

Tescom Software Systems Testing Ltd. (“Tescom” or “the Company”)

Quarterly Results for the Three Months Ended 31 March 2006

Tescom Software Systems Testing Ltd. (Symbol: TSCM), the international quality assurance and software testing service provider, announces its quarterly results for the three months ended 31 March 2006.

Highlights

- Revenues increased by 15.1% to NIS 59.6m (\$12.8m), versus NIS 51.8m in Q105
- Gross margins were 32.5%, compared to 38.7% in Q105
- Profit before tax was NIS 1.6m (\$0.3m), versus NIS 4.5m in Q105
- Diluted earnings per share were NIS 0.06 (\$0.01), versus NIS 0.19 in Q105
- Commencement of work on landmark transaction as main contractor with the Ministry of Finance in France
- New contract wins in the UK, US, Singapore and Australia
- Strengthening of senior sales and marketing management in the UK, US and Israel

Ofer Albeck, CEO of Tescom, said: “Tescom’s Q106 results reflect a significant increase in revenues over Q105, particularly in the UK, as well as in France, where our contract with the French Ministry of Finance has commenced. We look forward to a continuing positive trend in our top line throughout 2006, as the reorganization and strengthening of our senior sales and management team begins to bear fruit. The market in Israel remains extremely competitive, which has had a negative effect on our gross margins and profitability. In addition, the loss of a major customer in Australia has also affected profitability.

Despite this, Tescom has won a number of major new contracts, including long-term fixed contracts in the public sector, from which we expect to benefit during the remainder of 2006. We are looking at various strategic initiatives to increase our gross margins, including assessing the feasibility of staffing certain projects from less costly off-shore locations where suitable. We anticipate these initiatives will begin to have a positive effect on our operating results in the latter half of 2006.”

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Chief Executive's Review

Tescom's revenues increased by 15.1% from Q105, to NIS 59.6m (\$12.8m). Revenues increased in the UK, Continental Europe and in the US, mainly as a result of new large contracts in each of these three locations. Tescom's strategy is to continue focusing its efforts on large projects with fixed-price contracts, mainly in Europe and the US. During the quarter, the Company began work on a three-year contract with the French Ministry of Finance, and the Company hopes to leverage its experience in this area in order to position itself to benefit from other public sector projects throughout Europe.

In the UK, Tescom has been successful at gaining new contracts in both the private and public sector, working for the Governmental departments that perform testing on projects being carried out by systems integrators such as EDS. In early 2006, BSkyB made Tescom their principal supplier for testing across the UK, and Vodafone announced its continuing relationship with Tescom, including the successful project regarding their "push e-mail" service.

Tescom continues to make progress in the US, after winning several long-term contracts in the state and local government sector. Increased revenues in the US reflect the Company's performance on these contracts.

In the Asia-Pacific region, Tescom Singapore has won a new contract with the Land Transport Authority of Singapore and Tescom Australia signed a new contract with the Victorian State Government. These wins have partially offset the loss in revenues from the completion in 2005 of a large contract with Telstra.

Tescom Israel has experienced a small increase in revenues over the comparative quarter in 2005, primarily due to several new large contracts at top-tier customers in the Israeli market, including Teva and Straus-Elite. These wins were partially offset by a reduction in activity in the defence sector. The market continues to be very competitive, which is reflected in significantly lower margins. In light of this, Tescom Israel has taken steps to increase profitability in Israel, including the implementation of a cost reduction programme, and the restructuring and augmentation of its sales team.

Since the beginning of 2006, Tescom has strengthened its management team in a number of key areas. In January, Phil Serlin was appointed as Vice-President, Finance. Mr Serlin joined Tescom from Chiaro Networks Ltd. in Israel, where he served as Global Controller and Finance Manager since 2000. He brings extensive experience in financial reporting and regulatory affairs to Tescom.

In the first quarter, international operations outside Israel were consolidated into one division and David Oates was appointed to head it up. Based in Tescom's London office, he took up his position in April. Mr Oates joins Tescom from Primavera, where he was the Vice-President in charge of its international operations.

In April, Mika Liss, Tescom's Executive Vice-President in charge of Global Human Resources, was appointed interim Managing Director of Tescom's US operations. Ms Liss' appointment has coincided with the departure of Sarah Bajc from the Company's Atlanta office.

