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

FORM 10-K

(Mark One)

☒ **ANNUAL REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the year ended: December 31, 2005

OR

☐ **TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from __________ to __________

Commission File Number 0-28082

KVH Industries, Inc.
(Exact Name of Registrant as Specified in its Charter)

Delaware	**05-0420589**
(State or Other Jurisdiction of Incorporation or Organization)	**(IRS Employer Identification Number)**

50 Enterprise Center, Middletown, RI 02842
(Address of Principal Executive Offices)

(401) 847-3327
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act: None.

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.01 par value per share
(Title of Class)

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 Exchange Act. **Yes** ☐ **No** ☒

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. **Yes** ☒ **No** ☐

Indicate by check mark 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☒ Non-acceleratedfiler ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). **Yes** ☐ **No** ☒

As of June 30, 2005, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was $134,731,430 based on the closing sale price of $9.25 per share as reported on the Nasdaq National Market.

Indicate the number of shares outstanding of each of the registrant's classes of common stock.

Class	Outstanding at March 13, 2006
Common Stock, $0.01 par value per share	14,746,901 shares

DOCUMENTS INCORPORATED BY REFERENCE

Document	Parts Into Which Incorporated
Definitive Proxy Statement for the 2006 Annual Meeting of Stockholders	Part III

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PART I

ITEM 1. Business

Forward-Looking Statements

In addition to historical facts, this annual report contains forward-looking statements. Forward-looking statements are merely our current predictions of future events. These statements are inherently uncertain, and actual events could differ materially from our predictions. Important factors that could cause actual events to vary from our predictions include those discussed in this annual report under the headings “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations”, and “Item 1A.-Risk Factors.” We assume no obligation to update our forward-looking statements to reflect new information or developments. We urge readers to review carefully the risk factors described in this annual report and in the other documents that we file with the Securities and Exchange Commission. You can read these documents at *www.sec.gov*.

Additional Information Available

Our principal Internet address is www.kvh.com. Our website provides a hyperlink to a third-party website through which our annual, quarterly, and current reports, as well as amendments to those reports, are available free of charge. We believe these reports are made available as soon as reasonably practicable after we electronically file them with, or furnish them to, the SEC. We do not provide any information regarding our SEC filings directly to the third-party website, and we do not check its accuracy or completeness.

Introduction

We develop, manufacture and market mobile communications products for the land and marine markets and navigation, guidance and stabilization products for defense and commercial markets. Our expertise in mobile satellite antenna, digital compass and fiber optic gyro technologies has enabled us to lower the cost, decrease the size and improve the performance of our products. Our research and development, manufacturing and quality control capabilities have enabled us to meet the demanding standards of our military, consumer and commercial customers for performance and reliability. This combination of factors has allowed us to increase our penetration of existing markets and enter new markets.

We are a leading provider of mobile communications products, such as our TracVision, TracPhone and TracNet systems, that enable customers to receive live digital television, telephone and Internet services in their automobiles, recreational vehicles and marine vessels while in motion via satellite and wireless services. We sell our mobile communications products through an extensive international network of retailers, distributors and dealers. In January 2006, we announced an agreement with Microsoft to bring high-speed Internet access and MSN TV service to cars, boats, and recreational vehicles, thereby expanding our ability to support mobile Internet and supplement our existing mobile satellite product lines.

Our defense products include tactical navigation systems that provide uninterrupted navigation and pointing information in a broad range of military vehicles, including tactical trucks (HMMWVs) and light armored vehicles. We also offer precision fiber optic gyro-based systems that help stabilize platforms, such as gun turrets and radar units, and provide guidance for munitions. We sell our defense products directly to U.S. and allied governments and government contractors, as well as through an international network of authorized independent sales representatives. Our fiber optic products are also used in such commercial applications as train track geometry measurement systems, industrial robotics, optical stabilization, autonomous vehicles, and undersea remotely operated submersibles.

Our Solutions

Mobile Communications

We believe that there is an increasing demand for mobile access to live media and information on the move. Our objective is to connect mobile users to the satellite TV, communications, and Internet services they wish to use by utilizing the best available and most appropriate data sources, such as satellite broadcasts or wireless service. We have developed a comprehensive family of products marketed under the TracVision, TracPhone and TracNet brand names that use a range of technologies to address the unique needs of our communications markets. Our products use sophisticated robotics, stabilization and control software, sensing technologies, 12-volt integration, and advanced antenna designs to offer the following benefits:

Consistent and reliable mobile satellite communications. Our mobile satellite communications products can automatically search for, identify and point directly at the satellite, whether a vehicle or vessel is in motion or stationary. Our antennas use gyros and inclinometers to measure the pitch, roll and yaw of an antenna platform in relation to the earth. Microprocessors and our proprietary stabilization and control software use that data to compute the antenna movement necessary for the antenna's motors to point the antenna properly and maintain contact with the satellite. If an obstruction temporarily blocks the satellite signal, our products continue to track the satellite's location according to the movement of the antenna in order to carry out automatic, rapid reacquisition of the signal when a direct line of sight to the satellite is restored.

Wide range of products for the mobile user. We provide mobile satellite communications products for a variety of vehicles in the land mobile market, which includes luxury motor coaches, buses, recreational vehicles, trucks, and automobiles, as well as a variety of vessels in the marine market, which includes commercial shipping vessels, commercial fishing vessels, merchant ships, and yachts. We developed our earliest products for the luxury yacht market and have succeeded in reducing the size and cost of our products for introduction into the land market. Initially we focused on larger vehicles like motor coaches, but we subsequently added support for passenger vehicles. Our TracVision A5 brings satellite television to automobiles using a patented, low-profile antenna system that currently provides in-motion satellite television in most of the continental United States using the DIRECTV service. Our entry into the automotive arena was facilitated by our hybrid phased-array antenna technology. We are currently investigating opportunities to transfer our commercial mobile satellite antenna technology into military applications, including small, affordable, high-bandwidth antennas suitable for military vehicles.

Access to mobile, two-way Internet, e-mail, and MSN TV communication. We currently support global broadband Internet access in the marine marketplace through the use of our TracPhone satellite communication antennas and the Inmarsat satellite services. In January 2006 we announced our intention to bring to market by mid-2006 a mobile Internet system suitable for cars, recreational vehicles, and boats in cooperation with Microsoft's MSN TV division. The planned system will use evolution-data optimized (EVDO) high-speed cellular data services to provide two-way access to the Internet and the MSN TV service. EVDO is currently available in more than 170 metropolitan areas and continues to expand. Should users be outside the EVDO coverage area, a slower speed cellular service will continue to provide uninterrupted accessibility. For recreational vehicles and marine vessels that may travel beyond the range of a typical EVDO antenna, we anticipate offering external, amplified antennas to increase the reception range of the mobile Internet system.

Commitment to customer support. Our Certified Support Network (CSN) offers our TracVision, TracPhone and TracNet customers an international network of skilled technical dealers and support centers in many locations where our customers are likely to travel. We have selected distributors based on their technical expertise, professionalism and commitment to quality and regularly provide them with extensive training in the sale, installation and support of our products.

Defense

We offer a portfolio of digital compass- and fiber optic gyro-based systems that address the rigorous requirements of military customers for precision navigation, guidance and stabilization. Our systems offer:

Reliable, continuously available navigation and guidance. Our systems provide an unjammable source of reliable, easy-to-use and continuously available navigation and pointing data. For example, our TACNAV system can tell a vehicle driver in which direction to steer to reach a certain target, how much farther to the destination, and whether or not the vehicle is on course. Because our digital compass products measure the earth's magnetic field rather than detect satellite signals from the global positioning system (GPS), they are not susceptible to GPS jamming devices. Our new fiber optic gyro-based inertial measurement unit product, or IMU, enhances the accuracy of guided underwater munitions. This IMU, along with our core fiber optic technology, also has potential commercial and industrial applications.

Compatibility with a wide range of vehicles and platforms. We offer variants of our TACNAV system using both our fiber optic gyros and digital compasses, providing low-cost, integrated tactical navigation solutions for military vehicles ranging from tactical trucks to combat vehicles. TACNAV systems address the varying operational requirements of different vehicles, such as turret pointing on a tank and vehicle navigation on a combat support vehicle. We also offer several fiber optic gyro-based products that support stabilization applications, such as stabilization of turrets, optical targeting systems, radar and communication antennas in both the military and commercial markets.

Integration and aggregation of data from on-board systems. Our navigation systems function as standalone tools and also aggregate, integrate and communicate critical information from a variety of on-board systems. TACNAV can receive data from systems such as the vehicle's odometer, military and commercial GPS devices, laser rangefinders, turret angle indicators and laser warning systems. TACNAV can also output this data to an on-board computer for retransmission through the vehicle's communications systems to a digital battlefield management application. We have also demonstrated to the U.S. Army an early prototype of a new TACNAV system that successfully combined TACNAV with satellite communication technology, potentially enabling TACNAV to communicate directly with digital battlefield management applications.

Our Products

We offer a broad array of products to address the needs of a variety of customers in the markets for mobile communications and defense navigation, guidance and stabilization.

Mobile Communications Products

Our mobile communications products include our TracVision, TracPhone and TracNet products, which offer satellite television and voice, fax, data and Internet communications to customers in the land mobile and marine markets. We began to offer both our first KVH-branded mobile satellite communications product, the TracPhone K2, and our first mobile satellite TV antenna, the TracVision, in 1995. Since that time, we have expanded our product offerings to include more than 15 different mobile satellite communications products. Our mobile satellite communications antennas are housed in impact-resistant domes to protect them from inclement weather or debris.

Land. We design, manufacture, and sell a range of TracVision satellite TV antenna systems for use on a broad array of vehicles. Our land satellite business comprises two principal vehicle classes and opportunities: automotive and RV/truck.

In the automotive market, we offer the TracVision A5, which uses hybrid phased-array antenna technology to provide in-motion reception of satellite TV programming in the continental United States using the DIRECTV service. Our TracVision A5 product includes a mobile satellite communications antenna and a 12V receiver designed specifically for the automotive environment to convert the satellite signal into a video stream. The TracVision A5 stands approximately five inches high and mounts either to a vehicle's roof rack or directly to the vehicle's roof, making it practical for use aboard minivans, SUVs and other passenger vehicles. The antenna's hybrid phased-array technology integrates 260 small antenna elements across a flat surface, mechanically rotates that surface horizontally and uses an electronic "lens" to bend the satellite signal so that the broadcast energy strikes each of the individual elements at closer to a perpendicular angle. The separate signals from each small antenna element are then combined to create a single data stream. In January 2005, DIRECTV introduced its TOTAL CHOICE MOBILE satellite TV programming package for automotive applications. At this time, we are the only company authorized by DIRECTV to sell, promote, and activate mobile users for the TOTAL CHOICE MOBILE programming package. In April 2005, Cadillac endorsed the TracVision A5 as a dealer-installed accessory option for the Cadillac Escalade. Since that time, a limited number of Cadillac dealers have elected to offer the TracVision A5 as an option during a new car purchase.

In the RV/truck market, we offer a line-up of our TracVision satellite TV products, including products intended for both stationary and in-motion use. In November 2005, we announced the overhaul of our RV product line, phasing out our older analog systems in favor of the digital TracVision R-series. These antennas offer automatic satellite switching and integrated compatibility with the international DVB (Digital Video Broadcast) standard at price points traditionally reserved for our older analog systems, which offered fewer features. The 14.5-inch high in-motion TracVision R5 and stationary automatic TracVision R4, which began shipping in December 2005, use an elliptical parabolic antenna to reduce the antenna's profile to address height restrictions on the road. The in-motion TracVision R6, which is expected to begin shipping in the spring of 2006, will serve as the premier product of our RV-specific offerings. This new system is expected to incorporate a number of innovations, including a high-efficiency antenna that is expected to reduce the product profile to 12.5 inches high while offering reception comparable to the larger systems, integrated GPS for faster satellite acquisition, and electronic dew elimination technology. In addition to sales through aftermarket dealers, we sell our TracVision products to original equipment manufacturers for factory installation on new vehicles. Each of these systems works with a range of service providers, including DIRECTV, DISH Network, and other regional service providers. Although initially designed for automotive applications, the TracVision A5 is now also sold within the RV marketplace to provide access to DIRECTV programming in in-motion applications and for vehicles with height restrictions that could prevent them from safely using a satellite TV antenna based on parabolic technology, and/or where the accumulation of moisture on the outer surface of the antenna's radome is not a concern.

Marine. In the marine market, we offer a range of mobile satellite TV and communications products. Our marine TracVision satellite TV antennas vary in size from a lower-profile elliptical parabolic system similar to those offered for use on RVs to 14.5-, 18-, and 24-inch diameter round antennas. Our largest marine satellite TV system is the TracVision G8, which includes a 32-inch carbon fiber antenna for greater range and efficiency. In October 2005, we introduced the TracVision M3, the world's smallest stabilized marine satellite TV system. Historically, marine satellite TV use has generally been limited to vessels longer than 40 feet due to the size of the antennas themselves. However, with reception comparable to larger 18-inch diameter antennas, our high-efficiency TracVision M3 is designed for vessels 25 to 40 feet in length, which we believe is a largely untapped market opportunity. The TracVision M3 system also includes an integrated 12-volt marine receiver for DIRECTV service, and an RF remote control for convenient operation and flexibility in the choice of installation locations.

Our TracPhone products provide in-motion access to global satellite communications offered by Inmarsat, a satellite service provider that supports links for phone, fax and data communications as fast as 128 Kbps, or kilobits per second. The TracPhone F77, F55 and F33 antennas use the new Inmarsat Fleet service to offer voice as well as high-speed Internet service, while our TracPhone 252 antenna offers lower-cost voice and low-speed data services via the Inmarsat mini-M service. The TracPhone F77, F55 and F33 are manufactured by Thrane & Thrane A/S of Denmark and distributed exclusively by us in North America under the KVH TracPhone label and distributed in other markets on a non-exclusive basis.

Broadband Internet and MSN TV Products. In addition to the global Internet access offered by our Inmarsat-compatible TracPhone systems, we also manufacture Internet-specific products for boats, RVs, and automobiles. Our TracNet 3.0 product provides mobile broadband Internet access in Europe, where Internet-via-satellite is a relatively common method for Internet service. TracNet 3.0 uses one of our TracVision antennas to receive broadband downloads of Internet data and either a cellular or satellite system, such as one of our TracPhone systems, as a return path.

In January 2006, we announced an agreement with Microsoft in which we will serve as a distributor of the MSN TV service to the marine, RV, and automotive markets. Our planned TracNet 100 Mobile Internet Receiver with MSN TV service is expected to provide in-motion access to Web browsing, Microsoft Windows Media Player, MSN Mail and MSN Messenger, digital photo viewing, MSN Video, and MSN Radio with two-way connections made possible by broadband EVDO cellular services. EVDO service is available in more than 170 markets nationwide, with new markets being added on an ongoing basis. Connection speeds for EVDO service are similar to residential DSL broadband service, with maximum speeds in excess of 2.4 Mbps and typical speeds of 400 Kbps to 700 Kbps. When EVDO is unavailable, the system will automatically switch to standard 1xRTT data service, which is available in most cellular coverage areas. 1xRTT has a maximum upload and download speed of 144 Kbps, and typical speeds of 50 Kbps to 80 Kbps. An amplified external antenna will be used to extend the range of the TracNet 100 in marine and RV applications in which the vessel or vehicle may move beyond the range of the system's integrated antenna.

The TracNet 100 will also include WiFi output to provide Internet connectivity to a wide range of WiFi-enabled products. We intend to sell the TracNet 100 through our existing network of marine, RV, and automotive dealers. We anticipate that the product will be in production and available for retail sale by mid-2006.

Defense Products

Our defense products include digital compasses for tactical navigation, fiber optic gyros for tactical navigation and stabilization and our recently introduced inertial measurement unit for precision guidance of torpedoes and unmanned aerial vehicles. Our TACNAV digital compass products have been sold for use aboard U.S. Army, Marine Corps, and Navy vehicles as well as to many allied countries, including Australia, the United Kingdom, Canada, Germany, Italy, New Zealand, Saudi Arabia, Spain, Sweden, Taiwan, Malaysia and Switzerland. We believe that we are among the leading manufacturers of such systems. Our standard TACNAV products can be customized to our customers' specifications. At customer request, we offer training and other services on a time-and-materials basis.

Our fiber optic gyro products use an all-fiber design without moving parts, which provides precision, accuracy and durability. Fiber optic gyros can be used for precision tactical navigation systems for military vehicles for stabilizing antennas, radar, optical devices or turrets, and image stabilization and synchronization for shoulder- or tripod-mounted weapon simulators. Our fiber optic products also support a broad range of commercial and industrial applications.

Tactical Navigation. The TACNAV II Fiber Gyro Navigation system is a fiber optic gyro-based navigation and pointing system designed to support a variety of vehicle and weapons platforms. The system offers a compact design, continuous output of heading and pointing data, and a flexible architecture that allows it to function as either a stand-alone navigation module or as the central component of an expanded, multifunctional navigation system.

TACNAV TLS is a digital compass-based tactical navigation and targeting system designed for turreted vehicles, including reconnaissance vehicles, armored personnel carriers and light armored vehicles. The system offers a range of capabilities, including GPS backup and enhancement, vehicle position, hull and turret azimuth, navigation displays, and target location.

The TACNAV M100 GMENS, formerly TACNAV Light, is a digital compass-based battlefield navigation system specifically designed for non-turreted vehicles, such as HMMWVs and trucks. We believe that customers purchase the TACNAV M100 GMENS in part because of its low cost relative to its performance. In September 2003, the TACNAV M100 GMENS was designated by the U.S. Special Operations Command as a standard product, and in November 2003 the German Army gave the product a similar designation. The TACNAV M100 GMENS offers a range of capabilities, including GPS backup and enhancement, vehicle position, hull azimuth and navigation displays.

Guidance and Stabilization. Our TG-6000 Inertial Measurement Unit, or IMU, introduced in October 2003, is a guidance system that provides precise measurement of motion and acceleration in three dimensions. It uses a three-axis configuration of our high-performance DSP-based fiber optic gyros integrated with three accelerometers. We believe that this configuration provides outstanding performance, high reliability, low maintenance and easy system integration. The TG-6000 IMU is in full production as a component in the U.S. Navy’s new MK54 lightweight torpedo and is suitable for use in other applications that involve flight control, orientation, instrumentation and navigation, such as unmanned aerial vehicles.

Our open-loop DSP-3000 and DSP-4000 fiber optic gyros provide tactical-grade precision measurement of the rate and angle of a platform’s turning motion for significantly less cost than competing closed-loop gyros. These products use digital signal processing, or DSP, technology to deliver performance superior to analog signal processing devices, which experience greater temperature-sensitive drift and rotation errors. Applications for these products include inertial measurement units, integrated navigation systems, attitude/heading/reference systems, and stabilization of antenna, radar and optical equipment.

The DSP-3000 is slightly larger than a deck of cards. High-performance 2-axis and 3-axis configurations can be realized by integrating multiple DSP-3000 units. Currently, the DSP-3000 is used in an array of pointing and stabilization applications, including the U.S. Army’s Stabilized Remotely Operated Weapon System, or SRWS. Two DSP-3000 gyros are installed in every SRWS turret and provide the image and gun stabilization necessary to ensure that the weapon remains aimed at its target. The larger, militarized DSP-4000 uses the core DSP-3000 technology in both 1- and 2-axis configurations and is designed for use in high-shock and highly dynamic environments, such as gun turret stabilization. Our fiber optic products are also used in numerous commercial applications, such as train location control and track geometry measurement systems, industrial robotics, optical stabilization, autonomous vehicles, and undersea remotely operated submersibles.

Sales and Marketing

We sell our mobile satellite communications products through an international network of independent retailers, chain stores and distributors, as well as to manufacturers of marine vessels and recreational vehicles. We currently market and sell the TracVision A5 in the continental United States through consumer electronic chain stores and a large number of retailers specializing in automotive electronics, as well as a variety of specialty distributors of automotive after-market products and auto dealership expediters. We intend to continue the consideration of opportunities to expand our distribution network to include additional retailers and distributors in the continental United States. In April 2005, Cadillac endorsed the TracVision A5 as a dealer-installed accessory option, and the system is now available as part of a new car purchase at participating dealers. We are also pursuing arrangements with other automobile manufacturers to include our TracVision A5 product as optional or standard equipment on the vehicles they manufacture.

