

FORMULA SYSTEMS (1985) LTD
Form 20-F/A
February 01, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20-F/A

Amendment No. 1

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

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
^x1934
For the fiscal year ended December 31, 2016**

OR

**..TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934
For the transition period from _____ to _____**

OR

**..SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934
Date of event requiring this shell company report _____**

Commission File Number: 000-29442

FORMULA SYSTEMS (1985) LTD.

(Exact Name of Registrant as Specified in Its Charter and translation of Registrant's name into English)

Israel

(Jurisdiction of Incorporation or Organization)

5 Haplada Street, Or Yehuda 60218, Israel

(Address of Principal Executive Offices)

Asaf Berenstin; 5 Haplada Street, Or Yehuda 60218, Israel

Tel: 972 3 5389487, Fax: 972 3 5389645

(Name, Telephone, E-mail and/or Facsimile Number and Address of Company Contact Person)

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

<u>Title of Each Class</u>	<u>Name of Each Exchange On Which Registered</u>
American Depositary Shares, each representing one Ordinary Share, NIS 1 par value	NASDAQ Global Select Market

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

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

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

As of December 31, 2016, the registrant had 14,728,782 outstanding ordinary shares, NIS 1 par value, of which 197,485 were represented by American Depositary Shares.

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

Yes No

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

Yes No

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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Large accelerated filer Accelerated filer
Non-accelerated filer Emerging Growth Company

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards[†] provided pursuant to Section 13(a) of the Exchange Act.

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

U.S. GAAP International Financial Reporting Standards as issued by the International Accounting Standards Board Other

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

Item 17 Item 18

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

Yes No

EXPLANATORY NOTE

This Amendment No. 1, or the Amendment, to the Annual Report on Form 20-F for the year ended December 31, 2016, or the Annual Report, filed on May 16, 2017 with the Securities and Exchange Commission, or the SEC, is being filed by Formula Systems (1985) Ltd., or the Company, to amend the Annual Report for the sole purposes of:

Adding to our financial statements included under Item 18 of this Amendment, in accordance with Rule 2-05 of Regulation S-X, the report of the auditor of a subsidiary of the Company upon which our principal auditor relied, (i) and to which our principal auditor referred, in rendering its audit report on our consolidated financial statements that were included in the Annual Report. The subject audit report had been inadvertently omitted from the Annual Report.

Adding, in accordance with Item 17(c) of Form 20-F, an explicit statement in the notes to our consolidated (ii) financial statements and in our principal auditor's report (which are included in Item 18 of this Amendment), that our financial statements comply with IFRS as issued by the IASB.

In keeping with the SEC requirements related to this Amendment, it consists solely of (i) the entirety of Item 18 of Form 20-F, along with (ii) Exhibits 12.1 and 12.2, which constitute the required certifications of our principal executive officer and principal financial officer pursuant to Rule 13a-14(a)/Rule 15d-14(a) under the Securities Exchange Act of 1934, as amended, or the Exchange Act, and (iii) Exhibits 13.1 and 13.2, which consist of the certifications of our principal executive officer and principal financial officer pursuant to Rule 13a-14(b)/Rule 15d-14(b) under the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Other than as expressly set forth above, this Amendment does not, and does not purport to, amend, update or restate the information in any other item of the Annual Report, or reflect any events that have occurred after the Annual Report was originally filed.

ITEM 18. FINANCIAL STATEMENTS

Our consolidated financial statements and the report of our independent registered public accounting firm in connection therewith are filed as part of this Amendment to the Annual Report, as noted on the pages below:

<u>Reports of independent registered public accounting firm</u>	F-2 - F-4
<u>Consolidated statements of financial position</u>	F-5 - F-6
<u>Consolidated statements of profit or loss</u>	F-7
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ITEM 19. EXHIBITS

Exhibit

<u>No.</u>	
<u>1.1</u>	Memorandum of Association ⁽¹⁾
<u>1.2</u>	<u>Amended and Restated Articles of Association, as adopted by Formula Systems (1985) Ltd. on January 8, 2012</u> ⁽²⁾
<u>2.1</u>	Depository Agreement by and among Formula Systems (1985) Ltd., Bank of New York Mellon and the holders of the American Depository Shares of Formula Systems (1985) Ltd. ⁽¹⁾
<u>4.1</u>	<u>Form of Letter of Indemnification for officers and directors, adopted by Formula Systems (1985) Ltd. on January 8, 2012</u> ⁽³⁾
<u>4.2</u>	<u>English translation of Formula Systems (1985) Ltd. Employees and Office Holders Share Option Plan (2008)</u> ⁽⁴⁾
<u>4.3</u>	<u>Formula Systems (1985) Ltd. 2011 Share Incentive Plan and amendment</u> ⁽⁵⁾
<u>4.4</u>	<u>Formula Systems (1985) Ltd. Compensation Policy</u> ⁽⁶⁾
<u>8</u>	<u>List of Subsidiaries</u> †
<u>12.1</u>	<u>Certification of the Chief Executive Officer pursuant to Rule 13a-14(a)/Rule 15d-14(a) under the Exchange Act</u> *
<u>12.2</u>	<u>Certification of the Chief Financial Officer pursuant to Rule 13a-14(a)/Rule 15d-14(a) under the Exchange Act</u> *
<u>13.1</u>	<u>Certification of the Chief Executive Officer pursuant to Rule 13a-14(b)/Rule 15d-14(b) under the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> *
<u>13.2</u>	<u>Certification of the Chief Financial Officer pursuant to Rule 13a-14(b)/Rule 15d-14(b) under the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> *

- 15.1** Consent of Kost, Forer, Gabbay & Kaiserer, a member of Ernst & Young Global+
15.2 Consent of KDA Audit Corporation+

+ Filed with the original filing of the Annual Report.

* Filed herewith.

- (1) Incorporated by reference to the Registration Statement on Form F-1 (File No. 333-8858) filed with respect to the registrant's American Depositary Shares.
- (2) Incorporated by reference to Exhibit 99.1 to the report on Form 6-K filed by the registrant with the Securities and Exchange Commission on January 18, 2012.
- (3) Incorporated by reference to Exhibit 99.2 to the report on Form 6-K filed by the registrant with the Securities and Exchange Commission on January 18, 2012.
- (4) Incorporated by reference to the annual report on Form 20-F for the 2008 fiscal year filed by the registrant with the Securities and Exchange Commission on April 27, 2009.
- (5) Incorporated by reference to the annual report on Form 20-F for the 2013 fiscal year filed by the registrant with the Securities and Exchange Commission on April 30, 2014.
- (6) Incorporated by reference to Appendix A to Exhibit 99.2 to the report on Form 6-K filed by the registrant with the Securities and Exchange Commission on November 16, 2016.

SIGNATURES

The registrant hereby certifies that it meets all of the requirements for filing on Form 20-F and that it has duly caused and authorized the undersigned to sign this Amendment No. 1 to the annual report on its behalf.

FORMULA SYSTEMS (1985) LTD.

By: /s/Asaf Berenstin February 1, 2018
Asaf Berenstin Date
Chief Financial Officer

FORMULA SYSTEMS (1985) LTD. AND ITS SUBSIDIARIES

CONSOLIDATED FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2016

U.S. DOLLARS IN THOUSANDS

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Kost Forer Gabbay & Kasierer

3 Aminadav St.
Tel-Aviv 6706703, Israel

Tel: +972-3-6232525
Fax: +972-3-5622555
ey.com

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of

FORMULA SYSTEMS (1985) LTD.

We have audited the accompanying consolidated statement of financial position of Formula Systems (1985) Ltd. and its subsidiaries (the "Company") as of January 1, 2015, December 31, 2015 and 2016 and the related consolidated statements of profit or loss, comprehensive income, changes in equity and cash flows for each of the two years in the period ended December 31, 2016. These consolidated financial statements are the responsibility of the Company's board of directors and management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the financial statements of a subsidiary, which statements reflect total assets of 0.5%, 0.4% and 0.3% as of January 1, 2015, December 31, 2015 and 2016, respectively, and total revenues of 1% for the years ended December 31, 2015 and 2016, respectively, of the related consolidated totals. The financial statements of this subsidiary were audited by other auditor whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included in respect of this subsidiary, is based solely on the reports of the other auditor.

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

In our opinion, based on our audit and the report of the other auditor, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries as of January 1, 2015, December 31, 2015 and 2016 and the related consolidated results of their operations and their cash flows for each of the two years in the period ended December 31, 2016, in conformity with International Financial

Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated May 15, 2017 expressed an unqualified opinion thereon.

Tel-Aviv, Israel /s/ KOST FORER GABBAY & KASIERER
May 15, 2017 KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and the Board of Directors of

FORMULA SYSTEMS (1985) LTD.

We have audited Formula Systems (1985) Ltd. and its subsidiaries (the "Company") internal control over financial reporting as of December 31, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We did not examine the effectiveness of internal control over financial reporting of Magic Software Japan K.K, a wholly owned subsidiary of Magic Software Enterprises Ltd., whose financial statements reflect total assets constituting approximately 0% as of December 31, 2016 and revenues constituting 1%, for the year ended December 31, 2016, of the related consolidated totals. The effectiveness of Magic Software Japan K.K's internal control over financial reporting was audited by other auditor whose report has been furnished to us, and our opinion, insofar as it relates to the effectiveness of Magic Software Japan K.K's internal control over financial reporting, is based solely on the report of the other auditor.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those

policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

Management has excluded from its assessment of internal control over financial reporting as of December 31, 2016 the internal controls of subsidiaries acquired during 2016, which constituted approximately 4% of the Company's consolidated total assets as of December 31, 2016, and 7% of the net income for the period from the date of acquisitions out of the Company's consolidated net income for the year then ended. Accordingly, our audit of internal control over financial reporting of the Company also did not include an evaluation of the internal control over financial reporting of the acquired subsidiaries.

In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial position of the Company and its subsidiaries. as of January 1, 2015, December 31, 2015 and 2016, and the related consolidated statements of profit or loss, comprehensive income, changes in equity and cash flows for each of the two years in the period ended December 31, 2016 and our report dated May 15, 2017 expressed an unqualified opinion thereon.

Tel-Aviv, Israel /s/ KOST FORER GABBAY & KASIERER
May 15, 2017 KOST FORER GABBAY & KASIERER
A Member of Ernst & Young Global

FORMULA SYSTEMS (1985) LTD.**AND ITS SUBSIDIARIES****CONSOLIDATED STATEMENTS OF FINANCIAL POSITION****U.S. dollars in thousands**

	Note	January 1, 2015	December 31, 2015	December 31, 2016
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents		\$ 179,931	\$ 249,141	\$ 238,161
Short-term deposits		6,454	2,688	13
Marketable securities	5	27,699	31,605	37,516
Trade receivables (net of allowances for doubtful accounts of \$4,481, \$3,823 and \$ 4,676 as of January 1, 2015, December 31, 2015 and December 31, 2015 and December 31, 2016, respectively)		235,652	257,631	308,338
Other accounts receivable and prepaid expenses	20a	34,470	43,112	45,678
Inventories		2,437	4,807	3,953
<u>Total</u> current assets		486,643	588,984	633,659
LONG-TERM ASSETS:				
Marketable Securities	5	33,748	30,875	17,228
Deferred taxes	19e	15,983	16,347	15,227
Prepaid expenses and other accounts receivable		12,663	11,506	14,390
<u>Total</u> long-term assets		62,394	58,728	46,845
INVESTMENTS IN COMPANIES ACCOUNTED FOR AT EQUITY METHOD	7	528	-	24,080
PROPERTY, PLANTS AND EQUIPMENT, NET	8	22,111	22,003	26,130
INTANGIBLE ASSETS, NET	10	109,412	104,656	129,821
GOODWILL	9	424,807	441,021	497,784
<u>Total</u> assets		\$ 1,105,895	\$ 1,215,392	\$ 1,358,319

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

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FORMULA SYSTEMS (1985) LTD.**AND ITS SUBSIDIARIES****CONSOLIDATED STATEMENTS OF FINANCIAL POSITION****U.S. dollars in thousands (except share and per share data)**

	Note	January 1, 2015	December 31, 2015	2016
LIABILITIES AND EQUITY				
CURRENT LIABILITIES:				
Liabilities to banks and other financial institutions	11,20b	\$46,043	\$59,082	\$84,760
Debentures	12	-	213	3,274
Trade payables		56,580	68,051	80,114
Deferred revenue		37,986	39,694	37,030
Dividend payable		7,874	-	7,070
Employees and payroll accrual		70,456	76,653	90,709
Other accounts payable	20c	30,933	39,561	41,889
Liabilities in respect of business combinations		2,202	2,866	8,119
Redeemable non-controlling interests	2G	4,266	4,673	6,073
<u>Total</u> current liabilities		256,340	290,793	359,038
LONG-TERM LIABILITIES:				
Liabilities to banks and other financial institutions	11,20b	108,684	103,632	115,529
Debentures, net of current maturities	12	-	57,128	55,441
Other long term liabilities		4,763	7,997	9,384
Deferred taxes	19e	22,409	22,667	30,939
Deferred revenues		4,838	4,396	4,697
Liability in respect of business combinations		1,623	5,539	9,611
Liability in respect of capital lease		903	494	108
Redeemable non-controlling interests	2G	10,958	14,078	43,556
Employee benefit liabilities		3,077	3,389	6,174
<u>Total</u> long-term liabilities		157,255	219,320	275,439
COMMITMENTS AND CONTINGENCIES	17			
EQUITY	18			
Formula Systems (1985) equity:				
Share capital:				
Ordinary shares of NIS 1 par value - Authorized: 25,000,000 shares at January 1, 2015 and December 31, 2015 and 2016 Issued:		4,184	4,184	4,184

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15,287,402 January 1, 2015 and December 31, 2015 and 2016

Outstanding: 14,728,782 at January 1, 2015 and December 31, 2015 and 2016

Additional paid-in capital		106,501	98,946	100,571
Accumulated earnings		215,655	230,256	234,268
Accumulated other comprehensive loss		(1,305)	(3,228)	(2,377)
Treasury shares (568,620 shares as of January 1, 2015 and December 31, 2015 and 2016)		(259)	(259)	(259)
Total equity attributable to Formula Systems (1985) shareholders'		324,776	329,899	336,387
Non-controlling interests	20d	367,524	375,380	387,455
<u>Total</u> equity		692,300	705,279	723,842
<u>Total</u> liabilities, redeemable non-controlling interest and equity		\$1,105,895	\$1,215,392	\$1,358,319

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

FORMULA SYSTEMS (1985) LTD.**AND ITS SUBSIDIARIES****CONSOLIDATED STATEMENTS OF PROFIT OR LOSS**
U.S. dollars in thousands (except share and per share data)

	Year ended December 31,	
	Note 2015	2016
Revenues:	20g	
Proprietary software products and related services	\$242,818	\$273,235
Software services	730,376	835,386
Total revenues	973,194	1,108,621
Cost of revenues:		
Proprietary software products and related services	131,131	149,244
Software services	610,139	700,596
Total cost of revenues	741,270	849,840
Gross profit	231,924	258,781
Research and development expenses, net	15,123	22,328
Selling, marketing, general and administrative expenses	140,935	147,953
Operating income	75,866	88,500
Financial expenses	20e (14,955)	(17,594)
Financial income	5,422	6,008
Group's share of earnings of companies accounted for at equity, net	7 5	349
Income before taxes on income	66,338	77,263
Taxes on income	19g 15,984	21,163
Net income	\$50,354	\$56,100
Attributable to:		
Equity holders of the Company	19,829	22,445
Redeemable non-controlling interests	864	2,125
Non-controlling interests	29,661	31,530
	\$50,354	\$56,100

Net earnings per share attributable to Formula Systems (1985) Shareholders	20h		
Basic earnings per share		\$1.41	\$1.58
Diluted earnings per share		\$1.33	\$1.49

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

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FORMULA SYSTEMS (1985) LTD.**AND ITS SUBSIDIARIES****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****U.S. dollars in thousands**

	Year ended December 31,	
	2015	2016
Net income	\$50,354	\$56,100
Other comprehensive income (loss) (net of tax effect):		
Amounts that will not be reclassified subsequently to profit or loss:		
Actuarial loss from defined benefit plans	(416)	(2,696)
Amounts that will be or that have been reclassified to profit or loss when specific conditions are met:		
Gain from derivative instruments, net	9	-
Gain (loss) from available-for-sale financial assets	102	30
Amounts transferred to the statement of profit or loss for sale of available-for-sale financial assets	(300)	16
Exchange differences on translation of foreign operations	(3,726)	1,772
Total other comprehensive income (loss), net of tax	(4,331)	(878)
Total Comprehensive income	46,023	55,222
Total comprehensive income attributable to:		
Equity holders of the Company	17,693	21,948
Redeemable non-controlling interests	864	2,125
Non-controlling interests	27,466	31,149
	\$46,023	\$55,222

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

**FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
U.S. dollars in thousands (except share and per share data)**

	Share Capital		Additional	Retained	Accumulated	Treasury	Non-	Total
	Number	Amount	paid-in	earnings	other	shares	controlling	Equity
			capital		comprehensive	(cost)	interests	
					Loss			
Balance as of January 1, 2015	14,728,782	\$4,184	\$106,501	\$215,655	\$ (1,305)	\$ (259)	\$367,524	\$692,300
Net Income	-	-	-	19,829	-	-	29,661	49,490
Foreign currency translation reserve	-	-	-	-	(1,663)	-	(2,063)	(3,726)
Actuarial loss from defined benefit plans	-	-	-	(213)	-	-	(203)	(416)
Unrealized gain from derivative instruments, net	-	-	-	-	4	-	5	9
Unrealized gain from available-for-sale securities, net	-	-	-	-	38	-	64	102
Realized gain from available-for-sale securities	-	-	-	-	(302)	-	2	(300)
Total other comprehensive income (loss)	-	-	-	(213)	(1,923)	-	(2,195)	(4,331)
Total comprehensive income	-	-	-	19,616	(1,923)	-	27,466	45,159
Adjustment to redeemable non-controlling interests	-	-	(218)	-	-	-	(266)	(484)
Stock-based Compensation expenses (Note 14a-b)	-	-	1,561	-	-	-	3,305	4,866
Non-controlling interests changes due	-	-	(2,940)	-	-	-	4,828	1,888

to holding changes, including exercise of employees stock options									
Acquisition of non-controlling interests	-	-	(1,892)	-	-	-	(3,937)	(5,829)	
Dividend to Formula's shareholders	-	-	-	(5,015)	-	-	-	(5,015)	
Dividend to non- controlling interests in subsidiaries	-	-	-	-	-	-	(18,039)	(18,039)	
Distribution to parent for a business acquisition under common control	-	-	(5,314)	-	-	-	(5,501)	(10,815)	
Embedded conversion option of convertible debentures	-	-	1,248	-	-	-	-	1,248	
Balance as of December 31, 2015	14,728,782	\$4,184	\$98,946	\$230,256	\$ (3,228)	\$ (259)	\$375,380	\$705,279	

FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES

	Share	Capital	Additional	Retained	Accumulated	Treasury	Non-	Total
	Number	Amount	paid-in	earnings	other	shares	controlling	Equity
			capital		comprehensive	(cost)	interests	
					Loss			
Balance as of January 1, 2016	14,728,782	\$4,184	\$98,946	\$230,256	\$ (3,228)	\$ (259)	\$375,380	\$705,279
Net Income	-	-	-	22,445	-	-	31,530	53,975
Foreign currency translation reserve	-	-	-	-	828	-	944	1,772
Actuarial loss from defined benefit plans	-	-	-	(1,348)	-	-	(1,348)	(2,696)
Unrealized gain from available-for-sale securities, net	-	-	-	-	15	-	15	30
Realized loss (gain) from available-for-sale securities	-	-	-	-	8	-	8	16
Total other comprehensive income (loss)	-	-	-	(1,348)	851	-	(381)	(878)
Total comprehensive income	-	-	-	21,097	851	-	31,149	53,097
Adjustment to redeemable non-controlling interests	-	-	393	-	-	-	453	846
Stock-based Compensation expenses (Note 14a-b)	-	-	772	-	-	-	3,622	4,394
Non-controlling interests changes due to holding changes, including exercise of employees stock options	-	-	1,200	-	-	-	(559)	641
	-	-	(740)	-	-	-	(2,101)	(2,841)

Acquisition of non-controlling interests									
Dividend to Formula's shareholders	-	-	-	(17,085)	-	-	-	(17,085)	
Dividend to non-controlling interests in subsidiaries	-	-	-	-	-	-	(20,692)	(20,692)	
Non-controlling interests arising from initially consolidated companies	-	-	-	-	-	-	203	203	
Balance as of December 31, 2016	14,728,782	\$4,184	\$ 100,571	\$234,268	\$ (2,377)	\$ (259)	\$387,455	\$723,842	

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
U.S. dollars in thousands (except share and per share data)

	Year ended December 31,	
	2015	2016
Reserve from available-for-sale financial assets	328	351
Foreign currency translation reserve	(1,341)	(513)
Reserve from derivatives	4	4
Group's share of net other comprehensive income (loss) of companies accounted for at equity	(2,219)	(2,219)
Accumulated other comprehensive loss	\$ (3,228)	\$ (2,377)

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

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
U.S. dollars in thousands

	Year ended	
	December 31,	
	2015	2016
Cash flows from operating activities:		
Net income	\$50,354	\$56,100
Adjustments to reconcile net income to net cash provided by operating activities:		
Equity in losses (gains) of companies accounted for at equity	142	(349)
Depreciation and amortization	30,896	32,370
Changes in value of debentures	195	1,371
Decrease in employee benefit liabilities	(522)	(1,656)
Gain from sale of property, plants and equipment	-	(3,147)
Stock-based compensation expenses	4,866	4,394
Changes in value of short-term and long term loans from banks and others and deposits, net	(120)	500
Changes in deferred taxes, net	2,134	211
Change in liability in respect of business combinations	654	2,023
Gain from sale and increase in value of marketable securities classified as trading	(114)	(136)
Amortization of premium and accrued interest on marketable securities	(230)	(260)
Realized gain from sale of available for sale securities	(300)	16
Change in redeemable non-controlling interests' put options	905	1,779
Decrease (Increase) in inventories	(2,387)	923
Increase in trade receivables	(17,668)	(30,086)
Increase in other current and long-term accounts receivable	(4,154)	(513)
Increase in trade payables	9,982	5,423
Increase in other accounts payable and employees and payroll accrual	10,793	8,673
Increase (decrease) in deferred revenues	1,693	(2,681)
Net cash provided by operating activities	87,119	74,955

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

FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
U.S. dollars in thousands

	Year ended	
	December 31,	
	2015	2016
Cash flows from investing activities:		
Payments for business acquisitions, net of cash acquired (Appendix C)	(17,000)	(44,832)
Payments to former shareholders of consolidated companies	-	(1,784)
Purchase of intangible assets	(211)	(391)
Purchase of property and equipment	(6,766)	(9,137)
Proceeds from sale of (investment in) marketable securities, net	(690)	8,450
Proceeds from sale of property, plants and equipment	-	2,347
Investment in and loans to affiliates and other companies	-	(25,813)
Change in restricted cash in other accounts receivable	(888)	(544)
Changes in short term deposits, net	3,942	2,665
Capitalization of software development and other costs	(9,879)	(9,769)
Net cash used in investing activities	(31,492)	(78,808)
Cash flows from financing activities:		
Exercise of employees stock options in subsidiaries	1,987	931
Dividend paid to non-controlling interests and redeemable non-controlling interests in subsidiaries	(19,088)	(24,131)
Dividend to Formula's shareholders	(12,890)	(10,014)
Short-term bank credit, net	2,862	20,720
Repayment of long-term loans from banks and others	(26,902)	(37,415)
Receipt of long term loans	32,160	49,582
Proceeds from issuance of Series A and Series B debentures	58,556	
Repayment of long-term liabilities to office of the chief scientist	(555)	(510)
Purchase of non-controlling interests	(5,396)	(3,166)
Cash paid in conjunction with acquisitions of activities	(1,280)	(1,160)
Repayment of capital lease	(399)	(443)
Distribution to ultimate parent for a business acquisition under common control	(8,482)	(1,440)
Net cash provided by (used in) financing activities	20,573	(7,046)
Effect of exchange rate changes on cash and cash equivalents	(6,990)	(81)
Increase (decrease) in cash and cash equivalents	69,210	(10,980)
Cash and cash equivalents at beginning of year	179,931	249,141

Cash and cash equivalents at end of year	\$249,141	\$238,161
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The accompanying notes are an integral part of the financial statements.

