

EXECUTIVE RETENTION AGREEMENT

This Executive Retention Agreement (this "Agreement") is made and entered into as of this 29th day of August, 2005, by and between Three-Five Systems, Inc., a Delaware corporation with its principal place of business at 1600 North Desert Drive, Tempe, Arizona 85281 (the "Company"), and Jack L. Saltich ("Executive").

WITNESSETH:

WHEREAS, the Company is currently involved in a reorganization that may be implemented through Chapter 11 of the U.S. Bankruptcy Code (the "Reorganization");

WHEREAS, Executive is currently serving as the President and Chief Executive Officer of the Company;

WHEREAS, the Company desires to provide incentives to Executive to maintain his employment with the Company and assist in concluding the Reorganization; and

WHEREAS, the Company and Executive desire to set forth in writing the terms and conditions of their agreements and understandings with respect to Executive's continued employment with the Company during the Reorganization.

NOW, THEREFORE, in consideration of the premises and the mutual covenants and agreements contained herein and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto, intending to be legally bound, agree as follows:

1. **EMPLOYMENT.**

1.1 Executive hereby agrees to continue his employment with the Company during the Term (as defined in Section 2.1 hereof) in accordance with the terms and conditions set forth in this Agreement.

1.2 Executive represents and warrants to the Company that he is free to continue his employment with the Company as contemplated herein and that he has no other written or oral obligations or commitments which are reasonably likely to interfere with the performance of his obligations hereunder.

2. **TERM.**

2.1 The term of Executive's employment hereunder (the "Term") shall commence on the date of this Agreement and continue for a period ending on the earliest of (i) the date that is six (6) months from the date hereof; (ii) the date on which the Company's Plan of Reorganization under Chapter 11 of the U.S. Bankruptcy Code is confirmed by the U.S. Bankruptcy Court; (iii) the death of Executive; (iv) resignation by the Executive with the prior approval of the Board of Directors of the Company; and (v)

termination of Executive's employment by the Company as hereinafter provided (the earliest of such dates being referred to herein as the "Completion Date").

2.2 Executive shall have no right or entitlement by virtue of this Agreement to continued employment with the Company beyond the Term; provided, however, that nothing herein shall be construed to prevent the Company from offering employment to Executive subsequent to the Term upon such terms and conditions as may be mutually acceptable to the parties.

3. DUTIES AND EXTENT OF SERVICES.

3.1 During the Term, Executive may resign from his positions as President and Chief Executive Officer of the Company, but shall continue to be employed by the Company and shall perform the duties set forth on Exhibit A hereto. Executive shall report directly to the Company's Chief Restructuring Officer.

3.2 During the Term, Executive agrees to devote so much of his time, skill, attention and energy as may be necessary to perform the duties and responsibilities assigned to him under this Agreement. Executive may engage in any other business for gain, profit or other pecuniary advantage as long as such activity does not materially interfere with Executive's assigned duties and responsibilities pursuant to this Agreement.

4. COMPENSATION AND BENEFITS.

4.1 The Company shall compensate Executive during the Term at the same rate of salary that he received, and pursuant to the same payment terms as in effect, immediately prior to execution of this Agreement. During the Term, Executive shall be entitled to the same or substantially similar benefits that he and his dependents received from the Company immediately prior to the execution of this Agreement.

4.2 Provided that Executive has remained in the employ of the Company through the Completion Date, unless the Company has terminated Executive's employment for Cause (as defined below), promptly after the Completion Date, the Company shall pay to Executive a lump sum amount equal to Executive's base salary (as set forth in Section 4.1 above) for a period of sixteen (16) months less the length of the Term, which payment shall be reduced by applicable withholdings to the extent required by applicable laws.

4.3 Provided that Executive has remained in the employ of the Company through the Completion Date, unless the Company has terminated Executive's employment for Cause, the Company shall pay to Executive an incentive bonus in connection with the Reorganization (the "Success Fee") based upon the final cash distribution that is paid to the shareholders of the Company in the Reorganization (the "Shareholder Distribution"). The Success Fee shall be calculated as follows: (i) if the Shareholder Distribution is \$4 million or less, no Success Fee will be payable; and (ii) if the Shareholder Distribution is greater than \$4 million, the Success Fee shall be equal to 1.25% of the first \$2 million by which the Shareholder Distribution exceeds \$4 million, plus 2.5% of any amount by which the Shareholder Distribution exceeds \$6 million. Payment of the Success Fee shall be made in a lump sum at the same time as payment of the Shareholder Distribution.

5. TERMINATION OF AGREEMENT DUE TO DEATH.

5.1 In the event of Executive's death during the Term, this Agreement shall terminate and the Company shall pay to Executive's estate the payments required pursuant to Section 4.2 above and shall continue to provide insurance coverage to Executive dependents to the extent required by Section 4.2 above.

