

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 6-K

REPORT OF FOREIGN ISSUER

PURSUANT TO RULE 13a-16 OR 15d-16
OF THE SECURITIES EXCHANGE ACT OF 1934

For the month of March, 2005

Metalink Ltd.

(Translation of registrant's name into English)

Yakum Business Park, Yakum 60972, Israel

(Address of principal executive office)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F Form 40-F

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934. Yes No

The following are included in this Report on Form 6-K:

1. Audited financial statements for fiscal year ended December 31, 2004.

The information contained in this Report on Form 6-K is hereby incorporated by reference into the Registration Statement on Forms F-3 No. 333-104147, and No. 333-13806.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: March 31, 2005

By: /s/ Yuval Ruhama
Yuval Ruhama
Vice President of Finance
METALINK LTD.

METALINK LTD.

**CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2004**

METALINK LTD.
CONSOLIDATED FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2004

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Metalink Ltd.

We have audited the accompanying consolidated balance sheets of Metalink Ltd. ("the Company") and its subsidiaries as of December 31, 2004 and 2003, and the related consolidated statements of operations, shareholders' equity and comprehensive income (loss) and cash flows for each of the three years in the period ended December 31, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements 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 the Company and its subsidiaries as of December 31, 2004 and 2003 and the consolidated results of their operations and their consolidated cash flows for each of the three years in the period ended December 31, 2004, in conformity with U.S. generally accepted accounting principles.

Brightman Almagor & Co.
Certified Public Accountants
A member firm of Deloitte Touche Tohmatsu

Tel Aviv, Israel
January 26, 2005

METALINK LTD.
CONSOLIDATED BALANCE SHEETS

	December 31,	
	2 0 0 4	2 0 0 3
	(in thousands)	
ASSETS		
Current assets		
Cash and cash equivalents	\$ 12,239	\$ 16,225
Short-term investments (Note 3)	16,191	12,967
Trade accounts receivable	4,228	3,252
Other receivables (Note 10)	2,201	614
Prepaid expenses	801	951
Inventories (Note 4)	4,861	4,434
Total current assets	40,521	38,443
Long-term investments (Note 3)	22,639	35,013
Severance pay fund (Note 6)	1,897	1,555
Property and equipment, net (Note 5)	4,746	5,262
Total assets	\$ 69,803	\$ 80,273
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Trade accounts payable	\$ 2,323	\$ 1,651
Other payables and accrued expenses (Note 10)	4,354	3,944
Total current liabilities	6,677	5,595
Commitments and contingent liabilities (Note 7)		
Accrued severance pay (Note 6)	2,836	2,377
Shareholders' equity (Note 8)		
Ordinary shares NIS 0.1 par value (Authorized - 50,000,000 shares, issued and outstanding 20,174,748 and 19,855,317 shares as of December 31, 2004 and 2003, respectively)	603	596
Additional paid-in capital	130,134	129,005
Deferred stock-based compensation	(20)	(209)
Accumulated other comprehensive income (loss)	(137)	268
Accumulated deficit	(60,405)	(47,474)
	70,175	82,186
Treasury stock, at cost; 898,500 shares as of December 31, 2004 and 2003	(9,885)	(9,885)
Total shareholders' equity	60,290	72,301
Total liabilities and shareholders' equity	\$ 69,803	\$ 80,273

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

METALINK LTD.

CONSOLIDATED STATEMENTS OF OPERATIONS

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands except share and per share data)		
Revenues (Note 11)	\$ 22,112	\$ 14,943	\$ 6,636
Cost of revenues (Note 11):			
Costs and expenses (excluding non-cash compensation of \$36, \$51 and \$51, respectively)	11,637	7,787	4,589
Royalties to the Government of Israel (Note 7)	648	388	144
Total cost of revenues	12,285	8,175	4,733
Gross profit	9,827	6,768	1,903
Operating expenses:			
Gross research and development (excluding non-cash compensation of \$40, \$147 and \$165, respectively)	18,950	16,349	15,240
Less - Royalty bearing and other grants	4,083	3,394	3,213
Research and development, net	14,867	12,955	12,027
Selling and marketing (excluding non-cash compensation of \$109, \$236 and \$233, respectively)	6,566	5,884	4,814
General and administrative (excluding non-cash compensation of \$21, \$178 and \$350, respectively)	2,471	2,560	2,884
Non-cash compensation	206	612	799
Total operating expenses	24,110	22,011	20,524
Operating loss	(14,283)	(15,243)	(18,621)
Financial income, net	1,352	1,684	2,283
Net loss	\$ (12,931)	\$ (13,559)	\$ (16,338)
Loss per ordinary share:			
Basic	\$ (0.68)	\$ (0.73)	\$ (0.89)
Diluted	\$ (0.68)	\$ (0.73)	\$ (0.89)
Shares used in computing loss per ordinary share:			
Basic	19,140,706	18,638,398	18,407,190
Diluted	19,140,706	18,638,398	18,407,190

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

METALINK LTD.

STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)
(in thousands, except share data)

	Number of outstanding shares	Number of treasury shares	Share capital	Additional paid-in capital	Deferred stock-based compensation	Treasury stock (at cost)	Accumulated other comprehensive income (loss)	Accumulated deficit	Total comprehensive income (loss)	Total
Balance at January 1, 2002	19,194,988	898,500	\$ 580	\$ 127,029	\$ (1,650)	\$ (9,885)	\$ -	\$ (17,577)		\$ 98,497
Changes during 2002:										
Exercise of employee options and shares	255,568	-	6	554	-	-	-	-	-	560
Deferred stock-based compensation related to stock option grants to consultants	-	-	-	4	(4)	-	-	-	-	-
Cancellation of deferred stock-based compensation due to resignation of employees	-	-	-	(9)	9	-	-	-	-	-
Amortization of deferred stock-based compensation	-	-	-	-	799	-	-	-	-	799
Other comprehensive income:										
Unrealized gain on marketable securities	-	-	-	-	-	-	40	-	40	40
Loss for the year	-	-	-	-	-	-	-	(16,338)	(16,338)	(16,338)
Total comprehensive loss									<u>\$ (16,298)</u>	
Balance at December 31, 2002	19,450,556	898,500	586	127,578	(846)	(9,885)	40	(33,915)		83,558
Changes during 2003:										
Exercise of employee options	400,761	-	10	1,426	-	-	-	-	-	1,436
Exercise of consultant options	4,000	-	-	20	-	-	-	-	-	20
Deferred stock-based compensation related to stock option grants to consultants	-	-	-	12	(12)	-	-	-	-	-
Cancellation of deferred stock-based compensation due to resignation of employees	-	-	-	(31)	31	-	-	-	-	-
Amortization of deferred stock-based compensation	-	-	-	-	618	-	-	-	-	618
Other comprehensive income:										
Unrealized gain on marketable securities	-	-	-	-	-	-	228	-	228	228
Loss for the year	-	-	-	-	-	-	-	(13,559)	(13,559)	(13,559)
Total comprehensive loss									<u>\$ (13,331)</u>	
Balance at December 31, 2003	<u>19,855,317</u>	<u>898,500</u>	<u>\$ 596</u>	<u>\$ 129,005</u>	<u>\$ (209)</u>	<u>\$ (9,885)</u>	<u>\$ 268</u>	<u>\$ (47,474)</u>		<u>\$ 72,301</u>

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

METALINK LTD.

STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS) (CONT.)
(in thousands, except share data)

	<u>Number of outstanding shares</u>	<u>Number of treasury shares</u>	<u>Share capital</u>	<u>Additional paid-in capital</u>	<u>Deferred stock-based compensation</u>	<u>Treasury stock (at cost)</u>	<u>Accumulated other comprehensive income (loss)</u>	<u>Accumulated deficit</u>	<u>Total comprehensive income (loss)</u>	<u>Total</u>
Balance at January 1, 2004	19,855,317	898,500	\$ 596	\$ 129,005	\$ (209)	\$ (9,885)	\$ 268	\$ (47,474)		\$ 72,301
Changes during 2004:										
Exercise of employee options and shares	309,431	-	7	1,094	-	-	-	-	-	1,101
Exercise of consultant options	10,000	-	-	18	-	-	-	-	-	18
Deferred stock-based compensation related to stock option grants to consultants	-	-	-	17	(17)	-	-	-	-	-
Amortization of deferred stock-based compensation	-	-	-	-	206	-	-	-	-	206
Other comprehensive income:										
Unrealized loss on marketable securities	-	-	-	-	-	-	(405)	-	(405)	(405)
Loss for the year	-	-	-	-	-	-	-	(12,931)	(12,931)	(12,931)
Total comprehensive loss									<u>\$ (13,336)</u>	
Balance at December 31, 2004	<u>20,174,748</u>	<u>898,500</u>	<u>\$ 603</u>	<u>\$ 130,134</u>	<u>\$ (20)</u>	<u>\$ (9,885)</u>	<u>\$ (137)</u>	<u>\$ (60,405)</u>		<u>\$ 60,290</u>

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

METALINK LTD.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Cash flows from operating activities:			
Net loss	\$ (12,931)	\$ (13,559)	\$ (16,338)
Adjustments to reconcile net loss to net cash used in operating activities (Appendix)	1,359	3,008	4,244
Net cash used in operating activities	(11,572)	(10,551)	(12,094)
Cash flows from investing activities:			
Purchase of marketable debt securities and certificates of deposits	(16,218)	(11,143)	(171,758)
Proceeds from maturity and sales of marketable debt securities and certificates of deposits	24,189	29,296	177,342
Purchase of property and equipment	(1,504)	(1,991)	(838)
Net cash provided by investing activities	6,467	16,162	4,746
Cash flows from financing activities:			
Proceeds from issuance of shares and exercise of options, net	1,119	1,456	560
Net cash provided by financing activities	1,119	1,456	560
Increase (decrease) in cash and cash equivalents	(3,986)	7,067	(6,788)
Cash and cash equivalents at beginning of year	16,225	9,158	15,946
Cash and cash equivalents at end of year	\$ 12,239	\$ 16,225	\$ 9,158

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

METALINK LTD.