Our European sales subsidiary located in Denmark, KVH Europe A/S, coordinates our sales, marketing and support efforts for our mobile satellite communications products in Europe, the Middle East and Africa.

We sell our defense products directly to U.S. and allied governments and government contractors, as well as through an international network of authorized independent sales representatives. This same network also sells our fiber optic products to commercial/industrial entities.

Backlog

Our backlog was approximately $9.5 million on December 31, 2005, $8.7 million on December 31, 2004, and $4.6 million on December 31, 2003.

Backlog consists of orders evidenced by written agreements and specified delivery dates for customers who are acceptable credit risks. Military orders included in backlog are generally subject to cancellation for the convenience of the customer. When orders are cancelled, we recover actual costs incurred through the date of cancellation and the costs resulting from termination. Individual orders for defense products are often large and may require procurement of specialized long-lead components and allocation of manufacturing resources. The complexity of planning and executing larger orders requires customers to order well in advance of the required delivery date, resulting in backlog.

Backlog is not a meaningful indicator for predicting revenue in future periods. Commercial resellers for our mobile satellite communications products and legacy products do not carry extensive inventories and rely on us to ship products quickly. Generally due to the rapid delivery of our commercial products, our backlog for those products is not significant.

Intellectual Property

Our ability to compete effectively depends to a significant extent on our ability to protect our proprietary information. We rely primarily on patents and trade secret laws, confidentiality procedures and licensing arrangements to protect our intellectual property rights. We own more than 50 U.S. and foreign patents and have additional patent applications that are currently pending. In January 2006, we entered into a licensing agreement with Litton Systems, Inc., a wholly owned subsidiary of Northrop Grumman Systems Corporation, with respect to certain of its fiber optic gyroscope-related patents. We also register our trademarks in the United States and other key markets where we do business. Our patents and trademarks will expire at various dates between March 31, 2006 and June 22, 2025. We enter into confidentiality agreements with our consultants, key employees and sales representatives, and maintain controls over access to and distribution of our technology, software and other proprietary information. The steps we have taken to protect our technology may be inadequate to prevent others from using what we regard as our technology to compete with us.

We do not generally conduct exhaustive patent searches to determine whether the technology used in our products infringes patents held by third parties. In addition, product development is inherently uncertain in a rapidly evolving technological environment in which there may be numerous patent applications pending, many of which are confidential when filed, with regard to similar technologies.

From time to time, we have faced claims by third parties that our products or technologies infringe their patents or other intellectual property rights, and we may face similar claims in the future. A description of such claims initiated against us during 2005 and currently pending is found in this annual report under the heading “Item 3. Legal Proceedings”. Any claim of infringement could cause us to incur substantial costs defending against the claim, even if the claim is invalid, and could distract the attention of our management. If any of our products is found to violate third-party proprietary rights, we may be required to pay substantial damages. In addition, we may be required to re-engineer our products or seek to obtain licenses from third parties to continue to offer our products. Any efforts to re-engineer our products or obtain licenses on commercially reasonable terms may not be successful, which would prevent us from selling our products, and, in any case, could substantially increase our costs and have a material adverse effect on our business, financial condition and results of operations.

Manufacturing

Manufacturing operations for our mobile satellite communications and navigation products consist of light manufacture, final assembly and testing. Manufacturing operations for our fiber optic gyro products are more complex. We produce specialized optical fiber, fiber optic components and sensing coils and combine them with components purchased from outside vendors for assembly into finished goods. We own optical fiber drawing towers where we produce the specialized optical fiber that we use in all of our fiber optic products. We manufacture our mobile satellite communications products at our headquarters in Middletown, Rhode Island, and utilize a nearby leased facility for warehousing and distribution purposes. We manufacture our navigation and fiber optic gyro products in a leased facility located in Tinley Park, Illinois.

We contract with third parties for fabrication and assembly of printed circuit boards, injection-molded plastic parts, machined metal components, connectors and housings. We believe there are a number of acceptable vendors for the components we purchase. We regularly evaluate both domestic and foreign suppliers for quality, dependability and cost effectiveness. In some instances we utilize sole-source suppliers to develop strategic relationships to enhance the quality of materials and save costs. Our manufacturing processes are controlled by an ISO 9001-certified quality standards program.

Competition

We encounter significant competition in all of our markets, and we expect this competition to intensify in the future. Many of our primary competitors are well-established companies and some have substantially greater financial, managerial, technical, marketing, operational and other resources than we do.

In the market for mobile satellite communications products, we compete with a variety of companies. We believe the principal competitive factors in this market are product size, design, performance, reliability, and price. In the recreational vehicle and truck space, we compete directly with King Controls, MotoSAT, TracStar Systems, Inc., and Winegard Company.

Our TracVision A5 was the first commercially available, low-profile mobile satellite TV antenna for use on minivans, SUVs and other passenger vehicles. At this time, we are not aware of any competing products in full production and available for widespread sale. We are aware of other companies that intend to compete with us, including: RaySat, Winegard, Sirius Satellite Radio, and certain other suppliers of automotive parts.

In the marine market for satellite TV communications equipment, we compete with NaviSystem Marine Electronics Systems Srl, Orbit Satellite Television & Radio Network, King Controls, TracStar, Sea Tel, Inc., and Raymarine. In the marine market for telephone, fax, data and Internet communications equipment and services, we compete with Furuno Electric Co., Ltd., Globalstar LP, Iridium Satellite LLC, Japan Radio Company, Nera ASA and Thrane & Thrane A/S.

We will serve as a distributor of the MSN TV service to the marine, automotive, and recreational vehicle markets and as such, plan to offer what we believe will be a unique mobile Internet solution. However, we anticipate that our TracNet 100 mobile Internet system with MSN TV service will compete with such products as single-user EVDO cards for use with individual laptops; EVDO/WiFi hubs such as those manufactured by Kyocera, Junxion, and Top Global; proposed WiMAX services in urban areas, and Internet-via-satellite systems proposed by companies such as RaySat.

Foreign competition for our mobile satellite communications products has continued to intensify, most notably from companies based in South Korea that seek to compete primarily on price. We anticipate that this trend will continue.

In the defense navigation, guidance and stabilization markets, we compete primarily with Honeywell International Inc., Kearfott Guidance & Navigation Corporation, Leica Microsystems AG, Northrop Grumman Corporation and Smiths Group plc. We believe the principal competitive factors in these markets are performance, accuracy, features, reliability, durability and price.

Research and Development

Focused investments in research and development are critical to our future growth and competitive position in the marketplace. Our research and development efforts are directly related to timely development of new and enhanced products that are central to our core business strategy. The industries in which we compete are subject to rapid technological developments, evolving industry standards, changes in customer requirements, and new product introductions and enhancements. As a result, our success depends in part upon our ability, on a cost-effective and timely basis, to continue to enhance our existing products and to develop and introduce new products that improve performance and meet customers' operational and cost requirements. Our current research and development efforts include projects to achieve additional cost reductions in our products and the development of new products for our existing marine and land mobile communications markets, and navigation, guidance and stabilization application markets. We also plan to make future investments to pursue the integration of satellite communications technology with our existing TACNAV systems to enable them to send and receive navigation data directly to and from digital battlefield management or similar systems.

Our research and development activities consist of projects funded by us, projects funded with the assistance of Small Business Innovative Research (SBIR) grants, and customer-funded contract research. SBIR projects are generally directed towards the discovery of specific information requested by the government research sponsor. Many of these grants have enhanced our technologies, resulting in new or improved product offerings. Our customer-funded research efforts are made up of contracts with defense and OEM customers, whose performance specifications are unique to their product applications. Defense and OEM research often results in new product offerings. We strive to be the first company to bring a new product to market, and we use our own funds to accelerate new product development efforts.

Government Regulation

Our manufacturing operations are subject to various laws governing the protection of the environment and our employees. These laws and regulations are subject to change, and any such change may require us to improve our technologies, incur expenditures, or both, in order to comply with such laws and regulations.

We are subject to compliance with the U.S. Export Administration Regulations. Some of our products have military or strategic applications, and are on the Munitions List of the U.S. International Traffic in Arms Regulations. These products require an individual validated license to be exported to certain jurisdictions. The length of time involved in the licensing process varies and can result in delays of the shipping of the products. Sales of our products to either the U.S. government or its prime contractors are subject to the U.S. Federal Acquisition Regulations.

We are also subject to the laws and regulations of the various foreign jurisdictions in which we offer and sell our products, including those of the European Union.

Employees

On December 31, 2005, we employed 300 full-time employees. We also employ temporary or contract personnel, when necessary, to provide short-term and/or specialized support for production and other functional projects.

We believe our future success will depend upon the continued service of our key technical and senior management personnel and upon our continued ability to attract and retain highly qualified technical and managerial personnel. None of our employees is represented by a labor union. We have never experienced a work stoppage and consider our relationship with our employees to be good.

ITEM 1A. Risk Factors

An investment in our common stock involves a high degree of risk. You should carefully consider the following risk factors in evaluating our business. If any of these risks, or other risks not presently known to us or that we currently believe are not significant, develops into an actual event, then our business, financial condition and results of operations could be adversely affected. If that happens, the market price of our common stock could decline.

We may not be profitable in the future.

We have a history of variable profitability from operations. Although we generated net income during 2005, and in eight of the last twelve fiscal quarters, we incurred net losses of $6.1 million in 2004 and $1.5 million in 2003. As of December 31, 2005, we had an accumulated deficit of $14.5 million.

Shifts in our product sales mix toward our mobile satellite communications products may reduce our overall gross margins.

Our mobile communications products have historically had lower product gross margins than our defense products. During 2005, sales of our defense products grew at a substantially higher rate than our overall sales growth. However, during 2004, sales of our defense products declined compared to 2003. If the current shift in the product sales mix of satellite communications and defense products were to reverse, we could return to lower gross margins in the future.

The market for our mobile satellite TV products for minivans, SUVs and other passenger vehicles is still new and emerging, and our business may not grow as we expect.

We began shipping the TracVision A5 in September 2003. It was the first commercially available, low-profile mobile satellite TV antenna practical for use on minivans, SUVs and other passenger vehicles. Accordingly, the market for this product remains new and emerging. Consumers may not respond favorably to live satellite TV in passenger vehicles, and the market may not accept the TracVision A5 in a widespread manner. The relatively early stages of development of this market continues to make it difficult for us to predict customer demand accurately. For example, although sales of the TracVision A5 have grown between 2004 and 2005, the sales trend is below our original expectations. We have previously experienced temporary issues related to our production process and availability of adequate component supply. Although we believe we have successfully addressed the issues that have arisen, similar issues or other latent defects in the TracVision A5 could adversely affect sales.

We believe the success of the TracVision A5 will depend upon consumers' assessment of whether or not it meets their expectations for performance, quality, price and design. For example, the TracVision A5 is designed for use on open roads in the continental United States where there is a clear view of the transmitting satellite in the southern sky. Among the factors that could affect the success of the TracVision A5 are:

- the extent to which TracVision A5 gains the acceptance of the automotive OEMs;
- the performance, price and availability of competing or alternative products relative to the TracVision A5;
- the extent to which customers perceive mobile satellite TV services as a luxury or a preferred convenience;
- difficulties or inconveniences associated with scheduling installation at the point of sale;
- our limited experience with marketing a product to the automotive market, which is substantially larger and more fragmented than our other markets;
- the extent to which customers prefer live TV over recorded media;
- customers' willingness to pay monthly fees for satellite television service in automobiles;
- the adoption of laws or regulations that restrict or ban live television or other video technology in vehicles;
- poor performance arising from improper installation or installation of damaged equipment; and
- the extent to which increasing fuel prices may negatively affect consumer demand for SUVs and other large passenger vehicles.

Our effort to enter the OEM market for embedded mobile satellite TV products may not be successful.

During 2005, we announced that we intend to support factory installation of an embedded version of our TracVision A5 mobile satellite TV antenna for automobiles. However, the timetable for potential OEM acceptance of the embedded system is uncertain, and our efforts to enter this market may not be successful. In particular, there is a wide range of vehicle roof designs, environmental requirements and performance standards that our new product will have to address, and we may encounter unanticipated difficulties in designing antennas that will satisfy all of the unique requirements of various vehicle configurations. In addition, our success in entering this market will depend in part on the close cooperation of vehicle manufacturers, and we cannot be certain that we will obtain the necessary cooperation. Because different vehicles may require different designs, our manufacturing efficiency for these embedded antennas may be lower and we may generate lower margins than for the TracVision A5. The expenses we expect to incur in pursuing this market may have an adverse effect on our results of operations.

We expect that others will introduce competing mobile satellite TV antennas for automobiles.

When we began shipping our TracVision A5 in September 2003, it was the only commercially available, low-profile mobile satellite TV antenna for use on minivans, SUVs and other passenger vehicles. Any advantage we may have had by being the first to market such a product may erode as others enter this market. For example, RaySat made an initial, limited shipment of a phased-array satellite antenna for automobiles late in 2005. When or if it enters full production, it is expected to be sold exclusively though Audiovox as an Audiovox-branded product. Winegard has also previously announced its intention to offer an in-motion automotive satellite TV antenna. In addition, SIRIUS Satellite Radio announced in January 2005 that it intends to introduce in 2006 a service offering several streaming video channels through SIRIUS' existing satellite radio system. In January 2005, Delphi Corp., a prominent supplier of automotive parts, announced a new agreement with Comcast Corporation to work together to develop ways to allow users to select video content and transfer it to an in-vehicle entertainment system. No details were provided as to the time frame for a possible product. Competing satellite antenna products may have a slightly lower profile and customers may delay purchasing the TracVision A5 in anticipation of the release of any of these products. Competition from any of these products could impair our ability to sell the TracVision A5 and may force us to reduce the price of the TracVision A5. Moreover, Delphi's long-term relationships with automobile manufacturers may give it a significant advantage in selling mobile satellite TV antennas to those manufacturers.

We must achieve additional significant cost reductions for the TracVision A5 to reach our targeted profit margins.

Our product profit margins for the TracVision A5 have been low since its introduction. To reach our targeted profit margins, we must continue to significantly reduce our manufacturing costs for the TracVision A5. Although we have had success in improving profit margins since the introduction of the TracVision A5 in September 2003, we may be unable to achieve the additional cost reductions necessary to achieve our overall target profit margins. Although we have cost reduction programs in place that include obtaining volume purchasing discounts and redesigning certain components using lower cost materials and processes, technological or other challenges may prevent us from achieving all of the necessary cost reductions. Moreover, if the price of the TracVision A5 is not attractive to a broad range of customers, we may be forced to further lower the price, which would further impair our product profit margins unless we are able to achieve corresponding cost reductions.

High fuel prices may adversely affect sales of our mobile satellite communications products.

Fuel prices have been high and may remain high or increase in the foreseeable future. High fuel prices tend to have a disproportionate impact on the larger vehicles and vessels for which our mobile satellite communications products are designed, such as marine vessels, recreational vehicles and SUVs, because they consume relatively large quantities of fuel. The increased cost of operating these vehicles and vessels is adversely affecting and may continue to adversely affect demand for our mobile satellite communications products.

The market for mobile Internet services in vehicles and vessels may fail to develop or may be satisfied by alternative technological approaches.

Mobile Internet access is a relatively new market that is currently focused primarily on cell phones and Internet-enabled PDAs. We will serve as a distributor of the MSN TV service to the marine, automotive, and RV markets and as such, plan to offer what we believe will be a unique mobile Internet solution. However, competing products based around high-speed cellular services are available for single users and in integrated EVDO/WiFi hubs. Other technological developments, such as proposed WiMAX networks and Internet-via-satellite services may also displace wireless services with regard to range and cost, preventing us from successfully marketing and selling mobile Internet systems in the mobile marketplace.

Customers for TACNAV and our other defense products include the U.S. military and foreign governments, whose purchasing schedules and priorities can be unpredictable.

We sell TACNAV and our other defense products to the U.S. military and foreign military and government customers. These customers have unique purchasing requirements, which can make sales to these customers unpredictable. Factors that affect their purchasing decisions include:

- priorities for current battlefield operations;
- changes in modernization plans for military equipment;
- changes in tactical navigation requirements;
- allocation of funding for military programs;
- new military and operational doctrines that affect military equipment needs;
- sales cycles that are long and difficult to predict;
- shifting response time and / or delays in the approval process associated with the export licenses we must obtain prior to the international shipment of certain of our military products;
- delays in military procurement schedules; and
- delays in the testing and acceptance of our products.

These factors can cause substantial fluctuations in sales of TACNAV and our other defense products from period to period. Moreover, TACNAV and most of our other defense products must meet military quality standards, and our products may not continue to meet existing standards or more rigorous standards adopted in the future. Any failure to meet military contract specifications may produce delays as we attempt to improve our design, development, manufacturing or quality control processes. Furthermore, government customers and their contractors can generally cancel orders for our products for convenience or decline to exercise previously disclosed contract options. Even under firm orders with government customers, funding must usually be appropriated in the budget process in order for the government to complete the contract. The cancellation of or failure to fund orders for our products could substantially reduce our net sales and results of operations.

Only a few customers account for a substantial portion of our defense revenues, and the loss of any of these customers could substantially reduce our net sales.

We derive a significant portion of our defense revenues from a small number of customers, including the U.S. Government. The loss of business from any of these customers could substantially reduce our net sales and results of operations and could seriously harm our business.

Sales of TACNAV and our other defense products generally consist of a few large orders, and the delay or cancellation of a single order could substantially reduce our net sales.

Unlike our mobile satellite communications products, TACNAV and our other defense products are purchased through orders that can generally range in size from several hundred thousand dollars to more than one million dollars. As a result, the delay or cancellation of a single order could materially reduce our net sales and results of operations. Because our defense products typically have higher direct margins than our mobile satellite communications products, the loss of an order for defense products could have a disproportionately adverse effect on our results of operations.

We may fail to continue to increase the sale of our fiber optic products for commercial uses.

Our fiber optic products have numerous commercial applications where mobile communication, navigation, stabilization and precision pointing are required. For example, our fiber optic gyros have been used in commercial applications such as train location control and track geometry measurement systems, industrial robotics, and autonomous or remotely operated vehicles. We may not be successful in further developing and marketing our fiber optic products for commercial uses, which might limit the overall net sales of these products and limit our profitability accordingly.

We depend on others to provide programming for our TracVision products, Internet access for our TracNet products, and telephone, fax and data services for our TracPhone products.

Our TracVision products include only the equipment necessary to receive satellite television services; we do not broadcast satellite television programming. Instead, customers must obtain programming from another source. We currently offer marine and land mobile TracVision products compatible with the DIRECTV and DISH Network services in the continental United States, the ExpressVu service in Canada and various other regional services in other parts of the world. Our TracVision A5 currently offers access to only the DIRECTV service in the continental United States. Although DIRECTV is offering its TOTAL CHOICE MOBILE programming package at a price that we think should be attractive to consumers, DIRECTV has no obligation to continue to offer that package at the current price or at all. If customers become dissatisfied with the programming, pricing, service, availability or other aspects of this satellite television services product or if any one or more of these services becomes unavailable for any reason, we could suffer a substantial decline in sales of our TracVision products. The companies that operate these services have no obligation to inform us of technological or other changes, including discontinuation of the service, which could impair the performance of our TracVision products.

Our TracPhone and TracNet 3.0 products currently depend on satellite services provided by third parties. We rely on Inmarsat for satellite communications services for our TracPhone products. We rely on Telemar for TracNet 3.0 service in Europe.

Our TracNet 100 mobile Internet system will use high-speed EVDO cellular services offered by providers such as Verizon Wireless as well as Microsoft's MSN TV service. Should EVDO networks become unavailable, our TracNet 100 would be hampered in its ability to provide two-way Internet access. Likewise, if the status of MSN TV were to change, customers would no longer be able to access the Internet via the TV screens in their boats, RVs, and cars, a feature that offers KVH a competitive advantage over other mobile Internet solutions.

