tax rates during a period of up to seven years from the year in which such enterprise first earn taxable income (limited to twelve years from commencement of production or fourteen years from the date of approval, whichever is earlier).

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 15 - TAXES ON INCOME (CONT)

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

Income derived from the approved enterprise is tax exempt during the first two years of the seven year tax benefit period as above, and is subject to a reduced tax rate not exceeding 25% during the remaining years of benefits.

In the event of distribution of a cash dividend from income which was tax exempt as above, the Company and Bental would have to pay the 25% tax in respect of the amount distributed. Company has policy not to distribute cash dividends from such exempt income. As of December 31, 2012, the Company had accumulated a total amount of approximately \$9,000 of exempt income.

Conditions for the entitlement of benefits

The above mentioned benefits were subject to the fulfillment of the terms specified in the Law, the related regulations and the approval plans as specified above. Failure to fulfill these terms might result the cancellation of the tax benefits (all or some), in which case the Israeli companies will be required to repay all benefits including interest and fines. Management estimates that the Israeli companies comply with all terms as mentioned above.

Preferred Enterprises

Additional amendments to the Law became effective in January 2011 (the "2011 Amendment"). Under the 2011 Amendment, income derived by 'Preferred Companies' from 'Preferred Enterprises' (both as defined in the 2011 Amendment) would be subject to a uniform rate of corporate tax as opposed to the current incentives that are limited to income from Approved or Benefiting Enterprises during their benefits period. According to the 2011 Amendment, the uniform tax rate on such income, referred to as 'Preferred Income', would be 10% in areas in Israel that are designated as Development Zone A and 15% elsewhere in Israel during 2011-2012, 7% and 12.5%, respectively, in 2013-2014, and 6% and 12%, respectively, thereafter. Income derived by a Preferred Company from a 'Special Preferred Enterprise' (as defined in the Approved Enterprise) would enjoy further reduced tax rates for a period of ten years of 5% in Zone A and 8% elsewhere. As with dividends distributed from taxable income derived from an Approved Enterprise or Benefiting Enterprise during the applicable benefits period, dividends distributed from Preferred Income would be subject to a 15% tax (or lower, if so provided under an applicable tax treaty), which would generally be withheld by the distributing company. While the Company may incur additional tax liability in the event of distribution of dividends from tax exempt income generated from its Approved and Benefiting Enterprises, no additional tax liability will be incurred by the Company in the event of distribution of dividends from income taxed in accordance with the 2011 Amendment.

Under the transitional provisions of the 2011 Amendment, the Company and Bental elected to irrevocably implement the 2011 Amendment, commencing 2011 and thereafter, and be regarded as a "Preferred Enterprise" with respect to its existing Approved and Benefiting Enterprises while waiving benefits provided under the legislation prior to the 2011 Amendment.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## U.S. dollars in thousands

## NOTE 15 - TAXES ON INCOME (CONT)

Bental is located in area in Israel that is designated as Development Zone A and as such entitled to reduce tax rates of 10% during 2011-2012, 7% in 2013-2014, and 6% thereafter.

TAT is located in area in Israel that is designated as elsewhere and as such entitled to reduce tax rates of 15% during 2011-2012, 12.5% in 2013-2014, and 12.0% thereafter.

c. Reduction of Israeli corporate tax rate

The statutory rate of the Israeli corporate tax is as follows: 2012- 25%, 2011- 24% and 2010- 25%. In July 2009, the "Knesset" (Israeli Parliament) passed the Law for Economic Efficiency (Amended Legislation for Implementing the Economic Plan for 2009 and 2010), 2009, which prescribes, among others, an additional gradual reduction in the rates of the Israeli corporate tax and real capital gains tax starting 2011 to the following tax rates: 2012 - 23%, 2013 - 22%, 2014 - 21%, 2015 - 20%, 2016 and thereafter - 18%.

On December 6, 2011, the Knesset (Israel's Parliament) passed a law for changing the tax burden (Legislative Amendments), which cancels, among others, the gradual reduction in the corporate tax rates in Israel. In addition, the corporate tax in Israel was increased to 25% from the beginning of 2012. The effect of the abovementioned change on the financial statements is immaterial.

d. U.S. subsidiaries

U.S. subsidiaries are taxed based on federal and state tax laws. The effective tax rate for 2012, 2011, and 2010 was 38%.

e. Tax assessments

TAT's income tax assessments are considered final through 2007. TAT's and TAT Industries' tax years 2008 through 2011 are under an assessment process by the Israeli Tax authorities. Final tax assessments have not been received yet.

Bental income tax assessments are considered final through 2008.

Limco-piedmont income tax assessments are considered final through 2007.

TAT-GAL which was incorporated in 2008 has not received final tax assessment yet.

The Company and TAT Industries file a consolidated tax report for the Israeli tax authorities. Accordingly, each one the companies are entitled to use its tax losses (resulted from the first year of consolidated tax report) against taxable income of the other company and subject to certain limitations.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 15 - TAXES ON INCOME (CONT)

## f. Income tax reconciliation:

A reconciliation of the theoretical tax expense assuming all income is taxed at the statutory rate to taxes on income (tax benefit) as reported in the statements of income:

	Year ended December 31,		
	2012	2011	2010
Income (loss) before taxes on income (tax benefit) as reported in the statements of income	\$ 4,070	\$ (1,730)	\$ (6,906)
Statutory tax rate in Israel	25%	24%	25%
Theoretical taxes on income (tax benefit)	\$ 1,018	\$ (415)	\$ (1,726)
Increase (decrease) in taxes on income resulting from:			
Tax adjustment for foreign subsidiaries subject to a different tax rate	434	(86)	(1,118)
Reduced tax rate on income derived from "Preferred Enterprises" plans	(114)	177	-
Exempt income	(4)	(10)	-
Permanent differences	387	(36)	-
Valuation allowance	499	-	-
Deferred taxes on impairment of share in affiliated company	-	-	(1,332)
Tax in respect of prior years	(83)	(80)	(50)
Non-deductible expenses	(51)	134	73
Taxes on income (tax benefit) as reported in the statements of income (loss)	\$ 2,086	\$ (316)	\$ (4,153)

## g. Income (loss) before taxes on income (tax benefit) is comprised as follows:

	Year ended December 31,		
	2012	2011	2010
Domestic (Israel)	\$ 837	\$ 964	\$ 2,766
Foreign (United States)	3,233	(2,694)	(9,672)
	\$ 4,070	\$ (1,730)	\$ (6,906)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 15 - TAXES ON INCOME (CONT)

h. Taxes on income (tax benefit) included in the statements of income:

	Year ended December 31,		
	2012	2011	2010
Current:			
Domestic (Israel)	\$ 282	\$ 371	\$ 570
Foreign (United States)	287	213	(611)
	569	584	(41)
Deferred:			
Domestic (Israel)	119	218	46
Foreign (United States)	1,481	(1,038)	(4,108)
	1,600	(820)	(4,062)
Previous years:			
Domestic (Israel)	(45)	(126)	(50)
Foreign (United States)	(38)	46	-
	(83)	(80)	(50)
	<u>\$ 2,086</u>	<u>\$ (316)</u>	<u>\$ (4,153)</u>

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 15 - TAXES ON INCOME (CONT)

## i. Deferred income taxes:

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of TAT's deferred tax liabilities and assets are as follows:

	December 31,	
	2012	2011
Deferred tax assets (liabilities):		
Allowance for doubtful accounts	\$ 133	\$ 73
Unrealized gains	131	138
Provisions for employee benefits	270	227
Inventory	1,171	1,939
Other temporary differences	417	187
Deferred tax assets - short-term- other accounts receivables	<u>\$ 2,122</u>	<u>\$ 2,564</u>
Goodwill and intangible assets	\$ 884	\$ 1,273
Property, plant and equipment	707	762
Provisions for employee benefits and other temporary differences	64	70
Tax credits carryforward	274	106
Capital and state tax losses carryforward	1,823	184
Net operating losses carryforward	606	1,458
Deferred tax assets, before valuation allowance – Long-term	4,358	3,853
Valuation allowance	(1,823)	(184)
Deferred tax assets, net – Long-term	<u>\$ 2,535</u>	<u>\$ 3,669</u>
Other temporary differences Deferred tax Liabilities – Short-term- other accounts payable	<u>\$ (126)</u>	<u>\$ (179)</u>
Property, plant and equipment and intangible assets	(1,457)	(1,388)
Other	(33)	(25)
Deferred tax Liabilities - Long-term	<u>\$ (1,490)</u>	<u>\$ (1,413)</u>

As of December 31, 2012, TAT did not provide a valuation allowance in respect of deferred tax assets, since management currently believes that it is more likely than not that the deferred tax asset will be realized in the future. For capital losses and certain state tax losses, incurred by the U.S. subsidiaries, the Company provides valuation allowance as it cannot predict its future realization.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 15 - TAXES ON INCOME (CONT)

The following table summarizes the changes in the valuation allowance for deferred tax assets:

Balance, January 1, 2010	\$ -
Addition charged to expenses	200
Balance, December 31, 2010	200
Deductions	(16)
Balance, December 31, 2011	184
Addition charged to expenses	1,639
Balance, December 31, 2012	<u>\$ 1,823</u>

TAT does not intend to distribute earnings of a foreign subsidiary aggregating up to approximately \$12,000 (tax earnings and profits) as of December 31, 2012, and accordingly, no deferred tax liability has been established relative to these earnings. If such profits and earnings are distributed by cash dividend, it would be taxed at tax rate applicable to such distribution (25%) and an income tax liability of up to approximately \$3,000 would be incurred as of December 31, 2012.

TAT does not intend to distribute tax-exempt earnings deriving from Approved Enterprise aggregating approximately \$9,000 as of December 31, 2012, and accordingly, no deferred tax liability has been established related to these earnings. See also Note 15(b). If such tax-exempt income is distributed by cash dividend (including a liquidation dividend), it would be taxed at the reduced corporate tax rate applicable to such profits (25%) and an income tax liability of up to approximately \$2,250 would be incurred as of December 31, 2012.

- j. A reconciliation of the beginning and ending amount of unrecognized provision is as follows:

	Amount
Balance at January 1, 2010	\$ -
Additions for tax positions of prior years	84
Balance at December 31, 2010	84
Exchange rate differences	2
Balance at December 31, 2011	86
Exchange rate differences	(2)
Balance at December 31, 2012	<u>\$ 84</u>

Unrecognized tax benefits, mainly of a long-term nature, at December 31, 2012, 2011 and 2010 amounted to \$(1), \$2 and \$84, respectively. All of the above amounts of unrecognized tax benefits would affect the effective tax rate if recognized. The Group does not expect unrecognized tax benefits to change significantly over the next 12 months.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 16 - SEGMENT INFORMATION

## a. Segment Activities Disclosure:

TAT operates under four segments: (i) Original Equipment Manufacturing or “OEM” of Heat Management Solutions (ii) Heat Transfer Services and Products (iii) Maintenance, Repair and Overhaul or “MRO” services for Aviation Components and (iv) OEM of Electric Motion Systems.