APPENDIX TO CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	\$ 2,020	\$ 1,985	\$ 3,033
Amortization of marketable debt securities and deposit premium and accretion of discount	786	863	979
Increase in accrued severance pay, net	117	112	58
Amortization of deferred stock-based compensation	206	618	799
Capital loss	-	96	-
Changes in assets and liabilities:			
Decrease (increase) in assets:			
Trade accounts receivable	(976)	(2,216)	930
Other receivables and prepaid expenses	(1,449)	734	51
Inventories	(427)	(530)	(1,098)
Increase (decrease) in liabilities:			
Trade accounts payable	672	(99)	277
Other payables and accrued expenses	410	1,445	(785)
	<u>\$ 1,359</u>	<u>\$ 3,008</u>	<u>\$ 4,244</u>

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

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 1 - GENERAL

Metalink Ltd. (the "Company"), an Israeli fabless semiconductor Company, develops and markets high performance broadband access chip sets used by telecommunications and networking equipment manufactures. Company's broadband silicon solutions enable, very high speed streaming video, voice and data transmission and delivery throughout worldwide communication networks. The Company operates in one business segment. The Company generates revenues from the sale of its products mainly in Asia, Europe and North America.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared in accordance with U.S. generally accepted accounting principles.

A. Use of Estimates in Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

B. Financial Statements in U.S. Dollars

The reporting currency of the Company is the U.S. dollar ("dollar" or "\$"). The currency of the primary economic environment in which the operations of the Company and its subsidiaries are conducted is the dollar, and the dollar has been determined to be the Company's functional currency.

Transactions and balances originally denominated in dollars are presented at their original amounts. Non-dollar transactions and balances have been remeasured into dollars in accordance with the principles set forth in Statement of Financial Accounting Standard ("SFAS") No. 52. All exchange gains and losses from remeasurement of monetary balance sheet items resulting from transactions in non-dollar currencies are reflected in the statements of operations as they arise.

C. Principles of Consolidation

The consolidated financial statements include the financial statements of the Company and its wholly-owned subsidiaries. All material inter-company transactions and balances have been eliminated.

D. Cash Equivalents

Cash equivalents consist of short-term, highly liquid investments that are readily convertible into cash with original maturities when purchased of three months or less.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

E. Marketable Debt Securities

The Company accounts for its investments in marketable securities in accordance with SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS 115").

Management determines the appropriate classification of the Company's investments in marketable debt securities at the time of purchase and reevaluates such determinations at each balance sheet date. Held-to-maturity securities include debt securities for which the Company has the intent and ability to hold to maturity. Debt securities for which the Company does not have the intent or ability to hold to maturity are classified as available-for-sale.

As of December 31, 2004 and 2003 all marketable debt securities are designated as available-for-sale and accordingly are stated at fair value, with the unrealized gains and losses reported as a separate component of shareholders' equity under accumulated other comprehensive income (loss). Realized gains and losses on sales of investments, as determined on a specific identification basis, are included in the consolidated statement of operations.

F. Allowance for doubtful accounts

The allowance for doubtful accounts has been made on the specific identification basis.

G. Inventories

Inventories are stated at the lower of cost or market. Cost is determined as follows:
Raw materials, components and finished products - on the moving average basis.
Work-in-process - on the basis of actual manufacturing costs.

H. Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated by the straight-line method over the estimated useful lives of assets, as follows:

Computers and manufacturing equipment	3-7 years
Furniture and fixtures	10-15 years

Leasehold improvements are amortized by the straight-line method over the shorter of the term of the lease or the estimated useful life of the improvements.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

H. Property and Equipment (Cont.)

The Company periodically assesses the recoverability of the carrying amount of property and equipment based on expected undiscounted cash flows. If an asset's carrying amount is determined to be not recoverable, the Company recognizes an impairment loss based upon the difference between the carrying amount and the fair value of such assets, in accordance with SFAS No. 144 "Accounting for the Impairment or Disposal of Long-Lived Assets".

I. Revenue Recognition

The Company recognizes revenue upon the shipment of its products to the customer provided that persuasive evidence of an arrangement exists, title has been transferred, the price is fixed, collection of resulting receivables is probable and there are no remaining significant obligations. The Company generally provides a warranty period for up to 12 months at no extra charge. No warranty provision has been recorded for any of the reported periods, since based on the past experience, such amounts have been insignificant.

J. Research and Development Expenses

Research and development expenses, net of third-parties grants, are expensed as incurred. The Company has no obligation to repay the grants, if sales are not generated.

K. Deferred Income Taxes

Deferred income taxes are provided for temporary differences between the assets and liabilities, as measured in the financial statements and for tax purposes, at tax rates expected to be in effect when these differences reverse, in accordance with SFAS No. 109 "Accounting for Income Taxes" ("SFAS 109").

L. Net Loss Per Ordinary Share

Basic and diluted net loss per share have been computed in accordance with SFAS No. 128 "Earning per Share" using the weighted average number of ordinary shares outstanding. Basic loss per share excludes any dilutive effect of options and warrants. A total of 753,515, 560,547 and 282,016 incremental shares were excluded from the calculation of diluted net loss per ordinary share for 2004, 2003 and 2002, respectively due to the anti-dilutive effect.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

M. Stock-based compensation

The Company accounts for employees and directors stock-based compensation in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and in accordance with FASB Interpretation No. 44 ("FIN 44"). Pursuant to these accounting pronouncements, the Company records compensation for stock options granted to employees and directors over the vesting period of the options based on the difference, if any, between the exercise price of the options and the market price of the underlying shares at that date. With respect to variable awards, changes in the market price of the underlying shares at each balance sheet date affect the aggregate amount of compensation recorded. Deferred compensation is amortized to compensation expense over the vesting period of the options.