If any of our vendors were unable to fulfill their obligations, we would need to seek alternate suppliers or solutions. In that case, we may be required to retrofit or upgrade hardware and software as necessary to ensure the continued operation of the affected products. We may incur significant delays and expenses in our efforts to make the necessary changes and those efforts may be unsuccessful. Moreover, we may not be successful in identifying and entering into appropriate agreements with replacement suppliers on commercially reasonable terms, which would impair our ability to offer the affected products. Similarly, we may lose the goodwill of existing customers if any currently installed products cease to work for any extended period. Any such outcome could lead to a substantial reduction in sales.

Our mobile satellite communications products depend on the availability of third-party satellites, which face significant operational risks and could fail earlier than their expected useful lives.

Our mobile satellite communications products depend on the availability of programming and services broadcast through satellites owned by third parties. The unexpected failure of a satellite could disrupt the availability of programming and services, which could reduce the demand for, or customer satisfaction with, our products. These satellites face significant operational risks while in orbit. These risks include malfunctions that can occur as a result of satellite manufacturing errors, problems with power or control systems and general failures resulting from the harsh space environment. Moreover, each satellite has a limited useful life, and the satellite providers make no guarantees that the planned backup systems and capacity will be sufficient to support these satellite services in the event of a loss or reduction of service. We cannot assure that satellite services compatible with our products will continue to be available or that such services will continue to be offered at reasonable rates. The accuracy or availability of satellite signals may also be limited by ionospheric or other atmospheric conditions, intentional or inadvertent signal interference, or intentional limitations on signal availability imposed by the satellite provider. A reduction in the number of operating satellites on any system, the inoperability of any key satellite or the failure of any key satellite or satellites to provide an accurate or available signal could impair the utility of our products or the growth of current and additional market opportunities.

We depend on single manufacturing lines for our products, and any significant disruption in production could impair our ability to deliver our products.

We currently manufacture and assemble our products using individual production lines for each product category. We have experienced manufacturing difficulties in the past, and any significant disruption to one of these production lines will require time either to reconfigure and equip an alternative production line or to restore the original line to full capacity. Some of our production processes are complex, and we may be unable to respond rapidly to the loss of the use of any production line. For example, our production process uses some specialized equipment and custom molds that may take time to replace if they malfunction. In that event, shipments would be delayed, which could result in customer or dealer dissatisfaction, loss of sales and damage to our reputation. Finally, we have only a limited capability to increase our manufacturing capacity in the short term. If short-term demand for our products exceeds our manufacturing capacity, our inability to fulfill orders in a timely manner could also lead to customer or dealer dissatisfaction, loss of sales and damage to our reputation.

We depend on sole or limited source suppliers, and any disruption in supply could impair our ability to deliver our products on time or at expected cost.

We obtain many key components for our products from third-party suppliers, and in some cases we use a single or a limited number of suppliers. Any interruption in supply could impair our ability to deliver our products until we identify and qualify a new source of supply, which could take several weeks, months or longer and could increase our costs significantly. In general, we do not have written long-term supply agreements with our suppliers but instead purchase components through purchase orders, which expose us to potential price increases and termination of supply without notice or recourse. We do not generally carry significant inventories of product components, and this could magnify the impact of the loss of a supplier. If we are required to use a new source of materials or components, it could also result in unexpected manufacturing difficulties and could affect product performance and reliability.

We may increase the international scope of our operations, which could disrupt our operations.

Although we have historically manufactured all of our products in the U.S., in order for us to improve our operating margin performance and overall profitability, we may find it necessary to increase the international scope of our operations. This could include offshore manufacturing and/or the increased sourcing of raw materials from foreign countries. We have only limited experience in foreign manufacturing and we might not be successful in implementing or integrating an extended program. In addition, an increased reliance on foreign manufacturing and/or raw material supply would lengthen our supply chain and increase the risk that a disruption in that supply chain would have a material adverse affect on our operations and financial performance.

Any failure to maintain and expand our third-party distribution relationships may limit our ability to penetrate markets for mobile satellite communications products.

We market and sell our mobile satellite communications products through an international network of independent retailers, chain stores and distributors, as well as to manufacturers of marine vessels and recreational vehicles. If we are unable to maintain or increase the number of our distribution relationships, it could significantly reduce or limit our net sales. In addition, our distribution partners may sell products of other companies, including competing products, and are not required to purchase minimum quantities of our products. Moreover, our distributors may operate on low product margins and could give higher priority to products with higher margins than ours.

Our net sales and operating results could decline due to general economic trends or declines in consumer spending.

Our operating performance depends significantly on general economic conditions. Net sales of our satellite communications products are largely generated by discretionary consumer spending, and demand for these products could demonstrate slower growth than we anticipate as a result of regional and global economic conditions. Consumer spending tends to decline during recessionary periods and may decline at other times. Consumers may choose not to purchase our mobile satellite communications products due to a perception that they are luxury items. As global and regional economic conditions change, including the general level of interest rates, rising oil prices and demand for durable consumer products, demand for our products could be adversely affected.

If we are unable to improve our existing mobile satellite communications and defense products and develop new, innovative products, our sales and market share may decline.

The markets for mobile satellite communications products and defense navigation, guidance and stabilization products are each characterized by rapid technological change, frequent new product innovations, changes in customer requirements and expectations and evolving industry standards. If we fail to make innovations in our existing products and reduce the costs of our products, our market share may decline. Products using new technologies, or emerging industry standards, could render our products obsolete. If our competitors successfully introduce new or enhanced products that eliminate technological advantages our products may have in a certain market or otherwise outperform our products, or are perceived by consumers as doing so, we may be unable to compete successfully in the markets affected by these changes. For example, other companies have either announced their intentions or have begun to offer low-profile in-motion satellite antennas or alternative means for providing mobile entertainment. These products will compete with our TracVision A5 and may offer more attractive performance, pricing and other features.

If we cannot effectively manage our growth, our business may suffer.

We have previously expanded our operations to pursue existing and potential market opportunities. This growth placed a strain on our personnel, management, financial and other resources. If we fail to manage our future growth properly, we may incur unnecessary expenses and the efficiency of our operations may decline. To manage our growth effectively, we must, among other things:

- upgrade, expand or re-size our manufacturing facilities and capacity in a timely manner;
- successfully attract, train, motivate and manage a larger number of employees for manufacturing, sales and customer support activities;
- control higher inventory and working capital requirements; and
- improve the efficiencies within our operating, administrative, financial and accounting systems, and our procedures and controls.

We may be unable to hire and retain the skilled personnel we need to expand our operations.

To meet our growth objectives, we must attract and retain highly skilled technical, operational, managerial, and sales and marketing personnel. If we fail to attract and retain the necessary personnel, we may be unable to achieve our business objectives and may lose our competitive position, which could lead to a significant decline in net sales. We face significant competition for these skilled professionals from other companies, research and academic institutions, government entities and other organizations.

Our success depends on the services of our executive officers and key employees.

Our future success depends to a significant degree on the skills and efforts of Martin Kits van Heyningen, our co-founder, president and chief executive officer. If we lost the services of Mr. Kits van Heyningen, our business and operating results could be seriously harmed. We also depend on the ability of our other executive officers and members of senior management to work effectively as a team. None of our senior management or other key personnel is bound by an employment agreement. The loss of one or more of our executive officers or senior management members could impair our ability to manage our business effectively.

Competition may limit our ability to sell our mobile communications products and defense products.

The mobile satellite communications markets and defense navigation, guidance and stabilization markets in which we participate are very competitive, and we expect this competition to persist and intensify in the future. We may not be able to compete successfully against current and future competitors, which could impair our ability to sell our products. To remain competitive, we must enhance our existing products and develop new products, and we may have to reduce the prices of our products. Moreover, new competitors may emerge, and entire product lines may be threatened by new technologies or market trends that reduce the value of those product lines. For example, improvements in less expensive wireless and cellular technologies may limit demand for land-based satellite telephone and Internet services.

In the defense navigation, guidance and stabilization markets, we compete primarily with Honeywell International Inc., Kearfott Guidance & Navigation Corporation, Leica Microsystems AG, Northrop Grumman Corporation and Smiths Group PLC. In the market for mobile satellite communications products, we compete with a variety of companies. In the land mobile market for satellite TV communications equipment, we compete directly with King Controls, MotoSAT, TracStar Systems, Inc., and Winegard Company. There is also potential competition for sales of satellite TV to the automotive market from RaySat, Audiovox, Winegard, and Delphi. In the marine market for satellite TV communications equipment, we compete with NaviSystem Marine Electronic Systems Srl, Orbit Satellite Television & Radio Network, King Controls, TracStar, Sea Tel, Inc. and Raymarine. In the marine market for telephone, fax, data and Internet communications equipment, we compete with Furuno Electric Co., Ltd., Globalstar LP, Iridium Satellite LLC, Japan Radio Company, Nera ASA, and Thrane & Thrane A/S. In the mobile Internet market, we may compete with such products as single-user EVDO cards for use with individual laptops; EVDO/WiFi hubs such as those manufactured by Kyocera, Junxion, and Top Global; proposed WiMAX services in urban areas; and Internet-via-satellite systems proposed by companies such as RaySat. Moreover, new competitors may surface in the future. Among the factors that may affect our ability to compete in our markets are the following:

- many of our primary competitors are well-established companies that could have substantially greater financial, managerial, technical, marketing, personnel and other resources than we do;
- product improvements or price reductions by competitors may weaken customer acceptance of our products; and
- our competitors may have lower production costs than we do, which may enable them to compete more aggressively in offering discounts and other promotions.

Our international business operations expose us to a number of difficulties in coordinating our activities abroad and in dealing with multiple regulatory environments.

Historically, sales to customers outside the United States and Canada have accounted for a significant portion of our net sales. We have only one foreign sales office, which is located in Denmark, and we otherwise support our international sales from our operations in the United States. Our limited operations in foreign countries may impair our ability to compete successfully in international markets and to meet the service and support needs of our customers in countries where we have no infrastructure. We are subject to a number of risks associated with our international business activities, which may increase our costs and require significant management attention. These risks include:

- technical challenges we may face in adapting our mobile satellite communication products to function with different satellite services and technology in use in various regions around the world, including multiple satellite services in Europe;
- satisfaction of international regulatory requirements and procurement of any necessary licenses or permits;
- restrictions on the sale of certain defense products to foreign military and government customers;
- additional costs and delays associated with obtaining approvals and licenses under applicable export regulations;
- increased costs of providing customer support in multiple languages;
- more limited protection of our intellectual property;
- potentially adverse tax consequences, including restrictions on the repatriation of earnings;
- protectionist laws and business practices that favor local competitors, which could slow our growth in international markets;
- potentially longer sales cycles, which could slow our revenue growth from international sales;
- potentially longer accounts receivable payment cycles and difficulties in collecting accounts receivable;
- losses arising from foreign currency exchange rate fluctuations; and
- economic and political instability in some international markets.

If we are unable to maintain adequate product liability insurance, we may have to pay significant monetary damages in a successful product liability claim against us.

The development and sale of mobile satellite communication products and defense products entail an inherent risk of product liability. For example, consumers may ignore laws or warnings not to watch satellite television while driving and, as a result, may become involved in serious accidents, for which they may seek to hold us responsible. Product liability insurance is generally expensive for companies such as ours. Accordingly, we maintain only limited product liability insurance coverage for our products. Our current levels of insurance or any insurance we may subsequently obtain may not provide us with adequate coverage against potential claims, such as claims by those involved in accidents caused by drivers watching television. In addition, we may be unable to renew our policies on commercially reasonable terms or obtain additional product liability insurance on acceptable terms, if at all. If we are exposed to product liability claims for which we have insufficient insurance, we may be required to pay significant damages, which could seriously harm our financial condition and results of operations.

Exports of certain defense products are subject to the International Traffic in Arms Regulations and require a license from the U.S. Department of State prior to shipment.

We must comply with the United States Export Administration Regulations and the International Traffic in Arms Regulations, or ITAR. Our products that have military or strategic applications are on the munitions list of the ITAR and require an individual validated license in order to be exported to certain jurisdictions. Any changes in export regulations may further restrict the export of our products, and we may cease to be able to procure export licenses for our products under existing regulations. The length of time required by the licensing process can vary, potentially delaying the shipment of products and the recognition of the corresponding revenue. Any restriction on the export of a significant product line or a significant amount of our products could cause a significant reduction in net sales.

Our business may suffer if we cannot protect our proprietary technology.

Our ability to compete depends significantly upon our patents, our source code and our other proprietary technology. The steps we have taken to protect our technology may be inadequate to prevent others from using what we regard as our technology to compete with us. Our patents could be challenged, invalidated or circumvented, and the rights we have under our patents could provide no competitive advantages. Existing trade secrets, copyright and trademark laws offer only limited protection. In addition, the laws of some foreign countries do not protect our proprietary technology to the same extent as the laws of the United States, which could increase the likelihood of misappropriation. Furthermore, other companies could independently develop similar or superior technology without violating our intellectual property rights. Any misappropriation of our technology or the development of competing technology could seriously harm our competitive position, which could lead to a substantial reduction in net sales.

If we resort to legal proceedings to enforce our intellectual property rights, the proceedings could be burdensome, disruptive and expensive, distract the attention of management, and there can be no assurance that we would prevail.

Also, we have delivered certain technical data and information to the U.S. government under procurement contracts, and it may have unlimited rights to use that technical data and information. There can be no assurance that the U.S. government will not authorize others to use that data and information to compete with us.

Pending securities class action lawsuits could have a material adverse effect on our financial condition and results of operations.

We and certain of our officers are defendants in a class action lawsuit in the U. S. District Court for the District of Rhode Island. The suit asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder, as well as claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933, on behalf of purchasers of our securities between October 1, 2003 and July 2, 2004. We and certain of our directors and officers are also defendants in a shareholders' derivative action in the Rhode Island State Superior Court for Providence County. This suit asserts state law claims on our behalf between October 1, 2003 and the present arising from the allegations set forth in the class action complaint in the U.S. District Court described above. We and certain of our directors and officers are also defendants in a shareholders' derivative action in the U.S. District Court for the District of Rhode Island. This suit asserts federal and state claims on our behalf between October 1, 2003 and the present arising from the same allegations set forth in the class action complaint described above. We intend to vigorously defend ourselves against these claims. There can be no assurance, however, that we will not have to pay significant damages or amounts in settlement. An unfavorable outcome or prolonged litigation could materially harm our business. Litigation of this nature is expensive and time-consuming and diverts the time and attention of our management.

Claims by others that we infringe their intellectual property rights could harm our business and financial condition.

Our industries are characterized by the existence of a large number of patents and frequent claims and related litigation regarding patent and other intellectual property rights. We cannot be certain that our products do not and will not infringe issued patents, patents that may be issued in the future, or other intellectual property rights of others.

We do not generally conduct exhaustive patent searches to determine whether the technology used in our products infringes patents held by third parties. In addition, product development is inherently uncertain in a rapidly evolving technological environment in which there may be numerous patent applications pending, many of which are confidential when filed, with regard to similar technologies.

From time to time we have faced claims by third parties that our products or technology infringe their patents or other intellectual property rights, and we may face similar claims in the future. Any claim of infringement could cause us to incur substantial costs defending against the claim, even if the claim is invalid, and could distract the attention of our management. If any of our products are found to violate third-party proprietary rights, we may be required to pay substantial damages. In addition, we may be required to re-engineer our products or obtain licenses from third parties to continue to offer our products. Any efforts to re-engineer our products or obtain licenses on commercially reasonable terms may not be successful, which would prevent us from selling our products, and, in any case, could substantially increase our costs and have a material adverse effect on our business, financial condition and results of operations.

We are presently a defendant in two lawsuits brought by Electronic Controlled Systems, Inc., d/b/a King Controls, alleging infringement of three of its patents. We are defending ourselves vigorously against these claims, but there can be no assurances that we will not have to pay significant damages or amounts in settlement, that we will not be enjoined from selling certain of our mobile satellite communications products, or that the suit will not otherwise have a materially adverse effect on our operations or financial performance.

Fluctuations in our quarterly net sales and results of operations could depress the market price of our common stock.

We have experienced significant fluctuations in our net sales and results of operations from one quarter to the next. Our future net sales and results of operations could vary significantly from quarter to quarter due to a number of factors, many of which are outside our control. Accordingly, you should not rely on quarter-to-quarter comparisons of our results of operations as an indication of future performance. It is possible that our net sales or results of operations in a quarter will fall below the expectations of securities analysts or investors. If this occurs, the market price of our common stock could fall significantly. Our results of operations in any quarter can fluctuate for many reasons, including:

- demand changes for our mobile satellite communications products and defense products;
- the timing and size of individual orders from military customers;
- our ability to manufacture, test and deliver products in a timely and cost-effective manner;
- our success in winning competitions for orders;
- the timing of new product introductions by us or our competitors;
- the mix of products we sell;
- market and competitive pricing pressures;
- general economic climate; and
- seasonality of pleasure boat and recreational vehicle usage.

A large portion of our expenses, including expenses for facilities, equipment, and personnel, are relatively fixed. Accordingly, if our net sales decline or do not grow as much as we anticipate, we might be unable to maintain or improve our operating margins. Any failure to achieve anticipated net sales could therefore significantly harm our operating results for a particular fiscal period.

Our tax planning strategy involves assumptions that may cause our annual provision for tax expense or benefit to fluctuate materially. Moreover, our tax planning strategy is based upon our ability to sell our manufacturing and corporate headquarters facility located in Middletown, Rhode Island, as may be necessary.

We utilize a tax planning strategy as provided for under accounting principles generally accepted in the United States as a means of supporting the realizable nature of certain of our deferred tax assets. The strategy involves our ability to sell our Middletown, Rhode Island headquarters facility in order to generate taxable income for the sole purpose of utilizing certain of our capitalized tax loss carryforwards before they expire. The determination of taxable income, and therefore supportable deferred tax asset value, is based upon the difference between the property's estimated fair market value and our tax basis. Accordingly, the estimated net realizable value of our deferred tax asset is highly correlated to property values in and around the Middletown, Rhode Island area and therefore subject to changes in property value and or assumptions used in the valuation process. This fair market value subjectivity may cause us to record significant increases or decreases to our deferred tax assets during the year.

The strategy represents an action that we ordinarily would not take, but could take, if necessary, to realize an estimated $3.3 million in U.S. deferred tax assets or the equivalent of approximately $8.5 million in estimated taxable income as of December 31, 2005.

The market price of our common stock may be volatile.

Our stock price has historically been volatile. From January 1, 2004 to December 31, 2005, the trading price of our common stock ranged from $27.75 to $6.61. Many factors may cause the market price of our common stock to fluctuate, including:

- variations in our quarterly results of operations;
- the introduction of new products by us or our competitors;
- changing needs of military customers;
- changes in estimates of our performance or recommendations by securities analysts;
- the hiring or departure of key personnel;
- acquisitions or strategic alliances involving us or our competitors;
- changes in, or adoptions of, accounting principles;
- market conditions in our industries; and
- the global macroeconomic and geopolitical environment.

In addition, the stock market can experience extreme price and volume fluctuations. These fluctuations are often unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the market price of our common stock. When the market price of a company's stock drops significantly, stockholders often institute securities class action litigation against that company. We are now defending a securities class action lawsuit. This pending litigation has caused us to incur substantial costs and is diverting the time and attention of our management. These adverse consequences may continue until this action is finally resolved. Any similar litigation in the future could have similar consequences.

Acquisitions may disrupt our operations or adversely affect our results.

We evaluate strategic acquisition opportunities to acquire other businesses as they arise. The expenses we incur evaluating and pursuing acquisitions could have a material adverse effect on our results of operations. If we acquire a business, we may be unable to manage it profitably or successfully integrate its operations with our own. Moreover, we may be unable to realize the financial, operational, and other benefits we anticipate from any acquisition. Competition for acquisition opportunities could increase the price we pay for businesses we acquire and could reduce the number of potential acquisition targets. Further, acquisitions may involve a number of special financial and business risks, such as:

- charges related to any potential acquisition from which we may withdraw;
- diversion of our management's time, attention, and resources;
- loss of key acquired personnel;
- increased costs to improve or coordinate managerial, operational, financial, and administrative systems including compliance with the Sarbanes-Oxley Act of 2002;
- dilutive issuances of equity securities;
- the assumption of legal liabilities;
- amortization of acquired intangible assets; and
- potential write-offs related to the impairment of goodwill.

Our charter and by-laws and Delaware law may deter takeovers.

