

DEFENSE INDUSTRIES INTERNATIONAL INC  
Form 10-K  
April 14, 2011

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SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the fiscal year ended December 31, 2010

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

Commission File Number: 0-30105

DEFENSE INDUSTRIES INTERNATIONAL, INC.  
(Exact name of registrant as specified in its charter)

Nevada  
(State or other jurisdiction of  
incorporation or organization)

84-1421483  
(I.R.S. Employer  
Identification No.)

12 Hamefalsim Street, Petach Tikva  
Israel  
(Address of principal executive offices)

49514  
(Zip Code)

Registrant's telephone number (011) 972-3-7168383

Securities registered under Section 12(b) of the Act: None

Securities registered under Section 12(g) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, par value \$0.0001 per share	OTC Bulletin Board

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

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

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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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer  Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.)

Yes  No

The aggregate market value of the voting stock held by non-affiliates of the Registrant as of the most recently completed second fiscal quarter: \$1,041,689.64.

The number of the registrant's common shares (par value \$0.0001 per share) outstanding as of April 11, 2011 was 28,150,535 shares.

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## INTRODUCTION

Defense Industries International, Inc. is a manufacturer and global provider of personal military and civilian protective equipment and supplies. Our products are used by military, law enforcement, border patrol enforcement, and other special security forces, corporations, non-governmental organizations and individuals throughout the world. Our main products include body armor, bulletproof and stab-resistant clothing, combat vests, bomb disposal suits, battle pouch and combat harness units, flak jackets, ballistic helmets, dust protectors, padded coats, sleeping bags, weapon straps and belts, dry storage systems, liquid logistics products, ceramic and ultra high molecular weight materials (polyethylene plates which are used to manufacture personal military and civilian protective equipment), liquid logistic products (flexible water tanks in various sizes), ballistic wall coverings, tents, vehicle covers, VIP car armoring and lightweight vehicle armor kit production.

Our shares are traded on the Over the Counter Bulletin Board, or OTC Bulletin Board, under the symbol "DFNS.OB". As used in this annual report, the terms "we," "us" and "our" mean Defense Industries International, Inc. and its subsidiaries, unless otherwise indicated.

We use Achidatex, Export Erez, Isorad and Argo as trade names. All other trade names and trademarks appearing in this annual report are owned by their respective holders.

Our consolidated financial statements appearing in this annual report are prepared in U.S. dollars and in accordance with generally accepted accounting principles in the United States, or U.S. GAAP. All references in this annual report to "dollars" or "\$" are to U.S. dollars and all references in this annual report to "NIS" are to New Israeli Shekels.

Statements made in this annual report concerning the contents of any contract, agreement or other document are summaries of such contracts, agreements or documents and are not complete descriptions of all of their terms. If we filed any of these documents as an exhibit to this annual report or to any previous filing with the Securities and Exchange Commission, or SEC, you may read the document itself for a complete recitation of its terms.

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## FORWARD LOOKING STATEMENTS

This Annual Report on Form 10-K contains various "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, and within the Private Securities Litigation Reform Act of 1995, as amended. Such forward-looking statements reflect our current view with respect to future events and financial results. Forward-looking statements usually include the verbs "anticipates," "believes," "estimates," "expects," "intends," "plans," "projects," "understands" and other verbs suggesting uncertainty. We remind readers that forward-looking statements are merely predictions and therefore inherently subject to uncertainties and other factors and involve known and unknown risks that could cause the actual results, performance, levels of activity, or our achievements, or industry results, to be materially different from any future results, performance, levels of activity, or our achievements expressed or implied by such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

We have attempted to identify additional significant uncertainties and other factors affecting forward-looking statements in the Risk Factors section which appears in Item 1A.

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## PART I

### Item 1. Description of Business.

#### General

We are a manufacturer and global provider of personal military and civilian protective equipment and supplies. Our products are used by military, law enforcement, border patrol enforcement, and other special security forces, corporations, non-governmental organizations and individuals throughout the world.

Our main products include body armor, bomb disposal suits, bullet proof vests and jackets, tactical combat vests, ballistic wall coverings, bullet proof ceramic and polyethylene panels, V.I.P. car armoring and lightweight armor kits for vehicles, personal military equipment, dry storage systems, liquid logistic products, tents and other camping and travel gear.

#### Company History

Our predecessor was incorporated in the State of Utah on July 9, 1997 as Pawnbrokers Exchange, Inc. On July 8, 2002, we changed our corporate domicile from the State of Utah to the State of Nevada, through a merger with our then wholly owned subsidiary, Defense Industries International, Inc., or Defense Industries, a Nevada corporation organized on July 1, 2002. As part of the reincorporation, we changed our name to Defense Industries. Each issued and outstanding share of Pawnbrokers Exchange capital stock was converted into and exchanged for one share of Defense Industries common stock.

#### Organization

We are a holding company whose wholly owned subsidiaries include Export Erez USA, Inc., Rizzo Inc. (doing business as Owen Mills Company), or Owen Mills, Export Erez Ltd., or Export Erez, Mayotex Ltd., or Mayotex, Mayosar Technologies Ltd., or Mayosar, and Achidatex Nazareth Elite (1977) Ltd., or Achidatex. In addition, we hold 82% of the issued and outstanding share capital of Isorad IR Optics Ltd., or Isorad IR, and 20% of the issued and outstanding share capital of Mayo-Ben Investments and Development Ltd., or Mayo-Ben. We sometimes use the term Group to describe the operations of all of our subsidiaries as a group.

Export Erez is principally engaged in the design, production and marketing of personal military and civilian protective equipment and supplies such as body armor, bomb disposal suits, bulletproof vests, and associated heavy fabric products, such as battle pouches and combat harness units, tents and other camping equipment.

Achidatex is a leading manufacturer of ballistic shields, ultra high molecular weight materials, or UHMW materials, (which are used to manufacture personal military and civilian protective equipment), liquid logistic products (flexible water tanks in various sizes), combat flak jackets, tents and other personal military and civilian protective equipment and supplies. Achidatex also specializes in manufacturing long term storage systems for tanks, armored personnel carriers and other military vehicles, and for equipment that requires battlefield readiness and quick deployment, such as collapsible liquid storage tanks, mobile silos for storage of grains, liners for tank shipping systems, custom-made covers for artillery, vehicles, communication equipment, tarpaulins, various technical products and special-purpose defense items.

Mayotex is engaged in VIP car armoring and lightweight vehicle armor kit production.



In March 2011, Mayotex entered into an agreement to acquire all of the outstanding share capital of Philcar Ltd., an Israeli company operating in the field of equipping and armoring, lightweight and medium-weight vehicles. In December 2010, Mayotex acquired the business and intellectual property rights of Vacutec Industries Ltd., a manufacturer of fiberglass products for the automobile industry. We entered into these agreements in order to strengthen and broaden the scope of services and products offered by Mayotex. The closing of the agreement to acquire Philcar Ltd. is pending certain third parties consents to be obtained by Philcar and Philcar's parent company.

In December 2008, Mayotex entered into an investment agreement, or the Sarino Agreement, with Sarino Crystal Technologies Ltd. and Sarino Optronics Ltd., together Sarino, to form an entity which will cooperate in the manufacture of optical grade germanium crystals and the sale of lenses to be used in optical and infra-red night vision products utilizing the germanium crystals. Pursuant to the Sarino Agreement, Mayotex and Sarino incorporated Mayosar Technologies Ltd., or Mayosar, in which Mayotex held 50.1% of the outstanding shares and Sarino held the remaining 49.9% of the outstanding shares.

After a period of uncertainty, in December 2010 Sarino and Mayotex entered into a settlement agreement according to which Mayotex was registered as the holder of 100% of the issued and outstanding share capital of Mayosar and Mayosar in turn transferred its ownership interest in its then wholly owned subsidiary, Isorad IR Optics Ltd., or Optics, to Mayotex and Sarino

Pursuant to the above settlement agreement, Mayotex became the direct holder of 82% of the issued and outstanding share capital of Optics, a manufacturer of optical grade germanium crystals and lenses used in optical and infra-red night vision products utilizing the germanium crystals. For further details please see below under Item 7.

On October 27, 2010, our Mayotex subsidiary entered into an agreement to acquire a 20% stake in Mayo-Ben, a real estate company holding industrial properties in Israel which are occupied by our subsidiaries.

Owen Mills specializes in military and industrial sewing of marine and ballistic fabric products. Owen Mills manufactures in the U.S. many products similar to the products we manufacture in Israel.

In the fourth quarter of 2010, we began to implement a restructuring of our organizational structure aimed at improving the synergy within the Group by having each company within the Group specialize in a certain aspect of the Group's products and markets. As a part of this restructuring process, the Group leased two additional facilities in Sderot, Israel, a region which is defined by the Israeli Government as a 'national preference' and entitles a business that operates there to certain preferences in governmental tenders, in order to increase its manufacturing capacity. In addition, the Group acquired equipment and other fixed assets for these facilities. We estimate that this restructuring will be completed by the end of the second quarter of 2011. We intend to file petitions with the Israeli Investment Centre to obtain grants to finance some of the investments to be made within the framework of the restructuring process.

### Strategy

We believe that current international tensions, the continuing war on terrorism and military conflicts are all likely to result in additional interest in our products and that the demand for our products will continue to grow. We expect to address this growth by offering a comprehensive array of high quality branded security products that meet our customers' increasingly complex requirements. We also intend to enhance our position in the industry through additional strategic acquisitions that will broaden our portfolio of products.

The following elements define our growth strategy:

- Pursue strategic acquisitions. During 2010 we entered into an agreement to acquire the business of Vacutec Industries Ltd. and in March 2011 we entered into an agreement to acquire Philcar Ltd., both of which businesses complement our car armoring activities. We intend to continue to selectively pursue strategic acquisitions that complement our product offerings, provide access to new geographic markets, and provide additional distribution channels and new customer relationships.

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Pursue new strategic opportunities. We believe that the market for dry storage systems and solutions is a potential growth market for us and we are currently investing in the resources that will allow us to capitalize on opportunities in this market. We expanded our production capabilities in the U.S., where we leased larger premises and constructed a new production line, which is now fully operational.

- **Expand Distribution Networks and Product Offerings.** We expect to continue to strengthen our distribution network by expanding our range of branded law enforcement equipment through the acquisition of and by investing in the development of new and enhanced products which complement our existing offerings. We believe that a broader product line will strengthen our relationships with distributors and enhance our brand appeal with military, law enforcement and other end users.

## Products

We target our product at three principal markets (both international and local): the military and defense market, the civilian market and the industrial/agricultural market.

Our military products include body armor, bulletproof and stab-resistant clothing, combat vests, bomb disposal suits, battle pouch and combat harness units, flak jackets, ballistic helmets, dust protectors, padded coats, sleeping bags, weapon straps and belts, dry storage systems, liquid logistics products, ceramic and UHMW materials (which are used to manufacture personal military and civilian protective equipment), ballistic wall coverings, tents, and vehicle covers. Products currently under development include sophisticated stab-resistant solutions, lighter polyethylene ballistic plates and new lightweight vehicle armor kits.

Our second product group is intended for the civilian market, including law enforcement, border patrol enforcement, prison forces, special security forces, corporations, non-governmental organizations and individuals worldwide. Our civilian market products include adaptations of our military products, heavy-duty clothing and other types of sporting and camping equipment and clothing including, tents and sleeping bags. This product group includes armor for VIP luxury cars.

Our industrial/agricultural market products include special industrial fabrics and cloth tapes as well as flexible enclosures for temporary storage of agricultural products.

The following table details our current product line and target markets:

Product description	Target markets	Geographical market
Dust protectors and various covers	Military	International
Padded coats	Military, civilian	International
Protective vests and flak jackets	Military, civilian	International
Cooling jackets	Military	International
Overalls	Military	International
Vests	Military, civilian	International
Sleeping bags	Military, civilian	International
Carriers for grenade launchers	Military	International
Bags and totes	Military	International
Tents	Military, civilian	International
Camp beds	Military, civilian	International
Collapsible storage containers	Military, civilian	International
Evacuation stretchers	Military, civilian	International
Personal belts and weapon straps	Military	International
Woven fabrics: canvas, corduroy, nylon and aramid	Military, civilian, industrial	International
Ballistic wall coverings	Military, civilian, industrial	International

Ballistic plates and panels	Military, civilian	International
Car armor	Civilian	International
Lightweight vehicle armor kits	Military, civilian	International
Range of woven tapes	Military, civilian, industrial	International
Horseback riding accessories	Civilian	International
Long-term storage systems	Military, industrial/agricultural	International
Regular/digital colored printed truck coverings	Civilian	International
Ballistic aramid fabric	Military, civilian	International

We continue to improve our existing products and to develop new products for the military and the civilian markets, including mine protective shoes, stab-resistant solutions, improved armored car blast protection materials, and modified ballistic wall coverings. In addition, we are continuing to develop a new generation of complex products for protective vests to be used by security forces and armies.

## Product Quality

We have established a reputation for producing premium quality products that represent the cutting-edge in design and technological development. Through on going research and development efforts we believe that we are setting the standards for personal defense related products. Our manufacturing facilities meet American EQNET and the International ISO 9001; the United States Armed Forces MIL-STD-105D and MIL-I-45208A standards; the German Armed Forces and NATO AQAP standards; and the NIJ standards, NIJ 0101.03 and NIJ 0101.04, for “Ballistic Resistance of Personal Body Armor” that are accepted worldwide.

## Production

We develop, manufacture and assemble our own products in Israel and the United States. Our production facilities in Israel are located in Sderot, Nazareth, Ashkelon and the Alon Tavor Industrial Zone near Afula (which is currently being transferred to a new facility in Sderot). Our production facility in the United States is located in Van Nuys, California. We believe that we distinguish ourselves from most of our competition by our ability to manufacture the various components of our products and by the fact that we generally do not rely on other manufacturers. Our production process begins with the manufacture of fabrics and other basic components of our products and ends with quality control inspections of completed goods and products.

Our production facilities provide us with the capability to independently weave, cut, sew, glue, weld and assemble products and integrate systems. If workloads require, we use the services of sub-contractors, mainly for obtaining raw materials, sewing metal work, cloth coating work, dyeing and finishing, and digital printing.

In connection with our production activities, we have established five principal departments: research and development, technical design, mechanics processing, product assembly and quality control.

## Transportation and Distribution

Our manufacturing plants are located in Israel and in the State of California. Israel’s marine transportation routes are well-developed and, accordingly, we have no logistical difficulty in distributing our products and in most cases our products reach their destination within two to three weeks, depending on the arrangements with the customer. Products for export are shipped mainly as Free on Board (F.O.B.) shipping point, as per the Incoterm standard. Consignments are sent by sea or air, depending on the nature of the order and the urgency of supply. To date, our U.S. facility only serves our U.S. based customers and we have had no difficulties in distributing our products within the US.