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
U.S. dollars in thousands

	Year ended	
	December 31,	
	2015	2016
A. Supplemental cash flow information:		
Cash paid (received) in respect of:		
Interest paid	\$6,158	\$6,770
Interest received	\$(1,688)	\$(2,334)
Income tax	\$23,014	\$19,176
B. Non-cash activities:		
Dividend payable to Formula's shareholders	\$-	\$7,070
Purchase of property and equipment	\$-	\$(2,260)
C. Acquisition of newly-consolidated subsidiaries and activities, net of cash acquired:		
Assets and liabilities of subsidiaries consolidated as of acquisition date:		
Working capital (other than cash and cash equivalents)	(1,445)	(2,938)
Property and equipment	(360)	(3,494)
Goodwill and intangible assets	(25,673)	(92,878)
Other long-term assets	(134)	-
Liabilities to banks and others	47	3,391
Long-term liabilities	1,556	-
Deferred tax liability, net	425	10,130
Liability to formerly shareholders	4,117	11,997
Non-controlling interests at acquisition date	-	203
Redeemable non-controlling interests at acquisition date	4,467	28,757
Total	\$(17,000)	\$(44,832)

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

FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 1:- GENERAL

a. General:

Formula Systems (1985) Ltd. ("Formula" or the "Company") was incorporated in Israel and began its business operations in 1985. Since 1991, Formula's ordinary shares, par value NIS 1.0 per share, have been traded on the Tel-Aviv Stock Exchange ("TASE"), and, in 1997, began trading through American Depositary Shares ("ADSs") under the symbol "FORTY" on the NASDAQ Global Market in the United States until January 3, 2011, at which date the listing of Formula's ADSs was transferred to the NASDAQ Global Select Market ("NASDAQ"). Each ADS represents one ordinary share of Formula. The Company is considered an Israeli resident. As of November, 2010, the controlling shareholder of the Company is Asseco Poland S.A. ("Asseco"), a Polish public company, traded on the Warsaw Stock Exchange.

Formula, through its investees (collectively, the "Group") is engaged in providing software services, proprietary and non-proprietary software solutions, software product marketing and support, computer infrastructure and integration solutions and learning and integration. The Group operates through five directly held investees: Matrix IT Ltd. ("Matrix"); Magic Software Enterprises Ltd. ("Magic"), Sapiens International Corporation N.V ("Sapiens"), InSync Staffing Solutions, Inc ("Insync") and, TSG IT Advanced Systems Ltd. ("TSG").

b. Investees:

The following table presents certain information regarding ownership of Formula's significant investees, as of the dates indicated (the list consists only of active companies that are held directly by Formula):

Name of Investee	Percentage of ownership	
	December 31, 2015	2016
Matrix	50.04	50.01
Magic	46.40	47.26
Sapiens	49.13	48.85

Insync	90.09	90.09
TSG ⁽¹⁾	-	50.00

1) TSG's results of operations are reflected in the Company's results of operations using the equity method of accounting commencing May 9, 2016.

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 1:- general (Cont.)

c. Definitions:

In these financial statements:

The Company	-Formula Systems (1985) Ltd.
The Group	-Formula Systems (1985) Ltd. and its investees.
Subsidiaries	- Companies that are controlled by the Company (as defined in IFRS 10) and whose accounts are consolidated with those of the Company.
Jointly controlled entities	- Companies owned by various entities that have a contractual arrangement for joint control and are accounted for using the equity method of accounting.
Associates	- Companies over which the Company has significant influence and that are not subsidiaries. The Company's investment therein is included in the financial statements using the equity method.
Investees	-Subsidiaries, jointly controlled entities and associates.
Interested parties and controlling shareholder	- As defined in the Israeli Securities Regulations (Annual Financial Statements), 2010.
Related parties	- As defined in IAS 24.

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES

The following accounting policies have been applied consistently in the financial statements for all periods presented, unless otherwise stated.

- 1) Basis of presentation of the financial statements

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

The Company's financial statements have been prepared on a cost basis, except for: investment property; available-for-sale financial assets; financial assets and liabilities (including derivatives) which are presented at fair value through profit or loss.

The Company has elected to present the profit or loss items using the function of expense method.

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**FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

These financial statements for the year ended December 31, 2016 are the Group's first consolidated financial statements prepared in accordance with IFRS. The date of transition to IFRS is January 1, 2015. For all periods up to and including the year ended December 31, 2015, the Group prepared its financial statements in accordance with United States generally accepted accounting principles ("U.S. GAAP"). Accordingly, the Group has prepared financial statements that comply with IFRS applicable as of December 31, 2016, together with the comparative period data for the year ended December 31, 2015. An explanation of the principal adjustments made in representing its U.S. GAAP financial statements, including the statement of financial position as of January 1, 2015, the Group's date of transition to IFRS and the financial statements for the year ended December 31, 2015, in order to comply with IFRS, is provided in note 21 to our consolidated financial statements.

Pursuant to the transitional relief granted by the U.S. SEC in respect of the first-time adoption of IFRS, we have only provided financial statements and financial information for two fiscal years ended December 31, 2016 in this annual report as presented under IFRS.

2) Use of estimates and judgments

The preparation of the consolidated financial statements in conformity with IFRS requires management to make estimates, judgments and assumptions that affect the amounts reported in the financial statements and accompanying notes. The Company's management believes that the estimates, judgments and assumptions used are reasonable based upon information available at the time they are made. Actual results could differ from those estimates. The most significant assumptions are employed in estimates used in determining values of goodwill and identifiable intangible assets and their subsequent impairment analysis, revenue recognition, tax assets and tax positions, legal contingencies, research and development capitalization, contingent consideration related to acquisitions, determining the fair value of non-controlling interests and redeemable non-controlling interests, pension and other post-employment benefits and share-based compensation costs.

In the process of applying the significant accounting policies, the Group has made the following judgments which have the most significant effect on the amounts recognized in the financial statements:

Effective control:

The Company's management assess whether it controls an investee in which it holds less than the majority of the voting power, among others, by reference to the size of its voting power relative to the size and dispersion of other holders voting power including voting patterns at previous shareholders' meetings.

The Company's Management has concluded that despite the lack of absolute majority of voting power at the general meetings of shareholders of Sapiens and Magic, in accordance with IFRS 10, these investees are controlled by the Company. The conclusion regarding the existence of control as of January 1, 2015 and during the twelve months period ended 31 December 2015 and 2016, in accordance with IFRS 10, was made in accordance with the following factors:

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**FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Sapiens:

i. Governing bodies of Sapiens:

Decisions of Sapiens' shareholders general meeting are taken by a simple majority of votes represented at the general meeting. The annual (ordinary) general meeting adopts resolutions to appoint individual directors, choose Sapiens' independent auditors for the next year, as well as approve the company's financial statements and the management's report on operations.

In accordance with Sapiens' articles of association, the board of directors of Sapiens is responsible for managing its current business operations and is authorized to take substantially all decisions which are not specifically reserved to Sapiens' shareholders by its articles of association, including the decision to pay out dividends. Sapiens' board of directors is composed of 7 members, 4 of whom are independent directors. For the last 6 years, the Company has consistently reappointed the same members of the board of directors. Likewise, the previous composition of the board of directors was re-elected during the general meeting that was held in May 2016, this is when the Company's share interest in Sapiens was already below 50%.

ii. Shareholders structure of Sapiens:

Sapiens' shareholders structure is dispersed because, apart from the Company, just one shareholder holds more than 5% of the voting rights at the general meeting (5.36% of votes). There is no evidence that any shareholders have or had granted to any other shareholder a voting proxy at the general meeting. Over the last four years from 2013 to 2016, the Sapiens' general meetings were attended by shareholders representing in total between 70% and 77% of total voting power (including the Company's share power and bearing in mind that the Company presently holds approximately 48.85% of total voting rights). This means that the level of activity of Sapiens' other shareholders is relatively moderate or low. As of December 31, 2016, the attendance from shareholders would have to be higher than 98% in order to deprive the Company of an absolute majority of votes at the general meeting. In accordance with voting patterns at Sapiens' recent years shareholders' meetings, it is the Company's management belief that achieving such a high attendance seems unlikely.

Magic:

i. Governing bodies of Magic:

Decisions of Magic's shareholders general meeting are taken by a simple majority of votes represented at the general meeting. The annual (ordinary) general meeting adopts resolutions to appoint individual directors, choose Magic's independent auditors for the next year, as well as to approve Magic's financial statements and the management's report on operations.

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

In accordance with the Magic's articles of association, the board of directors of Magic is responsible for managing Magic's current business operations and is authorized to take substantially all decisions which are not specifically reserved to Magic shareholders by its articles of association, including the decision to pay out dividends. Magic's board of directors is composed of 5 members, 3 of whom are independent directors. In recent years, the Company has consistently reappointed the same members of the board of directors.

ii. Shareholders structure of Magic:

Magic's shareholders structure may be considered as dispersed because, apart from the Company, as of December 31, 2016 there was no other shareholder that held more than 5% of Magic's voting power (with the next major shareholder holding approximately 4.04%) and as of December 31, 2015 just one shareholder held more than 5% of Magic's voting power (approximately 5.41%) with the next major shareholder holding approximately 4.5%. There is no evidence that any shareholders have or had granted to any other shareholder a voting proxy at the general meeting. Over the last five years from 2012 to 2016, Magic's general meetings were attended by shareholders representing in total between 65% and 85% of total voting rights (including the Company's share power and bearing in mind that the Company presently holds approximately 47.26% of total voting power). This means that the level of activity of Magic's other shareholders is relatively moderate or low. As of December 31, 2016, the attendance from shareholders would have to be higher than 95% in order to deprive the Company of an absolute majority of votes at the general meeting. In accordance with voting patterns at Magic's recent years shareholders' meetings, it is the Company's management belief that achieving such a high attendance seems unlikely.

3) Consolidated financial statements:

The consolidated financial statements comprise the financial statements of companies that are controlled by the Company (subsidiaries). Control is achieved when the Company is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Potential voting rights are considered when assessing whether an entity has control. In a situation when the Company holds less than a majority of voting rights in a given entity, but it is sufficient to unilaterally direct the relevant activities of such entity, then the control is exercised. When assessing whether voting rights held by the Company are sufficient to give it power, the Company considers all facts and circumstances, including: the size of its holding of voting rights relative to the size and dispersion of other vote holders; potential voting rights held by the Company and other shareholders or parties; rights arising from other contractual arrangements; significant personal ties and any additional facts and

circumstances that may indicate that the Company has, or does not have the ability to direct the relevant activities when decisions need to be made, inclusive of voting patterns observed at previous meetings of shareholders.

The consolidation of the financial statements commences on the date on which control is obtained and ends when such control ceases.

The financial statements of the Company and of the subsidiaries, after being adjusted to comply with IFRS, are prepared for the same reporting period and using consistent accounting treatment of similar transactions and economic activities. Any discrepancies in the applied accounting policies are eliminated by making appropriate adjustments. Significant intragroup balances and transactions and gains or losses resulting from intragroup transactions are eliminated in full in the consolidated financial statements.

**FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Non-controlling interests in subsidiaries represent the equity in subsidiaries not attributable, directly or indirectly, to a parent. Non-controlling interests are presented in equity separately from the equity attributable to the equity holders of the Company. Profit or loss and components of other comprehensive income are attributed to the Company and to non-controlling interests. Losses are attributed to non-controlling interests even if they result in a negative balance of non-controlling interests in the consolidated statement of financial position.

The disposal of a subsidiary that does not result in a loss of control is recognized as a change in equity. In such events, in order to reflect changes in the ownership of a respective subsidiary, the Group shall adjust the carrying value of controlling interests and non-controlling interests. Any differences between the change in non-controlling interests and the fair value of consideration paid or received are recognized directly in equity and attributed to the owners of the Company.

4) Business combinations and goodwill:

Business combinations are accounted for by applying the acquisition method. The cost of the acquisition is measured at the fair value of the consideration transferred on the acquisition date with the addition of non-controlling interests in the acquiree. In each business combination, the Company whether to measures the non-controlling interests in the acquiree based on their fair value on the acquisition date or at their proportionate share in the fair value of the acquiree's net identifiable assets.

Direct acquisition costs are carried to the statement of profit or loss as incurred.

In a business combination achieved in stages, equity interests in the acquiree that had been held by the acquirer prior to obtaining control are measured at the acquisition date fair value while recognizing a gain or loss resulting from the revaluation of the prior investment on the date of achieving control.

Contingent consideration is recognized at fair value on the acquisition date and classified as a financial asset or liability in accordance with IAS 39, "Financial Instruments: Recognition and Measurement". Subsequent changes in the fair value of the contingent consideration are recognized in profit or loss. If the contingent consideration is classified as an equity instrument, it is measured at fair value on the acquisition date without subsequent remeasurement.

Goodwill is initially measured at cost which represents the excess of the acquisition consideration and the amount of non-controlling interests over the net identifiable assets acquired and liabilities assumed. If the resulting amount is negative, the acquirer recognizes the resulting gain on the acquisition date without subsequent measurement.

5) Investment in joint arrangements:

Joint arrangements are arrangements in which the Company has joint control. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

i. Joint ventures:

In joint ventures the parties that have joint control of the arrangement have rights to the net assets of the arrangement. A joint venture is accounted for at equity

ii. Joint operations:

In joint operations the parties that have joint control of the arrangement have rights to the assets and obligations for the liabilities relating to the arrangement. The Company recognizes in relation to its interest its share of the assets, liabilities, revenues and expenses of the joint operation.

6) Investments in associates:

Associates are companies in which the Group has significant influence over the financial and operating policies without having control. The investment in an associate is accounted for using the equity method.

7) Investments accounted for using the equity method:

The Group's investments in associates and joint ventures are accounted for using the equity method. Under the equity method, the investment in the associate or in the joint venture is presented at cost with the addition of post-acquisition changes in the Group's share of net assets, including other comprehensive income of the associate or the joint venture. Gains and losses resulting from transactions between the Group and the associate or the joint venture are eliminated to the extent of the interest in the associate or in the joint venture.

Goodwill relating to the acquisition of an associate or a joint venture is presented as part of the investment in the associate or the joint venture, measured at cost and not systematically amortized. Goodwill is evaluated for

impairment as part of the investment in the associate or in the joint venture as a whole.

The financial statements of the Company and of the associate or joint venture are prepared as of the same dates and periods. The accounting policies applied in the financial statements of the associate or the joint venture are uniform and consistent with the policies applied in the financial statements of the Group.

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Upon the acquisition of an associate or a joint venture achieved in stages when the former investment in the acquiree was accounted for pursuant to the provisions of IAS 39, the Group adopts the principles of IFRS 3 regarding business combinations achieved in stages. Consequently, equity interests in the acquiree that had been held by the Group prior to achieving significant influence or joint control are measured at fair value on the acquisition date and are included in the acquisition consideration while recognizing a gain or loss resulting from the fair value measurement.

8) Functional currency, presentation currency and foreign currency:

i. Functional currency and presentation currency:

The presentation currency of the financial statements is the U.S dollars (the "dollar"). The Group determines the functional currency of each investee, including companies accounted for at equity. The currency of the primary economic environment in which the operations of Formula and certain of its investees are conducted is the dollar, thus, the dollar is the functional and reporting currency of Formula and certain of its investees.

Assets, including fair value adjustments upon acquisition, and liabilities of an investee which is a foreign operation, are translated at the closing rate at each reporting date. Profit or loss items are translated at average exchange rates for all periods presented. The resulting translation differences are recognized in other comprehensive income (loss).

Intragroup loans for which settlement is neither planned nor likely to occur in the foreseeable future are, in substance, a part of the investment in the foreign operation and, accordingly, the exchange rate differences from these loans (net of the tax effect) are recorded in other comprehensive income (loss).

FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Upon the full or partial disposal of a foreign operation resulting in loss of control in the foreign operation, the cumulative gain (loss) from the foreign operation which had been recognized in other comprehensive income is transferred to profit or loss. Upon the partial disposal of a foreign operation which results in the retention of control in the subsidiary, the relative portion of the amount recognized in other comprehensive income is reattributed to non-controlling interests.

ii. Transactions, assets and liabilities in foreign currency:

Transactions denominated in foreign currency are recorded upon initial recognition at the exchange rate at the date of the transaction. After initial recognition, monetary assets and liabilities denominated in foreign currency are translated at each reporting date into the functional currency at the exchange rate at that date. Exchange rate differences, other than those capitalized to qualifying assets or accounted for as hedging transactions in equity, are recognized in profit or loss. Non-monetary assets and liabilities denominated in foreign currency and measured at cost are translated at the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currency and measured at fair value are translated into the functional currency using the exchange rate prevailing at the date when the fair value was determined.

9)

Cash equivalents:

Cash equivalents are considered as highly liquid investments, including unrestricted short-term bank deposits with an original maturity of three months or less from the date of investment or with a maturity of more than three months, but which are redeemable on demand without penalty and which form part of the Group's cash management. Cash and cash equivalent includes amounts held primarily in New-Israeli Shekel, U.S. dollars, Euro and British Pound.

10)

Short-term and restricted deposits:

Short-term bank deposits are deposits with an original maturity of more than three months from the date of investment and which do not meet the definition of cash equivalents. The deposits are presented according to their terms of deposit. Restricted deposits include deposits used to secure certain subsidiaries' ongoing projects and credit lines from

banks as well as, security deposits with respect to leases, and are classified under other receivables.

11) Allowance for doubtful accounts:

The allowance for doubtful accounts is determined in respect of specific trade receivables whose collection, in the opinion of the Group's management, is doubtful. The Group did not recognize an allowance in respect of groups of trade receivables that are collectively assessed for impairment due to immateriality. Impaired receivables are derecognized when they are assessed as uncollectible. The allowance for doubtful accounts is determined with respect to specific debts that are doubtful of collection. The bad debt expense net for the years ended December 31, 2015 and 2016 was \$ 747 and \$ 652 respectively.

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FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

12)

Inventories:

Inventories are measured at the lower of cost and net realizable value. The cost of inventories comprises costs of purchase and costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less estimated costs of completion and estimated costs necessary to make the sale. Inventories are mainly comprised of purchased merchandise and products which consist of educational software kits, computers, peripheral equipment and spare parts. Cost is determined on the "first in - first out" basis. The Group periodically evaluates the condition and aging of its inventories and makes provisions for impairment of slow moving inventories accordingly. No such impairments have been recognized in any period presented.

13)

Revenue recognition:

The Group derives its revenues primarily from the sale of information technology (or "IT") services which also include sale of: non-proprietary software products, including maintenance, integration and infrastructure, outsourcing, training and deployment. In addition, the Group generates revenues from licensing the rights to use its proprietary software, provision of related IT professional services (which may or may not be considered essential to the functionality of the software license), related maintenance and technical support, as well as implementation and post-implementation consulting services.

Revenues are recognized in profit or loss when the revenues can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably. When the Group acts as a principal and is exposed to the risks associated with the transaction, revenues are presented on a gross basis. When the Group acts as an agent and is not exposed to the risks and rewards associated with the transaction, revenues are presented on a net basis. Revenues are measured at the fair value of the consideration less any trade discounts, volume rebates and returns.

The Group generally considers all arrangements with payment terms extending beyond a minimum of six or a maximum of twelve months from the delivery of the elements not to be fixed or determinable. If the fee is not fixed or determinable, revenue is recognized as payments become due from the customer, provided that all other revenue

recognition criteria have been met.

The Group generally does not grant a right of return to its customers. When a right of return exists, revenue is deferred until the right of return expires, at which time revenue is recognized, provided that all other revenue recognition criteria are met. Deferred revenue includes unearned amounts received under maintenance and support contracts and amounts received from customers but not yet recognized as revenues.

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**FORMULA SYSTEMS (1985) LTD.
AND ITS SUBSIDIARIES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
U.S. dollars in thousands, except share and per share data**

NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Following are the specific revenue recognition criteria which must be met before revenue is recognized by the Company and its subsidiaries:

i. Revenues from software solutions and services:

a) Revenues from contracts based on actual inputs. Revenues from master agreements based on actual inputs are recognized based on actual labor hours.

b) Outsourcing - these agreements are similar in nature to agreements that are based on actual labor hours. The Group allocates employees to projects that are generally managed by the customers at their charge based on the pricing of labor hours. Revenues are recognized based on actual labor hours.

Certain of the software license sales may also include significant implementation and customization services with respect to such sales which are deemed essential to the functionality of the license. In addition, the Group also provides consulting services that are not deemed essential to the functionality of the license, as well as outsourcing IT services.

With respect to revenues that involve significant implementation and customization services to customer specific requirements and which are considered essential to the functionality of the product offered (for example when the Group sells software licenses as part of an overall solution offered to a customer that combines the sale of software licenses which includes significant implementation that is considered essential to the functionality of the license) whether generated by fixed-price or time-and-materials contracts the Company accounts for revenues for the services together with the software under contract, using the percentage-of-completion method. The percentage-of-completion method is used when the required services are quantifiable, based on the estimated number of labor hours necessary to complete the project, and under that method revenues are recognized using labor hours incurred as the measure of progress towards completion. This type of revenues is included in the Company's Proprietary software products and related services and software services revenue streams.