Our certificate of incorporation, by-laws and Delaware law contain provisions that could have an anti-takeover effect and discourage, delay or prevent a change in control or an acquisition that many stockholders may find attractive. These provisions may also discourage proxy contests and make it more difficult for our stockholders to take some corporate actions, including the election of directors. These provisions relate to:

- the ability of our board of directors to issue preferred stock, and determine its terms, without a stockholder vote;
- the classification of our board of directors, which effectively prevents stockholders from electing a majority of the directors at any one annual meeting of stockholders;
- the limitation that directors may be removed only for cause by the affirmative vote of the holders of two-thirds of our shares of capital stock entitled to vote;
- the prohibition against stockholder actions by written consent;
- the inability of stockholders to call a special meeting of stockholders; and
- advance notice requirements for stockholder proposals and director nominations.

ITEM 1B. Unresolved Staff Comments

None.

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ITEM 2. Properties

The following table provides information about our current facilities.

Location	Type	Principal Uses	Approximate Square Footage	Ownership	Lease Expiration
Middletown, Rhode Island	Office, plant and warehouse	Corporate headquarters, research and development, sales and service, manufacturing (mobile satellite communications products), marketing and administration	75,000	Purchased with mortgage loan	—
Middletown, Rhode Island	Warehouse	Warehousing (mobile satellite communications products)	39,000	Leased	March 2008
Tinley Park, Illinois	Plant and warehouse	Manufacturing, research and development (defense & fiber optic products)	23,000	Leased	April 2010
Kokkedal, Denmark	Office and warehouse	European headquarters, sales and service, marketing and administration	11,000	Leased	May 2014

We anticipate that any substantial increase in demand for our products would require us to expand our production capacity. Although we can expand production by adding additional shifts to our operations, we may need to identify and acquire or lease additional manufacturing facilities. We believe that suitable additional or substitute facilities will be available as required.

ITEM 3. Legal Proceedings

We are a defendant in a class action lawsuit in the U.S. District Court for the District of Rhode Island in which we and certain of our officers are named as defendants. The suit asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 under that statute, as well as claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933, on behalf of purchasers of our securities in the period October 1, 2003 and July 2, 2004 and seeks certain legal remedies, including compensatory damages. The Teamsters Affiliates Pension Plan has been appointed lead plaintiff. This matter consolidates into one action eight separate complaints filed between July 24, 2004 and September 15, 2004. On January 14, 2005, the defendants filed a motion to dismiss the consolidated complaint for failure to state a claim upon which relief can be granted. The court denied this motion in part and granted it in part. On October 14, 2005, we answered the consolidated complaint and denied liability and all allegations of wrongdoing. Subsequently, on December 13, 2005, plaintiffs filed a motion for class certification; that motion is pending.

On August 16, 2004, Hamid Mehrvar filed a shareholder’s derivative action in the Rhode Island State Superior Court for Newport County against us and certain of our officers and directors. The amended complaint asserts state law claims on our behalf arising between October 1, 2003 and the present in connection with the allegations set forth in the class action consolidated complaint in the U.S. District Court described above. On October 7, 2005, the court dismissed Mehrvar’s amended complaint without prejudice. By letter dated October 14, 2005, Mehrvar delivered a demand that we commence litigation for the same acts alleged in his complaint against the directors and senior officers who served during the period October 1, 2003 to the present. On March 1, 2006, Mehrvar filed a shareholder’s derivative action in the Rhode Island State Superior Court for Providence County against us and certain of our officers and directors. The amended complaint asserts state law claims on our behalf arising between October 1, 2003 and the present in connection with the allegations set forth in the class action consolidated complaint in the U.S. District Court described above and seeks certain legal and equitable remedies, including restitution from our directors and officers and corporate governance changes.

On June 20, 2005 Yemin Ji filed a shareholder’s derivative action in the U.S. District Court for the District of Rhode Island against us and certain of our officers and directors, asserting certain federal and state law claims on our behalf arising between October 6, 2003 and the present in connection with the same allegations set forth in the class action and Mehrvar complaints described above and seeks certain legal and equitable remedies, including restitution from our directors and officers and certain corporate governance changes. On August 23, 2005, we moved the Court to abstain from exercising jurisdiction and dismiss the action as duplicative of the Mehrvar case. The Court denied this motion. On January 5, 2006, we moved to dismiss the complaint on the same grounds on which the Rhode Island state court dismissed the derivative complaint in Mehrvar that was filed on August 16, 2004. The motion is pending.

In May 2005, Electronic Controlled Systems, Inc., d/b/a King Controls, filed a patent infringement suit against us in the U.S. District Court for the District of Minnesota. The three asserted patents relate generally to controlling a satellite dish to acquire a satellite signal. The complaint alleges that we willfully infringe the patents and seeks injunctive relief, enhanced damages and attorneys’ fees. KVH has denied the allegations and asserted counterclaims, including claims for false advertising. This litigation is in the discovery phase. In January 2006, Electronic Controlled Systems, Inc., d/b/a/ King Controls, filed a second patent infringement suit against us in the U.S. District Court for the District of Minnesota. The second suit concerns one of the same three patents asserted in the original suit filed in May 2005, alleges that we willfully infringe the patent and seeks both preliminary and permanent injunctive relief, enhanced damages and attorneys’ fees. We have denied the allegations and asserted counterclaims. A hearing on the plaintiff’s motion for a preliminary injunction is now scheduled for late May 2006.

Additionally, in the ordinary course of business, we are a party to inquiries, legal proceedings and claims including, from time to time, disagreements with vendors and customers.

ITEM 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of our stockholders during the fourth quarter of fiscal 2005.

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PART II

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

Market Information. Our common stock trades on the Nasdaq National Market under the symbol "KVHI" . The following table provides, for the periods indicated, the high and low sale prices for our common stock as reported on the Nasdaq National Market.

	High	Low
Year Ended December 31, 2004:		
First quarter	$27.75	$13.51
Second quarter	16.60	12.36
Third quarter	13.00	6.61
Fourth quarter	10.50	6.76
Year Ended December 31, 2005:		
First quarter	$13.23	$ 8.81
Second quarter	11.05	8.54
Third quarter	10.85	9.00
Fourth quarter	10.00	8.77

Stockholders. As of March 13, 2006, we had 129 holders of record of our common stock. This number does not include stockholders for whom shares were held in a nominee or "street" name.

Dividends. We have never declared or paid cash dividends on our capital stock, and we do not plan to pay any cash dividends in the foreseeable future. We currently intend to retain any future earnings to finance our operations and future growth. In addition, the terms of our bank line of credit place restrictions on our ability to pay cash dividends on our common stock.

ITEM 6. Selected Financial Data

We have derived the following selected financial data from our audited consolidated financial statements. You should read this data in conjunction with "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Item 8. Financial Statements and Supplementary Data."

	Year Ended December 31,				
	2005	2004	2003	2002	2001
	(in thousands, except per share data)				
Consolidated Statement of Operations Data:					
Net sales	$71,258	$62,303	$56,672	$47,694	$32,707
TracVision A5 revaluation charge	(100)	2,358	—	—	—
All other cost of sales	41,687	39,934	33,795	26,505	20,255
Total cost of sales	41,587	42,292	33,795	26,505	20,255
Gross profit	29,671	20,011	22,877	21,189	12,452
Operating expenses:					
Research and development	7,692	6,337	8,578	8,854	7,885
Sales and marketing	13,845	15,907	11,201	9,951	8,412
General and administrative	5,845	5,166	4,597	3,594	2,514
Income (loss) from operations	2,289	(7,399)	(1,499)	(1,210)	(6,359)
Other income (expense):					
Interest income (expense), net	1,269	471	(165)	(119)	140
Other (expense) income	(338)	35	(78)	(62)	(42)
Income (loss) before income taxes	3,220	(6,893)	(1,742)	(1,391)	(6,261)
Income tax expense (benefit)	289	(746)	(272)	86	—
Net income (loss)	$ 2,931	$ (6,147)	$ (1,470)	$ (1,477)	$ (6,261)
Per share information:					
Net income (loss) per common share—basic and diluted	$ 0.20	$ (0.44)	$ (0.13)	$ (0.13)	$ (0.61)
Number of shares used in per share calculation:					
Basic	14,571	14,109	11,403	11,040	10,217
Diluted	14,685	14,109	11,403	11,040	10,217

	December 31,				
	2005	2004	2003	2002	2001
	(in thousands)				
Consolidated Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$50,090	$45,728	$ 2,849	$ 7,239	$11,241
Working capital	61,613	58,650	16,514	17,971	18,700
Total assets	82,330	75,914	34,071	32,549	33,163
Long-term debt, excluding current portion	2,282	2,397	2,504	2,604	2,697
Total stockholders' equity	71,363	67,732	25,333	25,431	26,246

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the other financial information and consolidated financial statements and related notes appearing elsewhere in this annual report. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of a variety of factors, including those discussed under the heading "Item 1A. Risk Factors" and elsewhere in this annual report.

Overview

We develop, manufacture and market mobile communications products for the land and marine markets, and navigation, guidance and stabilization products for defense and commercial markets. Our mobile communications products enable customers to receive live digital television, telephone and Internet services in their automobiles, recreational vehicles and marine vessels while in motion via satellite and wireless services. We sell our mobile communications products through an extensive international network of independent retailers, chain stores, distributors, and automobile dealerships, as well as to manufacturers of marine vessels and recreational vehicles. Our defense products include tactical navigation systems that provide uninterrupted navigation and pointing information in a broad range of military vehicles, including tactical trucks (HMMWVs) and combat vehicles. We also offer precision fiber optic gyro-based systems that help stabilize platforms such as gun turrets and radar units, provide guidance for munitions and support a range of commercial and industrial applications. We sell our defense products directly to U.S. and allied governments and government contractors, as well as through an international network of authorized independent sales representatives.

We entered the market for mobile satellite antenna systems in 1993. Initially, we sold our antenna systems primarily to original equipment manufacturers. In 1995, we began to offer our mobile satellite communications products to customers under the KVH TracPhone brand. That year, we also introduced our first KVH-branded satellite TV antenna for the marine market, the TracVision. In 1999, we introduced a more compact antenna for use on recreational vehicles and motor coaches. In September 2003, we introduced the TracVision A5, which uses our low-profile satellite TV antenna technology and is our first product for the automotive market. In January 2006, we announced an agreement with Microsoft that establishes KVH as a distributor of MSN TV service to cars, boats, and RVs. We intend to offer a mobile Internet system using MSN TV for these platforms by mid-2006.

In 1979, we invented the first digital fluxgate compass for use in sailing vessels. Since then, we have further developed and refined this technology to produce reliable precision navigation systems in military environments. In 1997, we acquired fiber optic gyro technology from Andrew Corporation to complement and enhance our existing navigation and inertial measurement systems. Our fiber optic gyro product line consists of the DSP-3000 fiber optic gyro, the militarized DSP-4000 fiber optic gyro, and the TG-6000, our fiber optic gyro-based inertial measurement unit. These systems serve both military and commercial applications.

We generate revenue primarily from the sale of our mobile satellite communications and defense products. The following table provides, for the periods indicated, our net sales by product line category. Our legacy recreational navigation systems business, which includes digital marine compass systems and rangefinder products, has generated less than 5% of our revenue in each of the last three years. Rather than continue to report our legacy business separately, we have elected to allocate revenue from our legacy products between our mobile satellite communications products and defense products. The following table reflects this allocation for all fiscal years presented.

	Year Ended December 31,		
	2005	2004	2003
		(in thousands)	
Mobile satellite communications	$ 49,057	$ 48,500	$ 39,177
Defense	22,201	13,803	17,495
Net sales	$ 71,258	$ 62,303	$ 56,672

In addition to revenue from product sales, our mobile satellite communications revenue includes fees earned from product repairs, fees from satellite phone and Internet usage services, and certain DIRECTV account referral fees earned in conjunction with the sale of our products. We provide, for a fee, third-party satellite phone and Internet airtime to our TracPhone and Internet customers who choose to activate their subscriptions with us. Under current DIRECTV programs, we are eligible to receive a one-time new mobile account activation fee from DIRECTV for each customer who activates their DIRECTV service directly through us. Our defense revenue primarily includes product sales to both military and commercial markets and to a lesser extent, engineering services provided under development contracts. To date, revenues earned from product repairs, satellite phone and Internet usage services, DIRECTV activations and earnings under development contracts have not been a material portion of our revenue.

Our defense business is characterized by a small number of customers who place a small number of relatively large dollar value orders. In the years ended December 31, 2005, 2004 and 2003, our top four defense customers, including the U.S. military as a single customer, accounted for 53%, 48% and 71%, respectively, of our net sales attributable to defense products and 16%, 10% and 20%, respectively, of our total net sales for all products. Direct sales to the U.S. military accounted for 6%, 3% and 11% of our total net sales for the years ended December 31, 2005, 2004, and 2003, respectively. Orders for our defense products typically range in size from several hundred thousand dollars to over one million dollars. Accordingly, our quarterly net sales of defense products usually consist of only a few orders. Each order can have a significant impact on our net sales, and because our defense products generally have higher margins than our mobile satellite communications products, each order can have an impact on our net income that is disproportionately large relative to the revenue generated by the order. Moreover, customers of our defense products are predominantly governments and government contractors that typically must adhere to lengthy procurement processes, which make the timing of individual orders difficult to predict and often result in long sales cycles. Government customers and their contractors can generally cancel orders for our products for convenience.

We have historically derived a substantial portion of our revenue from sales to customers located outside the United States and Canada. The following table provides, for the periods indicated, sales to specified geographic regions:

	Year Ended December 31,		
	2005	2004	2003
		(in thousands)	
Originating from North American locations:			
United States and Canada	$ 57,837	$ 50,285	$ 47,221
Europe	2,918	2,166	3,140
Other	510	1,421	621
Total North America	61,265	53,872	50,982
Originating from European location:			
Europe	8,677	7,413	4,977
Other	1,316	1,018	713
Total Europe	9,993	8,431	5,690
Net sales	$ 71,258	$ 62,303	$ 56,672

See note 13 of notes to our consolidated financial statements for more information on our geographic segments.

Over the last two years we have introduced several new products that were the result of substantial investments that we made in advanced development during the 2001-2003 timeframe. As a result, in 2005 and 2004 we were able to bring the total research and development expenses, as a percentage of revenue, to a level that we believe was more appropriate and sustainable for the near term. We anticipate that this level of investment will allow us to satisfactorily maintain our efforts in the areas of identifying and evaluating new and innovative products based on our platform technologies, refining products for commercial introduction and improving manufacturing and development processes.

In addition to our internally funded research and development efforts, we also conduct research and development activities that are funded by our customers. These activities relate primarily to the customization of our defense products to meet specific customer requirements. In accordance with accounting principles generally accepted in the United States of America, we account for customer-funded research as revenue, and we account for the associated research costs as cost of goods sold. As a result, some of our expenditures for research and development activities are not included in the research and development expense that we calculate and present in our statement of operations. The following table presents our total annual research effort, representing the sum of research cost of goods sold and the operating expense of research and development as described in our statement of operations. Our management believes this information is useful because it provides a better understanding of our total expenditures on research and development activities.

	Year ended December 31,		
	2005	2004	2003
		(in thousands)	
Research and development expense presented on statement of operations	$ 7,692	$ 6,337	$ 8,578
Cost of customer-funded research and development included in cost of goods sold	1,418	1,240	937
Total expenditures on research and development activities	$ 9,110	$ 7,577	$ 9,515

As of December 31, 2005, we had approximately $50.1 million in cash, cash equivalents and marketable securities and an accumulated deficit of approximately $14.5 million.

Critical Accounting Policies

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosure at the date of our financial statements. Our significant accounting policies are summarized in note 1 to our consolidated financial statements. The significant accounting policies that we believe are the most critical in understanding and evaluating our reported financial results include the following:

Revenue Recognition

Revenue from Product Sales. Revenue from product sales is recognized when persuasive evidence of an arrangement exists, goods are shipped, title has passed and collectibility is reasonably assured. We establish reserves for potential sales returns and allowances, and evaluate, on a monthly basis, the adequacy of those reserves based upon historical experience and our expectations for future returns. Our standard sales terms require that:

- All sales are final;
- Terms are either Net 30 or Net 45;
- Shipments are tendered and shipped FOB (or as may be applicable, FCA, or EXW) KVH’s plant or warehouse; and
- Title and risk of loss or damage passes to the dealer or distributor at the point of shipment when delivery is made to the possession of the carrier.

Under certain limited conditions, KVH, at its sole discretion, provides for the return of goods. No product is accepted for return and no credit is allowed on any returned product unless KVH has granted and confirmed prior written permission by means of appropriate authorization.

See note 12 of notes to our consolidated financial statements for disclosures associated with our significant customers, including 10% customers.

Accounts Receivable

Our estimate for allowance for doubtful accounts related to trade receivables is primarily based on specific, historical criteria. We evaluate specific accounts where we have information that the customer may have an inability to meet its financial obligations. We make judgments, based on facts and circumstances, regarding the need to record a specific reserve for that customer against amounts owed to reduce the receivable to the amount that we expect to collect. We also provide for a general reserve based on an aging analysis of our accounts receivable. We evaluate these reserves on a monthly basis and adjust them as we receive additional information that impacts the amount reserved. If circumstances change, we could change our estimates of the recoverability of amounts owed to us by a material amount. For example, as of December 31, 2005, included in our allowance for doubtful accounts is a specific reserve in the amount of approximately $490,000 to reserve for all outstanding balances of a European distributor that entered into a voluntary liquidation proceeding under local law during 2004 and commenced formal bankruptcy proceedings under local law during June 2005. At the time this reserve was established (fourth quarter of 2004), our allowance for doubtful accounts substantially increased and our net accounts receivable were reduced accordingly.

Inventories

Inventory is valued at the lower of cost or market. We regularly review current quantities on hand, actual and projected sales volumes and anticipated selling prices on products and write down slow-moving and/or obsolete inventory to its net realizable value. Generally, our inventory does not become obsolete because the materials we use are typically interchangeable among various product offerings. If we overestimate projected sales or anticipated selling prices, our inventory might be overvalued, and we would have to reduce our inventory valuation accordingly.

See note 4 of notes to our consolidated financial statements for disclosures associated with our TracVision A5 inventory revaluation and other special charges.

Income Taxes and Deferred Income Tax Assets and Liabilities

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carry forwards. On a quarterly basis, we assess the recoverability of our deferred tax assets by considering whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Based on the history of operating losses in our ongoing business, we determined that it was more likely than not that portions of the deferred tax assets were not recoverable and therefore a valuation allowance was established. We determined that the remaining deferred tax assets were recoverable based on a tax planning strategy derived from our ability to sell our headquarters property located in Middletown, Rhode Island for the express purpose of generating taxable income to utilize certain operating loss carryforwards before they expire. This tax strategy is not an action that we ordinarily would take but would take, if necessary, to realize tax benefits prior to expiration. The amount of the deferred tax assets considered realizable could change in the future if there are changes in the feasibility of our tax planning strategy or a movement in the estimated unrealized gains associated with our Middletown property. For example, as a result of a revaluation of the property in 2004, the estimated net unrealized taxable gains associated with the land and building increased from approximately $6.9 million to $8.9 million, thereby generating a $775,000 release of deferred tax asset valuation allowance in 2004. In addition to our tax planning strategy, some portion or all of the previously reserved deferred tax assets could be realized in the future if we generate future earnings during the periods in which those temporary differences become deductible.

Results of Operations

The following table provides, for the periods indicated, certain financial data expressed as a percentage of net sales:

	Year Ended December 31,		
	2005	2004	2003
Net sales	100.0%	100.0%	100.0%
TracVision A5 revaluation charge	(0.1)	3.8	—
All other costs of sales	58.5	64.1	59.6
Total costs of sales	58.4	67.9	59.6
Gross profit	41.6	32.1	40.4
Operating expenses:			
Research and development	10.8	10.2	15.1
Sales and marketing	19.4	25.5	19.8
General and administrative	8.2	8.3	8.1
Income (loss) from operations	3.2	(11.9)	(2.6)
Other income (expense), net	1.3	0.8	(0.5)
Income (loss) before income taxes	4.5	(11.1)	(3.1)
Income tax expense (benefit)	0.4	(1.2)	(0.5)
Net income (loss)	4.1%	(9.9)%	(2.6)%

Years ended December 31, 2005 and 2004

Operating Summary

Net income for the year ended December 31, 2005 was $2.9 million, or $0.20 per basic and diluted common share, as compared to a net loss of $6.1 million, or $(0.44) per basic and diluted common share, for the year ended December 31, 2004.