Had compensation cost for the Company's stock option plans been determined based on fair value at the grant dates for all awards made in 2004, 2003 and 2002 in accordance with the provisions of SFAS No. 123 ("SFAS 123"), as amended by SFAS No. 148 "Accounting for Stock-Based Compensation" ("SFAS 148"), the Company's pro forma loss per share would have been as follows:

	2004	2003	2002
	(in thousands)		
Pro forma net loss			
Net loss for the year, as reported	\$ (12,931)	\$ (13,559)	\$ (16,338)
Deduct - stock-based compensation determined under APB 25	79	284	464
Add - stock-based compensation determined under SFAS 123	(3,013)	(3,241)	(3,686)
Pro forma net loss	<u>\$ (15,865)</u>	<u>\$ (16,516)</u>	<u>\$ (19,560)</u>
 Basic and diluted net loss per share			
As reported	\$ (0.68)	\$ (0.73)	\$ (0.89)
Pro forma	<u>\$ (0.83)</u>	<u>\$ (0.89)</u>	<u>\$ (1.06)</u>

For purposes of estimating fair value in accordance with SFAS 123, the Company utilized the Black-Scholes option-pricing model. The following assumptions were utilized in such calculations for the years 2004, 2003 and 2002 (all in weighted averages):

	2004	2003	2002
Risk-free interest rate	3.33%	3.22%	2.60%
Expected life of options	5 year	5 year	5 year
Expected volatility	51%	57%	70%
Expected dividend yield	none	none	none

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

N. Concentrations of Credit Risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents, bank deposits, marketable securities and trade receivables.

- (i) As of December 31, 2004 and 2003, the Company had cash and cash equivalents, short-term and long-term investments totaling \$51,069 and \$64,205, respectively, most of which are deposited in major U.S. financial institutions. Management believes that the financial institutions holding the Company's cash and cash equivalents and its deposits are financially sound. In addition, the marketable debt securities held by the Company consist of highly-rated corporate bonds and U.S. quasi-governmental agencies. Accordingly, limited credit risk exists with respect to this item.
- (ii) Most of the Company's revenues are generated in Asia, Europe and North America from a small number of customers (see Note 11). The Company generally does not require security from its customers. The Company maintains an allowance for doubtful accounts, which management believes adequately covers all anticipated losses in respect of trade receivables. As of December 31, 2004 and 2003 the amount for doubtful accounts was \$4.

O. Concentrations of Available Sources of Supply of Products

Certain components used in the Company's products are currently available to the Company from only one source and other components are currently available from only a limited number of sources. The Company does not have long-term supply contracts with its suppliers. In addition, the Company employs several unaffiliated subcontractors outside of Israel for the manufacture of its chipsets. While the Company has been able to obtain adequate supplies of components and has experienced no material problems with subcontractors to date, in the event that any of these suppliers or subcontractors is unable to meet the Company's requirements in a timely manner, the Company may experience an interruption in production. Any such disruption, or any other interruption of such suppliers' or subcontractors' ability to provide components to the Company and manufacture its chipsets, could result in delays in making product shipments, which could have a material adverse impact on the Company's business, financial condition and results of operations.

P. Fair Value of Financial Instruments

The financial instruments of the Company consist mainly of cash and cash equivalents, short-term investments, current accounts receivable, long-term investments, accounts payable and accruals. In view of their nature, the fair value of the financial instruments included in working capital and long term investments of the Company is usually identical or substantially similar to their carrying amounts.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Q. Reclassification

Certain prior years amounts have been reclassified in conformity with current year's financial statements presentation.

R. Effects of recently issued accounting standards

In November 2004 the FASB issued SFAS No. 151, "Inventory Costs, an Amendment of ARB No. 43, Chapter 4". SFAS No. 151 amends the guidance in ARB 43, Chapter 4, "Inventory Pricing", which provides guidance on the allocation of certain costs to inventory. SFAS 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage) should be recognized as current-period charges. In addition, SFAS 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. The provisions of this statement are effective for inventory costs incurred during fiscal years beginning after June 2005. The provisions of this statement shall be applied prospectively. The Company is assessing the impact of the adoption of this Standard, and currently estimates that its adoption is not expected to have a material effect on the Company's financial position and results of operations.

In December 2004, the FASB issued SFAS No. 123 (revised 2004) "Share Based Payments" ("SFAS 123(R)"). This Statement is a revision of FASB Statement No. 123, "Accounting for Stock-Based Compensation", which supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees" and its authoritative interpretations. SFAS 123(R) establishes standards for the accounting for transactions in which an entity exchanges its equity instruments for goods or services; focuses primarily on accounting for transactions in which an entity obtains employee and directors services in share-based payment transactions; and does not change the accounting guidance for share-based payment transactions with parties other than employees.

SFAS 123(R) eliminates the alternative to use APB 25's intrinsic value method of accounting that was provided in SFAS 123 as originally issued and requires to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. The fair-value-based method in this Statement is similar to the fair-value-based method in SFAS 123 in most respects. The costs associated with the awards will be recognized over the period during which an employee is required to provide service in exchange for the award - the requisite service period (usually the vesting period). The grant-date fair value of employee share options and similar instruments will be estimated using option-pricing models adjusted for the unique characteristics of those instruments (unless observable market prices for the same or similar instruments are available). If an equity award is modified after the grant date, incremental compensation cost will be recognized in an amount equal to the excess of the fair value of the modified award over the fair value of the original award immediately before the modification.

