BioLineRx Ltd.

2010 ANNUAL REPORT

BioLineRx Ltd.

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REPORT OF INDEPENDENT REGISTERED ACCOUNTING FIRM

To the shareholders of

BioLineRx Ltd.

We have audited the accompanying consolidated statements of financial position of BioLineRx Ltd. (the "Company") and its consolidated entities as of December 31, 2009 and 2010 and the related consolidated statements of comprehensive income (loss), changes in equity and cash flows for each of the three years in the period ended December 31, 2010. These financial statements are the responsibility of the Company's Board of Directors and management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its consolidated entities as of December 31, 2009 and 2010 and their results of operations and cash flows for each of the three years in the period ended December 31, 2010, in conformity with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").

Tel Aviv, Israel
March 27, 2011

Kesselman & Kesselman
Certified Public Accountants (Isr.)
Member of PricewaterhouseCoopers International Ltd.

BioLineRx Ltd.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	Note	December 31, 2009	December 31, 2010	Convenience translation into USD (Note 1b) December 31, 2010
		NIS in thousands		In thousands
Assets				
CURRENT ASSETS				
Cash and cash equivalents	2i, 5a	105,890	111,746	32,102
Short-term bank deposits	5b	-	28,037	8,054
Prepaid expenses		1,094	46	13
Trade accounts receivable	2k,15	37,750	-	-
Other receivables	14a	2,313	6,313	1,814
Total current assets		147,047	146,142	41,983
NON-CURRENT ASSETS				
Restricted deposits	2j, 12b(1)	3,704	2,414	693
Long-term prepaid expenses	14b	1,150	196	56
Property and equipment, net	6	4,175	4,509	1,295
Intangible assets, net	7	3,042	1,352	388
Asset in respect of retirement benefit obligations	2s	49	-	-
Total non-current assets		12,120	8,471	2,432
Total assets		159,167	154,613	44,415
Liabilities and equity				
CURRENT LIABILITIES	3a			
Current maturities of long-term bank loan	8	-	307	88
Accounts payable and accruals:				
Trade	14c(1)	6,452	3,849	1,106
OCS		14,005	5,993	1,722
Licensors		10,570	1,491	428
Other	14c(2)	10,203	10,551	3,031
Total current liabilities		41,230	22,191	6,375
NON-CURRENT LIABILITIES				
Long term bank loan, net of current maturities	8		432	124
Retirement benefit obligations	2s(1)	-	30	8
Total non-current liabilities		-	462	132
COMMITMENTS AND CONTINGENT LIABILITIES	12			
Total liabilities		41,230	22,653	6,507
EQUITY	9			
Ordinary shares		1,235	1,236	355
Share premium		412,513	414,435	119,056
Warrants		6,549	6,549	1,881
Capital reserve		22,963	27,623	7,935
Accumulated deficit		(325,323)	(317,883)	(91,319)
Total equity		117,937	131,960	37,908
Total liabilities and equity		159,167	154,613	44,415

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

BioLineRx Ltd.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	Note	Year ended December 31,			Convenience translation into USD (Note 1b)
		2008	2009	2010	2010
		NIS in thousands			In thousands
REVENUES	15,16	-	63,909	113,160	32,508
COST OF REVENUES	14d	-	(22,622)	(25,571)	(7,346)
GROSS PROFIT		-	41,287	87,589	25,162
RESEARCH AND DEVELOPMENT EXPENSES, NET	14e	(106,156)	(90,302)	(54,966)	(15,790)
SALES AND MARKETING EXPENSES	14f	-	(3,085)	(4,609)	(1,324)
GENERAL AND ADMINISTRATIVE EXPENSES	14g	(13,083)	(11,182)	(14,875)	(4,273)
GAIN ON ADJUSTMENT OF WARRANTS TO FAIR VALUE	2l	3,658	-	-	-
OPERATING INCOME (LOSS)		(115,581)	(63,282)	13,139	3,775
FINANCIAL INCOME	14h	13,001	3,928	3,056	877
FINANCIAL EXPENSES	14i	(12,269)	(2,164)	(8,755)	(2,515)
NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS) FOR THE YEAR		(114,849)	(61,518)	7,440	2,137
		NIS			USD
EARNINGS (LOSS) PER ORDINARY SHARE - BASIC	11a	(1.44)	(0.63)	0.06	0.02
EARNINGS PER ORDINARY SHARE - DILUTED	11a	-	-	0.06	0.02

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

BioLineRx Ltd.

STATEMENTS OF CHANGES IN EQUITY

	Ordinary shares	Warrants	Share premium	Capital Reserve	Accumulated deficit	Total
	NIS in thousands					
BALANCE AT JANUARY 1, 2008	625	-	307,658	23,926	(148,956)	183,253
CHANGES IN 2008:						
Warrants reclassified from liabilities to equity	-	947	-	-	-	947
Share-based compensation	-	-	-	9,035	-	9,035
Comprehensive loss for the year	-	-	-	-	(114,849)	(114,849)
BALANCE AT DECEMBER 31, 2008	625	947	307,658	32,961	(263,805)	78,386
CHANGES IN 2009:						
Exercise of warrants	*	*	3	-	-	3
Expiration of warrants	-	(947)	947	-	-	-
Employee stock options exercised	30	-	13,143	(13,057)	-	116
Employee stock options expired	-	-	340	(340)	-	-
Issuance of share capital and warrants, net	580	6,549	90,422	-	-	97,551
Share-based compensation	-	-	-	3,399	-	3,399
Comprehensive loss for the year	-	-	-	-	(61,518)	(61,518)
BALANCE AT DECEMBER 31, 2009	1,235	6,549	412,513	22,963	(325,323)	117,937
CHANGES IN 2010:						
Employee stock options exercised	1	-	291	(266)	-	26
Employee stock options expired	-	-	1,631	(1,631)	-	-
Share-based compensation	-	-	-	6,557	-	6,557
Comprehensive income for the year	-	-	-	-	7,440	7,440
BALANCE AT DECEMBER 31, 2010	1,236	6,549	414,435	27,623	(317,883)	131,960

* Represents an amount less than NIS 1,000.

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

BioLineRx Ltd.

CONSOLIDATED CASH FLOW STATEMENTS

	Year ended December 31,			Convenience translation into USD (Note 1b)
	2008	**2009**	**2010**	**2010**
	NIS in thousands			**In thousands**
CASH FLOWS - OPERATING ACTIVITIES				
Net income (loss) for the year	(114,849)	(61,518)	7,440	2,137
Adjustments required to reflect net cash used in operating activities (see appendix below)	21,080	(22,978)	33,231	9,546
Net cash provided by (used in) operating activities	(93,769)	(84,496)	40,671	11,683
CASH FLOWS - INVESTING ACTIVITIES				
Proceeds from sale of financial assets at fair value through profit or loss	27,851	30,837	-	-
Proceeds from sale of financial assets at fair value through profit or loss - restricted	-	3,767	-	-
Purchase of financial assets at fair value through profit or loss	(58,327)	-	-	-
Purchase of financial assets at fair value through profit or loss - restricted	(3,757)	-	-	-
Investment in short-term deposits	-	-	(28,333)	(8,139)
Investment in restricted deposits	-	(3,147)	(206)	(59)
Withdrawal of restricted deposits	5,977	251	1,353	389
Purchase of property and equipment	(3,255)	(235)	(1,853)	(532)
Grants received in respect of property and equipment	28	-	-	-
Proceeds from sale of property and equipment	-	3	-	-
Purchase of intangible assets	(1,790)	(628)	(492)	(141)
Net cash provided by (used in) investing activities	(33,273)	30,848	(29,531)	(8,482)
CASH FLOWS - FINANCING ACTIVITIES				
Issuance of share capital and warrants, net of issuance expenses	-	97,551	-	-
Proceeds of bank loan			1,020	293
Repayments of bank loan			(281)	(81)
Proceeds from exercise of warrants	-	3	-	-
Proceeds from exercise of employee stock options	-	116	26	7
Net cash provided by financing activities	-	97,670	765	219
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(127,042)	44,022	11,905	3,420
CASH AND CASH EQUIVALENTS – BEGINNING OF YEAR	193,798	60,379	105,890	30,420
EXCHANGE DIFFERENCES ON CASH AND CASH EQUIVALENTS	(6,377)	1,489	(6,049)	(1,738)
CASH AND CASH EQUIVALENTS - END OF YEAR	60,379	105,890	111,746	32,102

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

BioLineRx Ltd.

CONSOLIDATED CASH FLOW STATEMENTS

	Year ended December 31,			Convenience translation into USD (Note 1b)
	2008	2009	2010	2010
	NIS in thousands			In thousands
APPENDIX				
Adjustments required to reflect net cash used in operating activities:				
Income and expenses not involving cash flows:				
Depreciation and amortization	1,676	1,754	1,814	521
Impairment of intangible assets	603	584	1,846	530
Retirement benefit obligations	-	(63)	79	23
Long-term prepaid expenses	(103)	(880)	954	274
Gain on adjusting warrants to fair value	(3,658)	-	-	-
Loss on sale of property and equipment	-	1	-	-
Exchange differences on cash and cash equivalents	6,377	(1,489)	6,049	1,738
Gain on fair value adjustments to financial assets at fair value through profit or loss	(273)	(98)	-	-
Share-based compensation	9,035	3,399	6,557	1,884
Interest and exchange differences on short-term deposits			296	85
Interest and exchange differences on restricted deposits	156	(204)	143	41
	13,813	3,004	17,738	5,096
Changes in operating asset and liability items:				
Decrease (increase) in trade accounts receivable and other receivables	(9,812)	(29,877)	34,798	9,996
Increase (decrease) in accounts payable and accruals	17,079	3,895	(19,305)	(5,546)
	7,267	(25,982)	15,493	4,450
	21,080	(22,978)	33,231	9,546
Supplementary information on investing and financing activities not involving cash flows:				
Credit received in connection with purchase of property and equipment			104	30
Credit received in connection with purchase of intangible assets	238	245	100	29
Warrants reclassified from liabilities to equity	947	-	-	-
Supplementary information on interest received in cash	3,901	443	1,013	291

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

NOTE 1 – GENERAL INFORMATION

a. General

BioLineRx Ltd. (the “Company”) was incorporated and commenced operations in April 2003. The Company’s headquarters are in Jerusalem, Israel.

Since incorporation, the Company has been engaged, both independently and through its consolidated entities (collectively, the “Group”), in the development of therapeutics, from early-stage development to advanced clinical trials, for a wide range of medical needs.