Financial Review

Tescom's shares are traded on both the AIM market of the London Stock Exchange and the Tel Aviv Stock Exchange. In accordance with Israeli securities regulations, the Company files its quarterly results with the Israel Securities Authority. The Company's primary financial statements for Q1 2006 have been prepared in adjusted New Israeli Shekels ("NIS") and in accordance with accounting principles generally accepted in Israel ("Israeli GAAP"). Comparative figures for Q1 2005 have been prepared on the same basis. The US dollar amounts as of 31 March 2006 and for the three months then ended have been translated from the NIS figures using the closing NIS/US dollar exchange rate of 4.665 as of 31 March 2006.

Results

Revenues increased by 15.1%, to NIS 59.6m (\$12.8m) from NIS 51.8m in Q105, primarily resulting from new contracts in the UK and the Company's major contract with the Ministry of Finance in France.

Pre-tax profit amounted to NIS 1.6m (\$0.3m), versus NIS 4.5m in Q105. Despite the significant increase in revenues, Q106 results were affected by a 6% reduction in gross margins, mainly as a result of increased competition in Israel and the completion of a high-margin contract in Australia in 2005. In addition, G&A expenses increased by NIS 1.5m during the quarter, to NIS 13.2m (\$2.8m) from NIS 11.7m in Q105. This increase reflects the required adoption in Q106 of a new accounting standard relating to stock-option compensation, as well as severance costs related to the former Managing Director in the Company's UK office. Sales and marketing expenditure increased slightly during the period, to NIS 4.0m (\$0.9m), from NIS 3.8m in Q105. The Company's results were also negatively impacted by an increase in financial expenses of NIS 0.6m (\$0.1m), due to exchange rate differences between the NIS and other operating currencies in the various Group locations, primarily the US dollar.

The Company used NIS 6.0m (\$1.3m) in cash for operating activities in Q106, versus NIS 2.1m of cash generated from operations in Q105. The reduction in operating cash flow results primarily from an increase in trade receivables, as well as a reduction in net profits. The Company's cash balance at 31 March 2006 was NIS 6.9m (\$1.5m), which also reflects the payment of an NIS 4.7m (\$1.0m) dividend in January 2006. The Company maintains short-term bank credit lines in both Israel and the UK in the aggregate amount of approximately NIS 30m. NIS 13.5m had been drawn against these lines as of 31 March 2006.

Share Buyback

The Board of Tescom announced in July 2005 that it had approved a share buyback of its ordinary shares on the open market. In November, the buyback programme was extended to 31 March 2006. The total amount approved for the share repurchase was approximately \$550,000. From the July approval to 31 March 2006, 218,545 shares were bought back by the Company for a total sum of approximately NIS 1.4m (\$0.3m). These shares are held as treasury shares by the Company.

Dividends

The Company's dividend policy is subject to the future performance of the Company and its funding requirements. The Company declared a total interim dividend of NIS 4.7m (\$1.0m) in the fourth quarter of 2005, which was paid in January 2006. In view of 2005 financial results, the Board decided not to award a final dividend on account of 2005, and has not declared an interim dividend in 2006 in respect of the three months ended 31 March 2006.

Outlook

Tescom has won a number of significant long-term contracts in 2005 and the first quarter of 2006. These new contracts have positively affected the top line in Q106 and this trend is expected to continue throughout the remainder of the year. Competitive pressures, particularly in the Israeli market, continue to affect gross margins and operating profits, although there are signs of improving performance. As a result, the Board remains cautious, at this early stage, in its outlook for the year as a whole.

The Board of Tescom continues to examine a number of strategic opportunities to expand its businesses in other regions and enhance shareholder value.

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED BALANCE SHEETS

| | Convenience Translation | | | |
|---|------------------------------------|----------------------|---------------------------|------------------------------|
| | March 31, 2006 | 2006 | March 31, 2005 | December 31, 2005 |
| | (US\$ 000's) | | (NIS 000's) | (NIS 000's) |
| ASSETS | | | | |
| CURRENT ASSETS: | | | | |
| Cash and cash equivalents | 1,487 | 6,935 | 9,145 | 12,213 |
| Trade receivables | 13,067 | 60,961 | 49,990 | 52,302 |
| Other current assets and prepaid expenses | 1,729 | 8,064 | 7,385 | 6,619 |
| | <u>16,283</u> | <u>75,960</u> | <u>66,520</u> | <u>71,134</u> |
| LONG-TERM DEPOSITS | <u>109</u> | <u>508</u> | <u>-</u> | <u>454</u> |
| FIXED ASSETS: | | | | |
| Cost | 3,835 | 17,894 | 16,270 | 17,508 |
| Less - accumulated depreciation | 2,772 | 12,932 | 13,840 | 12,409 |
| | <u>1,063</u> | <u>4,962</u> | <u>2,430</u> | <u>5,099</u> |
| OTHER ASSETS, NET | <u>497</u> | <u>2,316</u> | <u>5,337</u> | <u>2,202</u> |
| | <u><u>17,952</u></u> | <u><u>83,746</u></u> | <u><u>74,287</u></u> | <u><u>78,889</u></u> |

The accompanying note is an integral part of the consolidated financial statements.