- OEM of Heat Management Solutions primarily includes the design, development, manufacture and sale of (i) a broad range of heat transfer components (such as heat exchangers, pre-coolers and oil/fuel hydraulic coolers) used in mechanical and electronic systems on-board commercial, military and business aircraft; (ii) environmental control and cooling systems on board aircraft and for ground applications; and (iii) a variety of other electronic and mechanical aircraft accessories and systems such as pumps, valves, power systems and turbines.
- Heat Transfer Services and Products primarily includes the maintenance, repair and overhaul of heat transfer equipment and in a lesser extent, the manufacturing of certain heat transfer products. TAT's Limco subsidiary operates an FAA certified repair station, which provides heat transfer MRO services and products for airlines, air cargo carriers, maintenance service centers and the military.
- MRO services for Aviation Components primarily includes the maintenance, repair and overhaul of APUs, landing gear and other aircraft components. TAT's Piedmont subsidiary operates an FAA certified repair station, which provides aircraft component MRO services for airlines, air cargo carriers, maintenance service centers and the military.
- OEM of Electric Motion Systems primarily includes the design, development, manufacture and sale of a broad range of electrical motor applications for airborne and ground systems.

The Group's chief operating decision-maker (CEO of the Company) evaluates performance, makes operating decisions and allocates resources based on financial data consistent with the presentation in the accompanying financial statements.

TAT evaluates segment performance based on revenue and operating income. The operating income reported in TAT's segments excludes other unallocated amounts. Although such amounts are excluded from the business segment results, they are included in reported consolidated earnings.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 16 - SEGMENT INFORMATION (CONT)

## b. Segments statement operations disclosure:

The following financial information is the information that management uses for analyzing the segment results. The figures are presented in consolidated method as presented to management.

The following financial information is a summary of the operating income of each operational segment:

Year ended December 31, 2012							
	OEM of Heat Management Solutions	OEM - Electric Motion Systems	Heat Transfer Services and Products	MRO services for Aviation Components	Amounts not allocated to segments	Elimination from inter companies sale	Consolidated
Revenues							
Sale of products and services	\$ 27,944	\$ 10,007	\$ 27,529	\$ 22,442	\$ -	\$ -	\$ 87,922
Intersegment revenues	3,088	-	180	-	-	(3,268)	-
Total revenues	31,032	10,007	27,709	22,442	-	(3,268)	87,922
Cost of revenues	23,105	8,043	19,671	19,044	-	(3,281)	66,582
Gross profit	7,927	1,964	8,038	3,398	-	13	21,340
Research and development expenses	581	157	414	-	-	-	1,152
Selling and marketing expenses	1,476	527	1,049	374	-	-	3,426
General and administrative expenses	3,530	1,377	3,270	3,310	-	-	11,487
Impairment of goodwill	-	1,015	-	-	-	-	1,015
Other expense (income)	(13)	22	-	-	-	-	9
Operating income (loss)	2,353	(1,134)	3,305	(286)	-	13	4,251
Financial expense, net	-	-	-	-	(181)	-	(181)
Income before taxes on income							\$ 4,070

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 16 - SEGMENT INFORMATION (CONT)

## b. Segments statement operations disclosure (cont)

	Year ended December 31, 2011						
	OEM of Heat Management Solutions	OEM - Electric Motion Systems	Heat Transfer Services and Products	MRO services for Aviation Components	Amounts not allocated to segments	Elimination from inter companies sale	Consolidated
Revenues							
Sale of products and services	\$ 25,993	\$ 11,658	\$ 27,600	\$ 20,146	\$ -	\$ -	\$ 85,397
Intersegment revenues	4,027	-	3	-	-	(4,030)	-
Total revenues	30,020	11,658	27,603	20,146	-	(4,030)	85,397
Cost of revenues	22,660	9,388	20,173	17,882	-	(3,884)	66,219
Write down of inventory and impairment charges of long lived assets	-	298	-	5,465	-	-	5,763
Gross profit	7,360	1,972	7,430	(3,201)	-	(146)	13,415
Research and development expenses	455	331	-	-	-	-	786
Selling and marketing expenses	1,203	619	1,026	591	-	-	3,439
General and administrative expenses	3,787	1,501	3,035	2,626	-	-	10,949
Other expense (income)	(190)	21	-	-	-	-	(169)
Operating income (loss)	2,105	(500)	3,369	(6,418)	-	(146)	(1,590)
Financial expense, net	-	-	-	-	(380)	-	(380)
Loss before tax benefit							\$ (1,970)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 16 - SEGMENT INFORMATION (CONT)

## b. Segments statement operations disclosure (cont)

	Year ended December 31, 2010						Consolidated
	OEM of Heat Management Solutions	OEM - Electric Motion Systems	Heat Transfer Services and Products	MRO services for Aviation Components	Amounts not allocated to segments	Elimination from inter companies sale	
Revenues							
Sale of products and services	\$ 26,012	\$ 13,046	\$ 24,365	\$ 16,332	\$ -	\$ -	\$ 79,755
Intersegment revenues	3,639	-	104	-	-	(3,743)	-
Total revenues	29,651	13,046	24,469	16,332	-	(3,743)	79,755
Cost of revenues	22,425	10,092	18,005	14,631	-	(3,965)	61,188
Write down of inventory	-	-	-	3,500	-	-	3,500
Gross profit	7,226	2,954	6,464	(1,799)	-	222	15,067
Research and development expenses	274	377	-	-	-	-	651
Selling and marketing expenses	1,186	526	1,014	749	-	-	3,475
General and administrative expenses	3,598	1,572	2,649	5,013	-	-	12,832
Impairment of goodwill and intangible assets	-	-	456	4,248	-	-	4,704
Operating income (loss)	2,168	479	2,345	(11,809)	-	222	(6,595)
Financial expense, net	-	-	-	-	(111)	-	(111)
Other expenses	-	-	-	-	(200)	-	(200)
Loss before tax benefit							\$ (6,906)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 16 - SEGMENT INFORMATION (CONT)

c. The following financial information identifies the assets to segment:

	As of December 31, 2012					
	OEM of Heat Management Solutions	OEM - Electric Motion Systems	Heat Transfer Services and Products	MRO services for Aviation Components	Amounts not allocated to segments	Consolidated
Assets	\$ 34,162	\$ 12,707	\$ 26,469	\$ 17,819	\$ 16,354	\$ 107,511
Depreciation and amortization	973	498	735	197	-	2,403
Expenditure for segment assets	1,047	247	756	344	-	2,394

	As of December 31, 2011					
	OEM of Heat Management Solutions	OEM - Electric Motion Systems	Heat Transfer Services and Products	MRO services for Aviation Components	Amounts not allocated to segments	Consolidated
Assets	\$ 33,972	\$ 13,941	\$ 27,242	\$ 20,380	\$ 19,783	\$ 115,318
Depreciation and amortization	1,137	655	758	721	-	3,271
Expenditure for segment assets	924	352	638	1,391	-	3,305
Goodwill	-	1,042	-	-	-	1,042

	As of December 31, 2010					
	OEM of Heat Management Solutions	OEM - Electric Motion Systems	Heat Transfer Services and Products	MRO services for Aviation Components	Amounts not allocated to segments	Consolidated
Assets	\$ 36,949	\$ 17,501	\$ 21,559	\$ 23,588	\$ 21,830	\$ 121,427
Depreciation and amortization	1,220	671	704	787	-	3,382
Expenditure for segment assets	739	826	625	896	-	3,086
Goodwill	-	1,156	-	-	-	1,156

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 17 - ENTITY-WIDE DISCLOSURE

- a. Total revenues and long-lived assests - by geographical location were as follows:

	Year ended December 31,					
	2012		2011		2010	
	Total revenues	Long-lived assets	Total revenues	Long-lived assets	Total revenues	Long-lived assets
Sale of products						
Israel	\$ 18,043	\$ 8,417	\$ 18,945	\$ 8,528	\$ 23,223	\$ 9,103
United states	17,023	-	20,975	-	7,193	-
France	4,604	-	3,264	-	2,971	-
Rest of Europe	2,402	-	2,784	-	2,596	-
Other	4,198	-	1,540	-	2,971	-
	<u>\$ 46,270</u>	<u>\$ 8,417</u>	<u>\$ 47,508</u>	<u>\$ 8,528</u>	<u>\$ 38,954</u>	<u>\$ 9,103</u>

	Year ended December 31,					
	2012		2011		2010	
	Total revenues	Long-lived assets	Total revenues	Long-lived assets	Total revenues	Long-lived assets
Services						
Israel	\$ 468	\$ -	\$ 384	\$ -	\$ 410	\$ -
United states	25,648	4,493	24,029	4,325	25,582	5,340
Netherland	3,303	-	4,378	-	3,750	-
Rest of Europe	4,624	-	3,875	-	4,823	-
Other	7,609	-	5,223	-	6,236	-
	<u>\$ 41,652</u>	<u>\$ 4,493</u>	<u>\$ 37,889</u>	<u>\$ 4,325</u>	<u>\$ 40,801</u>	<u>\$ 5,340</u>

- b. Major Customers

No single customer accounted for 10% or more of Group's total net revenue in any year presented.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

U.S. dollars in thousands

## NOTE 18 - SELECTED STATEMENTS OF INCOME DATA

	Year ended December 31,		
	2012	2011	2010
Financial income (expenses), net:			
Financial income:			
Foreign currency gains	\$ 1,301	\$ 1,168	\$ 1,102
Derivatives	399	352	149
Interest on cash equivalents, short-term bank deposits and others	348	308	319
	<u>2,048</u>	<u>1,828</u>	<u>1,570</u>
Financial expenses:			
Bank charges	(84)	(84)	(177)
Interest on short-term loans	(98)	(98)	(78)
Interest on long-term loans	(185)	(210)	(211)
Foreign currency losses	(1,433)	(1,159)	(1,215)
Derivatives	(321)	(642)	-
Others	(108)	(15)	-
	<u>(2,229)</u>	<u>(2,208)</u>	<u>(1,681)</u>
	<u>\$ (181)</u>	<u>\$ (380)</u>	<u>\$ (111)</u>

## NOTE 19 - SUPPLEMENTAL CONSOLIDATED BALANCE SHEETS INFORMATION

	Warranty provision	Inventory Reserve	Allowance for Doubtful Accounts
Balance, as of January 1, 2010	\$ 401	\$ 2,309	\$ 2,360
Additions	112	3,997	259
Write-offs, net of recoveries	(172)	(1,590)	(200)
Balance, as of December 31, 2010	341	4,716	2,419
Additions	169	2,717	31
Write-offs, net of recoveries	(222)	(844)	(2,260)
Balance, as of December 31, 2011	288	6,589	190
Additions	196	649	258
Write-offs, net of recoveries	(208)	(669)	(72)
Balance, as of December 31, 2012	<u>\$ 276</u>	<u>\$ 6,569</u>	<u>\$ 376</u>

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TAT TECHNOLOGIES LTD.