The provisions of SFAS 123(R) apply to all awards to be granted by the Company after June 30, 2005 and to awards modified, repurchased, or cancelled after that date. When initially applying the provisions of SFAS 123(R), in the third quarter of 2005, the Company will be required to elect between using either the "modified prospective method" or the "modified retrospective method". Under the modified prospective method, the Company is required to recognize compensation cost for all awards granted after the adoption of SFAS 123(R) and for the unvested portion of previously granted awards that are outstanding on that date.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Cont.)

R. Effects of recently issued accounting standards (Cont.)

Under the modified retrospective method, the Company is required to restate its previously issued financial statements to recognize the amounts previously calculated and reported on a pro forma basis, as if the original provisions of SFAS 123 had been adopted. Under both methods, it is permitted to use either a straight line or an accelerated method to amortize the cost as an expense for awards with graded vesting.

Management has recently commenced identifying the potential future impact of applying the provisions of SFAS 123(R), including each of its proposed transition methods, yet is currently unable to fully quantify the effect of this Standard on the Company's future financial position and results of operations. Nonetheless, it is expected that the adoption of SFAS 123(R) will increase the stock-based-award expenses the Company is to record in the future in comparison to the expenses recorded under the guidance currently applied by the Company.

In December 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets an amendment of APB No. 29". This Statement amends Opinion 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. The Statement specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. This Statement is effective for nonmonetary asset exchanges occurring in fiscal periods beginning after June 15, 2005. Earlier application is permitted for nonmonetary asset exchanges occurring in fiscal periods beginning after the date this Statement is issued. Retroactive application is not permitted.

NOTE 3 - INVESTMENT IN MARKETABLE SECURITIES AND DEPOSITS

A. Short-term investments

Comprised as follows:

	<u>December 31,</u>	
	<u>2 0 0 4</u>	<u>2 0 0 3</u>
	<u>(in thousands)</u>	
Corporate bonds	\$ 11,410	\$ 5,514
Certificates of deposit	4,781	6,638
U.S. quasi-governmental agencies	-	815
	<u>\$ 16,191</u>	<u>\$ 12,967</u>

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 3 - INVESTMENT IN MARKETABLE SECURITIES AND DEPOSITS (Cont.)

B. Long-term investments

Comprised as follows:

	December 31,	
	2 0 0 4	2 0 0 3
	(in thousands)	
Corporate bonds	\$ 11,111	\$ 16,499
Certificates of deposit	5,966	18,514
U.S. quasi-governmental agencies	5,562	-
	\$ 22,639	\$ 35,013

As of December 31, 2004 the aggregate maturities of marketable debt securities and deposits are as follows:

Year	(in thousands)
2006	\$ 20,220
2007	\$ 2,419

As of December 31, 2004 and 2003, all the investments are classified in accordance with SFAS 115 as available-for-sale.

NOTE 4 - INVENTORIES

Comprised as follows:

	December 31,	
	2 0 0 4	2 0 0 3
	(in thousands)	
Raw materials and components	\$ 1,983	\$ 709
Work-in-process	83	214
Finished products	2,795	3,511
	\$ 4,861	\$ 4,434

The balances are net of write-downs of \$607 and \$844 as of December 31, 2004 and 2003, respectively.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 5 - PROPERTY AND EQUIPMENT

Comprised as follows:

	December 31,	
	2004	2003
	(in thousands)	
Cost:		
Computers and manufacturing equipment	\$ 12,749	\$ 11,638
Furniture and fixtures	676	550
Leasehold improvements	1,131	864
	<u>\$ 14,556</u>	<u>\$ 13,052</u>
Accumulated depreciation and amortization:		
Computers and manufacturing equipment	\$ 9,240	\$ 7,364
Furniture and fixtures	205	148
Leasehold improvements	365	278
	<u>\$ 9,810</u>	<u>\$ 7,790</u>

NOTE 6 - ACCRUED SEVERANCE PAY, NET

The Company's liability for severance pay is calculated in accordance with Israeli law based on the latest salary paid to employees and the length of employment in the Company. The Company's liability for severance pay is fully provided for. Part of the liability is funded through individual insurance policies. The policies are assets of the Company and, under labor agreements, subject to certain limitations, they may be transferred to the ownership of the beneficiary employees.

The severance pay expenses for the years ended December 31, 2004, 2003 and 2002 were \$768, \$697 and \$538, respectively.

The Company has no liability for pension expenses to its employees.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 7 - COMMITMENTS AND CONTINGENT LIABILITIES

A. Royalties

- (i) The Company is committed to pay royalties to the Government of Israel on proceeds from the sale of products in the research and development of which the Government has participated by way of grants (received under the Chief Scientist program), up to the amount of 100%-150% of the grants received plus interest at LIBOR rate (in dollar terms). The royalties are payable at a rate of 4% for the first three years of product sales and 4.5% thereafter. The total amount of grants received, net of royalties paid or accrued, as of December 31, 2004 was \$19,053.

The research and development grants are presented in the statements of operations as an offset to research and development expenses.

The refund of the grants is contingent upon the successful outcome of the Company's research and development programs and the attainment of sales. The Company has no obligation to refund these grants, if sales are not generated. The financial risk is assumed completely by the Government of Israel. The grants are received from the Government on a project by project basis. If the project fails the Company has no obligation to repay any grant received for the specific unsuccessful or aborted project.