## Competition

The ballistic-resistant and body armor industry is highly competitive and fragmented throughout the world. In the United States the great majority of manufacturers are privately held companies, ranging from small limited product companies to large multinational corporations. We estimate that there are approximately twenty U.S.-based companies that compete in the body armor industry. The principal elements of competition are performance, price, innovative design, and quality. Name recognition and reputation are highly important in each country where products are sold. We believe that our products are highly competitive and well regarded, evidenced by our ability to sell to customers such as the United States Military, Israeli Defense Forces, NATO and many foreign governments. We also believe that we distinguish ourselves from our competition by (i) our ability to manufacture the various components of our products, (ii) the fact that we generally do not rely on other manufacturers and (iii) the diversification and range of our product lines.

Barriers to entry for new companies entering the body armor industry are low, consequently creating fierce competition. We believe that establishing a good reputation significantly enhances the competitive position of the industry's long-standing manufacturers. However, name and product reputation takes many years to develop. In the U.S. civilian market, (law enforcement, border patrol forces, prison forces and special forces) our products are less known than that of our competitors. We intend to expand our U.S. presence and to achieve greater market penetration.

We believe that our proprietary products such as dry storage systems, ballistic wall coverings and liquid logistic products encounter significantly less competition than the traditional body armor product line.

A rising demand for armoring large vehicles and boats has increased the demand for large lightweight armor plates. Those lightweight plates are molded under extreme high pressure. With our unique 5,000 metric ton press, we have the ability to mold the large size plates. We encounter less competition with respect to large size plates than with our standard sized molded armor plates product line.

In the civilian market, we are aware of approximately twenty major companies manufacturing similar products worldwide. A number of major manufacturers with greater resources than ours compete in the same market. In 2010, we continued to increase our marketing efforts through distributors who concentrate on the civilian market.

Our major competitor in sales to the Israeli Ministry of Defense is Rabintex, a larger, more established Israeli corporation. We also face competition from other Israeli companies and from a number of importers. Internationally, our competitors in the defense market include companies such as Point Blank, Safari Land of Ontario, California, BAE Systems Mobility & Protection Systems and A.B.A. in the United States, L.B.A. in England, Indigo in Spain, Sistema Compositi in Italy, Hellenic Arms Industries in Greece and Barman in Sweden. We believe that each of these competitors offers a more limited product line than we do.

#### Raw Materials

We use variety of ballistic protection materials, including aramid woven and non-woven fabrics and non-woven polyethylene sheets and ceramic material for personal protection products and steel for car armoring. Aramid fabrics that we both weave ourselves and acquire from other manufacturers, and non-woven uni-directional polyethylene sheets are used together, as the basic components of our ballistic protection products. As a result, our protective equipment provides excellent protection with relatively low weight, and we believe that it is highly competitive. We obtain our supplies on the basis of an open letter of credit, specialized documentary credit, and in the case of suppliers with whom we have dealt with for years, on open account. We have long-term relationships with some of our suppliers, and we believe that these suppliers are stable and do not anticipate any disruption in the steady supply of materials that we require. A disruption in the supply of materials could have an adverse impact on our operating results.

Our products are made from raw materials produced in Israel and abroad including, specialized composite materials such as Kevlar® produced by DuPont Company, Twaron® produced by Twaron Teijn Ltd., Dyneema® produced by D.S.M. Ltd. and Spectra® and Gold Flex® produced by Honeywell. We also use other specialized materials produced by different manufacturers such as specialized glass mixed with polycarbonate and various resins.

DuPont's Kevlar® brand fiber was initially introduced in 1965 and was the first material identified for use in the modern generation of concealable body armor. Kevlar® is a man-made organic fiber, with a combination of properties allowing high strength, low weight and high chemical and flame resistance. Through the years DuPont has continued to develop and design new generations of this high-performance fabric.

Spectra® fiber, manufactured by Honeywell, is an ultra-high-strength polyethylene fiber. It has one of the highest strength-to-weight ratios of any man-made fiber. Honeywell uses its Spectra® fiber to make its patented Spectra Shield®. Additional fibers that we use in the manufacture of body armor are Goldflex®, Twaron®, and Dyneema®. These state-of-the-art fibers are continuously being improved and advanced, which increases the possibility of superior new products entering the market.



As a result of the continuing unrest in Iraq, and in other geographical regions there has been a worldwide increase in demand since 2005 for the raw materials used in our products. Suppliers have increased their production and the market shortages that existed in recent years no longer exist. We anticipate that this trend will continue in 2011.

### Seasonality

Sales of our military and security clothing products and industrial products are not seasonal in nature. We generally experience a slight increase in sales of our camping equipment during the second quarter and in sales of our protective clothing during the fourth quarter.

### Marketing and Sales

Our sales and marketing strategies revolve principally around developing a reputable brand identity and ongoing customer relationships in addition to continuously improving the quality of our products and offering innovative new products. Specifically, our marketing strategy is designed to penetrate various markets by complying with stringent quality standards instituted in targeted countries.

Below are some of the steps we take in penetrating new markets with our next generation of products:

- Locate domestic entities to market our products;
- Actively participate in tenders and bids for contracts in military, police and civilian markets worldwide. We are currently negotiating for contract bids with the governments and governmental agencies in Sweden, Turkey, Mexico, Brazil, Uruguay, Chile, Trinidad, Guatemala, India, Peru, Brazil, Nigeria, Zambia, Uganda, France, Germany and the U.S.;
- Advertise in professional publications;
- Appear in international databases, such as Kompass, various “yellow page” directories and other directories; and
- Distribute brochures describing procedures and product offerings.

Our local marketing staff is divided into two groups. One group specializes in locating and submitting government bids and the other specializes in marketing to the civilian sector. Separate offices in Sderot and Nazareth Elite handle the local civilian market. Each of these offices deals with a different geographical region and a different line of products.

Our export marketing is handled by a free-lance marketing consultant and a group of in-house employees. Although our marketing consultant works almost exclusively for us, we do not have a formal written relationship with him. This marketing team carries out market surveys and searches for new markets for our products, as well as for new engagements with the international business community. The consultant is paid a fixed monthly fee and commissions that are determined in advance according to the scope and nature of the transaction.

### Customers

We have a worldwide customer base, including in the U.S., Israel, the Mediterranean, Europe, South America, Africa and Asia. In 2010 and 2009, we sold approximately 46.6% and 38.8%, respectively, of our products to our international customers with the balance sold in Israel. The primary end users of our products can be divided into three main groups: (i) military defense and security forces, (ii) civilian defense customers and (iii) civilian customers.

**Military Defense and Security Forces.** We provide this group with personal military and protective equipment such as body armor, bomb disposal suits, bullet proof vests and jackets, ballistic helmets and plates, battle pouch and combat harness units, backpacks, dry storage systems, liquid logistics systems, clothing, tents, vehicle covers and sleeping

bags. These items must meet certain “human engineering” requirements to provide comfort as well as maximum protection, to prevent penetration by bullets and knives, and to protect from fire, collisions and other hazards.

Civilian Defense Customers. This group includes members of civilian security forces such as law enforcement, prison forces, private security firms, airport security, personal bodyguards, and event security guards. The requirements of these customers for protective equipment are similar to those of military defense and security forces. However, since they primarily work in a civilian environment the products must meet certain aesthetic standards and the protective features need to be as unobtrusive as possible.

Civilian Customers. This group includes campers, hikers, pet owners and horse owners. We provide this group with equipment such as sleeping bags, tents, backpacks, and clothing adapted for specific needs such as mountain climbing, hiking and camping in all types of climates, horseback riding equipment and animal accessories. This customer group also includes those civilians in need of covers for cars, trucks, buses and other large vehicles.

Local Military Market. In 2010, sales to the Israeli Ministry of Defense decreased to \$4,801,560 from \$7,121,326 in 2009, accounting for 29% and 43.2% of our sales, respectively.

As of March 19, 2011, we had a backlog of firm orders from the Israeli Ministry of Defense of approximately \$1 million, including orders of approximately \$0.4 million that we received subsequent to December 31, 2010.

Export Military Market. Our customers in this market are military and law enforcement organizations, mostly in South America, North America and Europe. Their budgets fluctuate, and as a result we cannot identify definite trends in these markets. In 2010 and in 2009, we had sales of \$3,516,609 and \$1,946,546 in South America, sales of \$10,645 and \$258,047 in North America, sales of \$634,589 and \$1,203,367 in Europe and Asia, and \$1,808,361 and \$1,848,346 in Africa, respectively.

Since 2003, we have increased our export efforts and are continuing our efforts to strengthen our position in our existing export markets in the U.S., South America, Asia and Europe, and to extend our presence to new export markets in South America, Africa, Europe and Australia. We believe that these markets are growing and that any future success in such markets is mainly dependant on our ability to be competitive in our pricing and the quality of our products.

The following table presents details of our export military sales during the two years ended December 31, 2010:

	Year Ended December 31,	
	2010	2009
Sales to South America	\$ 3,516,609	\$ 1,946,546
Sales to North America	10,645	258,047
Sales to Europe and Asia	634,589	1,203,367
Sales to Africa	1,808,361	1,848,346
Total Export Military Sales	\$ 5,970,204	\$ 5,256,306

Local Civilian Market. Our product range offered to the civilian market is diversified. In 2010, our local civilian market business increased compared to 2009.

#### Backlog

We had approximately \$4.3 million of unfilled customer orders at December 31, 2010, as compared to approximately \$5.3 million of unfilled customer orders at December 31, 2009. Of our \$4.3 million of unfilled customer orders at December 31, 2010, approximately \$0.1 million was attributable to orders from military customers in South America, approximately \$0.3 million was attributable to orders from military customers in Europe and Asia, approximately \$1.9 million was attributable to orders from military customers in Africa, approximately \$0.6 million was attributable to the local civilian market and approximately \$1.4 million was attributable to the Israeli Ministry of Defense.



## Regulation

The U.S. National Institute of Justice, or NIJ, established standards for “Ballistic Resistance of Personal Body Armor” that are accepted worldwide. The NIJ issues performance standards that clearly specify a minimum performance level for each attribute that is critical for the equipment’s intended use. This coveted compliance standard has gained global acceptance as a benchmark for evaluation of the effectiveness of a given body armor model. The NIJ body armor-testing program relies on voluntary participation by manufacturers. However, many police departments require that armor be tested and found to be in compliance with NIJ standards before they purchase the armor. Our ballistic material combinations have been tested by NIJ certified ballistic laboratories and were found to comply with NIJ Standard 0101.04 and NIJ 2005 Interim Requirements Bullet-Resistant Body Armor and are being tested to be certified as complying with Standard NIJ 0101.06. As a result, our ballistic combinations have been approved to carry NIJ labels.

Our manufacturing practices have obtained ISO 9001 certification. This international certification harmonizes and establishes standards for quality manufacturing throughout the world. Over the years, ISO standards have expanded beyond the quality system and now confirm conformity in environmental issues, safety and occupational health. This voluntary certification process is designed to provide consistency in manufacturing processes and quality control.

Other quality control standards pertaining to our manufacturing facilities consist of the following:

- MIL-STD-105D, MIL-I-45208A (for the United States Armed Forces); and
- AQAP (for the German Armed Forces and NATO).

In order to participate in bids of the Israeli Ministry of Defense and other governments, companies must follow various rules and procedures. The bidder must be registered as a recognized supplier. The bidder must have government certification and is authorized to participate in bids only to the limit of its approved security classification. Under Israeli bid regulations, goods produced in Israel are given priority over foreign bidders. The bidder must keep to contractual schedules and milestones and the goods must pass final quality control tests before delivery. There are no special taxes on bids apart from the Israeli value added tax.

Since our business is highly regulated, the laws, rules and regulations applicable to our business are subject to regular modification and change. Future laws, rules or regulations may be adopted, making compliance much more difficult or expensive, and may otherwise adversely affect our business or prospective business.

## Research and Development

We continue to improve our existing products and develop new products for the military and civilian markets, including mine protective shoes, stab-resistant solutions, improved armored car blast protection materials, and modified ballistic wall coverings. We are also developing a new generation of complex products for protective vests used by security forces and armies all over the world.

In the years ended December 31, 2010 and 2009, we spent approximately \$44,924 and \$19,302, respectively, on research and development, which expenses were expensed. While, we have not as yet finalized our research and development budget for 2011, we expect that our R&D expenses will increase during 2011.

## Environmental Laws

We are unaware of any environmental laws that are applicable to us that will require us to spend any material amounts to achieve compliance.

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## Employees

As of December 31, 2010, we had 201 full-time employees, of whom 155 are in Israel and 46 are in the United States. We believe our relationship with our employees is good. Our employees are not represented by a collective bargaining organization and we have not experienced any work stoppages.

## Item 1A. Risk Factors

Investing in our stock involves a high degree of risk and uncertainty. You should carefully consider the risks and uncertainties described below before investing in our stock. Our business, prospects, financial condition and results of operations could be adversely affected due to any of the following risks. In that case, the value of our stock could decline, and you could lose all or part of your investment.

### Risks Related to Our Business and Our Industry

The products we sell are used in applications that are inherently risky and could give rise to product liability and other claims.

The products that we manufacture are typically used in applications and situations that involve high levels of risk of personal injury. Failure to use our products for their intended purposes, failure to use them properly, their malfunction, or, in some limited circumstances, even correct use of our products, could result in serious bodily injury or death. Our main products include personal military and civilian protective equipment and supplies such as body armor, bomb disposal suits, ballistic wall coverings, bulletproof vests, and associated heavy fabric products, such as battle pouches and combat harness units, dry storage systems, liquid logistic products, tents and other camping and travel gear.

The manufacture and sale of certain of our products may be the subject of product liability claims arising from the design, manufacture or use of such goods. If we are found to be liable in such claims, we may be required to pay substantial damages and our insurance costs may increase significantly as a result. Also, a significant or extended lawsuit, such as a class action, could also divert significant amounts of management's time and attention. Our insurance coverage may not be sufficient to cover the payment of any potential claim. In addition, this or any other insurance coverage may not be available or, if available, we may not be able to obtain it at a reasonable cost. Any material uninsured loss could have a material adverse effect on our business, financial condition and results of operations. In addition, the inability to obtain product liability coverage would prohibit us from bidding for orders from certain governmental customers since, at present, many bids from governmental entities require such coverage, and any such inability would have a material adverse effect on our business, financial condition and results of operations.

We are subject to extensive government regulation and our failure or inability to comply with these regulations could materially restrict our operations and subject us to substantial penalties.

