Aktionärsbrief
Halbjahresabschluss 2016

Sehr geehrte Aktionärinnen und Aktionäre von LifeWatch,

LifeWatch Highlights im 1. Semester

- *Umsatzwachstum von 8.6% auf USD 57.0 Millionen*
- *Halbjahresergebnisse durch verschiedene Einmalkosten negativ belastet*
- *Verlust vor Zinsen, Steuern und Abschreibungen von USD -3.0 Millionen gegenüber einem EBITDA von USD 7.2 Millionen im 1. Halbjahr 2015*
- *Adjustierter EBITDA von USD 6.6 Millionen im 1. Halbjahr 2016*
- *Nettoverlust von USD -9.8 Millionen gegenüber Reingewinn von USD 1.9 Millionen im 1. Halbjahr 2015*

Zusammenfassung

LifeWatch AG setzte das Umsatzwachstum im ersten Halbjahr 2016 weiter fort. Der Gesamtumsatz für die ersten sechs Monate betrug USD 57 Millionen, entsprechend einem Wachstum von 8.6% im Vergleich zur Vorjahresperiode. Das Geschäft mit Überwachungsdienstleistungen in den USA legte im ersten Semester im Vergleich zur Vorjahresperiode um 10% zu.

Das Umsatzwachstum im ersten Quartal 2016 hatte 12.3% betragen, schwächte sich im 2. Quartal im Vergleich zur Vorjahresperiode aber auf 5% ab. Dies ist teilweise auf einen Auftragsrückstand und eine Stornierung eines Geräteverkaufs zurückzuführen. Obwohl im Moment kein Rückstand besteht, dürfte dies während mehrerer Monate einen dämpfenden Einfluss auf den Absatz haben, was bedeutet, dass der Umsatz im 2. Halbjahr tiefer als vorgängig angenommen ausfallen dürfte. Dennoch geht das Management davon aus, dass sich dank des umfassenden Produkt- und Dienstleistungsangebots der Gesellschaft das Wachstum im weiteren Jahresverlauf beschleunigen wird.

Die Bruttomarge des ersten Halbjahres betrug 49.1% im Vergleich zu 52.8% in der Vorjahresperiode. Der Margenrückgang ist auf die Abschreibung von kapitalisierten Softwareentwicklungskosten, die Abschreibung von Lagerbeständen des Vital Signs Patch (VSP)-Projekts sowie andere obsolete Bestände zurückzuführen. Ohne diese Einmalabschreibungen hätte die Bruttomarge 55.5% betragen.

Während den ersten sechs Monaten des Geschäftsjahres unterzeichnete unsere US-Tochtergesellschaft LifeWatch Services Inc. 30 neue oder verbesserte Serviceverträge für unser Mobile Cardiac Telemetry (MCT)-Geschäft und 35 neue oderverbesserte Verträge für unsere Überwachungsdienstleistung für INR (Blutgerinnungszeit). Diese neuen Dienstleistungsverträge zeugen von der Stärke der Marke LifeWatch.

In Bezug auf den Ausblick erwartet das Management aufgrund der Abschwächung des Wachstums im 2. Quartal für das Gesamtjahr ein Umsatzwachstum im einstelligen Bereich. Für das Geschäftsjahr 2016 wird ein positiver EBITDA erwartet, aber aufgrund der in 2016 bereits verbuchten ausserordentlichen Kosten erwarten wir, dass das Betriebsergebnis (EBIT) und das Nettoergebnis negativ bleiben werden.

Bedeutende Einmalkosten belasten Profitabilität

Die Forschungs- und Entwicklungsausgaben (F&E) erhöhten sich im 1. Halbjahr 2016 auf 4.7% vom Umsatz (H1 2015: 3.8%). Ohne Kapitalisierung von Softwareentwicklungskosten würden die F&E-Ausgaben allerdings 5.8% des Umsatzes betragen (H1 2015: 5.7%). Verkaufs- und Marketingausgaben erhöhten sich im 1. Semester 2016 auf 19.5% vom Umsatz (H1 2015: 18.0%). Der Anstieg ist auf höhere Verkaufskommissionen im Vergleich zu 2015 zurückzuführen. Die allgemeinen Administrationskosten (G&A) wurden von zwei Einmalfaktoren negativ belastet (siehe untenstehende Tabelle), welche zum Anstieg auf USD 5.5 Millionen führten. Somit beliefen sich die G&A-Ausgaben im 1. Halbjahr 2016 auf 31.7% vom Umsatz (H1 2015: 23.8%).