Our 2005 results reflect a 14% increase in net sales over 2004 as well as an improvement in our gross margin to 42% in 2005 as compared to 32% in 2004. The primary driver behind the increase in net sales and related margin was an increase in sales related to our higher margin defense products of approximately $8.4 million year over year and the absence of the TracVision A5 revaluation charge in 2005. Operating expenses for the year ended December 31, 2005 were $27.4 million, essentially flat with those from the prior year.

Net Sales

Net sales for 2005 increased $9.0 million, or 14%, to $71.3 million from $62.3 million in 2004. Sales of our defense-related products were the primary reason for the improvement as they increased $8.4 million, or 61%, to $22.2 million in 2005. The increase in sales of defense products was primarily attributable to significant unit volume increases related to both our military navigation products and our fiber optic gyro products. We expect that net sales of our defense-related products will grow more slowly in 2006 than in 2005.

Net sales of our mobile satellite communications products increased $0.6 million, or 1%, to $49.1 million in 2005. The slight increase in net sales was primarily attributable to a 17% increase in net sales of marine satellite communications products, largely offset by a 13% decrease in net sales of land mobile satellite communications products. The decrease in net sales of our land mobile satellite communications products resulted from a significant unit volume decrease in sales of our recreational vehicle (RV) products to OEMs and in the aftermarket. We expect that net sales of our land mobile communications products for the RV market could continue to decline in 2006.

Costs of Sales

Our costs of sales consist of direct labor, materials and manufacturing overhead used to produce our products as well as engineering costs related to customer funded research and development. Our total costs of sales for 2005 decreased by $0.7 million, or 2%, to $41.6 million from $42.3 million in 2004. Our total costs of sales in 2004 included the TracVision A5 revaluation charge of $2.4 million, which was not repeated in 2005. All other costs of sales increased by $1.8 million, or 4.4%, to $41.7 million from $39.9 million in 2004. Although all other costs of sales increased from 2004 to 2005, it increased at a lower rate than the increase in our net sales. This was due to the mix of product sales and our ability to reduce certain product costs and overhead spending in 2005.

Gross margin in 2005 increased to 42% from 32% in 2004. The primary reason for the increase in margin was due to the overall increase in net sales of our higher margin defense products on a year over year basis, coupled with a 5.0 point gross margin improvement generated through the sale of our mobile communications products, substantially all of which resulted from the incurrence of the TracVision A5 revaluation charge recorded in 2004. We do not expect that our gross margin will increase to the same extent in 2006.

Operating Expenses

Research and development expense consists of direct labor, materials and other costs that support our internally funded product development activities. All research and development costs are expensed as incurred. Research and development expense in 2005 increased by $1.4 million, or 21%, to $7.7 million from $6.3 million in 2004. As a percentage of net sales, research and development expense remained fairly consistent on a year-over-year basis, increasing modestly in 2005 to 10.8% from 10.2% in 2004. The aggregate increase in 2005 reflects increases in consulting services and engineering staff, primarily to support the development of product enhancements, new technologies and new product offerings in both our mobile communications and defense product portfolios. Except for the effects of expensing stock options, which will begin in 2006, and assuming our revenue remains stable or increases, we anticipate future research and development expense as a percentage of revenue to remain at or near current levels.

Sales and marketing expense consists primarily of salaries and related expenses for sales and marketing personnel, sales commissions for in-house and third-party representatives, warranty expense, bad debt expense and other costs that support the sales function such as advertising, literature and promotional materials. Sales and marketing expense in 2005 decreased by $2.1 million, or 13%, to $13.8 million from $15.9 million in 2004. As a percentage of net sales, sales and marketing expense decreased in 2005 to 19.4% from 25.5% in 2004. The primary reasons for the decrease in sales and marketing expense in 2005 were an initiative to refine and focus our sales and marketing programs coupled with a reduction in bad debt expense. Specifically, in 2005 we reduced the national and direct marketing promotions associated with our TracVision A5 and other land mobile communications products. In addition, we also curtailed expenses associated with large accounts and trade show promotions within the marine and land mobile markets. To a lesser extent, reduced bad debt expense of approximately $0.6 million in 2005 primarily related to a large European distributor also contributed to the overall decrease in sales and marketing expense. Except for the effects of expensing stock options, which will begin in 2006, and assuming our revenue remains stable or increases, we anticipate sales and marketing expense as a percentage of revenue to remain stable or even decline modestly.

General and administrative expense consists of costs attributable to management, finance and accounting, information technology, human resources and certain outside professional services. General and administrative expense in 2005 increased by $0.7 million, or 13%, to $5.8 million from $5.2 million in 2004. As a percentage of net sales, general and administrative expense remained fairly consistent on a year-over-year basis decreasing slightly in 2005 to 8.2% from 8.3% in 2004. The primary reason for the increase in general and administrative expense in 2005 is the increase in personnel costs associated with supporting our infrastructure and compliance requirements. Except for the effects of expensing stock options, which will begin in 2006, and the costs associated with pending litigation, and assuming our revenue remains stable or increases, we anticipate future core general and administrative expense, as a percentage of revenue, to remain stable or even decline modestly.

Interest and Other Income, Net

Interest and other income, net increased by $0.4 million to $0.9 million in 2005 from $0.5 million in 2004. The primary reason for the increase is an increase in interest income of approximately $0.8 million, partially offset by an increase in loss on foreign currency of $0.4 million. The increase in interest income is a result of increased returns on our investments consisting primarily of fixed income securities coupled with an overall higher average cash and investments balance in 2005 from 2004.

Income Tax Expense

In 2005 we recorded an income tax provision of approximately $0.3 million. The primary components of the provision were comprised of current US federal income tax expense of approximately $0.1 million, deferred U.S. income tax expense of approximately $0.1 million and approximately $0.1 million in foreign income tax expense as a result of income generated from our wholly owned subsidiary in Denmark.

During 2004, we recorded a foreign income tax expense of approximately $30,000 as a result of profitability in our foreign subsidiary. Moreover, during 2004 we recorded an approximate $0.8 million release of deferred tax asset valuation allowance (tax benefit) as a result of a revaluation of the net realizable deferred tax assets in connection with our tax planning strategy.

Years ended December 31, 2004 and 2003

Operating Summary

Net loss for the year ended December 31, 2004, was $6.1 million, or ($0.44) per basic and diluted common share, and was significantly greater than the net loss of $1.5 million, or ($0.13) per basic and diluted common share, in the year ended December 31, 2003. Our results reflected a 9.9% increase in sales over 2003, offset primarily by:

- a $2.4 million, or 3.8 percentage points of revenue, second-quarter TracVision A5 lower of cost or market inventory and non-cancelable future purchase commitment revaluation adjustment; and
- a 4.5 percentage points of revenue decline in gross margin, excluding the TracVision A5 revaluation adjustment, primarily resulting from a shift in product sales mix away from our higher margin defense products and towards our relatively lower-margin mobile satellite communication products.

Total operating expenses increased by $3.0 million or 12.4%, from $24.4 million in 2003 to $27.4 million in 2004 due mostly to increased new product sales and marketing expenses, especially those related to the launch of the TracVision A5, and, to a lesser extent, general and administrative professional fees. As a percentage of sales, total operating expenses increased slightly from 43.0% in 2003 to 44.0% in 2004, primarily as a result of increased sales and marketing expenses related to our new products.

Net Sales

Net sales for 2004 increased by $5.6 million, or 9.9%, to $62.3 million from $56.7 million in 2003. Sales of our mobile satellite communications products, which included our TracVision A5, continued to show strong growth, increasing 24% to $48.5 million in 2004 from $39.2 million in 2003 (including certain legacy products). This increase was primarily attributable to unit volume increases in our marine and land mobile satellite communications products, both in the U.S. and in Europe. Sales results reflected our expansion within the mobile satellite communication markets, our introduction of new products, including the TracVision A5 for the automotive market and the TracVision G8 for the marine market, and increased sales to major distributors, large account retailers and marine and recreational vehicle original equipment manufacturers.

Sales of our defense products decreased by $3.7 million, or 21%, to $13.8 million in 2004 from $17.5 million in 2003 (including certain legacy products). A decline in sales of our TACNAV tactical navigation systems represented the entire decline in defense sales, and was attributable to a shift in U.S. government procurement priorities. Partially offsetting the decline of TACNAV product sales within the defense markets was an $0.8 million increase in sales of our fiber optic gyro products and a $0.5 million increase in contracted engineering and product modification services. The increase in our fiber optic gyro sales was primarily the result of new product offerings, including the DSP-4000 and the DSP-3000 fiber optic gyros and the TG-6000, our fiber optic gyro-based inertial measurement unit.

Cost of Sales

Costs of sales for 2004 increased by $8.5 million, or 25.1%, to $42.3 million from $33.8 million in 2003. The resulting gross margin percentage decreased to 32.1% in 2004 from 40.4% in 2003. Increases in the costs of sales for 2004 from 2003 primarily resulted from:

- a $2.4 million TracVision A5 lower of cost or market inventory and non-cancelable future purchase commitment revaluation adjustment (approximately 3.8 gross margin points);
- a continued shift in the mix of product sales, away from our relatively higher-margin defense products to our relatively lower-margin mobile satellite communication products, including the TracVision A5 (approximately 2.8 gross margin points); and
- higher manufacturing support and overhead costs, primarily resulting from facility and systems infrastructure additions to support sales growth, and in part from increased warranty costs for new products (approximately 1.7 gross margin points).

The $2.4 million charge described above resulted from our decision to lower the price of the TracVision A5 in June 2004. As the price reduction produced a lower of cost or market condition, we revalued certain TracVision A5 on-hand inventory and future purchase commitments to the anticipated lower product costs of redesigned components. Consequently, since the June 2004 revaluation, the TracVision A5 product cost has reflected this lower cost structure. As we fulfill the future purchase commitments, we charge to costs of sales the portion of the cost attributable to our current, lower component costs, and we charge the excess against the accrued loss on TracVision A5 non-cancelable future purchase commitments. Once we have fully consumed the on-hand inventory and purchase commitments for the original components we will phase-in the redesigned low cost components. We anticipate that the actual new component phase-in process will begin during the first quarter of 2005. At present, we do not anticipate further lower of cost or market or non-cancelable future purchase revaluation charges arising from the June 2004 price reduction decision. Although the go-forward production costs for the TracVision A5 were reduced, the gross margin for the TracVision A5 remains considerably below the gross margins of all our other products. As a consequence, the growth in the sales of the TracVision A5 as a percentage of our total sales has adversely affected our overall gross margin results.

Operating Expenses

Total research and development expense decreased by $2.2 million, or 26.1%, to $6.3 million in 2004 from $8.6 million in 2003. As a percentage of net sales, research and development expense decreased to 10.2% in 2004 from 15.1% in 2003. The decrease reflects a reduction of engineering investment following the introduction of several major new products, including the TracVision A5 and the TracVision G8, as well as the DSP-4000 and DSP-3000 fiber optic gyros, and the TG-6000 inertial measurement unit (IMU).

Sales and marketing expense increased by $4.7 million, or 42.0%, to $15.9 million in 2004 from $11.2 million in 2003. As a percentage of net sales, sales and marketing expense increased to 25.5% in 2004 from 19.8% in 2003. This increase was primarily a result of promotional and marketing activities directed at enhancing the market awareness of the TracVision A5 and other land mobile satellite communication products. Additional increases resulted from expanded recreational vehicle and marine OEM, large account and trade show promotions, customer support programs and increased product sales commissions that scale with sales volume. To a lesser extent, an increase in bad debt expense of $0.7 million, of which approximately $0.6 million was associated with a single European distributor, also contributed to the total increase.

General and administrative expenses increased by $0.6 million, or 12.4%, to $5.2 million in 2004 from $4.6 million in 2003. As a percentage of net sales, general and administrative expenses increased to 8.3% in 2004 from 8.1% in 2003. Legal and accounting compliance expenses accounted for the majority of our cost increases. To a lesser extent, salary and salary-related costs also contributed to this increase.

Interest and Other Income

Interest and other income (expense) increased by $0.7 million to $0.5 million in 2004 from ($0.2) million in 2003. The majority, or $0.6 million, was the result of higher interest income earned on the investment of approximately $48.0 million received from our common stock public offering in February 2004. Also adding to the increase were foreign currency gains, as well as improved investment yields stemming from rising interest rates.

Income Taxes

During 2004, we recorded a foreign income tax expense of approximately $30,000 as a result of profitability in our foreign subsidiary. Moreover, during 2004 we recorded an approximate $0.8 million release of deferred tax asset valuation reserves (tax benefit) as a result of a revaluation of the net realizable deferred tax assets in connection with our tax planning strategy.

In 2003, we recorded approximately $0.3 million in tax benefit upon receiving a favorable outcome from an IRS audit of our income tax returns for the fiscal years 1996 through 1998. The $0.3 million recovery in 2003 was partially offset by $51,000 in foreign subsidiary taxes associated with local profitability.

Liquidity and Capital Resources

We have historically funded our operations from product sales, net proceeds from public and private equity offerings, bank financings, proceeds received from exercises of stock options, and to a lesser extent, equipment leasing and financing arrangements. As of December 31, 2005, we had $50.1 million in cash, cash equivalents and marketable securities and $61.6 million in working capital.

For the year ended December 31, 2005, we generated $6.1 million in cash from operations as compared to cash used in operations of $4.4 million for the year ended December 31, 2004. The primary reason for the increase is attributable to our increase in revenue and related gross margin coupled with our ability to keep operating expenses and our investment in working capital stable in 2005.

Net cash used in investing activities for the year ended December 31, 2005 was $2.9 million as compared to cash used in investing activities of $37.0 million for the year ended December 31, 2004. The primary reason for the decrease is a reduction in the purchase of marketable securities in 2005 of approximately $32.9 million driven by our investment of offering proceeds in 2004. In 2005, we spent approximately $2.3 million on capital expenditures, reflecting an increase of approximately $0.8 million from 2004. The 2005 capital expenditures consisted primarily of new computer and manufacturing equipment necessary to support our infrastructure and planned growth.

Net cash provided by financing activities for the year ended December 31, 2005 was $0.7 million as compared to net cash provided by financing activities of $48.9 million for the year ended December 31, 2004.

The primary reason for the decrease is due to the completion of our common stock offering in February 2004, in which we issued 2.75 million shares at a price of $18.75 per share for total net proceeds of approximately $48.0 million. The 2005 cash provided by financing activities represents proceeds received from stock options of $0.8 million, partially offset by repayments of long-term debt.

Currently, we have a revolving loan agreement with a bank that provides for a maximum available credit of $15.0 million and expires on July 17, 2006. We pay interest on any outstanding amounts at a rate equal to, at our option, LIBOR plus 2.0%, or the greater of the Federal Funds Effective Rate plus 0.5% or the bank's prime interest rate. We pay monthly fees at an annual rate of 0.25% on up to $10.0 million of the unused portion of the loan facility. The loan facility advances funds using an asset availability formula based upon our eligible accounts receivable and inventory balances, less a fixed reserve amount. We may terminate the loan agreement prior to its full term without penalty, provided we give 30 days written notice to the bank. As of December 31, 2005, no borrowings were outstanding under the facility.

On January 11, 1999, we entered into a mortgage loan in the amount of $3.0 million. The note term is 10 years, with a principal amortization of 20 years at a fixed rate of interest of 7.0%. Land, building and improvements secure the mortgage loan. The monthly mortgage payment is approximately $23,000, including interest and principal. Due to the difference in the term of the note and amortization of the principal, a balloon payment of $2.0 million is due on February 1, 2009. Under the mortgage loan we may prepay our outstanding loan balance subject to certain early termination charges as defined in the mortgage loan agreement.

We believe that the $50.1 million in cash, cash equivalents and marketable securities, together with our other existing working capital, will be adequate to meet planned operating and capital requirements through the foreseeable future. However, as the need or opportunity arises, we may seek to raise additional capital through public or private sales of securities or through additional debt financing. There are no assurances that we will be able to obtain any additional funding or that such funding will be available on acceptable terms.

Contractual Obligations and Other Commercial Commitments

As of December 31, 2005, our contractual commitments consisted of a mortgage note payable, near-term purchase order commitments, facility leases and equipment leases. The principal repayment of the mortgage note is based on a 20-year amortization schedule, but the term is 10 years, requiring a balloon payment of $2.0 million on February 1, 2009. There are no loan-to-value covenants in the loan that would require early pay-down of the mortgage if the market value of the property should decline. Our purchase commitments include unconditional purchase orders for inventory and manufacturing materials extending out over various periods throughout 2006. We are also obligated under multi-year facility leases that terminate at various times between 2008 and 2014. Our other operating leases represent vehicle and equipment operating leases.

The following table summarizes our obligations under these commitments at December 31, 2005:

	Payment Due by Period				
Contractual Obligations	Total	Less than 1 Year	1–3 Years	3-5 Years	More than 5 Years
			(in thousands)		
Mortgage and other loans	$ 2,397	$ 115	$ 255	$ 2,027	$ —
Purchase commitments	8,024	8,024	—	—	—
Facility lease obligations	2,220	517	876	471	356
Other operating lease obligations	169	101	60	8	—
Total	$12,810	$ 8,757	$ 1,191	$ 2,506	$ 356

In the first quarter of 2006, we entered into a licensing agreement with Litton Systems, Inc., a wholly owned subsidiary of Northrop Grumman Systems Corporation (Grumman) to provide us with the right to access/use certain patented technologies owned by Grumman. Under the agreement, which spans the life of the patented technology, we will pay a licensing fee to Grumman equal to 4.5% of the net selling price for each unit sold in which the licensed technology is utilized. The agreement provides for minimum payments during the next four years of $312,500, $250,000, $250,000 and $187,500, respectively.

We have not entered into any off-balance sheet commercial commitments, such as standby letters of credit, guarantees or standby repurchase obligations.

Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards (SFAS) No. 123(R), “Share-Based Payment.” SFAS No. 123(R) addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise, or (b) liability instruments that are based on the fair value of the enterprise’s equity instruments or that may be settled by the issuance of such equity instruments. SFAS No. 123(R) requires an entity to recognize the grant-date fair-value of stock options and other equity-based compensation issued to employees in the statement of operations.

SFAS No. 123 requires entities to disclose information about the nature of the share-based payment transactions and the effects of those transactions on the financial statements. SFAS No. 123(R) is effective for us in 2006. As a result, beginning January 1, 2006 we will record compensation expense related to outstanding employee stock options in accordance with the provisions of SFAS No. 123(R). The actual impact of implementing SFAS No. 123(R) will depend upon a number of variables, however, based on current information, we anticipate the effect on 2006 results to be an expense of approximately $0.9 million or $(0.06) per share.

In November 2004, the FASB issued SFAS No. 151, “Inventory Costs”, to amend the guidance in Chapter 4, “Inventory Pricing”, of FASB Accounting Research Bulletin No. 43, “Restatement and Revision of Accounting Research Bulletins.” SFAS No. 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). SFAS No. 151 requires that those items be recognized as current-period charges. Additionally, SFAS No. 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This statement is effective for fiscal years beginning after June 15, 2005. We will adopt this statement in 2006 and adoption is not expected to have a material impact on our financial position or results of operations.

ITEM 7A. Quantitative and Qualitative Disclosure About Market Risk

Our primary market risk exposure is in the area of foreign currency exchange risk. We are exposed to currency exchange rate fluctuations related to our subsidiary operations in Denmark. Certain functions in Denmark are transacted in the Danish Krone or Euro, yet reported in the U.S. dollar, the functional currency. For foreign currency exposures existing at December 31, 2005, a 10% unfavorable movement in the foreign exchange rates for our subsidiary location would not expose us to material losses in earnings or cash flows.

From time to time, we purchase foreign currency forward exchange contracts generally having durations of no more than 4 months. These forward exchange contracts are intended to offset the impact of exchange rate fluctuations on intercompany payments due from our foreign subsidiary. Forward exchange contracts are accounted for as cash flow hedges and are recorded on the balance sheet at fair value until executed. Changes in the fair value are recognized in earnings. For the year ended December 31, 2005 we recorded a gain of $40,000 related to these contracts. Such gain is reflected within “other (expense) income” in our 2005 consolidated statement of operations. As of December 31, 2005, there were no outstanding forward contracts.

