

**On Track Innovations Ltd.
and Subsidiaries**

**Interim Consolidated
Financial Statements
As of September 30, 2008
(Unaudited)**

Interim Consolidated Financial Statements as of September 30, 2008

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Interim Consolidated Balance Sheets

US dollars in thousands, except share and per share data

| | September 30 2008 (Unaudited) | December 31 2007 (Audited) |
|---|--|---|
| Assets | | |
| Current Assets | | |
| Cash and cash equivalents | \$ 21,633 | \$ 35,470 |
| Short-term investments | 10,323 | 6,379 |
| Trade receivables (net of allowance for doubtful accounts of \$ 2,837 and \$2,767 as of September 30, 2008 and December 31, 2007, respectively) | 7,158 | 8,028 |
| Other receivables and prepaid expenses | 3,472 | 3,636 |
| Inventories | <u>12,131</u> | <u>13,242</u> |
| Total current assets | <u>54,717</u> | <u>66,755</u> |
| Severance pay deposits fund | 2,091 | 1,576 |
| Investment in an affiliated company | 1,217 | 1,382 |
| Property, plant and equipment, net | 19,179 | 20,851 |
| Intangible assets, net | 4,285 | 4,509 |
| Goodwill | <u>24,569</u> | <u>23,387</u> |
| Total Assets | <u>\$ 106,058</u> | <u>\$ 118,460</u> |

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

Interim Consolidated Balance Sheets

US dollars in thousands, except share and per share data

| | September 30 2008 (Unaudited) | December 31 2007 (Audited) |
|--|--|---|
| Liabilities and Shareholders' Equity | | |
| Current Liabilities | | |
| Short-term bank credit and current maturities of long-term bank loans | \$ 5,662 | \$ 5,336 |
| Trade payables | 7,886 | 10,291 |
| Other current liabilities | 4,720 | 5,344 |
| Total current liabilities | <u>18,268</u> | <u>20,971</u> |
| Long-Term Liabilities | | |
| Long-term loans, net of current maturities | 2,097 | 2,432 |
| Accrued severance pay | 4,862 | 3,981 |
| Deferred tax liabilities | 730 | 728 |
| Total long-term liabilities | <u>7,689</u> | <u>7,141</u> |
| Total liabilities | <u>25,957</u> | <u>28,112</u> |
| Minority interests | <u>352</u> | <u>-</u> |
| Shareholders' Equity | | |
| Ordinary shares of NIS 0.1 par value: authorized - 50,000,000 shares as of September 30, 2008 and December 31, 2007; issued 21,135,190 and 19,627,068 shares as of September 30, 2008 and December 31, 2007, respectively; Outstanding 21,021,838 and 19,434,011 as of September 30, 2008 and December 31, 2007, respectively | 497 | 454 |
| Additional paid-in capital | 181,438 | 174,494 |
| Accumulated other comprehensive income | 615 | 846 |
| Accumulated deficit | <u>(102,801)</u> | <u>(85,446)</u> |
| Total shareholders' equity | <u>79,749</u> | <u>90,348</u> |
| Total Liabilities and Shareholders' Equity | <u>\$ 106,058</u> | <u>\$ 118,460</u> |