In December 2004, the Company formed a limited partnership, BioLine Innovations Jerusalem L.P. (the “Partnership”), which commenced operations on January 1, 2005. The Company holds a 99% interest in the Partnership, with the remaining 1% held by a wholly-owned subsidiary of the Company, BioLine Innovations Ltd. (the “Subsidiary”). The Partnership was established to operate an industrial research and development center in an incubator located in Jerusalem (the “Incubator”) under an agreement with the State of Israel. See Note 12a(1).

In February 2007, the Company listed its securities on the Tel Aviv Stock Exchange (“TASE”) – see Note 9.

In January 2008, the Company established a wholly-owned subsidiary, BioLineRx USA Inc., which serves as the Group’s business development arm in the United States. In January 2011, the Company announced its intention to transfer its business development activities to Israel.

As noted above, the Company has been engaged in the development of therapeutics since its incorporation. As of the date of these financial statements, the Company has succeeded in out-licensing two of its products. Nevertheless, the Company cannot determine with reasonable certainty if and when it will become profitable on a current basis.

b. Convenience translation into US dollars (“dollars” or “USD”)

For the convenience of the reader, the reported New Israeli Shekel (NIS) amounts as of December 31, 2010 have been translated into dollars, at the representative rate of exchange on March 31, 2011 (USD 1 = NIS 3.481). The dollar amounts presented in these financial statements should not be construed as representing amounts that are receivable or payable in dollars or convertible into dollars, unless otherwise indicated.

c. Approval of consolidated financial statements

The consolidated financial statements of the Company for the year ended December 31, 2010 were approved by the Board of Directors of the Company on March 27, 2011, and signed on its behalf by the Chairman of the Board, the Company’s Chief Executive Officer and the Company’s Chief Financial and Operating Officer.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES

a. Basis of presentation

The Company's consolidated financial statements as of December 31, 2010 and 2009, and for each of the three years in the period ended December 31, 2010, have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"). The significant accounting policies described below have been applied on a consistent basis for all years presented, unless noted otherwise.

The consolidated financial statements have been prepared on the basis of historical cost, subject to adjustment of financial assets and liabilities to their fair value through profit or loss and adjustment of assets and liabilities in connection with retirement benefit obligations.

The Company classifies its expenses on the statement of comprehensive income (loss) based on the operating characteristics of such expenses. The Company's annual operating cycle consists of a standard 12-month period.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. Areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4. Actual results may differ materially from estimates and assumptions used by the Group's management.

b. Consolidation of the financial statements

Consolidated entities (the Partnership and the Subsidiaries) include all entities over which the Company has the power to govern the financial and operating policies, which generally involves holding more than 50% of the shares or interests conferring voting rights of the applicable entity. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls an entity. Consolidated entities are fully consolidated from the date on which control of such entities is transferred to the Company and they are de-consolidated from the date that control ceases. The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group.

c. Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which each entity operates (the "functional currency"). The consolidated financial statements are presented in NIS, which is the Group's functional and presentation currency.

Transactions that are executed in currencies other than the Group's functional currency ("foreign currency transactions") are translated into the functional currency using the exchange rates prevailing at the date of each transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in profit or loss.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

d. Property and equipment

Property and equipment are stated at historical cost less depreciation and related grants received from the Office of the Chief Scientist of the Israeli Ministry of Industry, Trade and Labor (the "OCS"). Historical cost includes expenditures that are directly attributable to the acquisition of the items. Assets are depreciated by the straight-line method over the estimated useful lives of the assets, provided that the Group's management believes the residual values of the assets to be negligible, as follows:

	%
Computers and communications equipment	20-33
Office furniture and equipment	6-15
Laboratory equipment	15-20

The assets' residual values, methods of depreciation and useful lives are reviewed, and adjusted, if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

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

Grants received from the OCS are recognized in profit or loss over the life of a depreciable asset as a reduction in depreciation expense.

e. Intangible assets

The Group applies the cost method of accounting in subsequent measurements of intangible assets. Under this method of accounting, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Intellectual property
The Group recognizes in its financial statements intangible assets developed by the Group to the extent that the conditions stipulated in o. below are met. Intellectual property acquired by the Group is initially measured at cost. Intellectual property acquired by the Group is not amortized and is tested annually for impairment. See f. below.

Computer software
Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized over the estimated useful lives of the software programs (3-5 years).

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

f. Impairment of non-financial assets

Intangible assets are tested annually for impairment, except for computer software that is amortized, as detailed in 2e above. In addition, impairment testing of intellectual property is required when the Group decides to terminate or suspend the development of a project based on such intellectual property. Property and equipment, as well as computer software, are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized equal to the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and the asset's value in use to the Group.

g. Government grants

Government grants are recognized at fair value, whenever it is probable that the grant will be received and that the Group will comply with all the conditions in respect thereof.

Government grants related to periodic costs are deferred and recognized in profit or loss over the period required to match the related costs.

Government grants related to fixed assets are recorded as a reduction in the book value of the related assets, and are charged to profit and loss in accordance with the straight-line method.

h. Financial assets

1) Classification

The Group classifies its financial assets in the following categories: at fair value through profit or loss and loans and receivables. The classification depends on the purpose for which each financial asset was acquired. The Group's management determines the classification of financial assets at initial recognition:

a) Financial assets at fair value through profit or loss

A financial asset is classified in this category if management has designated it as a financial asset upon initial recognition, because it is managed and its performance is evaluated on a fair-value basis in accordance with a documented risk management or investment strategy. The Group's investment policy with regard to its excess cash, as adopted by the Company's Board of Directors, is composed of the following objectives: (i) preserving investment principal, (ii) providing liquidity and (iii) providing optimum yields pursuant to the policy guidelines and market conditions. The policy provides detailed guidelines as to the securities and other financial instruments in which the Group is allowed to invest. In addition, in order to maintain liquidity, investments are structured to provide flexibility to liquidate at least 50% of all investments within 15 business days. Information about these assets, including details of the portfolio and income earned, is provided internally on a quarterly basis to the Group's key management personnel. Any divergence from this investment policy requires approval from the Company's Board of Directors.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

h. Financial assets (cont.)

b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These assets are included in current assets, except for installments which are due more than 12 months subsequent to the balance sheet date. Such installments are included in non-current assets. The Group's loans and receivables include "accounts receivable," "cash and cash equivalents," "short-term investments," "restricted deposits" and "bank loans" in the balance sheet. See Notes 2i, 2j and 2k.

2) Recognition and measurement

Regular purchases and sales of financial assets are recognized on the trade-date - the date on which the Group commits to purchase or sell the asset. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the income statement. Financial assets are de-recognized when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are subsequently carried at amortized cost using the effective interest method.

Gains or losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are presented in the income statement within "other (losses)/gains - net" in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognized in the income statement as part of other income when the Group's right to receive payments is established.

3) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

i. Cash equivalents

In the consolidated statement of cash flows, cash and cash equivalents includes cash on hand and short-term bank deposits (up to three months from date of deposit) that are not restricted as to withdrawal or use, and are therefore considered to be cash equivalents.

j. Restricted deposits

The Company has placed a lien on NIS and dollar deposits in banks to secure its liabilities to various parties. Those deposits are presented separately as non-current assets, in accordance with the timing of the restriction. See Note 12b(1).

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

k. Trade receivables

Trade receivable balances relate to amounts receivable from customers of the Group in respect of sub-licenses granted, or services that have been provided, in the ordinary course of business. If collection of these amounts is expected within one year or less, they are classified in current assets; otherwise, they are reflected in non-current assets.

Trade receivables are initially recognized at their fair value. Thereafter, they are measured at amortized cost, based on the effective interest method, less any allowance for doubtful accounts.

l. Warrants

Receipts in respect of warrants are classified as equity to the extent that they confer the right to purchase a fixed number of shares for a fixed exercise price. As part of the Company's initial public offering on the TASE in February 2007, the Company issued Series 1 warrants with an exercise price linked to the Israeli Consumer Price Index ("CPI"). Accordingly, the exercise price was not deemed to be fixed and, as such, the Series 1 warrants did not qualify for equity classification. As long as the exercise price was linked to the CPI, the Series 1 warrants were classified as liabilities and carried at fair value, with changes in their fair value recognized in profit or loss. The issuance costs of the Series 1 warrants were also directly charged to profit or loss. Following the amendment in 2008 of the terms of the Series 1 warrants, pursuant to which the linkage of the exercise price to the CPI was cancelled, the warrants were classified in equity.

m. Share capital

The Company's Ordinary Shares are classified as equity. Incremental costs directly attributable to the issuance of new shares or warrants are reflected in equity as a deduction from the issuance proceeds.

n. Trade payables

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities. Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

o. Deferred taxes

Deferred taxes are recognized using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax assets are recognized only to the extent that it is probable that future taxable income will be available against which the temporary differences can be utilized.

As the Group is currently engaged primarily in development activities and is not expected to generate taxable income in the foreseeable future, no deferred tax assets are included in the financial statements.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

p. Revenue recognition

The Group recognizes revenue in accordance with International Accounting Standard ("IAS") 18 – "Revenue," including guidance regarding arrangements with multiple deliverables. Pursuant to this guidance, the Group applies revenue recognition criteria to the separately identifiable components of a single transaction. The consideration from the arrangement is allocated among the separately identifiable components by reference to their fair value.

Revenues incurred in connection with the out-licensing of the Group's patents and other intellectual property are recognized when all of the following criteria have been met as of the balance sheet date:

- The Group has transferred to the buyer the significant risks and rewards of ownership of the patents and intellectual property.
- The Group does not retain either the continuing managerial involvement to the degree usually associated with ownership or the effective control over the patent and intellectual property.
- The amount of revenue can be measured reliably.
- It is probable that the economic benefits associated with the transaction will flow to the Group.
- The costs incurred or to be incurred in respect of the sale can be measured reliably.

Revenues in connection with rendering of services are recognized by reference to the stage of completion of the transaction as of the balance sheet date, if and when the outcome of the transaction can be estimated reliably.

Revenues from royalties are recognized on an accrual basis in accordance with the substance of the relevant agreement.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

q. Research and development expenses

Research expenses are charged to operations as incurred.

An intangible asset arising from development (or from the development phase of an internal project) is recognized if all of the following conditions are fulfilled:

- technical feasibility exists for completing development of the intangible asset so that it will be available for use or sale.
- it is management's intention to complete development of the intangible asset for use or sale.
- the Company has the ability to use or sell the intangible asset.
- it is probable that the intangible asset will generate future economic benefits, including existence of a market for the output of the intangible asset or the intangible asset itself or, if the intangible asset is to be used internally, the usefulness of the intangible asset.
- adequate technical, financial and other resources are available to complete development of the intangible asset, as well as the use or sale thereof.
- the Company has the ability to reliably measure the expenditure attributable to the intangible asset during its development.