6. TERMINATION OF AGREEMENT BY EXECUTIVE

6.1 Executive may voluntarily terminate this Agreement at any time during the Term by giving the Company written notice of his intent to terminate, which termination shall automatically become effective upon the date of such notice or upon such later date (not more than thirty (30) days thereafter) as shall be set forth in such notice. In no event shall the Company be prohibited from immediately terminating this Agreement pursuant to Section 7 hereof if an action or event giving Cause (as defined below) for termination occurs (i) before the date of such notice, or (ii) between the date of such notice and the effective date specified therein.

6.2 In the event Executive voluntarily terminates this Agreement prior to the Completion Date without the prior approval of the Board of Directors of the Company, Executive shall not be entitled to any compensation, remuneration or other sums provided for in this Agreement payable after the termination date (including any payments set forth in Section 4.2 hereof) and the Company and Executive thereafter shall have no further obligations under this Agreement with the exception of the covenants contained in Section 9 herein, which shall survive such termination.

7. TERMINATION OF AGREEMENT BY COMPANY

7.1 Nothing in this Agreement shall be construed to prevent the Company from terminating this Agreement during the Term with or without Cause (as hereafter defined), effective immediately upon notification to Executive. In the event this Agreement is terminated by the Company for Cause, Executive shall not be entitled to any compensation, remuneration or other sums provided for in this Agreement payable after the date of the action or event which constitutes Cause for such termination (including any payments set forth in Section 4.2 hereof).

7.2 For purposes of this Agreement, "Cause" shall mean and include any or all of the following: (i) Executive willfully neglects the duties Executive is required to perform under the terms of this Agreement, demonstrates behavior substantially incompatible with the goals, objectives, or business interests of the Company, or commits such acts of dishonesty, fraud, misrepresentation, or any acts or moral turpitude, as would prevent the effective performance of Executive's duties, (ii) a conviction of Executive for a felony (from which, through lapse of time or otherwise, no successful appeal shall have been made), (iii) material violation(s) of the Company's policies and/or procedures by Executive, if Executive fails to take such remedial steps as deemed necessary by the Company to cure the problem within thirty (30) days following the Company's written notice to Executive of such material breach, or (iv) a material breach by Executive of any of the terms of this Agreement that is not cured to the reasonable satisfaction of the Company within thirty (30) days following the Company's written notice to Executive of such material breach.

8. ASSIGNMENT

8.1 This Agreement shall be assigned and transferred to, and shall be binding upon and shall inure to the benefit of, any successor of the Company and any such successor shall be deemed substituted for the “Company” for all purposes under the terms of this Agreement.

8.2 This Agreement shall inure to the benefit of and be enforceable by Executive’s personal or legal representatives, executors, administrators, successors, heirs, devisees, and legatees.

9. CONFIDENTIALITY; RETURN OF COMPANY PROPERTY

9.1 Executive agrees that, through the performance of his duties as an executive of the Company and by virtue of the relationship of trust and confidence between Executive and the Company, Executive possesses and will possess certain proprietary or non-public information of the Company and its affiliates which is of a special and unique nature and value to the Company and its affiliates, including, without limitation, business plans and strategies, financial information and operating results, market information and projections, manufacturing processes, equipment and methods, product information, trade secrets, methods or practices of obtaining or doing business, information relating to customers and their requirements, supplier information, and any related know-how, proprietary computer programs, data, and information whatsoever (“Confidential Information”). Executive covenants and agrees that he will not, at any time, whether during the Term or otherwise, reveal, divulge or make known to any person (other than the Company and its affiliates, a successor to the Company or as otherwise directed by the Company) or use for Executive’s own account, any Confidential Information, whether or not obtained with knowledge and permission of the Company and whether or not developed or otherwise created in whole or in part through the efforts of Executive.

9.2 Executive agrees to deliver to the Company at the expiration or termination of his employment with the Company (whether or not the Company shall so request), or at any other time the Company may request, all memoranda, notes, plans, programs, lists, correspondence, data, books, manuals, records, reports and other documents (and copies thereof), whether in hardcopy or electronic format, containing or reflecting any Confidential Information or otherwise relating to the business of the Company or its affiliates which Executive may then possess or have under his control, or which subsequently come into Executive’s possession or under his control.

9.3 It is specifically understood, acknowledged and agreed by Executive that (a) the restrictions contained in Section 9 of this Agreement represent a reasonable and necessary protection of the legitimate interests of the Company and that Executive’s failure, or threatened failure, to observe and comply with these covenants and agreements shall constitute a substantial and material breach of this Agreement and will cause irreparable harm to the Company; (b) it is and will continue to be difficult to ascertain the nature, scope and extent of such harm; and (c) a remedy at law for such failure, or threatened failure, by Executive will be inadequate. Accordingly, it is the intention of the parties that, in the event of any breach, or threatened breach, of Section 9 of this Agreement, the Company shall be entitled, to temporary or permanent injunctive relief, and all other appropriate legal and/or equitable relief against Executive including attorney fees if applicable, in order to cure or prevent any breach by Executive, of the covenants and agreements contained in this Section. Such relief shall be in addition to any other remedies available to the Company at law or in equity, or under any other provision of this Agreement.