Royalty expenses to the Government of Israel for the years ended December 31, 2004, 2003 and 2002 were \$648, \$388 and \$144, respectively.

- (ii) The Company is obligated to pay royalties to certain third parties, based on agreements, which allow the Company to incorporate their products into the Company's products. Royalty expenses to these parties for the years ended December 31, 2004, 2003 and 2002 were \$371, \$231 and \$80, respectively.

B. Lease Commitments

- (i) The premises of the Company in Israel are rented under an operating lease agreement expiring in September 2010. In addition, the premises of the subsidiary in the United States are rented under two operating lease agreements: until March 2006, and until November 2006.

Future aggregate minimum annual rental payments pursuant to the existing lease commitments in effect as of December 31, 2004, are as follows:

<u>Year</u>	<u>(in thousands)</u>
2005	\$ 1,120
2006	1,008
2007	947
2008	947
2009 and thereafter	1,657

The Company arranged for a bank guarantee in favor of the lessors of the premises in Israel and in the United States totaling \$233.

Total rent expenses for the years ended December 31, 2004, 2003 and 2002 were \$1,044, \$983 and \$936, respectively.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 7 - COMMITMENTS AND CONTINGENT LIABILITIES (Cont.)

B. Lease Commitments (Cont.)

- (ii) The Company leases its motor vehicles under cancelable operating lease agreements, for periods through 2006. The minimum payment under these operating leases upon cancellation of these lease agreements, amounted to \$141 as of December 31, 2004. Lease expenses for the years ended December 31, 2004, 2003 and 2002, were \$948, \$716 and \$732, respectively.

C. Legal Claim

In July 1998, a former employee filed a claim against the Company in the Tel Aviv District Labor Court (the "Court") demanding that the Company issue him ordinary shares and pay on his behalf any taxes relating to such issuance; that the Company pay him statutory severance pay together with the statutory penalty for late payment of such severance pay and travel expenses; and that the Company release his managers insurance and continuing education fund. The Company filed a counterclaim against this former employee. In March 2001 the Court ordered that certain of the disputes between the parties be referred to a two-stage arbitration and pursuant to the Court's order the Company issued 75,765 ordinary shares (which are held in trust) in favor of the former employee. In addition, in January 2002, the Company paid the former employee \$16 in payment of statutory severance pay and reimbursement of travel expenses. In August 2002, the arbitrators in the first stage of the arbitration awarded \$391 to the former employee (which the Company paid in September 2002).

In December 2003 the former employee filed a claim in the second phase of the arbitration in the amount of \$3.9 million. The Company contested this claim and filed a claim for damages against the former employee in the amount of \$950 and for a refund of the \$435 already paid to him according to the foregoing judgment and of the \$35 paid as statutory severance pay and reimbursement of travel expenses.

The parties failed to reach agreement as to identity of the arbitrators who will adjudicate the second phase of the arbitration and the former employee filed a motion petitioning the court to appoint an arbitrator. The Company filed a claim in which it seeks a declaratory judgment that the arbitration agreement between the parties and all the arbitration proceedings under it are null and void. The Company also filed its response to the motion for the appointment of an arbitrator. The former employee filed a statement of defense contesting the Company's claim.

The Company believes that the resolution of this matter will not have a material adverse effect on the results of operations, liquidity, or financial condition, nor cause a material change in the number of outstanding ordinary shares, but there can be no assurance that the Company will necessarily prevail, due to the inherent uncertainties in litigation.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 8 - SHARE CAPITAL

- A. In December 1999, the Company completed an initial public offering in the United States and issued 4,600,000 ordinary shares (including the underwriters' over-allotment) for net proceeds of \$49,838. Following the public offering, the Company's shares are traded on the Over-the-counter market and are listed on the NASDAQ National Market.

In March 2000, the Company completed a second public offering in the United States and issued 1,500,000 ordinary shares for net proceeds of \$ 62,702.

Since December 2000, the shares of the Company are also traded on the Tel-Aviv Stock Exchange.

In October 2000 and March 2001, the Board of Directors of the Company approved the purchase of up to 1,000,000 of the Company's ordinary shares for up to \$10,000. Through December 31, 2003, the Company had purchased 898,500 of its ordinary shares, in the aggregate amount of \$9,885.

B. Employee Stock Purchase Plan

During 2000, the Board of Directors approved an Employee Stock Purchase Plan (the "ESPP"), effective October 2000. Under the ESPP, the maximum number of shares to be made available is 160,000 with an annual increase to be added on the first day of the year commencing 2001 equal to the lesser of 140,000 shares or 3/4 % of the outstanding shares on such date or a lesser amount determined by the Board of Directors.

Any employee of the Company is eligible to participate in the ESPP. Employee stock purchases are made through payroll deductions. Under the terms of the ESPP, employees may not deduct an amount exceeding \$25 in total value of stock in any one year. The purchase price of the stock will be 85% of the lower of the fair market value of an ordinary share on the first day of the offering period and the fair market value on the last day of the offering period. The offering period was determined to be six months. The ESPP shall terminate on October 31, 2010, unless terminated earlier by the Board of Directors. As of December 31, 2004, 329,080 ordinary shares were issued under the ESPP, and an additional 108,143 ordinary shares are available for issuance.