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

Interim Consolidated Statements of Operations

US dollars in thousands, except share and per share data

| | Nine months ended September 30 | | Three months ended September 30 | |
|--|--------------------------------|-------------|---------------------------------|-------------|
| | 2008 | 2007 | 2008 | 2007 |
| | (Unaudited) | (Unaudited) | (Unaudited) | (Unaudited) |
| Revenues | | | | |
| Sales | \$ 29,265 | \$ 28,617 | \$ 10,317 | \$ 9,328 |
| Licensing and transaction fees | 1,884 | 1,852 | 546 | 527 |
| Total revenues | 31,149 | 30,469 | 10,863 | 9,855 |
| Cost of revenues | | | | |
| Cost of sales | 19,093 | 18,467 | 6,052 | 6,260 |
| Total cost of revenues | 19,093 | 18,467 | 6,052 | 6,260 |
| Gross profit | 12,056 | 12,002 | 4,811 | 3,595 |
| Operating expenses | | | | |
| Research and development | 8,909 | 8,203 | 3,008 | 3,050 |
| Selling and marketing | 8,086 | 6,858 | 2,911 | 2,797 |
| General and administrative | 10,559 | 13,444 | 3,210 | 6,397 |
| Amortization of intangible assets | 1,025 | 986 | 367 | 329 |
| Total operating expenses | 28,579 | 29,491 | 9,496 | 12,573 |
| Operating loss | (16,523) | (17,489) | (4,685) | (8,978) |
| Financial income (expense), net | (667) | 1,472 | (101) | 281 |
| Other expense, net | - | (111) | - | - |
| Loss before taxes on income and minority interests | (17,190) | (16,128) | (4,786) | (8,697) |
| Taxes on income | 177 | 197 | 55 | 66 |
| Minority interest | - | 1,037 | - | 847 |
| Equity in loss of affiliate | (342) | (271) | (92) | (109) |
| Net loss | \$ (17,355) | \$ (15,165) | \$ (4,823) | \$ (7,893) |
| Basic and diluted net loss per ordinary share | \$ (0.86) | \$ (0.81) | \$ (0.23) | \$ (0.41) |
| Weighted average number of ordinary shares used in computing basic and diluted net loss per ordinary share | 20,091,808 | 18,788,245 | 20,857,776 | 19,080,884 |

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

Interim Consolidated Statements of Shareholders' Equity and Comprehensive Loss

US dollars in thousands, except share and per share data

| | Number of Shares issued | Share capital | Additional paid-in capital | Accumulated other comprehensive income | Accumulated deficit | Total shareholders' equity |
|--|----------------------------|------------------|----------------------------------|---|------------------------|----------------------------------|
| Balance as of December 31, 2006 (audited) | 18,592,880 | \$ 431 | \$ 163,102 | \$ 424 | \$ (64,803) | \$ 99,154 |
| Changes during the nine-month period ended September 30, 2007 (unaudited): | | | | | | |
| Stock-based compensation related to options and shares issued to employees and others | - | - | 5,053 | - | - | 5,053 |
| Exercise of options and warrants | 241,578 | 8 | - | - | - | 8 |
| Shares and warrants issued in connection with the purchase of property plant and equipment | 530,000 | 9 | 3,557 | - | - | 3,566 |
| Foreign currency translation adjustments | - | - | - | 462 | - | 462 |
| Net unrealized loss on available-for-sale securities | - | - | - | (33) | - | (33) |
| Net loss | - | - | - | - | (15,165) | (15,165) |
| Balance as of September 30, 2007 (unaudited) | 19,364,458 | \$ 448 | \$ 171,712 | \$ 853 | \$ (79,968) | \$ 93,045 |
| Balance as of December 31, 2007 (audited) | 19,627,068 | \$ 454 | \$ 174,494 | \$ 846 | \$ (85,446) | \$ 90,348 |
| Changes during the nine-month period ended September 30, 2008 (unaudited): | | | | | | |
| Stock-based compensation related to options and shares issued to employees and others | - | - | 5,294 | - | - | 5,294 |
| Exercise of options and warrants | 1,207,424 | 34 | 734 | - | - | 768 |
| Shares and options issued in connection with the purchase of a subsidiary | 300,698 | 9 | 916 | - | - | 925 |
| Foreign currency translation adjustments | - | - | - | (208) | - | (208) |
| Net unrealized loss on available-for-sale securities | - | - | - | (23) | - | (23) |
| Net loss | - | - | - | - | (17,355) | (17,355) |
| Balance as of September 30, 2008 (unaudited) | 21,135,190 | \$ 497 | \$ 181,438 | \$ 615 | \$ (102,801) | \$ 79,749 |