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2012 STOCK OPTION PLAN

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ARTICLE I

PURPOSE; TYPES OF AWARDS; CONSTRUCTION

**1.1 Purpose.** The purpose of this Plan is to enhance the profitability and value of the Company for the benefit of its stockholders by enabling the Company to offer Eligible Employees, Consultants and Non-Employee Directors incentive awards to attract, retain and reward such individuals and strengthen the mutuality of interests between such individuals and the Company's stockholders.

**1.2 Types of Awards.** This Plan is intended to enable the Company to issue Awards under varying tax regimes, including, without limitation:

(a) Awards to be granted to Participants who are deemed to be residents of the State of Israel for purposes of taxation, pursuant and subject to the provisions of Section 102 of the Ordinance, including without limitation the Israeli Income Tax Rules (Tax Benefits in Stock Issuance to Employees) 5763-2003 (the "**Rules**") or such other rules published by the Israeli Income Tax Authorities (the "**ITA**") (such Awards, "**102 Stock Options**"). 102 Stock Options may either be granted to a Trustee of without a trustee;

(b) Incentive Stock Options within the meaning of Section 422 of the Code, or the corresponding provision of any subsequently enacted United States federal tax statute, as amended from time to time, to be granted to Participants who are deemed to be residents of the U.S. for purposes of taxation;

**1.3 Construction.** To the extent any provision herein conflicts with the conditions of any relevant tax law or regulation which are relied upon for tax relief in respect of a particular Award to a Participant, the provisions of such law or regulation shall prevail over those of the Plan and the Committee is empowered hereunder to interpret and enforce the said prevailing provisions.

ARTICLE II

DEFINITIONS

For purposes of this Plan, the following terms shall have the following meanings:

**2.1 "Acquisition Event"** means a merger or consolidation in which the Company is not the surviving entity, any transaction that results in the acquisition of substantially all of the Company's outstanding Ordinary Shares by a single person or entity or by a group of persons and/or entities acting in concert, or the sale or transfer of all or substantially all of the Company's assets.

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2.2 “**Affiliate**” means each of the following: (a) any Subsidiary; (b) any Parent; (c) any corporation, trade or business (including, without limitation, a partnership or limited liability company) which is directly or indirectly controlled 50% or more (whether by ownership of stock, assets or an equivalent ownership interest or voting interest) by the Company or one of its Affiliates; (d) any corporation, trade or business (including, without limitation, a partnership or limited liability company) which directly or indirectly controls 50% or more (whether by ownership of stock, assets or an equivalent ownership interest or voting interest) of the Company; (e) any other entity in which the Company or any of its Affiliates has a material equity interest and which is designated as an “Affiliate” by resolution of the Committee; and (f) for the purpose of 102 Stock Options, also an “Employing Company” within the meaning of section 102(a) of the Ordinance.

2.3 “**Award**” means any award under this Plan of any Stock Option. All Awards shall be granted by, confirmed by, and subject to the terms of, a written agreement executed by the Company and the Participant.

2.4 “**Board**” means the Board of Directors of the Company.

2.5 “**Cause**” means with respect to a Participant’s Termination of Employment or Termination of Consultancy, the following: (a) in the case where there is no employment agreement, consulting agreement, change in control agreement or similar agreement in effect between the Company or an Affiliate and the Participant at the time of the grant of the Award (or where there is such an agreement but it does not define “cause” (or words of like import)), termination due to: (i) a Participant’s conviction of, or plea of guilty or nolo contendere to, a felony; (ii) perpetration by a Participant of an illegal act, dishonesty, or fraud which could cause significant economic injury to the Company; (iii) a Participant’s insubordination, refusal to perform his or her duties or responsibilities for any reason other than illness or incapacity or materially unsatisfactory performance of his or her duties for the Company; (iv) continuing willful and deliberate failure by the Participant to perform the Participant’s duties in any material respect, provided that the Participant is given notice and an opportunity to effectuate a cure as determined by the Committee; or (v) a Participant’s willful misconduct with regard to the Company that could have a material adverse effect on the Company; or (b) in the case where there is an employment agreement, consulting agreement, change in control agreement or similar agreement in effect between the Company or an Affiliate and the Participant at the time of the grant of the Award that defines “cause” (or words of like import), “cause” as defined under such agreement; provided, however, that with regard to any agreement under which the definition of “cause” only applies on occurrence of a change in control, such definition of “cause” shall not apply until a change in control actually takes place and then only with regard to a termination thereafter. With respect to a Participant’s Termination of Directorship, “cause” means an act or failure to act that constitutes cause for removal of a director under applicable Israeli law.

2.6 “**Change in Control**” has the meaning set forth in Section 7.2.

2.7 “**Change in Control Price**” has the meaning set forth in Section 7.1.

2.8 “**Code**” means the Internal Revenue Code of 1986, as amended. Any reference to any section of the Code shall also be a reference to any successor provision and any Treasury Regulation promulgated thereunder.

**2.9** **“Committee”** means a committee or subcommittee of the Board appointed from time to time by the Board, provided that the composition of the Committee shall at all times be in compliance with any mandatory requirements of the applicable law. Subject to the aforesaid, such committee or subcommittee shall consist of two or more non-employee directors, each of whom is intended to be, (i) to the extent required by Rule 16b-3 promulgated under Section 16(b) of the Exchange Act, a “non-employee director” as defined in Rule 16b-3; (ii) to the extent required Section 162(m) of the Code, an “outside director” as defined in Section 162(m) of the Code; and (iii) an “independent director” as defined under applicable stock exchange rules. To the extent that no Committee exists that has the authority to administer this Plan, the functions of the Committee shall be exercised by the Board. If for any reason the appointed Committee does not meet the requirements of Rule 16b-3 or Section 162(m) of the Code or any other regulation set by the applicable law, such noncompliance shall not affect the validity of Awards, grants, interpretations or other actions of the Committee.

**2.10** **“Company”** means TAT Technologies Ltd., an Israeli corporation, and its successors by operation of law.

**2.11** **“Companies Law”** shall mean the Israel Companies Law-1999 and the regulations promulgated thereunder, all as amended from time to time.

**2.12** **“Consultant”** means any natural person who provides bona fide consulting or advisory services to the Company or its Affiliates pursuant to a written agreement, which are not in connection with the offer and sale of securities in a capital-raising transaction, and do not, directly or indirectly, promote or maintain a market for the Company’s or its Affiliates’ securities.

**2.13** **“Detrimental Activity”** means: (a) the disclosure to anyone outside the Company or its Affiliates, or the use in any manner other than in the furtherance of the Company’s or its Affiliate’s business, without written authorization from the Chief Executive Officer of the Company, of any confidential information or proprietary information, relating to the business of the Company or its Affiliates that is acquired by a Participant prior to the Participant’s Termination; (b) any activity while employed or performing services that results, or if known could result, in the Participant’s Termination that is classified by the Company as a termination for Cause; (c) the Participant’s Disparagement, or inducement of others to do so, of the Company or its Affiliates or their past and present officers, directors, employees or products; or (d) breach of any agreement between the Participant and the Company or an Affiliate (including, without limitation, any employment agreement or noncompetition or nonsolicitation agreement). If it is determined by a court of competent jurisdiction that any provision in this Plan in respect of Detrimental Activities is excessive in duration or scope or otherwise is unenforceable, then such provision may be modified or supplemented by the court to render it enforceable to the maximum extent permitted by law.

**2.14** **“Disability”** means with respect to a Participant’s Termination: (i) the inability of a Grantee to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months, as determined by a medical doctor satisfactory to the Committee or, if applicable, (ii) a permanent and total disability as defined in Section 22(c)(3) of the Code. A Disability shall only be deemed to occur at the time of the determination by the Committee of the Disability. Notwithstanding the foregoing, for Awards that are subject to Section 409A of the Code, Disability shall mean that a Participant is disabled under Section 409A(a)(2)(C)(i) of the Code.

**2.15** **“Disparagement”** means making comments or statements to the press, the Company’s or its Affiliates’ employees, consultants or any individual or entity with whom the Company or its Affiliates has a business relationship which could reasonably be expected to adversely affect in any manner: (a) the conduct of the business of the Company or its Affiliates (including, without limitation, any products or business plans or prospects); or (b) the business reputation of the Company or its Affiliates, or any of their products, or their past or present officers, directors or employees.

**2.16** "Employee" - means any person, including an Officer or Director, who is in the employ of the Company or any Related Entity, subject to the control and direction of the Company or any Related Entity as to both the work to be performed and the manner and method of performance. The payment of a director's fee by the Company or a Related Entity shall not be sufficient to constitute "employment" by the Company. In addition, the term "Employee" includes those persons who are included in the term "employee" under rule 701 of the Securities Act of 1933.

For the absence of doubt, the term "Employee" when related to the Award of 102 Stock Options shall mean any employee as such term is defined in Section 102 of the Ordinance. Without derogating from the foregoing Employee shall include any employee or Office Holder (as such term is defined in the Israeli Companies Law, 5759 - 1999) of the Company or any Subsidiary except for such persons that are deemed to be "Controlling Shareholder" under Section 32(9) to the Ordinance.

**2.17** "Eligible Employees" means each employee of the Company or an Affiliate, including, for the purpose of Section 102, an individual who is serving as an "office holder" as defined under the Companies Law, but excluding any "Controlling Shareholder" as defined under Section 32(9) of the Ordinance.

**2.18** "Exchange Act" means the Securities Exchange Act of 1934, as amended. Any references to any section of the Exchange Act shall also be a reference to any successor provision.

**2.19** "Exercise Period" shall mean the period, commencing on the date of grant of an Option, during which an Option shall be exercisable, subject to any vesting provisions thereof and the termination provisions hereof.

**2.20** "Exercise Price" shall mean the exercise price for each Share covered by an Option.

**2.21** "Fair Market Value" means, unless otherwise required by any applicable provision of the Code (or any regulations issued thereunder) or the Ordinance, as may be applicable, as of any date and except as provided below, the closing price reported for the Ordinary Shares on the applicable date: (a) as reported on the principal national securities exchange in the United States on which it is then traded; or (b) if not traded on any such national securities exchange, as quoted on an automated quotation system sponsored by the Financial Industry Regulatory Authority or if the Ordinary Shares shall not have been reported or quoted on such date, on the first day prior thereto on which the Ordinary Shares were reported or quoted. If the Ordinary Shares are not traded, listed or otherwise reported or quoted, then Fair Market Value means the fair market value of the Ordinary Shares as determined by the Committee in good faith in whatever manner it considers appropriate taking into account the requirements of Section 422 of the Code or Section 409A of the Code, as applicable. For purposes of the grant of any Award, the applicable date shall be the trading day immediately prior to the date on which the Award is granted. For purposes of the exercise of any Award, the applicable date shall be the date a notice of exercise is received by the Committee or, if not a day on which the applicable market is open, the next day that it is open.

**2.22** "Family Member" means "family member" as defined in Section A.1.(5) of the general instructions of Form S-8, as may be amended from time to time, or by the Ordinance and/or the Companies Law, all as may be applicable.

**2.23** **"Incentive Stock Option"** means any Stock Option awarded to an Eligible Employee of the Company, its Subsidiaries and its Parent (if any) under this Plan intended to be and designated as an "Incentive Stock Option" within the meaning of Section 422 of the Code.