C. Stock Options

- (i) Under the Company's six Stock Option Plans (the "Plans"), up to 6,542,433 options approved to be granted to employees and directors of the Company or its subsidiary.
- (ii) Pursuant to the Plans, as of December 31, 2004, an aggregate of 1,687,187 options of the Company are still available for future grants.
- (iii) The options granted vest over periods of up to five years from the date of the grant, and most of them will expire after 10 years from the date of the grant. With respect to options granted at exercise prices below the fair market value of the underlying shares at the date of grant, deferred compensation is recorded and charged to earnings over the vesting period of the options in accordance with APB 25 and FIN 44.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 8 - SHARE CAPITAL (Cont.)

C. Stock Options (Cont.)

A summary of the status of the Company's stock option plans as of December 31, 2004, 2003 and 2002 and changes during the years then ended are as follows:

	December 31, 2004		December 31, 2003		December 31, 2002	
	Shares	Weighted average exercise price	Shares	Weighted average exercise price	Shares	Weighted average exercise price
Options outstanding at beginning of year	3,144,079	\$ 6.63	3,685,626	\$ 6.59	3,666,381	\$ 7.00
Granted during year	688,855	5.03	244,250	6.09	360,447	3.27
Forfeited during year	(264,167)	6.63	(385,036)	9.09	(275,126)	8.79
Exercised during year	(252,064)	3.45	(400,761)	3.58	(66,076)	1.93
Outstanding at end of year	<u>3,316,703</u>	6.54	<u>3,144,079</u>	6.63	<u>3,685,626</u>	6.59
Options exercisable at end of year	<u>2,443,491</u>	\$ 6.91	<u>2,349,473</u>	\$ 6.69	<u>2,218,214</u>	\$ 6.52
Weighted average fair value of options granted during year	<u>\$ 2.41</u>		<u>\$ 3.16</u>		<u>\$ 1.51</u>	

The following table summarizes information relating to stock options outstanding as of December 31, 2004:

Exercise price	Options outstanding			Options exercisable	
	Number outstanding at December 31, 2004	Weighted average remaining contractual life (in years)	Weighted average exercise price	Number exercisable at December 31, 2004	Weighted average exercise price
\$ 0.00 – 2.66	285,217	13.21	\$ 1.30	277,097	\$ 1.26
\$ 2.76 – 3.28	179,050	7.20	3.06	158,250	3.07
\$ 3.39 – 4.00	434,580	4.15	3.90	415,680	3.92
\$ 4.15 – 5.00	978,445	7.38	4.60	424,500	4.92
\$ 5.04 – 7.00	302,360	8.79	6.54	179,160	6.75
\$ 7.01 – 8.95	422,392	5.52	7.81	335,392	7.81
\$ 9.00 – 22.06	714,659	5.45	13.02	653,412	13.00
	<u>3,316,703</u>	6.93	\$ 6.54	<u>2,443,491</u>	\$ 6.91

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 8 - SHARE CAPITAL (Cont.)

D. Options issued to consultants

In April 2000, the Company adopted the "Share Option Plan - 2000" to provide for the grant of options to members of the advisory board of the Company and independent contractors. The options are exercisable over five years. As of December 31, 2004, 233,460 options have been granted (9,460, 8,000 and 16,000 in 2004, 2003 and 2002, respectively) under this plan to certain sales representatives and advisors of the Company at an exercise price of \$ 1.85 - \$ 15.75 per share. The Company accounted for these options under the fair value method of FAS No. 123 and EITF 96-18. The fair value was determined using the Black-Scholes pricing model with the following assumptions: risk-free interest rate of 2.6%-6.50%; volatility rate of 56.4%-108.9%; dividend yields of 0% and an expected life of one to five years.

Compensation expenses of \$127, \$334 and \$334 were recognized for the years ended December 31, 2004, 2003 and 2002, respectively.

NOTE 9 - TAXES ON INCOME

A. Taxation under Various Laws

(i) The Company and its subsidiaries are assessed for tax purposes on an unconsolidated basis. The Company is assessed under the provisions of the Israeli Income Tax Law (Inflationary Adjustments), 1985, pursuant to which results for tax purposes are measured in NIS in real terms in accordance with changes in the Israeli CPI. The Company's foreign subsidiaries are subject to the tax rules in their countries of incorporation.

(ii) "Approved enterprise"

The production facilities of the Company have been granted "approved enterprise" status in two separate programs under the Law for the Encouragement of Capital Investments, 1959, as amended. Under this law, income attributable to each of these enterprises, is fully exempt from tax for two years, commencing with the first year in which such enterprise generates taxable income, and is entitled to a reduced tax rate (25%) for a further eight years, respectively. The expiration date of the period of benefits is limited to the earlier of twelve years from commencement of production or fourteen years from the date of the approval. As of December 31, 2004, the period of benefits had not yet commenced.

Income derived from sources other than the "approved enterprise" is taxable at the ordinary corporate tax rate of 35% in 2004 (regular "Company Tax"). The regular Company Tax rate is to be gradually reduced to 30% until 2007 (34% in 2005, 32% in 2006 and 30% in 2007).

In the event of a distribution of cash dividends to the Company's shareholders of earnings subject to the tax-exemption, the Company will be liable to tax at a rate of 25% of the amounts of dividend distributed.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 9 - TAXES ON INCOME (Cont.)