| | Nine months ended September 30 | | Three months ended September 30 | |
|---|-----------------------------------|---------------------|------------------------------------|---------------------|
| | 2008 (Unaudited) | 2007 (Unaudited) | 2008 (Unaudited) | 2007 (Unaudited) |
| Total comprehensive loss: | | | | |
| Net loss | \$ (17,355) | \$ (15,165) | \$ (4,823) | \$ (7,893) |
| Foreign currency translation adjustments | (208) | 462 | (421) | 221 |
| Net unrealized gain on available-for-sale securities | (12) | 43 | (44) | 25 |
| Reclassification adjustment for gain on available-for-sale securities | (11) | (76) | (9) | (2) |
| Total comprehensive loss | \$ (17,586) | \$ (14,736) | \$ (5,297) | \$ (7,649) |

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

Interim Consolidated Statements of Cash Flows

US dollars in thousands, except share and per share data

| | Nine months ended September 30 | |
|---|---------------------------------------|-------------------------|
| | 2008 | 2007 |
| | (Unaudited) | (Unaudited) |
| Cash flows from operating activities | | |
| Net loss | \$ (17,355) | \$ (15,165) |
| Adjustments required to reconcile net loss to net cash used by operating activities: | | |
| Stock-based compensation related to options and shares issued to employees and others | 5,134 | 5,053 |
| Equity in loss of an affiliate company | 342 | 271 |
| Amortization of intangible assets | 1,025 | 986 |
| Depreciation | 2,578 | 1,792 |
| Minority interest | - | (1,037) |
| Accrued severance pay, net | 366 | 190 |
| Decrease in deferred tax liabilities | (183) | (197) |
| Decrease in trade receivables | 878 | 4,400 |
| Decrease (increase) in other receivables and prepaid expenses | 240 | (768) |
| Decrease (increase) in inventories | 1,127 | (2,312) |
| Increase (decrease) in trade payables | (2,420) | 83 |
| Increase (decrease) in other current liabilities | (631) | 579 |
| Other, net | 17 | (257) |
| Net cash used in operating activities | <u>\$ (8,882)</u> | <u>\$ (6,382)</u> |
| Cash flows from investing activities | | |
| Acquisition of consolidated subsidiaries, net of cash acquired (Supplement C) | (565) | - |
| Proceeds from maturity of available -for sale securities | 24,621 | 67,569 |
| Purchase of available-for sale securities | (28,574) | (64,356) |
| Purchase of property and equipment | (1,176) | (2,795) |
| Receipts on account of loans and receivables | - | 237 |
| Other, net | 21 | (19) |
| Net cash provided by (used in) investing activities | <u>\$ (5,673)</u> | <u>\$ 636</u> |
| Cash flows from financing activities | | |
| Increase in short-term bank credit, net | 333 | 2,003 |
| Exercise of options and warrants | 768 | 8 |
| Repayment of long-term bank loans | (389) | (257) |
| Net cash provided by financing activities | <u>712</u> | <u>1,754</u> |
| Effect of exchange rate changes on cash | <u>6</u> | <u>88</u> |
| Decrease in cash and cash equivalents | (13,837) | (3,904) |
| Cash and cash equivalents at the beginning of the period | <u>35,470</u> | <u>30,049</u> |
| Cash and cash equivalents at the end of the period | <u>\$ 21,633</u> | <u>\$ 26,145</u> |

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

Interim Consolidated Statements of Cash Flows (cont'd)

US dollars in thousands, except share and per share data

| | Nine months ended September 30 | |
|--|---------------------------------------|--------------------|
| | 2008 | 2007 |
| | (Unaudited) | (Unaudited) |
| Supplementary cash flows activities: | | |
| A. Cash paid during the period for: | | |
| Interest | \$ 47 | \$ 82 |
| Income taxes | \$ 6 | \$ 19 |
| B. Non-cash transactions: | | |
| Purchase of property and property and equipment | 90 | 3,566 |
| C. Acquisition of a consolidated subsidiary | | |
| Assets and liabilities of the subsidiary at date of acquisition: | | |
| Property and equipment | (31) | - |
| Goodwill | (830) | - |
| Technology | (59) | - |
| Customer contract | (561) | - |
| Non competition agreement | (194) | - |
| Deferred tax liabilities | 185 | - |
| Issuance of shares in consideration for the acquisition | 775 | - |
| Direct costs of acquisition paid via grant of shares and options | 150 | - |
| | \$ (565) | - |