Other development costs that do not meet the foregoing conditions are charged to operations as incurred. Development costs previously expensed are not recognized as an asset in subsequent periods. As of December 31, 2010, the Group has not yet capitalized development expenses.

r. Government participation in research and development expenses

The Group receives participation in research and development expenses from the State of Israel through the OCS, both in the form of loans extended to the Incubator for research and development, as described in Note 12a(1), and in the form of grants, as described in Note 12a(2).

Despite the formal difference between the two types of support from the OCS, there is no material financial difference between them. Each loan and grant qualifies as a "forgivable loan" in accordance with IAS 20, "Accounting for Government Grants and Disclosure of Government Assistance," since the loans and grants are repayable only if the Group generates revenues related to the project that is the subject of the loan or grant.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

r. Government participation in research and development expenses (cont.)

The Company recognizes each forgivable loan on a systematic basis at the same time the Company records, as an expense, the related development costs for which the grant/loan is received, provided that there is reasonable assurance that (a) the Company complies with the conditions attached to the grant/loan and (b) the grant/loan will be received. The amount of the forgivable loan is recognized based on the participation rate approved by the OCS.

The Company accounts for each forgivable loan as a liability unless it is more likely than not that the Company will meet the terms of forgiveness, in which case the forgivable loan is accounted for as a government grant and carried to income as a reduction of research and development expenses.

Government grants received in respect of investments in property and equipment are presented as a reduction of the cost of such assets.

If forgivable loans are initially carried to income, as described above, and, in subsequent periods, it appears more likely than not that the project will be successful and that the loans will be repaid or royalties paid to the OCS, the Group recognizes a liability on the balance sheet.

s. Employee benefits

1) Pension and severance pay obligations

Israeli labor laws and the Group's agreements require the Group to pay retirement benefits to employees terminated or leaving their employ in certain other circumstances. Most of the Group's employees are covered by a defined contribution plan under Section 14 of the Israel Severance Pay Law.

The amount recorded as an employee benefit expense in respect of defined contribution plans for the years 2008, 2009 and 2010 was NIS 1,884,000, NIS 1,887,000, and NIS 1,982,000, respectively.

With respect to the remaining employees, the Group records a liability on its balance sheet for defined benefit plans that represents the present value of the defined benefit obligation as of balance sheet date, net of the fair value of plan assets, and adjustments for unrecognized actuarial gains or losses. The defined benefit obligation is computed annually by independent actuaries, using the corridor method. The present value of the defined benefit liability is determined by discounting the anticipated future cash outflows, using interest rates that are denominated in the currency in which the benefits will be payable.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged to income.

Past-service costs are recognized immediately in income, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In such cases, the past-service costs are amortized on a straight-line basis over the vesting period.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

s. Employee benefits (cont.)

2) Vacation days and recreation pay

Labor laws in Israel provide that every employee is entitled to vacation days and recreation pay, both of which are computed annually. The entitlement with respect to each employee is based on the employee's length of service with the Company. The Group recognizes a liability and an expense in respect of vacation and recreation pay based on the individual entitlement of each employee.

3) Share-based payments

The Group operates an equity-settled, share-based compensation plan, under which it receives services from employees as consideration for equity instruments (options) of the Group. The fair value of the employee services received in exchange for the grant of the options is recognized as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted:

- including any market performance conditions (for example, the Company's share price);
- excluding the impact of any service and non-market performance vesting conditions (for example, profitability, sales growth targets and the employee remaining with the entity over a specified time period); and
- excluding the impact of any non-vesting conditions.

Non-market vesting conditions are included in assumptions about the number of options that are expected to vest. The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting period, the Group revises its estimates of the number of options that are expected to vest based on the non-marketing vesting conditions. It recognizes the impact of the revision to original estimates, if any, in the income statement, with a corresponding adjustment to equity.

When the options are exercised, the Company issues new shares. The proceeds received, net of any directly attributable transaction costs, are credited to share capital (at par value) and share premium when the options are exercised.

t. Earnings (loss) per share

1) Basic

The basic earnings (loss) per share is calculated by dividing the earnings (loss) attributable to the holders of Ordinary Shares by the weighted average number of outstanding Ordinary Shares during the year.

2) Diluted

The diluted earnings (loss) per share is calculated by adjusting the weighted average number of outstanding Ordinary Shares, assuming conversion of all dilutive potential shares. The Company's dilutive potential shares consist of warrants and options granted to employees and service providers. The dilutive potential shares were not taken into account in computing loss per share in 2008 and 2009, as their effect would not have been dilutive.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

u. Changes in accounting policy and disclosures

1) New and amended standards adopted during 2010

The Group has adopted the following new and amended accounting standards as of January 1, 2010, which did not have a material effect on the financial statements of the Group:

a) IAS 27 (revised) requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control and these transactions will no longer result in goodwill or gains and losses. The standard also specifies the accounting when control is lost. Any remaining interest in the entity is re-measured to fair value, and a gain or loss is recognized in profit or loss. The Group did not carry out any transactions with non-controlling interests during 2010 and, accordingly, the initial adoption of IAS 27 (revised) did not have any impact on the Group's financial statements.

b) IFRS 3 (revised), "Business Combinations" is effective prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009. The revised standard continues to apply the acquisition method to business combinations but with some significant changes compared with IFRS 3. For example, all payments to purchase a business are recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently remeasured through the statement of comprehensive income. There is a choice on an acquisition-by-acquisition basis to measure the non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. All acquisition-related costs are expensed. The Group elected to adopt IFRS 3 (revised) on a prospective basis for all business combinations, effective January 1, 2010. The initial adoption of IFRS 3 (revised) did not have an effect on the Group's financial statements.

c) IAS 1 (amendment), "Presentation of Financial Statements," clarifies that the potential settlement of a liability by the issue of equity is not relevant to its classification as current or non-current. By amending the definition of current liability, the amendment permits a liability to be classified as non-current (provided that the entity has an unconditional right to defer settlement by transfer of cash or other assets for at least 12 months after the accounting period) notwithstanding the fact that the entity could be required by the counterparty to settle in shares at any time. The Group adopted IAS 1 (amendment) effective January 1, 2010. The initial adoption of IAS 1 (amendment) did not have an effect on the Group's financial statements.

NOTE 2 – SIGNIFICANT ACCOUNTING POLICIES (cont.)

u. Changes in accounting policy and disclosures (cont.)

1) New and amended standards adopted during 2010 (cont.)

d) IFRS 7 "Financial Instruments – Disclosures" (amendment), requires enhanced disclosures about fair value measurement and liquidity risk. In particular, the amendment requires disclosure of fair value measurements in accordance with a fair value measurement hierarchy. The amendment did not have a material impact on the Group's financial statements for the periods reported herein.

e) IAS 38 (amendment), "Intangible Assets," is part of the IASB's annual improvements project published in May 2008. The amendment provides that a prepayment may only be recognized in the event that payment has been made in advance of obtaining the right of access to goods or receipt of services.

The amendment also establishes that when re-measuring the book value of a debt instrument at termination of fair value hedge accounting, the effective interest calculated as of the date hedge accounting terminates should be used. The amendment did not have a material impact on the Group's financial statements for the periods reported herein.

2) Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Group, and which are not expected to have a material impact on the Group's financial statements

IAS 32 (amendment), "Classification of Rights Issues," was issued in October 2009. For rights issues offered for a fixed amount of foreign currency, current practice appears to require such issues to be accounted for as derivative liabilities. The amendment states that if such rights are issued pro rata to all existing shareholders of an entity in the same class for a fixed amount of currency, they should be classified as equity regardless of the currency in which the exercise price is denominated. The amendment will be effective for annual periods beginning on or after February 1, 2010, with early application permissible. The Group intends to apply this amendment in its financial statements beginning on January 1, 2011.

NOTE 3 – FINANCIAL RISK MANAGEMENT

According to estimates by the Group's management, the Group's exposure to credit risks as of December 31, 2010 is immaterial (see Note 3b). The activities of the Group expose the Group to market risks, particularly as a result of currency risks.

The Company's finance department is responsible for carrying out risk management activities in accordance with policies approved by the Company's Board of Directors. In this regard, the finance department identifies, defines and assesses financial risks in close cooperation with other Company departments. The Board of Directors provides written guidelines for overall risk management, as well as written policies dealing with specific areas, such as exchange rate risk, interest rate risk, credit risk, use of financial instruments, and investment of excess cash.

NOTE 3 – FINANCIAL RISK MANAGEMENT (cont.)

a. Market risks

1) Concentration of currency risks

The Group's activities are partly denominated in foreign currency, which exposes the Group to risks resulting from changes in exchange rates (primarily the dollar).

The effect of fluctuations in various exchange rates on the Group's income and equity is as follows:

	December 31, 2010				
	Income (loss)		Value on	Income (loss)	
Sensitive instrument	**10% increase**	**5% increase**	**balance sheet**	**5% decrease**	**10% decrease**
			NIS in thousands		
Dollar-linked balances:					
Cash and cash equivalents	7,339	3,670	73,394	(3,670)	(7,339)
Short-term bank deposits	2,804	1,402	28,037	(1,402)	(2,804)
Restricted deposits*	57	28	569	(28)	(57)
Other receivables	529	265	5,294	(265)	(529)
Trade payables	(179)	(90)	(1,792)	90	179
Payable to licensors	(149)	(75)	(1,491)	75	149
Total dollar-linked balances	10,401	5,200	104,011	(5,200)	(10,401)
Euro-linked trade payables	(41)	(20)	(406)	20	41
Total	10,360	5,180	103,605	(5,180)	(10,360)

* See also Note 12b(1).

The Group also maintains cash and cash equivalent balances that are linked to other currencies in amounts that are not material.

The Company believes that the likelihood of a fluctuation in exchange rates of up to 10% in the coming period is reasonable.

	December 31, 2009				
	Income (loss)		Value on	Income (loss)	
Sensitive instrument	**10% increase**	**5% increase**	**balance sheet**	**5% decrease**	**10% decrease**
			NIS in thousands		
Dollar-linked balances:					
Cash and cash equivalents	3,367	1,684	33,674	(1,684)	(3,367)
Restricted deposits*	60	30	604	(30)	(60)
Trade receivables	3,775	1,888	37,750	(1,888)	(3,775)
Trade payables	(299)	(149)	(2,987)	149	299
Payable to licensors	(1,057)	(528)	(10,570)	528	1,057
Total dollar-linked balances	5,846	2,925	58,471	(2,925)	(5,846)
Euro-linked balances:					
Cash and cash equivalents	155	77	1,550	(77)	(155)
Trade payables	(219)	(110)	(2,196)	110	219
	(64)	(33)	(646)	33	64
Trade payables linked to pound sterling	40	20	399	(20)	(40)
Total	5,882	2,912	58,224	(2,912)	(5,822)

* See also Note 12b(1).