We are subject to extensive regulation by governmental authorities and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on our operations. Furthermore, we have material contracts with governmental entities and are subject to rules, regulations and approvals applicable to government contractors. For the years ended December 31, 2010 and 2009, the Israeli Ministry of Defense accounted for \$4,801,560 and \$7,121,326 of our sales, respectively. We are also subject to routine audits to assure our compliance with these requirements. In addition, a number of our employees are required to obtain specified levels of security classification. Our business may suffer if we or our employees are unable to obtain the security classifications that are needed to perform services contracted for the Israeli Ministry of Defense, one of our major customers. Our failure to comply with these contract terms, rules or regulations could expose us to substantial penalties, including the



loss of these contracts and disqualification as a government contractor of certain governments.

Reduction in military budgets worldwide may cause a reduction in our revenues, which would adversely affect our business, operating results and financial condition.

A significant portion of our revenues is derived from the sale of products to military markets. These revenues, on a consolidated basis, totaled \$11,114,557 or 67%, of our revenues in the year ended December 31, 2010 and \$12,724,098, or 77.1%, of our revenues in the year ended December 31, 2009. Our sales to the Israeli Ministry of Defense declined to \$4,801,560 in the year ended December 31, 2010, compared to \$7,121,326 in the year ended December 31, 2009. The military budgets of the State of Israel and other countries may be reduced in the future. Declines in government military budgets may result in reduced demand for our products, resulting in a reduction of our revenues and would adversely affect our business, results of operations and financial condition.

We have significant international operations and are therefore subject to additional financial and regulatory risks.

While our principal executive offices are located in Israel, 47% of our sales in the year ended December 31, 2010, and 38.8% of our sales in the year ended December 31, 2009, were generated from exports. We are seeking to increase the level of our international business activity. Our overseas operations are subject to various risks, including; foreign import controls (which may be arbitrarily imposed and enforced and which could preclude sales to certain customers).

One component of our strategy is to expand our operations into selected international markets. Military procurement, for example, has traditionally been international in scope. Countries in which we actively market include U.S., Sweden, Chile, Mexico, Guatemala, India, Peru, Brazil, Nigeria, Trinidad, Zambia, Uganda, France and Germany. However, we may be unable to execute our business model in these markets or new markets. Further, foreign providers of competing products and services may have a substantial advantage over us in attracting consumers and businesses in their country due to earlier established businesses in that country, greater knowledge with respect to the cultural differences of consumers and businesses residing in that country and/or their focus on a single market.

In pursuing our international expansion strategy, we face several additional risks, including:

- Reduced protection of intellectual property rights in some countries;
  - Licenses, tariffs and other trade barriers;
  - Longer sales and payment cycles;
  - Greater difficulties in collecting accounts receivable;
  - Potential adverse tax consequences;
  - Laws and business practices favoring local competition;
- Costs and difficulties of doing business and customizing products for foreign countries;
- Compliance with a wide variety of complex foreign laws and treaties;
  - Political and economic instability; and
- Variance and unexpected changes in local laws and regulations.

We may operate in areas where local government policies regarding foreign entities and the local tax and legal regimes are often uncertain, poorly administered and in a state of flux. We cannot be certain that we are in compliance with, or will be protected by, all relevant local laws at any given point in time. A subsequent determination that we failed to comply with relevant local laws and taxation regimes could have a material adverse effect on our business, financial condition and results of operations. One or more of these factors could adversely affect our future international operations and, consequently, could have a material adverse effect on our business, financial condition and results of operation.

We depend on sales to key customers and the loss of one or more of our key customers would result in a loss of a significant amount of our revenues.

A significant portion of our revenues is derived from a small number of customers. The Israeli Ministry of Defense accounted for 29% of our revenues in the year ended December 31, 2010. In the fiscal year ended December 31, 2009, the Israeli Ministry of Defense accounted for 43.2% of our revenues. We anticipate that a significant portion of our future revenues will continue to be derived from sales to a small number of customers. If our principal customers do not continue to purchase products from us at current levels or if such customers are not retained and we are not able to derive sufficient revenues from sales to new customers to compensate for their loss, our revenues would be reduced and adversely affect our business, financial condition and results of operations.

Our business may be negatively affected by the current economic climate.

The current economic climate and the uncertainty in global economic conditions resulting from the recent disruption in credit markets pose a risk to the overall economy that could impact customer demand for our products, as well as our ability to manage normal commercial relationships with our customers, suppliers and creditors. If the current situation deteriorates significantly, our business could be negatively impacted, including such areas as reduced demand for our products from a slow-down in the general economy, reduced governmental and military budgets, or supplier or customer disruptions resulting from tighter credit markets.

Currency exchange rate fluctuations in the world markets in which we conduct business could have a material adverse effect on our business, results of operations and financial condition.

We may be adversely affected by fluctuations in currency exchange rates. A significant portion of our expenses are incurred in NIS and Euros. We do not currently engage in any currency hedging transactions intended to reduce the effect of fluctuations in foreign currency exchange rates on our results of operations. If we were to determine that it was in our best interests to enter into any hedging transactions in the future, there can be no assurance that we will be able to do so or that such transactions, if entered into, will materially reduce the effect of fluctuations in foreign currency exchange rates on our results of operations. In addition, if for any reason exchange or price controls or other restrictions on the conversion of foreign currencies into NIS were imposed, our business could be adversely affected. There can be no assurance such fluctuations in the future will not have a material adverse effect on revenues from international sales, and consequently, on our business, operating results and financial condition.

Sales of our products are subject to governmental procurement procedures and practices; termination, reduction or modification of contracts with our customers, and especially with the government of Israel, or a substantial decrease in our customers' budgets may adversely affect our business, operating results and financial condition.

Our military products are sold primarily to government agencies and authorities, many of which have complex and time-consuming procurement procedures. A long period of time often elapses from the time we begin marketing a product until we actually sell that product to a particular customer. In addition, our sales to government agencies, authorities and companies are directly affected by those customers' budgetary constraints and the priority given in their budgets to the procurement of our products. The termination, reduction or modification of our contracts or subcontracts with the Government of Israel in the event of change in requirements, policies or budgetary constraints would have an adverse effect on our business, operating results and financial condition.

Our markets are highly competitive and if we are unable to compete effectively, we will be adversely affected.

The markets in which we operate are highly competitive with a large number of competitors ranging from small businesses to multinational corporations. Competitors who are larger, better financed and better known than us may

compete more effectively than we can. In order to stay competitive in our industry, we must keep pace with changing technologies and client preferences. If we are unable to differentiate our products from those of our competitors, our revenues may decline. In addition, our competitors have established relationships among themselves or with third parties to increase their ability to address client needs. As a result, new competitors or alliances among competitors may emerge and compete more effectively than we can.

There are limited sources for some of our raw materials and any shortage may significantly curtail our manufacturing operations.

The raw materials that we use in manufacturing ballistic resistant garments, armor plates and car armoring include: Kevlar® fiber produced by Dupont Ltd., Twaron® fiber produced by Twaron Teijn Ltd., Dyneema UD® fabric produced by DSM Ltd. and Spectra UDC® fabric and Gold Flex® fabric produced by Honeywell and Ultra High Molecular Weight polyprene materials produced by Honeywell and DSM Ltd. We purchase these materials directly from DSM and Honeywell or in the form of woven cloth from independent weaving companies. In the event DuPont or Twaron Teijn ceases to produce or sell Kevlar® or Twaron® to us for any reason, we would utilize the other ballistic resistant materials as a substitute. However, none of them is expected to become a complete substitute for Kevlar® or Twaron® in the near future. If our supply of any of these materials were materially reduced or cut off, or if there were a material increase in the prices of these materials, our manufacturing operations could be adversely affected and our costs increased, and our business, financial condition and results of operations would be materially adversely affected.

We may be unable to complete or integrate acquisitions effectively, if at all, and as a result may incur unanticipated costs or liabilities or operational difficulties.

We intend to grow through the acquisition of businesses and assets that will complement our current businesses. Furthermore, we may have to divert our management's attention and our financial and other resources from other areas of our business to potential new businesses. We cannot be certain that we will be able to identify other attractive acquisition targets, obtain financing for acquisitions on satisfactory terms, or successfully acquire identified targets. Our inability to implement our acquisition strategy successfully may hinder the expansion of our business. Because we intend to acquire new businesses and assets to develop and offer new products, failure to implement our acquisition strategy may also adversely affect our ability to offer new products in line with industry trends.

We may not be successful in integrating the operations of businesses into our existing operations. Integration may result in unanticipated liabilities or unforeseen operational difficulties, which may be material, or require a disproportionate amount of management's attention. Acquisitions may result in us incurring additional indebtedness or issuing preferred stock or additional common stock. Competition for acquisition opportunities in the industry may rise, thereby increasing our cost of making acquisitions or causing us to refrain from making further acquisitions.

Our resources may be insufficient to manage the demands imposed by any future growth.

Expansion of our operations may place significant demands on our management, administrative, operating and financial resources. Growth of our customer base, the types of products offered and the geographic markets served can place a significant strain on our resources. In addition, we believe that we may encounter difficulties in identifying and hiring personnel who are qualified both in the provision and marketing of our security products, based on our current compensation levels. Our future performance and profitability will depend in large part on our ability to attract and retain additional management and other key personnel, our ability to implement successful enhancements to our management, accounting and information technology systems, and our ability to adapt those systems, as necessary, to respond to growth in our business.

Technological advances, the introduction of new products, and new design and manufacturing techniques could adversely affect our operations unless we are able to adapt to the resulting change in conditions.

Our future success and competitive position depend to a significant extent upon our proprietary technology. We must make significant investments to continue to develop and refine our technologies. We may be required to expend substantial funds for and commit significant resources to the conduct of continuing research and development

activities, the engagement of additional engineering and other technical personnel, the purchase of advanced design, production and test equipment, and the enhancement of design and manufacturing processes and techniques. Our future operating results will depend to a significant extent on our ability to continue to provide design and manufacturing services for new products that compare favorably on the basis of time to market, cost and performance with the design and manufacturing capabilities. The success of new design and manufacturing services depends on various factors, including utilization of advances in technology, innovative development of new solutions for customer products, efficient and cost-effective services, timely completion and delivery of new product solutions and market acceptance of customers' end products. Because of the complexity of some of our products, we may experience delays from time to time in completing the design and manufacture of new product solutions. In addition, there can be no assurance that any new product solutions will receive or maintain customer or market acceptance. If we were unable to design and manufacture solutions for new products of our customers on a timely and cost-effective basis, such inability could have a material adverse effect on our business, financial condition and results of operations.

We may need to raise additional capital in the future, which may not be available to us.

We may need to raise additional funds for a number of uses, including:

- Maintaining and expanding research and development;
- Implementing marketing and sales activities for our products;
- Hiring additional qualified personnel; and
- Supporting an increased level of operations.

We may not be able to obtain additional funds on acceptable terms or at all. If we cannot raise needed funds on acceptable terms, we may be required to delay, scale back or eliminate some aspects of our operations and we may not be able to:

- Develop new products;
- Enhance our existing products;
- Remain current with evolving industry standards;
- Take advantage of future opportunities; or
- Respond to competitive pressures or unanticipated requirements.

If adequate funds are not available to us, our business, results of operations and financial condition will be materially and adversely affected. Any equity or debt financings, if available at all, may cause dilution to our then-existing shareholders and may increase our financing expenses. If additional funds are raised through the issuance of equity securities, the net tangible book value per share of our common stock would decrease and the percentage ownership of then current shareholders would be diluted.

We have in the past and may in the future experience deficiencies, including material weaknesses, in our internal control over financial reporting. Our business and our share price may be adversely affected if we do not remediate these material weaknesses or if we have other weaknesses in our internal controls.

With respect to our financial statements for years ended December 31, 2010 and 2007, and the first three quarterly periods in the year ended December 31, 2008, we identified control deficiencies, including several material weaknesses, in our internal control over financial reporting. The material weaknesses related to our year end financial statement closing process resulting from insufficient knowledge of our financial staff regarding U.S. GAAP. We have taken steps to remediate our material weaknesses as follows:

we have recruited a new chief financial officer and continue to recruit and hire additional accounting staff with technical expertise to ensure the proper application of accounting principles generally accepted in the United States; we are implementing revised policies and procedures and enhancing our review of complex transactions to ensure consistent application of U.S. GAAP and enhanced internal control over financial reporting; and we are increasing the level of preparation and review of our financial statements, and in connection therewith, we are implementing additional control procedures as part of our quarter and year-end close processes as well as adding resources in connection with our review of key financial estimates.



Our business and our share price may be adversely affected if we do not remediate these material weaknesses or if we have other weaknesses in our internal controls.

We may fail to maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act of 2002, which could have an adverse effect on our financial results and the market price of our ordinary shares.

The Sarbanes-Oxley Act of 2002 imposes certain duties on us and our executives and directors. Our efforts to comply with the requirements of Section 404 have resulted in increased general and administrative expense and a diversion of management time and attention, and we expect these efforts to require the continued commitment of resources. Section 404 of the Sarbanes-Oxley Act requires us to provide management's annual review and evaluation of our internal control over financial reporting in connection with the filing of our Annual Report on Form 10-K for each fiscal year. The rules governing the standards that must be met for management to assess our internal control over financial reporting are complex and require significant documentation, testing and possible remediation to meet the detailed standards under the rules. During the course of its testing, our management may identify material weaknesses or significant deficiencies, which may not be remedied prior to the deadline imposed by the Sarbanes-Oxley Act. If we fail to maintain the adequacy of our internal controls, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal controls over financial reporting. Failure to maintain effective internal controls over financial reporting could result in investigation or sanctions by regulatory authorities, and could have a material adverse effect on our operating results, investor confidence in our reported financial information, and the market price of our ordinary shares.

### Risk Factors Related to Our Common Stock

If we fail to remain current on our reporting requirements, we could be removed from the OTC Bulletin Board which would limit the ability of stockholders to sell their securities in the secondary market.

Companies trading on the OTC Bulletin Board, such as our company, must be reporting companies under Section 12 of the Securities Exchange Act of 1934, as amended, and must be current in their reports under Section 13, in order to maintain price quotation privileges on the OTC Bulletin Board. If we fail to remain current in our reporting requirements, we could be removed from the OTC Bulletin Board. As a result, the market liquidity for our securities could be severely adversely affected by limiting the ability of stockholders to sell their securities in the secondary market.

Our shares of common stock are thinly traded, so you may be unable to sell at or near “ask” prices or at all if you need to sell your shares to raise money or otherwise desire to liquidate your shares.