**2.24** **"KMN Person"** means (i) KMN Holdings Ltd, an Israeli corporation; (ii) any Affiliate of KMN Holdings Ltd.; or (iii) any officer, director or employee of any Person specified in clause (i)-(ii) above.

**2.25** **"Non-Employee Director"** means a director of the Company who is not an active employee of the Company or an Affiliate.

**2.26** **"Non-Qualified Stock Option"** means any Stock Option awarded under this Plan that is not an Incentive Stock Option.

**2.27** **"Ordinance"** means the Israeli Income Tax Ordinance (New Version) 1961, and the regulations promulgated thereunder, all as amended from time to time.

**2.28** **"Ordinary Shares" or "Shares"** means the Ordinary Shares, par value NIS 0.90 per share, of the Company.

**2.29** **"Parent"** means any parent corporation of the Company within the meaning of Section 424(e) of the Code, or by the Ordinance and/or the Companies Law, all as may be applicable.

**2.30** **"Participant"** means an Eligible Employee, Non-Employee Director or Consultant to whom an Award has been granted pursuant to this Plan.

**2.31** **"Person"** means any individual, corporation, partnership, limited liability company, firm, joint venture, association, joint-stock company, trust, incorporated organization, governmental or regulatory or other entity.

**2.32** **"Plan"** means this TAT Technologies Ltd 2012 Stock Option Plan, as amended from time to time.

**2.33** **"Retirement"** means a voluntary Termination of Employment or Termination of Consultancy at or after age 65 or such earlier date after age 50 as may be approved by the Committee, in its sole discretion, with respect to such Participant at the time of grant, or thereafter provided that the exercise of such discretion does not make the applicable Award subject to Section 409A of the Code, except that Retirement shall not include any involuntary Termination of Employment or Termination of Consultancy by the Company or an Affiliate for any reason with or without Cause. With respect to a Participant's Termination of Directorship, Retirement means the failure to stand for reelection or the failure to be reelected on or after a Participant has attained age 65 or, with the consent of the Board, provided that the exercise of such discretion does not make the applicable Award subject to Section 409A of the Code, before age 65 but after age 50.

**2.34** **"Rule 16b-3"** means Rule 16b-3 under Section 16(b) of the Exchange Act as then in effect or any successor provision.

**2.35** **"Securities Act"** means the Securities Act of 1933, as amended and all rules and regulations promulgated thereunder. Any reference to any section of the Securities Act shall also be a reference to any successor provision.

- 2.36 **"Section 102"** means section 102 of the Ordinance.
- 2.37 **"Section 162(m) of the Code"** means the exception for performance-based compensation under Section 162(m) of the Code and any applicable Treasury regulations thereunder.
- 2.38 **"Section 409A of the Code"** means the nonqualified deferred compensation rules under Section 409A of the Code and any applicable Treasury regulations thereunder.
- 2.39 **"Stock Option"** or **"Option"** means any option to purchase Ordinary Shares granted to Eligible Employees, Non-Employee Directors or Consultants granted pursuant to Article VI.
- 2.40 **"Subsidiary"** means any subsidiary corporation of the Company within the meaning of Section 424(f) of the Code, or by the Ordinance and/or the Companies Law, all as may be applicable.
- 2.41 **"Ten Percent Stockholder"** means a person owning stock possessing more than 10% of the total combined voting power of all classes of stock of the Company, its Subsidiaries or its Parent.
- 2.42 **"Termination"** means a Termination of Consultancy, Termination of Directorship or Termination of Employment, as applicable.
- 2.43 **"Termination of Consultancy"** means: (a) that the Consultant is no longer acting as a consultant to the Company or an Affiliate; or (b) when an entity which is retaining a Participant as a Consultant ceases to be an Affiliate unless the Participant otherwise is, or thereupon becomes, a Consultant to the Company or another Affiliate at the time the entity ceases to be an Affiliate. In the event that a Consultant becomes an Eligible Employee or a Non-Employee Director upon the termination of his or her consultancy, unless otherwise determined by the Committee, in its sole discretion, no Termination of Consultancy shall be deemed to occur until such time as such Consultant is no longer a Consultant, an Eligible Employee or a Non-Employee Director. Notwithstanding the foregoing, the Committee may, in its sole discretion, otherwise define Termination of Consultancy in the Award agreement or, if no rights of a Participant are reduced, may otherwise define Termination of Consultancy thereafter.
- 2.44 **"Termination of Directorship"** means that the Non-Employee Director has ceased to be a director of the Company; except that if a Non-Employee Director becomes an Eligible Employee or a Consultant upon the termination of his or her directorship, his or her ceasing to be a director of the Company shall not be treated as a Termination of Directorship unless and until the Participant has a Termination of Employment or Termination of Consultancy, as the case may be.
- 2.45 **"Termination of Employment"** means: (a) a termination of employment (for reasons other than a military or personal leave of absence granted by the Company) of a Participant from the Company and its Affiliates; or (b) when an entity which is employing a Participant ceases to be an Affiliate, unless the Participant otherwise is, or thereupon becomes, employed by the Company or another Affiliate at the time the entity ceases to be an Affiliate. In the event that an Eligible Employee becomes a Consultant or a Non-Employee Director upon the termination of his or her employment, unless otherwise determined by the Committee, in its sole discretion, no Termination of Employment shall be deemed to occur until such time as such Eligible Employee is no longer an Eligible Employee, a Consultant or a Non-Employee Director. Notwithstanding the foregoing, the Committee may, in its sole discretion, otherwise define Termination of Employment in the Award agreement or, if no rights of a Participant are reduced, may otherwise define Termination of Employment thereafter.

**2.46** **“Transfer”** means: (a) when used as a noun, any direct or indirect transfer, sale, assignment, pledge, hypothecation, encumbrance or other disposition (including the issuance of equity in a Person), whether for value or no value and whether voluntary or involuntary (including by operation of law), and (b) when used as a verb, to directly or indirectly transfer, sell, assign, pledge, encumber, charge, hypothecate or otherwise dispose of (including the issuance of equity in a Person) whether for value or for no value and whether voluntarily or involuntarily (including by operation of law). “Transferred” and “Transferable” shall have a correlative meaning.

**2.47** **“Trustee”** shall mean the trustee appointed by the Committee or the Board, as the case may be, to hold the respective Options and/or Shares (and, in relation with 102 Stock Options, approved by the Israeli tax authorities), if so appointed.

### ARTICLE III

#### ADMINISTRATION

**3.1** **The Committee.** This Plan shall be administered and interpreted by the Committee. In the event that the Board does not create a committee to administer the Plan, the Plan shall be administered by the Board in its entirety. In the event that an action necessary for the administration of the Plan is required under law to be taken by the Board, then such action shall be so taken by the Board. In any such event, all references herein to the Committee shall be construed as references to the Board.

**3.2** **Grants of Awards.** The Committee shall have full authority to grant Stock Options, pursuant to the terms of this Plan, to Eligible Employees, Consultants and Non-Employee Directors. In particular, the Committee shall have the authority:

- (a) to select the Eligible Employees, Consultants and Non-Employee Directors to whom Awards may from time to time be granted hereunder;
- (b) to determine whether and to what extent Awards, or any combination thereof, are to be granted hereunder to one or more Eligible Employees, Consultants or Non-Employee Directors;
- (c) to determine the number of Ordinary Shares to be covered by each Award granted hereunder;
- (d) to determine the terms and conditions, not inconsistent with the terms of this Plan, of any Award granted hereunder (including, but not limited to, the exercise price, any restriction or limitation, any vesting schedule or acceleration thereof, or any forfeiture restrictions or waiver thereof, regarding any Award and the Ordinary Shares relating thereto, based on such factors, if any, as the Committee shall determine, in its sole discretion);
- (e) to determine whether and under what circumstances a Stock Option may be settled in cash, and/or Ordinary Shares under Section 6.4(d);
- (f) to determine whether a Stock Option is an Incentive Stock Option or Non-Qualified Stock Option;
- (g) to determine whether to require a Participant, as a condition of the granting of any Award, to not sell or otherwise dispose of shares acquired pursuant to the exercise of an Award for a period of time as determined by the Committee, in its sole discretion, following the date of the acquisition of such Award;

(h) to set the performance criteria with respect to any Award for which the grant, vesting or payment of such Award is conditioned upon the attainment of specified performance criteria and to certify the attainment of any such performance criteria; and

(i) generally, to exercise such powers and to perform such acts as the Committee deems necessary or expedient to promote the best interests of the Company that are not in conflict with the provisions of this Plan.

**3.3 Guidelines.** Subject to Article VIII hereof, the Committee shall, in its sole discretion, have the authority to adopt, alter and repeal such administrative rules, guidelines and practices governing this Plan and perform all acts, including the delegation of its responsibilities (to the extent permitted by applicable law and applicable stock exchange rules), as it shall, from time to time, deem advisable; to construe and interpret the terms and provisions of this Plan and any Award issued under this Plan (and any agreements relating thereto); and to otherwise supervise the administration of this Plan. The Committee may, in its sole discretion, correct any defect, supply any omission or reconcile any inconsistency in this Plan or in any agreement relating thereto in the manner and to the extent it shall deem necessary to effectuate the purpose and intent of this Plan; provided, that with regard to any provision of this Plan or any agreement relating thereto that is intended to comply with Section 162(m) of the Code or Section 102 of the Ordinance as may be applicable, any such action by the Committee shall be permitted only to the extent such action would be permitted under Section 162(m) of the Code or Section 102 of the Ordinance, as may be applicable. The Committee may, in its sole discretion, adopt special guidelines and provisions for persons who are residing in or employed in, or subject to, the taxes of, any domestic or foreign jurisdictions to comply with applicable tax and securities laws of such domestic or foreign jurisdictions. This Plan is intended to comply with the applicable requirements of Section 102 of the Ordinance and/or Rule 16b-3 and with respect to Awards intended to be "performance-based," the applicable provisions of Section 162(m) of the Code and this Plan shall be limited, construed and interpreted in a manner so as to comply therewith.

**3.4 Decisions Final.** Any decision, interpretation or other action made or taken in good faith by or at the direction of the Company, the Board or the Committee (or any of its members) arising out of or in connection with this Plan shall be within the absolute discretion of all and each of them, as the case may be, and shall be final, binding and conclusive on the Company and all employees and Participants and their respective heirs, executors, administrators, successors and assigns.

**3.5 Procedures.** If the Committee is appointed, the Board shall designate one of the members of the Committee as chairman and the Committee shall hold meetings at such times and places as it shall deem advisable, including, without limitation, by telephone conference or by written consent to the extent permitted by the Companies Law or any other applicable law. A majority of the Committee members shall constitute a quorum. All determinations of the Committee shall be made by a majority of its members. Any decision or determination reduced to writing and signed by all the Committee members, shall be fully effective as if it had been made by a vote at a meeting duly called and held. The Committee shall keep minutes of its meetings and shall make such rules and regulations for the conduct of its business as it shall deem advisable.

**3.6 Designation of Consultants/Liability.**

(a) The Committee may, in its sole discretion, designate employees of the Company and professional advisors to assist the Committee in the administration of this Plan.