Andere Erhöhungen in den G&A-Ausgaben betreffen Kosten im Zusammenhang mit einem Bonusplan für alle Mitarbeitenden, höhere Lohnkosten, Anwerbegebühren für verschiedene neue Kadermitarbeiter, ein neues

Design für die Webseite, Kosten für FDA-Berater, die Aufrüstung der weltweiten Interkonnektivität und die Umsetzung eines neuen Disaster Recovery Systems.

Die Rückstellung für die Mittel zum Vergleich der Qui Tam Klage sobald die erwarteten behördlichen Zustimmungen vorliegen sowie die Reduktion in der Einigung mit Highmark sind, zusammen mit einer Rückerstattung im Pharmalife-Rechtsfall und der Einigung in einem Mitarbeiterdisput wegen Entlassung, unter anderen Kosten verbucht und stellen Einmalkosten für die Einigung in Rechtsfällen im 1. Semester dar.

Als Folge dieser Einmalposten verzeichnete LifeWatch im ersten Halbjahr 2016 einen Betriebsverlust (EBIT) von USD -7.63 Millionen (H1 2015: USD 3.81 Millionen) und einen Verlust vor Zinsen, Steuern und Abschreibungen (EBITDA) von USD -3.0 Millionen (H1 2015: USD 7.2 Millionen). Nach Abzug der Finanzierungskosten, Steuern und dem anteiligen Verlust am Aufbau der Tätigkeiten in der Türkei resultierte ein Nettoverlust von USD -9.8 Millionen (H1 2015: Reingewinn von USD 1.9 Millionen).

Trotz dieser negativen Entwicklungen erwirtschaftete die Gesellschaft in den ersten sechs Monaten 2016 einen positiven Cash-Flow aus Geschäftstätigkeit von USD 0.9 Millionen im Vergleich zu USD 4.2 Millionen im 1. Semester 2015.

Als Ergebnis des bedeutenden Nettoverlustes sank die Eigenkapitalquote per 30. Juni 2016 auf 20.8%, dies im Vergleich zu 32.5% per Ende Dezember 2015 und 54.3% per 30. Juni 2015. Die Kapitalerhöhung, welche am 22. Juli 2016 abgeschlossen wurde, sowie die erwartete Verbesserung der Ergebnisse im 2. Halbjahr werden zu einer deutlichen Verbesserung der Eigenkapitalquote führen.

Die untenstehende Tabelle zeigt die adjustierten EBIT- und EBITDA-Zahlen:

Einmalposten *(in USD Millionen)*:	
Vital Signs Patch Entwicklung / Inventar	-3.612
Qui Tam Einigung	-12.975
Reduktion der Highmark Einigung	8.973
Pharmalife-Rückerstattung nach Gegenrechnung Einigung in Mitarbeiterdisput	0.248
Honorare im Zusammenhang mit Rechtsfällen	-0.964
Automatisierung der Berechnung von Forderungsausfällen	-1.247
Total	**-9.577**
Adjustierter EBIT	1.952
Adjustierte EBIT-Marge	3.4%
Adjustierter EBITDA	6.620
Adjustierte EBITDA-Marge	11.6%

Laufende Entwicklungen und Marktaktivitäten

Wie bereits angekündigt beabsichtigt die Gesellschaft, ein reiner Dienstleistungsanbieter zu werden. Die Software-Entwicklung wird weiter in-house betrieben, aber die Hardware-Entwicklung wird eingestellt. Die Gesellschaft geht davon aus, dass in Zukunft die Geräte entweder von einem Drittanbieter zugekauft oder auf Auftragsbasis von einer Drittpartei entwickelt werden. Die Anpassung der Strategie beinhalten gewisse Umstrukturierungen unserer Forschungs- und Entwicklungsaktivitäten in Israel, welche in der zweiten Jahreshälfte umgesetzt werden.