B. Losses from Continuing Operations

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Israeli company	\$ (12,454)	\$ (12,337)	\$ (15,109)
U.S. subsidiary	(477)	(1,222)	(1,229)
	\$ (12,931)	\$ (13,559)	\$ (16,338)

C. Theoretical Income Taxes

The following is a reconciliation of the taxes on income assuming that all income is taxed at the ordinary statutory corporate tax rate in Israel and the effective income tax rate:

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Net loss as reported in the consolidated statements of operations	\$ (12,931)	\$ (13,559)	\$ (16,338)
Theoretical tax on the above amount (35% in 2004, 36% in 2003 and 2002)	\$ (4,526)	\$ (4,881)	\$ (5,882)
Tax benefit arising from the approved enterprise	3,736	3,824	4,684
Increase in valuation allowance	896	1,014	1,161
Permanent differences, net	(106)	43	37
Effective income tax rate	\$ -	\$ -	\$ -

D. Deferred Taxes

The main components of the Company's deferred tax assets are as follows:

	December 31,	
	2 0 0 4	2 0 0 3
	(in thousands)	
Net operating loss carry forwards in Israel	\$ 3,424	\$ 2,544
Net operating loss carry forwards of non-Israeli subsidiary	1,322	1,344
Other reserve and allowances	715	677
Total gross deferred tax assets	5,461	4,565
Less - Valuation allowance	5,461	4,565
Total deferred tax asset	\$ -	\$ -

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 9 - TAXES ON INCOME (Cont.)

D. Deferred Taxes (Cont.)

Under SFAS No. 109, deferred tax assets are to be recognized for the anticipated tax benefits associated with net operating loss carryforwards and deductible temporary differences, unless it is more likely than not that some or all of the deferred tax assets will not be realized. The adjustment is made by a valuation allowance.

Since the realization of the net operating loss carryforwards and deductible temporary differences is less likely than not, a valuation allowance has been established for the full amount of the tax benefits.

Tax loss carryforwards of the Company totaling \$68,484 are unlimited in duration, denominated in NIS and linked to the Israeli CPI.

Tax loss carryforwards of a U.S. subsidiary totaling \$3,887 expire between 2017 and 2021.

E. Tax Assessments

The Company and its subsidiary have not received final tax assessments for income tax purposes since incorporation.

NOTE 10 - SUPPLEMENTARY BALANCE SHEET INFORMATION

A. Other Receivables

Comprised as follows:

	December 31,	
	2 0 0 4	2 0 0 3
	(in thousands)	
Research and development participation from the Government of Israel	\$ 1,387	\$ -
Interest receivable on long- term investments	254	406
Loan to former employee (*)	132	132
Tax authorities	94	-
Others	334	76
	<u>\$ 2,201</u>	<u>\$ 614</u>

(*) Interest bearing loan granted to former employee under mediation and arbitration proceedings between the Company and the former employee. The loan is secured by a pledge of shares of the Company. For further details see Note 7C.

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 10 - SUPPLEMENTARY BALANCE SHEET INFORMATION (Cont.)

B. Other Payables and Accrued Expenses

Comprised as follows:

	December 31,	
	2 0 0 4	2 0 0 3
	(in thousands)	
Payroll and related amounts	\$ 2,687	\$ 2,387
Accrued expenses	1,337	1,109
Royalties to the Government of Israel	330	274
Others	-	174
	\$ 4,354	\$ 3,944

NOTE 11 - SUPPLEMENTARY STATEMENT OF OPERATIONS INFORMATION

A. Geographic Information

The following is a summary of revenues and long-lived assets by geographic area. Revenues are attributed to geographic region based on the location of the customers.

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Revenues:			
Korea	\$ 6,348	\$ 2,370	\$ 45
United States	4,034	4,101	1,285
Israel	2,520	1,842	3,170
Italy	1,473	1,120	913
Mexico	37	1,784	-
Other foreign countries (mainly European)	7,700	3,726	1,223
	\$ 22,112	\$ 14,943	\$ 6,636
	December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Long-lived assets:			
Israel	\$ 4,247	\$ 4,785	\$ 4,781
United States	499	477	571
	\$ 4,746	\$ 5,262	\$ 5,352

METALINK LTD.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(in thousands, except share and per share data)

NOTE 11 - SUPPLEMENTARY STATEMENT OF OPERATIONS INFORMATION (Cont.)

B. Sales to Major Customers

The following table summarizes the percentage of revenues from sales to major customers (exceeding 10% of total revenues for the year):

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
Customer A	23%	(*)	(*)
Customer B	12%	23%	(*)
Customer C	10%	(*)	45%
Customer D	(*)	17%	(*)
Customer E	(*)	(*)	14%

(*) Less than 10%.

C. Cost of Revenues:

	Year ended December 31,		
	2 0 0 4	2 0 0 3	2 0 0 2
	(in thousands)		
Materials and production expenses	\$ 9,464	\$ 7,314	\$ 4,110
Salaries, wages and employee benefits	329	318	402
Depreciation and amortization	468	536	412
Other manufacturing costs	529	385	356
	10,790	8,553	5,280
Decrease (increase) in finished products and work-in-process	847	(766)	(691)
	11,637	7,787	4,589
Royalties to the Government of Israel	648	388	144
	\$ 12,285	\$ 8,175	\$ 4,733

NOTE 12 - RELATED PARTIES

Payroll and related amounts to related parties in 2004, 2003 and 2002 were \$151, \$147 and \$406, respectively.