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED BALANCE SHEETS

| | Convenience Translation | | | |
|---|------------------------------------|---------------|---------------------------|------------------------------|
| | March 31, 2006 | 2006 | March 31, 2005 | December 31, 2005 |
| | (US\$ 000's) | | (NIS 000's) | (NIS 000's) |
| LIABILITIES AND EQUITY | | | | |
| CURRENT LIABILITIES: | | | | |
| Short-term bank credit | 2,905 | 13,552 | 8,630 | 7,595 |
| Trade payables | 1,048 | 4,888 | 3,793 | 3,907 |
| Other current liabilities and accrued expenses | 6,919 | 32,278 | 24,132 | 31,555 |
| Dividend payable | - | - | - | 4,700 |
| | <u>10,872</u> | <u>50,718</u> | <u>36,555</u> | <u>47,757</u> |
| LONG-TERM LIABILITIES: | | | | |
| Long-term bank loans | 10 | 46 | 123 | 77 |
| Accrued severance pay, net | 362 | 1,691 | 1,124 | 1,253 |
| | <u>372</u> | <u>1,737</u> | <u>1,247</u> | <u>1,330</u> |
| EQUITY | <u>6,708</u> | <u>31,291</u> | <u>36,485</u> | <u>(*) 29,802</u> |
| | <u>17,952</u> | <u>83,746</u> | <u>74,287</u> | <u>78,889</u> |

(*) Restated

The accompanying note is an integral part of the consolidated financial statements.

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS

| | Convenience Translation | Three months ended | | Year ended |
|-------------------------------------|------------------------------------|---------------------------|-------------|---------------------|
| | Three months ended | Three months ended | | December 31, |
| | March 31, 2006 | 2006 | 2005 | 2005 |
| | (US\$ 000's) | (NIS 000's) | | (NIS 000's) |
| Revenues | 12,784 | 59,636 | 51,810 | 209,194 |
| Cost of revenues | 8,628 | 40,250 | 31,758 | 133,497 |
| Gross profit | 4,156 | 19,386 | 20,052 | 75,697 |
| Selling and marketing expenses | 855 | 3,992 | 3,834 | 12,154 |
| General and administrative expenses | 2,835 | 13,218 | 11,722 | (*) 55,393 |
| | 3,690 | 17,210 | 15,556 | (*) 67,547 |
| Operating income | 466 | 2,176 | 4,496 | (*) 8,150 |
| Financial income (expenses), net | (125) | (584) | 21 | 712 |
| Other expenses, net | (5) | (23) | - | (7,161) |
| Profit before taxes on income | 336 | 1,569 | 4,517 | (*) 1,701 |
| Taxes on income | 140 | 653 | 1,535 | 4,222 |
| Net profit (loss) | 196 | 916 | 2,982 | (*) (2,521) |
| Earnings (loss) per share | 0.01 | 0.06 | 0.19 | (*) (0.16) |

(*) Restated

The accompanying note is an integral part of the consolidated financial statements.