NOTE 3 – FINANCIAL RISK MANAGEMENT (cont.)

a. Market risks (cont.)

1) Concentration of currency risks (cont.)

Set forth below is data regarding exchange rates and the CPI:

	Exchange rate of USD 1	Exchange rate of € 1	Exchange rate of £ 1	Israeli CPI*
	NIS	NIS	NIS	Points
As of December 31:				
2009	3.775	5.442	6.111	122.57
2010	3.549	4.738	5.493	125.83
Percentage increase (decrease) in:				
2009	(0.7)%	2.7 %	10.2%	3.9%
2010	(6.0)%	(12.9 %)	(10.1%)	2.7%

* Based on the index for the month ending on each balance sheet date, on the basis of 2000 average = 100.

Set forth below is information on the linkage of monetary items:

	December 31, 2009			December 31, 2010		
	Dollar	Other currencies	NIS	Dollar	Other currencies	NIS
	NIS in thousands					
Assets:						
Current assets:						
Cash and cash equivalents	33,674	1,949	70,267	73,394	320	38,032
Short term bank deposits	-	-	-	28,037	-	-
Other receivables	-	-	2,313	5,294	-	1,019
Trade receivables	37,750	-	-	-	-	-
Non-current assets:						
Restricted deposits	604	-	3,100	569	-	1,845
Total assets	72,028	1,949	75,680	107,294	320	40,896
Liabilities:						
Current liabilities:						
Current maturities of bank loan:	-	-	-	-	-	307
Accounts payable and accruals:						
Trade	2,987	2,221	1,244	1,792	515	1,542
OCS	-	-	14,005	-	-	5,993
Licensors	10,570	-	-	1,491	-	-
Other	-	-	10,203	-	-	6,775
Non-current liabilities:						
Long-term bank loan, net of current maturities	-	-	-	-	-	432
Total liabilities	13,557	2,221	25,452	3,283	515	15,049
Net asset value	58,471	(272)	50,228	104,011	(195)	25,847

NOTE 3 – FINANCIAL RISK MANAGEMENT (cont.)

a. Market risks (cont.)

2) Fair value of financial instruments

As of December 31, 2010, the financial instruments of the Group consist of non-derivative assets and liabilities (primarily working capital items and restricted deposits).

In view of their nature, the fair value of the financial instruments included in working capital is generally close or identical to their carrying amount. The fair value of the restricted cash in long-term deposits also approximates the carrying amount, as these financial instruments bear interest at a rate similar to the prevailing interest rate.

3) Exposure to market risks and the management thereof

The trade receivable balance as of December 31, 2009 relates to the transaction with Ikaria Holdings, Inc. ("Ikaria"), which, as described in Note 15, was collected in April 2010. The Company has also invested in deposits and short-term government bonds. Accordingly, in the opinion of the Company's management, the market risks to which the Company is exposed are primarily related to the exposure to currency risks, as mentioned above. Additionally, the Company's management does not consider the interest rate risk mentioned in paragraph 4 below to be material.

4) Interest rate risks

The Company's management does not consider interest rate risk to be material as the Company holds deposits and short-term government bonds whose fair value and/or cash flows are not materially affected by changes in the interest rate.

b. Credit risks

Credit risks are managed at the Group level. These risks relate to cash and cash equivalents, bank deposits and trade receivables.

The Group's cash and cash equivalents at December 31, 2009 and 2010 were mainly deposited with major Israeli banks. In the Company's opinion, the credit risk in respect of these balances is remote.

The Group considers its maximum exposure to credit risk to be as follows:

	December 31,	
	2009	2010
	NIS in thousands	
Assets:		
Cash and cash equivalents	105,890	111,746
Short term bank deposits	-	28,037
Trade accounts receivable	37,750	-
Other receivables	2,313	6,313
Restricted deposits	3,704	2,414
Total	149,657	148,510

NOTE 3 – FINANCIAL RISK MANAGEMENT (cont.)

c. Liquidity risks

The Company's management monitors rolling forecasts of the Group's liquidity reserves on the basis of anticipated cash flows and maintains the liquidity balances at a level that is sufficient to meet its needs.

As mentioned in Note 1, although the Company has succeeded in out-licensing two of its products, it cannot determine with reasonable certainty if and when it will become profitable on a current basis. Management of the Company believes that the Company's current cash balances will enable it to execute its operating plans through the end of 2012. Accordingly, in the event that the Company does not continue to generate cash from its operating activities, the Company's long-term operations in their current form are contingent on the Company's raising additional capital in the future.

d. Financial instruments

As of December 31, 2009 and 2010, the Group's financial instruments consisted solely of loans and receivables.

NOTE 4 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

As part of the financial reporting process, the Company's management is required to make certain assumptions and estimates that may affect the value of the assets, liabilities, income, expenses and some of the disclosures included in the Company's consolidated financial statements. By their very nature, such estimates are subjective and complex and consequently may differ from actual results.

The accounting estimates and assumptions that are used in the preparation of the financial statements are continually evaluated and are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

Described below are the critical accounting estimates that are used in the preparation of the financial statements, the formulation of which required the Company's management to make assumptions as to circumstances and events that involve significant uncertainty. In using its judgment to determine the accounting estimates, the Company takes into consideration, as appropriate, the relevant facts, past experience, the effect of external factors and reasonable assumptions under the circumstances.

a. Development expenses

Development expenses are capitalized in accordance with the accounting policy described in Note 2o. The capitalization of costs is based on management's judgment of technological and economic feasibility, which is usually achieved when a product development project reaches a predefined milestone, or when the Company enters into a transaction to sell the know-how that resulted from the development process. In determining the amount to be capitalized, management makes assumptions as to the future anticipated cash inflows from the assets, the discount rate and the anticipated period of future benefits. The Company's management has concluded that, as of December 31, 2010, the foregoing conditions have not been met and therefore development expenses have not been capitalized for any project.

If management had assessed that the aforementioned conditions had been met, the capitalization of development costs would have increased the Group's profit.

NOTE 4 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (cont.)

b. Grants/loans from the OCS

In accordance with the accounting treatment described in Note 2p, the Company's management is required to evaluate whether there is reasonable assurance that the grant/loan received will be paid or repaid. Additionally, whenever the grant/loan is initially recognized as income, management is required to evaluate whether the payment of royalties/repayment of loans to the OCS is considered more likely than not.

See Notes 12a(1) and 12a(2) with regard to the expected amount repayable to the OCS as of December 31, 2010.

c. Revenue recognition

In accordance with the accounting treatment described in Note 2p, the Company's management is required to evaluate whether it is probable that the economic benefits related to the out-licensing agreements with Ikaria and Cypress Bioscience will flow to the Group and whether it is possible to reliably measure the amount of the revenues relating to the transaction.

As of December 31, 2010, receipt of additional economic benefits associated with such transactions was not considered probable. Accordingly, no revenues with respect to additional milestone payments were recorded in the 2010 financial statements.

NOTE 5 – CASH, CASH EQUIVALENTS AND SHORT-TERM BANK DEPOSITS

a. Cash and cash equivalents

	December 31,	
	2009	2010
	NIS in thousands	
Cash on hand and in bank	700	1,642
Short-term bank deposits	105,190	110,104
	105,890	111,746

The short-term bank deposits included in cash and cash equivalents bear interest at annual rates of between 0.65% and 1.51%. The carrying amount of cash and cash equivalents is close or identical to their fair value, since they bear interest at rates similar to the prevailing market interest rates.

b. Short-term bank deposits

The short-term bank deposits are linked to the dollar and bear interest at annual rates of between 1.03% and 1.67%.

NOTE 6 – PROPERTY AND EQUIPMENT

Set forth below are the composition of property and equipment and the accumulated depreciation thereon, grouped by major classifications, and the changes therein for the respective years:

	Cost				Accumulated depreciation				Net book value December 31,	
	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	2007	2008
	NIS in thousands				NIS in thousands				NIS in thousands	
Composition in 2008										
Office furniture and equipment	446	250	-	696	76	35	-	111	370	585
Computers and communications equipment	1,137	314	-	1,451	705	292	-	997	432	454
Laboratory equipment, net*	1,654	1,346	-	3,000	459	374	-	833	1,195	2,167
Leasehold improvements	2,830	1,317	-	4,147	1,097	772	-	1,869	1,733	2,278
	6,067	3,227	-	9,294	2,337	1,473	-	3,810	3,730	5,484
* Item is net of OCS grants received - see b. below	(2,222)	(28)	-	(2,250)	478	334	-	812	(1,744)	(1,438)

	Cost				Accumulated depreciation				Net book value December 31,	
	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	2008	2009
	NIS in thousands				NIS in thousands				NIS in thousands	
Composition in 2009										
Office furniture and equipment	696	-	-	696	111	58	-	169	585	527
Computers and communications equipment	1,451	106	8	1,549	997	258	(4)	1,251	454	298
Laboratory equipment, net*	3,000	136	-	3,136	833	467	-	1,300	2,167	1,836
Leasehold improvements	4,147	-	-	4,147	1,869	764	-	2,633	2,278	1,514
	9,294	242	8	9,528	3,810	1,547	(4)	5,353	5,484	4,175
* Item is net of OCS grants received - see Note 12a(1)d	(2,250)	-	-	(2,250)	812	338	-	1,150	(1,438)	(1,100)

NOTE 6 – PROPERTY AND EQUIPMENT (cont.)