(b) The Committee may, in its sole discretion, employ such legal counsel, consultants and agents as it may deem desirable for the administration of this Plan and may rely upon any opinion received from any such counsel or consultant and any computation received from any such consultant or agent. Expenses incurred by the Committee or the Board in the engagement of any such counsel, consultant or agent shall be paid by the Company. The Committee, its members and any person designated pursuant to subsection (a) above shall not be liable for any action or determination made in good faith with respect to this Plan. To the maximum extent permitted by applicable law, no officer of the Company or member or former member of the Committee or of the Board shall be liable for any action or determination made in good faith with respect to this Plan or any Award granted under it.

**3.7 Indemnification.** To the maximum extent permitted by applicable law and the Articles of Association of the Company and to the extent not covered by insurance directly insuring such person, each officer or employee of the Company or any Affiliate and member or former member of the Committee or the Board shall be indemnified and held harmless by the Company against any cost or expense (including reasonable fees of counsel reasonably acceptable to the Committee) or liability (including any sum paid in settlement of a claim with the approval of the Committee), and advanced amounts necessary to pay the foregoing at the earliest time and to the fullest extent permitted, arising out of any act or omission to act in connection with the administration of this Plan, except to the extent arising out of such officer's, employee's, member's or former member's fraud. Such indemnification shall be in addition to any rights of indemnification the officers, employees, directors or members or former officers, employees, directors or members may have under applicable law, under the Articles of Association of the Company or any Affiliate. Notwithstanding anything else herein, this indemnification will not apply to the actions or determinations made by an individual with regard to Awards granted to him or her under this Plan.

#### ARTICLE IV

#### SHARE LIMITATION

##### 4.1 Shares

(a) General Limitations. The initial aggregate number of Ordinary Shares with respect to which Awards may be granted under this Plan shall not exceed 380,000 shares (subject to any increase or decrease pursuant to Section 4.2), which may be either authorized and unissued Ordinary Shares or Ordinary Shares held in or acquired for the treasury of the Company or both. If any Stock Option, granted under this Plan expires, terminates or is canceled for any reason without having been exercised in full, the number of Ordinary Shares underlying any unexercised Award shall again be available for the purpose of Awards under this Plan. The number of Ordinary Shares available for the purpose of Awards under this Plan shall be reduced by (i) the total number of Stock Options exercised, regardless of whether any of the Ordinary Shares underlying such Awards are not actually issued to the Participant as the result of a net settlement, and (ii) any Ordinary Shares used to pay any exercise price or tax withholding obligation with respect to any Award. In addition, the Company may not use the cash proceeds it receives from Stock Option exercises to repurchase Ordinary Shares on the open market for reuse under this Plan.

(b) Individual Participation Limitations.

(i) The maximum number of Ordinary Shares subject to all Awards of Stock Options which may be granted under this Plan during any fiscal year of the Company to each Eligible Employee or Consultant shall be 100,000 shares (which shall be subject to any further increase or decrease pursuant to Section 4.2).

(ii) The maximum number of Ordinary Shares subject to all Awards of Stock Options which may be granted under this Plan during any fiscal year of the Company to each Non-Employee Director shall not exceed 50,000 (which shall be subject to any further increase or decrease pursuant to Section 4.2) with respect to any fiscal year of the Company.

(iii) The individual Participant limitations set forth in this Section 4.1(b) shall be cumulative; that is, to the extent that Ordinary Shares for which Awards are permitted to be granted to an Eligible Employee or Consultant during a fiscal year are not covered by an Award to such Eligible Employee or Consultant in a fiscal year, the number of Ordinary Shares available for Awards to such Eligible Employee or Consultant shall automatically increase in the subsequent fiscal years during the term of this Plan until used.

**4.2 Changes**

(a) The existence of this Plan and the Awards granted hereunder shall not affect in any way the right or power of the Board or the stockholders of the Company to make or authorize (i) any adjustment, recapitalization, reorganization or other change in the Company's capital structure or its business, (ii) any merger or consolidation of the Company or any Affiliate, (iii) any issuance of bonds, debentures, preferred or prior preference stock ahead of or affecting the Ordinary Shares, (iv) the dissolution or liquidation of the Company or any Affiliate, (v) any sale or transfer of all or part of the assets or business of the Company or any Affiliate or (vi) any other corporate act or proceeding.

(b) Subject to the provisions of Section 4.2(d), in the event of any such change in the capital structure or business of the Company by reason of any stock split, reverse stock split, stock dividend, combination or reclassification of shares, recapitalization, merger, consolidation, spin-off, reorganization, partial or complete liquidation, issuance of rights or warrants to purchase any Ordinary Shares or securities convertible into Ordinary Shares, any sale or transfer of all or part of the Company's assets or business, or any other corporate transaction or event having an effect similar to any of the foregoing and effected without receipt of consideration by the Company, then the Committee shall make such adjustments consistent with such change in such manner as the Committee deems equitable to prevent substantial dilution or enlargement of the rights granted to, or available for, Participants under this Plan, to the aggregate number and kind of shares that thereafter may be issued under this Plan, the number and kind of shares or other property (including cash) to be issued upon exercise of an outstanding Award and the purchase price thereof, and/or the individual Participant limits set forth in Section 4.1(b). Any such adjustment determined by the Committee shall be final, binding and conclusive on the Company and all Participants and employees and their respective heirs, executors, administrators, successors and assigns. Except as provided in this Section 4.2 or in the applicable Award agreement, a Participant shall have no rights by reason of any issuance by the Company of any class or securities convertible into stock of any class, any subdivision or consolidation of shares of stock of any class, the payment of any stock dividend, any other increase or decrease in the number of shares of stock of any class, any sale or transfer of all or part of the Company's assets or business or any other change affecting the Company's capital structure or business.

(c) Fractional Ordinary Shares resulting from any adjustment in Awards pursuant to Section 4.2(a) or (b) shall be aggregated until, and eliminated at, the time of exercise by rounding-down for fractions less than one-half and rounding-up for fractions equal to or greater than one-half. No cash settlements shall be made with respect to fractional shares eliminated by rounding. Notice of any adjustment shall be given by the Committee to each Participant whose Award has been adjusted and such adjustment (whether or not such notice is given) shall be effective and binding for all purposes of this Plan.

(d) In the event of an Acquisition Event, the Committee may, in its sole discretion, terminate all outstanding and unexercised Stock Options effective as of the date of the Acquisition Event, by delivering notice of termination to each Participant at least 20 days prior to the date of consummation of the Acquisition Event, in which case during the period from the date on which such notice of termination is delivered to the consummation of the Acquisition Event, each such Participant shall have the right to exercise in full all of his or her Stock Options that are then outstanding (subject to any limitations on exercisability otherwise contained in the Award agreements), but any such exercise shall be contingent on the occurrence of the Acquisition Event, and, provided that, if the Acquisition Event does not take place within a specified period after giving such notice for any reason whatsoever, the notice and exercise pursuant thereto shall be null and void.

If an Acquisition Event occurs but the Committee does not terminate the outstanding Awards pursuant to this Section 4.2(d), then the provisions of Section 4.2(b) and Article VII shall apply.

**4.3 Minimum Purchase Price.** Notwithstanding any provision of this Plan to the contrary, if authorized but previously unissued Ordinary Shares are issued under this Plan, such shares shall not be issued for a consideration that is less than as permitted under applicable law.

## ARTICLE V

### ELIGIBILITY

**5.1 General Eligibility.** All Eligible Employees, prospective employees and Consultants of the Company and its Affiliates, and Non-Employee Directors of the Company, are eligible to be granted Awards. Eligibility for the grant of Awards and actual participation in this Plan shall be determined by the Committee in its sole discretion. Notwithstanding anything herein to the contrary, no Award under which a Participant may receive Ordinary Shares may be granted under this Plan to an Eligible Employee, Consultant or Non-Employee Director of any Affiliate if such shares of Common Stock do not constitute "service recipient stock" for purposes of Section 409A of the Code, when applicable, with respect to such Eligible Employee, Consultant or Non-Employee Director.

**5.2 102 Stock Options.** Subject to Applicable Law, 102 Stock Options may not be granted to "controlling shareholders" as defined under the Ordinance and may only be granted to Employees, including officers and directors, of the Company or any Affiliate thereof, who are Israeli residents ("**Eligible 102 Participants**"). Awards to Eligible 102 Participants in Israel shall be 102 Stock Options. Eligible 102 Participants may receive only 102 Stock Options, which may either be grants to a Trustee or grants under Section 102 without a trustee. Unless otherwise permitted by the Ordinance and the Rules, no 102 Stock Options to a Trustee may be granted until the expiration of thirty (30) days after the requisite filings under the Ordinance and the Rules have been appropriately made with the ITA.

**5.3 Incentive Stock Options.** Notwithstanding anything herein to the contrary, and subject to the provisions of Section 5.1(b) above, only Eligible Employees of the Company, its Subsidiaries and its Parent (if any) are eligible to be granted Incentive Stock Options under this Plan. Eligibility for the grant of an Incentive Stock Option and actual participation in this Plan shall be determined by the Committee in its sole discretion.

**5.4 General Requirement.** The vesting and exercise of Awards granted to a prospective employee or consultant are conditioned upon such individual actually becoming an Eligible Employee or Consultant.

## ARTICLE VI

### STOCK OPTIONS

**6.1 Options.** Each Stock Option granted under this Plan shall be of one of three types: (a) an Incentive Stock Option (b) a 102 Stock Option or (b) a Non-Qualified Stock Option.

**6.2 Grants.** The Committee shall, in its sole discretion, have the authority to grant to any Eligible Employee (subject to Sections 5.2, 5.3 above and Section 6.3 below) Incentive Stock Options, 102 Stock Options and/or Non-Qualified Stock Options, according to the applying tax regime and the provisions of this Plan. The Committee shall, in its sole discretion, have the authority to grant Non-Qualified Stock Options to any Consultant or Non-Employee Director. To the extent that any Stock Option does not qualify as an Incentive Stock Option (whether because of its provisions or the time or manner of its exercise or otherwise), such Stock Option or the portion thereof which does not qualify shall constitute a separate Non-Qualified Stock Option.

**6.3 Terms of Options.** Options granted under this Plan shall be evidenced by a written agreement between the Company and the Participant or a written notice delivered by the Company and accepted by the Participant (the “**Option Agreement**”), subject to the following terms and conditions and which Option Agreement shall be in such form and contain such additional terms and conditions, not inconsistent with the terms of this Plan, as the Committee, in its sole discretion, shall deem desirable from time to time, unless otherwise specifically provided in such Option Agreement or the terms referred to in Sections 6.3 (a) through (o) below.

(a) **Number of Shares.** Each Option Agreement shall state the number of Shares covered by the Option.

(b) **Type of Option.** Each Option Agreement shall specifically state the type of Option granted thereunder and whether it constitutes an Incentive Stock Option, Non-Qualified Stock Option, 102 Stock Option and the relevant track, or otherwise.