Estimates of total project requirements are based on prior experience of customization, delivery and acceptance of the same or similar technology, and are reviewed and updated regularly by management. After delivery, if uncertainty exists about customer acceptance of the software, license revenue is not recognized until acceptance. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract. As of each of January 1, 2015 and December 31, 2015 and 2016, no estimated losses were identified.

ii. Revenues from sales, distribution and support of software products:

The Group recognizes revenues from the sale of software only after the significant risks and rewards of ownership of the software have been transferred to the buyer for which a necessary condition is delivery of the software, either physically or electronically, or providing the right to use or permission to make copies of the software. The Group reports income on a gross basis since it acts as a principal and bears the risks and rewards derived from the transaction. The Group recognizes revenues from providing software related services. When the stage of completion cannot be determined reliably, revenues are recognized on a straight-line basis over the agreement period.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Revenue from third-party sales is recorded at a gross or net amount according to certain indicators. The application of these indicators for gross and net reporting of revenue depends on the relative facts and circumstances of each sale and requires significant judgment.

Revenues from sale agreements that do not provide a general right of return and consist of multiple elements such as hardware, service and support agreements are split into different accounting units which are separately recognized. An element only represents a separate accounting unit if and only if it has standalone value for the customer. Moreover, there should be reliable and objective evidence of the fair value of all the elements in the agreement or of the fair value of undelivered elements. Revenues from the various accounting units are recognized when the revenue recognition criteria are met with respect to all the elements of the accounting unit based on their specific type and only up to the amount of the consideration that is not contingent on completion or performance of the other elements in the contract.

Maintenance and support includes annual maintenance contracts providing for unspecified upgrades for new versions and enhancements on a when-and-if-available basis for an annual fee. The right for unspecified upgrades for new versions and enhancements on a when-and-if-available basis does not specify the features, functionality and release date of future product enhancements for the customer to know what will be made available and the general timeframe in which it will be delivered. Revenues from maintenance services are recognized on a straight-line basis at the relative portion of the maintenance contract that is determined for each reporting year. Revenues that have been received before the respective service has been provided are carried to deferred income.

iii. Revenues from training and implementation services:

Revenues from trainings and implementations are recognized when providing the service. Revenues from training services in respect of courses conducted over a period of up to 3 months will be recognize over the period of the course. Revenues from training services in respect of courses ordered in advance and long-term or short term (for a period of up to a year) retraining courses months will be recognized over the period of the course. Revenues from projects which usually ordered by organizations, will be recognize under the actual inputs recognize using the basis hours actual invested in the project.

iv. Revenues from hardware products and infrastructure solutions:

Revenues from hardware products and infrastructure solutions are recognized after all the significant risks and rewards of ownership of the products have been transferred to the buyer. The Group does not retain any continuing management involvement that is associated with ownership and does not retain the effective control of the sold products, the amount of revenues can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the Group and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

14)

Government grants:

Government grants are recognized when there is reasonable assurance that the grants will be received and the Group will comply with the attached conditions. Government grants received from the Office of the Chief Scientist in Israel ("OCI") are recognized upon receipt as a liability if future economic benefits are expected from the research project that will result in royalty-bearing sales. A liability for the loan is first measured at fair value using a discount rate that reflects a market rate of interest. The difference between the amount of the grant received and the fair value of the liability is accounted for as a Government grant and recognized as a reduction of research and development expenses. After initial recognition, the liability is measured at amortized cost using the effective interest method. Royalty payments are treated as a reduction of the liability. If no economic benefits are expected from the research activity, the grant receipts are recognized as a reduction of the related research and development expenses. In that event, the royalty obligation is treated as a contingent liability in accordance with IAS 37.

In each reporting date, the Group evaluates whether there is reasonable assurance that the liability recognized, in whole or in part, will not be repaid (since the Group will not be required to pay royalties) based on the best estimate of future sales and using the original effective interest method, and if so, the appropriate amount of the liability is derecognized against a corresponding reduction in research and development expenses. Amounts paid as royalties are recognized as settlement of the liability.

15)

Taxes on income:

Current or deferred taxes are recognized in profit or loss, except to the extent that they relate to items which are recognized in other comprehensive income or equity.

Current taxes:

The current tax liability is measured using the tax rates and tax laws that have been enacted or substantively enacted by the reporting date as well as adjustments required in connection with the tax liability in respect of previous years.

Deferred taxes:

Deferred taxes are computed in respect of temporary differences between the carrying amounts in the financial statements and the amounts attributed for tax purposes. Deferred taxes are measured at the tax rate that is expected to apply when the asset is realized or the liability is settled, based on tax laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is not probable that they will be utilized. Deductible carryforward losses and temporary differences for which deferred tax assets had not been recognized are reviewed at each reporting date and a respective deferred tax asset is recognized to the extent that their utilization is probable.

Taxes on income that relate to distributions of an equity instrument and to transaction costs of an equity transaction are accounted for pursuant to IAS 12.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Taxes that would apply in the event of the disposal of investments in investees have not been taken into account in computing deferred taxes, as long as the disposal of the investments in investees is not probable in the foreseeable future. Also, deferred taxes that would apply in the event of distribution of earnings by investees as dividends have not been taken into account in computing deferred taxes, since the distribution of dividends does not involve an additional tax liability or since it is the Company's policy not to initiate distribution of dividends from a subsidiary that would trigger an additional tax liability.

Deferred taxes are offset if there is a legally enforceable right to offset a current tax asset against a current tax liability and the deferred taxes relate to the same taxpayer and the same taxation authority.

16)

Leases:

The criteria for classifying leases as finance or operating leases depend on the substance of the agreements and are made at the inception of the lease in accordance with the following principles as set out in IAS 17.

The Group as lessee:

i.

Financial leases:

A lease that transfers substantially all the risks and rewards incidental to ownership of the leased asset to the Group is classified as a finance lease. At the commencement of the lease term, the leased asset is measured at the lower of the fair value of the leased asset or the present value of the minimum lease payments. The leased asset is depreciated over the shorter of its useful life and the lease term.

ii.

Operating leases:

Leases in which substantially all the risks and rewards of ownership of the leased asset are not transferred to the Group are classified as operating leases. Lease payments are recognized as an expense in profit or loss on a straight-line basis over the lease term.

17) Property, plant and equipment, net

Property, plant and equipment are measured at cost, including directly attributable costs, less accumulated depreciation, accumulated impairment losses and any related investment grants and excluding day-to-day servicing expenses. Cost includes spare parts and auxiliary equipment that are used in connection with plant and equipment. The cost of an item of property, plant and equipment comprises the initial estimate of the costs of dismantling and removing the item and restoring the site on which the item is located.

Depreciation is calculated on a straight-line basis over the useful life of the assets at annual rates as follows:

	%
Computers, software and peripheral equipment	20-33 (mainly 33%)
Office furniture and equipment	6-20
Motor vehicles	15
Buildings	2-4

Leasehold improvements are amortized using the straight-line method over the term of the lease (including option terms that are deemed to be reasonably assured) or the estimated useful life of the improvements, whichever is shorter.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The useful life, depreciation method and residual value of an asset are reviewed at least each year-end (at the end of the year) and any changes are accounted for prospectively as a change in accounting estimate. Depreciation of an asset ceases at the earlier of the date that the asset is classified as held for sale and the date that the asset is derecognized. For impairment testing of property, plant and equipment, see Note 2(20) below.

18)

Research and development costs:

Research expenditures incurred in the process of software development are recognized in profit or loss when incurred. An intangible asset arising from a software development project or from the development phase of an internal project is recognized if the Group can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale; the Group's intention to complete the intangible asset and use or sell it; the ability to use or sell the intangible asset; how the intangible asset will generate future economic benefits; the availability of adequate technical, financial and other resources to complete the intangible asset; and the ability to measure reliably the respective expenditure asset during its development. The Group establishes technological feasibility upon completion of a detailed program design or working model.

Research and development costs incurred between completion of the detailed program design and the point at which the product is ready for general release, have been capitalized.

Capitalized software costs are measured at cost less any accumulated amortization and any accumulated impairment losses on a product by product basis. Amortization of capitalized software costs begin when development is complete and the product is available for use. The Group considers a product to be available for use when the Group completes its internal validation of the product that is necessary to establish that the product meets its design specifications including functions, features, and technical performance requirements. Internal validation includes the completion of coding, documentation and testing that ensure bugs are reduced to a minimum. The internal validation of the product takes place a few weeks before the product is made available to the market. In certain instances, The Group enters into a short pre-release stage, during which the product is made available to a selected number of customers as a beta program for their own review and familiarization. Subsequently, the release is made generally available to customers. Once a product is considered available for use, the capitalization of costs ceases and amortization of such costs to "cost of sales" begins.

Capitalized software costs are amortized on a product by product basis by the straight-line method over the estimated useful life of the software product (between 4-7 years, due to their high rates of acceptance, the continued reliance on these products by existing customers, and the demand for such products from prospective customers, all of which validate the Group's expectations) which provides greater amortization expense compared to the revenue-curve method.

Research and development costs incurred in the process of developing product enhancements are generally charged to expenses as incurred.

The Group assesses the recoverability of its Capitalized software costs on a regular basis by assessing the net realizable value of these intangible assets based on the estimated future gross revenues from each product reduced by the estimated future costs of completing and disposing of it, including the estimated costs of performing maintenance and customer support over its remaining economical useful life using internally generated projections of future revenues generated by the products, cost of completion of products and cost of delivery to customers over its remaining economical useful life. During the years ended December 31, 2015 and 2016, no such unrecoverable amounts were identified.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

19) Other intangible assets:

Separately acquired intangible assets are measured on initial recognition at cost including directly attributable costs. Intangible assets acquired in a business combination are measured at fair value at the acquisition date. Expenditures relating to internally generated intangible assets, excluding capitalized development costs, are recognized in profit or loss when incurred.

Intangible assets with a finite useful life are amortized over their useful life and reviewed for impairment whenever there is an indication that the asset may be impaired. The amortization period and the amortization method for an intangible asset are reviewed at least at each year end

Other intangible assets are comprised mainly of customer-related intangible assets, backlogs, brand names, capitalized courses development costs, non-compete agreements and acquired technology and Patent, and are amortized over their useful lives using a method of amortization that reflects the pattern in which the economic benefits of the intangible assets are consumed or otherwise used up. The useful life of intangible assets is as follows:

	Years
Customer relationship and acquired technology	3-15
Capitalized courses development costs	3
Brand names	5
Backlog, non-compete agreements and other intangibles	2-10
Patent	10

The Group assesses the recoverability of its intangible assets on a regular basis by determining whether the amortization of the asset over its remaining useful life can be recovered through undiscounted future operating cash flows from the specific software product sold. During the years ended December 31, 2015 and 2016, no unrecoverable amounts were identified.

Intangible assets with indefinite useful lives are not systematically amortized and are tested for impairment annually or whenever there is an indication that the intangible asset may be impaired. The useful life of these assets is reviewed annually to determine whether their indefinite life assessment continues to be supportable. If the events and circumstances do not continue to support the assessment, the change in the useful life assessment from indefinite to finite is accounted for prospectively as a change in accounting estimate and on that date the asset is tested for impairment. Commencing from that date, the asset is amortized systematically over its useful life.

20)

Impairment of non-financial assets:

The Group evaluates the need to record an impairment of non-financial assets (property, plant and equipment, capitalized software costs and other intangible assets, goodwill, investments in joint venture) whenever events or changes in circumstances indicate that the carrying amount is not recoverable.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

If the carrying amount of non-financial assets exceeds their recoverable amount, the assets are reduced to their recoverable amount. The recoverable amount is the higher of fair value less costs of sale and value in use. In measuring value in use, the expected future cash flows are discounted using a pre-tax discount rate that reflects the risks specific to the asset. The recoverable amount of an asset that does not generate independent cash flows is determined for the cash-generating unit to which the asset belongs. Impairment losses are recognized in profit or loss.

An impairment loss of an asset, other than goodwill, is reversed only if there have been changes in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. Reversal of an impairment loss, as above, shall not be increased above the lower of the carrying amount that would have been determined (net of depreciation or amortization) had no impairment loss been recognized for the asset in prior years and its recoverable amount. The reversal of impairment loss of an asset presented at cost is recognized in profit or loss.

The following criteria are applied in assessing impairment of these specific assets:

- i. Goodwill in respect of subsidiaries:

The Group reviews goodwill for impairment once a year, on December 31, or more frequently if events or changes in circumstances indicate that there is an impairment.

Goodwill is tested for impairment by assessing the recoverable amount of the cash-generating unit (or group of cash-generating units) to which the goodwill has been allocated. An impairment loss is recognized if the recoverable amount of the cash-generating unit (or group of cash-generating units) to which goodwill has been allocated is less than the carrying amount of the cash-generating unit (or group of cash-generating units). Any impairment loss is allocated first to goodwill. Impairment losses recognized for goodwill cannot be reversed in subsequent periods.

- ii. Investment in associate or joint venture using the equity method:

After application of the equity method, the Group determines whether it is necessary to recognize any additional impairment loss with respect to the investment in associates or joint ventures. The Group determines at each reporting date whether there is objective evidence that the carrying amount of the investment in the associate or the joint venture is impaired. The test of impairment is carried out with reference to the entire investment, including the goodwill attributed to the associate or the joint venture.

During the years ended December 31, 2015 and 2016, no impairment indicators were identified.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

21) Financial instruments:

A. Financial assets:

Financial assets within the scope of IAS 39 are initially recognized at fair value plus directly attributable transaction costs, except for financial assets measured at fair value through profit or loss in respect of which transaction costs are recorded in profit or loss. After initial recognition, the accounting treatment of financial assets is based on their classification as follows:

i. Financial assets at fair value through profit or loss:

This category includes financial assets held for trading.

ii. Loans and receivables:

Loans and receivables are investments with fixed or determinable payments that are not quoted in an active market. After initial recognition, loans are measured based on their terms at amortized cost plus directly attributable transaction costs using the effective interest method and less any impairment losses. Short-term borrowings are measured based on their terms, normally at face value.

iii. Available-for-sale financial assets:

Available-for-sale financial assets are (non-derivative) financial assets that are designated as available for sale or are not classified in any of the three preceding categories. After initial recognition, available-for-sale financial assets are measured at fair value. Gains or losses from fair value adjustments, except for interest, exchange rate differences that relate to debt instruments and dividends from an equity instrument, are recognized in other comprehensive income. When the investment is disposed of or in case of impairment, the other comprehensive income (loss) is transferred to

profit or loss.

B.

Financial liabilities:

Financial liabilities are initially recognized at fair value. Loans and other liabilities measured at amortized cost are presented less direct transaction costs. After initial recognition, the accounting treatment of financial liabilities is based on their classification as follows:

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

i. Financial liabilities at amortized cost:

After initial recognition, loans and other liabilities are measured based on their terms at amortized cost less directly attributable transaction costs using the effective interest method.

ii. Financial liabilities at fair value through profit or loss:

Financial liabilities at fair value through profit or loss include financial liabilities classified as held for. Derivatives, including separated embedded derivatives, are classified as held for trading unless they are designated as effective hedging instruments.

C. Offsetting financial instruments:

Financial assets and financial liabilities are offset and the net amount is presented in the statement of financial position if there is a legally enforceable right to set off the recognized amounts and there is an intention either to settle on a net basis or to realize the asset and settle the liability simultaneously.

The right of set-off must be legally enforceable not only during the ordinary course of business of the parties to the contract but also in the event of bankruptcy or insolvency of one of the parties. In order for the right of set-off to be currently available, it must not be contingent on a future event, there may not be periods during which the right is not available, or there may not be any events that will cause the right to expire.

D. Compound financial instruments:

i. Convertible debentures which contain both an equity component and a liability component are separated into two components. This separation is performed by first determining the liability component based on the fair value of an

equivalent non-convertible liability. The value of the conversion component is determined to be the residual amount. Directly attributable transaction costs are apportioned between the equity component and the liability component based on the allocation of proceeds to the equity and liability components.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Convertible debentures that are denominated in foreign currency contain two components: the conversion component and the debt component. The liability conversion component is initially recognized as a financial derivative at fair value. The balance is attributed to the debt component. Directly attributable transaction costs are allocated between the liability conversion component and the liability debt component based on the allocation of the proceeds to each component.

E. Embedded derivatives:

The Group assesses the existence of an embedded derivative and whether it is required to be separated from a host contract when the Group first becomes party to the contract. Reassessment of the need to separate an embedded derivative only occurs if there is a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required.

F. Issue of a unit of securities:

The issue of a unit of securities involves the allocation of the proceeds received (before issue expenses) to the securities issued in the unit based on the following order: financial derivatives and other financial instruments measured at fair value in each period. Then fair value is determined for financial liabilities that are measured at amortized cost. The proceeds allocated to equity instruments are determined to be the residual amount. Issue costs are allocated to each component pro rata to the amounts determined for each component in the unit.

G. Put option granted to non-controlling interests:

When the Group grants non-controlling interests a put option to sell part or all of their interests in a subsidiary during a certain period, on the date of grant, the non-controlling interests are classified as a financial liability under redeemable non-controlling interests.

The Group remeasures the financial liability at the end of each reporting period based on the estimated present value of the consideration to be transferred upon the exercise of the put option. If the Group has present ownership of the non-controlling interests, these non-controlling interests are accounted for as if they are held by the Group and changes in the amount of the liability are carried to profit or loss. If the Group does not have present ownership, the interests are accounted for using the partial recognition method. Accordingly, a portion of net profit attributable to non-controlling interests is still allocated to profit or loss but at the end of the reporting period the non-controlling interests are reclassified as a financial liability. The difference between non-controlling interests at the end of the reporting period and the present value of the liability is recognized directly in equity of the Group, under "Adjustment to redeemable non-controlling interests". If the option is exercised in subsequent periods, the consideration paid upon exercise is treated as settlement of the liability. If the option expires, the liability is settled and it is a portion of the investment in the subsidiary disposed of, without loss of control therein.

As of December 31, 2016, there are no redeemable non-controlling interests which are subject to immediate exercise.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

The following table provides a reconciliation of the redeemable non-controlling interests:

January 1, 2016	\$18,751
Net income attributable to redeemable non-controlling interest	2,124
Share-based compensation attributable to redeemable non-controlling interest	215
Change in redeemable non-controlling interest to redemption value	715
Increase in redeemable non-controlling interest as part of acquisitions	29,174
Increase in redeemable non-controlling interest due to change in ownership in subsidiaries	292
Dividend in redeemable non-controlling interest	(1,537)
Foreign currency translation adjustments	(105)
December 31, 2016	\$49,629

H. Derecognition of financial instruments:

i. Financial assets:

A financial asset is derecognized when the contractual rights to the cash flows from the financial asset expire or the Group has transferred its contractual rights to receive cash flows from the financial asset or assumes an obligation to pay the cash flows in full without material delay to a third party, and in addition it has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A transaction involving factoring of accounts receivable and credit card vouchers is derecognized when the abovementioned conditions are met.

If the Group transfers its rights to receive cash flows from an asset and neither transfer nor retains substantially all the risks and rewards of the asset nor transfers control of the asset, a new asset is recognized to the extent of the Group's continuing involvement in the asset. When continuing involvement takes the form of guaranteeing the transferred

asset, the extent of the continuing involvement is the lower of the original carrying amount of the asset and the maximum amount of consideration received that the Company could be required to repay. As of December 31, 2016, the Group has no open factoring transactions.

ii.

Financial liabilities:

A financial liability is derecognized when it is extinguished, that is when the obligation is discharged or cancelled or expires. A financial liability is extinguished when the debtor (the Group) discharges the liability by paying in cash, other financial assets, goods or services or is legally released from the liability.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

I. Impairment of financial assets:

The Group assesses at the end of each reporting period whether there is any objective evidence of impairment of a financial asset or group of financial assets as follows:

i. Financial assets carried at amortized cost:

Objective evidence of impairment exists when one or more events that have occurred after initial recognition of the asset have a negative impact on the estimated future cash flows. The amount of the loss recorded in profit or loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not yet been incurred) discounted at the financial asset's original effective interest rate. If the financial asset has a variable interest rate, the discount rate is the current effective interest rate. In a subsequent period, the amount of the impairment loss is reversed if the recovery of the asset can be related objectively to an event occurring after the impairment was recognized. The amount of the reversal, up to the amount of any previous impairment, is recorded in profit or loss.

ii. Available-for-sale financial assets:

For equity instruments classified as available-for-sale financial assets, evidence of impairment includes a significant or prolonged decline in the fair value of the asset below its cost and evaluation of changes in the technological, economic or legal environment or in the market in which the issuer of the instrument operates. The determination of a significant or prolonged impairment depends on the circumstances at each reporting date. In making such a determination, historical volatility in fair value is considered, as well as a decline in fair value of 20% or more, or a decline in fair value whose duration is six months or more. Where there is evidence of impairment, the cumulative loss recorded in other comprehensive income is reclassified to profit or loss. In subsequent periods, any reversal of the impairment loss is recognized in other comprehensive income.

During 2015 and 2016 the Company did not recognize an impairment charge over its investments in available-for-sale marketable securities.

J. Extinguishing financial liabilities with equity instruments:

Equity instruments issued to replace a debt are measured at the fair value of the equity instruments issued if their fair value can be reliably measured. If their fair value cannot be reliably measured, the equity instruments are measured based on the fair value of the financial liability extinguished on the date of extinguishment. The difference between the carrying amount of the financial liability extinguished and the fair value of the equity instruments issued is recognized in profit or loss.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

22) Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurement is based on the assumption that the transaction will take place in the asset's or the liability's principal market, or in the absence of a principal market, in the most advantageous market.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. Fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use. The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs. All assets and liabilities measured at fair value or for which fair value is disclosed are categorized into levels within the fair value hierarchy based on the lowest level input that is significant to the entire fair value measurement:

Level 1 -quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 -inputs other than quoted prices included within Level 1 that are observable directly or indirectly.

Level 3 - inputs that are not based on observable market data (valuation techniques which use inputs that are not based on observable market data).

Assets and liabilities measured at fair value on a recurring basis are comprised of marketable securities, foreign currency forward contracts and contingent consideration of acquisitions (see Note 6).

23) Treasury shares:

Company shares held by the Company and/or subsidiaries are recognized at cost of purchase and presented as a deduction from equity. Any gain or loss arising from a purchase, sale, issue or cancellation of treasury shares is recognized directly in equity.

24)

Provisions

A provision in accordance with IAS 37 is recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. When the Group expects part or all of the expense to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense is recognized in the statement of profit or loss net of any reimbursement.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Following are the types of provisions included in the financial statements:

i. Legal claims

A provision for claims is recognized when the Group has a present legal or constructive obligation as a result of a past event, it is more likely than not that an outflow of resources embodying economic benefits will be required by the Group to settle the obligation and a reliable estimate can be made of the amount of the obligation.

ii. Contingent liability recognized in a business combination

A contingent liability in a business combination is measured at fair value upon initial recognition. In subsequent periods, it is measured at the higher of the amount initially recognized less, when appropriate, cumulative amortization, and the amount that would be recognized at the end of the reporting period in accordance with IAS 37.