Set forth below are the composition of property and equipment and the accumulated depreciation thereon, grouped by major classifications, and the changes therein for the respective years (cont.):

	Cost				Accumulated depreciation				Net book value	
									December 31,	
	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	2009	2010
	NIS in thousands				NIS in thousands				NIS in thousands	
Composition in 2010										
Office furniture and equipment	696	28	-	724	169	42	-	211	527	513
Computers and communications equipment	1,549	372	(772)	1,1 49	1,251	234	(772)	713	298	436
Laboratory equipment, net*	3,136	1,510	-	4,646	1,300	611	-	1,911	1,836	2,735
Leasehold improvements	4,147	47	-	4,194	2,633	736	-	3,369	1,514	825
	9,528	1,957	(772)	10,713	5,353	1,623	(772)	6,204	4,175	4,509
* Item is net of OCS grants received - see Note 12a(1)d	(2,250)	-	-	(2,250)	1,150	338	-	1,488	(1,100)	(762)

NOTE 7 – INTANGIBLE ASSETS

	Cost				Accumulated depreciation and impairment				Net book value	
	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	December 31, 2007	December 31, 2008
	NIS in thousands				NIS in thousands				NIS in thousands	
Composition in 2008										
Intellectual property	1,568	1,856	-	3,424	-	-	603	603	1,568	2,821
Computer software	549	172	-	721	134	203	-	337	415	384
	2,117	2,028	-	4,145	134	203	603	940	1,983	3,205

	Cost				Accumulated depreciation				Net book value	
	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	December 31, 2008	December 31, 2009
	NIS in thousands				NIS in thousands				NIS in thousands	
Composition in 2009										
Intellectual property	3,424	589	(436)	3,577	603	-	148	751	2,821	2,826
Computer software	721	39	-	760	337	207	-	544	384	216
	4,145	628	(436)	4,337	940	207	148	1,295	3,205	3,042

	Cost				Accumulated depreciation				Net book value	
	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	Balance at beginning of year	Additions during year	Deletions during year	Balance at end of year	December 31, 2009	December 31, 2010
	NIS in thousands				NIS in thousands				NIS in thousands	
Composition in 2010										
Intellectual property	3,577	-	(1,846)	1,731	751	-	-	751	2,826	980
Computer software	760	347	-	1,107	544	191	-	735	216	372
	4,337	347	(1,846)	2,838	1,295	191	-	1,486	3,042	1,352

During 2009, intellectual property dispositions with a total cost of NIS 436,000 were recorded to cost of revenues in respect of the BL-1040 project (see Note 14). During 2010, the Group wrote-off intellectual property in the total amount of NIS 1,846,000 in respect of three projects that were terminated – BL-2030, BL-4060 and BL-5020.

Depreciation in respect of computer software and the amortization of intellectual property in 2010 were included in research and development expenses.

NOTE 8 – LONG-TERM BANK LOAN

a. Composition:

	December 31,	
	2009	2010
	NIS in thousands	
Loan balance	-	739
Less current maturities	-	(307)
	-	432

The loan is denominated in NIS, linked to the CPI and bears interest at an annual rate of 2.4%. The book value of the loan approximates its fair value.

The loan is repayable in 36 monthly installments.

b. Future repayments of long-term bank loans (other than current maturities) in the years subsequent to the balance sheet date are as follows:

2012	307
2013	125
	432

NOTE 9 – EQUITY

a. Share capital

As of December 31, 2009 and 2010, share capital is composed of Ordinary Shares, par value NIS 0.01 per share, as follows:

	Number of Ordinary Shares	
	December 31,	
	2009	2010
Authorized share capital	250,000,000	250,000,000
Issued share capital	123,497,029	123,558,660
Paid-up share capital	123,497,029	123,558,660

	In NIS	
	December 31,	
	2009	2010
Authorized share capital	2,500,000	2,500,000
Issued share capital	1,234,970	1,235,587
Paid-up share capital	1,234,970	1,235,587

The Ordinary Shares are traded on the Tel Aviv Stock Exchange. The price per Ordinary Share as of December 31, 2010 was NIS 3.21.

NOTE 9 – EQUITY (cont.)

b. Rights related to shares

The Ordinary Shares confer upon their holders voting and dividend rights and the right to receive assets of the Company upon its liquidation. As of December 31, 2010 and 2009, all outstanding share capital consisted of Ordinary Shares.

c. Changes in the Company's equity

1) In February 2007, the Company conducted an initial public offering on the TASE of 28,690,000 Ordinary Shares and 14,345,000 Series 1 warrants. The net proceeds to the Company from the issuance amounted to approximately NIS 198,000,000.

   Each Series 1 warrant was exercisable into one Ordinary Share at an exercise price of NIS 8.50 which, in accordance with the original terms of such warrants, was linked to the CPI (subject to adjustments). The warrants were exercisable over a period of two years from the date of their listing for trading. The consideration allocated to the warrants was approximately NIS 32,100,000, computed under the Black-Scholes model, which reflected their fair value as of the issuance date. Issuance costs related to the warrants of approximately NIS 2,100,000 were recorded as an expense. As of December 31, 2007, the warrants were marked to market on the Company's balance sheet (at the market price on the TASE), with the change in fair value of the warrants recorded to income (see also Note 2l). In July 2008, the exercise price of the warrants ceased to be linked to the CPI and, accordingly, the market value of the warrants at that time, amounting to NIS 947,000, was reclassified from current liabilities to equity.

   In February 2009, 380 warrants were exercised for total consideration of NIS 3,000, and the remaining 14,344,620 warrants expired.

2) In July 2009, the Company issued 46,667,719 Ordinary Shares in a public rights offering. The total net proceeds from the offering amounted to NIS 51,800,000, after deducting NIS 900,000 of issuance costs. The rights offering included an embedded benefit of 25% to the Company's shareholders (such embedded benefit being essentially a stock dividend for financial statement purposes).

3) In December 2009, the Company issued 11,293,419 Ordinary shares and 7,528,946 Series 2 warrants in a public offering. Each warrant is exercisable into one Ordinary Share at an exercise price of NIS 6.08 (not linked). The warrants are exercisable for a period of two years from the date that they were registered for trading.

   The total net proceeds from the offering amounted to NIS 45,700,000, after deducting NIS 1,400,000 in issuance costs. The issuance costs have been allocated between share premium and the warrants based on the relative market value (as indicated on the TASE) of the shares and warrants on the date of the offering.

NOTE 9 – EQUITY (cont.)

d. Share-based payments

1) In 2003, the Company's Board of Directors approved a stock compensation plan for employees and consultants pursuant to which 1,328,500 Ordinary Shares were reserved for issuance upon the exercise of options. In 2005, the Company's Board of Directors approved an expansion of the stock compensation plan for employees and consultants to allow the allotment of an additional up to 2,136,022 options exercisable into Ordinary Shares. In 2007, the Company's Board of Directors approved a grant to employees and consultants of 9,996,556 shares and options exercisable into Ordinary Shares.

In February and March 2010, the Company's Board of Directors approved the grant of 4,020,300 options to the Company's employees and members of the Scientific Advisory Board. Each option is exercisable into one Ordinary Share, par value NIS 0.01. The options vest as follows: 50% at the end of two years from the grant date; 25% at the end of three years from the grant date; and the remaining 25% at the end of four years from the grant date.

2) Employee stock options

The following table contains additional information concerning options granted to employees and directors under the existing stock-option plans:

	Year ended December 31,					
	2008		2009		2010	
	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)	Number of options	Weighted average exercise price (in NIS)
Outstanding at beginning of year	5,071,486	1.02	5,509,986	1.16	2,053,551	2.44
Granted	491,500	2.98	198,330	2.31	4,905,400	4.11
Forfeited	(53,000)	4.25	(658,137)	2.61	(443,873)	4.89
Exercised	-	-	(2,996,628)	0.04	(53,103)	0.46
Outstanding at end of year	5,509,986	1.16	2,053,551	2.44	6,461,975	3.56
Exercisable at end of year	2,972,124	0.67	689,946	2.92	1,120,270	1.69

The total consideration received from the exercise of stock options during 2009 and 2010 was NIS 116,000 and NIS 26,000, respectively.

The weighted average price of the Company's shares on the dates of exercise was NIS 2.42 and NIS 3.53 for 2009 and 2010, respectively.

NOTE 9 – EQUITY (cont.)

d. Share-based payments (cont.)

2) Employee stock options (cont.)

Set forth below is data regarding the range of exercise prices and weighted-average remaining contractual life (in years) for the options outstanding at the end of each of the years indicated.

As of December 31,	Number of options outstanding	Range of exercise prices (in NIS)	Weighted average remaining contractual life (in years)
2008	5,509,986	0.04 - 5.04	7.45
2009	2,053,551	0.04 - 5.04	6.56
2010	6,461,975	0.04 - 5.04	4.69

The Ordinary Shares allotted under these plans will confer the same rights as all other Ordinary Shares in the Company.

Employees of the Group have been granted options under Section 102 of the Israeli Income Tax Ordinance (the "Ordinance"). Non-employees of the Group (service providers, consultants, etc.), as well as controlling shareholders in the Company (as this term is defined in Section 32(9) of the Ordinance), have been granted options under Section 3(i) of the Ordinance.

The fair value of all options granted to employees through December 31, 2010 has been determined using the Black-Scholes option-pricing model. These values are based on the following assumptions as of the applicable grant dates:

	2008	2009	2010
Expected dividend yield	0%	0%	0%
Expected volatility *	70%	64%	66%
Risk-free interest rate	5%	5%	4%
Expected life of options (in years)	7	7	5

* Expected volatility has been computed on the basis of specific Company market data, as well as the data of similar companies operating in the same industry.

NOTE 9 – EQUITY (cont.)

d. Share-based payments (cont.)

3) Stock options to consultants

From inception through December 31, 2006, the Company issued to consultants options for the purchase of 220,990 Ordinary Shares at an average exercise price of USD 0.01 per share. In 2007, the Company changed the exercise price to NIS 0.039 per share. The options vest over four years

In 2007, the Group issued options to consultants for the purchase of 144,242 Ordinary Shares at an average exercise price of NIS 0.73 per share. The options vest over four years.

The above options may be exercised for a period of 10 years.

In 2010, the Group issued options to consultants for the purchase of 300,000 Ordinary Shares at an average exercise price of NIS 4.03 per share. The options vest over four years and may be exercised for a period of 5 years.

The Company's management estimates the fair value of the options granted to consultants based on the value of services received over the vesting period of the applicable options. The value of such services (primarily in respect of clinical advisory services) is estimated based on the additional cash compensation the Company would need to pay if such options were not granted. The value of services recorded in 2008, 2009 and 2010 amounted to NIS 437,000, NIS 640,000 and NIS 1,054,000, respectively.

4) See Note 15 regarding the option provided to Cypress Bioscience to pay up to half of the first milestone payment in consideration for the issuance of the Company's Ordinary Shares.

NOTE 10 – TAXES ON INCOME

a. Corporate taxation in Israel

Beginning with the 2008 tax year, the results of the Company and its Israeli subsidiaries for tax purposes are measured in nominal terms. Prior to 2008, results for tax purposes had been measured in real terms, taking into account changes in the CPI, pursuant to the Israeli Inflationary Adjustments Law, 1985.