Our shares of common stock are “thinly-traded” on the OTC Bulletin Board, meaning that the number of persons interested in purchasing our common stock at or near ask prices at any given time may be relatively small or non-existent. This situation is attributable to a number of factors, including the fact that we are a small company which is relatively unknown to stock analysts, stock brokers, institutional investors and others in the investment community that generate or influence sales volume, and that even if we came to the attention of such persons, they tend to be risk-averse and would be reluctant to follow an unproven development stage company such as ours or purchase or recommend the purchase of our shares until such time as we became more seasoned and viable. As a consequence, there may be periods of several days or more when trading activity in our shares is minimal or non-existent. We cannot give you any assurance that a broader or more active public trading market for our common stock will develop or be sustained, or that current trading levels will be sustained. Due to these conditions, we can give you no assurance that you will be able to sell your shares at or near ask prices or at all if you need money or otherwise desire to liquidate your holdings.

We are subject to the penny stock rules and these rules may adversely effect trading in our common stock.

Until our shares qualify for inclusion in the NASDAQ Stock Market system, the public trading, if any, of our common stock will be on the OTC Bulletin Board. As a result, an investor may find it more difficult to dispose of, or to obtain accurate quotations as to the price of, the common stock offered. Our common stock is subject to provisions of Section 15(g) and Rule 15g-9 of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), commonly referred to as the “penny stock rule.” Section 15(g) sets forth certain requirements for transactions in penny stocks, and Rule 15g-9(d) incorporates the definition of “penny stock” that is found in Rule 3a51-1 of the Exchange Act. The SEC generally defines “penny stock” to be any equity security that has a market price less than \$5.00 per share, subject to certain exceptions. If our common stock is deemed to be a penny stock, trading in the shares will be subject to additional sales practice requirements on broker-dealers who sell penny stock to persons other than established customers and accredited investors. The definition of “Accredited Investors” includes among others, persons with assets in excess of \$1,000,000 or annual income exceeding \$200,000 or \$300,000 together with their spouse. For transactions covered by these rules, broker-dealers must make a special suitability determination for the purchase of such security and must have the purchaser’s written consent to the transaction prior to the purchase. Additionally, for any transaction involving a penny stock, unless exempt, the rules require the delivery, prior to the first transaction, of a risk disclosure document, prepared by the SEC, relating to the penny stock market. A broker-dealer also must disclose the commissions payable to both the broker-dealer and the registered representative, and current quotations for the securities. Finally, monthly statements must be sent disclosing recent price information for the penny stocks held in an account and information on the limited market in penny stocks. Consequently, these rules may restrict the ability of a broker-dealer to trade and/or maintain a market in our common stock and may affect the ability of our

shareholders to sell their shares.

We do not intend to pay dividends for the foreseeable future

We have not declared or distributed dividends in the past and do not currently have a dividend distribution policy. The declaration of dividends is subject to the discretion of our Board of Directors and applicable law and will depend on various factors, including our operating results, financial condition, current and anticipated cash needs, contractual restrictions and any other factors deemed relevant by our board of directors. You should not rely on an investment in our company if you require dividend income from your investment in our company. The success of your investment will likely depend entirely upon any future appreciation of the market price of our common stock, which is uncertain and unpredictable. There is no guarantee that our common stock will appreciate in value or even maintain the price at which you purchased your common stock

#### Risks Relating to Our Location in Israel

Political, economic and military instability in Israel may disrupt our operations and negatively affect our business condition, harm our results of operations and adversely affect our share price.

Our subsidiaries Export Erez, Achidatex, Mayotex, Mayosar and Optics are incorporated and based in, and currently derive substantially most of their revenues from markets within the State of Israel. We also maintain our executive offices in Israel. As a result, political, economic and security conditions in Israel directly influence us. Since the establishment of the State of Israel in 1948, Israel and its Arab neighbors have engaged in a number of armed conflicts. A state of hostility, varying in degree and intensity, has led to security and economic problems for Israel. Major hostilities between Israel and its neighbors may hinder Israel's international trade and lead to economic downturn. This, in turn, could have a material adverse effect on our operations and business.

Since the establishment of the State of Israel in 1948, Israel and its Arab neighbors have engaged in a number of armed conflicts. A state of hostility, varying from time to time in intensity and degree, has led to security and economic problems for Israel. Major hostilities between Israel and its neighbors may hinder Israel's international trade and lead to economic downturn. This, in turn, could have a material adverse effect on our operations and business. There has been an increase in unrest and terrorist activity in Israel, which began in September 2000 and which continued with varying levels of severity. In recent years, there has been an escalation in violence among Israel, Hamas, Hezbollah, the Palestinian Authority and other groups. Recently, countries in the region have experienced political instability, the effects of which are currently difficult to assess. Ongoing or future violence between Israel and the Palestinians as well as tension between Israel and neighboring Syria, the Islamic Republic of Iran and Lebanon or political instability in the region may have a material adverse effect on our business, financial conditions and results of operations.

Furthermore, there are a number of countries, primarily in the Middle East, as well as Malaysia and Indonesia, that restrict business with Israel or Israeli companies, and we are precluded from marketing our products to these countries. Restrictive laws or policies directed towards Israel or Israeli businesses may have an adverse impact on our operations, our financial results or the expansion of our business.

Many of our officers and employees in Israel are obligated to perform annual reserve duty in the Israeli Defense Forces and may be called for active duty under emergency circumstances at any time. If a military conflict or war arises, these individuals could be required to serve in the military for extended periods of time. Our operations could be disrupted by the absence for a significant period of one or more of our executive officers or key employees or a significant number of other employees due to military service. Any disruption in our operations could adversely affect our business.



Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

Our executive offices are located at 12 Hamefalsim Street, Petach Tikva, Israel. Our manufacturing, production and distribution facilities are located at several locations in Israel and the United States. We lease premises at such locations under non-cancelable operating leases with expiration dates through December 2015. Three of the operating leases are with affiliated parties. The locations are:

The production activities of Achidatex and Export Erez are located in a 6,000 square meter building in the Nazareth Industrial Area, owned by an Israeli company in which Mayo-Ben has a 57.5% interest. The annual rental expense for this facility was \$289,308 in 2010. The lease will expire in December 31, 2012; however, under the investment agreement entered into between the Mayotex and Mayo-Ben, Mayo-Ben undertook to extend the lease for a period of 36 months on the same terms and conditions as the current lease and provided Achidatex and Export Erez with two (2) months of free rent in 2011.

Achidatex sub-leases 678 square meters of industrial space in the Nazareth Industrial Area, which is used for its dyeing activities. The annual rental expense for this facility was \$57,862 in 2010.

Export Erez leases approximately 300 square meters of office space for our headquarter offices in Petach-Tikva at an annual rental expense of \$32,148 in 2010. The lease will expire on April 30, 2012.

Mayotex leases 1,000 square meters of industrial space and additional 1,280 square meters of outdoor space in the Industrial Area of Ashkelon from Mayo-Ben for its car armor installations. Pursuant to the investment agreement between Mayotex and Mayo-Ben, Mayotex entered into a new lease agreement for this property under which the parties agreed to a retroactive reduction in rent to \$57,059 in 2010 instead of \$67,506. In addition, under the new lease agreement, the term of the lease was extended until December 2015. Under the new lease agreement, Mayotex will pay annual rental fees of \$56,255 for the first 2.5 years under the agreement, and annual rental fees of \$64,291 for the remaining 2.5 years under the agreement.

Export Erez leases approximately 1,219 square meters of space in the Industrial Area of Sderot, primarily for its cut and sew operations. The annual rental expense for this space was \$72,582 in 2010. In December 2010, Export Erez entered into a new lease agreement for these premises under which the: (i) lease period was extended until December 2015; (ii) annual rental fees were reduced to \$58,778 for the first 2.5 years (instead of \$82,289 as provided under the previous agreement); and (iii) annual rental fees of \$66,615 for the remaining 2.5-year period will be \$66,615.

Mayotex leases approximately 1,734 square meters of industrial space in the Alon Tavor Industrial Zone near Afula, Israel for its dry storage business. In 2010, Mayotex exercised its right of early termination effective June 30, 2011.

Owen Mills leased approximately 9,000 square feet of space in Van Nuys, California at an annual rental expense of \$82,767 in 2010. In December 2010, Owen Mills entered into a new lease agreement for a period of five years for approximately 17,000 square feet of space in another facility in Van Nuys, California, at an annual rental expense of \$156,000. The annual rental fee will increase by 3% on each anniversary of the agreement.

In January 2011, Export Erez entered into a lease agreement for 2,025 square meters of industrial space at the Industrial Area of Sderot to be used for our company's dry storage business which is being transferred from the facility in Alon Tavor. The lease period is until February 28, 2014, with annual rental fees of \$91,133 (with two

(2) months of free rent in the first year). Export Erez has an option to renew the lease for an additional three year term at \$94,936 per year.

In February 2011, Mayotex entered into a lease agreement in respect of 2,025 square meters of industrial space at the Industrial Area of Sderot for use by the car armoring business of Mayotex and the fiberglass business of Vacutec. Once the Philcar acquisition is completed, we intend to move its operation to this facility. The lease period is until April 30, 2014 with an option to renew for an additional period of two (2) years. Mayotex will pay annual rent of \$84,623 during the lease period and annual rent of \$88,572 during the option period.

We believe that our facilities are adequate for our purposes and that all of the above mentioned properties are adequately covered by insurance.

Item 3.

Legal Proceedings.

On February 11, 2009, a lawsuit was filed in the Jerusalem District Court, or the Court, against our subsidiary, Achidatex, its chief executive officer, Mr. Avraham Haztor, and our subsidiary Export Erez USA Inc. Export Erez was subsequently added as a defendant in the action. The suit alleges that Achidatex materially breached its February 22, 2000 agreement with the plaintiff, relating to the development of inflatable mine-field crossing enabling sandals, by failing to register patents for the technology underlying the sandals, worldwide and only registered patents in the United States. The plaintiff further claims that the defendants, jointly and severally, committed a breach of trust. The plaintiff is seeking damages in the amount of NIS 10 million (approximately \$2.8 million). We filed a statement of defense rejecting the plaintiff's claims and asserted a claim against the plaintiff and others for a declaratory judgment that the plaintiff breached his contractual undertakings towards Achidatex. The petition to consolidate the counter-claim with the plaintiff's claim was ordered by the Court and the claims are now being heard together. Our subsidiaries filed a statement of defense and the proceedings are currently at the stage at which the parties have to submit affidavits containing evidence. We believe that the risk under the above lawsuit is not material to the business of our subsidiaries. We intend to vigorously defend our position against the lawsuit.

On July 12, 2010, a lawsuit was filed in the Tel-Aviv Regional Labor Court, or the Labor Court against our company, our subsidiaries, Mayotex and Export Erez, and against an officer of our company, by a former employee. The plaintiff alleges that we breached her employment agreement and violated certain Israeli labor related legislation by not paying her severance, payment in lieu of vacation, recuperation payments, contribution to a study fund, payments due during a prior notice period and compensation for unpaid overtime. She also claimed that she was the subject of sexual harassment and consequently we violated certain applicable Israeli legislation. The plaintiff is seeking damages of \$414,775. Management believes that the amounts sought are exaggerated and that the exposure, if any, is not material to the business of the Group. We have filed statements of defense rejecting the former employee's claims and initiated a counter claim for \$28,129 in respect of libel and slander. We intend to vigorously defend our position. The Labor Court has imposed a gag order on the parties to the lawsuit.

Item 4.

(Removed and Reserved).



## PART II

## Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Securities.

## Market Information

Our common stock is traded on the Over the Counter Bulletin Board under the symbol "DFNS.OB." The table below contains the high and low bid closing prices of our common stock as reported on the OTCBB for the time periods indicated. These quotations reflect inter-dealer prices, without retail mark-up, markdown or commission, and may not necessarily represent actual transactions.

	Price Range	
	High	Low
Fiscal Year Ended December 31, 2010		
First Quarter	\$ 0.22	\$ 0.12
Second Quarter	0.19	0.12
Third Quarter	0.16	0.10
Fourth Quarter	0.12	0.6
Fiscal Year Ended December 31, 2009		
First Quarter	\$ 0.28	\$ 0.15
Second Quarter	0.33	0.19
Third Quarter	0.28	0.19
Fourth Quarter	0.25	0.14

The closing price for our common stock on April 8, 2011, as reported on the OTCBB, was \$0.085.

## Holders of Record

OTC Transfer Agent, Inc., located at 231 E 2100 S, Salt Lake City, Utah is the registrar and transfer agent for our common stock. As of April 11, 2011, there were 28,150,535 shares of our common stock outstanding and we had 29 shareholders of record.

## Dividends

We have not declared or distributed dividends in the past and do not currently have a dividend distribution policy. Any future dividend policy will be determined by our Board of Directors, subject to the applicable law, and will be based upon conditions then existing, including our results of operations, financial condition, current and anticipated cash needs, contractual restrictions and other factors as the Board of Directors may deem relevant.

## Compensation Plans

We currently do not have any compensation plans under which our securities are authorized for issuance.

## Item 6. Selected Financial Data.

Not applicable.



Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following is management's discussion and analysis of certain significant factors which have affected our financial position and operating results during the periods included in the accompanying consolidated financial statements, as well as information relating to the plans of our current management.

Overview

We are a manufacturer and global provider of personal military and civilian protective equipment and supplies. Our products are used by military, law enforcement, border patrol enforcement, and other special security forces, corporations, non-governmental organizations and individuals throughout the world. Our main products include body armor, bomb disposal suits, bullet proof vests and jackets, ballistic wall coverings, bullet proof ceramic and polyethylene panels, V.I.P. car armoring and lightweight armor kits for vehicles, personal military equipment, dry storage systems, liquid logistic products, tents and other camping and travel gear.

We believe that current international tensions, the continuing war on terrorism and conflicts in Iraq and Afghanistan are all likely to result in additional interest in our products, and that the demand for our products will continue to grow. We expect to address this growth by offering a comprehensive array of high quality branded security products that meet our customers' increasingly complex security products requirements.

Material Trends

Gross Profit Margins. Our pricing policy, although slightly different from one product to the other, is based on maintaining our existing overall gross margins. We do not expect a material change in our gross profit margins in the foreseeable in future.

Current Economic Overview. We generate revenues from sales of our products to the civilian and military markets. Accordingly, our business is affected by economic conditions. The volatile economic conditions throughout 2009 slowed-down our sales process and complicated our ability to conduct transactions. The current economic climate and the uncertainty in the global economic conditions could impact the ability of our customers, including governmental entities, to make capital expenditures, thereby affecting their ability to purchase our products. In addition, the turmoil in the financial markets may limit our ability to obtain financing in 2010. Our business and financial performance, including collection of our accounts receivable, realization of inventory and recoverability of assets including investments, may be adversely affected if economic conditions deteriorate or continue to be volatile. Our profitability may also be adversely affected by our fixed costs and the possibility that we would be unable to scale back other costs within a time frame sufficient to match any decreases in revenue relating to changes in market and economic conditions. The turmoil in the financial markets may limit our ability to obtain financing for our working capital requirements.