25) Combination of businesses under common control

A business combination involving business entities under common control is a business combination whereby all of the combining business entities are ultimately controlled by the same party or parties, both before and after the business combination, and that control is not transitory. This refers in particular to transactions such as a transfer of companies or ventures between individual companies within a capital group, or a merger of a parent company with its subsidiary.

The effects of combinations of businesses under common control are accounted for by the Group by the pooling of interests method, assuming that: assets and liabilities of the combining business entities are measured at their carrying values as disclosed in the Group's consolidated financial statements; merger-related transaction costs are expensed in the income statement (financial expenses); mutual balances of accounts receivable/payable are eliminated; any difference between the purchase price paid/transferred and the value of net assets acquired (at their carrying values

disclosed in the consolidated financial statements) shall be recognized in equity of the acquirer (such amounts recognized in equity are not included in reserve capital, and therefore they are not distributable).

On August 18, 2015 (the “Acquisition Date”), Sapiens consummated the acquisition from Asseco of all issued and outstanding shares of Insseco Sp. Z O.O. (“Insseco”). Asseco is the ultimate parent company of Sapiens, through Asseco’s holdings in Formula, which is the direct parent company of Sapiens. Insseco is a newly established company into which Asseco had transferred all of its Polish insurance employees, certain fixed assets, certain customer contracts and certain software, including intellectual property rights. Insseco has an established presence in the Polish insurance market, and services major insurance customers in Poland, including top tier insurance carriers

The acquisition of Insseco from Asseco, is a transaction between entities under common control, and therefore accounted for under the pooling of interest method. As the common control commenced on December 23, 2014, the balance sheets as of December 31, 2014 of Sapiens and, as such, of Formula were adjusted to reflect the carrying amounts combination between Sapiens and Insseco. The results of Sapiens and of Formula for the twelve-month period ended December 31, 2015 were also adjusted to reflect the combination with Insseco, accordingly.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Under the pooling-of-interests method, the equity accounts of the combining entities are combined and the difference between the consideration paid and the net assets acquired is reflected as an equity transaction (i.e., distribution to parent company). As opposed to the purchase method of accounting, no intangible assets are recognized in the transaction, other than those existed in the combining entities and no goodwill is recognized as a result of the combination.

The application of the pooling-of-interests method with respect to the acquisition of Insseco increased the total assets, liabilities and equity as of December 31, 2014 by \$ 4,387, \$ 2,290, and \$ 2,097, respectively. Revenues, pretax income and net income of Insseco for the twelve month period ended December 31, 2015, which are included in the consolidated statements of profit or loss amounted to \$ 10,516, \$ 1,324 and \$ 1,165, respectively. (see additional information in Note 4(ii)(a)).

26) Derivative financial instruments designated as hedges:

A material portion of the Group's revenues, expenses and earnings is exposed to changes in foreign exchange rates. Depending on market conditions, foreign exchange risk is also managed through the use of derivative financial instruments. These financial instruments serve to protect net income against the impact of the translation into U.S. dollars of certain foreign exchange-denominated transactions. Therefore, The Group enters into contracts for derivative financial instruments such as forward currency contracts to hedge risks associated with foreign exchange rate and interest rate fluctuations.

The derivative instruments primarily hedge or offset exposures to Euro, Japanese Yen and New Israeli Shekel ("NIS") exchange rate fluctuations.

Any gains or losses arising from changes in the fair values of derivatives that do not qualify for hedge accounting are recorded immediately in profit or loss.

Hedges qualify for hedge accounting, among others, when at inception of the hedging relationship there is a formal designation and documentation of the hedging relationship and of the Group's risk management objective and strategy for undertaking the hedge. Hedges are assessed on an ongoing basis to determine whether they are highly effective during the reporting period for which the hedge is designated. Hedges are accounted for as follows:

i.

Fair value hedges:

The change in the fair value of the derivative (the hedging item) and the hedged item is recognized in profit or loss. For fair value hedges relating to hedged items carried at amortized cost, the adjustment to carrying value is amortized to profit or loss over the remaining term to maturity. Any adjustment of the hedged financial instrument for which the effective interest rate method is used, is recognized in profit or loss. If the hedged item is derecognized, the unamortized changes to fair value are recognized immediately in profit or loss.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

ii. Cash flow hedges:

The effective portion of the change in the fair value of the hedging instrument is recognized in other comprehensive income (loss) while any ineffective portion is recognized immediately in profit or loss.

Amounts recognized as other comprehensive income (loss) are reclassified to profit or loss when the hedged transaction affects profit or loss, such as when the hedged income or expense is recognized or when a forecasted transaction occurs. Where the hedged item is a non-financial asset or liability, their cost also includes the gain (loss) from the hedging instrument.

If the forecast transaction or firm commitment is no longer expected to occur, amounts previously recognized in other comprehensive income (loss) are reclassified to profit or loss. If the hedging instrument expires or is sold, terminated or exercised, or if its designation as a hedge is revoked, amounts previously recognized in other comprehensive income (loss) remain in other comprehensive income (loss) until the forecast transaction or firm commitment occurs.

Hedge accounting is not applied to financial derivatives used as an economic hedge of financial assets and liabilities. At December 31, 2015 and 2016, the Group did not have any cash flow hedges.

27) Employee benefit liabilities:

The Group has several employee benefit plans:

i. Short-term employee benefits:

Short-term employee benefits are benefits that are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services. These benefits include salaries, paid annual leave, paid sick leave, recreation and social security contributions and are recognized as expenses as the services are rendered. A liability in respect of a cash bonus or a profit-sharing plan is recognized when the Group has a legal or constructive obligation to make such payment as a result of past service rendered by an employee and a reliable estimate of the amount can be made.

ii. Post-employment benefits:

The plans are normally financed by contributions to insurance companies and classified as defined contribution plans or as defined benefit plans.

Formula's and its Israeli investees' has defined with respect to their Israeli employees contribution plans pursuant to section 14 of Israel's Severance Pay Law, 1963 (the "Severance Pay Law") under which the Group pays fixed contributions and will have no legal or constructive obligation to pay further contributions if the fund does not hold sufficient amounts to pay all employee benefits relating to employee service in the current and prior periods. Contributions to the defined contribution plan in respect of severance or retirement pay are recognized as an expense when contributed concurrently with performance of the employee's services.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Formula's and its Israeli investees' also operates a defined benefit plan in respect of severance pay to their Israeli employees pursuant to the Severance Pay Law. According to the Law, employees are entitled to severance pay upon dismissal or retirement. The liability for termination of employment is measured using the projected unit credit method. The actuarial assumptions include rates of employee turnover and future salary increases based on the estimated timing of payment. The amounts are presented based on discounted expected future cash flows using a discount rate determined by reference to market yields at the reporting date on high quality corporate bonds that are linked to Israel's Consumer Price Index with a term that is consistent with the estimated term of the severance pay obligation.

In respect of its severance pay obligation to certain of its employees, the Group makes current deposits in pension funds and insurance companies ("the plan assets"). Plan assets comprise assets held by a long-term employee benefit fund or qualifying insurance policies. Plan assets are not available to the Group's own creditors and cannot be returned directly to the Group.

The liability for employee benefits shown in the statement of financial position reflects the present value of the defined benefit obligation less the fair value of the plan assets.

Remeasurements of the net liability are recognized in other comprehensive income in the period in which they occur.

Total expenses in respect of employee benefit liabilities for the years 2015 and 2016 were \$ 13,555 and \$ 14,470, respectively.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

28)

Earnings per share:

Earnings per share are calculated by dividing the net income attributable to equity holders of the Company by the weighted number of Ordinary shares outstanding during the period. Potential Ordinary shares are included in the computation of diluted earnings per share when their conversion decreases earnings per share from continuing operations. Potential Ordinary shares that are converted during the period are included in diluted earnings per share only until the conversion date and from that date in basic earnings per share. The Company's share of earnings of investees is included based on its share of earnings per share of the investees multiplied by the number of shares held by the Company.

29)

Concentration of credit risk

Financial instruments that potentially subject the Group to concentrations of credit risk consist principally of cash and cash equivalents, short-term bank deposits, restricted cash, trade receivables, marketable securities and foreign currency derivative contracts.

The majority of the Group's cash and cash equivalents, bank deposits and marketable securities are invested with major banks in Israel, the United States and Europe. Such cash and cash equivalents and short-term deposits in the United States may be in excess of insured limits and are not insured in other jurisdictions. Management believes that these financial instruments are held in financial institutions with high credit standing, and accordingly, minimal credit risk exists with respect to these investments.

The Group's marketable securities include investments in commercial and government bonds and foreign banks. The Group's marketable securities are considered to be highly liquid and have a high credit standing. In addition, managements of the Group's investees limit the amount that may be invested in any one type of investment or issuer, thereby reducing credit risk concentrations and consider their portfolios in foreign banks to be well-diversified (also refer to Note 5).

The Group's trade receivables are generally derived from sales to large organizations located mainly in Israel, North America, Europe and Asia Pacific. The Group performs ongoing credit evaluations of its customers and to date has not experienced any material losses. In certain circumstances, Formula and its investees may require letters of credit, other collateral or additional guarantees. From time to time, the Group sells certain of its accounts receivable to financial institutions, within the normal course of business.

The Group maintains an allowance for doubtful accounts receivable based upon management's experience and estimate of collectability of each outstanding invoice. The allowance for doubtful accounts is determined with respect to specific debts that are doubtful of collection. The bad debt expenses, net for the years ended December 31, 2015 and 2016 was \$ 747 and \$ 652 respectively. The risk of collection associated with accounts receivable is mitigated by the diversity and number of customers.

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NOTE 2:- SIGNIFICANT ACCOUNTING POLICIES (Cont.)

From time to time, the Group transfers financial assets by factoring of accounts receivable and credit card vouchers to a financial institution IAS-39 establishes a standard for determining when a transfer of financial assets should be accounted for as a sale. Certain underlying conditions must be met for the transfer of financial assets to qualify for accounting as a sale. All sales of receivable were closed during the years and as so there are no outstanding sales of receivables as of December 31, 2015 and 2016.

The agreements pursuant to which the Company sells certain of its trade receivables are structured such that the Company (i) transfers the proprietary rights in the receivable from the Company to the financial institution; (ii) legally isolates the receivable from the Company's other assets, and presumptively puts the receivable beyond the legal reach of the Company and its creditors, even in bankruptcy or other receivership; (iii) confers on the financial institution the right to pledge or exchange the receivable; and (iv) eliminates the Company's effective control over the receivable, in the sense that the Company is not entitled and shall not be obligated to repurchase the receivable other than in case of failure by the Company to fulfill its commercial obligation.

From time to time, the Group enters into foreign exchange forward and option contracts intended to protect against the changes in value of forecasted non-dollar currency cash flows. These derivative instruments are designed to offset a portion of the Company's non-dollar currency exposure (see Note 2 (26) above).

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NOTE 3:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION

1. IFRS 15, "Revenue from Contracts with Customers":

IFRS 15 ("the new Standard") was issued by the IASB in May 2014. The new Standard replaces IAS 18, "Revenue", IAS 11, "Construction Contracts", IFRIC 13, "Customer Loyalty Programs", IFRIC 15, "Agreements for the Construction of Real Estate", IFRIC 18, "Transfers of Assets from Customers" and SIC-31, "Revenue - Barter Transactions Involving Advertising Services".

The new Standard introduces a five-step model that will apply to revenue earned from contracts with customers:

Step 1: Identify the contract with a customer, including reference to contract combination and accounting for contract modifications.

Step 2: Identify the separate performance obligations in the contract

Step 3: Determine the transaction price, including reference to variable consideration, financing components that are significant to the contract, non-cash consideration and any consideration payable to the customer.

Step 4: Allocate the transaction price to the separate performance obligations on a relative stand-alone selling price basis using observable information, if it is available, or using estimates and assessments.

Step 5: Recognize revenue when a performance obligation is satisfied, either at a point in time or over time.

The Company is evaluating the possible effects of the new Standard. However, at this stage, the Company is unable to quantify the impact on the financial statements.

The new Standard is to be applied retrospectively for annual periods beginning on January 1, 2018. Early adoption is permitted. At this stage, the Group does not intend to adopt IFRS 15 early.

The new Standard allows the option of modified retrospective adoption with certain reliefs according to which the new Standard will be applied to existing contracts from the initial period of adoption and thereafter with no restatement of comparative data. Under this option, the Group will recognize the cumulative effect of the initial adoption of the new Standard as an adjustment to the opening balance of retained earnings (or another component of equity, as applicable) as of the date of initial application. Alternatively, the new Standard permits full retrospective adoption with certain reliefs.

At this stage, the Group is evaluating the different options for adoption of the new Standard.

2. IFRS 9, "Financial Instruments"

In July 2014, the IASB issued the final and complete version of IFRS 9, "Financial Instruments" ("IFRS 9"), which replaces IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 mainly focuses on the classification and measurement of financial assets and it applies to all assets in the scope of IAS 39.

According to IFRS 9, all financial assets are measured at fair value upon initial recognition. In subsequent periods, debt instruments are measured at amortized cost only if both of the following conditions are met:

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NOTE 3:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION (Cont.)

the asset is held within a business model whose objective is to hold assets in order to collect the contractual cash flows.
the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Subsequent measurement of all other debt instruments and financial assets should be at fair value. IFRS 9 establishes a distinction between debt instruments to be measured at fair value through profit or loss and debt instruments to be measured at fair value through other comprehensive income.

Financial assets that are equity instruments should be measured in subsequent periods at fair value and the changes recognized in profit or loss or in other comprehensive income (loss), in accordance with the election by the Company on an instrument-by-instrument basis. If equity instruments are held for trading, they should be measured at fair value through profit or loss.

According to IFRS 9, the provisions of IAS 39 will continue to apply to derecognition and to financial liabilities for which the fair value option has not been elected.

According to IFRS 9, changes in fair value s of financial liabilities which are attributable to the change in credit risk should be presented in other comprehensive income. All other changes in fair value should be presented in profit or loss.

IFRS 9 also prescribes new hedge accounting requirements.

IFRS 9 is to be applied for annual periods beginning on January 1, 2018. Early adoption is permitted.

The Group believes that the amendments to IFRS 9 are not expected to have a material impact on the consolidated financial statements, but at the end of the reporting period the impact analysis has not yet been completed.

3. Amendments to IFRS 10 and IAS 28 regarding sale or transfer of assets between an investor and its associate or joint venture:

In September 2014, the IASB issued amendments to IFRS 10 and IAS 28 ("the amendments") regarding the accounting treatment of the sale or transfer of assets (an asset, a group of assets or a subsidiary) between an investor and its associate or joint venture. According to the amendments, when the investor loses control of a subsidiary or a group of assets that are not a business in a transaction with its associate or joint venture, the gain will be partially eliminated so that the gain to be recognized is the gain from the sale to the other investors in the associate or joint venture. According to the amendments, if the remaining rights held by the investor represent a financial asset as defined in IFRS 9, the gain will be recognized in full. If the transaction with an associate or joint venture involves loss of control of a subsidiary or a group of assets that are a business, the gain will be recognized in full. The amendments are to be applied prospectively. A mandatory effective date has not yet been determined by the IASB but early adoption is permitted.

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NOTE 3:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION (Cont.)

4. Amendments to IAS 7, "Statement of Cash Flows", regarding additional disclosures of financial liabilities:

In January 2016, the IASB issued amendments to IAS 7, "Statement of Cash Flows", ("the amendments") which require additional disclosures regarding financial liabilities. The amendments require disclosure of the changes between the opening balance and the closing balance of financial liabilities, including changes from cash flows, changes arising from obtaining or losing control of subsidiaries, the effect of changes in foreign exchange rates and changes in fair value.

The amendments are effective for annual periods beginning on or after January 1, 2017. Comparative information for periods prior to the effective date of the amendments is not required. Early application is permitted. The Company will include the necessary disclosures in the financial statements when applicable.

5. IFRS 16, "Leases":

In January 2016, the IASB issued IFRS 16, "Leases" ("the new Standard"). According to the new Standard, a lease is a contract, or part of a contract, that conveys the right to use an asset for a period of time in exchange for consideration.

According to the new Standard:

Lessees are required to recognize an asset and a corresponding liability in the statement of financial position in respect of all leases (except in certain cases) similar to the accounting treatment of finance leases according to the existing IAS 17, "Leases".

Lessees are required to initially recognize a lease liability for the obligation to make lease payments and a corresponding right-of-use asset. Lessees will also recognize interest and depreciation expense separately.

Variable lease payments that are not dependent on changes in the Consumer Price Index ("CPI") or interest rates, but are based on performance or use (such as a percentage of revenues) are recognized as an expense by the lessees as incurred and recognized as income by the lessors as earned.

In the event of change in variable lease payments that are CPI-linked, lessees are required to remeasure the lease liability and the effect of the remeasurement is an adjustment to the carrying amount of the right-of-use asset.

The new Standard includes two exceptions according to which lessees are permitted to elect to apply a method similar to the current accounting treatment for operating leases. These exceptions are leases for which the underlying asset is of low value and leases with a term of up to one year.

The accounting treatment by lessors remains substantially unchanged, namely classification of a lease as a finance lease or an operating lease.

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NOTE 3:- DISCLOSURE OF NEW STANDARDS IN THE PERIOD PRIOR TO THEIR ADOPTION (Cont.)

The new Standard is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted provided that IFRS 15, "Revenue from Contracts with Customers", is applied concurrently. For leases existing at the date of transition, the new Standard permits lessees to use either a full retrospective approach, or a modified retrospective approach, with certain transition relief whereby restatement of comparative data is not required.

The Company is evaluating the possible effects of the new Standard. However, at this stage, the Company is unable to quantify the impact on the financial statements.

NOTE 4:- BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS

i. Formula

a. Acquisition of TSG IT Advanced Systems Ltd

On May 9, 2016, Formula and Israel Aerospace Industries (IAI) concluded the joint purchase of TSG – a subsidiary and the military arm of Ness Technologies, engaged in the fields of command and control systems, intelligence, homeland security and cyber security. The total purchase price in the transaction amounted to \$ 51,532 in cash, with each of IAI and Formula acquiring 50% of TSG for \$ 25,766. TSG is a leading provider of core command and control systems to Israel's defense organization, including the Israeli Defense Forces and the Israeli Police.

As TSG is jointly controlled by both Formula and IAI, its results of operations are reflected in the Company's profit or loss using the equity method of accounting commencing May 9, 2016.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed by the Company at the date of acquisition:

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Net Assets	\$1,824
Intangible assets	13,693
Backlog	2,221
Deferred tax liability	(3,979)
Dividend preference derivative	2,140
Goodwill	9,867
Total assets acquired net of acquired cash	\$25,766

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

b. Investment in Sapiens

On November 19, 2013, Sapiens completed a follow-on public offering of its ordinary shares on the NASDAQ. Sapiens issued 6,497,400 shares at a price of \$ 6.25 per share before issuance expenses. Total net proceeds from the issuance amounted to approximately \$ 37,791. As a result of the offering, Formula's interest in Sapiens' outstanding common shares was diluted from 56.8% to 48.6% and due to the loss of control in Sapiens in accordance with IFRS 10, the Company started applying the equity method of accounting to reflect its investment in Sapiens. The gain recognized in relation of Formula's interest in in Sapiens' outstanding common shares, diluting to 48.6%, amounted to \$ 61,164 and is presented in the income statement as equity in gains of affiliated companies, net. The fair value of the retained investment in Sapiens was measured according to Sapiens' share price on November 19, 2013 of \$ 7.09 per share.

From August 21, 2014 through December 23, 2014, Formula purchased an aggregate of 1,545,802 common shares of Sapiens through broker-initiated and private transactions for an aggregate purchase price of \$ 11,908, pursuant to which Formula's holdings in Sapiens were increased to 50.2%. As a result of Formula's gaining control in Sapiens, Formula's investment in Sapiens was consolidated in Formula's closing balances as of December 31, 2014. The gain recognized in relation to the consolidation of Sapiens and the related re-measurement of the investment to fair value amounted to \$ 3,413 and is presented in the income statement as equity in gains of affiliated companies, net.

The acquisition was accounted for using the purchase method. The results of operations of Sapiens have been consolidated commencing as of December 23, 2014.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed, with reference to the acquisition as of December 23, 2014:

Net assets	\$ 170,834
Customer relationships	20,707

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Developed and acquired Technology	19,066
Backlog and deferred revenues	3,351
Deferred revenues	513
Deferred tax liability, net	(11,972)
Non-controlling interests	(173,565)
Goodwill	145,730
Net assets acquired	\$ 174,664

In performing the purchase price allocation, management considered, among other factors, analyses of historical financial performance, highest and best use of the acquired assets and estimates of future performance of Sapiens' business. In performing the purchase price allocation, the fair value of intangible assets such as customer relationship was determined based on the income approach and core technology was valued using the relief from royalty method.

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

ii. Sapiens

a. Acquisition of Insseco

On August 18, 2015 (the “acquisition date”), Sapiens completed the acquisition from Asseco of all issued and outstanding shares of Insseco. Asseco is the ultimate parent company of Sapiens, through holding in Formula, which is the direct parent company of Sapiens. Insseco is a newly established company into which Asseco had transferred all of its Polish insurance employees, certain fixed assets, certain customer contracts and certain software including intellectual property rights. Insseco has a team of approximately 140 insurance professionals and an established presence in the Polish insurance market, and services major insurance customers in Poland, including top tier insurance carriers.

Sapiens paid the acquisition consideration in cash, consisting of 34,300 Polish Zloty or approximately \$ 9,100. In addition, the transaction consideration includes upside or downside performance based payments relating to achievements of revenue goals and profitability over the next five years. If the aggregate revenues generated by Insseco from its activity from July 1, 2015 through June 30, 2020 exceed 90,000 Polish Zloty or approximately \$ 23,800, Asseco shall be entitled to receive additional amounts ranging from 3% to 15% of the excess amount of the respective revenues. If the aggregate revenues generated by Insseco for the period from July 1, 2015 through June 30, 2018 are below 84,000 Polish Zloty or \$ 22,200, the seller shall pay Sapiens an amount equal to 35% of the deficiency below such amount. In addition, the amounts payable to Asseco may be adjusted upwards or downwards as a result of changes in the profitability of a specific account that Sapiens acquired as part of the acquisition. The estimated fair value of the contingent payments as of December 31, 2016 is \$ 1,000.

The acquisition of Insseco from Asseco, which was as of the acquisition date the ultimate parent company of Sapiens, is a transaction between entities under common control, and therefore accounted for under the pooling of interest. Under the pooling-of-interests method, combination between two businesses under common control is accounted for at carrying amounts with retrospective adjustment of prior period financial statements, therefore balance sheet as of December 31, 2014 of Sapiens and as such of Formula were adjusted to reflect the carrying amounts combination between Sapiens and Insseco. The results of Sapiens for the twelve-month period ended December 31, 2015 were also adjusted to reflect the combination with Insseco, accordingly.