Die Geschäftsleitung beobachtet die Situation nach den kürzlich erfolgten politischen Entwicklungen in der Türkei derzeit genau, ist aber immer noch der Meinung, dass eine kontrollierte Markteinführung unseres Herzüberwachungsgeschäftes bis zum Jahresende erfolgen kann. Eine volle Lancierung könnte 2017 erfolgen. Die Gesellschaft investierte im 1. Halbjahr 2016 ungefähr USD 1 Million in die Bereitstellung der Infrastruktur, inklusive die Anstellung von Personal und den Erhalt der in der Türkei notwendigen Bewilligungen. Die Geschäftsleitung erwartet, dass zusätzliche Mittel in der 2. Jahreshälfte benötigt werden.

Andere interne Projekte, welche die Verbesserung der Kundenorientierung und Effizienzsteigerungen zum Ziel haben, sollten in der zweiten Jahreshälfte 2016 ebenfalls Früchte tragen.

Kapitalerhöhung

Die Gesellschaft schloss die Kapitalerhöhung mit der Ausgabe von 4'994'019 neuen Namenaktien zum Ausgabepreis von CHF 9.00 pro Aktie am 22. Juli 2016 ab, wodurch der Gesellschaft Nettoeinnahmen von rund CHF 43.7 Millionen zuflossen. Die Gesellschaft hat bis jetzt USD 16 Millionen dieses Mittelzuflusses genutzt, um die Einigung im Highmark Rechtsfall zu begleichen (USD 13 Millionen) und die Kreditlinie bei der Bank Leumi zurückzuzahlen (USD 3 Millionen).

Ausblick

LifeWatch revidiert die in der Medienmitteilung vom 6. Juli 2016 prognostizierten Vorgaben für das Gesamtjahr. Während wir weiterhin davon ausgehen, eine positive EBITDA-Marge im einstelligen Bereich erzielen zu können sowie ein negatives Betriebsergebnis EBIT und einen Nettoverlust zu verzeichnen, erwarten wir nun aufgrund des im 2. Quartal verlangsamten Wachstums der Absatzerlöse ein Umsatzwachstum im einstelligen Bereich.

Obwohl das erste Halbjahr 2016 enttäuschend verlief, ist die Geschäftsleitung überzeugt, mit der Einigung in den zwei älteren Rechtsfällen die wesentlichsten übriggebliebenen Probleme der Vergangenheit endlich gelöst zu haben, sodass sich die Gesellschaft nun vollständig auf das zukünftige Wachstum des Geschäftes konzentrieren kann.

Mit der Markteinführung des neuen Mobile Cardiac Telemetry (MCT) 1-Kanal Pflasters, dem anstehenden Abschluss verschiedener interner Entwicklungsprojekte und dem geplanten Eintritt in den türkischen Markt hat die Gesellschaft die Basis für zukünftiges Wachstum gelegt. Deren Auswirkungen sollten sich in 2017 und darüber hinaus materialisieren.

Im Namen des Verwaltungsrats und der Geschäftsleitung danken wir allen unseren Mitarbeitenden für ihren Einsatz und ihr Engagement zur Gestaltung der Zukunft von LifeWatch. Wir danken auch unseren Geschäftspartnern sowie unseren Patienten für ihre Loyalität und das Vertrauen. Und nicht zuletzt danken wir Ihnen, geschätzte Aktionärinnen und Aktionäre, für Ihr Vertrauen und insbesondere Ihre Unterstützung, welche in der Zeichnung von 83% des Bezugsrechtsangebots im Rahmen der kürzlich erfolgten Kapitalerhörung zum Ausdruck kamen.

Freundliche Grüsse,

Dr. Robert Bider
Präsident des Verwaltungsrats

Dr. Stephan Rietiker
Chief Executive Officer

Im Zweifelsfall gilt der englische Bericht zum Halbjahresabschluss.