(c) **Exercise Price.** Each Option Agreement shall state the Exercise Price, which, in the case of an Incentive Stock Option, shall not be less than one hundred percent (100%) of the Fair Market Value of the Shares covered by the Option on the date of grant or such other amount as may be required pursuant to the Code. In the case of any other Option, the per share Exercise Price shall be equal to the amount determined by the Committee. In the case of an Incentive Stock Option granted to any Ten-Percent Shareholder, the Exercise Price shall be no less than 110% of the Fair Market Value of the Shares covered by the Option on the date of grant. In no event shall the Exercise Price of an Option be less than the par value of the shares for which such Option is exercisable. Subject to Article III and to the foregoing, the Committee may reduce the Exercise Price of any outstanding Option. The Exercise Price shall also be subject to adjustment as provided in Article VII hereof.

(d) Exercise Period. Each Option Agreement shall state the Exercise Period, as fixed by the Committee, subject to the vesting provisions set by the Committee as mentioned below, the early termination provisions set forth in Sub-Sections (h) through (k) hereof and provided that no Stock Option shall be exercisable more than five years after the date the Stock Option is granted.; At the expiration of the Exercise Period, all unexercised Options shall become null and void.

(e) Exercisability and Vesting Terms. Stock Options shall be exercisable at such time or times and subject to such terms and conditions as shall be determined by the Committee at grant and each Option Agreement shall provide the vesting schedule for the Stock Options as determined by the Committee. If the Committee provides, in its discretion, that any Stock Option is exercisable subject to certain limitations and/or vesting schedule (including, without limitation, that such Stock Option is exercisable only in installments and/or within certain time periods and/or subject to performance goals and/or measurements.), the Committee may waive such limitations on the exercisability at any time at or after grant in whole or in part (including, without limitation, waiver of the installment exercise provisions or acceleration of the time at which such Stock Option may be exercised), based on such factors, if any, as the Committee shall determine, in its sole discretion and the provisions with respect to any Stock Option need not be the same as the provisions with respect to any other Stock Option. Unless otherwise determined by the Committee at grant, the Stock Option agreement shall provide that (i) in the event the Participant engages in Detrimental Activity prior to any exercise of the Stock Option, all Stock Options held by the Participant shall thereupon terminate and expire, (ii) as a condition of the exercise of a Stock Option, the Participant shall be required to certify (or shall be deemed to have certified) at the time of exercise in a manner acceptable to the Company that the Participant is in compliance with the terms and conditions of this Plan and that the Participant has not engaged in, and does not intend to engage in, any Detrimental Activity, and (iii) in the event the Participant engages in Detrimental Activity during the one year period commencing on the later of the date the Stock Option is exercised or becomes vested, the Company shall be entitled to recover from the Participant at any time within one year after such exercise or vesting, and the Participant shall pay over to the Company, an amount equal to any gain realized as a result of the exercise (whether at the time of exercise or thereafter).

(f) Method of Exercise. Subject to whatever installment exercise and waiting period provisions apply under subsection (e) above, to the extent vested, Stock Options may be exercised in whole or in part at any time during the Stock Option term, by giving written notice of exercise to the Company specifying the number of Ordinary Shares to be purchased. Such notice shall be in a form acceptable to the Company and shall be accompanied by payment in full of the Exercise Price as follows: (i) in cash or by check, bank draft or money order payable to the order of the Company; (ii) solely to the extent permitted by applicable law, if the Ordinary Shares are traded on a national securities exchange or quoted on a national quotation system sponsored by the Financial Industry Regulatory Authority, and the Committee authorizes, through a procedure whereby the Participant delivers irrevocable instructions to a broker reasonably acceptable to the Committee to deliver promptly to the Company an amount equal to the Exercise Price; or (iii) on such other terms and conditions as may be acceptable to the Committee (including, without limitation, the relinquishment of Stock Options or by payment in full or in part in the form of Ordinary Shares (for which the Participant has good title free and clear of any liens and encumbrances) based on the Fair Market Value of the Ordinary Shares on the payment date as determined by the Committee, in its sole discretion). No Ordinary Shares shall be issued until payment therefor, as provided herein, has been made or provided for.

(g) Non-Transferability of Options. No Stock Option shall be Transferable by the Participant otherwise than by will or by the laws of descent and distribution, and all Stock Options shall be exercisable, during the Participant's lifetime, only by the Participant. Notwithstanding the foregoing, the Committee may determine, in its sole discretion, at the time of grant or thereafter that a Non-Qualified Stock Option that is otherwise not Transferable pursuant to this Section is Transferable to a Family Member in whole or in part and in such circumstances, and under such conditions, as determined by the Committee, in its sole discretion. A Non-Qualified Stock Option that is Transferred to a Family Member pursuant to the preceding sentence (i) may not be subsequently Transferred otherwise than by will or by the laws of descent and distribution and (ii) remains subject to the terms of this Plan and the applicable Award agreement. Any Ordinary Shares acquired upon the exercise of a Non-Qualified Stock Option by a permissible transferee of a Non-Qualified Stock Option or a permissible transferee pursuant to a Transfer after the exercise of the Non-Qualified Stock Option shall be subject to the terms of this Plan and the applicable Award agreement.

(h) Termination by Death, Disability or Retirement. Unless otherwise determined by the Committee at grant and specifically stated in the Option Agreement, or if no rights of the Participant are reduced, thereafter, if Participant's Termination is by reason of death, Disability or Retirement, all Stock Options that are held by such Participant (or, if relevant, by a Trustee under Section 102 of the Ordinance) that are vested and exercisable at the time of the Participant's Termination may be exercised by the Participant (or, in the case of death, by the legal representative of the Participant's estate) at any time within a period of one year from the date of such Termination, but in no event beyond the expiration of the Exercise Period of such Stock Options; provided, however, that in the case of Retirement, if the Participant dies within such Exercise Period, all unexercised Stock Options held by such Participant shall thereafter be exercisable, to the extent to which they were exercisable at the time of death, for a period of one year from the date of such death, but in no event beyond the expiration of the Exercise Period of such Stock Options.

(i) Involuntary Termination Without Cause. Unless otherwise determined by the Committee at grant and specifically stated in the Option Agreement, or if no rights of the Participant are reduced, thereafter, if a Participant's Termination is by involuntary termination without Cause, all Stock Options that are held by such Participant (or, if relevant, by a Trustee under Section 102 of the Ordinance) that are vested and exercisable at the time of the Participant's Termination may be exercised by the Participant at any time within a period of 90 days from the date of such Termination, but in no event beyond the expiration of the Exercise Period of such Stock Options.

(j) Voluntary Termination. Unless otherwise determined by the Committee at grant and specifically stated in the Option Agreement, or if no rights of the Participant are reduced, thereafter, if a Participant's Termination is voluntary (other than a voluntary termination described in subsection (k)(y) below), all Stock Options that are held by such Participant (or, if relevant, by a Trustee under Section 102 of the Ordinance) that are vested and exercisable at the time of the Participant's Termination may be exercised by the Participant at any time within a period of 30 days from the date of such Termination, but in no event beyond the expiration of the stated term of such Stock Options.

(k) Termination for Cause. Unless otherwise determined by the Committee at grant and specifically stated in the Option Agreement, or if no rights of the Participant are reduced, thereafter, if a Participant's Termination (x) is for Cause or (y) is a voluntary Termination (as provided in sub-section (j) above) after the occurrence of an event that would be grounds for a Termination for Cause, all Stock Options, whether vested or not vested, that are held by such Participant (or, if relevant, by a Trustee under Section 102 of the Ordinance) shall thereupon terminate and expire as of the date of such Termination.

(l) Unvested Stock Options. Unless otherwise determined by the Committee at grant and specifically stated in the Option Agreement, or if no rights of the Participant are reduced, thereafter, Stock Options that are not vested as of the date of a Participant's Termination for any reason shall terminate and expire as of the date of such Termination.

(m) Incentive Stock Option Limitations. To the extent that the aggregate Fair Market Value (determined as of the time of grant) of the Ordinary Shares with respect to which Incentive Stock Options are exercisable for the first time by an Eligible Employee during any calendar year under this Plan and/or any other stock option plan of the Company, any Subsidiary or any Parent exceeds \$100,000, such Options shall be treated as Non-Qualified Stock Options. Should any provision of this Plan not be necessary in order for the Stock Options to qualify as Incentive Stock Options, or should any additional provisions be required, the Committee may, in its sole discretion, amend this Plan accordingly, without the necessity of obtaining the approval of the stockholders of the Company.

(n) Form, Modification, Extension and Renewal of Stock Options. Subject to the terms and conditions and within the limitations of this Plan, Stock Options shall be evidenced by such an Option Agreement, and the Committee may, in its sole discretion (i) subject to Section 8.1(d) and the applicable law, modify, extend or renew outstanding Stock Options granted under this Plan (provided that the rights of a Participant are not reduced without his or her consent and provided that such action does not extend the Stock Option beyond its stated term), and (ii) accept the surrender of outstanding Stock Options (up to the extent not theretofore exercised) and authorize the granting of new Stock Options in substitution therefor (to the extent not theretofore exercised). Notwithstanding anything herein to the contrary, an outstanding Option may not be modified to reduce the exercise price thereof nor may a new Option at a lower price be substituted for a surrendered Option (other than adjustments or substitutions in accordance with Section 4.2), unless such action is approved by the stockholders of the Company.

(o) Other Terms and Conditions. Stock Options may contain such other provisions, which shall not be inconsistent with any of the terms of this Plan, as the Committee shall, in its sole discretion, deem appropriate.

#### **6.4 102 Stock Options.**

(a) Stock Options granted pursuant to this Section 6.4 are intended to be granted under Section 102 of the Ordinance pursuant to either (i) Section 102(b)(2) thereof as capital gains track options ("**102 Capital Gains Track Options**"), or (ii) Section 102(b)(1) thereof as ordinary income track options ("**102 Ordinary Income Track Options**"); together with 102 Capital Gains Track Options, "**102 Trustee Options**"). 102 Trustee Options shall be granted subject to the following special terms and conditions contained in this Section 6.4, the general terms and conditions specified in Section 6.3 hereof and other provisions of the Plan, except for any provisions of the Plan applying to Stock Options under different tax laws or regulations.

(b) The Company may grant only one type of 102 Trustee Option at any given time to all Participants who are to be granted 102 Trustee Options pursuant to this Plan, and shall file an election with the ITA regarding the type of 102 Trustee Option it elects to grant before the date of grant of any 102 Trustee Options (the “**Election**”). Such Election shall also apply to any bonus shares received by any Participant as a result of holding the 102 Trustee Options. The Company may change the type of 102 Trustee Option that it elects to grant only after the passage of at least 12 months from the end of the year in which the first grant was made in accordance with the previous Election, or as otherwise provided by applicable law. Any Election shall not prevent the Company from granting Options, pursuant to Section 102(c) of the Ordinance without a Trustee (“**102 Non-Trustee Options**”).

(c) Each 102 Trustee Option will be deemed granted on the date stated in a written notice to be provided by the Company, provided that on or before such date (i) the Company has provided such notice to the Trustee and (ii) the Participant has signed all documents required pursuant to applicable law and under the Plan.