Under the pooling-of-interests method, the equity accounts of the combining entities are combined and the difference between the consideration paid and the net assets acquired is reflected as an equity transaction (i.e., distribution to parent company). As opposed to the purchase method of accounting, no intangible assets are recognized in the transaction, other than those existed in the combining entities and no goodwill is recognized as a result of the combination. The application of the pooling-of-interests method with respect to the acquisition of Insseco increased the total assets, liabilities and equity as of December 31, 2014 by \$ 4,387, \$ 2,290, and \$ 2,097, respectively. Revenues, pretax income and net income of Insseco for the twelve month period ended December 31, 2015, which are included in the consolidated statements of income amounted to \$ 10,516, \$ 1,324 and \$ 578, respectively.

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NOTE 4:- BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

b. Acquisition of Knowledge Partners International

On August 1, 2014, Sapiens completed the acquisition of all of the outstanding shares of Knowledge Partners International (KPI), a pioneer and recognized leader in decision management consultancy, services and training, in consideration of \$ 2,380, composed of the following:

Cash	\$2,203
Share consideration ⁽¹⁾	177
Net assets acquired	\$2,380

(1) Sapiens issued 57,000 shares of its subsidiary, Sapiens Software Solution (Decision) Ltd, reflecting 3% of the subsidiary's outstanding shares. According to the agreement, the sellers will have the right to sell their minority interests to the Company during the period commencing on the date that is 48 months following the acquisition date, and the Company will have a corresponding call option.

Sapiens issued additional 88,500 restricted shares of its subsidiary, Sapiens Software Solution (Decision) Ltd, expensed over a vesting period of three years commencing on the acquisition date.

c. Acquisition of Ibexi Solution Private Limited

On May 6, 2015, Sapiens completed the agreement to acquire all of outstanding shares of Ibexi Solution Private Limited (Ibexi), an India-based provider of insurance business and technology solutions, in total consideration of \$ 4,764 including a contingent obligation valued at \$ 949 on the acquisition date. As of December 31, 2016, the estimated fair value of the contingent payment is \$1,680. In addition, an amount of approximately \$ 1,900 is subject to continued employment and therefore not part of the purchase price, but is recognized over the service period. Acquisition related costs were immaterial

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed, with reference to the acquisition as of the acquisition date:

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

Net assets	\$1,105
Intangible assets	1,315
Goodwill	2,344
Net assets acquired	\$4,764

d. Acquisition of Maximum Processing Inc.

On May 26, 2016, Sapiens entered into an agreement to purchase the entire share capital of Maximum Processing Inc.'s (MaxPro) for a consideration of \$ 4,278 (of which \$1,490 was deposited at closing in escrow)). In addition, the seller has performance based payments relating to achievements of revenue and profitability targets over three years (2016-2018) of up to \$ 2,500. Such payments are also subject to continued employment and therefore, not part of the purchase price. MaxPro specializes in providing business and technology solutions across the insurance industry. Acquisition related costs were immaterial.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed, with reference to the acquisition as of the acquisition date:

Net assets	\$(240)
Intangible assets	1,859
Goodwill	2,659
Net assets acquired	\$4,278

e. Acquisition of 4Sight Business Intelligence Inc

On June 7, 2016, Sapiens entered into an agreement to purchase 100% of the total outstanding shares of 4Sight Business Intelligence Inc. (4Sight). 4sight's system provides analytics software for the insurance industry. Sapiens paid the acquisition consideration in cash, consisting of \$ 330. In addition, the seller has performance based payments relating to achievements of revenue and profitability targets over three years (2016-2018) of up to \$ 2,200. Such

payments are also subject to continued employment and therefore, are not part of the purchase price. Acquisition related costs were immaterial

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed, with reference to the acquisition as of the acquisition date:

Net assets	\$(145)
Intangible assets	279
Deferred taxes	(112)
Goodwill	308
Net assets acquired	\$330

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NOTE 4:- BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

iii. Magic

a. Acquisition of Formula Telecom Solutions Ltd. (FTS)

On October 1, 2014 Magic acquired the entire share interests in Formula Telecom Solutions Ltd. (FTS), an Israel-based software vendor, for a total consideration of \$ 5,800. FTS specializes in the development, sale, service and support of Business Support Systems (BSS), including convergent charging, billing, customer management, policy control and payment software solutions for the telecommunications industry. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The results of operations were included in the consolidated financial statements of the Company commencing October 1, 2014.

The following table summarizes the estimated fair values of the assets acquired and liabilities at the date of acquisition:

Net Assets	\$(57)
Intangible assets	2,951
Goodwill	2,906
Total assets acquired	\$5,800

b. Acquisition of Comblack IT Ltd

On April 14, 2015 Magic acquired a 70% interest in Comblack IT Ltd. ("Comblack"), an Israeli-based company that specializes in software professional and outsourced management services mainly for mainframes and complex large-scale environments, for a total consideration of \$1,821, of which \$ 1,523 was paid upon closing and \$ 298 which was payable contingent upon the acquired business meeting certain operational targets in 2015. Magic and the seller hold mutual Call and Put options respectively for the remaining 30% interest in Comblack. As a result of the Put option, Magic recorded redeemable non-controlling interest in the amount of \$ 989 on the acquisition date. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The results of operations were included in the consolidated financial statements of the Company commencing April 1, 2015.

The following table summarizes the estimated fair values of the assets acquired and liabilities at the date of acquisition:

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

Net Assets, excluding cash acquired	\$(405)
Redeemable non-controlling interests	(989)
Intangible assets	1,249
Goodwill	1,966

Total assets acquired net of acquired cash \$ 1,821

In March 2016, Magic paid the seller the remaining contingent payments for meeting the 2015 operational targets.

c. Acquisition of Infinigy Solutions LLC

On June 30, 2015 Magic acquired a 70% interest in Infinigy Solutions LLC ("Infinigy"), a US-based services company focused on expanding the development and implementation of technical solutions throughout the telecommunications industry with offices across the US, providing nationwide coverage and support for wireless engineering, deployment services, surveying, environmental service and project management, for a total consideration of \$ 6,527, of which \$ 5,600 was paid upon closing and \$ 927 is payable contingent upon the acquired business meeting certain operational targets in 2016 and 2017. Magic and the seller hold mutual Call and Put options respectively for the remaining 30% interest in Infinigy. As a result of the Put option, Magic recorded redeemable non-controlling interest in the amount of \$ 3,590. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The results of operations were included in the consolidated financial statements of the Company commencing July 1, 2015.

The following table summarizes the estimated fair values of the assets acquired and liabilities at the date of acquisition:

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Net Assets, excluding cash acquired	\$1,182
Redeemable non-controlling interests	(3,590)
Intangible assets	3,675
Goodwill	5,260
Total assets acquired net of acquired cash	\$6,527

In July 2016, Magic paid the seller \$ 534 with respect to the acquired business meeting certain of its 2016 operational targets. As of December 31, 2016 the contingent payment with respect to the acquired business meeting its 2017 operational target amounted to \$ 685.

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

d. Acquisition of Roshtov Software Industries Ltd

On July 11, 2016 Magic acquired a 60% interest in Roshtov Software Industries Ltd ("Roshtov"), an Israeli-based software company that is a market leader in Israel in patient record information systems, for a total cash consideration of \$ 20,550, which was paid upon closing. The purchaser and the seller hold mutual Call and Put options respectively for the remaining 40% interest in Roshtov. As a result of the Put option, Magic recorded redeemable non-controlling interest in the amount of \$ 14,012. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The results of operations were included in the consolidated financial statements of the Company commencing July 2016.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition ⁽¹⁾:

Net Assets, excluding cash acquired	\$ 15
Redeemable non-controlling interests	(14,012)
Intangible assets	22,439
Deferred tax liabilities	(5,610)
Goodwill	17,718
Total assets acquired net of acquired cash	\$20,550

(1) The estimated fair values of the tangible and intangible assets are provisional and are based on information that was available as of the acquisition date to estimate the fair value of these amounts. Magic's management believes the information provides a reasonable basis for estimating the fair values of these amounts, but is waiting for additional information necessary to finalize those fair values. Therefore, provisional measurements of fair value reflected are

subject to change. Magic expects to finalize the tangible and intangible assets valuation and complete the acquisition accounting as soon as practicable but no later than the measurement period.

e. Acquisition of in Shavit Software (2009) Ltd

On October 31, 2016 Magic acquired the entire share interests in Shavit Software (2009) Ltd., an Israeli-based company that specializes in software professional and outsourced management services, for a total consideration of \$ 6,836, of which \$ 4,699 was paid upon closing, \$ 1,633 (measured based on present value) was allocated to a deferred payment which is due in 2018 and \$ 504 is contingent upon the acquired business meeting certain operational targets in 2017, 2018 and 2019. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

The results of operations were included in the consolidated financial statements of the Company commencing November 1, 2016.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition (1):

Net Assets, excluding cash acquired	\$801
Intangible assets	4,215
Deferred tax liabilities	(1,053)
Goodwill	2,873
 Total assets acquired net of acquired cash	 \$6,836

(1) The estimated fair values of the tangible and intangible assets are provisional and are based on information that was available as of the acquisition date to estimate the fair value of these amounts. The Company's management believes the information provides a reasonable basis for estimating the fair values of these amounts, but is waiting for additional information necessary to finalize those fair values. Therefore, provisional measurements of fair value reflected are subject to change. The Company expects to finalize the tangible and intangible assets valuation and complete the acquisition accounting as soon as practicable but not later than the measurement period.

f. Other acquisitions by Magic in 2015 and 2016

During the years ended December 31, 2015 and 2016, Magic acquired additional activities whose influence on the financial statements of the Company was immaterial, for a total consideration of \$ 1,892 and \$ 8,884, respectively. In addition, during 2015, Magic increased its ownership interest in Complete Business Solutions from 96.3% to 100% and in CommIT Embedded Ltd. from 50.1% to 75%, for a total consideration of \$ 244 and \$ 1,412 (of which \$ 356 were paid in January 2016), respectively.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition (1):

Net Assets, excluding cash acquired	\$2,174
Non-controlling interests	(1,209)
Intangible assets	2,106
Deferred tax liabilities	(427)
Goodwill	6,240

Total assets acquired net of acquired cash \$8,884

(1) The estimated fair values of the tangible and intangible assets are provisional and are based on information that was available as of the acquisition date to estimate the fair value of these amounts. Magic's management believes the information provides a reasonable basis for estimating the fair values of these amounts, but is waiting for additional information necessary to finalize those fair values. Therefore, provisional measurements of fair value reflected are subject to change. Magic expects to finalize the tangible and intangible assets valuation and complete the acquisition accounting as soon as practicable but no later than the measurement period.

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NOTE 4:- BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

iv. Matrix

a. Acquisition of SeeV Solutions Ltd

During January 2015, Matrix acquired a 75% interest in SeeV Solutions Ltd from its former shareholders for NIS 4,875 (approximately \$ 1,232). In addition, the purchaser and the seller hold mutual Call and Put options respectively for the remaining 25% interest in the company valued at NIS 1,713 (approximately \$ 433). SeeV engages in permanent placement of employees in start-ups and high-tech companies.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition:

Net Assets	\$340
Redeemable non-controlling interests	(433)
Intangible assets	270
Deferred tax liabilities	(72)
Goodwill	1,127
Total assets acquired	\$1,232

b. Acquisition of Tiltan Systems Engineering Ltd

On April 1, 2015, Matrix acquired 64% interest in Tiltan Systems Engineering Ltd from its other shareholders (prior to the acquisition Matrix held a 36% interest in Tiltan share capital) for an amount of NIS 2,600 (approximately \$ 654). Following right after the acquisition Matrix holds the entire share capital of Tiltan and consequently recognized a loss of NIS 565 (approximately \$ 142) resulting from the fair value measurement of its investment in Tiltan. The excess of the purchase price over the estimated fair value of the assets acquired and liabilities assumed in a total of approximately NIS 4, 900 (approximately \$ 1,233), NIS 640 (approximately \$ 161) was allocated to deferred taxes, and the remaining balance was allocated to goodwill.

c. Acquisition of Hydus Inc

On April 1, 2015 Xtivia Inc (a wholly owned subsidiary of Matrix) completed the acquisition of the entire share capital of Hydus Inc for a total consideration of \$ 2,505 (net of acquired cash). Hydus Inc. is a U.S based consulting firm specializing in software services in the field of Enterprise Information Management (EIM). In addition, the sellers may be eligible for future consideration, valued at \$ 1,441 on the acquisition date (\$ 1,739 as of December 31, 2016), subject to obtaining accumulated operating income targets during three years (not exceeding Hydus operating income).

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition:

Net Assets	\$583
Intangible assets	580
Deferred tax liabilities	(203)
Goodwill	2,986
Total assets acquired	\$3,946

d. Acquisition of Ono Apps Ltd

On May 7, 2015, Matrix completed the acquisition of the entire share capital of Ono Apps Ltd., an Israeli based service provider specializing in mobile applications development services, for a total consideration of NIS 4,584 (approximately \$ 1,186). In addition, the sellers may be eligible for future consideration, valued at \$ 316 as of the acquisition date, subject to obtaining accumulated operating income targets during three years commencing on January 1, 2016 and not exceeding NIS 5,000 (approximately \$ 1,300). Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition:

Net Assets	\$86
Intangible assets	420

Deferred tax liabilities	(111)
Goodwill	1,107
Total assets acquired	\$1,502

e. Acquisition of Programa Logistics Systems Ltd

On March 30, 2016, Matrix acquired a 60% interest in Programa Logistics Systems Ltd., for a total consideration of NIS 7,295 (approximately \$ 1,937). In addition the sellers may be eligible for future consideration valued, on the acquisition date, at NIS 1,144 (\$ 304) which is contingent upon the acquired business meeting certain operational targets in the years 2016-2018. Programa, an Israeli company, is a provider of advisory services and design and development of solutions in supply chain, production and logistics. Matrix and the seller hold mutual Call and Put options respectively for the remaining 40% interest in Programa. As a result of the Put option, Matrix recorded redeemable non-controlling interest of \$ 2,471 on the acquisition date. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition:

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

Net Assets	\$267
Redeemable non-controlling interests	(2,471)
Intangible assets	1,216
Goodwill	3,229
 Total assets acquired	 \$2,241

As of December 31, 2016, Programa's redeemable non-controlling interest amount to \$ 2,411.

f. Acquisition of Network Infrastructure Technologies Inc

On October 4, 2016, Exzac Inc, a wholly owned subsidiary of Matrix, completed the acquisition of a 60% interest in Network Infrastructure Technologies Inc. ("NIT") for a cash consideration of \$ 6,750. In addition the sellers may be eligible for future consideration valued, on the acquisition date, at \$ 743 which is contingent upon the acquired business meeting certain operational targets in the years 2017-2019. NIT, a U.S based company, mainly provides IT help desk services to the Healthcare and Finance sectors for managing their information systems. Matrix and the seller hold mutual Call and Put options respectively for the remaining 40% interest in NIT. As a result of the Put option, Matrix recorded redeemable non-controlling interest of \$ 7,263 on the acquisition date. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition:

Net Assets	\$977
Redeemable non-controlling interests	(7,263)
Intangible assets	3,512
Deferred tax liabilities	(1,405)
Goodwill	11,672

Total assets acquired \$7,493

g. Acquisition of Second to none solutions Inc.

On November 8, 2016, Xtivia Technologies Inc., a wholly owned subsidiary of Matrix, completed the acquisition of a 55% interest in Second to none solutions Inc. ("Stons") for a consideration of \$ 287 paid in cash. Stons is a certified distributor of IBM products to U.S federal and enterprise customers. Matrix and the seller hold mutual Call and Put options respectively for the remaining 45% interest in Stons. As a result of the Put option, Matrix recorded redeemable non-controlling interest of \$ 2,184 on the acquisition date. In addition the sellers may be eligible for future consideration valued, on the acquisition date, at \$ 514 which is contingent upon the acquired business meeting certain operational targets in the years 2017-2019. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

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NOTE 4:- BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition(1):

Intangible assets	\$917
Redeemable non-controlling interests	(2,184)
Deferred tax liabilities	(314)
Goodwill	2,382
 Total assets acquired	 \$801

(1) The estimated fair values of the tangible and intangible assets are provisional and are based on information that was available as of the acquisition date to estimate the fair value of these amounts. Matrix's management believes the information provides a reasonable basis for estimating the fair values of these amounts, but is waiting for additional information necessary to finalize those fair values. Therefore, provisional measurements of fair value reflected are subject to change. Matrix expects to finalize the tangible and intangible assets valuation and complete the acquisition accounting as soon as practicable but no later than the measurement period.

h. Acquisition of Aviv Management Engineering Systems Ltd.

On December 27, 2016, Matrix completed the acquisition of an 85% interest of Aviv Management Engineering Systems Ltd ("Aviv") for a consideration of NIS 19,699 in cash (approximately \$ 5,123). In addition the sellers may be eligible for future consideration valued, on the acquisition date, at NIS 1,576 (approximately \$ 410) which is contingent upon the acquired business meeting certain operational targets in the years 2017-2019. Aviv provides management consulting and multidisciplinary engineering consulting focusing in four areas of expertise: environmental planning, project management, urban and physical planning and management consulting. Matrix and the seller hold mutual Call and Put options respectively for the remaining 15% interest in Aviv. As a result of the Put option, Matrix recorded redeemable non-controlling interest of NIS 5,714 (approximately \$ 1,486) on the acquisition date. Acquisition related costs were immaterial. The acquisition was accounted for by the purchase method.

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NOTE 4:-BUSINESS COMBINATION, SIGNIFICANT TRANSACTION AND SALE OF BUSINESS (Cont.)

The following table summarizes the provisional estimated fair values of the assets acquired and liabilities at the date of acquisition(1):

Net Assets	\$(668)
Redeemable non-controlling interests	(1,486)
Intangible assets	2,264
Deferred tax liabilities	(1,096)
Goodwill	6,519
Total assets acquired	\$5,533

(1) The estimated fair values of the tangible and intangible assets are provisional and are based on information that was available as of the acquisition date to estimate the fair value of these amounts. Matrix's management believes the information provides a reasonable basis for estimating the fair values of these amounts, but is waiting for additional information necessary to finalize those fair values. Therefore, provisional measurements of fair value reflected are subject to change. Matrix expects to finalize the tangible and intangible assets valuation and complete the acquisition accounting as soon as practicable but no later than the measurement period.

NOTE 5:-MARKETABLE SECURITIES

The Group invests in marketable debt and equity securities, which were classified at fair value through profit or loss and as available-for-sale securities. The following is a summary of marketable securities:

a. Composition:

January 1,	December 31,
2015	2015 2016

Short-term:

Fair value through profit or loss ⁽¹⁾	15,784	11,011	6,790
Available-for-sale	11,915	20,594	30,726

Total short-term securities	\$ 27,699	\$31,605	\$37,516
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Long-term:

Available-for-sale	33,748	30,875	17,228
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Total long-term securities	\$ 33,748	\$30,875	\$17,228
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⁽¹⁾ The Group recognized trading gains in amounts of \$ 114 and \$ 136 during the years ended December 31, 2015 and 2016, respectively.

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NOTE 5:-MARKETABLE SECURITIES (Cont.)

b. The following is a summary of marketable securities which are classified as available-for-sale:

	December 31, 2015				2016			
	Amortized cost	Unrealized losses	Unrealized Gains	Market value	Amortized cost	Unrealized losses	Unrealized gains	Market Value
Available-for-sale:								
Government bonds	\$5,242	\$ (19)	\$ -	\$5,223	\$3,167	\$ (3)	\$ -	\$3,164
Commercial bonds	46,328	(317)	-	46,011	44,821	(261)	-	44,560
Equity securities	118	-	117	235	118	-	112	230
<u>Total</u> available-for-sale marketable securities	\$51,688	\$ (336)	\$ 117	\$51,469	\$48,106	\$ (264)	\$ 112	\$47,954

	January 1, 2015			
	Amortized cost	Unrealized losses	Unrealized Gains	Market value
Available-for-sale:				
Government bonds	\$5,161	\$ (33)	\$ -	\$5,128
Commercial bonds	40,064	(410)	-	39,654
Equity securities	447	-	434	881
<u>Total</u> available-for-sale marketable securities	\$45,672	\$ (443)	\$ 434	\$45,663

Interest receivable of available-for-sale marketable securities included in other receivables and prepaid expenses amounted to \$ 280, \$ 334 and \$ 226 as of January 1, 2015, and December 31, 2015 and 2016, respectively.

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In 2015 and 2016 the Group received proceeds from sale and maturity of available-for-sale marketable securities of \$ 2,136 and \$16,541 and recorded related net gains (losses) of \$ 300 and \$ (16) in financial income (expenses), respectively.

The amortized costs of available-for-sale debt securities at December 31, 2016, by contractual maturities, are shown below:

	Amortized cost	Unrealized gains (losses)		Market value
		Gains	Losses	
Due up to three years	\$ 46,264	\$ -	\$ (232) \$46,032
Due between three to five years	\$ 1,724	\$ -	\$ (32) \$1,692
	\$ 47,988	\$ -	\$ (264) \$47,724

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NOTE 5:-MARKETABLE SECURITIES (Cont.)

The following is the change in the other comprehensive income from available-for-sale securities during 2016 and 2015:

	Other comprehensive income
Other comprehensive income from available-for-sale securities as of January 1, 2015	\$ 319
Unrealized gain from available-for-sale securities	102
Realized gain reclassified into profit or loss	(300)
Other comprehensive income from available-for-sale securities as of December 31, 2015	121
Unrealized gain from available-for-sale securities	30
Realized loss reclassified into profit or loss	16
Other comprehensive income from available-for-sale securities as of December 31, 2016	\$ 167

Note 6:-Fair value measurement

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and considers counterparty credit risk in its assessment of fair value.

The Company's financial assets and liabilities measured at fair value on a recurring basis, excluding accrued interest components; consisted of the following types of instruments as of January 1, 2015 and December 31, 2015 and 2016:

Fair value measurements			
December 31, 2016			
Level 1	Level 2	Level 3	Total

Assets:

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Equity securities	\$1,001	\$-	\$-	\$1,001
Government and corporate debentures	6,019	47,724	-	53,743
Foreign currency derivative contracts ⁽¹⁾	-	-	-	-
Dividend preference derivative in TSG ⁽²⁾	-	-	2,120	2,120
 Total financial assets	 \$7,020	 \$47,724	 \$2,120	 \$56,864
 Liabilities:				
Redeemable non-controlling interests ⁽¹⁾	\$-	\$-	\$49,629	\$49,629
Foreign currency derivative contracts	-	-	-	-
Contingent consideration ⁽¹⁾	-	-	17,730	17,730
	-	-	-	-
Total financial liabilities	\$-	\$-	\$67,359	\$67,359

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NOTE 6:- FAIR VALUE MEASUREMENT (Cont.)