FINANZÜBERSICHT

Kennzahlen (nicht testiert, USD Millionen):

	H1 2016	**H1 2015**
Umsatz	57.02	52.51
Bruttogewinn	28.01	27.75
in % des Umsatzes	*49.1%*	*52.8%*
EBITDA / (LBITDA)	(2.96)	7.23
in % des Umsatzes	*NA*	*13.8%*
EBIT / (LBIT)	(7.63)	3.81
in % des Umsatzes	*NA*	*7.3%*
Nettogewinn (Verlust)	(9.80)	1.94
in % des Umsatzes	*NA*	*3.7%*
Gewinn (Verlust) pro Aktie	(0.73)	0.14
Total Anlagevermögen, netto	16.58	16.22
Bilanzsumme	76.32	71.94
Total Eigenkapital	15.90	39.04
in % der Bilanzsumme	20.8%	54.3%
Cash Flow, netto	(3.90)	0.02
Mitarbeitende	631	612

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Valor-Nr.:	1281545
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Weitere Information finden sich auf unserer Website: www.lifewatch.com

LIFEWATCH AG

CONDENSED CONSOLIDATED FINANCIAL STATEMENTS FOR JUNE 30, 2016

(UNAUDITED)

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CONDENSED CONSOLIDATED INTERIM BALANCE SHEET

USD thousands	**June 30, 2016**	June 30, 2015	December 31, 2015
	Unaudited	Unaudited	Audited
Assets			
Current assets:			
Cash and cash equivalents	**3,497**	**7,108**	7,400
Restricted bank deposit	**-**	**790**	-
Accounts receivable (trade & other), net	**14,865**	**13,857**	13,275
Deferred income taxes	**13,105**	**8,518**	13,142
Marketable securities and structures	**52**	**-**	-
Inventories	**1,044**	**2,487**	1,750
Total current assets	**32,563**	**32,760**	**35,567**
Other non-current assets:			
Marketable securities and structures	**-**	**52**	52
Deferred income taxes	**6,002**	**4,684**	6,018
Loan to associate company	**1,416**	**-**	-
Other investments and non-current receivables (trade and others)	**895**	**884**	895
Total non-current assets	**8,313**	**5,620**	**6,965**
Property plant and equipment, net	**16,580**	**16,224**	**16,348**
Goodwill, intangible and other assets, net	**18,861**	**17,335**	**20,440**
Total assets	**76,317**	**71,939**	**79,320**

USD thousands	June 30, 2016	June 30, 2015	December 31, 2015
	Unaudited	Unaudited	Audited
Liabilities and stockholders' equity			
Current liabilities:			
Current portion of long-term loans and other liabilities	10,056	4,828	6,508
Accounts payable and accruals (trade and other)	23,997	19,261	21,419
Provision for settlement	23,225	3,221	22,284
Total current liabilities	57,278	27,310	**50,211**
Non-current liabilities:			
Loans and other liabilities, net of current maturities	1,441	1,874	1,616
Accrued severance and other employee benefits	832	326	776
Obligation to associate company	-	-	155
Provision for settlement	-	2,838	-
Accrued expenses	880	555	797
Total non-current liabilities	3,153	5,593	**3,344**
Total liabilities	60,431	32,903	**53,555**
Shareholders' equity:			
Share capital, warrants, treasury shares, capital surplus and accumulated other comprehensive income (loss)	149,528	148,992	149,611
Accumulated deficit	(123,846)	(111,898)	(111,898)
Net (loss) income for the period	(9,796)	1,942	(11,948)
Total shareholders' equity	15,886	39,036	**25,765**
Total liabilities & shareholders' equity	76,317	71,939	**79,320**

Condensed Consolidated Interim Statements of Operations

	6 months ending June 30,	
USD thousands (except share and per share data)	**2016 Unaudited**	**2015 Unaudited**
Revenues	**57,015**	**52,512**
Cost of revenues	29,006	24,765
Gross profit	**28,009**	**27,747**
Research and development expenses	2,706	1,982
Selling and marketing expenses	11,119	9,453
General and administrative expenses	18,055	12,500
Legal settlements and other expenses, net	3,754	-
Total operating expenses	**35,634**	**23,935**
(Loss) income from operation	**(7,625)**	**3,812**
Financial and other expenses, net	(722)	(443)
(Loss) income before taxes	**(8,347)**	**3,369**
Tax expense	(503)	(1,427)
Share in losses of associated company	(946)	-
(Loss) income for the period	**(9,796)**	**1,942**

WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING USED IN COMPUTATION OF (LOSS) EARNINGS PER SHARE (IN THOUSANDS)		
Basic	13,468	13,404
Diluted	13,468	13,417
(LOSS) EARNINGS PER SHARE (USD)		
Basic	(0.73)	0.14
Diluted	(0.73)	0.14

Condensed Consolidated Interim statements of comprehensive Income (Loss)

Net (loss) income	**(9,796)**	**1,942**
Other comprehensive income:		
Actuary income from pension fund	32	-
Total other comprehensive income	32	-
Comprehensive (loss) income	**(9,764)**	**1,942**

CONDENSED CONSOLIDATED INTERIM STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

USD thousands	Paid-in share capital including premium	Accumulated deficit	Capital reserve	Treasury Shares	Accumu-lated other comprehen-sive loss	Total
BALANCE AT JANUARY 1, 2016 (AUDITED)	**150,422**	**(123,846)**	**70**	**(116)**	**(765)**	**25,765**
Changes During The Six Months Ended June 30, 2016 (Unaudited):						
Net loss for the period		(9,796)				**(9,796)**
Stock-based compensation for board members	(182)					**(182)**
Other comprehensive income					32	**32**
Treasure shares	7			18		**25**
Issuance of shares in respect of exercise of options granted to employees	42					**42**
BALANCE AT JUNE 30, 2016 (UNAUDITED)	**150,289**	**(133,642)**	**70**	**(98)**	**(733)**	**15,886**
BALANCE AT JANUARY 1, 2015 (AUDITED)	**149,518**	**(111,898)**	**70**	**(370)**	**(437)**	**36,883**
Changes During The Six Months Ended June 30, 2015 (Unaudited):						
Net income for the period	-	1,942	-	-	-	**1,942**
Issuance of shares in respect of exercise of options granted to employees	211	-	-	-	-	**211**
BALANCE AT JUNE 30, 2015 (UNAUDITED)	**149,729**	**(109,956)**	**70**	**(370)**	**(437)**	**39,036**

CONDENSED CONSOLIDATED INTERIM STATEMENT OF CASH FLOW

	6 months ending June 30,	
USD thousands	**2016 Unaudited**	**2015 Unaudited**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) income for the period	(9,796)	1,942
Adjustments required to reconcile (loss) income for the period to net cash provided by operating activities:		
Income and expenses not involving cash flows:		
Share in affiliate loses	946	-
Write-off of other assets	2,393	-
Depreciation and amortization	4,668	3,422
Change in deferred income tax, net	53	1,413
Stock-based compensation for board members	189	-
Changes in operating assets and liabilities:		
(Increase) in accounts receivable, including non-current portion	(1,590)	(1,518)
Decrease (increase) in inventories	706	(514)
Increase (decrease) in accounts payable and accruals:		
Provision for settlement	941	(2,040)
Trade and others	2,379	1,483
Net cash provided by operating activities	**889**	**4,188**
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of fixed assets	(1,569)	(4,721)
Investment in and loans to associated company	(2,518)	-
Investment in intangible assets	(1,043)	(1,006)
Restricted bank deposit	-	(10)
Net cash used in investing activities	**(5,130)**	**(5,737)**
CASH FLOWS FROM FINANCING ACTIVITIES:		
Issuance of shares in respect of exercise of employee stock options	42	211
Proceeds from sale of treasury shares	25	-
Obligation under capital lease undertaken, net	(3,263)	(1,141)
Short term credit from bank and others	3,534	2,500
Net cash provided by financing activities	**338**	**1,570**
(Decrease) increase in cash and cash equivalents	**(3,903)**	**21**
Balance of cash and cash equivalents at beginning of period	7,400	7,087
Balance of cash and cash equivalents at end of period	**3,497**	**7,108**