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

Notes to the Interim Consolidated Financial Statements

US dollars in thousands, except share and per share data

Note 1 - Organization and Basis of Presentation

A. Description of business

On Track Innovations Ltd. (the "Company") was founded in 1990, in Israel. The Company and its subsidiaries (together "the Group") are principally engaged in the field of design and development of contactless microprocessor-based smart card systems. Commencing November 2002, the Company's shares are listed for trading on NASDAQ.

B. Basis of presentation

The accompanying unaudited interim consolidated financial statements contain all adjustments (consisting only of normal recurring adjustments) which, in the opinion of management, are necessary to present fairly, the financial information included therein. It is suggested that these financial statements be read in conjunction with the audited consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 20-F for the year ended December 31, 2007. Results for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

Note 2 – The allotment of shares of Millennium Card Technology Ltd. ("MCT") to the Company

In September 2008, the Company's subsidiary MCT has allotted additional 3,000 shares of HK\$1.00 to the Company against the waiver of the debt of MCT to the Company in the principle amount of USD 6,900,000, so that such loan shall be converted into the said 3,000 shares.

Following the proposed shares allotment, MCT's share capital will be held 90% by the Company.

Note 3 – Acquisition of ID Parking

In June 2008, the Company completed, through its subsidiary PARX Ltd, the purchase of 100% of the share capital of ID Parking, a France-based company that provides electronic parking solutions across France.

ID Parking was purchased for an aggregate purchase price of 750,000 euro (not included \$319 thousand transaction costs), comprised of 250,000 euro (\$396 thousand) in cash and 500,000 euro (\$775 thousand) in the Company's ordinary shares. The ID Parking Transaction shares are subject to a lock-up arrangement, under which one third of those shares (100,233 ordinary shares) will be released from lock-up every six months for an aggregate period of 18 months following June 30, 2008 (closing date). According to the lock up arrangement, the number of shares will be calculated according to the actual share price at the time of their release. In the case that the share value exceeds 500,000 Euro, a respective amount of shares will be forfeited, and if the value is less than 500,000 Euro, the Company will pay the difference in cash.

A maximum of up to 300,698 of the Company's ordinary shares have been allocated to complete the Transaction.

The acquisition was accounted for as a purchase and the Company allocated the purchase price according to the fair value of the tangible and intangible assets acquired and liabilities assumed.

ID Parking operations have been included in the Company's consolidated financial statements since June 30, 2008. In connection with the acquisition the Company recognized three intangible assets: customer contract, fair value of \$455 thousand, non competition agreement, fair value of \$127 thousand and technology, fair value of \$48 thousand. The Company also recognized goodwill in the amount of \$725 thousand.

Notes to the Interim Consolidated Financial Statements

US dollars in thousands, except share and per share data

Note 4 - Inventories

Inventories consisted of the following:

| | September 30 2008 (Unaudited) | December 31 2007 (Audited) |
|-------------------|--|---|
| Raw materials | \$ 4,759 | \$ 4,697 |
| Work in progress | 4,328 | 5,530 |
| Finished products | 3,044 | 3,015 |
| | \$ 12,131 | \$ 13,242 |

Note 5 - Recently Issued Accounting Pronouncements

1. SFAS 141R - Business Combinations (SFAS 141R)

In December 2007, the Financial Accounting Standards Board ("FASB") issued FASB Statement No. 141R, Business Combinations ("SFAS 141R"). SFAS 141R requires most identifiable assets, liabilities, noncontrolling interests, and goodwill acquired in a business combination to be recorded at "full fair value". SFAS 141R is effective for periods beginning on or after December 15, 2008, and earlier adoption is prohibited. SFAS 141R will be applied to business combinations occurring after the effective date.