	Fair value measurements			
	December 31, 2015			
	Level 1	Level 2	Level 3	Total
Assets:				
Equity securities	\$3,525	\$-	\$-	\$3,525
Government and corporate debentures	7,721	51,235	-	58,956
Foreign currency derivative contracts	-	121	-	121
Total financial assets	\$11,246	\$51,356	\$-	\$62,602
Liabilities:				
Redeemable non-controlling interests ⁽¹⁾	\$-	\$-	\$18,751	\$18,751
Foreign currency derivative contracts	-	12	-	12
Contingent consideration ⁽¹⁾	-	-	7,106	7,106
Total financial liabilities	\$-	\$12	\$25,857	\$25,869

	Fair value measurements			
	January 1, 2015			
	Level 1	Level 2	Level 3	Total
Assets:				
Equity securities	\$4,658	\$-	\$-	\$4,658
Government and corporate debentures	12,007	44,782	-	56,789
Foreign currency derivative contracts	-	87	-	87
Total financial assets	\$16,665	\$44,869	\$-	\$61,534
Liabilities:				
Redeemable non-controlling interests ⁽¹⁾	\$-	\$-	\$15,224	\$15,224
Contingent consideration ⁽¹⁾	-	-	3,563	3,563
Total financial liabilities	\$-	\$-	\$18,787	\$18,787

(1)

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The fair value of redeemable non-controlling interests and contingent consideration was determined based on the present value of the future expected cash flow.

- (2) The fair value of dividend preference derivative in TSG was estimated using the Monte-Carlo simulation technique.

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Note 7:- Investments in companies accounted for at equity METHOD

- a. The following is a summary of Formula's investments in companies accounted for at equity:

	January 1, 2015	December 31, 2015	December 31, 2016
Affiliated companies	528	-	38
Joint venture (see Note 4(i)a)	-	-	24,042
	528	-	24,080

The following table summarizes activity related to Formula's investments in companies accounted for at equity:

	2016
January 1, 2016	\$-
Acquisition of shares in joint venture	16,024
Investment in Capital notes of joint venture	7,669
Company's share of earnings (losses) of joint venture	349
Affiliated company due to business combination of Subsidiary	38
December 31, 2016	\$24,080

- b. Composition of investment in joint venture :

	January 1, 2015	December 31, 2015	December 31, 2016
Details of investment in TSG:			
Shares	-	-	16,373
Capital notes	-	-	7,669
Dividend preference derivative in TSG ⁽¹⁾	-	-	2,120

	-	-	26,162
Goodwill included in the investment	-	-	9,867

(1) Dividend preference derivative in TSG is included in Company's long term prepaid expenses and other receivables and is accounted for at fair value through to profit or loss.

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Note 7:-Investments in companies accounted for at equity (Cont.)

c. Group's share of statements of financial position of companies accounted for at equity, after being adjusted to comply with IFRS, based on the interests therein, as of the below reporting dates:

	January 1, 2015	December 31, 2015	December 31, 2016
Statement of financial position of companies accounted for at equity at reporting date:			
Current assets	-	-	12,367
Noncurrent assets ⁽¹⁾	-	-	234
Current liabilities	-	-	(8,485)
Noncurrent liabilities	-	-	(815)
	-	-	3,301
Adjustments for differences in accounting policies:			
Excess cost of intangible assets net of deferred tax liabilities	-	-	10,912
Goodwill	-	-	9,867
Total investment in companies accounted for at equity	-	-	24,080

(1) Does not include balance of goodwill in an amount of \$ 9,867 as of December 31, 2016.

d. Group's share of statement of income of companies accounted for at equity, after being adjusted to comply with IFRS, based on the interests therein, during the periods shown below (with respect to the Group's interest in TSG, for the periods from May 1, 2016 until December 31, 2016, and with respect to the Group's interest in Subsidiary's affiliate, only for the period from December 26, 2016):

	Year ended December 31, 2015	December 31, 2016
Revenues of companies accounted for at equity in the reporting year:		
Revenues	-	19,324
Amortization of excess cost related to revenues	-	(193)
Company's share of revenues of companies accounted for at equity	-	19,131
Income (loss)	-	1,372
Amortization of excess costs	-	(1,023)

Company's share of income of companies accounted for at equity - 349

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NOTE 8:- PROPERTY, PLANTS AND EQUIPMENT, NET

Composition:

	January 1, 2015	December 31, 2015	2016
Cost:			
Computers, equipment and software	\$ 54,635	\$ 52,283	\$ 60,074
Motor vehicles	417	673	1,552
Buildings	1,852	1,846	1,833
Leasehold improvements	19,087	17,840	20,991
	75,991	72,642	84,450
Accumulated depreciation:			
Computers, equipment and software	\$ 43,417	\$ 40,381	\$ 46,659
Motor vehicles	212	242	531
Buildings	822	907	23
Leasehold improvements	9,429	9,109	11,107
	53,880	50,639	58,320
Depreciated cost	\$ 22,111	\$ 22,003	\$ 26,130

In December 2016, Matrix has sold its full rights in a land property for a total consideration of approximately \$ 4,473. The group recognized a gain from the aforementioned sale in an amount of approximately \$ 3,147. Simultaneously to the sale, Matrix had leased the land for its operations. The lease is treated as an operating lease in accordance with IAS 17.

Depreciation expenses totaled \$ 7,092 and \$ 7,880 for the years ended December 31, 2015 and 2016, respectively.

Note 9:- Goodwill

The changes in the carrying amount of goodwill for the years ended December 31, 2015 and 2016 were as follows:

Balance as of January 1, 2015	\$	424,807	
Adjustments due to purchase price allocation		458	
Adjustments to negative goodwill write-off		(458)
Acquisition of subsidiaries		17,104	
Classifications		(90)
Foreign currency translation adjustments		(800)
Balance as of December 31, 2015		441,021	
Acquisition of subsidiaries		53,498	
Classifications		389	
Foreign currency translation adjustments		2,876	
Balance as of December 31, 2016	\$	497,784	

The Company performed annual impairment tests during the fourth quarter of 2016 and did not identify any impairment losses (See Note 2(20)).

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NotE 10:- Intangible Assets, Net

a. Intangible assets, net, are comprised of the following as of the below dates:

	January 1, 2015	December 31, 2015	2016
Original amounts:			
Capitalized Software costs	\$ 155,519	\$ 164,573	\$ 175,456
Customer relationship	73,666	81,019	111,526
Acquired technology	11,733	11,792	20,455
Patent	1,234	1,230	1,248
Backlog and non-compete agreement	4,974	5,722	6,063
Other intangibles	3,418	3,622	4,066
	250,544	267,958	318,814
Accumulated amortization:			
Capitalized Software costs	102,817	111,595	122,293
Customer relationship	29,207	38,019	49,538
Acquired technology	4,787	6,023	7,871
Patent	51	174	302
Backlog and non-compete agreement	1,142	4,273	5,611
Other intangibles	3,128	3,218	3,378
	141,132	163,302	188,995
Total	\$ 109,412	\$ 104,656	\$ 129,821

b. Amortized expenses totaled \$ 23,346 and \$ 24,490 for the years ended December 31, 2015 and 2016, respectively.

c. Estimated other intangible assets amortization for the years ended:

December 31,

2017	\$27,193
2018	24,324
2019	21,751

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2020	17,702
2021 and thereafter	38,851
Total	\$ 129,821

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Note 11:-Long term Liabilities to Banks and Others

December 31, 2016	Linkage Basis	a.		Composition:		
		Long-term liabilities	Current maturities	Total long-term liabilities net of current maturities	Total long-term liabilities net of current maturities	Total long-term liabilities net of current maturities
Interest rate		December 31, 2016			December 31, 2015	January 1, 2015
%						
2.64-5.85	NIS - Unlinked	\$ 155,583	40,054	115,529	\$ 103,632	\$ 108,684

In November 2016, Magic obtained a loan in the amount of \$ 31,356 linked to the New Israel shekel from an Israeli financial institution. The principal amount is payable in seven equal annual installments with the final payment due on November 2, 2023 and bears a fixed interest rate of 2.60% per annum, payable in two semi-annual payments. As of December 31, 2016, Magic was in full compliance with the financial covenants.

On February 28, 2017, Sapiens (via its wholly-owned subsidiary, Sapiens Americas Corporation, or the Borrower) entered into a secured credit agreement, with HSBC Bank USA, National Association, for, the acquisition of StoneRiver. Pursuant to the credit agreement, Sapiens borrowed \$ 40 million, for a five-year term. The Loan will mature in February 2022 and is payable in equal consecutive quarterly principal installments of principal and accrued interest. The loan bears interest at the rate of LIBOR plus 1.85%. For additional information see note 22.

	b.			Maturity dates:		
	January 1, 2015	December 31, 2015	December 31, 2016			
First year (current maturities)	\$ 26,127	\$ 36,378	\$ 40,054			
Second year	31,512	33,263	33,803			
Third year	28,393	27,521	37,836			
Fourth year	22,631	18,923	21,663			
Fifth year and thereafter	26,148	23,925	22,227			
Total	\$ 134,811	\$ 140,010	\$ 155,583			

- c. For details of liens, guarantees and credit facilities, see Note 17.

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NOTE 12:- DEBENTURES

On September 16, 2015, Formula concluded a public offering in Israel on the Tel-Aviv Stock Exchange (the "TASE") of (i) NIS 101,014 (net of issuance expenses) Series A Secured Debentures (the "Series A Secured Debentures") that are in NIS (not linked to any currency or index) and secured by liens on certain shares of Formula's investees (Matrix, Sapiens and Magic) held by Formula (with a loan-to-value of not more than 60% measured on the date of the issuance), and of (ii) \$ 32,148 (net of issuance expenses) Series B Convertible Debentures (the "Series B Convertible Debentures") that are linked to the U.S Dollar and convertible into ordinary shares of Formula (the Convertible Debentures together with the Secured Debentures - the "New Debentures"). The New debentures were offered and sold pursuant to a shelf prospectus filed with the Israeli Securities Authority (the "ISA") and TASE on August 6, 2015, amended thereafter on September 3, 2015.

Formula accounts for the outstanding principal amount of our New Debentures as long-term liability, in accordance with IAS 39, with current maturities classified as short-term liabilities. Formula has identified and separated an equity component contained in Series B Convertible Debentures, by first determining the liability component, in accordance with IAS 32, based on the fair value of an equivalent non-convertible liability. The conversion component valued at \$ 1,248 has been determined to be the residual amount.

Debt issuance costs were capitalized and reported as deferred financing costs, which are amortized over the life of the New Debentures using the effective interest rate method. As of December 31, 2016, the value of Series A Secured Debentures and the value of Series B Convertible Debentures was NIS 102,739 (approximately \$ 26,720) and \$ 32,364 respectively.

The public offering of the New Debentures was made only in Israel and not to U.S. persons (as defined in Rule 902(k) under the Securities Act of 1933, as amended (the "Securities Act")), in an overseas directed offering (as defined in Rule 903(b)(i)(ii) under the Securities Act), and was exempt from registration under the Securities Act pursuant to the exemption provided by Regulation S thereunder. The sale of the debentures was not registered under the Securities Act, and the debentures may not be offered or sold in the United States and/or to U.S. persons without registration under the Securities Act or an applicable exemption from the registration requirements of the Securities Act.

Series A Secured Debentures (NIS 102,260,000 par value)

The Series A Secured Debentures were issued at a purchase price equal to 100% of their par value and bear fixed annual interest at a rate of 2.8% (which may vary based on the credit rating of the debentures), payable semi-annually. The proceeds of the offering, before early commitment commission valued at \$ 129 with respect to the units for which the qualified investors have committed to subscribe, and issuance costs of \$ 190, amounted to NIS 102,260 (approximately \$ 26,295). The principal of the Series A Secured Debentures, are nominated in NIS (not linked to any currency or index) and will be paid to holders in eight equal annual installments commencing on July 2, 2017. Formula may redeem the Series A Secured Debentures or any part thereof at its discretion after 60 days from their issuance date subject to certain conditions.

In accordance with the terms of the indenture related to Series A Secured debentures, the collateral will consist of the following shares of the Company's subsidiaries and affiliate held by the Company:

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NOTE 12:- DEBENTURES (Cont.)

2,435,910 ordinary shares, par value 1.0 New Israeli Shekels ("NIS") per share, of the Company's subsidiary, Matrix IT Ltd.;

2,338,483 ordinary shares, par value NIS 0.1 per share, of the Company's affiliate, Magic Software Enterprises Ltd.;

and

1,260,266 common shares, par value €0.01 per share, of the Company's affiliate, Sapiens International Corporation N.V.

Series B Convertible Debentures (NIS 125,000,000 par value)

The Series B Convertible Debentures were issued at a purchase price equal to 102% of their par value and bear fixed annual interest at a rate of 2.74% (which may vary based on the credit rating of the debentures), payable in one installment upon maturity of the debentures on March 26, 2019 (at which time the accrued interest will constitute 10% of the principal amount of the Convertible Bonds, in the aggregate). The proceeds of the offering, before early commitment commission valued at \$ 131 with respect to the units for which the qualified investors committed to subscribe, and issuance costs of \$ 236, amounted to NIS 127,500 (approximately \$ 32,785). The principal of the Bonds is subject to adjustment based on changes in the exchange rate between the NIS and the U.S. Dollar relative to the exchange rate on September 8, 2015 (3.922), and will be repaid on March 26, 2019. Formula may not redeem the Series B Convertible Debentures or any part thereof at its discretion.

The Series B Convertible Debentures are convertible, at the election of each holder, into the Formula's ordinary shares at a conversion price of NIS 157 par value of Convertible Debentures per one share from the date of issuance and until March 10, 2019. The conversion price is subject to adjustment in the event that the Company effects a share split or reverse share split, a rights offering or a distribution of bonus shares or a cash dividend. As of December 31, 2016, the adjusted conversion price to one share is NIS 151.52166 par value following cash dividend distributions.

During 2016, and as of December 31, 2016, the Company satisfied all of the financial covenants associated with both, the Convertible Bonds and the Secured Bonds.

As at 31 December 2016, liabilities of Formula under the above-mentioned bonds amounted to \$ 58,715.

	Effective		January, 1	December 31,	
Series	interest rate	Currency	2015	2015	2016
Short-term A	3.07	% NIS	-	213	3,274
Long-term A	3.07	% NIS	-	25,905	23,077
B	3.65	% NIS/USD	-	31,223	32,364
			-	57,128	55,441

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NOTE 12:- DEBENTURES (Cont.)

The following is the change in the carrying amount of the New Debentures during 2015 and 2016:

Balance as of January 1, 2015	-
Issuance of convertible and secured debentures, net	\$58,394
Equity conversion component	(1,248)
Accrued interest	476
Premium and issuance costs amortization	77
Foreign currency translation adjustments	(358)
Balance as of January 1, 2016	\$57,341
Accrued interest	1,653
Interest payments	(964)
Premium and issuance costs amortization	296
Foreign currency translation adjustments	389
Balance as of December 31, 2016	\$58,715

As of December 31, 2016, the aggregate principal annual payments of the bonds are as follows:

	Repayment amount
2017	3,324
2018	3,324
2019	35,195
2020	3,324
2021 and thereafter	13,300
Total	58,467

Note 13:- RELATED PARTY TRANSACTIONS

On August 18, 2015, Sapiens completed the acquisition from Asseco Poland S.A. ("Asseco") of all issued and outstanding shares of Insseco. Asseco is the parent company of Formula. Please see note 1 above for further information concerning this acquisition.

Under the share purchase agreement for that acquisition, Asseco committed to assign all customer contracts to Insseco that relate to the intellectual property that Sapiens acquired as part of the acquisition. In the event that Asseco cannot obtain the consent of any customer to the assignment of its contract to Insseco, Asseco will hold that customer's contract in trust for the benefit of Insseco. Under that arrangement, in 2015, Insseco invoiced Asseco in a back-to-back manner for all invoices issued by Asseco on Insseco's behalf to customers under those contracts that were not yet assigned by Asseco to Insseco.

During the years ended December 31, 2015 and 2016, Asseco provided back office and professional services and fixed assets to Insseco in an amount totaling approximately \$1,700 and \$1,900, respectively.

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Note 14:-Employee Option Plans

In March 2011, Formula's shareholders approved the adoption of Formula's 2011 Employee and Officer Share Incentive Plan (the "2011 plan"). Pursuant to the 2011 plan, Formula may grant from time to time to Formula's and its investees' employees and officers (which are not Formula's controlling shareholders) Ordinary shares, restricted shares or options to purchase up to 545,000 ordinary shares of Formula. The 2011 plan is administered by Formula's board of directors. The 2011 plan provides that share based compensation may be granted, from time to time, to such grantees to be determined by the board, at an exercise price and under such terms to be determined at its sole and absolute discretion. Share based compensation may be granted under the 2011 plan through March 2021. In 2012, Formula increased the amount of ordinary shares reserved for issuance under the 2011 plan by 1,200,000 options.

In March 2011, concurrently with the amendment and extension of Formula's chief executive officer's service agreement, Formula approved a grant of options to its chief executive officer, exercisable for an additional 543,840 ordinary shares. The options vest in equal quarterly installments, over a four year period that commences in December 31, 2011 and concludes in December 31, 2015. The exercise price of the options is NIS 0.01 per share. In May 2011, the chief executive officer exercised all of these options for redeemable restricted shares, for which the Company's redemption right was to lapse in accordance with the remaining vesting schedule for the unvested options from which they arose. Total fair value of the grant was calculated based on the Formula share price on the grant date and totaled \$ 9,055 (\$ 16.65 per share).

In December 2011, at which time Formula was negotiating an amendment and an extension of its chief executive officer's service agreement, it redeemed all of the above-described 543,840 shares for no consideration.

In March 2012, concurrently with the amendment and extension of its chief executive officer's service agreement, the board of directors of Formula awarded him with a new share option incentive plan, following the redemption of the 543,840 redeemable ordinary shares, which were granted to him in March 2011 and which were not yet vested in their redemption date. Under the 2011 plan, the chief executive officer of Formula was granted with options exercisable to 1,122,782 ordinary shares of Formula (the "New grant"), as long as he continue to serve as (i) a director of Formula and/or (ii) a director of each of the directly held subsidiaries of Formula; provided that if he fails to meet the foregoing requirement (A) due to the request of the board of directors of either Formula or any of its directly held subsidiaries (other than a request which is based on actions or omissions by the chief executive officer that would constitute "cause" under his service agreement with Formula), (B) because the chief executive officer is prohibited under the governing law or charter documents of the relevant company or the stock exchange rules and regulations applicable to such company from being a director of such company (other than due to his actions or omissions) or (C)

notwithstanding the chief executive officer's willingness to be so appointed (but provided that neither (A) nor (B) applies); then, in each of (A), (B) and (C), the chief executive officer will be deemed to have complied with clauses (i) or (ii) above. The options vest, i.e., Formula's redemption right with respect to the options and the underlying ordinary shares issuable upon exercise lapses, in equal quarterly installments over an eight year period that commenced in March 2012 and concludes on December 31, 2019. The exercise price of the options is NIS 0.01 per share. The New grant is accounted for as a modification to the March 2011 grant to the chief executive officer. Total fair value of the grant was calculated based on the share price on the grant date and totaled \$ 18,347 (\$ 16.34 per share).

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Note 14:- Employee Option Plans (Cont.)

In accordance with the terms of the option grant, the shares issuable upon exercise of the options will be deposited with a trustee and Formula's chief executive officer will not be permitted to vote or dispose of them until the shares are released from the trust.

In June 2013 all options were exercised into shares however they have been deposited with a trustee and Formula's chief executive officer is not permitted to vote or dispose of them until the shares are released from the trust. All shares participate in dividends and have the right to vote, however for so long as the shares are held by the trustee (even if they have vested) the voting rights may only be exercised by the trustee. In accordance with the guidelines of Formula incentive plan for so long as the shares underlying any grant under the plan are being held by the trustee they will be voted by the trustee in the same proportion as the results of the shareholder meeting. Only those shares for which the vesting period has expired may be collected from the trustee.

As of December 31, 2016 all 1,122,782 restricted shares were deposited with the trustee with 701,739 Ordinary Shares, constituting the currently vested portion of the 1,122,782 restricted shares that Formula chief executive officer was granted.

In November 2014, Formula board of directors awarded its chief financial officer with 10,000 restricted shares under the 2011 plan (the "restricted shares"). These restricted shares vest on a quarterly basis over a four-year period, commencing on November 13, 2014 and concludes in November 13, 2018, provided that during such time the chief financial officer will continue to serve as (i) an officer of the Company and/or (ii) an officer in one of the directly held affiliates, except that if he fail to meet the service condition due to the request of the board of directors b. of either Formula or any of its directly held affiliates (other than a termination of his provision of services which is based on actions or omissions by him that will constitute "cause" under his grant agreement with Formula); then, the chief financial officer will be deemed to have complied with clauses (i) or (ii) above. Notwithstanding the foregoing, if a change of control of the Company occurs, then all unvested restricted shares will immediately become vested. Total fair value of the grant was calculated based on the Formula share price on the grant date and equaled to \$ 239 (\$ 23.9 per share).

As of December 31, 2016 all 10,000 restricted shares were deposited with the trustee with 5,000 Ordinary Shares, constituting the currently vested portion of the 10,000 restricted shares that Formula chief financial officer was granted.

Formula's investees grant, from time to time, options to their officers and employees to purchase shares in the c.respective companies. In general, the options expire 5-10 years after grant. For further information with respect to expenses relating to the benefit to the employees, an additional disclosure required IFRS, see Note 2(28).

d. The following table sets forth the breakdown of stock-based compensation expense resulting from stock options grants, as included in the consolidated statements of income:

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Note 14:- Employee Option Plans (Cont.)

	Year ended December 31,	
	2015	2016
Cost of revenues	\$31	\$15
Research and development expenses	48	17
Selling and marketing expenses	137	71
General and administrative expenses	4,078	4,266
Total stock-based compensation expense	\$4,294	\$4,369

Matrix:

The following table is a summary of employee option activity as of December 31, 2016, and changes during the year ended December 31, 2016, in Matrix:

	Number of options	Weighted average exercise price	Weighted average remaining contractual term (in years)	Aggregate intrinsic value
Outstanding at January 1, 2016	2,375,000	4.39	4.18	3,145
RSU Exercised	75,000	-		
Outstanding at December 31, 2016	2,300,000	4.26	3.13	8,591
Exercisable at December 31, 2016	-	-	-	-

The aggregate intrinsic value in the table above represents the total intrinsic value that would have been received by the option holders had all option holders exercised their options on December 31, 2016. This value would change

based on the change in the market value of Matrix' ordinary shares and the change in the exchange rate between the New Israeli Shekel and U.S. dollar. As of December 31, 2016, there was \$ 837 of total unrecognized compensation costs related to non-vested share-based compensation arrangements granted under Matrix equity incentive plan. The total intrinsic value of options exercised during the years ended December 31, 2015 and 2016 was \$ 807 and \$ 0, respectively.