The primary objective of our investment activities is to preserve principal and maintain liquidity, while at the same time maximize income. We have not entered into any instruments for trading purposes. Some of the securities that we invest in may have market risk. To minimize this risk, we maintain our portfolio of cash equivalents and short-term investments in a variety of securities, including commercial paper, investment grade asset-backed corporate securities, money market funds and government agency and non-government debt securities. As of December 31, 2005, a hypothetical 100 basis-point increase in interest rates would result in an approximate $20,000 decrease in the fair value of our investments that have maturities of greater than one year. However, due to the conservative nature of our investments, the relatively short duration of their maturities, our ability to either convert some or all of our long-term investments to less interest rate-sensitive holdings or hold most securities until maturity, we believe interest rate risk is mitigated. As of December 31, 2005, approximately 89% of the $35.9 million classified as available-for-sale marketable securities will mature or reset within one year. We do not invest in any financial instruments denominated in foreign currencies. Accordingly, interest rate risk is not considered material.

ITEM 8. Financial Statements and Supplementary Data

Our consolidated financial statements and supplementary data, together with the report of KPMG LLP, our independent registered public accounting firm, are included in Part IV of this annual report on Form 10-K.

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

None.

ITEM 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures, which are designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer, or CEO, and chief financial officer, or CFO, as appropriate to allow timely decisions regarding required disclosure.

Under the supervision and with the participation of our CEO and CFO, our management has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this annual report. Based on that evaluation, our CEO and CFO concluded that our disclosure controls and procedures were effective as of December 31, 2005.

Evaluation of Changes in Internal Controls over Financial Reporting

Under the supervision and with the participation of our CEO and CFO, our management has evaluated changes in our internal controls over financial reporting that occurred during our last fiscal quarter. Based on that evaluation, our CEO and CFO did not identify any change in our internal controls over financial reporting that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

Management’s Report on Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is the process designed by and under the supervision of our CEO and CFO to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of our financial statements for external reporting in accordance with accounting principles generally accepted in the United States of America. Management has evaluated the effectiveness of our internal control over financial reporting using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control—Integrated Framework.

Under the supervision and with the participation of our CEO and CFO, our management has assessed the effectiveness of our internal control over financial reporting as of December 31, 2005 and concluded that it is effective.

Our independent registered public accounting firm, KPMG LLP, has issued an attestation report regarding the effectiveness of our internal control over financial reporting and management's assessment of the effectiveness of our internal control over financial reporting as of December 31, 2005, and that report is included below.

Important Considerations

The effectiveness of our disclosure controls and procedures and our internal control over financial reporting is subject to various inherent limitations, including cost limitations, judgments used in decision making, assumptions about the likelihood of future events, the soundness of our systems, the possibility of human error, and the risk of fraud. Moreover, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions and the risk that the degree of compliance with policies or procedures may deteriorate over time. Because of these limitations, there can be no assurance that any system of disclosure controls and procedures or internal control over financial reporting will be successful in preventing all errors or fraud or in making all material information known in a timely manner to the appropriate levels of management.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
KVH Industries, Inc.:

We have audited management's assessment, included in the accompanying Management's Report on Internal Control over Financial Reporting, that KVH Industries, Inc. maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. KVH Industries, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of KVH Industries, Inc.'s internal control over financial reporting based on our audit.

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

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

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

In our opinion, management's assessment that KVH Industries, Inc. maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in *Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*. Also, in our opinion, KVH Industries, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of KVH Industries, Inc. and subsidiary as of December 31, 2005 and 2004, and the related consolidated statements of operations, changes in stockholders' equity and accumulated other comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2005, and our report dated March 15, 2006, expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP
Providence, Rhode Island
March 15, 2006

ITEM 9B. Other Information

None.

PART III

We have omitted the information required in Part III of this annual report because we intend to include that information in our definitive proxy statement for our 2006 annual meeting of stockholders, which we expect to file before 120 days after the end of fiscal 2005. We incorporate that information in this annual report by reference to our 2006 proxy statement.

ITEM 10. Directors and Executive Officers of the Registrant

Information in our 2006 proxy statement under the captions "Directors and Executive Officers," "Section 16(a) Beneficial Ownership Reporting Compliance" and "Code of Ethics" is incorporated by reference.

ITEM 11. Executive Compensation

Information in our 2006 proxy statement under the caption "Compensation of Directors and Executive Officers" is incorporated by reference.

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

Information in our 2006 proxy statement under the captions "Principal Stockholders" and "Equity Compensation Plans" is incorporated by reference.

ITEM 13. Certain Relationships and Related Transactions

None.

ITEM 14. Principal Accountant Fees and Services

Information in our 2006 proxy statement under the caption "Principal Accountant Fees and Services" is incorporated by reference.

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PART IV

ITEM 15. Exhibits and Financial Statement Schedules

		Page
1.	Financial Statements	

| 2. | Financial Statement Schedules | |
| | None. | |

3. Exhibits

Exhibit No.	Description	Filed with this Form 10-K	Incorporated by Reference		
			Form	Filing Date	Exhibit No.
3.1	Amended and Restated Certificate of Incorporation		S-1	February 16, 1996	3.3
3.2	Certificate of Amendment of Certificate of Incorporation		S-3	November 26, 2003	4.2
3.3	Amended, Restated and Corrected By-Laws		8-K	January 23, 2004	3.1
4.1	Specimen certificate for the common stock		S-1/A	March 22, 1996	4.1
*10.1	Amended and Restated 1995 Incentive Stock Option Plan		10-K	March 15, 2004	10.2
*10.2	Amended and Restated 1996 Incentive and Nonqualified Stock Option Plan		10-K	March 15, 2004	10.3
*10.3	Amended and Restated 1996 Employee Stock Purchase Plan		8-K	December 13, 2005	10.1
*10.4	2003 Incentive and Nonqualified Stock Option Plan		10-K	March 15, 2004	10.5
10.5	Open End Mortgage and Security Agreement dated January 11, 1999 with IDS Life Insurance Co. for 50 Enterprise Center, Middletown, RI		10-K	March 24, 1999	99.1
10.6	Loan and Security Agreement dated March 27, 2000 with Fleet Capital Corporation		10-K	March 30, 2000	10.38
10.7	First Amendment to Loan and Security Agreement dated March 7, 2003 with Fleet Capital Corporation		8-K/A	November 26, 2003	10.1
10.8	Second Amendment to Loan and Security Agreement dated as of June 25, 2003 with Fleet Capital Corporation		8-K	June 27, 2003	99.1
10.9	Amended and Restated Credit and Security Agreement dated July 17, 2003 with Fleet Capital Corporation		8-K	July 18, 2003	99.1
10.10	Independent Retailer Agreement dated June 21, 2004 with DIRECTV, Inc.		10-Q	August 6, 2004	10.1
*10.11	Form of Nonqualified Stock Option agreement granted under the 1996 Incentive and Nonqualified Stock Option Plan		10-K	March 15, 2005	10.12
*10.12	Form of Incentive Stock Option agreement granted under the 1996 Incentive and Nonqualified Stock Option Plan		10-K	March 15, 2005	10.13
*10.13	Form of Nonqualified Stock Option agreement granted under the 2003 Incentive and Nonqualified Stock Option Plan		10-K	March 15, 2005	10.14
*10.14	Form of Incentive Stock Option agreement granted under the 2003 Incentive and Nonqualified Stock Option Plan		10-K	March 15, 2005	10.15
10.15	Written Description of Option Acceleration on December 9, 2005		8-K	December 13, 2005	10.2

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Exhibit No.	Description	Filed with this Form 10-K	Incorporated by Reference		
			Form	Filing Date	Exhibit No.
21.1	List of Subsidiaries		S-1	March 28, 1996	21.1
23.1	Consent of KPMG LLP	X			
31.1	Rule 13a-14(a)/15d-14(a) certification of principal executive officer	X			
31.2	Rule 13a-14(a)/15d-14(a) certification of principal financial officer	X			
32.1	Rule 1350 certification	X			

* Management contract or compensatory plan.

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SIGNATURES

Pursuant to the requirements of Section 13 or Section 15(d) 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.

KVH Industries, Inc.

Date: March 16, 2006

By: /S/ MARTIN A. KITS VAN HEYNINGEN

Martin A. Kits van Heyningen
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons in the capacities and on the dates indicated.

Name	Title	Date
/S/ MARTIN A. KITS VAN HEYNINGEN **Martin A. Kits van Heyningen**	President, Chief Executive Officer and Director (Principal Executive Officer)	March 16, 2006
/S/ PATRICK J. SPRATT **Patrick J. Spratt**	Chief Financial Officer (Principal Financial and Accounting Officer)	March 16, 2006
/S/ ARENT H. KITS VAN HEYNINGEN **Arent H. Kits van Heyningen**	Chairman of the Board	March 16, 2006
/S/ ROBERT W.B. KITS VAN HEYNINGEN **Robert W.B. Kits van Heyningen**	Director	March 16, 2006
/S/ MARK S. AIN **Mark S. Ain**	Director	March 16, 2006
Stanley K. Honey	Director	
/S/ BRUCE J. RYAN **Bruce J. Ryan**	Director	March 16, 2006
/S/ CHARLES R. TRIMBLE **Charles R. Trimble**	Director	March 16, 2006

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
KVH Industries, Inc.:

We have audited the accompanying consolidated balance sheets of KVH Industries, Inc. and subsidiary as of December 31, 2005 and 2004, and the related consolidated statements of operations, changes in stockholders' equity and accumulated other comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2005. 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 financial position of KVH Industries, Inc. and subsidiary at December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2005, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of KVH Industries, Inc.'s internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)*, and our report dated March 15, 2006 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

/s/ KPMG LLP
Providence, Rhode Island
March 15, 2006

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KVH INDUSTRIES, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

	December 31, 2005	December 31, 2004
ASSETS		
Current assets:		
Cash and cash equivalents	$ 14,159,945	$ 10,289,145
Marketable securities	35,930,101	35,438,442
Accounts receivable, net of allowance for doubtful accounts of approximately $626,000 in 2005 and $677,000 in 2004	12,283,225	9,576,869
Costs and estimated earnings in excess of billings on uncompleted contracts	235,200	746,638
Inventories	6,563,550	7,250,597
Prepaid expenses and other assets	792,928	486,872
Deferred income taxes	205,365	645,730
Total current assets	70,170,314	64,434,293
Property and equipment, net	8,662,681	8,218,294
Intangible assets, less accumulated amortization of approximately $1,016,000 in 2005 and $890,000 in 2004	63,152	189,177
Other non-current assets	99,993	58,565
Deferred income taxes	3,333,775	3,013,430
Total assets	**$ 82,329,915**	**$ 75,913,759**
LIABILITIES AND STOCKHOLDERS' EQUITY		
Commitments and contingencies (notes 6, 7 and 15)		
Current liabilities:		
Accounts payable	$ 3,479,653	$ 1,604,006
Accrued compensation and employee-related expenses	2,976,531	1,765,690
Accrued other	948,465	435,099
Accrued product warranty costs	611,169	440,020
Accrued professional fees and license and settlement costs	371,360	435,888
Accrued loss on TracVision A5 non-cancelable purchase commitments	55,000	996,856
Current portion of long-term debt	114,985	107,233
Total current liabilities	8,557,163	5,784,792
Long-term debt excluding current portion	2,281,663	2,396,648
Deferred revenue	128,391	—
Total liabilities	10,967,217	8,181,440
Stockholders' equity:		
Preferred stock, $0.01 par value. Authorized 1,000,000 shares; none issued.	—	—
Common stock, $0.01 par value. Authorized 20,000,000 shares; issued and outstanding 14,638,100 as of December 31, 2005 and 14,487,841 as of December 31, 2004.	146,381	144,878
Additional paid-in capital	85,889,934	85,072,874
Accumulated deficit	(14,504,823)	(17,435,809)
Accumulated other comprehensive loss	(168,794)	(49,624)
Total stockholders' equity	**71,362,698**	**67,732,319**
Total liabilities and stockholders' equity	**$ 82,329,915**	**$ 75,913,759**

See accompanying Notes to Consolidated Financial Statements.

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KVH INDUSTRIES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31,		
	2005	2004	2003
Net sales	$ 71,257,981	$ 62,302,541	$ 56,672,605
TracVision A5 revaluation charge	(100,050)	2,358,420	—
All other costs of sales	41,686,618	39,933,088	33,795,341
Total costs of sales	41,586,568	42,291,508	33,795,341
Gross profit	29,671,413	20,011,033	22,877,264
Operating expenses:			
Research and development	7,692,426	6,336,781	8,578,628
Sales and marketing	13,844,955	15,907,155	11,200,733
General and administrative	5,844,681	5,166,066	4,596,799
Income (loss) from operations	2,289,351	(7,398,969)	(1,498,896)
Other income (expense):			
Interest income (expense), net	1,269,070	471,226	(165,459)
Other (expense) income	(338,352)	34,746	(78,044)
Income (loss) before income taxes	3,220,069	(6,892,997)	(1,742,399)
Income tax expense (benefit)	289,083	(745,667)	(271,945)
Net income (loss)	**$ 2,930,986**	**$ (6,147,330)**	**$ (1,470,454)**
Per share information:			
Net income (loss) per share, basic and diluted	**$ 0.20**	**$ (0.44)**	**$ (0.13)**
Number of shares used in per share calculation:			
Basic	**14,571,207**	**14,109,039**	**11,403,258**
Diluted	**14,685,321**	**14,109,039**	**11,403,258**

See accompanying Notes to Consolidated Financial Statements.

KVH INDUSTRIES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY AND ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
Balances at January 1, 2003	**$ 111,498**	**$35,134,093**	**$ (9,818,025)**	**$ 3,927**	**$25,431,493**
Comprehensive loss:					
Net loss			(1,470,454)	—	(1,470,454)
Settlement of foreign exchange contract			—	(3,927)	(3,927)
Comprehensive loss					(1,474,381)
Non-cash stock based compensation expense	—	12,057	—	—	12,057
Common stock issued under benefit plan	185	225,197	—	—	225,382
Exercise of warrants	1,090	(1,090)	—	—	—
Exercise of stock options	3,128	1,135,494	—	—	1,138,622
Balances at December 31, 2003	**115,901**	**36,505,751**	**(11,288,479)**	**—**	**25,333,173**
Comprehensive loss:					
Net loss			(6,147,330)	—	(6,147,330)
Unrealized loss on marketable securities			—	(49,624)	(49,624)
Comprehensive loss					(6,196,954)
Issuance of common stock	27,500	47,955,730	—	—	47,983,230
Common stock issued under benefit plan	236	221,731	—	—	221,967
Exercise of stock options	1,241	389,662	—	—	390,903
Balances at December 31, 2004	**144,878**	**85,072,874**	**(17,435,809)**	**(49,624)**	**67,732,319**
Comprehensive income:					
Net income			2,930,986	—	2,930,986
Unrealized loss on marketable securities			—	(119,170)	(119,170)
Comprehensive income					2,811,816
Common stock issued under benefit plan	241	191,787	—	—	192,028
Exercise of stock options	1,262	625,273	—	—	626,535
Balances at December 31, 2005	**$146,381**	**$85,889,934**	**$(14,504,823)**	**$ (168,794)**	**$71,362,698**

See accompanying Notes to Consolidated Financial Statements.

KVH INDUSTRIES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2005	2004	2003
Cash flows from operating activities:			
Net income (loss)	$ 2,930,986	$ (6,147,330)	$ (1,470,454)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	1,957,507	2,042,950	1,723,748
Deferred income tax	120,020	(770,573)	(33,280)
Provision for doubtful accounts	68,705	713,993	52,812
(Gain) loss on disposal of equipment	(22,021)	104,603	—
TracVision A5 revaluation and related charges	(100,050)	2,471,545	—
Non-cash stock-based compensation expense	—	—	12,057
Changes in operating assets and liabilities:			
Accounts receivable	(2,775,081)	1,062,313	(1,689,695)
Costs and estimated earnings in excess of billings on uncompleted contracts	511,438	(331,223)	(38,357)
Inventories	687,047	(1,788,021)	(2,354,871)
Prepaid expenses and other assets	(306,036)	315,191	(641,417)
Accounts payable	1,875,647	(1,986,488)	1,269,390
Accrued expenses	973,132	(96,117)	498,808
Deferred revenue	144,282	—	(64,243)
Net cash provided by (used in) operating activities	6,065,576	(4,409,157)	(2,735,502)
Cash flows from investing activities:			
Purchase of marketable securities	(2,610,829)	(35,488,066)	—
Capital expenditures	(2,275,870)	(1,522,066)	(2,935,690)
Proceeds from the sale of equipment	22,021	5,097	—
Redemption of marketable securities	2,000,000	—	—
Other long-term assets	(41,428)	(12,046)	—
Net cash used in investing activities	(2,906,106)	(37,017,081)	(2,935,690)
Cash flows from financing activities:			
Repayment of long-term debt	(107,233)	(109,954)	(83,312)
Proceeds from sale of common stock, net	—	48,363,712	—
Proceeds from stock option and benefit plan	818,563	612,870	1,364,004
Net cash provided by financing activities	711,330	48,866,628	1,280,692
Net increase (decrease) in cash and cash equivalents	3,870,800	7,440,390	(4,390,500)
Cash and cash equivalents at beginning of year	10,289,145	2,848,755	7,239,255
Cash and cash equivalents at end of year	$ 14,159,945	$ 10,289,145	$ 2,848,755
Supplemental disclosure of cash flow information:			
Cash paid during the year for interest	$ 196,670	$ 189,442	$ 209,688

See accompanying Notes to Consolidated Financial Statements.

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2005, 2004 and 2003
(all tabular amounts in thousands except per share amounts)

(1) Summary of Significant Accounting Policies

(a) Description of Business

KVH Industries, Inc. (KVH) develops, manufactures and markets mobile communications products for the land mobile and marine markets, and navigation, guidance and stabilization products for both defense and commercial markets.

KVH is among the leading providers of mobile communications products that enable customers to receive live television, telephone and Internet services in their cars, recreational vehicles and marine vessels while on the move via satellite and wireless services. KVH sells its TracVision, TracPhone, and TracNet mobile communications products through an extensive international network of retailers, distributors and dealers.

KVH's defense products include tactical navigation systems that provide uninterrupted access to navigation information in a spectrum of military vehicles, including HMMWVs and light armored vehicles. KVH also offers precision fiber optic gyro-based systems that enable platform stabilization and munitions guidance. KVH's defense products are sold directly to U.S. and allied governments and government contractors, as well as through an international network of authorized independent sales representatives. In addition, KVH's defense products have numerous commercial applications such as train location control and track geometry measurement systems, industrial robotics, and optical stabilization.

(b) Principles of Consolidation

The consolidated financial statements include the financial statements of KVH Industries, Inc. and its wholly owned subsidiary, KVH Europe A/S ("KVH Europe"). All significant inter-company accounts and transactions have been eliminated in consolidation.

(c) Use of Estimates

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

(d) Concentration of credit risk

Cash, cash equivalents and marketable securities. KVH is potentially subject to financial instrument concentration of credit risk through its cash, cash equivalent and marketable securities investments. To mitigate these risks KVH maintains cash, cash equivalents and marketable securities with reputable and nationally recognized financial institutions. As of December 31, 2005, $35.9 million classified as marketable securities was held by Lehman Brothers Inc., and the majority of the cash and cash equivalents was held by Bank of America, Inc. KVH performs periodic evaluations of the relative credit standing of these financial institutions as a means of limiting the amount of credit exposure.

Trade accounts receivable. Concentrations of risk with respect to trade accounts receivable are generally limited due to the large number of customers and their dispersion across several geographic areas. Although KVH does not foresee credit risk associated with these receivables to deviate from historical experience,
repayment is dependent upon the financial stability of those individual customers and their respective economies.