The Partnership is not subject to tax under Israeli tax law; rather, each of the partners thereof (the Company and the Subsidiary) is liable for the tax applicable to the operations of the Partnership in proportion to their respective share in the Partnership's results.

b. Tax rates

The income of the Company and the Subsidiary is taxed at standard Israeli corporate tax rates. Israeli corporate tax rates for 2008 and thereafter are as follows: 2008 - 27%, 2009 - 26%, 2010 - 25%, 2011 - 24%, 2012 - 23%, 2013 - 22%, 2014 - 21%, 2015 - 20%, 2016 and thereafter - 18%.

Capital gains (except "real" capital gains on the sale of marketable securities, which are taxed at the standard corporate tax rates) are taxed as follows: capital gains derived after January 1, 2003 are subject to a tax rate of 25%, while capital gains derived until that date are taxed at the standard corporate tax rate.

NOTE 10 – TAXES ON INCOME (cont.)

c. Tax loss carryforwards

As of December 31, 2010, the tax loss carryforwards of the Company were approximately NIS 252,000,000 and the tax loss carryforwards of the Subsidiary were approximately NIS 1,000,000. The tax loss carryforwards of the Company have no expiration date.

The Company has not created deferred tax assets in respect of these tax loss carryforwards. See Note 2o.

d. Tax assessments

The Company and its subsidiaries have not been assessed for tax purposes since their respective incorporation or formation.

e. Theoretical taxes

As described in Note 2o, the Company has not recognized any deferred tax assets in the financial statements, since the Company does not expect to generate taxable income in the foreseeable future. The tax on the Group's profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the consolidated entities as follows:

	Year ended December 31,					
	2008		2009		2010	
		NIS in thousands		**NIS in thousands**		**NIS in thousands**
Income (loss) before taxes	27%	(114,849)	26%	(61,518)	25%	7,440
Theoretical tax expense (tax benefit)		(31,009)		(15,995)		1,860
Disallowed deductions (tax exempt income):						
Gain on adjusting warrants to fair value		(988)		-		-
Share-based compensation		2,439		852		1,639
Other		52		51		25
Difference between the measurement basis of income reported for tax purposes and the measurement basis of income for financial reporting purposes (see Note 9a)		(2,491)		(10)		-
Realization of tax loss carryforwards for which deferred taxes were not created		-		-		(3,652)
Increase in taxes for tax losses and timing differences incurred in the reporting year for which deferred taxes were not recognized		31,997		15,102		128
Taxes on income for the reported year		-		-		-

NOTE 10 – TAXES ON INCOME (cont.)

f. Deductible temporary differences

The amount of cumulative deductible temporary differences, other than unused tax loss carryforwards (as mentioned in c. above), for which deferred tax assets have not been recognized in the statement of financial position as of December 31, 2009 and 2010, were NIS 12,958,000 and NIS 13,086,000, respectively. These temporary differences have no expiration dates.

g. Value-added tax (VAT)

The Company is jointly registered for VAT purposes together with certain of its subsidiaries.

NOTE 11 – EARNINGS (LOSS) PER SHARE

a. The following table contains the data used in the computation of the basic earnings (loss) per share:

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Income (loss) as reported in financial statements	(114,849)	(61,518)	7,440
Income (loss) attributed to ordinary shares	(114,849)	(61,518)	7,440
Number of shares used in basic calculation (in thousands)	78,131	96,693	123,512
Adjustment for incremental dilutive shares from the theoretical exercise of options and warrants	-	-	1,035
Number of shares used in diluted calculation (in thousands)	-	-	124,547
	NIS		
Basic earnings (loss) per ordinary share*	(1.44)	(0.63)	0.06
Diluted earnings (loss) per ordinary share*	-	-	0.06

* The loss per share and the number of shares for the years 2008 and 2009 have been retroactively adjusted in order to give retroactive effect to the benefit embedded in the rights offering, as detailed in Note 9c(3). The embedded benefit, which is the equivalent of a stock dividend, in such rights offering was 25%.

Diluted loss per share data is not presented for 2008 and 2009, due to the antidilutive effect of the inclusion of potentially dilutive shares.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES

a. Commitments

1) Agreement with the State of Israel for the operation of a biotechnology incubator (the “Incubator”)

As part of the Incubator Agreement between the Partnership and the State of Israel, represented by the OCS (see principal provisions below), the State of Israel has agreed to grant loans to the Partnership to partially finance projects approved by the OCS.

The loans bear interest in accordance with the Interest and Linkage Law, 1961 (as of December 31, 2009 and 2010 – 1.70% and 1.40%, respectively), and are repayable at the discretion of the Partnership (but subject to the conditions described below concerning the sale of project assets or the realization of income from the project), as follows:

- In the three years of a project’s incubator stage, the loan is repayable, plus accrued interest.
- In the subsequent two years, the loan is repayable under the same terms, provided that the Incubator undertakes to maintain the advancement of the project at a rate similar to that of the preceding years.
- In the three following years, the loan is repayable with the addition of a double interest charge, provided that the Incubator undertakes to continue advancing the project at a rate similar to that of the preceding years.

If the Incubator sells assets or generates income from a project (including any intellectual property related thereto), at least 25% of the income from such sale must be used to repay the project loan, up to the original amount of the loan with the addition of interest as described herein. The Partnership is required to repay the loan in full upon the sale of a project’s intellectual property or the grant of an exclusive license to use the project’s intellectual property. The total payments to the State of Israel from such income will not exceed the original amount of the applicable loan with the addition of interest and linkage to the CPI. In certain circumstances, if the intellectual property or manufacturing rights are transferred outside of Israel, the repayment amounts may be greater.

Pursuant to the Incubator Agreement, the Incubator has undertaken to register a first-ranking pledge in favor of the OCS to cover the loans made to the Incubator. In accordance with the agreement, each pledge is specific to a loan for a specific project and includes a restriction on the transfer of, and/or licensing rights in, technologies that originate from the project, and on any equipment purchased for the use of the project. The Group has signed and submitted the pledge registration documents to the OCS.

The proceeds from the sale or use of a project-related intellectual property serve as the exclusive source for repayment of OCS loans financing such projects, and the sole collateral for the repayment of project loans are pledges on project-related intellectual property and assets purchased with loan proceeds.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. Commitments (cont.)

1) Agreement with the State of Israel for the operation of a biotechnology incubator (cont.)

In 2008, 2009 and 2010, the Group received NIS 9,240,000, NIS 6,338,000, and NIS 1,916,000, respectively, from the OCS, of which NIS 6,902,000, NIS 3,491,000, and NIS 842,000, respectively, were related to discontinued projects. The Company has agreed with the OCS on a procedure for the discontinuation of projects by the Incubator and the action that should be taken to forgive or repay loans received in respect of such discontinued projects.

The biotechnological incubators program is an initiative of the OCS that is designed to strengthen and promote the Israeli biotechnology industry, as well as biotechnology projects. This program was launched in late 2001, following publication of Directive No. 8.4 of the Director-General of Israel's Ministry of Industry, Trade and Labor ("Directive 8.4"). This directive implements the recommendations of the "Monitor" report, which reviewed ways to promote the Israeli biotechnology industry and recommended the establishment of for-profit incubators to support commercially viable projects by providing physical, organizational, professional, marketing and business infrastructure to promote research and development by early-stage biotechnology enterprises.

Directive 8.4 was amended in May 2004, to prescribe two tracks for operating biotech incubators (see (e) below). Immediately after the amendment of Directive 8.4, the OCS issued a call for proposals to establish and operate incubators. The Company, whose proposal was accepted by the OCS, entered into an agreement with the OCS, through the Partnership, for the operation of a designated biotechnology incubator. The principal provisions of the Incubator Agreement are as follows:

(a) Period of the agreement

The Incubator Agreement originally had a six-year period expiring on December 31, 2010. However, in accordance with an approval certificate that was received from the OCS, the Incubator Agreement was extended for two additional years, through 2012, and it was also agreed that the Group would be permitted to file a request for an additional one-year extension (through December 2013) prior to expiration of the first extension.

(b) Scope of Incubator operations

The Incubator is designed for the simultaneous operation of at least eight OCS-approved projects. The Group may operate additional projects within the Incubator's facilities that are not funded by the State or under the incubator program, provided that the operation of such additional projects does not interfere with OCS-approved projects.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. **Commitments** (cont.)

1) Agreement with the State of Israel for the operation of a biotechnology incubator (cont.)

(c) Summary of the Group's obligations

Within the framework of the Incubator Agreement, the Group has agreed to operate a biotechnology-designated incubator, to identify projects suitable for OCS approval, to make adequate premises and physical infrastructure available for at least eight projects and to provide administrative, organizational, professional and business support to the projects in order to facilitate research and development of commercially viable biotechnology projects. Among other things, some minimum requirements have been set for Incubator staff in terms of skills and employment levels. In addition, the Group has agreed to maintain a central laboratory for the use of all projects, equip the laboratory in accordance with the specifications provided in Directive 8.4 and in the Group's incubator proposal, and operate the Incubator using capable personnel. The Group is also required to make consulting and auditing services (accounting, legal, patent consulting, quality assurance, information science services, regulatory consulting and clinical trials) available to the projects at an acceptable scope and quality, from service providers approved by the OCS. The Group has undertaken to invest at least NIS 2,700,000 per year in the operation of the Incubator.

(d) Summary of OCS obligations

The OCS has undertaken to finance 50% of the cost of the equipment required for setting up the central laboratory and to make available State loans to each of the projects approved by the OCS at the rates of 85%, 80% and 75% of the project's approved budget in its first three years of operation, respectively, which are to be repaid to the State as described above. Each Incubator project is limited to a period of three years and a maximum budget of NIS 8,100,000, in respect of which the Group is responsible for obtaining the complementary financing (15% to 25%) for all three years, as described above.

In exchange for the services from the Incubator, the Group is entitled to receive participation by the OCS in operating expenses of up to 20% of the personnel costs associated with each project's approved budget, and may not collect additional payments in respect of the basket of services required by the OCS. The participation limit also applies to the operating expenses of the central laboratory, but does not apply to the costs of consumable materials.

(e) The different tracks

Directive 8.4 offers two tracks for the operation of an incubator. Under the first track, each project is incorporated as a separate and independent company in which the incubator receives shares (the separate companies will allocate at least 30% of their share capital to the holder of the license/knowhow, up to 5% of the share capital for incubator services, and the remaining shares will be allotted to the incubator and other investors in proportion to their investments in the independent company, including the incubator's investments derived from State loans).

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. **Commitments** (cont.)