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Note 14:- Employee Option Plans (Cont.)

Sapiens:

The following table is a summary of employee option activity as of December 31, 2016, and changes during the year ended December 31, 2016, in Sapiens:

	Year ended December 31, 2016			
	Amount of options	Weighted average exercise price	Weighted average remaining contractual life (in years)	Aggregate intrinsic value
Outstanding at January 1, 2016	2,175,488	5.36	3.49	9,274
Granted	310,000	11.63		
Exercised	(276,170)	3.52		
Expired and forfeited	(71,535)	6.17		
Outstanding at December 31, 2016	2,137,783	6.91	3.43	15,171
Exercisable at December 31, 2016	1,172,950	4.84	2.56	10,646

In 2015 and 2016, Sapiens granted 673,408 and 310,000 stock options to purchase its shares to employees and directors, respectively. The weighted average grant date fair values of the options granted during the years ended December 31, 2015 and 2016 were \$ 3.79 and \$ 4.30, respectively. All outstanding options are in the money as of December 31, 2016.

The total intrinsic value of options exercised during the years ended December 31, 2015 and 2016 was \$ 10,294 and \$2,304, respectively.

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The options outstanding under Sapiens' stock option plans as of December 31, 2016 have been separated into ranges of exercise price as follows:

Ranges of exercise price	Options outstanding as of December 31, 2016	Weighted Average remaining contractual Term (Years)	Weighted average exercise price \$	Options Exercisable as of December 31, 2016	Weighted Average Exercise price of Options Exercisable \$
1.28-1.88	64,590	2.87	1.44	64,590	1.44
2.06-2.50	273,972	1.69	2.40	273,972	2.40
3.25-3.57	288,221	1.53	3.37	288,221	3.37
4.52	74,000	2.40	4.52	43,000	4.52
5.05-5.33	67,500	2.60	5.08	48,750	5.07
6.07-6.81	230,000	3.15	6.48	174,167	6.38
7.21-7.48	209,500	3.21	7.44	90,250	7.42
8.22-9.73	500,000	4.63	8.80	140,000	8.65
10.58-11.21	280,000	4.78	10.76	50,000	10.58
12.43-13.02	150,000	5.69	12.73	-	-
	2,137,783	3.43	6.91	1,172,950	4.84

The total equity-based compensation expense related to all of Sapiens' equity-based awards, recognized for the years ended December 31, 2015 and 2016, was \$ 1,349 and \$ 1,955, respectively. As of December 31, 2016, there was \$ 3,288 of total unrecognized compensation cost related to non-vested options, which is expected to be recognized over a period of up to four years.

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Note 14:-Employee Option Plans (Cont.)

During 2016, 29,500 of the 88,500 restricted shares of Sapiens Decision, the Company's majority-owned subsidiary that were granted to one of the former shareholders of KPI in 2014 vested, thereby reducing the Company's percentage ownership of Sapiens Decision from 95.7% to 94.25%. During 2016, Sapiens Decision granted 10,000 options to certain of its employees to purchase shares of Sapiens Decision.

Magic:

A summary of employee option activity under the Magic plans as of December 31, 2016

and changes during the year ended December 31, 2016 are as follows:

	Number of options	Weighted average exercise price	Weighted average remaining contractual term (in years)	Aggregate intrinsic value
Outstanding at January 1, 2016	493,917	4.47	5.99	523
Granted	-	-		
Exercised	(20,550)	2.01		
Forfeited	-	-		
Outstanding at December 31, 2016	473,367	4.58	5.10	991
Exercisable at December 31, 2016	342,742	3.80	4.36	983

The aggregate intrinsic value in the table above represents the total intrinsic value that would have been received by the option holders had all option holders exercised their options on December 31, 2016. This amount is changed based on the market value of the Company's ordinary shares. Total intrinsic value of options exercised during the years ended December 31, 2015 and 2016 was \$ 210 and \$ 112, respectively. As of December 31, 2016, there was \$ 60 of unrecognized compensation cost related to non-vested share-based compensation arrangements granted under the Magic's plans. This cost is expected to be recognized over a period of approximately three years.

The options outstanding as of December 31, 2016, have been separated into ranges of exercise price categories, as follows:

Ranges of Exercise price	Options outstanding	Weighted average remaining contractual life (Years)	Weighted average exercise price \$	Options exercisable	Weighted average exercise price of exercisable options \$
0-1	1,075	2.24	-	1,075	-
1.01-2	20,000	1.98	1.12	20,000	1.12
2.01-3	106,667	2.69	2.31	106,667	2.31
3.01-4	165,625	4.77	4.00	165,625	4.00
4.01-5	-	-	-	-	-
5.01-6	75,000	6.61	6.00	-	-
6.01-7	50,000	7.87	6.89	21,875	6.89
7.01-8	-	-	-	-	-
8.01-9	55,000	7.35	8.01	27,500	8.01
	473,367	5.10	4.58	342,742	3.80

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Note 15:- Liability in respect of capital lease

The following are details of the Company's future minimum lease commitments in respect of capital leases as of December 31, 2016:

	Minimum lease payments	Interest	Present value of minimum lease payment
First year (included in other accounts payable)	438	25	413
Second year	118	10	108
Total	556	35	521

Note 16:-EMPLOYEE BENEFIT LIABILITIES

Employee benefits consist of post-employment benefits, other long-term benefits and termination benefits.

a. Post-employment benefits:

According to the labor laws and Severance Pay Law in Israel, the Company is required to pay compensation to an employee upon dismissal or retirement or to make current contributions in defined contribution plans pursuant to section 14 to the Severance Pay Law, as specified below. The Company's liability is accounted for as a post-employment benefit. The computation of the Company's employee benefit liability is made according to the current employment contract based on the employee's salary and employment term which establish the entitlement to receive the compensation.

The post-employment employee benefits are normally financed by contributions classified as defined benefit plan or as defined contribution plan, as detailed below.

1) Defined contribution plans:

Section 14 to the Severance Pay Law, 1963 applies to part of the compensation payments, pursuant to which the fixed contributions paid by the Group into pension funds and/or policies of insurance companies release the Group from any additional liability to employees for whom said contributions were made. These contributions and contributions for benefits represent defined contribution plans.

2)

Defined benefit plans:

The Group accounts for that part of the payment of compensation that is not covered by contributions in defined contribution plans, as above, as a defined benefit plan for which an employee benefit liability is recognized and for which the Group deposits amounts in central severance pay funds and in qualifying insurance policies.

According to Matrix's agreements with one of its senior officer, he is entitled to an adaptation bonus in the amount of 12 salaries. This liability has been recognized as a defined benefit.

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Note 16:-EMPLOYEE BENEFIT LIABILITIES (Cont.)

b. Composition of defined benefit plans:

	January 1, 2015	December 31, 2015	2016
Defined benefit obligation	76,236	72,630	76,370
Fair value of plan assets	(73,159)	(69,241)	(70,196)
Net defined benefit liability	3,077	3,389	6,174

Note 17:- Commitments and Contingencies

a. Liens:

A lien has been incurred by Formula over certain portion of its investments in outstanding shares of Matrix, Magic and Sapiens, in pursuant to financial institution credit agreement entered on January 2014 and with respect to the Secured Bonds issued by Formula in September 2015 on the TASE.

b. Guarantees:

1. The Group has provided certain bank guarantees in an aggregate of approximately \$ 20,800 as security for its subsidiary companies' performance of various contracts with customers and suppliers. If the subsidiaries were to breach certain terms of such contracts, the customers could demand that the banks providing the guarantees distribute the amounts claimed to be due.

2. The Group has provided bank guarantees in an aggregate of approximately \$ 4,650 as security for its subsidiary companies' rent to be paid for offices. If such subsidiaries were to breach certain terms of their leases, the lessors could demand that the banks providing the guarantees distribute the amounts claimed to be due.

3. As of December 31, 2016, the Group had restricted bank deposits of \$ 261 in favor of bank guarantees.
 4. As of December 31, 2016, the Group has restricted bank deposits of \$ 255 in favor of subsidiary companies' various contracts with customers.

c. Covenants:

In connection with the Group's credit facility agreements, primarily Formula and Matrix, with various financial institutions, the Group committed to the following:

i) Matrix

In the context of Matrix engagements with banks for receiving credit facilities, Matrix has undertaken to maintain the following financial covenants, as they will be expressed in its financial statements, as described:

The total rate of Matrix debts and liabilities to banks with the addition of debts in respect of debentures that have a)been and/or will be issued by it and shareholders' loans that have been and/or will be provided by it (collectively, "the debts") will not exceed 40% of its total balance sheet.

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Note 17:- Commitments and Contingencies (Cont.)

- b) The ratio of Matrix debts less cash to the annual EBITDA will not exceed 3.5.
- d) Matrix equity shall not be lower than NIS 275,000 (approximately \$ 71,521) at all times.
- d) Matrix balances of cash and short-term investments in its balance sheet shall not be lower than NIS 50,000 (approximately \$ 13,004).
- e) In the event that Formula ceases to hold 30% of Matrix share capital or is no longer the largest shareholder in Matrix, the credit may be placed for immediate repayment.
- f) Matrix has committed that the shareholder's interest of Matrix IT-Systems shall never be below 50.1% Matrix will not create any pledge on all or part of its property and assets in favor of any third party and will not provide any guarantee to secure any third party's debts as they are today and as they will be without the banks' consent (except for a first rate fixed pledge on an asset which acquisition will be financed by a third party and which the pledge will be in his favor).
- g) Matrix will not sell and/or transfer all or part of its assets to others in any manner whatsoever without the banks' advance written consent, unless it is done in the ordinary course of business.
- h) Matrix committed not to distribute dividends that will cause its equity (when measured based on International Financial Reporting Standards ("IFRS")) to be less than NIS 275,000 (approximately \$ 71,521). As of December 31, 2016, Matrix's equity was approximately NIS 631,252 (approximately \$ 164,175, as measured based on IFRS).

ii)

Formula

1.

Liability to Financial Institution

In the context of Formula's credit facility from a financial institution, Formula has undertaken to maintain the following financial covenants, as they will be expressed in its financial statements, as described:

- a) Formula shareholders' equity (not including minority interests) shall not be less than \$ 160,000 at all times.
- b) The ratio of Formula shareholders' equity (not including minority interests) to total consolidated assets will not be less than 20%.
- c) The ratio of Company's financial debts less cash, short-term deposit and short-term marketable securities to the annual EBITDA will not exceed 3.5 (all based on the company's consolidated financial statements).
- d) The ratio of Company's financial debts less cash, short-term deposit and short-term marketable securities to the total assets will not exceed 30% (all based on the company's consolidated financial statements).

e) Formula's liabilities to banks and other financial institutions in its standalone balance sheet shall not be higher than NIS 450,000 (approximately \$ 117,035).

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Note 17:- Commitments and Contingencies (Cont.)

f) Formula will not create any pledge on all or part of its property and assets in favor of any third party and will not provide any guarantee to secure any third party's debts as they are today and as they will be without the financial institution's consent.

g) Formula will not sell and/or transfer all or part of its assets to others in any manner whatsoever without the financial institution's advance written consent, unless it is done in the ordinary course of business.

2. Debentures

Series A Secured Debentures and Series B Convertible Debentures contain, in addition to standard terms and obligations, including among others, the following obligations:

a) a covenant not to distribute dividends unless (i) Formula shareholders' equity (not including minority interests) shall not be less than \$ 250 million, (ii) Formula's net financial indebtedness (financial indebtedness net of cash, marketable securities, deposits and other liquid financial instruments) shall not exceed 65% of net CAP (which is defined financial indebtedness, net, plus shareholders equity), (iii) the amount of the distributions shall be equal to profits for the years ended December 31, 2014 and 2015 and 75% of profits accrued from January 1, 2016 until the distribution and (iv) no event of default shall have occurred.; and

b) Financial covenants, including (i) the equity attributable to the shareholders of Formula, as reported in Formula's annual or quarterly financial statements, will not be less than \$ 160 million, (ii) Formula's net financial indebtedness (financial indebtedness net of cash, marketable securities, deposits and other liquid financial instruments) shall not exceed 65% of net CAP (which is defined as financial indebtedness, net, plus shareholders equity) and (iii) at all times, Formula's cash balance will not be less than the annual interest payment (compounded) for the unpaid principal amount of the Series B debentures.

c) Standard events of default including among others:

- i. suspension of trading of the debentures on the TASE over a period of 60 days.
- ii. If the rating of the debentures is less than BBB- by Standard and Poors Maalot or equivalent rating of other rating agencies
 - iii. failure to have the debentures rated over a period of 60 days
 - iv. If there is a change in control without consent of the rating agency; and
 - v. If Formula fails to continue to control any of its subsidiaries;

As of December 31, 2016, Matrix and Formula are in compliance with the above financial covenants.

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Note 17:- Commitments and Contingencies (Cont.)

d. Legal proceedings:

In August 2009, an Israeli software company and one of its owners initiated an arbitration proceeding against Magic and one of its subsidiaries, claiming an alleged breach of a non-disclosure agreement between the parties (the "First Arbitration"). The software company sought damages in the amount of approximately NIS 52 million (approximately \$ 13.4 million). The arbitrator rendered his decision in January 2015 and determined the damages that Magic should pay the plaintiffs an amount of \$ 2.3 million.

In September 2016, the same software company filed a lawsuit for the sum of NIS 34,106 against Magic and one of its subsidiaries, in the context of the First Arbitration. In the lawsuit, the software company claims that warning letters that Magic has sent to its clients in Israel and abroad, warning the clients against the possibility that the conversion procedure offered by the software company may amount to an infringement of Magic's copyrights (the "Warning Letters") may have caused it irreparable damages resulting from the loss profit of potential business transactions. The lawsuit is based on the decision given in the First Arbitration, in which it was decided that the Warning Letters constituted a breach of a non-disclosure agreement signed between the parties and awarded certain damages to the software company.

The software company claims that the First Arbitration awarded it damages for only the years 2009 and 2010, and they are allowed to sue for damages relating to the years 2011 through 2016 in separate proceedings. On January 23, 2017, Magic filed its statement of defense, maintaining, on various grounds, that the new lawsuit must be dismissed. The plaintiffs filed their response on April 2, 2017. In view of the nature of the claims, both factual and legal, that were raised in the proceedings, the likelihood of an expert-based ruling and given the preliminary stage of the proceeding, it is impossible at this stage to properly evaluate the prospect of the lawsuit being successful.

2. On August 27, 2015, a wholly-owned subsidiary of Sapiens was summoned to a hearing at a court in Amsterdam in connection with a claim initiated against it by one of its customers.

Although the software system provided by the subsidiary has been used by the customer since 2008, the customer claims that the software system furnished to the customer did not comply with the requirements of the customer and that the subsidiary failed to correct errors in the software systems in accordance with the service level agreement between the parties. The remedies sought by the customer are (i) termination of all contracts with the subsidiary and (ii) refund of all amounts paid by the customer to the subsidiary under the foregoing contracts plus damages in an

aggregate amount of approximately € 21,500.

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Note 17:- Commitments and Contingencies (Cont.)

As of the date of publication of these financial statements, the legal proceedings are at its early stage and Sapiens has included in its financial statements a provision which reflects the current estimate of the potential outcome of the foregoing claim.

On February 26, 2017, a bill of indictment was submitted by the Israeli Antitrust Authority against a subsidiary of Matrix (the "Sub") and against a junior employee of the Sub, claiming that the junior employee and as follows the Sub were allegedly a party in a binding agreement and also by "obtaining by fraud", in one indictment regarding a tender of \$ 360.

In addition to the above-described legal proceedings, from time to time, Formula and/or its subsidiaries and affiliates are subject to legal, administrative and regulatory proceedings, claims, demands and investigations in the ordinary course of business, including claims with respect to intellectual property, contracts, employment and other matters. The Group accrues a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Significant judgment is required in the determination of both the probability and as to whether a loss is reasonably estimable. These accruals are reviewed at least quarterly and adjusted to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular matter. The Group intends to defend itself vigorously against the above claims, and it generally intends to vigorously defend any other legal claims to which it is subject. While for most litigation, the outcome is difficult to determine, to the extent that there is a reasonable possibility that the losses to which the Group may be subject could exceed the amounts (if any) that it has already accrued, the Group attempts to estimate such additional loss, if reasonably possible, and disclose it (or, if it is an immaterial amount, indicate accordingly). The aggregate provision that the Group has recorded for all other legal proceedings (other than the particular material proceedings described above) is not material.

Furthermore, in respect of its ordinary course legal, administrative and regulatory proceedings (that is, other than the particular material proceedings described above), the Group estimates, in accordance with the procedures described above, that as of the current time there is no reasonable possibility that it will incur material losses exceeding the non-material amounts already recognized.

e.

Operating lease commitments:

The following are details of the Company's future minimum lease commitments for facilities and equipment, office space and motor vehicles under non-cancelable operating leases as of December 31, 2016:

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Note 17:- Commitments and Contingencies (Cont.)

2017	26,166
2018	15,536
2019	10,144
2020	6,525
2021 and Thereafter	4,311
	62,682

Rent expenses for the years 2015 and 2016, were approximately \$ 22,701 and \$ 25,411 respectively.

The Company leases motor vehicles under a cancelable lease agreement. The Company has an option to be released from this lease agreement, which may result in penalties ranging between one and three times lease monthly cost.

f. Royalty commitments:

Sapiens Technologies (1982) Ltd. ("Sapiens Technologies"), a wholly owned subsidiary of Sapiens incorporated in Israel, was partially financed under programs sponsored by the Israel Innovation Authority (formerly the Office of the Chief Scientist) ("OCS") for the support of certain research and development activities conducted in Israel. In exchange for participation in the programs by the OCS, Sapiens Technologies agreed to pay 3.5% of total net consolidated license and maintenance revenue and 0.35% of the net consolidated consulting services revenue related to the software developed within the framework of these programs based on an understanding with the OCS reached in January 2012. The royalties will be paid up to a maximum amount equaling 100%-150% of the grants provided by the OCS, linked to the dollar, and for grants received after January 1, 1999, bear annual interest at a rate based on LIBOR.

Royalty expenses in Sapiens, after being adjusted to comply with IFRS, amounted to \$ 136 and \$ 0 in 2015 and 2016, respectively. Royalty expenses in Sapiens consolidated and are included in cost of revenues.

As of December 31, 2016, Sapiens had a contingent liability to pay royalties of \$7,119

g.

Insurance:

The Company and its subsidiaries and affiliates insure themselves in bodily injury and property damage insurance policies, including third party, professional liability and employer's liability insurance policies.

Formula, Sapiens and Magic directors and officers (D&O) are insured under an "umbrella" policy for insurance of directors and officers including D&O side A DIC policy (another layer of protection for officers) acquired by the Company for itself and its subsidiaries, for a period of 12 months from June 17, 2015.

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Note 18:- Equity

The composition of the Company's share capital is as follows:

	December 31, 2015		Outstanding	December 31, 2016		Outstanding
	Authorized	Issued		Authorized	Issued	
Ordinary shares, NIS 1 par value each	25,000,000	15,297,402	14,728,782	25,000,000	15,297,402	14,728,782

	January 1, 2015		Outstanding
	Authorized	Issued	
Ordinary shares, NIS 1 par value each	25,000,000	15,297,402	14,728,782

a. Formula's Ordinary Shares, par value NIS 1 per share, are traded on the TASE and Formula's ADSs, each representing one ordinary share, are traded on the NASDAQ.

b. Formula holds 568,620 of its ordinary shares.

c. In December 2013, Formula declared a cash dividend of approximately \$ 4,563 (or \$ 0.31 per share) to shareholders of record on January 20, 2014 that was payable on February 6, 2014.

d. In June 2014, Formula declared a cash dividend of approximately \$ 7,065 (or \$ 0.48 per share) to shareholders of record on July 14, 2014 that was payable on July 31, 2014.

e. In December 2014, Formula declared a cash dividend of approximately \$ 7,875 (or \$ 0.535 per share) to shareholders of record on January 19, 2015 that was payable on February 4, 2015.

f. In June 2015, Formula declared a cash dividend of approximately \$ 5,008 (or \$ 0.34 per share) to shareholders of record on July 20, 2015 that was payable on August 6, 2015.

g. In January 2016, Formula declared a cash dividend of approximately \$ 5,008 (or \$ 0.34 per share) to shareholders of record on January 20, 2016 that was payable on February 4, 2016.

h. In June 2016, Formula declared a cash dividend of approximately \$ 5,008 (or \$ 0.34 per share) to shareholders of record on July 13, 2016 that was payable on July 28, 2016.

i. In December 2016, Formula declared a cash dividend of approximately \$ 7,070 (or \$ 0.48 per share) to shareholders of record on December 30, 2016 that was payable on January 12, 2017.

h. For information concerning Formula employees and officers share-based plan, see Note 14.

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Note 19:- Taxes ON INCOME

a. Israeli taxation:

1. Corporate tax rate in Israel:

Taxable income of Israeli companies is subject to tax at the rate of 26.5% in 2014 and 2015, and 25% in 2016.

In December 2016, the Israeli Parliament approved the 2016 Amendment which reduced the corporate income tax rate to 24% (instead of 25%) effective from January 1, 2017 and to 23% effective from January 1, 2018.

2. Tax benefits under the Israeli Law for the Encouragement of Capital Investments, 1959 ("the Law"):

Certain of Formula's Israeli subsidiaries have been granted "Approved Enterprise" and "Preferred Enterprise" status pursuant to the Law, which provides certain tax benefits including tax exemptions and reduced tax rates. Income not eligible for Approved Enterprise and Preferred Enterprise benefits is subject to corporate tax at the rate that would have otherwise been applicable on the Approved or Preferred Enterprise's income.

The entitlement to the above benefits is conditional upon the fulfillment of the conditions stipulated by the Laws and regulations. Should any of Formula's Israeli subsidiaries fail to meet such requirements in the future, income attributable to their relevant entity's Approved Enterprise or Preferred Enterprise programs could be subject to the statutory Israeli corporate tax rate, and the entity could be required to refund a portion of the tax benefits already received with respect to such programs. As of December 31, 2016, management believes that these Israeli subsidiaries are in compliance with all of the conditions required by the Law.

Approved enterprise tax regime

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Under Approved Enterprise track, A Company is tax exempt in the first two years/six years/ten years of the benefit period (dependent on the development area) and subject to tax at the reduced rate of 10%-25% for a period of five/eight years (if the benefit period qualifying for tax exemption is two years) or one year/four years (if the benefit period qualifying for tax exemption is six years)/for the remaining benefit period (dependent on the level of foreign investment).