SUPPLEMENTARY DISCLOSURE OF NON-CASH ACTIVITIES		
Capital leases of fixed assets	**3,102**	**-**

NOTES TO CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

NOTE 1

Basis of presentation

The condensed consolidated interim financial statements of LifeWatch AG ("LifeWatch") and its subsidiaries (together the "Company") have been prepared in accordance with accounting principles generally accepted in the United States of America ("US GAAP") for interim financial information and accordingly do not include all information and disclosures as required by US GAAP for complete financial statements. The year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by US GAAP. Please refer to the consolidated financial statements as of December 31, 2015, as included in the Annual Report 2015, for further information. The financial statements are presented in United States Dollars ($ or USD). As per June 30, 2016 and for the period then ended, the primary statements are disclosed in USD thousands. The comparative prior year figures are disclosed accordingly. The par value of capital stock is denominated in Swiss francs (CHF).

In the opinion of management, these condensed consolidated interim financial statements reflect all adjustments necessary, which are of a normal recurring nature, to fairly state the condensed consolidated balance sheets, condensed consolidated statements of operations, condensed consolidated statements of comprehensive income (loss), condensed consolidated changes in shareholders' equity and cash flows for the interim periods presented.

NOTE 2

Liquidity

As of June 30, 2016 the Company has recorded a liability of approximately $23.2 million as a result of the settlement of legal cases, see notes 7 and 8. This total liability affects the future liquidity of the Company. Furthermore, upon the Company's announcement of the material adverse ruling for one of the cases, the Company received a Notice of Default from one of its primary commercial lenders.

In order to satisfy the liability of the legal cases and sustain the Company's operations and meet its business objectives, the Company obtained shareholder approval for an ordinary capital increase of up to 5,000,000 shares at its Annual General Meeting, held on April 15, 2016. This ordinary capital increase (rights issue) was successfully completed on July 22nd, 2016 with 83% of existing investors subscribing for their shares. The Company received net proceeds of CHF 43.7 million.

As of June 30, 2016, the Company had cash reserves of approximately $3.5 million and an outstanding line of credit balance of $6.0 million. One of the Company's credit lines is currently restricted to $3.0 million and is fully drawn whereas the other credit line of $6.0 million, of which $3 million is drawn, is unrestricted.

NOTE 3

Property plan and equipment

a. Composition of assets, grouped by major classifications, is as follows:

USD thousands	June 30, 2016	June 30, 2015	December 31, 2015
	Unaudited	Unaudited	Audited
Cost			
Manufacturing and peripheral equipment	12,725	12,291	13,175
Office furniture and equipment	3,281	3,027	3,136
Monitoring units	29,230	26,577	27,237
Motor vehicles	17	17	17
Leasehold improvements	1,710	1,537	1,600
Total costs	**46,963**	**43,449**	**45,165**
Less – accumulated depreciation and amortization	**30,383**	**27,225**	**28,817**
Total	**16,580**	**16,224**	**16,348**

b. Depreciation expenses in respect of fixed assets totaled USD 4,440 thousand USD 3,419 thousand and USD 8,005 thousand for the six months ended June 30, 2016, June 30, 2015, and for the twelve months ended December 31, 2015, respectively.

NOTE 4

Accrued pension benefits

The Company maintains retirement savings plans for its employees as required by law at each of its locations. With the exception of Switzerland these plans are defined contribution plans and as such no obligation exists for the Company over and above the contributions which are made during the year concerned. In Switzerland the plan qualifies as a defined benefit plan. The pension plan provides benefits upon retirement based upon the amount held in the fund at retirement.

The net periodic benefit cost for the Swiss pension plan for the six months ending June 30, 2016 and 2015 are as follows:

	Defined Benefit Pension Plan	
	June 30	
	2016	2015
	Unaudited	
	U.S. dollars in thousands	
Net periodic benefit cost		
Service cost	200	208
Interest cost	19	12
Expected return on plan assets	(35)	(22)
Actuarial loss recognized in current year	49	15
Prior service cost recognized in current year	(12)	10
Net periodic benefit cost	**221**	**223**

In accordance with ASC 715, the initial net liability was recorded in Accumulated Other Comprehensive Income and is being amortized in equal installments over the expected remaining service life of employees, which is approximately 9.7 years as of June 30, 2016. The amortized amount for the period ended June 30, 2016 is $32 thousand.