Exchange rate fluctuation. Exchange rate fluctuation affects our financial results in several ways. Most of our deposits and a portion of our tradable securities are linked to the rate of exchange between the U.S. dollar and the NIS. Accordingly, the devaluation of the U.S. dollar against the NIS is reflected as comprehensive income in our consolidated statements of operations.

We develop products in Israel and sell them in Israel, North and South America, Asia, Africa and several European countries. Our sales in Israel are denominated in NIS, while most of our export sales are denominated in U.S. dollars. Under U.S. GAAP we report all of our sales in U.S. dollars. Accordingly, appreciation of the U.S. dollar against the NIS reduces our reported sales while the devaluation of the U.S. dollar against the NIS increases our reported sales.

Our cost of sales and operating expenses are affected in the same manner. Most of our purchases of raw material are made in U.S. dollars while most of our labor and other operating expenses are in NIS, however, under U.S. GAAP we report our cost of sales and operating expenses in U.S. dollars. Accordingly, appreciation of the U.S. dollar against the NIS reduces our reported cost of sales and operating expenses while the devaluation of the U.S. dollar against the NIS increases our reported cost of sales and operating expenses.

In the year ended December 31, 2010, the U.S. dollar depreciated against the NIS by approximately 6% and our financial results were adversely affected. However, because exchange rates between the U.S. dollar and the NIS fluctuate continuously, exchange rate fluctuations and especially larger periodic devaluations will have an impact on our profitability and period-to-period comparisons of our results. We cannot assure you that in the future our results of operations may not be materially adversely affected by currency fluctuations.

#### The Sarino Agreement

On December 17, 2008, our subsidiary, Mayotex Ltd., or Mayotex, entered into an agreement with Sarino Crystal Technologies Ltd. and Sarino Optronics Ltd., or Sarino, to form an entity which will cooperate in the manufacture of optical grade germanium crystals and sales of lenses to be used in optical and infra-red night vision products utilizing the germanium crystals, or the Sarino Agreement.

On December 21, 2008, Mayosar Ltd., or Mayosar, which was incorporated by Mayotex and Sarino, through its wholly owned subsidiary Optics entered into an agreement, or the Isorad Agreement, to purchase the Germanium Crystals Business of Isorad Ltd., an Israeli governmental company, or Isorad. The Isorad Agreement provided for the purchase of certain know-how, equipment, inventories and production activities of germanium crystals for lenses used in infra-red night vision system applications.

After a period of uncertainty, in August 2010, Mayosar, Optics and Isorad executed an addendum to the 2008 agreement, according to which the parties confirmed the validity of the Isorad Agreement under certain conditions.

Pursuant to the Isorad Agreement, Optics is to pay annual royalties of 3% out of sales for a period of 15 years commencing the effective date of the Isorad Agreement, or the Effective Date, with a minimum of approximately \$133,000 payable per year during the first 18 months, or until the date of completion of the transfer of the site of the Optics business from Isoard's premises, whichever is earlier (this payment includes a reimbursement of costs for the usage of the site and equipment in this initial period), and approximately \$53,000 per year during the years following the initial 18 month period.

Isorad has the right to acquire 5% of the share capital of Optics on a fully diluted basis for their nominal value during the 24 month period beginning on the Effective Date. Such right was extended for an additional 12-month period until January 1, 2012. If the Israeli Government does not approve the 5% purchase of the Optics shares by Isorad within the above period, the right to acquire the shares will expire and Isorad will be entitled to a payment of \$75,000.

Optics has the right during the four-year period following the Effective Date to redeem its commitment to pay royalties under the Isorad Agreement and to repurchase Isorad's shares (or Isoard's option above to acquire shares) in consideration of a fixed payment of \$750,000, less all royalties and the above \$75,000 payment (in the event Isorad waived its right to be issued Optics shares) paid to through that date.

Pursuant to the Sarino Agreement:

Mayotex will have operational control of Mayosar.

Mayotex paid Sarino Crystal Technologies Ltd. \$1 million, or the Sarino Payment, out of which \$300,000 is non-refundable to Mayotex and the remaining \$700,000 will be earned by Sarino based on 10% of sales over \$3 million and up to \$10 million during the first 36 months of operations. Amounts not earned are to be refunded to Mayotex, including interest of Libor + 2% per year. The refundable consideration is secured by Sarino's interest in Mayosar and personal guarantees provided by Sarino Crystal Technologies Ltd.'s controlling shareholders.



Mayotex agreed to provide Mayosar with a loan in the aggregate amount of \$2 million under a timetable to be determined by Mayosar's board of directors. Such loan will bear interest at the rate of Libor + 2%, and is payable from profits generated by Mayosar.

In December 2010 Sarino and Mayotex entered into an agreement, or the December Agreement within the framework thereof, the parties agreed to amend the terms and conditions of the Sarino Payment to provide for: (i) a loan term of 10 years, commencing as of December 19, 2010; (ii) interest at LIBOR plus 1% per year commencing as of December 19, 2010; and (iii) the grant to Sarino Crystal Technologies Ltd. of a put option under which it could repay the Sarino Payment by selling its stake in Optics to Mayotex. Based on a purchase price allocation analysis, we recorded the Sarino loan as a liability against the minority interest.

In the event of an allotment of shares representing 5% of Optics' share capital to Isorad upon the exercise by Isorad of its option, Optics will issue additional shares of Optics to Mayotex on a pro rata basis, in order for Mayotex to retain a 82% interest in Optics' share capital.

In March 2011, Mayotex entered into an agreement with Rabintex Industries Ltd., or Rabintex, to purchase Philcar Ltd., or Philcar, a company that specializes in equipping and protecting vehicles in accordance with the specified requests of its customers, for \$214,304. Under the terms of the agreement, Mayotex may have to pay Rabintex additional compensation of up to \$160,728, depending on the amount of orders that Philcar receives from certain customers during the six-month period following the closing of the transaction. The closing of the agreement is pending certain third parties consents to be obtained by Philcar and Rabintex.

#### Critical Accounting Policies

We have identified the following policies as critical to the understanding of our financial statements. The preparation of our financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of sales and expenses during the reporting periods. Our financial statements have been prepared in accordance with accounting principles generally accepted in the United States.

Segments. During 2010 and 2009, we operated and managed two strategic business units: production for the civilian market and the military market. These operational segments are further broken down between Israel (local) and other (export) sales in order to better analyze trends in sales and profit margins. We do not allocate assets between segments because assets are used in more than one segment and any allocation would be impractical. (See Note 15(A) to our financial statements for segment information).

Revenue Recognition. Revenues from sales of products are recognized under the completed contract method upon shipment to customers. We provide a warranty on goods ranging from three to four years on certain products. Our policy to consider the establishment of a reserve for warranty expenses, based upon our historical experience. We did not establish a reserve at December 31, 2010 and December 31, 2009. If we change any of our assumptions with regard to our recognition of revenues, or if there is a change with respect to warranties expenses our financial position and results of operations may change materially.

Impairment of Intangible Assets and Long-Lived Assets. We periodically evaluate our intangible assets and long-lived assets (mainly property and equipment) for potential impairment indicators. Our judgments regarding the existence of impairment indicators are based on legal factors, market conditions, operational performance and prospects of our acquired businesses and investments. Our long-lived assets are reviewed for impairment annually and whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of the assets to the

future undiscounted cash flows expected to be generated by the assets. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. In measuring the recoverability of assets, we are required to make estimates and judgments in assessing our future cash flows which derive from the estimated useful life of our current primary assets, and compare that with the carrying amount of the assets. Additional significant estimates used by management in the methodologies used to assess the recoverability of our long-lived assets include estimates of future short-term and long-term growth rates, useful lives of assets, market acceptance of products and services, our success in winning bids and other judgmental assumptions, which are also affected by factors detailed in our risk factors section. If these estimates or the related assumptions change in the future, we may be required to record impairment charges for our long-lived assets. Future events could cause us to conclude that impairment indicators exist and that additional intangible assets and long-lived assets associated with our acquired businesses and our long-lived assets are impaired. Any resulting impairment loss could have a material adverse impact on our financial condition and results of operations.

The Company accounts for business combinations under ASC 805, "Business Combinations." ASC 805 requires recognition of assets acquired, liabilities assumed, and non-controlling interest in the acquiree at the acquisition date, measured at their fair values as of that date. ASC 805 also requires the fair value of acquired in-process research and development to be recorded as intangibles with indefinite lives, contingent consideration to be recorded on the acquisition date, and restructuring and acquisition-related deal costs to be expensed as incurred. Any excess of the fair value of net assets acquired over purchase price and any subsequent changes in estimated contingencies are to be recorded in earnings. In addition, changes in valuation allowance related to acquired deferred tax assets and in acquired income tax position are to be recognized in earnings.

ASC 805 requires significant judgment by management in determining the valuation of the acquired assets and intangible assets. As of December 31, 2010, management had not completed its valuation of the Isorad assets. The valuation of the acquired intangibles assets, including intellectual properties and technology, non compete agreement, customer relationships and trade name are provisional and may change upon completion of the Company's final valuation. As required by ASC 805, significant changes from the provisional valuation may result in a retrospective adjustment in the amounts reported at December 31, 2010.

Foreign Currency Translation and Transactions. The functional currency of Export Erez, Mayotex, and Achidatex is the New Israeli Shekel, or NIS. The financial statements for all of these entities are then translated into U.S. dollars from NIS at period-end exchange rates as to assets and liabilities and average exchange rates as to revenues and expenses. Capital accounts are translated at their historical exchange rates when the capital transactions occurred. Foreign currency transaction gains or losses from transactions denominated in currencies other than NIS are recognized in net income in the period the gain or loss occurs. Any change in exchange rates may have a material impact on our financial position and results of operations.

Fair Value of Financial Instruments. Our financial instruments are principally non-derivative assets and non-derivative liabilities (non-derivative assets include cash and cash equivalents, deposits in banks and other financial institutions, marketable securities, trade accounts receivable, other assets; non-derivative liabilities include short-term debt, trade accounts payable, and other current liabilities). Because of the nature of these financial instruments, fair value generally equals or approximates the amounts presented in the consolidated financial statements. The carrying amount of our long-term debt approximates quoted market prices or current rates offered to us for debt of the same remaining maturities.



**Disclosure of Certain Risks and Concentrations of Credit Risk.** At December 31, 2010 and 2009, we held cash and cash equivalents, in the aggregate amount of \$3,502,461 and \$3,783,631, respectively, and most of these amounts were deposited with Israeli banks. Under Israeli law, the Bank of Israel insures all bank deposits without limits on the amount. Therefore, we do not anticipate losses in respect to these items.

A significant portion of our sales are made to government institutions and private industry in Israel. Consequently, the exposure to credit risks relating to these trade receivables is limited. Export sales are made primarily with a letter of credit by the buyer or under controlled credit with specific accredited customers, so the receivable is collectible. We perform ongoing credit evaluations of our customers and generally do not require collateral. An appropriate allowance for doubtful accounts is included in trade accounts receivable.

**Trading Securities.** We invest in mutual funds and common stock in Israel and in common stock in the United States. All trading securities as of December 31, 2010 and 2009 are carried at their fair market value based upon quoted market prices of those investments at year-end. Net realized and unrealized gains and losses on trading securities are included in net earnings in other income for the years ended December 31, 2010 and 2009.

**Accounts Receivable.** Accounts receivable consist primarily of receivables from customers and institutions. We record a provision for doubtful accounts, when appropriate, to allow for any amounts which may be unrecoverable based upon an analysis of our prior collection experience, customer creditworthiness and current economic trends.

**Inventories.** Inventories are stated at the lower of cost or market value. Inventories allowances are provided to cover risks arising from obsolete and slow-moving items, discontinued products and excess inventories according to revenue forecasts. As of December 31, 2010 and 2009, inventories allowances were \$724,426 and \$539,794, respectively.

Cost is determined as follows:

- Raw materials and components – using the first-in, first-out (FIFO) method.
- Work in progress and finished goods – represents the cost of raw materials, components and, manufacturing costs which include direct and indirect allocable costs.

Any change in our assumptions with respect to the need to write-off or write-down the value of our inventories may have material affect on our financial position or results of operations.

**Property Plant and Equipment.** Fixed assets are stated at cost, net of accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets of three to sixteen years.

Leasehold improvements are amortized using the straight line method over the period of the lease contract, provided that this period does not exceed the useful life of the asset. Fixed assets not in use, held for resale, are stated at the lower of net cost or estimated realizable value. Expenditures for maintenance and repairs are charged to expense as incurred, while renewals and betterment of a permanent nature are capitalized.

## Results of Operations

### Key Indicators

Our management views revenues, the sources of our revenues, gross profit margin and the level of inventory compared to revenues as the key performance indicators in assessing our company's financial condition and results of operations. While our management believes that demand for our products is stable, our business is subject to a high

degree of volatility because of the impact of geopolitical events and government budgeting.

## Year Ended December 31, 2010 Compared with Year Ended December 31, 2009

Net Revenues and Gross Profit Margin. Net revenues for the year ended December 31, 2010 increased to \$16,585,163 from \$16,503,104 in the year ended December 31, 2009, an increase of 0.5%. The increase is primarily attributable to an increase of approximately \$0.7 million in our sales to the export military market segment, an increase of approximately \$1.1 million in sales to the local civilian market segment and the appreciation of the U.S. dollar against the NIS, which was offset in part by a decrease of approximately \$2.3 million in sales to the local military market segment. The decrease in sales to the local military market segment is attributable to a general decrease in orders from the Israeli Ministry of Defense.

The following tables set forth the breakdown of sales by segment and subsidiary for the years ended December 31, 2010 and December 31, 2009.

## Sales by segment

	Year Ended December 31,	
	2010	2009
Sales to the local civilian market	\$ 3,716,420	\$ 2,625,347
Sales to export civilian market	1,754,186	1,153,659
Sales to the local military market	5,144,353	7,467,792
Sales to export military market	5,970,204	5,256,306
Total	\$ 16,585,163	\$ 16,503,104

## Sales by Subsidiaries

	Year Ended December 31,					
	2010		2009			
	Sales	% of Sales	Sales	% of Sales		
Export Erez	\$ 7,902,447	47.6 %	\$ 10,752,729	65.2 %		
Achidatex	6,938,937	41.8 %	4,596,716	27.8 %		
Owen Mills	1,743,779	10.5 %	1,153,659	7.0 %		
Total	\$ 16,585,163	100 %	\$ 16,503,104	100 %		

Gross Profit. Gross profit for the year ended December 31, 2010 was \$2,895,425 compared to \$3,388,488 for the year ended December 31, 2009. This decrease in gross profit in 2010 is primarily attributable to higher overhead expenses, higher labor costs due to the appreciation of the NIS against the dollar and a large sale bearing a lower profit margin.