Under the terms of the Approved Enterprise program, income that is attributable to one of Sapiens' Israeli subsidiaries was exempt from income tax for a period of two years commencing 2014.

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Note 19:- Taxes ON INCOME (Cont.)

Preferred enterprise tax regime

In August 2013, the Law for Changing National Priorities (Legislative Amendments for Achieving Budget Targets for 2013 and 2014), 2013 which includes Amendment 71 to the Law for the Encouragement of Capital Investments ("the Amendment") was enacted. Per the Amendment, the tax rate on preferred income from a preferred enterprise in 2014 and thereafter will be 16% (in development area A - 9%). As for changes in tax rates resulting from the enactment of Amendment 73 to the Law, see below. Certain of Formula Israeli subsidiaries under Sapiens and Magic had filed a request to apply the new benefits under the 2011 Amendment and therefore subjected to the amended tax rate of 16%.

The Amendment also prescribes that any dividends distributed to individuals or foreign residents from the preferred enterprise's earnings as above will be subject to tax at a rate of 20%.

New Amendment- Technological preferred enterprise

On December 29, 2016, a new legislation amended was enacted to the Investment Law, effective as of January 1, 2017, as part of the Economic Efficiency Law (Legislative Amendments for Applying the Economic Policy for the 2017 and 2018 Budget Years), 2016, which includes Amendment 73 to the Law for the Encouragement of Capital Investments ("the 2017 Amendment"), was published.

Under the 2017 Amendment a new status of "Preferred Technology Enterprise" was introduced to the Investment Law. Under the 2017 Amendment, a Preferred Technology Enterprise which is located in areas other than Development Zone A will be subject to tax at a rate of 12% on profits derived from intellectual property. The implementation of the 2017 Amendment is subject to regulations to be promulgated by the Finance Minister by March 31, 2017. As such regulations have not yet been promulgated and as the definitive criteria to determine the tax benefits have not yet been established, it cannot be concluded that the legislation with respect to Technological Preferred Enterprises had been enacted or substantively enacted as of that date. Accordingly, the above changes in the tax rates were not taken into account in the computation of deferred taxes as of December 31, 2016. Under the transition provisions of the new legislation, the Formula subsidiaries may decide to irrevocably implement the new law while waiving benefits provided under the current law or to remain subject to the current law. Formula and its subsidiaries are examining the

impact of the 2017 Amendment and the degree to which they will qualify as a Preferred Technology Enterprise and the amount of Preferred Technology Income that they may have, or other benefits that they may receive, from the 2017 Amendment.

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Note 19:- Taxes ON INCOME (Cont.)

3. Tax benefits under the Israeli Law for the Encouragement of Industry (Taxes), 1969:

It is Formula's management's belief that certain of its Israeli investees currently qualify as an "Industrial Company," within the meaning of the Law for the Encouragement of Industry (Taxes), 1969 (the "Industrial Encouragement Law"). That Industrial Encouragement Law defines an "Industrial Company" as a company that is resident in Israel and that derives at least 90% of its income in any tax year, other than income from defense loans, capital gains, interest and dividends, from an enterprise whose major activity in a given tax year is industrial production. Under the Industrial Encouragement Law, these Israeli subsidiaries are entitled to amortization of the cost of purchased know-how and patents over an eight-year period for tax purposes as well as accelerated depreciation rates on equipment and buildings. Eligibility for the benefits under the Industrial Encouragement Law is not subject to receipt of prior approval from any governmental authority.

4. Foreign Exchange Regulations:

Under the Foreign Exchange Regulations, certain Israeli subsidiaries of Formula calculate their tax liability in U.S. Dollars according to certain orders. The tax liability, as calculated in U.S. Dollars is translated into NIS according to the exchange rate as of December 31st of each year.

5. Structural changes in Matrix :

On March 27, 2014, a tax ruling was signed determining that from December 31, 2012 as part of a merger procedure 23 companies wholly owned directly or indirectly by Matrix IT will transfer all their assets and liabilities, subject to the provisions of section 103 and section 104 of the Israeli Income Tax Ordinance.

On August 21, 2014, a tax ruling was signed determining that from December 31, 2013 as part of the merger procedures, 7 companies wholly owned directly or indirectly by Matrix IT will transfer all their assets and liabilities, subject to the provisions of section 103 and section 104 of the Tax income.

On August 22, 2016, a tax ruling was signed determining that from December 31, 2015 as part of the merger procedures, 5 companies wholly owned directly or indirectly by Matrix IT will transfer all their assets and liabilities, subject to the provisions of section 103 of the Tax income.

On December 29, 2016 Matrix applied for a merger process as an extension of the above mentioned merger for 4 additional companies holly owned directly or indirectly by Matrix IT, subject to the provisions of section 103 of the Israeli Income Tax Ordinance. The approval is pending.

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Note 19:- Taxes ON INCOME (Cont.)

b. Non-Israeli investees:

Non-Israeli investees are taxed according to the tax laws in their respective country of residence. Neither Israeli income taxes, foreign withholding taxes nor deferred income taxes were provided in relation to undistributed earnings of the non-Israelis subsidiaries. This is because the Group intends to permanently reinvest undistributed earnings in the foreign subsidiaries in which those earnings arose. If these earnings were distributed to Israel in the form of dividends or otherwise, the Group may be subject to additional Israeli income taxes (subject to an adjustment for foreign tax credits) and non-Israeli withholding taxes.

The amount of undistributed earnings of foreign subsidiaries and affiliates that are considered to be reinvested as of December 31, 2016 and 2015 was \$ 47,354, and \$42,002, respectively. However, a determination of the amount of the unrecognized deferred tax liability for temporary difference related to those undistributed earnings of foreign subsidiaries is not practicable due to the complexity of the structure of our group of investees for tax purposes and the difficulty of projecting the amount of future tax liability.

c. Net operating loss carried forward:

Formula

Formula stand-alone had cumulative losses for tax purposes as of December 31, 2016 totaling approximately \$ 61,960 (as of December 31, 2015, the amount was \$ 61,060), which can be carried forward and offset against taxable income in the future for an indefinite period.

Matrix

Matrix had cumulative losses for tax purposes as of December 31, 2016 totaling approximately \$ 34,890 (as of December 31, 2015, the amount was \$ 40,720), which can be carried forward and offset against taxable income in the future for an indefinite period.

Magic

As of December 31, 2016, Magic and its subsidiaries had operating loss carry forwards of \$ 17,183 (as of December 31, 2015, the amount was \$ 19,012), which can be carried forward and offset against taxable income in the future for an indefinite period.

Utilization of U.S. net operating losses may be subject to substantial annual limitations due to the "change in ownership" provisions ("annual limitations") of the Internal Revenue Code of 1986 and similar state provisions. The annual limitation may result in the expiration of net operating losses before utilization.

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Note 19:- Taxes ON INCOME (Cont.)

Sapiens

As of December 31, 2016, certain subsidiaries of Sapiens had tax loss carry-forwards totaling approximately \$ 24,177 (as of December 31, 2015, the amount was \$ 29,050). Most of these carry-forward tax losses have no expiration date.

Insync

Insync didn't have cumulative losses for tax purposes as of December 31, 2016 (as of December 31, 2015, the amount was \$ 49).

Formula, its subsidiaries and its affiliates have cumulative losses for tax purposes as of December 31, 2016 totaling approximately \$ 145,870 (as of December 31, 2015, the amount was \$ 157,441), of which \$ 118,997 was in respect of companies in Israel which can be carried forward and offset against taxable income in the future for an indefinite period (as of December 31, 2015, the amount was \$ 131,245), and approximately \$ 26,873 of which was in respect of companies abroad (as of December 31, 2015, that amount was \$ 26,196).

d. Income tax assessments:

Formula and its subsidiaries are routinely examined by various taxing authorities. Below is a summary of the income tax assessments of Formula and its subsidiaries:

Formula

Formula has received final tax assessments (or assessments that are deemed final) through the tax year 2012.

Matrix

Matrix has received final tax assessments (or assessments that are deemed final) through the tax year 2013. Matrix's subsidiaries have received final tax assessments (or assessments that are deemed final) through the tax year 2012.

Magic

Magic and its Israeli subsidiaries have received final tax assessments (or assessments that are deemed final) through the year 2012.

Sapiens

Tax assessments filed by part of Sapiens' Israeli subsidiaries through the year ended December 31, 2011 are considered to be final (or are deemed final).

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Note 19:- Taxes ON INCOME (Cont.)

e. Deferred tax assets (liabilities), net:

1. Composition, net:

	December 31,	
	2015	2016
Net operating losses carried forward	\$8,839	\$6,885
Allowances, reserves and intangible assets	(12,347)	(19,586)
Capitalized software costs	490	(267)
Differences in measurement basis (cash basis for tax purposes)	(3,302)	(2,744)
Total	\$ (6,320)	\$ (15,712)

2. Presentation in balance sheets:

	December 31,	
	2015	2016
Other non-current assets	\$16,347	\$15,227
Long-term liabilities	(22,667)	(30,939)
	\$ (6,320)	\$ (15,712)

f. Income before taxes on income:

Year ended

December 31,
 2015 2016

Domestic (Israel) \$51,735 \$51,552

Foreign	14,603	25,711
Total	\$66,338	\$77,263

g. Taxes on income (tax benefit) consist of the following:

Year ended

December 31,
2015 2016

Current taxes	\$15,350	\$20,952
Deferred taxes	634	211
Total	\$15,984	\$21,163

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Note 19:- Taxes ON INCOME (Cont.)

h. Theoretical tax:

The following table presents reconciliation between the theoretical tax expense, assuming that all income was taxed at statutory tax rates, and the actual income tax expense, as recorded in the Company's statements of income:

	Year ended	
	December 31,	
	2015	2016
Income before income taxes, as per the statement of operations	\$66,338	\$77,263
Statutory tax rate in Israel	26.5 %	25 %
Tax computed at the statutory tax rate	17,579	19,316
Non-deductible expenses	2,091	1,320
Effect of different tax rates	(54)	(1,143)
Effect of "Approved, Beneficiary or Preferred Enterprise" status	(2,406)	(1,338)
Group's share of earnings of companies accounted for at equity	-	(87)
Deferred taxes on current losses (utilization of carry forward losses) and temporary differences for which a valuation allowance was provided, net	1,676	1,442
Effect of change in Israel tax rates	-	112
Tax-deductible costs, not included in the accounting costs	(733)	(342)
Taxes in respect of prior years	(1,284)	1,839
Other	(885)	44
Taxes on income	15,984	\$21,163

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Note 19:- Taxes ON INCOME (Cont.)

i. Uncertain tax positions:

A reconciliation of the beginning and ending amount of total unrecognized tax benefits in Formula's subsidiaries is as follows:

Balance as of January 1, 2015	1,625
Increase due to consolidation in a subsidiary ⁽¹⁾	154
Decrease related to prior years' tax positions	(326)
Increase related to current year tax positions	1,039
Balance as of December 31, 2015	2,492
Increase due to consolidation in a subsidiary	227
Decrease related to prior years' tax positions	(286)
Increase related to current year tax positions	847
Balance as of December 31, 2016	3,280

(1) The amount initially consolidated as part of the acquisition of subsidiary in 2015 is net of Tax Deducted at Source assets in an amount of \$ 635

The Group recognizes accrued interest and penalties related to unrecognized tax benefits as a component of income tax expense. For the years ended December 31, 2015 and 2016, the amounts recognized, on a consolidated basis, for interest and penalties expenses related to uncertain tax positions were \$ 224 and \$ 68, respectively. In addition, the Group's consolidated liability for unrecognized tax benefits including accrued interest and penalties related to uncertain tax positions was \$ 422 and \$490 at December 31, 2015 and 2016, respectively, which is included within income tax accrual in the Group's consolidated balance sheets.

The entire balance of unrecognized tax benefits, if recognized, would reduce the Company's annual effective tax rate.

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Note 20:- Supplementary Financial Statement Information

Balance Sheets:

a. Other accounts receivable and prepaid expenses:

Composition:

	January 1, 2015	December 31, 2015	December 31, 2016
Government departments	\$ 14,005	\$ 20,973	\$ 15,097
Employees	448	363	365
Prepaid expenses and advances to suppliers	17,379	18,573	22,634
Restricted deposits	633	1,609	2,405
Related Parties	848	1,242	1,865
Other	1,157	352	3,312
Total	\$ 34,470	\$ 43,112	\$ 45,678

b. Liabilities to Banks and other financial institutions:

	December 31, 2016	Linkage basis	January 1, 2015	December 31, 2015	December 31, 2016
Bank credit in NIS	2.2	NIS-Unlinked	\$ 378	\$ 51	\$-
Bank credit in USD	3-6	USD-Unlinked	2,853	-	996
Short-term bank loans	1.6-2.35	NIS-Unlinked	15,313	21,273	42,336
Current maturities of long-term loans from banks and other financial institutions (see Note 11)	2.6-5.85	NIS-Unlinked	26,127	36,378	40,054
Accumulated interest on long-term loans from other financial institutions (see Note 11)	2.6-5.5	NIS-Unlinked	1,372	1,367	1,338
Other			-	13	36

Total \$ 46,043 \$ 59,082 \$ 84,760

c. Other accounts payable:

Composition:

	January 1, 2015	December 31, 2015	December 31, 2016
Government institutions	\$ 15,094	\$ 20,119	\$ 22,777
Customer advances	187	697	617
Accrued royalties to the OCS (Note 15f)	788	754	495
Accrued expenses and other current liabilities	14,864	17,991	18,000
Total	\$ 30,933	\$ 39,561	\$ 41,889

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Note 20:- Supplementary Financial Statement Information (Cont.)

d. Non-controlling interest in material partially owned subsidiaries:

	January 1, 2015	December 31, 2015	December 31, 2016
Matrix	\$ 83,389	\$ 86,567	\$ 91,606
Sapiens	178,132	182,757	188,470
Magic Software	105,962	105,958	107,271
Other	41	98	108
	\$ 367,524	\$ 375,380	\$ 387,455

e. Financial income and expenses:

Composition:

	Year ended	
	December 31, 2015	2016
Financial expenses:		
Business combination and redeemable non-controlling interests revaluation	\$ 1,204	\$ 2,602
Bank charges, interest and foreign exchange differences	6,370	6,972
Interest expenses on short-term and long-term loans	6,830	6,061
Financial costs related to Debentures	551	1,959
	14,955	17,594
Financial income:		
Income from marketable securities	1,122	865
Interest income from deposits and foreign exchange differences	4,300	5,143
	5,422	6,008

Total

\$(9,533) \$(11,586)

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Note 20:- Supplementary Financial Statement Information (Cont.)

f. Operating segments:

The Company operates in the software services and proprietary software products and related services through four directly held entities: Matrix, Sapiens, Magic and Insync.

Matrix

Matrix provides software solutions and services, software development projects, outsourcing, integration of software systems and services – all in accordance with its customers' specific needs. Matrix also provides upgrading and expansion of existing software systems.

Matrix operates through its directly and indirectly held subsidiaries in the following segments: (1) Software solutions and services in Israel (Information Technology – IT); (2) Software solutions and services in the U.S (Information Technology – IT) (3) Learning and integration; (4) Computer infrastructure and integration solutions; and, (5) Software product marketing and support.

Software solutions and services in Israel:

The software solutions and services in Israel provided by Matrix consist mainly of providing tailored software solutions and upgrading and expanding existing software systems. These services include, among others, developing customized software, adapting software to the customer's specific needs, implementing software and modifying it based on the customer's needs, outsourcing, project management, software testing and QA and integrating all or part of the above elements. The scope of work invested in each element varies from one customer to the other.

Software solutions and services in U.S:

Activity in this sector is mainly providing solutions and services of Governance Risk and Compliance ("GRC") experts, including activities on the following topics: risk management, management and prevention of fraud, Anti-Money Laundering and securing compliance with the regulations on these issues, through Matrix-IFS (formerly Exzac Inc.), a wholly owned subsidiary of Matrix, as well as providing solutions and specialized technological services in areas such as: portals, BI (Business Intelligence) DBA (Data Base Administration), CRM (Customer Relation Management) and EIM (Enterprise Information Management), and in addition, the activity in this segment includes IT help desk services specializing in healthcare and software product distribution services particularly IBM products. The activity in this segment is performed mostly through Matrix IFS and Xtivia Technologies Inc, wholly owned subsidiaries of Matrix.

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Note 20:- Supplementary Financial Statement Information (Cont.)

Learning and integration:

Matrix's activities in this segment consist of operating a network of high-tech training and instruction centers which provide application courses, professional training courses and advanced professional studies in the high-tech industry, courses of soft skills and management training and provision of training and implementation of computer systems.

Computer infrastructure and integration solutions:

Matrix's activities in this segment is primarily providing computer solutions to computer and communications infrastructures, marketing and sale of computers and peripheral equipment to business customers, providing related services, and cloud computing solutions (through the business specializing unit of the Company - Cloud Zone) and a myriad of services regarding Database services and Big data services (through the specialized business unit Data zone).

Software product marketing and support:

Matrix's activities in this segment include marketing, distributing and support for various software products the principal of which are CRM, computer systems management infrastructures, web world content management, database and data warehouse mining, application integration, database and systems, data management and software development tools.

Sapiens

Sapiens is a leading global provider of proprietary software solutions for the insurance industry, with an emerging focus on the broader financial services sector. Sapiens offerings include a broad range of software solutions and services, comprised of (i) core software solutions for the insurance industry, including Property & Casualty/General Insurance ("P&C") and Life, Annuities and Pensions ("L&P") products, and record keeping software solutions for providers of Retirement Services (ii) variety of technology based solution including business decision management solutions for the financial services industry, including insurance, banking and capital markets and (iii) global Services including project delivery and implementation of the Company' software solutions.

Sapiens has developed scalable, configurable, rule-based core software platforms which offer its clients comprehensive and function-rich solutions. Sapiens solutions allow its customers to support new delivery channels such as mobile and social, rapidly deploy new products, and improve operational efficiency. As its software is customizable to match specific business requirements, it supports its customers' operations across different market segments, geographies and regulatory regimes. In addition, its software solutions enable compliance with complex and rapidly evolving regulations in the insurance and wider financial services industry.

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Note 20:- Supplementary Financial Statement Information (Cont.)

Sapiens technology-based solutions include application development and business decision management platforms. Its application development platforms allow for the deployment of tailor-made solutions that address unique business needs for which pre-packaged software solutions may not be available. Its business decision management platform, Sapiens DECISION, allows business professionals to design, simulate, implement, change and analyze the business logic that drives financial operations and compliance in a business-friendly format and environment. Its platform facilitates the swift deployment of new or changed business logic that originates from regulatory updates or market changes, reduces costs and improves efficiency by shortening the software development lifecycle. This platform empowers the organization's business users as they manage their business strategy, rules and logic by using business terms rather than programming language. Sapiens' insurance solutions are deployed at leading insurance carriers globally. Sapiens' service offerings include a standard consulting offering that helps customers make better use of IT in order to achieve their business objectives.

Magic

Magic is a global provider of proprietary application development and business process integration software solutions and related professional services, and a vendor of IT outsourcing services.

Magic software solutions are used by customers to develop, deploy and integrate on-premise, mobile and cloud-based business applications quickly and cost effectively. In addition, its technology enables enterprises to accelerate the process of delivering business solutions that meet current and future needs and allow customers to dramatically improve their business performance and return on investment. Its software solutions include application platforms for developing and deploying specialized and high-end large-scale business applications (Magic xpa application platform, formerly branded uniPaaS and Appbuilder) and an integration platform that allows the integration and interoperability of diverse solutions, applications and systems in a quick and efficient manner (Magic xpi business and process integration platform, formerly branded iBOLT). These solutions enable Magic customers to improve their business performance and return on investment by supporting the affordable and rapid delivery and integration of business applications, systems and databases. Note 18: -Supplementary Financial Statement Information (Cont.)

Using its products solutions, enterprises and independent software vendors can accelerate time-to-market by rapidly building integrated solutions, deploying them in multiple environments while leveraging existing IT resources. In

addition, its solutions are scalable and platform-agnostic, enabling its customers to build solutions by specifying their business logic requirements in a commonly used language rather than in computer code, and to benefit from seamless platform upgrades and cross-platform functionality without the need to re-write applications. Magic technology also enables future proof protection and supports current market trends such as the development of mobile applications that can be deployed on a variety of smartphones and tablets, and cloud environments.

With respect to IT outsourcing services, Magic offers a vast range of professional services in the areas of infrastructure design and delivery, application development, technology consulting planning and implementation services, support services and supplemental outsourcing and staffing services.

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Note 20:- Supplementary Financial Statement Information (Cont.)

Magic products and services are available through a global network of regional offices, independent software vendors, system integrators, distributors and value added resellers as well as original equipment manufacturers and consulting partners in approximately 50 countries.

Insync

InSync is a U.S based national supplier of employees to Vendor Management Systems (VMS) Workforce Management Program accounts. Insync specializes in providing professionals in the following areas; Accounting and Finance, Administrative, Customer Service, Clinical, Scientific and Healthcare, Engineering, Manufacturing and Operations, Human Resources, IT Technology, LI/MFG, and Marketing and Sales. InSync currently supports more than 30 VMS program customers with employees in over 40 states.

The Company evaluates the performances of each of its directly held subsidiaries based on operating income/loss. Headquarters and finance expenses of Formula are allocated proportionally among the subsidiaries:

Goodwill in material partially owned subsidiaries:

	January 1, 2015	December 31, 2015	December 31, 2016
Matrix	\$ 156,224	\$ 162,283	\$ 187,790
Sapiens	213,093	215,430	218,992
Magic Software	55,490	63,308	91,002
	\$ 424,807	\$ 441,021	\$ 497,784

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Note 20:- Supplementary Financial Statement Information (Cont.)

	Matrix	Sapiens	Magic	Insync	Adjustments	Total
Year ended December 31, 2016:						
Revenues from external customers	660,012	216,190	198,096	34,323	-	1,108,621
Inter-segment revenues	2,578	-	3,550	-	(6,128)	-
Total Revenues	662,590	216,190	201,646	34,323	(6,128)	1,108,621
Unallocated corporate expenses	-	-	-	-	(2,626)	(2,626)
Depreciation and amortization	6,513	14,079	11,608	245	73	32,518
Operating income (loss)	46,220	26,326	17,520	1,060	(2,626)	88,500
Financial income (expense) net						(11,586)
Group's share of earnings (losses) of companies accounted for at equity, net						349
Taxes on income						(21,163)
Net income						56,100
Year ended December 31, 2015:						
Revenues from external customers	583,661	185,123	174,491	29,919	-	973,194
Inter-segment revenues	2,921	-	1,539	-	(4,460)	-
Revenues	586,582	185,123	176,030	29,919	(4,460)	973,194
Unallocated corporate expenses	-	-	-	-	(5,200)	(5,200)
Depreciation and amortization	6,144	14,127	9,885	280	2	30,438