(d) Each 102 Trustee Option, each Share issued pursuant to the exercise of any 102 Trustee Option, and any rights granted thereunder, including, without limitation, bonus shares, shall be allotted and issued to and registered in the name of the Trustee and shall be held in trust for the benefit of the Participant for a period of not less than the requisite period prescribed by the Ordinance and the Rules or such longer period as set by the Committee (the “**Required Holding Period**”). In the event that the requirements under Section 102 to qualify an Stock Option as a 102 Trustee Option are not met, then the Stock Option may be treated as a 102 Non-Trustee Option, all in accordance with the provisions of Section 102 and the Rules. After termination of the Required Holding Period, the Trustee may release such 102 Trustee Option and any such Shares, provided that (i) the Trustee has received an acknowledgment from the ITA that the Grantee has paid any applicable taxes due pursuant to the Ordinance or (ii) the Trustee and/or the Company and/or its Affiliate withholds any applicable taxes due pursuant to the Ordinance arising from the 102 Trustee Options and/or any Shares allotted or issued upon exercise of such 102 Trustee Options. The Trustee shall not release any 102 Trustee Options or Shares issued upon exercise thereof prior to the payment in full of the Participant’s tax liabilities arising from such 102 Trustee Options and/or Shares or the withholding referred to in (ii) above.

(e) Each 102 Trustee Option shall be subject to the relevant terms of the Ordinance and the Rules, which shall be deemed an integral part of the 102 Trustee Option and shall prevail over any term contained in the Plan or Option Agreement which is not consistent therewith. Any provision of the Ordinance, the Rules and any approvals by the Income Tax Commissioner not expressly specified in this Plan or Option Agreement which, as determined by the Committee, are necessary to receive or maintain any tax benefit pursuant to Section 102 shall be binding on the Participant. The Participant granted a 102 Trustee Option shall comply with the Ordinance and the terms and conditions of the Trust Agreement entered into between the Company and the Trustee. The Participant agrees to execute any and all documents, which the Company and/or its Affiliates and/or the Trustee may reasonably determine to be necessary in order to comply with the Ordinance and the Rules.

(f) During the Required Holding Period, the Participants shall not release from trust or sell, assign, transfer or give as collateral, the Shares issuable upon the exercise of a 102 Trustee Option and/or any securities issued or distributed with respect thereto, until the expiration of the Required Holding Period. Notwithstanding the above, if any such sale or release occurs during the Required Holding Period it will result in adverse tax consequences to the Participant under Section 102 of the Ordinance and the Rules, which shall apply to and shall be borne solely by such Participant. Subject to the foregoing, the Trustee may, pursuant to a written request from the Participant, release and transfer such Shares to a designated third party, provided that both of the following conditions have been fulfilled prior to such release or transfer: (i) payment has been made to the ITA of all taxes required to be paid upon the release and transfer of the Shares, and confirmation of such payment has been received by the Trustee and (ii) the Trustee has received written confirmation from the Company that all requirements for such release and transfer have been fulfilled according to the terms of the Company’s corporate documents, the Plan, the Option Agreement and any applicable law.



(g) If a 102 Trustee Option is exercised during the Required Holding Period, the Shares issued upon such exercise shall be issued in the name of the Trustee for the benefit of the Participant. If such 102 Trustee Option is exercised after the expiration of the Required Holding Period, the Shares issued upon such exercise shall, at the election of the Participant, either (i) be issued in the name of the Trustee, or (ii) be issued to the Participant, provided that the Participant first complies with all applicable provisions of the Plan and all taxes with respect thereto shall have been fully paid to the ITA.

(h) The foregoing provisions of this Section 6.4 relating to 102 Trustee Options shall not apply with respect to 102 Non-Trustee Options, which shall, however, be subject to the relevant provisions of Section 102 and the Rules.

(i) Upon receipt of a 102 Trustee Option, the Participant will sign an undertaking to release the Trustee from any liability with respect to any action or decision duly taken and executed in good faith by the Trustee in relation to the Plan, or any 102 Trustee Option or Share granted to such Participant thereunder.

## ARTICLE VII

### CHANGE IN CONTROL PROVISIONS

**7.1 Benefits.** In the event of a Change in Control of the Company, and except as otherwise provided by the Committee in an Option Agreement, a Participant's unvested Award shall not vest and a Participant's Award shall be treated in accordance with one of the following methods as determined by the Committee in its sole discretion:

(a) Awards, whether or not then vested, shall be continued, assumed, have new rights substituted therefor or be treated in accordance with Section 4.2(d) hereof, as determined by the Committee in its sole discretion. Notwithstanding anything to the contrary herein, for purposes of Incentive Stock Options, any assumed or substituted Stock Option shall comply with the requirements of Treasury Regulation § 1.424-1 (and any amendments thereto).

(b) The Committee, in its sole discretion, may provide for the purchase of any Awards by the Company or an Affiliate for an amount of cash equal to the excess of the Change in Control Price (as defined below) of the Ordinary Shares covered by such Awards, over the aggregate exercise price of such Awards. For purposes of this Section 7.1, Change in Control Price shall mean the highest price paid per Ordinary Shares in any transaction related to a Change in Control of the Company; provided, however, that such price shall not exceed the fair market value of the Common Stock at the time of purchase as determined in accordance Section 409A of the Code.

(c) The Committee may, in its sole discretion, provide for the cancellation of any Appreciation Awards without payment, if the Change in Control Price is less than the exercise price of such Appreciation Award.

(d) Notwithstanding anything else herein, the Committee may, in its sole discretion, provide for accelerated vesting or lapse of restrictions, of an Award at any time.

**7.2 Change in Control.** Unless otherwise determined by the Committee in the applicable Award agreement or other written agreement approved by the Committee, a “Change in Control” shall be deemed to occur following any transaction if: (i) any “person” as such term is used in Sections 13(d) and 14(d) of the Exchange Act (other than the Company, any KMN Person, any trustee or other fiduciary holding securities under any employee benefit plan of the Company, or any company owned, directly or indirectly, by the stockholders of the Company in substantially the same proportions as their ownership of Ordinary Shares of the Company), becomes the “beneficial owner” (as defined in Rule 13d-3 under the Exchange Act), directly or indirectly, of 50% or more of the combined voting power of the then outstanding securities of the Company (or its successor corporation); provided, however, that a merger or consolidation effected solely to implement a recapitalization of the Company shall not constitute a Change in Control of the Company; (ii) the stockholders of the Company approve a plan of complete liquidation of the Company; provided, that this subsection (ii) shall not constitute a Change in Control with respect to the amount of any payment pursuant to an Award under this Plan, or any portion thereof, that is triggered upon a Change in Control and that is intended to constitute “non-qualified deferred compensation” pursuant to Section 409A of the Code; or (iii) the consummation of the sale or disposition by the Company of all or substantially all of the Company’s assets other than (x) the sale or disposition of all or substantially all of the assets of the Company to a person or persons who beneficially own, directly or indirectly, at least 50% or more of the combined voting power of the outstanding voting securities of the Company at the time of the sale or (y) pursuant to a spinoff type transaction, directly or indirectly, of such assets to the stockholders of the Company.

## ARTICLE VIII

### TERMINATION OR AMENDMENT OF PLAN

**8.1 Termination or Amendment.** Notwithstanding any other provision of this Plan, the Board may at any time, and from time to time, amend, in whole or in part, any or all of the provisions of this Plan (including any amendment deemed necessary to ensure that the Company may comply with any regulatory requirement referred to in Article X), or suspend or terminate it entirely, retroactively or otherwise; provided, that without the approval of the holders of the Company’s Ordinary Shares entitled to vote in accordance with applicable law and the exchange or system on which the Company’s securities are then listed or traded, no amendment may be made that would:

(a) increase the aggregate number of Ordinary Shares that may be issued under this Plan pursuant to Section 4.1 (except by operation of Section 4.2);

(b) change the classification of individuals eligible to receive Awards under this Plan;

(c) other than adjustments or substitutions in accordance with Section 4.2, amend the terms of outstanding Awards to reduce the exercise price of outstanding Stock Options or to cancel outstanding Stock Options (where prior to the reduction or cancellation the exercise price equals or exceeds the fair market value of the Ordinary Shares underlying such Awards) in exchange for cash, or Stock Options with an exercise price that is less than the exercise price of the original Stock Options;

- (d) extend the maximum Exercise Period under Section 6.3;
- (e) award any Stock Option in replacement of a canceled Stock Option with a higher exercise price, except in accordance with Section 6.3(I); or
- (f) require stockholder approval in order for this Plan to comply with the applicable rules of any exchange or system on which the Company's securities are listed or traded at the request of the Company, the applicable provisions of Section 162(m) of the Code or, to the extent applicable to Incentive Stock Options, Section 422 of the Code.

#### ARTICLE IX

##### UNFUNDED PLAN

**9.1 Unfunded Status of Plan.** This Plan is an "unfunded" plan for incentive and deferred compensation. With respect to any payments as to which a Participant has a fixed and vested interest but that are not yet made to a Participant by the Company, nothing contained herein shall give any such Participant any rights that are greater than those of a general unsecured creditor of the Company.

#### ARTICLE X

##### GENERAL PROVISIONS

##### 10.1 RIGHTS AS A STOCKHOLDER; VOTING AND DIVIDENDS.

(a) A Participant shall have no rights as a shareholder of the Company with respect to any Ordinary Shares covered by the Award until the date of the lawful issuance of such Shares to the Participant. In the case of 102 Option Awards (if such Share Options are being held by a Trustee), a the Trustee shall have no rights as a shareholder of the Company with respect to any Shares covered by such Award until the date of the lawful issuance of such Shares for the Participant's benefit, and the Participant shall have no rights as a shareholder of the Company with respect to any Shares covered by the Award until the date of the release of such Shares from the Trustee to the Participant and the issuance of such Shares. No adjustment shall be made for dividends (ordinary or extraordinary, whether in cash, securities or other property) or distribution of other rights for which the record date is prior to the date such Share are issued, except as provided in Article VII hereof.

(b) With respect to all Ordinary Shares issued in the form of Awards hereunder or upon the exercise of Awards hereunder, any and all voting rights attached to such Shares and the Participant's entitlement to receive dividends distributed with respect to such Shares, shall be subject to the provisions of the Company's Articles of Association, as amended from time to time, and subject to any applicable law.

(c) Regarding Share issued pursuant to the exercise of any 102 Trustee Option any rights distributed to the Participants shall be deposited with and/or issued to the Trustee for the benefit of the Participants. All said rights, excluding dividends, shall be held by the Trustee for the applicable Required Holding Period. In the case that the Company distributes dividends, than the amount of dividends with respect of Shares held in trust shall be paid to the Participants that are the beneficial holders of such Shares, subject to deduction at source of the applicable tax.

(d) The Company may, but shall not be obligated to, register or qualify the sale of Shares under any applicable securities law or any other applicable law.

**10.2 Legend.** The Committee may require each person receiving Ordinary Shares pursuant to a Stock Option under this Plan to represent to and agree with the Company in writing that the Participant is acquiring the shares without a view to distribution thereof. In addition to any legend required by this Plan, the certificates for such shares may include any legend that the Committee, in its sole discretion, deems appropriate to reflect any restrictions on Transfer.