NOTE 5

Income taxes

a. Deferred income taxes

Deferred income taxes are determined by the asset and liability method based on the estimated future tax effects of differences between the financial accounting and tax basis of assets and liabilities under the applicable tax law. Deferred tax balances are computed using the tax rates expected to be in effect when these differences reverse.

Deferred tax assets and liabilities are classified as current or noncurrent based on the classification of the related assets or liabilities for financial reporting or, if not related to an asset or liability for financial reporting, according to the expected reversal dates of the specific temporary differences.

NOTE 5

Income taxes (*continued)*

b. Income tax uncertainties

The determination of the Company's tax liabilities involves dealing with uncertainties in the application of complex tax regulations. The Company recognizes liabilities for uncertain tax positions based on the two-step process prescribed by applicable accounting principles. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step requires the Company to estimate and measure the tax benefit as the largest amount that is more than 50% likely of being realized upon ultimate settlement. It is inherently difficult and subjective to estimate such amounts, as this requires the Company to determine the probability of various possible outcomes. The Company reevaluates these uncertain tax positions. This evaluation is based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, effectively settled issues under audit, and new audit activity. Such a change in recognition or measurement could result in the recognition of a tax benefit or an additional charge to the tax provision in the period.

c. Carry forward tax losses

The Company and the Israeli subsidiary have carryforward losses as of June 30, 2016 and estimate that both entities will not utilize the deferred taxes related to those carryforward losses in the future and have recorded full valuation allowances for each entity.

The US subsidiaries have carryforward tax losses, as of June 30, 2016 and 2015 in the amounts of approximately $40.1 million and $41.2 million, respectively that may be used to offset future taxable income. These carryforward losses expire between 2023 and 2035. No valuation allowance was recorded in respect of deferred tax assets related to these carryforward tax losses as of June 30, 2016.

NOTE 6

Segment and geographic information

The Company's reportable segments consist of:

- Sales of Systems - Development, manufacture and marketing of trans-telephonic and wireless diagnostic equipment for the medical industry.
- Patient Services - Cardiac monitoring services of MCT, Event, Holter, INR, Pacemaker and sleep disorder services.
- Other - Company activities and expenses that are not assigned directly to either of the above segments.

The table below presents information about reported segments:

USD thousands	Sales of Systems	Patient Services	Other	Reconciling Items	Consolidated total
For the 6 months ended June 30, 2016 (Unaudited):					
Revenues from external customers	(587)	57,602	-	-	57,015
Inter-segments revenues	3,878	-	-	(3,878)	-
Total	**3,291**	**57,602**	**-**	**(3,878)**	**57,015**
Operating (loss) income	(8,116)	1,590	(2,965)	1,866	(7,625)
Depreciation and amortization	532	9,478	30	(5,372)	4,668
Goodwill	-	15,859	-	-	15,859
Capital investments	246	7,851	47	(3,473)	4,671
Total assets	**101,016**	**105,334**	**4,651**	**(134,684)**	**76,317**
For the 6 months ended June 30, 2015 (Unaudited):					
Revenues from external customers	165	52,347	-	-	52,512
Inter-segments revenues	8,270	-	-	(8,270)	-
Total	**8,435**	**52,347**	**-**	**(8,270)**	**52,512**
Operating income (loss)	4,018	4,583	(3,125)	(1,664)	3,812
Depreciation and amortization	255	9,044	18	(5,895)	3,422
Goodwill	-	14,976	-	-	14,976
Capital investments	393	11,682	11	(7,365)	4,721
Total assets	**106,338**	**83,611**	**2,385**	**(120,395)**	**71,939**

NOTE 6

Segment and geographic information (*continued)*

Following are data regarding revenues and long-lived assets classified by geographical location of the customers:

USD thousands	Revenues	Long-lived assets
For the six months ended June 30, 2016 (Unaudited)		
United States and Canada	57,603	15,034
Europe	-	376
Asia	(595)	-
Other	7	1,170
Total	**57,015**	**16,580**
For the six months ended June 30, 2015 (Unaudited)		
United States and Canada	52,347	14,756
Europe	11	254
Asia	154	-
Other	-	1,214
Total	**52,512**	**16,224**

NOTE 7

Material contingencies and credit agreements

a. In March 2016, an arbitrator from the International Centre for Dispute Resolution issued a material adverse decision against the Company, relating to its dispute with Highmark over billing and payment practices. The arbitrator found the Company liable for damages for the years 2009 – 2010 in the approximate amount of $18.7 million plus six percent per annum simple pre-judgement interest from January 2013. This amount will be reduced by approximately $0.7 million in offsets which have been previously taken. The liability was reflected in the Company's 2015 annual report. For subsequent events relating to this award see Note 8a.

A Qui Tam ("Whistleblower") action filed under seal in 2013 was unsealed and served upon the Company at the end of 2014. The case contained allegations related to billing processes for clinical services provided off shore. In June 2016, the Company announced a preliminary settlement in the case. The parties recently signed a Memorandum of Understanding that would require the Company to pay a total of $12.75 million to the US Government and the Whistleblower, and are awaiting approval of the proposed settlement from the Department of Justice.

In 2014, the Company released its former CFO for cause. In 2015, the former executive filed an action with the Israeli labor court claiming wrongful termination and demanded his notice pay as well as other damages amounting to approximately $250 thousand. The matter was settled for $125 thousand in the labor court on May 31, 2016 and will be paid in the second half of the year.

As of June 30, 2016 and 2015, the total amount of provisions for repayments was $23,225 thousand and $6,059 thousand, respectively.

NOTE 7

Material contingencies and credit agreements *(continued)*

b. Line of Credit agreement update

On February 1, 2016, the Company entered into an amended and restated line and security agreement with a US based financial institution. The restated agreement increases the maximum borrowings under the line of credit to $7.0 million and extends the maturity date to February 2, 2017. This agreement is in default as of March 15, 2016 and frozen with an outstanding balance of $3 million as detailed in Company's 2015 annual report. The line of credit agreement was repaid and canceled in August 2016.

c. Credit Facility agreement

On January 16, 2016, the Company entered into a $6.0 million Credit Facility with a Switzerland based financial institution, which is intended to be used for and finance general corporate activities. The interest rate for all advances that are drawn by the Company is determined by the bank and paid quarterly. The Credit Facility is collateralized with a $6.6 million First Demand Guarantee by the Company, and expires on June 30, 2017.

This credit facility was suspended as of March 31, 2016. In May 2016, the amount available was reduced to $3.0 million. The Credit Facility was fully reinstated in June 2016 and as of June 30, 2016, $3.0 million was drawn.

d. Vital Connect agreement

The Company exercised its option to terminate the license and supply agreement with Vital Connect as of June 30, 2016, because technical issues prevented the first commercial use of the solution within the foreseen time period. Vital Connect has communicated with the Company by letter and has reserved the right to take action for damages related to loss of sales of USD 9.6 million, which they believe they have suffered. The Company is of the opinion that the Vital Connects claim is unfounded.

NOTE 8

Subsequent events

a. Legal Settlements

On June 1, 2016, the Company announced that it had reached an agreement with the private health insurer to reduce its $18.7 million plus six percent per annum simple pre-judgement interest from January 2013 award to $13.0 million. In return, the Company agreed to release the private health insurer and its affiliates from the antitrust case the Company has pending against them. The settlement agreement is conditional upon payment being made by August 15, 2016 at the latest. The settlement was paid in July 2016.

b. Capital Increase update

In April 2016, the Company announced shareholder approval to raise additional capital through the issuance of a maximum of 5.0 million ordinary shares of CHF 1.30 par value. This ordinary capital increase (rights issue) was successfully completed on July 22nd, 2016 with 83% of existing investors subscribing for their shares. The Company received CHF 43.7 million net of costs.