Our gross profit margin for the year ended December 31, 2010 was 17.5% compared to 20.5% for the year ended December 31, 2009. The decline is primarily attributable to higher overhead expenses, higher labor costs due to the appreciation of the NIS against the dollar, and a lower margin sale. Export Erez's gross margin for the year ended December 31, 2010 was 14% compared to 13.6% for the year ended December 31, 2009, primarily due to a decrease in expenses. Achidatex's gross margin for the year ended December 31, 2010 was 20% compared to 22.7% for the year ended December 31, 2009, primarily due to higher labor and rental charges. Owen Mills' gross margin was 22.9% for the year ended December 31, 2010 compared to 15.3% for the year ended December 31, 2009, mainly due to an increase in revenues.

Selling Expenses. Selling expenses for the year ended December 31, 2010 increased by 28.1% to \$1,211,801 from \$945,968 for the year ended December 31, 2009. The increase in our selling expenses was attributable primarily to an increase in costs of export sales and commissions paid on export sales, as well as higher labor costs compared to 2009.

Export Erez's selling expenses for the year ended December 31, 2010 were \$534,364 compared to \$451,880 for the year ended December 31, 2009. Achidatex's selling expenses for the year ended December 31, 2010 were \$517,991 compared to \$387,510 for the year ended December 31, 2009. Owen Mills selling expenses for the year ended December 31, 2010 were \$158,090 compared to \$105,442 for the year ended December 31, 2009. Defense Industries selling expenses for the year ended December 31, 2010 were \$1,355 compared to \$1,136 for the year ended December 31, 2009.

**General and Administrative Expenses.** General and administrative expenses for the year ended December 31, 2010 increased by 60% to \$3,044,026 from \$1,902,410 for the year ended December 31, 2009, primarily due to an increase in consultant fees and labor costs.

**Acquisition Related Costs.** In order to complete the Isorad Agreement, we incurred \$1,058,814 of expenses which were expensed in 2010.

**Compensation for War Damages.** Export Erez and Mayotex received \$50,909 and \$165,129, respectively, in compensation from the Israeli Government under the "Property tax and compensation payments for war damages" Regulations, for the loss of employment days and potential revenues during 2009 and 2008 due to the security and military situation in the area in which Export Erez and Mayotex were located. This \$216,038 of compensation was recorded as a reduction to our operating expenses in 2009.

**Financial Expenses.** We had net financial expenses for the year ended December 31, 2010 of \$ 398,565 as compared to net financial expenses of \$73,212 for the year ended December 31, 2009. This is mainly due to the change in the U.S. dollar exchange rate versus the NIS, which resulted in an expense of \$363,875 for the year ended December 31, 2010 compared to income of \$66,396 for the year ended December 31, 2009.

**Other Income (Expense), Net.** We had other income, net for the year ended December 31, 2010 of \$138,707 as compared to other income, net of \$304,002 for the year ended December 31, 2009. Our other income in 2010 is attributable primarily to realized and unrealized gains on trading securities and gains due to changes in the fair market value of funds invested in respect of employees' rights upon retirement and a gain recognized upon the dissolution of our Dragonwear subsidiary. Our other income in 2009 is attributable primarily to realized and unrealized gains on trading securities and gains due to changes in the fair market value of funds invested in respect of employee rights upon retirement.

**Income Tax Expense.** Our income tax expense for the year ended December 31, 2010 was \$101,167 as compared to income tax expense of \$464,672 for the year ended December 31, 2009. In 2010 and 2009, we did not record a tax benefit related to the loss incurred by our U.S. operations due to our deferred tax valuation allowance. In 2009, we recorded a deferred tax liability in respect of taxes on tax-exempt income derived from a Beneficiary Enterprise in Israel of \$235,947. Export Erez's income tax expense for the year ended December 31, 2010 was \$117,638 compared to \$274,801 for the year ended December 31, 2009. Achidatex's income tax expense for the year ended December 31, 2010 was \$16,471 compared to \$189,871 for the year ended December 31, 2009. Owen Mills did not have any income tax expense in 2010 or 2009.

**Net Income (Loss).** Our consolidated net loss for the year ended December 31, 2010 was \$2,573,076 as compared to net income of \$522,266 in the year ended December 31, 2009. Export Erez's net loss for the year ended December 31, 2010 was \$1,935,159 compared to net income of \$255,061 for the year ended December 31, 2009. Achidatex's net loss for the year ended December 31, 2010 was \$438,927 compared to net income of \$495,952 for the year ended December 31, 2009. Owen Mills' net loss for the year ended December 31, 2010 was \$116,936 compared to a net loss of \$170,642 for the year ended December 31, 2009.

#### Liquidity and Capital Resources

As of December 31, 2010, we had \$3,502,461 in cash and cash equivalents, \$1,894,864 in trading securities and working capital of \$7,299,260 as compared to \$3,783,631 in cash and cash equivalents, \$2,312,048 in trading securities and working capital of \$10,150,359 at December 31, 2009.



On October 27, 2010, Mayotex entered into an agreement to invest up to \$1.5 million in Mayo-Ben, a real estate company holding industrial properties in Israel which are occupied by our subsidiaries under lease agreements. In consideration of the investment, we acquired 20 per cent of the share capital of Mayo-Ben on a fully diluted basis. Mayo-Ben is controlled by the estate of Mr. Joseph Fostbinder, our former majority shareholder and chairman. The subscription price is subject to adjustment based on an appraisal of Mayo-Ben's fair value to be conducted by a major accounting firm in Israel.

Mayotex also agreed to lend Mayo-Ben \$1 million to be utilized by Mayo-Ben to improve and renovate its industrial properties, subject to and upon the terms of the agreement. Within the framework of a recent amendment to the Disengagement Plan Law, 5765 – 2005, under which several of our subsidiaries received compensation for their forced evacuation from the Gaza Strip area, such subsidiaries are eligible to apply for additional compensation, subject to certain requirements, including investment in the factories and properties to which they moved their activities and businesses, such as the properties held by Mayo-Ben. We expect that a portion of the grants, if any, to be received from the Israeli government within the above framework, will be used for renovations and improvements to the properties occupied by our subsidiaries and will entitle our subsidiaries to apply for additional grants and tax benefits. On March 28, 2011, Mayotex and Mayo-Ben entered into an addendum to the agreement pursuant to which, in the event that the subscription price will be subject to adjustment, Mayotex may elect to provide a portion of the investment amount by means of a loan instead of a subscription for the shares of Mayo-Ben. Such loan would be provided on the same conditions as the renovation loan, provided, however, that: (i) the loan granted to Mayo-Ben pursuant to the addendum, will not be subject to repayment under the terms of the renovation loan; and (ii) will bear interest of LIBOR minus 0.5%. Under the terms of the addendum, Mayotex will be entitled, at its own cost and expense, to obtain a new appraisal report that may challenge the findings of the original appraisal report upon the expiration of the third anniversary of the addendum.

Mayotex has agreed to forgive repayment of the loan in the event that Mayo-Ben invests at least the amount of the loan in the renovation and improvement of the properties in accordance with a renovation plan agreed to by both parties and to the complete satisfaction of Mayotex within a three (3) year period commencing on the first closing date of the transaction, of which at least \$200,000 must be spent for such renovations prior to August 30, 2011.

Pursuant to the draft of an appraisal report obtained by Mayotex to determine the fair company value of Mayo-Ben, the parties agreed that the fair company value of Mayo-Ben for the purpose of this agreement is \$3,734,574 and Mayotex agreed to exercise its right under the addendum to convert a portion of the investment amount exceeding the fair value of 20% of the outstanding share capital of Mayo-Ben into a loan, resulting in a total investment in Mayo-Ben of \$938,750 and loans of \$1,620,052 (including accrued interest). Pursuant to the appraisal report, Mayo-Ben's fair company value includes approximately \$676,000 attributable to the net cash flows derived by Mayo-Ben from two consulting agreements with Export Erez and Mayotex.

Mayo-Ben requested that the appraiser re-consider certain information underlying the draft analysis, which may affect the company valuation of Mayo-Ben in the final appraisal report. Mayotex further agreed to extend the term during which Mayo-Ben is entitled to object to the appraisal report to twelve months. In anticipation of the final appraisal report, Mayo-Ben and Mayotex agreed that until a final determination is made, to apply a company valuation based on the company valuation determined in the draft report, but not to reduce such valuation by the above revenue component. In addition, Mayo-Ben and Mayotex agreed that the final purchase price allocation will be subject to the final purchase price allocation report.

#### Cash Flows

Year ended	
December	December
31, 2010	31, 2009

Net cash provided by operating activities	\$ 530,990	\$ 1,503,984
Net cash provided by (used in) investing activities	(1,375,051)	1,961,761
Net cash provided by (used in) financing activities	334,782	(1,557,843)
Net increase (decrease) in cash and cash equivalents	(281,170 )	2,063,710
Cash and cash equivalents at beginning of year	3,783,631	1,719,921
Cash and cash equivalents at end of year	3,502,461	3,783,631

Operating activities. Net cash provided by operating activities was \$530,990 for the year ended December 31, 2010 as compared to \$1,503,984 provided by operating activities in the year ended December 31, 2009. The decrease in cash provided by operating activities was primarily attributable to our net loss of \$2,573,076, an increase in other current assets of \$747,167, an increase in related party accounts of 312,766, and an increase in funds reserved in respect of employee rights upon retirement of \$46,512, offset by a decrease in accounts receivable of \$1,145,232, a decrease in trading securities of \$503,715, a decrease in inventories of \$460,849, an increase in other current liabilities of \$369,770, and an increase in accounts payable of \$185,514. In 2009, our cash flow from operating activities reflected net income of \$522,266, a decrease in inventories of \$1,251,844, a decrease in trading securities of \$215,407, a decrease in trading securities of \$215,407, an increase in liability for employee rights upon retirement of \$80,300 and an increase in related parties accounts of \$76,230, offset by a decrease in other current liabilities of \$822,100, a decrease in accounts payable of \$305,859, an increase in funds reserved in respect of employee rights upon retirement of \$124,242 and an increase in other current assets of \$59,698.



Investing activities. Net cash used in investing activities was \$1,375,051 for the year ended December 31, 2010 as compared to net cash provided by investing activities of \$1,961,761 in the year ended December 31, 2009. During the year ended December 31, 2010, we provided a loan of \$1,000,000 to an associated company, invested \$225,863 in such company and purchased fixed assets of \$227,162. During the year ended December 31, 2009, \$3,000,000 was provided from the redemption of restricted bank deposits, \$938,666 was used for a refundable deposit for the purchase of Isorad and \$99,573 (net of sales of fixed assets in the amount of \$58,662) was used to purchase fixed assets.

Financing activities. Net cash provided by financing activities was \$334,782 for the year ended December 31, 2010 as compared to net cash of \$1,557,843 used in financing activities for the year ended December 31, 2009. During the year ended December 31, 2010, we incurred short-term debt of \$462,711 and long-term debt of \$167,653, offset by the repayment of \$295,582 of long-term debt. During the year ended December 31, 2009, we paid \$1,200,000 to the former minority shareholders of Achidatex for their interests in Achidatex and our company, and repaid \$337,339 of long-term debt and \$20,504 of short-term debt.

Most of our large contracts, which are Israeli Governmental contracts, are supported by letters of credit. As a result, we believe that we have limited exposure to doubtful accounts receivables. We have strived to balance our accounts payable and accounts receivable.

We believe that we have sufficient working capital and borrowing capability to sustain our current level of operations for the next twelve months.

#### Contractual Obligations

The following table summarizes our contractual obligations and commercial commitments as of December 31, 2010.

	Total	Payments due by Period			
		less than 1 year	2-3 years	4 -5 years	5 years and more
Long-term debt obligations	\$446,204	\$205,259	\$215,612	\$25,333	-
Estimated interest payments on long-term debt obligations	29,789	15,388	10,635	3,766	-
Operating lease obligations	1,917,288	651,868	899,170	365,299	-
Total	\$2,393,281	\$873,515	\$1,125,417	\$394,398	-

#### Recent Accounting Pronouncements

See "New Accounting Pronouncements" set forth in Note 1 of the Notes to the Consolidated Financial Statements under Item 8 of this Annual Report on Form 10-K, for information pertaining to recently adopted accounting standards or accounting standards to be adopted in the future.

#### Foreign Currency Exchange Risk

We develop products in Israel and sell them in Israel, North and South America, Asia, Africa and several European countries. Our sales in Israel are denominated in NIS while most of our export sales are denominated in U.S. dollars. In addition, our labor expenses are primarily paid in NIS while our expenses for raw materials are paid primarily in U.S. dollars. As a result, our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets.



Our foreign currency exposure is significant due to the depreciation of the U.S. dollar versus the NIS. We expect our exposure will continue to be significant, since a significant portion of the prices of our raw material purchases, as well as part of our sales are denominated in U.S. dollars.

In the year ended December 31, 2010, the inflation rate in Israel was 2.7% and the NIS appreciated in relation to the U.S. dollar at a rate of 6%, from NIS 3.775 per \$1 on December 31, 2009 to NIS 3.549 per \$1 on December 31, 2010. In the year ended December 31, 2009, the inflation rate in Israel was 3.91% and the NIS appreciated in relation to the U.S. dollar at a rate of 0.71%, from NIS 3.802 per \$1 on December 31, 2008 to NIS 3.775 per \$1 on December 31, 2009. If future inflation in Israel exceeds the devaluation of the NIS against the U.S. dollar or if the timing of such devaluation lags behind increases in inflation in Israel, our results of operations may be materially adversely affected.

We did not enter into any foreign exchange contracts in the year ended December 31, 2010.

#### Inflation and Seasonality

We do not believe that our operating results have been materially affected by inflation during the preceding two years. There can be no assurance, however, that our operating results will not be affected by inflation in the future. Our business is subject to minimal seasonal variations with slightly increased sales historically in the second and fourth quarters of fiscal year. We generally experience a slight increase in sales of our camping equipment during the second quarter and in sales of our protective clothing during the fourth quarter.

#### Market Risk

At December 31, 2010 and 2009, we held cash and cash equivalents in the aggregate amount of \$3,502,461 and \$3,783,631, respectively, and most of these amounts were deposited with Israeli banks. Under Israeli law, the Bank of Israel insures all bank deposits without limits on the amount. Therefore, we do not anticipate losses in respect to these deposits.

As of December 31, 2010 we held \$1,894,864 of trading securities compared to \$2,312,048 of trading securities at December 31, 2009. Such securities are subject to market risk, and in 2010 we recorded recognized and unrecognized gains of \$33,218 with respect to our holdings due to the improved conditions in the stock market.