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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(1) Summary of Significant Accounting Policies—*(continued)*

KVH establishes reserves for potential bad debt and evaluates, on a monthly basis, the adequacy of those reserves based upon historical experience and its expectations for future collectibility concerns. Activity within KVH's reserve for bad debt for the periods presented is as follows:

	2005	2004	2003
Beginning balance	$ 677	$ 120	$153
Additions charged to expense	68	714	53
Deductions (write-offs/recoveries) from reserve	(119)	(157)	(86)
Ending balance	$ 626	$ 677	$120

Included in the 2004 expense was approximately $556,000 in specific reserve resulting from a voluntary liquidation under local law of a European distributor.

(e) Revenue Recognition

Product Sales. Revenue from product sales is recognized when persuasive evidence of an arrangement exists, goods are shipped, title has passed and collectibility is reasonably assured. KVH establishes reserves for potential sales returns and allowances, and evaluates, on a monthly basis, the adequacy of those reserves based upon historical experience and expectations for future returns. KVH standard sales terms require that:

- All sales are final;
- Terms are either Net 30 or Net 45;
- Shipments are tendered and shipped FOB (or as may be applicable, FCA, or EXW) KVH's plant or warehouse; and
- Title and risk of loss or damage passes to the dealer or distributor at the point of shipment when delivery is made to the possession of the carrier.

Under certain limited conditions, KVH, at its sole discretion, provides for the return of goods. No product is accepted for return and no credit is allowed on any returned product unless KVH has granted and confirmed prior written permission by means of appropriate authorization.

Contracted Service Revenue. Customer and government-agency contracted engineering service and grant revenue under development contracts is recognized during the period in which KVH performs the service or development efforts in accordance with the agreement. Performance is determined principally by comparing the accumulated costs incurred to date with management's estimate of the total cost to complete the contracted work. Costs and recognized proportionate income not yet billed are recognized within the accompanying consolidated balance sheets in the caption "costs and estimated earnings in excess of billings on uncompleted contracts."

Standard product modification, enhancement and development contract revenue is recognized upon the complete delivery and title transfer of all customer-approved products. Costs of contracts in progress are accumulated within the accompanying consolidated balance sheets in the caption "costs and estimated earnings in excess of billings on uncompleted contracts" and relieved upon product delivery.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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(1) Summary of Significant Accounting Policies—*(continued)*

Revisions to costs and income estimates are reflected in the period in which the facts that require revision become known. Any advance payments arising from such extended-term development contracts are recorded as deposits. If, in any period, estimated total costs under a contract indicate a loss, then such loss is provided for in that period. To date, contracted service revenue has not been a significant portion of KVH's total revenue.

Product service revenue. Revenue from services other than under development contracts is recognized when completed services are provided to the customer and collectibility is reasonably assured. To date, product service revenue has not been a significant portion of KVH's total revenue.

Satellite activation and usage revenue. Service activation fees are recognized upon receiving notice from the third party satellite service provider that a purchaser of KVH's product has established service with the satellite service provider. Re-sold satellite connectivity and usage revenue is recognized based upon usage by the subscriber. In general, connectivity and usage services are billed one month in arrears and recognized when earned. To date, satellite activation and usage revenue has not been a significant portion of KVH's total revenue.

Extended warranty revenue. Beginning in 2005, KVH began selling extended warranty contracts to certain of its customers. Revenue under these contracts will be recognized in future periods ratably over the contract term. No revenue was recognized in 2005 related to extended warranty contracts, and amounts collected, which approximated $144,000 are reflected in accrued other and deferred revenue in the accompanying 2005 consolidated balance sheet.

(f) Fair Value of Financial Instruments

The carrying amounts of accounts receivable, contracts receivable, costs and estimated earnings in excess of billings on uncompleted contracts, accounts payable and accrued expenses approximate fair value due to the short maturity of these instruments. The carrying amount of KVH's mortgage loan approximates fair value based on currently available quoted rates of similarly structured mortgage facilities. See note 2 for information on the fair value of KVH's marketable securities.

(g) Cash, Cash Equivalents and Marketable Securities

In accordance with KVH's investment policy, cash in excess of operational needs is invested in money market funds, investment-grade corporate and U.S. government debt as well as certain asset-backed securities. KVH considers all highly liquid investments with an original maturity of ninety days or less, as of the date of purchase, to be cash equivalents. KVH determines the appropriate classification of marketable securities at each balance sheet date. Available-for-sale marketable securities are carried at their fair value with unrealized gains and losses included in accumulated other comprehensive income (loss) in the accompanying consolidated balance sheets.

KVH reviews investments in debt and equity securities for other than temporary impairment whenever the fair value of an investment is less than amortized cost and evidence indicates that an investment's carrying amount is not recoverable within a reasonable period of time. To determine whether an impairment is other-than-temporary, KVH considers whether it has the ability and the intent to hold the investment until a market price recovery and considers whether evidence indicating the cost of the investment is recoverable outweighs evidence

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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(all tabular amounts in thousands except per share amounts)

(1) Summary of Significant Accounting Policies—*(continued)*

to the contrary. Evidence considered in this assessment includes the reasons for the impairment, compliance with KVH's investment policy, the severity and duration of the impairment, changes in value subsequent to year-end and forecasted performance of the investee. KVH has reviewed its securities with unrealized losses as of December 31, 2005 and 2004, and has concluded that no other-than-temporary impairments exist.

Interest income earned on KVH's cash, cash equivalents and marketable securities is reflected in "interest income (expense), net" in the accompanying statements of operations and approximated $1.5 million, $0.7 million and $0.1 million for the years ended December 31, 2005, 2004 and 2003, respectively.

(h) Inventories

Inventories are stated at the lower of cost or market using the first-in first-out costing method.

(i) Property and Equipment

Property and equipment are stated at cost. Depreciation and amortization are computed on the straight-line method over the estimated useful lives of the respective assets. The principal lives used in determining the depreciation rates of various assets are: buildings and improvements, 40 years; leasehold improvements, over the shorter of the assets useful life or the term of the lease; machinery and equipment, 5 years; office and computer equipment, 3-7 years; and motor vehicles, 4 years.

(j) Long-lived Assets

KVH's management reviews long-lived assets and certain identifiable intangibles for impairment 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 an asset to undiscounted future net cash flows expected to be generated by the asset. 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. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

(k) Product Warranty

KVH's products carry limited warranties that range from one to two years and vary by product. The warranty period begins as of confirmed date of end-consumer installation. KVH accrues estimated product warranty costs at the time of sale and any additional amounts are recorded when such costs are probable and can be reasonably estimated. Such costs are reflected within sales and marketing expense in the accompanying statements of operations.

(l) Shipping and Handling Costs

Shipping and handling costs are expensed as incurred and included in cost of sales.

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
December 31, 2005, 2004 and 2003
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(1) Summary of Significant Accounting Policies—*(continued)*

(m) Research and Development

Expenditures for research and development, including customer-funded research and development, are expensed as incurred. Revenue from customer-funded research and development is included in net sales, and the related product development costs are included in cost of goods sold. Revenue and related development costs from customer-funded research and development are as follows:

	Year ended December 31,		
	2005	2004	2003
Customer-funded revenues	$ 1,852	$ 1,752	$ 1,196
Customer-funded costs	1,418	1,240	937

(n) Advertising Costs

Costs related to advertising are expensed as incurred. Advertising expense was $2.2 million, $3.7 million, and $2.2 million for the years ended December 31, 2005, 2004 and 2003, respectively, and is included in sales and marketing expense in the accompanying consolidated statements of operations.

(o) Foreign Currency Translation

The financial statements of KVH's foreign subsidiary, located in Denmark, are maintained in the United States dollar functional currency for both reporting and consolidation purposes. Exchange rates in effect on the date of the transaction are used to record monetary assets and liabilities. Revenue and other expense elements are recorded at rates that approximate the rates in effect on the transaction dates. Realized foreign currency remeasurement gains and losses are recognized within "other (expense) income" in the accompanying consolidated statements of operations. For the years ended December 31, 2005, 2004 and 2003, foreign currency (losses) gains approximated $(0.3) million, $0.1 million, and $0.1 million, respectively.

(p) Stock-based Compensation

KVH accounts for its various stock-based compensation plans using the intrinsic value method prescribed by Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." The following pro forma information is based on provisions of Statement of Financial Accounting Standards (SFAS) No. 123, "Accounting for Stock-Based Compensation," as amended by SFAS No. 148, "Accounting for Stock-Based Compensation—Transition and Disclosure" (see note 8).

	Year ended December 31,		
	2005	2004	2003
Net income (loss) as reported	$2,931	$(6,147)	$(1,470)
Compensation expense under SFAS 123	2,809	1,887	1,330
Pro forma net income (loss)	$ 122	$(8,034)	$(2,800)
Income (loss) per share—basic and diluted			
As reported	$ 0.20	$ (0.44)	$ (0.13)
Pro forma	$ 0.01	$ (0.57)	$ (0.25)

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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(1) Summary of Significant Accounting Policies—*(continued)*

(q) Income Taxes

Income taxes are accounted for under the asset and liability method. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases.

Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In accordance with SFAS No. 109, KVH has adopted a tax planning strategy to support the realization of a portion of its total domestic deferred tax assets (see note 10).

(r) Income (Loss) per Common Share

Basic net income (loss) per share is calculated based on the weighted average number of common shares outstanding during the period. Diluted net income (loss) per share incorporates the dilutive effect of common stock equivalent options, warrants and other convertible securities, if any, as determined in accordance with the treasury-stock accounting method. Common stock equivalents related to options to purchase approximately 0.8 million, 1.2 million, and 1.0 million shares of common stock for the years ended December 31, 2005, 2004, and 2003, respectively, have been excluded from the fully diluted calculation of income (loss) per share, as inclusion would be anti-dilutive.

A reconciliation of the basic and diluted weighted average common shares outstanding is as follows:

	2005	2004	2003
Net income (loss)	$ 2,931	$ (6,147)	$ (1,470)
Weighted average common shares outstanding—basic	14,571	14,109	11,403
Incremental common shares issuable—stock options	114	—	—
Weighted average common shares outstanding—diluted	14,685	14,109	11,403
Income (loss) per share—basic and diluted	$ 0.20	$ (0.44)	$ (0.13)

(s) Derivative Instruments

KVH occasionally enters into foreign currency forward contracts to hedge a portion of anticipated Euro-denominated transactions against currency fluctuations. KVH accounts for these derivative instruments at fair value and records any changes in fair value within “other (expense) income” in the accompanying statements of operations.

KVH recorded foreign currency contract gains (losses) of approximately $39,000 and $21,000, for the years ended December 31, 2005 and 2004. There were no currency contract gains or losses recorded in 2003.

(t) Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123(R), “Share-Based Payment.” SFAS No. 123(R) addresses the accounting for share-based payment transactions in which an enterprise receives employee services in exchange for (a) equity instruments of the enterprise, or (b) liability

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(1) Summary of Significant Accounting Policies—*(continued)*

instruments that are based on the fair value of the enterprise's equity instruments or that may be settled by the issuance of such equity instruments. SFAS No. 123(R) requires an entity to recognize the grant-date fair-value of stock options and other equity-based compensation issued to employees in the statement of operations.

SFAS No. 123(R) requires entities to disclose information about the nature of the share-based payment transactions and the effects of those transactions on the financial statements. SFAS No. 123(R) is effective for KVH in 2006. As a result, beginning January 1, 2006 KVH will record compensation expense related to outstanding employee stock options in accordance with the provisions of SFAS No. 123(R). The actual impact of implementing SFAS No. 123(R) will depend upon a number of variables; however, based on current information, KVH anticipates the effect on 2006 results to be an expense of approximately $0.9 million or $(0.06) per share.

In November 2004, the FASB issued SFAS No. 151, "Inventory Costs", to amend the guidance in Chapter 4, "Inventory Pricing", of FASB Accounting Research Bulletin No. 43, "Restatement and Revision of Accounting Research Bulletins." SFAS No. 151 clarifies the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material (spoilage). SFAS No. 151 requires that those items be recognized as current-period charges. Additionally, SFAS No. 151 requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This statement is effective for fiscal years beginning after June 15, 2005. KVH will adopt this statement in 2006 and adoption is not expected to have a material impact on KVH's financial position or results of operations.

(2) Marketable Securities

Included in marketable securities as of December 31, 2005 and 2004 are the following:

December 31, 2005	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Demand notes	$ 1,677	$ —	$ —	$ 1,677
Cash and cash equivalents	4,705	—	—	4,705
Federal obligations	8,499	—	(58)	8,441
Corporate obligations	21,218	—	(111)	21,107
Total marketable securities designated as available for sale	$ 36,099	$ —	$ (169)	$ 35,930

December 31, 2004	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents	$ 2,334	$ —	$ —	$ 2,334
Auction rate notes	6,511	—	—	6,511
Commercial paper	7,981	—	(3)	7,978
Federal agency obligations	8,571	3	(27)	8,547
Corporate obligations	10,091	—	(23)	10,068
Total marketable securities designated as available for sale	$ 35,488	$ 3	$ (53)	$ 35,438

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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(2) Marketable Securities—*(continued)*

The amortized costs and estimated fair value of debt securities as of December 31, 2005 and 2004 are shown below by effective maturity. Effective maturities will differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

December 31, 2005	Amortized Cost	Estimated Fair Value
Due in less than one year	$ 31,950	$ 31,849
Due after one year and within two years	3,114	3,063
Due after two years and within three years	1,035	1,018
	$ 36,099	$ 35,930

December 31, 2004	Amortized Cost	Estimated Fair Value
Due in less than one year	$ 29,343	$ 29,299
Due after one year and within two years	4,073	4,065
Due after two years and within three years	2,072	2,074
	$ 35,488	$ 35,438

No gains or losses were recognized on KVH's marketable securities during the year ended December 31, 2005 and 2004.

(3) Inventories

Inventories as of December 31, 2005 and 2004 include the costs of material, labor, and factory overhead. Inventories consist of the following:

	December 31,	
	2005	2004
Raw materials	$ 3,673	$ 4,070
Finished goods	2,407	2,403
Work in process	484	778
	$ 6,564	$ 7,251

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(all tabular amounts in thousands except per share amounts)

(4) Inventory Revaluation and Other Special Charges

In July 2004, KVH initiated a new pricing initiative for the TracVision A5 mobile satellite antenna. As a result of the associated price reduction, and in accordance with Accounting Research Bulletin 43, KVH recognized a $2.6 million loss related to a TracVision A5 inventory revaluation and other related pricing initiatives in June 2004. Total net charges for the year ended December 31, 2004 were as follows:

Loss on non-cancelable inventory purchase commitments	$ 1,425
Revaluation of inventory to net realizable value	836
Loss on disposal of TracVision A5 tooling and equipment (1)	97
TracVision A5 revaluation charge recognized in cost of sales	2,358
Other TracVision A5 pricing initiative charges not included in cost of sales	211
Total TracVision A5 revaluation and other charges	$ 2,569

(1) For presentation purposes, loss on disposal of TracVision A5 tooling and equipment was included within the Statement of Cash Flows caption—Loss on disposal of equipment.

Balances and activity related to the TracVision A5 liability since inception is as follows:

Category	Balance Recorded as of June 30, 2004	Additions/ Adjustments to Provisions	Utilization	Balance as of Dec. 31, 2004	Reductions/ Adjustments to Provisions	Utilization	Balance as of Dec. 31, 2005
Non-cancelable inventory purchase commitments	$ 1,480	$ (55)	$ (430)	$ 995	$ (98)	$ (842)	$ 55
Other TracVision A5 pricing initiative	150	61	(209)	2	(2)	—	—
Accrued loss on TracVision A5 non-cancelable purchase commitments	$ 1,630	$ 6	$ (639)	$ 997	$ (100)	$ (842)	$ 55

(5) Property and Equipment

Property and equipment, net, as of December 31, 2005 and 2004 consist of the following:

	December 31,	
	2005	2004
Land	$ 807	$ 807
Building and improvements	3,642	3,576
Leasehold improvements	1,557	1,473
Machinery and equipment	9,872	8,234
Office and computer equipment	5,438	5,073
Motor vehicles	367	347
	21,683	19,510
Less accumulated depreciation	13,020	11,292
	$ 8,663	$ 8,218

Depreciation for the years ended December 31, 2005, 2004 and 2003 amounted to approximately $1.8 million, $2.0 million, and $1.6 million, respectively.

KVH INDUSTRIES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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(6) Debt and Line of Credit

In January 1999, KVH entered into a mortgage loan in the amount of $3.0 million. The note term is 10 years, with a principal amortization of 20 years at a fixed rate of interest of 7%. Land, building and improvements with an approximate carrying value of $3.7 million as of December 31, 2005, secure the mortgage loan. The monthly mortgage payment is approximately $23,000, including interest and principal. Due to the difference in the term of the note and amortization of the principal, a balloon payment of approximately $2.0 million is due on February 1, 2009. The mortgage principal paid during the year ended December 31, 2005 totaled approximately $107,000. Interest expense on the mortgage approximated $171,000, $179,000 and $185,000 for the years ended December 31, 2005, 2004 and 2003, respectively, and is reflected within “interest income (expense) net”, in the accompanying statements of operations.

The following is a summary of future principal payments under the mortgage:

Years ending December 31,	Principal Payment
2006	$ 115
2007	123
2008	132
2009	2,027
Total outstanding at December 31, 2005	$ 2,397

Since March 27, 2000, KVH has maintained a revolving loan agreement. The loan agreement currently provides for a maximum available credit of $15.0 million and will expire on July 17, 2006. In the event of a draw down, KVH would pay interest at a rate equal to, at its option, LIBOR plus 2%, or the greater of the Federal Funds Effective Rate plus 0.5% or the bank’s prime interest rate. Fees are paid at an annual rate of 0.25% on up to $10.0 million of the unused portion of the loan facility. The loan facility advances funds using an asset availability formula based upon KVH’s eligible accounts receivable and inventory balances, less a fixed reserve amount. KVH may terminate the loan agreement prior to its full term, provided the bank is given 30 days’ written notice. At December 31, 2005, no borrowings were outstanding under the facility.

(7) Commitments and Contingencies

KVH has certain operating leases for facilities, automobiles, and various equipment. The following reflects future minimum payments under operating leases that have initial or remaining non-cancelable lease terms in excess of one year at December 31, 2005:

Years ending December 31,	Operating Leases
2006	$ 618
2007	572
2008	364
2009	308
Thereafter	527
Total minimum lease payments	$ 2,389

(all tabular amounts in thousands except per share amounts)

(7) Commitments and Contingencies—*(continued)*

Total rent expense incurred under facility operating leases for the years ended December 31, 2005, 2004 and 2003 amounted to $522,000, $336,000, and $210,000, respectively.

In the normal course of business, KVH enters into unconditional purchase order obligations with its suppliers for inventory and other operational purchases. Outstanding and unconditional purchase order obligations as of December 31, 2005 approximated $8.0 million.

In the first quarter of 2006, KVH entered into a licensing agreement with Litton Systems, Inc., a wholly owned subsidiary of Northrop Grumman Systems Corporation (Grumman) to provide KVH with the right to access/use certain patented technologies owned by Grumman. Under the agreement, which spans the life of the patented technology, KVH will pay a licensing fee to Grumman equal to 4.5% of the net selling price for each unit sold in which the licensed technology is utilized. The agreement provides for minimum payments during the next four years of $312,500, $250,000, $250,000 and $187,500, respectively.

(8) Stockholders' Equity

(a) Employee Stock Options

KVH currently has a 1996 Incentive and Non-Qualified Stock Option Plan and a 2003 Incentive and Non-Qualified Stock Option Plan (the "Plans").

KVH has reserved 2,000,967 shares of its common stock for issuance upon exercise of options granted or to be granted under the Plans. These options generally vest in equal annual amounts over four to five years beginning on the date of the grant. The Plans provide that options be granted at exercise prices not less than market value on the date the option is granted and options are adjusted for such changes as stock splits and stock dividends. No options are exercisable for periods of more than 10 years after date of grant.