All certificates for Ordinary Shares delivered under this Plan shall be subject to such stop transfer orders and other restrictions as the Committee may, in its sole discretion, deem advisable under the rules, regulations and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Ordinary Shares are then listed or any national securities exchange system upon whose system the Ordinary Shares are then quoted, any applicable Federal or state securities law, and any applicable corporate law, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

**10.3 Other Plans.** Nothing contained in this Plan shall prevent the Board from adopting other or additional compensation arrangements, subject to stockholder approval if such approval is required; and such arrangements may be either generally applicable or applicable only in specific cases.

**10.4 No Right to Employment/Directorship/Consultancy.** Neither this Plan nor the grant of any Option hereunder shall give any Participant or other employee, Consultant or Non-Employee Director any right with respect to continuance of employment, consultancy or directorship by the Company or any Affiliate, nor shall they be a limitation in any way on the right of the Company or any Affiliate by which an employee is employed or a Consultant or Non-Employee Director is retained to terminate his or her employment, consultancy or directorship at any time.

**10.5 Withholding of Taxes.** The Company shall have the right to deduct from any payment to be made pursuant to this Plan, or to otherwise require, prior to the issuance or delivery of any Ordinary Shares or the payment of any cash hereunder, payment by the Participant of, any Federal, state or local taxes required by law to be withheld. Any statutorily required withholding obligation with regard to any Participant may be satisfied, subject to the consent of the Committee, by reducing the number of Ordinary Shares otherwise deliverable or by delivering Ordinary Shares already owned. Any fraction of a share of Ordinary Shares required to satisfy such tax obligations shall be disregarded and the amount due shall be paid instead in cash by the Participant.

**10.6 No Assignment of Benefits.** No Award or other benefit payable under this Plan shall, except as otherwise specifically provided by law or permitted by the Committee, be Transferable in any manner, and any attempt to Transfer any such benefit shall be void, and any such benefit shall not in any manner be liable for or subject to the debts, contracts, liabilities, engagements or torts of any person who shall be entitled to such benefit, nor shall it be subject to attachment or legal process for or against such person.

**10.7 Listing and Other Conditions.**

(a) Unless otherwise determined by the Committee, as long as the Ordinary Shares are listed on a national securities exchange or system sponsored by a national securities association, the issue of any Ordinary Shares pursuant to an Award shall be conditioned upon such shares being listed on such exchange or system. The Company shall have no obligation to issue such shares unless and until such shares are so listed, and the right to exercise any Option with respect to such shares shall be suspended until such listing has been effected.

(b) If at any time counsel to the Company shall be of the opinion that any sale or delivery of Ordinary Shares pursuant to an Option is or may in the circumstances be unlawful or result in the imposition of excise taxes on the Company under the statutes, rules or regulations of any applicable jurisdiction, the Company shall have no obligation to make such sale or delivery, or to make any application or to effect or to maintain any qualification or registration under the Securities Act or otherwise, with respect to Ordinary Shares or Awards, and the right to exercise any Option shall be suspended until, in the opinion of said counsel, such sale or delivery shall be lawful or will not result in the imposition of excise taxes on the Company.

(c) Upon termination of any period of suspension under this Section 10.7, any Award affected by such suspension which shall not then have expired or terminated shall be reinstated as to all shares available before such suspension and as to shares which would otherwise have become available during the period of such suspension, but no such suspension shall extend the term of any Award.

(d) A Participant shall be required to supply the Company with any certificates, representations and information that the Company requests and otherwise cooperate with the Company in obtaining any listing, registration, qualification, exemption, consent or approval the Company deems necessary or appropriate.

**10.8 Governing Law.** This Plan and actions taken in connection herewith shall be governed and construed in accordance with the laws of Israel (regardless of the law that might otherwise govern under applicable Israeli principles of conflict of laws).

**10.9 Construction.** Wherever any words are used in this Plan in the masculine gender they shall be construed as though they were also used in the feminine gender in all cases where they would so apply, and wherever any words are used herein in the singular form they shall be construed as though they were also used in the plural form in all cases where they would so apply.

**10.10 Other Benefits.** No Award granted or paid out under this Plan shall be deemed compensation for purposes of computing benefits under any retirement plan of the Company or its Affiliates nor affect any benefits under any other benefit plan now or subsequently in effect under which the availability or amount of benefits is related to the level of compensation.

**10.11 Costs.** The Company shall bear all expenses associated with administering this Plan, including expenses of issuing Ordinary Shares pursuant to any Awards hereunder.

**10.12 No Right to Same Benefits.** The provisions of Awards need not be the same with respect to each Participant, and such Awards to individual Participants need not be the same in subsequent years.

**10.13 Death/Disability.** The Committee may in its sole discretion require the transferee of a Participant to supply it with written notice of the Participant's death or Disability and to supply it with a copy of the will (in the case of the Participant's death) or such other evidence as the Committee deems necessary to establish the validity of the transfer of an Award. The Committee may, in its discretion, also require that the agreement of the transferee to be bound by all of the terms and conditions of this Plan.

**10.14 Section 16(b) of the Exchange Act.** All elections and transactions under this Plan by persons subject to Section 16 of the Exchange Act involving shares of Common Stock are intended to comply with any applicable exemptive condition under Rule 16b-3. The Committee may, in its sole discretion, establish and adopt written administrative guidelines, designed to facilitate compliance with Section 16(b) of the Exchange Act, as it may deem necessary or proper for the administration and operation of this Plan and the transaction of business thereunder.

**10.15 Section 409A of the Code / Section 102 of the Ordinance.** Although the Company does not guarantee the particular tax treatment of an Award granted under this Plan, Awards made under this Plan are intended to comply with, or be exempt from, the applicable requirements of Section 409A of the Code and/or Section 102 of the Ordinance, as may be applicable, and this Plan and any Award agreement hereunder shall be limited, construed and interpreted in accordance with such intent. In no event whatsoever shall the Company or any of its Affiliates be liable for any additional tax, interest or penalties that may be imposed on a Participant by Section 409A of the Code and/or Section 102 of the Ordinance, as may be applicable, or any damages for failing to comply with Section 409A of the Code and/or Section 102 of the Ordinance, as may be applicable.

**10.16 Successor and Assigns.** This Plan shall be binding on all successors and permitted assigns of a Participant, including, without limitation, the estate of such Participant and the executor, administrator or trustee of such estate.

**10.17 Severability of Provisions.** If any provision of this Plan shall be held invalid or unenforceable, such invalidity or unenforceability shall not affect any other provisions hereof, and this Plan shall be construed and enforced as if such provisions had not been included.

**10.18 Payments to Minors, Etc.** Any benefit payable to or for the benefit of a minor, an incompetent person or other person incapable of receipt thereof shall be deemed paid when paid to such person's guardian or to the party providing or reasonably appearing to provide for the care of such person, and such payment shall fully discharge the Committee, the Board, the Company, its Affiliates and their employees, agents and representatives with respect thereto.

**10.19 Headings and Captions.** The headings and captions herein are provided for reference and convenience only, shall not be considered part of this Plan, and shall not be employed in the construction of this Plan.

## ARTICLE XI

### EFFECTIVE DATE OF PLAN

The Plan was adopted by the Board on November 24, 2011 and amended by the Board on December 13, 2011 and on March 22, 2012 subject to, and to be effective upon, the approval of the stockholders of the Company in accordance with the requirements of the laws Israel.

## ARTICLE XII

### TERM OF PLAN

No Award shall be granted pursuant to this Plan on or after March 22, 2022, but Awards granted prior to such date may extend beyond that date.

ARTICLE XIII

NAME OF PLAN

This Plan shall be known as “The TAT Technologies Ltd 2012 Stock Option Plan.”



## Report of Independent Registered Public Accounting Firm

The Board of Directors  
First Aviation Services Inc.

We have audited the accompanying consolidated balance sheets of First Aviation Services Inc. and Subsidiaries (the "Company") as of December 31, 2012 and 2011, and the related consolidated statements of operations, comprehensive loss, stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of First Aviation Services Inc. and Subsidiaries as of December 31, 2012 and 2011, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 3, the 2011 consolidated financial statements have been restated to correct misstatements.

/s/ Dixon Hughes Goodman LLP

Memphis, Tennessee  
March 20, 2013

999 South Shady Grove Road, Suite 400, Memphis, TN 38120 | T 901.761.3000 | F 901.761.9667 | dhgllp.com





List of Subsidiaries of the Registrant

We own the following significant subsidiaries:

1. Limco-Piedmont Inc., a 100%-owned Delaware subsidiary.
  2. Limco Airepair Inc., a wholly-owned Delaware subsidiary of Limco-Piedmont Inc.
  3. Piedmont Aviation Component Services LLC, a North Carolina limited liability company, wholly-owned subsidiary of Limco-Piedmont Inc.
  4. TAT-GAL Inc., a wholly-owned California subsidiary.
  5. Bental Industries Ltd., a 70%-owned Israeli subsidiary.
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**CERTIFICATION OF CHIEF EXECUTIVE OFFICER  
Pursuant to Rule 13a-14(a) and 15d-14(a)  
Under the Securities Exchange Act of 1934, as Amended**

I, Itsik Maaravi, certify that:

1. I have reviewed this annual report on Form 20-F of TAT Technologies 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 registrant as of, and for, the periods presented in this report;
  4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13(a)-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
    - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated Subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
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(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant'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 registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: April 25, 2013

/s/ Itsik Maaravi

Itsik Maaravi

Chief Executive Officer

\* The originally executed copy of this Certification will be maintained at the Company's offices and will be made available for inspection upon request.

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**CERTIFICATION OF CHIEF FINANCIAL OFFICER  
Pursuant to Rule 13a-14(a) and 15d-14(a)  
Under the Securities Exchange Act of 1934, as Amended**

I, Yaron Shalem, certify that:

1. I have reviewed this annual report on Form 20-F of TAT Technologies 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 registrant as of, and for, the periods presented in this report;
  4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13(a)-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
    - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated Subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
    - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
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(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant'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 registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: April 25, 2013

/s/ Yaron Shalem

Yaron Shalem

Chief Financial Officer (Principal Accounting Officer)

\* The originally executed copy of this Certification will be maintained at the Company's offices and will be made available for inspection upon request.

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of TAT Technologies Ltd. (the "Company") on Form 20-F for the period ending December 31, 2012 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Itsik Maaravi, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Itsik Maaravi  
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Itsik Maaravi  
Chief Executive Officer

April 25, 2013

\* The originally executed copy of this Certification will be maintained at the Company's offices and will be made available for inspection upon request.

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of TAT Technologies Ltd. (the "Company") on Form 20-F for the period ending December 31, 2012, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Yaron Shalem, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. ss. 1350, as adopted pursuant to ss. 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Itsik Maaravi

Yaron Shalem  
Chief Financial Officer (Principal Accounting Officer)

April 25, 2013

\* The originally executed copy of this Certification will be maintained at the Company's offices and will be made available for inspection upon request.

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