#### Interest Rate Risk

We have variable rate loans that we borrow from Israeli banks which are based on the local Prime Rate. Each increase of 1% in the Prime Rate will increase our interest expense by \$7,124.

#### Off-Balance Sheet Arrangements

None.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

Not Applicable.

Item 8. Financial Statements.

See Index to Consolidated Financial Statements on page F-0.



Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

Item9A. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures. As of December 31, 2010, our company's chief executive officer and chief financial officer conducted an evaluation regarding the effectiveness of our company's disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Exchange Act. Based upon the evaluation of these controls and procedures, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were not effective with respect to the material weaknesses, as described below in our internal control over financial reporting, that have not been fully remediated as of the end of the fiscal year 2010.

Disclosure Controls and Internal Controls. As provided in Rule 13a-14 of the General Rules and Regulations under the Securities and Exchange Act of 1934, as amended, Disclosure Controls are defined as meaning controls and procedures that are designed with the objective of insuring that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), is recorded, processed, designed and reported within the time periods specified by the SEC's rules and forms. Disclosure Controls include, within the definition under the Exchange Act, and without limitation, controls and procedures to insure that information required to be disclosed by us in our reports is accumulated and communicated to our management, including our chief executive officer and principal financial officer, as appropriate to allow timely decisions regarding disclosure. Internal Controls are procedures which are designed with the objective of providing reasonable assurance that (1) our transactions are properly authorized; (2) our assets are safeguarded against unauthorized or improper use; and (3) our transactions are properly recorded and reported, all to permit the preparation of our financial statements in conformity with generally accepted accounting principles.

#### Management's Annual Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of the Chief Executive Officer and Chief Financial Officer and effected by our board of directors, management and other personnel, 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.

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's evaluation of internal control over financial reporting includes using the Committee of Sponsoring Organizations of the Treadway Commission, or COSO, framework, an integrated framework for the evaluation of internal controls issued by COSO, to identify the risks and control objectives related to the evaluation of our control environment.

Based on their evaluation under the framework described above, our chief executive officer and chief financial officer have concluded that our internal control over financial reporting was ineffective as of December 31, 2010 because of material weaknesses related to our year end financial statement closing process resulting from insufficient knowledge of our financial staff regarding the application of U.S. GAAP to complex transactions.



#### Remediation Plan

We have taken the following steps to remediate our material weaknesses as follows:

- we have recruited a new chief financial officer and continue to recruit and hire additional accounting staff with technical expertise to ensure the proper application of accounting principles generally accepted in the United States;
- we are implementing revised policies and procedures and enhancing our review of complex transactions to ensure consistent application of U.S. GAAP and enhanced internal control over financial reporting; and
- we are increasing the level of preparation and review of our financial statements, and in connection therewith, we are implementing additional control procedures as part of our quarter and year-end close processes as well as adding resources in connection with our review of key financial estimates.

#### Changes in Internal Control over Financial Reporting

No change in our internal control over financial reporting occurred during the quarter ended December 31, 2010, that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

This annual report does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by our registered public accounting firm pursuant to the rules of the Securities and Exchange Commission that permit us to provide only management's report in this annual report.

Item 9B.

Other Information.

None.

## PART III

## Item 10. Directors, Executive Officers and Corporate Governance.

## Officers and Directors

Set forth below are the name, age, principal position and a biographical description of each of our directors, executive officers and key management personnel. Our Board of Directors is comprised of only one class. All of our directors will serve until the next annual meeting of stockholders and until their successors are elected and qualified, or until their earlier death, retirement, resignation or removal. Executive officers serve at the discretion of the Board of Directors, and are appointed to serve until the first Board of Directors meeting following the annual meeting of stockholders.

Name	Age	Position Held
Uri Nissani	56	Chief Executive Officer, President and Chairman of the Board of Directors
Chaim Hadad	36	Chief Financial Officer
Motti Hassan	60	Director
Tsippy Moldovan	53	Director
Arie Kizman	57	Chief Executive Officer of Achidatex
Eyal Avidov	50	Chief Executive Officer of Mayotex
Daniel Davidi	46	Chief Executive Officer of Export Erez

Uri Nissani was appointed Chief Executive Officer, President and a member of the Board of Directors effective January 1, 2010 and as Chairman of the Board effective October 13, 2010. From January 15, 2007 until December 15, 2009, Mr. Nissani served as the Head of Business Development of S.D.S (Star Defense Systems) Ltd., and Star Night Technologies Ltd., each of which are Israeli companies listed on the Tel Aviv Stock Exchange. Star Night Technologies Ltd. is a holding company holding a controlling stake in S.D.S (Star Defense Systems) Ltd. S.D.S (Star Defense Systems) Ltd. manufactures and markets products mainly for the defense industry and operates through three divisions: (i) a night vision solutions division; (ii) a safety and rescue products division; and (iii) an avionic systems division. Mr. Nissani also served as a director of S.D.S. (Star Defense Systems) Ltd. from October 1, 2006 until December 31, 2008. Mr. Nissani has significant experience in managing companies engaged in the defense industry and his background enhances the breadth of experience of our board of directors.

Chaim Hadad has served as our chief financial officer since January 2011. Prior to that, Mr Hadad served as controller of Skyvision Network Services Ltd. from April 2009 to October 2010. From March 2006 to February 2009, Mr. Hadad served as Manager of the Accounting and Controlling Department at Tnuva Food Industries Cooperative Agriculturist Society and CFO of Tnuva USA.

Motti Hassan has served as a director since October 30, 2002. Mr. Hassan, an electronics engineer served in the Israeli Army as a system engineer for 15 years until July 2000 when he retired and joined a private company in the field of professional video, as a sales and business development manager. Mr. Hassan holds a B.Sc. degree in Electronic



Engineering from the Ben Gurion University, Beer Sheva, Israel. Mr. Hassan's significant experience in the military and his engineering background enhance the breadth of experience of our board of directors.

Tsippy Moldovan has served as a director since March 2002. From 1987 until January 15, 2011, Mrs. Moldovan served as our Chief Financial Officer. Mrs. Moldovan attended Buchnich Accounting School in Ashkelon, Israel and completed course work in economics and management accounting from Mishlav School, Tel Aviv, Israel. Mrs. Moldovan's significant experience with our company and accounting background enhance the breadth of experience of our board of directors.

Arie Kizman has served as the Chief Executive Officer of Achidatex since October 2010. Prior to joining Achidatex, and from 2004 until December 2009, Mr. Kizman served as the Chief Executive Officer of Automotive Industries Ltd. In the past 25 years Mr. Kizman served in executive positions with Machshirey Tnua Group and Automotive Industries Ltd. Automotive Industries Ltd. assembles vehicles of various types and size for military, police and civilian use in both local and international markets and in addition to its automotive activities, manufacturers precise and complicated metal products.

Eyal Avidov has served as the Chief Executive Officer of Mayotex since December 2010. Prior to that and from January 2007 until March 2010, Mr. Avidov served as the Chief Executive Officer of Autocool, an Israeli company engaged in the field of air-conditioning systems for motor vehicles. During the years 2000 through 2006, Mr. Avidov served as a sales manager with Peugeot-Citroen, an Israeli company engaged in car sales.

Daniel Davidi has served as the Chief Executive Officer of Export Erez since November 2010. Prior to that, and from May 2009 until October 2010, Mr. Davidi was engaged as a security adviser in the Republic of Colombia and managed a private securities business owned by him. From 2005 until February 2009, Mr. Davidi served as the Israeli military attaché in Romania, Ukraine and Bulgaria.

On January 17, 2011, Mr. Yoel Or tendered his resignation as a director, effective as of February 1, 2011, for reasons related to the expansion of his personal business. On January 26, 2011, Mr. Avi Melamed tendered his resignation as a director, effective immediately, citing personal reasons. Ms. Meira Fostbinder and her son, Mr. Gil Fostbinder, resigned as directors effective October 13, 2010. We intend to elect new directors in 2011.

#### Family Relationships

None.

#### Audit Committee Financial Expert

Since we are an OTC Bulletin Board company, we are not required to establish an audit committee or to have an audit committee financial expert to serve on such committee. We hope to comply with those requirements in the future.

#### Section 16(a) Beneficial Ownership Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our executive officers, directors and persons who own more than 10% of a registered class of our equity securities to file with the SEC initial statements of beneficial ownership, reports of changes in ownership and annual reports concerning their ownership of common stock and other of our equity securities on Forms 3, 4 and 5, respectively. Executive officers, directors and greater than 10% shareholders are required by Commission regulations to furnish us with copies of all Section 16(a) reports they file.

To our knowledge, based solely on our review of the copies of such forms received by us, or written representations from certain reporting persons that no additional forms were required for those persons, we believe that during fiscal year 2010 all of our executive officers and directors subject to these reporting requirements filed the required reports on a timely basis.

#### Code of Ethics

We have adopted a Code of Ethics for Executive and Financial Officers, which applies to our chief executive officer, chief financial officer, corporate controller and other finance organization employees, and a Code of Conduct, which

applies to all of our employees. The Code of Ethics and the Code of Conduct are publicly available on our website at [www.defense-industries.com](http://www.defense-industries.com). Written copies are available upon request. If we make any substantive amendments to the Code of Ethics or the Code of Conduct or grant any waivers, including any implicit waiver, from a provision of these codes to our chief executive officer, chief financial officer or corporate controller, we will disclose the nature of such amendment or waiver on our website.

## Item 11. Executive Compensation

## Summary Compensation

The following table sets forth information concerning the total compensation during the last two fiscal years. As of December 31, 2010, no other executive officer was paid in excess of \$100,000.

## Summary Compensation Table

Name and Principal Position	Year	Salary (\$)	Bonus (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity Incentive Plan Compensation (\$)	All Other Compensation (\$)	Total
Uri Nissani- Chief Executive Officer, President and Chairman of the Board of Directors	2010 *	237,650	-	-	-	-	-	\$ 237,650
Joseph Fostbinder – former Chief Executive Officer and Chairman of the Board of Directors	2009 **	96,935	-	-	-	-	-	\$ 96,935
Baruch Tosh - former President ***	2009	109,197	-	-	-	-	-	\$ 109,197

\* In March 2011 Mr. Nissani's service agreement with the Company was terminated. Mr. Nissani will provide the Company with the services as an independent contractor, through a company wholly owned by him.

\*\* Mr. Fostbinder died in June 2009.

\*\*\* Mr. Tosh was replaced as President effective January 1, 2010.

The aggregate value of all other perquisites and other personal benefits furnished to each of these executive officers was less than \$10,000 for the years ended December 31, 2010 and 2009

## Grants of Plan-Based Awards for 2010

We did not award any stock options to our executive officers during the fiscal year ended December 31, 2010.

## Long-Term Incentive Plans-Awards in Last Fiscal Year

We do not currently have any long-term incentive plans.

## Outstanding Equity Awards at Fiscal Year End

We did not grant any equity awards to our executive officers during the fiscal year ended December 31, 2010.

## Option exercises and stock vested table.

None

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## Directors Compensation

Our directors do not receive compensation for their services on our Board of Directors or any committee thereof. The following table sets forth the compensation received by each of our Directors in 2010.

Name	Fees Earned or Paid in Cash (\$)	Stock Awards (\$)	Option Awards (\$)	Non-Equity		All Other Compensation (\$)	Total (\$)
				Incentive Plan Compensation (\$)	Nonqualified Deferred Compensation (\$)		
Uri Nissani	-	-	-	-	-	237,650 (1)	237,650
Motti Hassan	-	-	-	-	-	-	-
Avi Melamed	-	-	-	-	-	-	-
Tsippy Moldovan	-	-	-	-	-	32,402 (2)	32,402
Yoel Or	-	-	-	-	-	-	-
Meira Fostbinder	-	-	-	-	-	17,443 (3)	17,443
Gil Fostbinder	-	-	-	-	-	34,661 (4)	34,661
Dan Zarchin	-	-	-	-	-	124,916 (5)	124,916

(1) Mr. Nissani earned \$237,650 in consideration for his employment as our Chief Executive Officer in 2010.

(2) Ms. Moldovan, who resigned as chief financial officer effective January 15, 2011, earned \$32,402 in consideration for her employment as our chief financial officer in 2010.

(3) Ms. Fostbinder, who resigned as a director effective October 13, 2010, earned \$17,443 in consideration for her employment as our vice president of finance, secretary and treasurer in 2010.

(4) Mr. Fostbinder, who resigned as a director effective October 13, 2010, earned \$34,661 in consideration for his employment as assistant general manager of Mayotex Ltd., our wholly-owned subsidiary in 2010.

(5) Mr. Zarchin, who resigned as a director effective January 7, 2010, earned \$124,916 for his consulting services.

## Employment Agreements

Mr. Uri Nissani was appointed CEO, President and a member of the board of directors of the Company effective January 1, 2010. Subject to the execution of an option agreement and approval by our shareholders (if determined to be necessary), which as of the date of this report has not been finalized, Mr. Nissani has been granted options to purchase 7,088,259 shares of our common stock, par value \$0.0001 each. Options to purchase 4,252,960 shares will vest in ten quarterly installments beginning March 31, 2010. The remaining 2,835,299 options will vest upon achievement of certain milestones with respect to our performance in 2010 and 2011, as shall be agreed by the parties in the Option Agreement.

## Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The following table sets forth the number of shares of common stock beneficially owned as of April 8, 2011 by (i) those persons or groups known to us who will beneficially own more than 5% of our common stock; (ii) each director; (iii) each named executive officer whose compensation exceeded \$100,000 in the fiscal year ended December 31,

2010; and (iv) all directors and executive officers as a group. The information is determined in accordance with Rule 13(d)-3 promulgated under the Exchange Act based upon information furnished by persons listed or contained in filings made by them with the SEC by information provided by such persons directly to us. Except as indicated, the stockholders listed below possess sole voting and investment power with respect to their shares.

Name	Number of Shares of Common Stock Beneficially Owned (2)	Percentage of Outstanding Shares of Common Stock (3)
Uri Nissani (4)	19,460,000	69.13
Achiam Investments Ltd.(4)	19,460,000	
Motti Hassan	---	
Tsippy Moldovan	9,788	*
All officers and directors as a group (3 persons)	19,469,788	69.16

\* Less than 1% percent

(1) The addresses of Uri Nissani and Motti Hassan are c/o Defense Industries International, Inc., 12 Hamefalsim Street, Petach Tikva, Israel.

(2) Beneficial ownership is determined in accordance with the rules of the SEC and generally includes voting or investment power with respect to securities. Common stock relating to options currently exercisable or exercisable within 60 days of the date of this table, are deemed outstanding for computing the percentage of the person holding such securities but are not deemed outstanding for computing the percentage of any other person. Except as indicated by footnote, and subject to community property laws where applicable, the persons named in the table above have sole voting and investment power with respect to all shares shown as beneficially owned by them.