1) Agreement with the State of Israel for the operation of a biotechnology incubator (cont.)

(e) The different tracks (cont.)

Under the second track, the projects are directly run within the incubator by the concessioner, with the holder of the license/know-how being entitled to a fixed amount for the use of his know-how as well as to royalties upon the sale of the knowhow and in respect of the sales of a final product developed under the project. An incubator operating under the second track is allowed to operate additional specific projects under the guidelines of the first track, subject to fulfillment of the provisions in the guidelines. The Group has elected to operate the Incubator under the second track.

(f) Primary restrictions imposed on the Group and the Incubator

The agreement stipulates certain restrictions regarding operation of the Incubator and the projects, including, among others: maximum ownership of 15% in the Incubator by university research institutions; a limitation of subcontracting to no more than 40% of the approved budget; ownership by the Group (or the project company under the first track) of the intellectual property created in the project (it should be noted that an exception to this rule was carved out in a recent amendment to the R&D law from January 2011 regarding academic institutions); a prohibition on duplicate grants and participation or duplicity of projects; compliance with guidelines on investment of funds; restrictions on the terms of the licensing agreements with the holders of the know-how, which mainly involves securing the rights of the OCS; compliance with the Israel R&D Law (the Encouragement of Research and Development in Industry Law) in terms of keeping in Israel the intellectual property and manufacturing rights relating to OCS-funded projects.

(g) Repayment of loans

Repayment of State loans is restricted to a project’s own resources out of the proceeds received from the sale or licensing of a project (at least 25% of the proceeds). The sale or licensing of the technology is subject to payment of the aforementioned royalties, up to the amount of the loans received from the State for such project.

The State is entitled to foreclose on the collateral related to a given project to secure repayment of the related loan at the end of eight years from the date of project approval, or even earlier, in the event of a breach of the Incubator Agreement by the Group, liquidation, and other events as set forth in the agreement.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. **Commitments** (cont.)

1) Agreement with the State of Israel for the operation of a biotechnology incubator (cont.)

(h) Security

The Group has provided a bank guarantee to the OCS in the amount of NIS 8,100,000 to secure its liabilities under the Incubator Agreement. After two years from the initial date of the Incubator Agreement, the amount of the guarantee is reduced every year by half the amount of the Incubator's reported approved expenses, subject to a minimum guarantee of NIS 1,500,000 (see Note 12b). Additionally, the rights in the various projects are pledged to the State to secure repayment of the loan out of project proceeds. With respect to incubators operating under the second track, a floating charge is placed on all intellectual property and all equipment purchased in connection with a project, including a restriction on the transfer or licensing of the technology created in the project. The collateral discussed in this paragraph may be forfeited even after the repayment period or upon breach of the Incubator Agreement.

(i) To the best knowledge of the Company's management, as of the date of approval of these financial statements, the Group is in compliance with its material obligations to the OCS under the Incubator Agreement.

With respect to the accounting treatment of State loans, see Note 2r.

2) Obligation to pay royalties to the Government of Israel

The Company is required to pay royalties to the Government of Israel, computed on the basis of proceeds from the sale or license of products whose development was supported by Government grants.

This obligation relates solely to the Government's financial participation in the development of products by the Company outside the framework of the Incubator operated by the Partnership.

In accordance with the terms of the financial participation, the Government is entitled to royalties on the sale or license of any product whose development was supported with Government participation. These royalties are 3% in the first three years from initial repayment, 4% of sales in the three subsequent years and 5% of sales in the seventh year until repayment of 100% of the grants (linked to the USD) received by the Company plus annual interest at the LIBOR rate. As of December 31, 2010, the maximum amount of royalties payable by the Company to the Government of Israel is NIS 3,000,000.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. Commitments (cont.)

3) Licensing agreements

From time to time, the Group enters into in-licensing agreements with academic institutions, research institutions and companies in connection with development of certain technologies (the "licensors").

The objective of each engagement with a licensor is to obtain rights for one or more drugs in the preliminary stages of development by the licensors, to continue joint development of the drugs by the Group and the licensors until advanced stages of development and, consequently, to manufacture, distribute and market the drugs or to out-license the development, manufacture and commercialization rights to third parties. Such post-development activities are carried out by either the Group and/or by companies or institutions to which the Group has entered into an out-license agreement, subject to certain restrictions stipulated in the various agreements.

The licenses that have been granted to the Group are broad and comprehensive, and generally include various provisions and usage rights, as follows: (i) territorial scope of the license (global); (ii) term of the license (unrestricted but not shorter than the life of the patent); and (iii) development of the therapeutic compound (allowing the Group to perform all development activities on its own, or by outsourcing under Group supervision, as well as out-licensing development under the license to other companies, subject to the provisions of the licensing agreements).

According to the provisions of the licensing agreements, the intellectual property rights in the development of any licensed technology remain with the licensor until the date the applicable license agreement is effective, while the rights in products and/or other deliverables developed by the Group after the license is granted belong to the Group. In cases where the licensor has a claim to an invention that was jointly developed with the Group, the licensor also co-owns the related intellectual property. In any event, the scope of the license also covers these rights.

In addition, the Group generally undertakes in the licensing agreements to protect registered patents resulting from developments under the various licenses, to promote the registration of developments in cooperation with the licensor, and to bear responsibility for all related costs. Pursuant to the various agreements, the Group will work to register the various patents worldwide, and if the Group decides not to initiate or continue a patent registration proceeding in a given country, the Group is required to notify the applicable licensor to this effect and the licensor will be entitled to take action for registration of the patent in such country.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. Commitments (cont.)

3) Licensing agreements (cont.)

The consideration paid pursuant to the licensing agreements includes several components that are payable over the license period and that relate, inter alia, to the progress made in research and development activities, as well as commercial success, as follows: (a) one-time payment of up to USD 200,000 and/or periodic payments of up to USD 30,000 per year; (b) royalties on amounts the Group receives from an out-licensing transaction that range from 20% to 29.5% of net consideration; (c) payments through the early stages of development (i.e. through the end of phase 2) of up to USD 150,000; (d) payments of up to USD 2,000,000 upon the achievement of milestones necessary for advancing to phase 3; (e) payments of up to USD 5,000,000 from the end of a successful phase 3 trial through approval of the therapeutic compound; and (f) royalties on sales of the final product resulting from development under the license or including any component thereof, ranging between 3%-5% of the Group’s net sales of the product.

A license agreement may be cancelled, generally upon the occurrence of one of the following events: (a) the Group’s failure to meet certain milestones stipulated in the applicable license agreement and appended timetables; (b) default, insolvency, receivership, liquidation, etc., of the Group that is not imposed and/or lifted within the timeframe stipulated in the license agreement; and (c) fundamental breach of the license agreement that is not corrected within the stipulated timeframe. In addition, some of the agreements may be cancelled with prior notice of 30 to 90 days, due to unsuccessful development or any other cause.

The Group has undertaken to indemnify the various licensors, their employees, officers, representatives or anyone acting on their behalf for any damage and/or expense that they may incur in connection with the Group’s use of a license granted to it, all in accordance with the terms stipulated in the applicable license agreements.

Some of the license agreements are accompanied by consulting, support and cooperation agreements, pursuant to which the Group is committed to pay the various licensers a fixed monthly amount, over the period stipulated in the agreement, for their assistance in the continued research and development under the license.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

a. Commitments (cont.)

4) Lease agreements

a) The Company has entered into an operating lease agreement in connection with the lease of its premises. The agreement expires on December 15, 2012. The Group has an option to extend the lease agreement for two additional periods of 24 months each. The annual lease fees are linked to the dollar and amount to approximately NIS 921,000. As to bank deposits pledged to secure the Company's liability under the lease agreement, see Note 12b(1).

b) The Company has entered into operating lease agreements in connection with a number of vehicles. The lease periods are generally for three years. The annual lease fees, linked to the dollar, are approximately NIS 1,816,000. To secure the terms of the lease agreements, the Group has made certain prepayments to the leasing companies, representing approximately two months of lease payments. These amounts were recorded as prepaid expenses. See also Note 14b.

5) Early Development Program ("EDP") agreement

In January 2007, the Company entered into an agreement with Pan Atlantic for the funding of an early development program (the "EDP Agreement"). According to the EDP Agreement, Pan Atlantic undertook to provide grants for the promotion of drug-development projects in the preliminary stages of research in an aggregate amount of up to USD 5,000,000, in semi-annual "calls" of up to USD 625,000 each, through April 2011. In parallel, for every dollar of EDP project funding provided by Pan Atlantic, the Company committed to provide twenty cents of funding (i.e., a funding ratio of 5:1). Pan Atlantic undertakings under the EDP agreement are not subject to Pan Atlantic being a lender to, or a shareholder of, the Company.

In consideration for the EDP funding commitment, the Company granted to Pan Atlantic the right to participate in a future initial public offering of the Company outside of Israel, at the public offering price, in an amount of up to USD 5,000,000.

During 2008, 2009 and 2010, Pan Atlantic provided funding to the Group of NIS 2,876,000, NIS 4,881,000 and NIS 3,877,000, respectively, under the EDP Agreement. The amounts recognized as a reduction of research and development expenses in 2008, 2009 and 2010 were NIS 2,525,000, NIS 3,297,000 and NIS 2,997,000, respectively.

NOTE 12 – COMMITMENTS AND CONTINGENT LIABILITIES (cont.)

b. Contingent liabilities

Guarantees and liens:

1) As part of the Group's obligations under the Incubator Agreement and to secure the Group's liabilities to the OCS, the Company has provided a NIS 8,100,000 bank guarantee (linked to the CPI) in favor of Israel's Ministry of Finance.

The guarantee is valid through March 2011. According to the Incubator Agreement, after the two year anniversary of the initial date of the Incubator Agreement, the amount of the guarantee will be reduced every year by half of the amount of the Incubator's reported approved expenses. As of December 31, 2010, the balance of the guarantee amounted to approximately NIS 1,500,000.

To secure the above guarantee, the Group has pledged to a bank a short-term deposit in the amount of NIS 1,800,000, which is presented under non-current assets.

2) To secure the Company's liability to the lessor of its premises, the Group has pledged several dollar-denominated bank deposits in the amount of USD 160,000 (NIS 569,000), which are presented under non-current assets.