All stock option values were derived using the Black-Scholes option-pricing model. The per share weighted-average fair values of stock options granted during 2005, 2004 and 2003 were $5.07, $8.34, and $9.49, respectively. The weighted-average assumptions used to value options as of their grant date were as follows:

	Year Ended December 31,		
	2005	2004	2003
Risk-free interest rate	4.0%	3.2%	2.7%
Expected volatility	58.2%	91.1%	93.9%
Expected life (years)	4.37	4.31	4.13
Expected dividends	N/A	N/A	N/A

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(8) Stockholders' Equity—*(continued)*

The changes in outstanding employee stock options for the three years ended December 31, 2005, 2004 and 2003 are as follows:

	Number of Shares	Weighted-average Exercise Price
Outstanding at January 1, 2003	1,150,279	$ 5.56
Granted	314,425	13.97
Exercised	(350,815)	4.83
Expired or canceled	(88,698)	6.82
Outstanding at December 31, 2003	1,025,191	$ 8.28
Granted	370,875	12.29
Exercised	(125,672)	3.31
Expired or canceled	(50,832)	10.44
Outstanding at December 31, 2004	1,219,562	$ 9.92
Granted	426,950	10.05
Exercised	(140,733)	5.70
Expired or canceled	(79,163)	10.95
Outstanding at December 31, 2005	1,426,616	$ 10.32

The following table summarizes information about employee stock options at December 31, 2005:

Range of Exercise Prices	Number Outstanding	Average Remaining Life in Years	Outstanding Weighted-Average Exercise Price	Number Exercisable	Exercisable Weighted-Average Exercise Price
$ 4.01 – 6.00	49,213	0.56	$ 5.87	49,213	$ 5.87
6.01 – 9.00	477,503	1.63	7.12	344,554	7.04
9.01 – 13.50	654,325	3.71	10.61	261,249	11.47
13.51 – 20.02	245,575	2.94	16.65	245,575	16.65
	1,426,616	2.78	$ 10.32	900,591	$ 10.88

As of December 31, 2004 and 2003 the number of options exercisable was 490,661 and 354,686, respectively, and the weighted average exercise price of those options was $8.41 and $8.28, respectively.

On December 9, 2005, the Compensation Committee of the Board of Directors accelerated the vesting of existing "out-of-the-money" stock options that had exercise prices per share equal to or greater than ten percent (10%) above the closing market price on December 8, 2005. On such date, the closing market price was $9.93. Accordingly, options to purchase approximately 271,000 shares of KVH's common stock became exercisable on December 9, 2005 as a result of this acceleration. These options had exercise prices ranging from $10.99 to $17.62 per share. The decision to accelerate the vesting of these stock options was made primarily to reduce the cumulative non-cash compensation expense that would have been recorded in KVH's statement of operations in future periods as a result of the adoption of SFAS No. 123(R) in 2006.

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(8) Stockholders' Equity—*(continued)*

(b) Employee Stock Purchase Plan

The Employee Stock Purchase Plan (the "ESPP") covers substantially all of KVH's employees in the United States and Denmark. The ESPP allows eligible employees the right to purchase common stock on a semi-annual basis at 85% of the market price. During 2005, 2004 and 2003, 24,122, 23,645, and 18,516 shares, respectively, were issued under this plan. As of December 31, 2005, approximately 38,000 shares were reserved for future issuance under the plan.

(9) Common Stock Issuance

On February 13, 2004, KVH completed an underwritten public offering of 2,750,000 shares of its common stock at $18.75 per share. Net proceeds to KVH, after deducting offering costs, were approximately $48.0 million and are expected to be used for working capital and general corporate purposes. Financing expenses totaled approximately $3.6 million and included $2.8 million in underwriting fees.

(10) Income Taxes

Income tax expense (benefit) for the years ended December 31, 2005, 2004 and 2003 attributable to income (loss) from operations is presented below.

	Current	Deferred	Total
Year ended December 31, 2005			
Federal	$ 61	$ 105	$ 166
State	—	15	15
Foreign	112	(4)	108
	$ 173	$ 116	$ 289
Year ended December 31, 2004			
Federal	$ —	$ (676)	$(676)
State	—	(99)	(99)
Foreign	25	4	29
	$ 25	$ (771)	$(746)
Year ended December 31, 2003			
Federal	$ (280)	$ —	$(280)
State	—	—	—
Foreign	—	8	8
	$ (280)	$ 8	$(272)

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(10) Income Taxes—*(continued)*

The actual income tax expense (benefit) differs from the "expected" income tax expense (benefit) computed by applying the United States Federal corporate income tax rate of 34% to income (loss) before taxes as follows:

	Year Ended December 31,		
	2005	2004	2003
Computed "expected" tax expense (benefit)	$1,095	$(2,344)	$(592)
Increase (decrease) in income taxes resulting from:			
Non-deductible expenses	22	20	18
Foreign tax rate and regulation differential	(27)	20	(14)
(Increase) decrease of valuation reserve resulting from tax strategy revaluation	120	(775)	
Change in tax reserves	—	—	(65)
Change in valuation allowance	(921)	2,333	381
Net income tax expense (benefit)	$ 289	$ (746)	$(272)

The components of results of operations before income taxes, determined by tax jurisdiction, are as follows:

	Year Ended December 31,		
	2005	2004	2003
United States	$2,821	$(6,919)	$(1,805)
Denmark	399	26	63
Total	$3,220	$(6,893)	$(1,742)

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities for the periods presented are as follows:

	December 31,	
	2005	2004
Deferred tax assets:		
Accounts receivable, due to allowance for doubtful accounts	$ 495	$ 451
Inventories	494	311
Operating loss carry forwards	8,010	9,901
Intangibles due to differences in amortization	153	129
Research and alternative minimum tax credit carry forwards	215	197
State tax credit carry forwards	194	165
Accrued loss on TracVision A5 non-cancelable purchase commitments	21	387
Accrued expenses	452	186
Gross deferred tax assets	10,034	11,727
Less valuation allowance	(6,033)	(7,299)
Net deferred tax assets	4,001	4,428
Deferred tax liability:		
Property and equipment, due to differences in depreciation	(462)	(769)
Net deferred tax asset	$ 3,539	$ 3,659

(10) Income Taxes—*(continued)*

Approximately $0.2 million of KVH's net deferred tax asset is attributable to future deductible amounts within the Danish tax jurisdiction for KVH's wholly owned subsidiary located in Denmark.

As of December 31, 2005, KVH had federal net operating loss carry forwards available to offset future taxable income of approximately $22.2 million. KVH also had state net operating loss carry forwards available to offset future state taxable income of approximately $9.2 million. The federal net operating loss carry forwards expire in years 2019 through 2024. State net operating loss carry forwards expire in years 2006 through 2024.

As of December 31, 2005, KVH had research and development tax credit carry forwards in the amount of $151,000 that expire in years 2008 through 2012. KVH also had alternative minimum tax credits of $64,000 that have no expiration date. As of December 31, 2005, KVH's state tax credit carry forwards available to reduce future state tax expense were approximately $194,000. These state tax credit carry forwards expire in years 2006 through 2011.

KVH's ability to utilize these net operating loss carryforwards and credits may be limited in the future if KVH experiences an ownership change pursuant to Internal Revenue Code 382. An ownership change occurs when the ownership percentages of 5% or greater stockholders changes by more than 50% over a three-year period.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets depends upon the generation of future taxable income during the periods in which those temporary differences become deductible. KVH has recorded a valuation allowance against a portion of its deferred tax assets because management believes that, after considering all of the available objective evidence, including available tax planning strategies, historical and prospective, with greater weight given to historical evidence, it is more likely than not that a portion of the asset will not be realized.

Total valuation allowance decreased by approximately $1.3 million from December 31, 2004. Subsequently recognized tax benefits relating to valuation allowances for deferred tax assets, if any, will be allocated as follows: $4.3 million to continuing operations and $1.7 million to stockholders' equity for amounts attributable to the exercise of employee stock options.

KVH's tax planning strategy provides a basis for the realization of a portion of its total domestic deferred tax assets as of December 31, 2005 and 2004. Specifically, as of December 31, 2005 and 2004, KVH has approximately $3.3 million and $3.5 million of deferred tax assets, which consist of federal net operating loss carry forwards available to offset future taxable income. KVH's strategy to utilize these assets is based upon its ability to sell its property located in Middletown, Rhode Island (Middletown Property) for the express purpose of generating taxable income to utilize these loss carry forwards before they expire. This tax strategy is not an action that KVH ordinarily would take but would take, if necessary, to realize tax benefits prior to expiration. In 2004, as a result of an independent and certified appraisal of KVH's land and building located at 50 Enterprise Center, Middletown, RI, KVH recorded the release of $775,000 in deferred tax asset valuation allowance to increase the U.S. net realizable deferred tax assets to $3.45 million. This increase is derived from the estimate that the property sale would generate approximately $8.9 million in net taxable gains, should KVH be required to

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(10) Income Taxes—*(continued)*

execute on its strategy to preserve its deferred tax assets. Because the realizable value of KVH's deferred tax assets is derived from the fair market valuation of the Middletown Property, future tax benefit and expenses are highly correlated to changes in property values in Rhode Island.

KVH's policy is that undistributed earnings of its foreign subsidiary are indefinitely reinvested and, accordingly, no related provision for U.S. federal and state income taxes has been provided. Upon distribution of those earnings in the form of dividends or otherwise, KVH will be subject to both U.S. income taxes (less foreign tax credits) and withholding taxes in Denmark.

(11) 401(k) Profit Sharing Plan

KVH has a 401(k) Profit Sharing Plan (the Plan) for all eligible employees. Participants may defer a portion of their pre-tax earnings subject to limits determined by the Internal Revenue Service. Participants age 50 or older may be eligible to make additional contributions. As of December 31, 2005, KVH matches one half of the first 3% contributed by the Plan participants. KVH contributions vest over a four-year period from the date of enrollment in the Plan. Total KVH contributions were approximately $144,000, $61,000 and $0 for the years ended December 31, 2005, 2004, and 2003, respectively.

(12) Business and Credit Concentrations

Significant portions of KVH's net sales are as follows:

	Year ended December 31,		
	2005	2004	2003
Net sales to foreign customers outside the U.S. and Canada	18.8%	19.3%	16.7%
Net sales to the United States Army Tank and Automotive Command	*	*	11.3%
Net sales to Camping World Inc.	*	10.1%	*

* Represents less than 10% of net sales in the respective year.

For the year ended December 31, 2005 no single customer accounted for 10% or more of KVH's consolidated net sales.

(13) Segment Reporting

Under common operational management, KVH designs, develops, manufactures and markets its navigation, guidance and stabilization and mobile communication sensor products for use in a wide variety of applications. Products are generally sold directly to third-party consumer electronic dealers and retailers, consumer manufacturers, government contractors or directly to U.S. and other foreign government agencies. Primarily, sales originating in North America consist of sales within the United States and Canada and, to a lesser extent, Mexico, Asia/Pacific and some Latin and South American countries. North American sales also include all defense-related product sales throughout the world. Sales originating from KVH's Denmark subsidiary principally consist of sales into Western European countries, including the United Kingdom, France, Italy, and Spain, as well as a growing number of sales into Russia and certain Middle Eastern countries.

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(13) Segment Reporting—*(continued)*

KVH operates in two geographic segments, exclusively in the mobile communication, navigation and guidance equipment industry, which it considers to be a single business activity. KVH has two primary product categories: mobile communication and navigation, guidance and stabilization. Mobile communication sales and services include automotive, marine and land mobile communication equipment, such as satellite-based telephone, television and broadband Internet connectivity services. Defense sales and services include sales of commercial marine and defense-related navigation, guidance and stabilization equipment based upon digital compass and fiber optic sensor technology, as well as sales of KVH fiber optic gyros for commercial applications. Defense services also include development contract revenue.

	Sales Originating From		
Year ended December 31, 2005	**North America**	**Europe**	**Total**
Mobile communication sales to United States and Canada	$39,064	$ —	$39,064
Mobile communication sales to Europe	—	8,677	8,677
Mobile communication sales to other geographic areas	—	1,316	1,316
Defense sales to United States and Canada	18,773	—	18,773
Defense sales to Europe	2,918	—	2,918
Defense sales to other geographic areas	510	—	510
Intercompany sales	5,771	22	5,793
Subtotal	67,036	10,015	77,051
Eliminations	(5,771)	(22)	(5,793)
Net sales	$61,265	$ 9,993	$71,258
Segment net income	$ 2,640	$ 291	$ 2,931
Depreciation and amortization	$ 1,929	$ 29	$ 1,958
Total assets	$80,085	$ 2,245	$82,330

	Sales Originating From		
Year ended December 31, 2004	**North America**	**Europe**	**Total**
Mobile communication sales to United States and Canada	$40,070	$ —	$40,070
Mobile communication sales to Europe	—	7,413	7,413
Mobile communication sales to other geographic areas	—	1,018	1,018
Defense sales to United States and Canada	10,215	—	10,215
Defense sales to Europe	2,166	—	2,166
Defense sales to other geographic areas	1,421	—	1,421
Intercompany sales	5,226	79	5,305
Subtotal	59,098	8,510	67,608
Eliminations	(5,226)	(79)	(5,305)
Net sales	$53,872	$ 8,431	$62,303
Segment net income (loss)	$ (6,184)	$ 37	$ (6,147)
Depreciation and amortization	$ 1,997	$ 46	$ 2,043
Total assets	$74,005	$ 1,909	$75,914

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(13) Segment Reporting—*(continued)*

Year ended December 31, 2003	Sales Originating From North America	Europe	Total
Mobile communication sales to United States and Canada	$33,487	$ —	$33,487
Mobile communication sales to Europe	—	4,977	4,977
Mobile communication sales to other geographic areas	—	713	713
Defense sales to United States and Canada	13,734	—	13,734
Defense sales to Europe	3,140	—	3,140
Defense sales to other geographic areas	621	—	621
Intercompany sales	3,899	65	3,964
Subtotal	54,881	5,755	60,636
Eliminations	(3,899)	(65)	(3,964)
Net sales	$50,982	$5,690	$56,672
Segment net income (loss)	$ (1,526)	$ 56	$ (1,470)
Depreciation and amortization	$ 1,695	$ 28	$ 1,723
Total assets	$32,093	$1,978	$34,071

(14) Selected Quarterly Financial Results (Unaudited)

Financial information for interim periods was as follows:

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(in thousands, except per share amounts)			
2005				
Net sales	$17,893	$18,807	$16,742	$17,816
Gross profit	7,111	7,778	7,100	7,683
Income tax expense	(157)	(76)	(13)	(43)
Net income	$ 301	$ 952	$ 674	$ 1,004
Income per share (a):				
Basic	$ 0.02	$ 0.07	$ 0.05	$ 0.07
Diluted	$ 0.02	$ 0.06	$ 0.05	$ 0.07
2004				
Net sales	$17,997	$14,532	$13,763	$16,011
TracVision A5 revaluation charge	—	2,413	—	(55)
Gross profit	6,973	2,172	4,690	6,176
Income tax (expense) benefit	(87)	(51)	64	820
Net income (loss)	$ 128	$ (4,948)	$ (1,596)	$ 269
Income (loss) per share (a):				
Basic and diluted	$ 0.01	$ (0.34)	$ (0.11)	$ 0.02

(a) Income (loss) per share is computed independently for each of the quarters. Therefore, the income (loss) per share for the four quarters may not equal the annual income (loss) per share data.

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(15) Legal Matters

KVH is a defendant in a class action lawsuit in the U.S. District Court for the District of Rhode Island in which KVH and certain of its officers are named as defendants. The suit asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 under that statute, as well as claims under Sections 11, 12(a)(2) and 15 of the Securities Act of 1933, on behalf of purchasers of our securities in the period October 1, 2003 to July 2, 2004 and seeks certain legal remedies, including compensatory damages. The Teamsters Affiliates Pension Plan has been appointed lead plaintiff. This matter consolidates into one action eight separate complaints filed between July 24, 2004 and September 15, 2004. On January 14, 2005, the defendants filed a motion to dismiss the consolidated complaint for failure to state a claim upon which relief can be granted. The court denied this motion in part and granted it in part. On October 14, 2005, the defendants answered the consolidated complaint and denied liability and all allegations of wrongdoing. Subsequently, on December 13, 2005, plaintiffs filed a motion for class certification; that motion is pending.

On August 16, 2004, Hamid Mehrvar filed a shareholder’s derivative action in the Rhode Island State Superior Court for Newport County against KVH and certain of its officers and directors. The amended complaint asserts state law claims on KVH’s behalf arising between October 1, 2003 and the present in connection with the allegations set forth in the class action consolidated complaint in the U.S. District Court described above. On October 7, 2005, the court dismissed Mehrvar’s amended complaint without prejudice. By letter dated October 14, 2005, Mehrvar delivered a demand that KVH commence litigation for the same acts alleged in his complaint against the directors and senior officers who served during the period October 1, 2003 to the present. On March 1, 2006, Mehrvar filed a shareholder’s derivative action in the Rhode Island State Superior Court for Providence County against KVH and certain of its officers and directors. The amended complaint asserts state law claims on KVH’s behalf arising between October 1, 2003 and the present in connection with the allegations set forth in the class action consolidated complaint in the U.S. District Court described above and seeks certain legal and equitable remedies, including restitution from KVH’s directors and officers and corporate governance changes.

On June 20, 2005 Yemin Ji filed a shareholder’s derivative action in the U.S. District Court for the District of Rhode Island against KVH and certain of its officers and directors, asserting certain federal and state law claims on KVH’s behalf arising between October 6, 2003 and the present in connection with the same allegations set forth in the class action and Mehrvar complaints described above and seeks certain legal and equitable remedies, including restitution from KVH’s directors and officers and corporate governance changes. On August 23, 2005, KVH moved the Court to abstain from exercising jurisdiction and dismiss the action as duplicative of the Mehrvar case. The Court denied this motion. On January 5, 2006, defendants moved to dismiss the complaint on the same grounds on which the Rhode Island state court dismissed the derivative complaint in Mehrvar that was filed on August 16, 2004. The motion is pending.

In May 2005, Electronic Controlled Systems, Inc., d/b/a King Controls, filed a patent infringement suit against KVH in the U.S. District Court for the District of Minnesota. The three asserted patents relate generally to controlling a satellite dish to acquire a satellite signal. The complaint alleges that KVH willfully infringes the patents and seeks injunctive relief, enhanced damages and attorneys’ fees. KVH has denied the allegations and asserted counterclaims, including claims for false advertising. This litigation is in the discovery phase. In January 2006, Electronic Controlled Systems, Inc., d/b/a/ King Controls, filed a second patent infringement suit against KVH in the U.S. District Court for the District of Minnesota. The second suit concerns one of the same three patents asserted in the original suit filed in May 2005, alleges that KVH willfully infringes the patent and seeks both preliminary and permanent injunctive relief, enhanced damages and attorneys fees. KVH has denied the allegations and asserted counterclaims. A hearing on the plaintiff's motion for a preliminary injunction is currently scheduled for late May.

Additionally, in the ordinary course of business, KVH is a party to inquiries, legal proceedings and claims including, from time to time, disagreements with vendors and customers.

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors
KVH Industries, Inc.:

We consent to the incorporation by reference in the Registration Statement Nos. 333-112341, 333-08491 and 333-67556 on Form S-8 of our reports dated March 15, 2006, with respect to the consolidated balance sheets of KVH Industries, Inc., and subsidiary as of December 31, 2005 and 2004, and the related consolidated statements of operations, changes in stockholders' equity and accumulated other comprehensive income (loss) and cash flows for each of the years in the three-year period ended December 31, 2005, management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2005, and the effectiveness of internal control over financial reporting as of December 31, 2005, which reports appear in the December 31, 2005 Annual Report on Form 10-K of KVH Industries, Inc. and subsidiary.

/s/ KPMG LLP

Providence, Rhode Island
March 15, 2006

Exhibit 31.1

Certification

I, Martin A. Kits van Heyningen, President and Chief Executive Officer of KVH Industries, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of KVH Industries, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 16, 2006

/s/ Martin A. Kits van Heyningen
Martin A. Kits van Heyningen
President and Chief Executive Officer

Exhibit 31.2

Certification

I, Patrick J. Spratt, Chief Financial Officer of KVH Industries, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of KVH Industries, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 16, 2006

/s/ Patrick J. Spratt
Patrick J. Spratt
Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report on Form 10-K of KVH Industries, Inc. (the "Company") for the year ended December 31, 2005, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned chief executive officer and chief financial officer of the Company, certifies, to the best knowledge and belief of the signatory, pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Martin A. Kits van Heyningen
Martin A. Kits van Heyningen
President and Chief Executive Officer

Date: March 16, 2006

/s/ Patrick J. Spratt
Patrick J. Spratt
Chief Financial Officer

Date: March 16, 2006