(3) Based upon 28,150,535 shares of common stock outstanding.

(4) Mr. Nissani is the chairman of the board of directors and sole shareholder of Achiam Investments Ltd. and therefore has investment and voting control over the 19,460,000 shares of our common stock held of record by Achiam Investments Ltd.

### Item 13. Certain Relationships and Related Transactions and Director Independence.

Effective January 1, 2010, Mr. Uri Nissani was appointed as our company's Chief Executive Officer, President and member of our Board of Directors. Under the engagement letter entered into by our company and Mr. Nissani, commencing January 1, 2010, Mr. Nissani was to be employed by our company and render management services, including the performance of the roles of chief executive officer and president, in consideration of a monthly salary of \$12,000, the use of a company car and social and other benefits as are customary and required under Israeli law. The terms of Mr. Nissani's engagement provides for 180-days prior notice for termination of the employee-employment relation.

Pursuant to the terms of the engagement letter, we granted Mr. Uri Nissani, subject to obtaining final approval of the final option agreement by our Board of Directors and certain other approvals and authorizations, which as of the date hereof have not yet been obtained, options to purchase 7,088,259 shares of common stock of our company; of which 2,835,299 options will vest upon the achievement of certain milestones with respect to our company's performance in 2010 and 2011, as shall be agreed by the parties in a detailed option agreement to be entered into by Mr. Nissani and the company. The remaining 4,252,960 stock options were to vest in 10 equal quarterly installments of 425,296 stock options, commencing on March 31, 2010. The exercise price of the options are to be agreed upon by the parties, provided that in no event shall the exercise price exceed the quoted market price on the OTCBB at the close of business on December 31, 2009. As of December 31, 2010, the parties have not signed a detailed option agreement



and none of the options are deemed to be granted.

On October 13 2010, Meira Fostbinder (as the Executrix of the estate of Mr. Joseph Fostbinder, the former controlling shareholder of our company), Meira Fostbinder (individually), Sharon Fostbinder and Avital Gerson, or the Fostbinders, entered into a share purchase agreement, or the Share Purchase Agreement with Achiam Investments Ltd., or Achiam, a private company controlled by Mr. Nissani, under which Achiam agreed to purchase and the Fostbinders agreed to sell, an aggregate of 19,460,000 shares of our company's common stock, or approximately 69.13%, of the outstanding shares of our common stock.

On November 1, 2010 our Export Erez subsidiary entered into a 24-month consulting agreement with Mayo-Ben for a monthly consideration of \$13,394 (\$338,123 for the entire term of the agreement). Pursuant to this consulting agreement, Mayo-Ben will provide Export Erez through one of its controlling shareholders, Ms. Sharon Fossbinder (the daughter of our former controlling shareholder), consulting services with respect to the business of Export Erez, including advice to the board of directors and management of Export Erez in respect of the operation of its business, developing scalable and efficient operations and business processes and with respect to participating in tenders within the framework of Export Erez's operation of business. In addition to the above services, Mayo-Ben further undertook to: (i) provide Export Erez all of the assistance it will require in connection with the filing and preparation of a petition to be filed with the Israeli Government in respect of obtaining additional grants pursuant to an amendment of the Disengagement Law; (ii) waive all rights that it may have had in respect of the portion of any additional grants it may be entitled to under Disengagement Law; (iii) enter into an a perpetual and irrevocable non-compete undertaking; and (iv) enter into a confidentiality and intellectual property assignment agreement.

On November 1, 2010 our Mayotex subsidiary entered into a 24 month consulting agreement with Mayo-Ben for a monthly consideration of \$13,394 (\$338,123for the entire term of the agreement). Pursuant to this consulting agreement, Mayo-Ben will provide Mayotex through one of its controlling shareholders, Mr. Gil Fostbinder (the son of our former controlling shareholder), consulting services with respect to the business of Export Erez, including advice to the board of directors and management of Export Erez in respect of the operation of its business, developing scalable and efficient operations and business processes and with respect to participating in tenders within the framework of Export Erez's operation of business. In addition to the above services, Mayo-Ben further undertook to: (i) provide Export Erez all of the assistance it will require in connection with the filing and preparation of a petition to be filed with the Israeli Government in respect of obtaining additional grants pursuant to an amendment of the Disengagement Law; (ii) waive all rights that it may have had in respect of the portion of any additional grants it may be entitled to under Disengagement Law; (iii) enter into an a perpetual and irrevocable non-compete undertaking; and (iv) enter into a confidentiality and intellectual property assignment agreement.

Pursuant to a lease agreement effective since January 1, 2001 (as extended and amended from time to time), our Achidatex and Export Erez subsidiaries lease an industrial building located in the Nazareth Industrial Zone, from a company owned by the former shareholders of Achidatex, Mr. Avraham Hatzor, Mr. Freddy Davidovitz, Mr. Shmuel Davidovitz and Mayo-Ben. The lease will expire on December 31, 2012; however, under the investment agreement between Mayotex and Mayo-Ben, Mayo-Ben undertook to extend the lease agreement on terms and conditions that will be no less beneficial to Achidatex and Export Erez as the terms and conditions of the current lease agreement.

Our Export Erez subsidiary leases approximately 1,219 square meters of space in the Industrial Area of Sderot from Mayo-Ben, primarily for its cut and sew operations. Export Erez recently entered into a new lease agreement, pursuant to the terms of the investment agreement with Mayo-Ben. The new lease provides for: (i) the extension of the lease until December 2015; (ii) reduced annual rental fees of \$58,778 for the first 2.5 years (instead of \$82,289 as provided under the previous agreement); and (iii) annual rental fees of \$66,615 for the remaining 2.5-year period.

Our Mayotex subsidiary leases 1,000 square meters of industrial space and an additional 1,280 square meters of outdoor space in the Industrial Area of Ashkelon from Mayo-Ben for its car armor installations activity. Pursuant to the investment agreement with Mayo-Ben and effective as of January 2011, Mayotex entered into a new lease agreement with Mayo-Ben under which: (i) the lease period was extended until December 2015; (ii) the annual rental fees for the initial 2.5-year period will be \$56,255; and (iii) the annual rental fees for the remaining 2.5 years will be \$64,291. The parties further agreed that the rental fees for 2010 will be retroactively reduced to \$57,059 (instead of \$67,506 as provided under the previous agreement).

#### Item 14. Principal Accounting Fees and Services

The following table sets forth, for each of the years indicated, the fees incurred to our independent registered public accounting firm, Baker Tilly Virchow Krause, LLP during 2010 and 2009. All of such fees were pre-approved by our Board of Directors.

Services Rendered	Year Ended December 31,	
	2010	2009
Audit (1)	\$ 51,827	\$ 69,281
Audit-related	-	--
Tax fees (3)	14,470	20,728
<b>Total</b>	<b>\$ 66,290</b>	<b>\$ 90,009</b>

(1) Audit services consist of work performed in connection with the audited financial statements for each fiscal year and in the review of financial statements included in quarterly reports during the year, as well as work normally done by the independent auditor in connection with statutory and regulatory filings, such as consents letters for SEC registration statements.

(2) Tax fees relate to the completion of our tax filings in the U.S.

#### Pre-Approval Policies and Procedures

Our Board of Directors has adopted a policy and procedures for the pre-approval of audit and non-audit services rendered by our independent public accountants, Baker Tilly Virchow Krause, LLP. The policy generally pre-approves certain specific services in the categories of audit services, audit-related services, and tax services up to specified amounts, and sets requirements for specific case-by-case pre-approval of discrete projects, those which may have a material effect on our operations or services over certain amounts. All services were pre-approved during 2010.

Pre-approval may be given as part of the Board of Directors' approval of the scope of the engagement of our independent auditor or on an individual basis. The pre-approval of services may be delegated to one or more of the Board of Directors' members, but the decision must be presented to the Board of Directors at its next scheduled meeting. The policy prohibits retention of the independent public accountants to perform the prohibited non-audit functions defined in Section 201 of the Sarbanes-Oxley Act or the rules of the SEC, and also considers whether proposed services are compatible with the independence of the public accountants.

PART IV

Item 15. Exhibits, Financial Statement Schedules.

The following documents are filed as a part of this Report:

(a)Financial Statements

See Item 8.

(b)Financial Statement Schedules

None.

(c)Exhibits

The following is a list of exhibits filed as part of this Annual Report on Form 10-K. Where so indicated by footnote, exhibits that were previously filed are incorporated by reference.

Exhibit Number	Description
3.1	Certificate of Incorporation (1)
3.2	Certificate of Amendment to the Certificate of Incorporation (2)
3.3	By-laws (3)
4.1	Share Purchase Agreement among Meira Fostbinder (as the heir of Mr. Joseph Fostbinder), Meira Fostbinder, Sharon Fostbinder, Avital Gerson and Achiam Investments Ltd. dated October 13, 2010 (4)
4.2	Investment Agreement for the Subscription to and Sale of Shares of Mayo-Ben Investments and Development Ltd. (5)
4.3	Addendum to the Agreement for the Subscription to and Sale of Shares of Mayo-Ben Investments and Development Ltd.
21.1	Subsidiaries of the Company
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
32.1	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	Engagement letter between the registrant and Mr. Uri Nissani dated December 31, 2009 (6)

- 
- (1) Filed as Exhibit 3 to the Registrant's Form 10-KSB for the year ended December 31, 2001.
- (2) Filed as Appendix C to the Registrant's Filing on Schedule 14C, filed with the Commission on December 30, 2002.
- (3) Filed as Appendix D to the Registrant's Filing on Schedule 14C, filed with the Commission on December 30, 2002.
- (4) Filed as Exhibit 99.1 to the Registrant's Report on Form 8-K bearing a cover date of October 13, 2010, filed October 18, 2010.
- (5) Filed as Exhibit 10.1 to the Registrant's Report on Form 8-K dated bearing a cover date of October 27, 2010, filed November 7, 2010.
- (6)

Filed as Exhibit 99.1 to the Registrant's Report on Form 8-K bearing a cover date of January 1, 2010, filed January 7, 2010.

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the Company caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DEFENSE INDUSTRIES INTERNATIONAL, INC.

Dated: April 12, 2011

/s/ Uri Nissani  
Name: Uri Nissani  
Title: Chief Executive Officer and President

In accordance with the Securities Exchange Act of 1934, this report has been signed below on April 12, 2011 by the following persons on behalf of the Registrant and in the capacities indicated.

/s/ Uri Nissani  
Name: Uri Nissani  
Title: Chairman of the Board of Directors, Chief Executive Officer and President

/s/ Chaim Hadad  
Name: Chaim Hadad  
Title: Chief Financial and Principal Accounting Officer

/s/ Motti Hassan  
Name: Motti Hassan  
Title: Director

/s/ Tsippy Moldovan  
Name: Tsippy Moldovan  
Title: Director

DEFENSE INDUSTRIES INTERNATIONAL, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of:  
Defense Industries International, Inc. and Subsidiaries.

We have audited the accompanying consolidated balance sheets of Defense Industries International, Inc. and Subsidiaries (the "Company") as of December 31, 2010 and 2009, and the related consolidated statements of operations, changes in equity and comprehensive income and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. 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 provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above, present fairly, in all material respects, the consolidated financial position of Defense Industries International, Inc. and Subsidiaries as of December 31, 2010 and 2009 and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Baker Tilly Virchow Krause, LLP

Baker Tilly Virchow Krause, LLP  
An independent member of Baker Tilly International

Minneapolis, Minnesota  
April 14, 2011



DEFENSE INDUSTRIES INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS

## ASSETS

	Note	December 31, 2010	December 31, 2009
<b>CURRENT ASSETS</b>			
Cash and cash equivalents		\$3,502,461	\$3,783,631
Trading securities	3	1,894,864	2,312,048
Accounts receivable, net of allowance for doubtful accounts of \$368,477 and \$343,629, respectively		2,324,985	3,352,751
Inventories	4	4,402,517	4,124,141
Deferred taxes	11	191,318	148,710
Other current assets		398,297	225,112
<b>Total Current Assets</b>		<b>12,714,442</b>	<b>13,946,393</b>
<b>PROPERTY, PLANT AND EQUIPMENT, NET</b>	<b>5</b>	<b>1,864,346</b>	<b>1,741,594</b>
<b>INVESTMENT AND LOANS TO ASSOCIATED COMPANY</b>	<b>6</b>	<b>1,274,991</b>	<b>---</b>
<b>OTHER ASSETS</b>			
Fund in respect of employee rights upon retirement		881,184	780,960
Intangible assets, net	17	1,300,445	---
Deferred taxes	11	22,155	25,659
Refundable deposits on purchase of a business	1	---	1,993,696
<b>Total Other Assets</b>		<b>2,203,784</b>	<b>2,800,315</b>
<b>TOTAL ASSETS</b>		<b>\$18,057,563</b>	<b>\$18,488,302</b>

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

DEFENSE INDUSTRIES INTERNATIONAL, INC. AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS (Cont.)

## LIABILITIES AND EQUITY

	Note	December 31, 2010	December 31, 2009
<b>CURRENT LIABILITIES</b>			
Accounts payable		\$1,519,545	\$1,408,741
Accounts payable - related parties	14	156,753	462,968
Short-term debt	7	1,299,546	876,554
Other current liabilities	8	1,674,027	1,047,771
<b>Total Current Liabilities</b>		<b>4,649,871</b>	<b>3,796,034</b>
<b>LONG-TERM LIABILITIES</b>			
Long-term portion of debt	9	240,945	268,250
Long portion of minimum royalty payment to the Government of Israel	1	466,500	---
Deferred taxes liabilities	11	261,866	229,191
Liability for employee rights upon retirement	10	967,309	911,440
<b>Total Long-Term Liabilities</b>		<b>1,936,620</b>	<b>1,408,881</b>
<b>TOTAL LIABILITIES</b>		<b>6,586,491</b>	<b>5,204,915</b>
<b>COMMITMENTS AND CONTINGENCIES</b>	12		
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<b>PARENT COMPANY SHAREHOLDERS' EQUITY</b>			
Preferred stock, \$0.0001 par value, 50,000,000 shares authorized, none issued and outstanding		---	---
Common stock, \$0.0001 par value, 250,000,000 shares authorized; 29,200,535 shares issued and 28,150,535 shares outstanding at December 31, 2010		2,920	2,920
Additional paid-in capital		2,997,370	2,997,370
Treasury stock (1,050,000 shares at cost)		(252,000 )	(252,000 )
Retained earnings		7,603,276	10,176,352
Accumulated other comprehensive gain		1,119,506	358,745