The Company does not expect the adoption of SFAS 141R to have a material impact on its balance sheet or statement of operations.

2. SFAS 160 – Noncontrolling Interest in Consolidated Financial Statements (SFAS 160)

In December 2007, the FASB issued FASB Statement No. 160, Noncontrolling Interests in Consolidated Financial Statements – an amendment to ARB No. 51 ("SFAS 160"). SFAS 160 requires noncontrolling interests (previously referred to as minority interests) to be reported as a component of equity, which changes the accounting for transactions with noncontrolling interest holders. SFAS 160 is effective for periods beginning on or after December 15, 2008, and earlier adoption is prohibited. SFAS 160 will be applied prospectively to all noncontrolling interests, including any that arose before the effective date.

The Company does not expect the adoption of SFAS 160 to have a material impact on its balance sheet or statement of operations.

3. SFAS 161 – Disclosures about Derivative Instruments and Hedging Activities (SFAS 161)

In March 2008, the FASB issued FASB Statement No. 161, Disclosures about Derivative Instruments and Hedging Activities ("SFAS 161"). SFAS 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand the effects of the derivative instruments on an entity's financial position, financial performance, and cash flows. It is effective for financial statements issued for fiscal years and interim periods beginning on or after November 15, 2008, with early adoption encouraged.

The Company does not expect the adoption of SFAS 161 to have a material impact on its balance sheet or statement of operations.

Notes to the Interim Consolidated Financial Statements

US dollars in thousands, except share and per share data

Note 6 -Recently Adopted Accounting Pronouncements

1. SFAS 157 – Fair Value Measurements (SFAS 157)

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurement (“SFAS 157”). SFAS 157 defines fair value, establishes a framework for the measurement of fair value, and enhances disclosures about fair value measurements. The Statement does not require any new fair value measures. SFAS 157 is effective for fair value measures already required or permitted by other standards for fiscal years beginning after November 15, 2007. The Company is required to adopt SFAS 157 beginning on January 1, 2008. SFAS 157 is required to be applied prospectively, except for certain financial instruments. Any transition adjustment will be recognized as an adjustment to opening retained earnings in the year of adoption. In February 2008, the FASB issued SFAS No. 157-2, which grants a one-year deferral of SFAS 157’s fair-value measurement requirements for nonfinancial assets and liabilities, except for items that are measured or disclosed at fair value in the financial statements on a recurring basis. The adoption of SFAS 157 did not have a material effect on the Company’s balance sheet or results of operations.

2. SFAS 159 – Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159)

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (“SFAS 159”). SFAS 159 permits all entities the option to measure most financial instruments and certain other items at fair value at specified election dates and to report related unrealized gains and losses in earnings. The fair value option will generally be applied on an instrument-by-instrument basis and is generally an irrevocable election. SFAS 159 is effective for fiscal years beginning after November 15, 2007. The adoption of SFAS 159 did not have a material effect on the Company’s balance sheet of results of operations.

3. EITF 07-03 -Accounting for Advance Payments for Goods or Services to Be Used in Future Research and Development Activities” (“EITF 07-03”)

In June 2007, the FASB reached a final consensus on Emerging Issues Task Force Issue 07-3, “Accounting for Advance Payments for Goods or Services to Be Used in Future Research and Development Activities” (“EITF 07-03”). The consensus reached by the FASB requires companies involved in research and development activities to capitalize such non-refundable advance payments for goods and services pursuant to an executory contractual arrangement because the right to receive those services in the future represents a probable future economic benefit. Those advance payments will be capitalized until the goods have been delivered or the related services have been performed. The consensus on EITF 07-03 is effective prospectively for financial statements issued for fiscal years beginning after December 15, 2007, and interim periods within those fiscal years. Earlier application is not permitted. The adoption of EITF 07-03 did not have a material effect on the Company’s balance sheet of results of operations.