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

| | <u>Convenience Translation</u> | <u>Three months ended</u> | | <u>Year ended</u> |
|---|------------------------------------|-------------------------------------|------------|---------------------|
| | <u>Three months ended</u> | <u>Three months ended</u> | | <u>December 31,</u> |
| | <u>March 31, 2006</u> | <u>March 31, 2006 2005</u> | | <u>2005</u> |
| | <u>(US\$ 000's)</u> | <u>(NIS 000's)</u> | | <u>(NIS 000's)</u> |
| <u>Cash flows from operating activities</u> | | | | |
| Net profit (loss) | 196 | 916 | 2,982 | (*) (2,521) |
| Adjustments to reconcile net profit (loss) to net cash provided by (used in) operating activities (a) | (1,476) | (6,887) | (**) (866) | (*) 9,157 |
| Net cash provided by (used in) operating activities | (1,280) | (5,971) | (**) 2,116 | 6,636 |
| <u>Cash flow from investing activities</u> | | | | |
| Purchase of fixed assets | (37) | (174) | (481) | (4,345) |
| Proceeds from sale of fixed assets | 3 | 12 | - | 588 |
| Maturities of short-term bank deposits, net | - | - | 7,703 | 7,703 |
| Payments for forwards transactions | - | - | (**) (98) | (106) |
| Proceeds from sale of forward transactions | 16 | 78 | (**) 5 | 333 |
| Net cash provided by (used in) investing activities | (18) | (84) | (**) 7,129 | 4,173 |
| <u>Cash flows from financing activities</u> | | | | |
| Payment of dividends declared in prior year | (1,008) | (4,700) | - | - |
| Exercise of stock options | - | - | - | 3,676 |
| Shares repurchased by the Company | (142) | (662) | - | (796) |
| Repayment of convertible debentures | - | - | (19,643) | (19,643) |
| Proceeds of long-term bank loan | - | - | 184 | 184 |
| Repayment of long-term bank loan | (7) | (31) | - | (46) |
| Short term bank credit, net | 1,278 | 5,957 | (318) | (1,354) |
| Net cash provided by (used in) financing activities | 121 | 564 | (19,777) | (17,979) |
| Effect of exchange rate changes on cash and cash equivalents | 46 | 213 | (58) | (352) |
| Decrease in cash and cash equivalents | (1,131) | (5,278) | (10,590) | (7,522) |
| Cash and cash equivalents at the beginning of the period | 2,618 | 12,213 | 19,735 | 19,735 |
| Cash and cash equivalents at the end of the period | 1,487 | 6,935 | 9,145 | 12,213 |

(*) Restated

(**) Reclassified

The accompanying note is an integral part of the consolidated financial statements.

TESCOM SOFTWARE SYSTEMS TESTING LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Convenience Translation | Three months ended | | Year ended |
|---|------------------------------------|---------------------------|---------------------------|---------------------|
| | Three months ended | Three months ended | | December 31, |
| | March 31, 2006 | 2006 | March 31, 2005 | 2005 |
| | (US\$ 000's) | (NIS 000's) | | (NIS 000's) |
| a) <u>Adjustments to reconcile net profit (loss) to net cash provided by (used in) operating activities</u> | | | | |
| Depreciation and amortization | 79 | 378 | 520 | 1,539 |
| Impairment of goodwill | - | - | - | 2,600 |
| Deferred income taxes, net | (176) | (826) | (57) | (924) |
| Increase in accrued severance pay, net | 94 | 438 | 326 | 455 |
| Gain from forward transactions | (16) | (78) | (**) 93 | (227) |
| Loss (gain) on sale of fixed assets | - | 1 | - | (2) |
| Exchange differences on convertible debentures | - | - | 257 | 257 |
| Exchange differences on short-term deposits | - | - | 57 | 57 |
| Share-based compensation expenses | 53 | 248 | - | (*) 1,295 |
| Exchange differences on long-term loan | - | - | (1) | - |
| Increase in trade receivables | (1,719) | (8,028) | (128) | (2,463) |
| Decrease (increase) in other current assets and prepaid expenses (including long-term deposits) | (153) | (711) | 374 | 1,839 |
| Increase in trade payables | 198 | 925 | 401 | 544 |
| Increase (decrease) in other current liabilities and accrued expenses | 164 | 766 | (2,708) | 4,187 |
| | <u>(1,476)</u> | <u>(6,887)</u> | <u>(**) (866)</u> | <u>(*) 9,157</u> |
| b) <u>Non-cash transactions</u> | | | | |
| Dividend declared | - | - | - | 4,700 |
| Receivables in respect of shares | - | - | 3 | - |

(*) Restated

(**) Reclassified

The accompanying note is an integral part of the consolidated financial statements.

NOTE 1:- GENERAL AND PRESENTATION

The accompanying financial statements have been prepared in adjusted New Israeli Shekels (“NIS”) and in accordance with accounting principles generally accepted in Israel (“Israeli GAAP”). The US dollar amounts as of March 31, 2006 and for the three months then ended have been translated for the convenience of the reader, using the closing NIS/US dollar exchange rate of 4.665 as of March 31, 2006.

These financial statements should be read in conjunction with the Company's audited annual financial statements and accompanying notes as of December 31, 2005.

The restatements in these financial statements relate to the adoption of two new accounting standards during the reporting period in respect of stock-based compensation and earnings per share, pursuant to Israeli GAAP. Both of these accounting standards required restatement of prior periods.