NOTE 13 – TRANSACTIONS AND BALANCES WITH RELATED PARTIES

Transactions with related parties

Expenses (income):

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Participation in EDP project funding (see below)	(2,525)	(3,297)	(2,997)
Benefits to related parties:			
Compensation and benefits to senior management, including benefit component of option grants	10,561	7,039	8,208
Number of individuals to which this benefit related	5	6	5
Compensation and benefits to directors, including benefit component of option grants	1,074	584	858
Number of individuals to which this benefit related	3	3	3

This amount relates to a grant received from a related party of the Company, in accordance with the EDP Agreement as detailed in Note 12a(5).

NOTE 13 – TRANSACTIONS AND BALANCES WITH RELATED PARTIES (cont.)

Key management compensation

Key management includes directors (executive and non-executive), executive officers and the internal auditor. The compensation paid or payable to key management for services during each of the years indicated is presented below.

	Year ended December 31,		
	2008	2009	2010
	NIS in thousands		
Salaries and other short-term employee benefits	4,084	5,115	5,609
Post-employment benefits	365	320	343
Other long-term benefits	42	36	42
Share-based compensation	7,144	2,152	3,072
	11,635	7,623	9,066

NOTE 14 – SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION

a. Other receivables

	December 31,	
	2009	2010
	NIS in thousands	
Withholding tax*	-	5,294
Institutions	1,991	649
Grants receivable from the OCS	322	370
	2,313	6,313

* See Note 15.

b. Long-term prepaid expenses

The prepaid expenses relate to operating lease agreements in respect of the vehicles used by the Group, and, in 2009, materials utilized by the Company to produce the BL-1040 compound amounting to NIS 880,000. During 2010, after an assessment of the Group regarding the realizable value of the materials, they were written off to R&D expenses.

NOTE 14 – SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (cont.)

c. Accounts payable and accruals

	December 31,	
	2009	**2010**
	NIS in thousands	
1) Trade:		
Accounts payable:		
In Israel	1,224	1,539
Overseas	5,208	2,307
Checks payable	20	3
	6,452	3,849
2) Other:		
Payroll and related expenses	1,318	1,496
Accrual for vacation and recreation pay	881	1,092
Accrued expenses	4,924	4,176
Grants on account of EDP project development financing not yet recognized in income	2,896	3,776
Other	184	11
	10,203	10,551

The carrying amount of accounts payable and accruals is close or identical to their fair value, as the effect of discounting is not material.

NOTE 14 – SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (cont.)

d. Cost of revenues

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Payments to licensors*	-	17,817	25,571
Payment to the OCS*	-	4,369	-
Intellectual property dispositions	-	436	-
	-	22,622	25,571

* See Notes 15 and 16

e. Research and development expenses – net

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Payroll and related expenses, including vehicles	21,161	16,384	18,566
Depreciation and amortization	2,180	1,633	1,705
Impairment of intellectual property	-	148	1,846
Patent related expenses	3,841	2,907	1,770
Research and development services	95,665	66,534	16,265
Professional fees	594	1,113	1,999
Materials	1,693	248	301
Overseas travel	2,231	471	215
Office supplies and telephone	2,699	2,661	2,682
Payments to the OCS (see Notes 15, 16)	-	8,739	17,438
Other	1,691	187	360
	131,755	101,025	63,147
Less – OCS participations in research and development costs - see also Notes 12a(1) and (2)	(23,074)	(7,426)	(5,184)
Less – participations in research and development costs by a related party - see Note 13	(2,525)	(3,297)	(2,997)
	106,156	90,302	54,966

NOTE 14 – SUPPLEMENTARY FINANCIAL STATEMENT INFORMATION (cont.)

f. Sales and marketing expenses

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Payroll and related expenses	-	1,396	2,090
Marketing	-	1,400	2,258
Overseas travel	-	289	261
	-	3,085	4,609

g. General and administrative expenses

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Payroll and related expenses, including vehicles	7,863	6,792	6,205
Professional fees	3,707	2,499	6,540
Office supplies and telephone	170	121	111
Office maintenance	100	117	69
Depreciation	99	121	109
Other	1,144	1,532	1,841
	13,083	11,182	14,875

h. Finance income

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Gain on change in fair value of financial assets at fair value through profit or loss	273	98	-
Income from interest and exchange differences on deposits	12,728	3,830	3,056
	13,001	3,928	3,056

i. Finance expenses

	Year ended December 31,		
	2008	**2009**	**2010**
	NIS in thousands		
Exchange differences	12,172	2,064	8,696
Bank commissions	97	100	59
	12,269	2,164	8,755

NOTE 15 – IKARIA AGREEMENT

During the third quarter of 2009, the Group entered into an out-licensing agreement with Ikaria, pursuant to which the Company granted Ikaria an exclusive, worldwide license to develop, manufacture and commercialize BL-1040 – a compound for the treatment of patients that have suffered an acute myocardial infarction (“AMI”). The agreement was signed in July 2009 and the transaction closed in September 2009, following receipt by the Company of OCS approval for the transaction, and transfer by the Company to Ikaria of all deliverables as stipulated under the agreement.

In accordance with the agreement, Ikaria is obligated to use commercially reasonable efforts to complete clinical development of and to commercialize BL-1040, and will bear all subsequent costs involved in the continued development of the product, the conduct and funding of its commercialization, and the prosecution and maintenance of patents.

Prior to execution of the agreement, the Company commenced a pilot phase 1/2 study designed to assess the safety and preliminary efficacy of BL-1040. According to the agreement, the Company was required to bear the costs related to completion of the study from that stage. Such costs, related to follow up and documentation of results, were accrued in 2009.

Total payments to the Company under the agreement (not including royalties) are up to USD 282,500,000, subject to the achievement of certain milestones. Upon the closing of the agreement, the Company became entitled to the first payment in the amount of USD 7,000,000, which was received in October 2009. In connection with this payment, the Company undertook to indemnify Ikaria for any obligations it may have had to withhold taxes on such payment. In April 2010, the first milestone payment of USD 10,000,000 was received, in respect of which withholding tax of 15% was deducted. In March 2011, the Company filed an income tax return to request a refund of the tax withheld. Approximately 50% of the remaining payments are subject to certain development and regulatory milestones and the rest are subject to commercialization milestones. The abovementioned first two payments were recognized as revenues in 2009, and future milestone payments will be recognized as revenues if and when their receipt will become probable and their amount can be reliably measured.

The Company is also entitled to royalties on the net sales of any product developed under the agreement, ranging from 11% to 15%, depending on annual net sales levels.

The out-licensing agreement with Ikaria terminates on the date that the last patent rights in respect of BL-1040 are still valid (through at least 2024).

The Group is required to pay to the licensors of the BL-1040 compound 28% of all consideration received under the agreement. This expense is recorded in the statement of comprehensive income (loss) as cost of revenues. Additionally, the Group is obligated to repay the grants and loans received from the OCS regarding the BL-1040 project, in accordance with the Israeli R&D Law and as agreed with the OCS. This expense, up to the amount of funding received from the OCS, has been recorded in the statement of comprehensive (income) loss in research and development expenses, with the balance recorded in cost of revenues.

NOTE 16 – CYPRESS AGREEMENT

In June 2010, the Group entered into an exclusive, royalty-bearing out-licensing agreement with Cypress Bioscience for United States, Canada and Mexico (the "territories"), with regard to BL-1020, a therapeutic candidate for the treatment of schizophrenia. Under the agreement, Cypress Bioscience is obligated to use commercially reasonable efforts to develop, obtain regulatory approval for, and to commercialize BL-1020 in the territories, and will bear all subsequent costs involved in the continued development of the product, the conduct and funding of its commercialization, and the prosecution and maintenance of patents in the territories. The agreement became effective in August 2010, upon receipt of the consent of the OCS.

The total potential payments from the agreement to the Group, not including royalties, are up to USD 365,000,000, as follows: (1) USD 30,000,000 which was paid to the Group in August 2010 upon closing of the agreement; (2) up to USD 250,000,000 in connection with the achievement of certain performance-based milestones; and (3) up to USD 85,000,000 upon the achievement of certain sales-based milestones.

With regard to the first performance-based milestone of USD 10,000,000, Cypress Bioscience is entitled to pay up to one-half of the amount as an investment in the Company's Ordinary Shares. In management's estimation, based on a valuation received from an independent economic consulting firm, the fair value of this derivative instrument is not material and, therefore, it has not been deducted from the revenues recognized in respect of the upfront payment.

In addition to the above payments, the Group is also entitled under the agreement to royalties ranging from 12% to 18% of net sales of BL-1020 in the territories.

The Group retained the rights to BL-1020 for the rest of the world outside of the territories. In addition, pursuant to the agreement, the Group has the right to use all preclinical, clinical and other similar data generated by or on behalf of Cypress Bioscience, including its regulatory filings, subject to future reimbursement of 50% of expenses (as defined) incurred by Cypress Bioscience in generating such data and other information.

The Group is required to pay 22.5% of all consideration received under the agreement to the licensors of BL-1020. As a result, USD 6,750,000 was charged to cost of revenues during the period in respect of the USD 30,000,000 upfront payment.

In addition, the Group is obligated to repay grants received from the OCS regarding the BL-1020 project, in accordance with the Israeli R&D Law and as agreed with the OCS. In this regard, during the year, the Group recorded a liability to the OCS for the full amount of the grants received in respect of the project, in the total amount of NIS 17,438,000. This amount has been reflected in research and development expenses in these financial statements. The Group paid NIS 11,445,000 of this liability to the OCS in August 2010, leaving a remaining balance of NIS 5,993,000, reflected in current liabilities as of December 31, 2010.

In January 2011, Cypress Bioscience was acquired by the Royalty Pharma Group.

NOTE 17 –EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

a. In January 2011, the Group announced its intention to transfer its business development activities to Israel from the US.

b. In February 2011, the Company granted 15,000 options to an employee, exercisable into Ordinary Shares at an exercise price of NIS 2.873 per share. The options vest over a four-year period.

c. (Unaudited) In May 2011, the Company signed an agreement, effective June 1, 2011, to reacquire all development and commercialization rights to BL-1020 granted to Cypress Bioscience pursuant to the license agreement signed in June 2010 (see Note 16), as well as terminate the license agreement. In consideration for the reacquisition of such rights, including substantially all materials required for timely commencement of the BL-1020 clinical trial expected to commence in June 2011, the Company is obligated to pay Cypress Bioscience a 1% royalty on worldwide net sales of BL-1020 up to an aggregate cumulative amount of USD 80,000,000. In addition, the Company is obligated to pay Cypress Bioscience 10% of all future one-time payments received in respect of BL-1020, not to exceed an aggregate cumulative amount of USD 10,000,000, as reimbursement for costs that Cypress Bioscience incurred in developing the intellectual property portfolio, designing the clinical trial and conducting substantially all preparations to launch the trial.