9.4 On the Completion Date, Executive shall return to the Company all Company property in Executive's actual or constructive possession. Notwithstanding the foregoing, as of the Completion Date, the Company shall transfer to Executive ownership of Executive's laptop and desktop computers and peripherals in Executive's possession. Executive agrees that all Confidential Information shall be removed from Executive's laptop and desktop computers on the Completion Date. In addition, Executive shall be entitled to retain his Company-supplied cell phone, provided that Executive transfers cellular service to a private account commencing on the Completion Date.

10. **GOVERNING LAW**

10.1 This Agreement shall be governed by and construed pursuant to the laws of the State of Arizona, without giving effect to the conflict of laws provisions thereof. In the event that any action hereunder is brought in any state or federal court the parties hereby waive any right they may have to a jury trial.

11. **NOTICES.**

11.1 Any notice required or permitted to be given pursuant to this Agreement shall be in writing and either (i) delivered in hand to Executive or (ii) sent by certified or registered mail, return receipt requested, addressed as follows:

If to the Company, at the address specified in the first paragraph of this Agreement, to the attention of the Chief Restructuring Officer.

If to Executive, to him at his residence address as then appearing in the Company's payroll records.

Any such address may be changed by any party by written notice to the other given in accordance herewith. Any notice given in the manner described in clause (i) shall be deemed given when delivered. Any notice given in the manner described in clause (ii) shall be deemed given when deposited for delivery so addressed with postage and certification or registration fees prepaid.

12. **SEVERABILITY**

12.1 If any provision of this Agreement shall be held to be invalid or unenforceable, and is not reformed by an arbitrator, court, or other finder of fact, such invalidity or unenforceability shall attach only to such provision and shall not in any way affect or render invalid or unenforceable any other provision of this Agreement, and this Agreement shall be carried out as if such invalid or unenforceable provision were not contained herein.

13. **AMENDMENT AND WAIVER**

13.1 This Agreement may not be amended or modified except by a writing executed by the parties hereto. No extension of time for, or waiver of the performance of, any obligation of any party hereto shall be effective unless it is made in a writing signed by the party granting such extension or waiver. Unless it specifically states otherwise, no waiver shall constitute or be construed as a

continuing waiver, or a waiver of any subsequent breach or non-performance.

14. **CONSULTATION WITH COUNSEL**

14.1 Executive acknowledges that in the execution of this Agreement, the Company advised him to consult with an attorney prior to executing this Agreement. Executive has either consulted with an attorney or has voluntarily chosen not to do so, but in either event, has read this Agreement and fully understands all of its terms and agrees to said terms voluntarily and with full knowledge of the duties and obligations imposed hereby. Further, Executive understands that he and his counsel, if any, have had the opportunity to negotiate changes to the provisions of this Agreement. As a result, this Agreement has been prepared jointly by the parties hereto. In the event of ambiguity, the terms hereof shall not be construed in favor of, or against, any party on account of its participation in such preparation.

15. **ENTIRE AGREEMENT; NO THIRD PARTY BENEFICIARIES**

15.1 This Agreement sets forth the entire agreement between the parties hereto as to the subject matter hereof and supersedes all prior agreements, understandings and negotiations, both written and oral, between the parties with respect to such subject matter; provided that Executive shall remain bound by any pre-existing agreements or restrictions arising from his past status as an employee, officer or director of the Company relating to matters such as the Company's intellectual property, confidentiality, and similar matters. Except as specifically provided herein, this Agreement is not intended to confer upon any person other than the parties hereto any rights or remedies hereunder.

16. **COUNTERPARTS**

16.1 This Agreement may be executed in any number of counterparts, each of which shall be deemed an original for all purposes, and all of which together shall constitute one agreement.

17. **ARBITRATION OF DISPUTES**

17.1 Any dispute between the parties arising from or related to this Agreement or the breach thereof shall be referred to mediation within thirty (30) days of written notice by either party that a dispute exists. Mediation will involve a single neutral mediator, jointly selected by the parties. If the parties are unable to jointly agree upon a mediator with the aforementioned thirty (30) day period, the matter shall be substituted to the American Arbitration Association for mediation under the National Rules for the Resolution of Employment Disputes – Employment Mediation Rules, or successor Rules, and shall take place in Phoenix, Arizona.

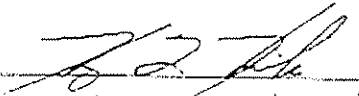
17.2 If the dispute is not resolved by mediation within ninety (90) days of the date of the notice of the dispute, then, upon notice by either party to the other, the claim shall be resolved by final and binding arbitration heard by the mediator sitting as arbitrator, or, if either party objects to the mediator's service as arbitrator, by final and binding arbitration administered by the American Arbitration Association under its National rules for the Resolution of Employment Disputes, or successor Rules, and judgment upon the award rendered by a single arbitrator may be entered in any court having jurisdiction thereof.

17.3 Either party may enforce these mediation or arbitration provisions or seek interim or provisional relief from a court until the dispute is arbitrated or otherwise resolved. Except to the extent required by applicable law or regulation, neither party nor any mediator or arbitrator may disclose the existence, content or results of any mediation or arbitration hereunder without the prior written consent of both parties.

[Signature Page Follows]

IN WITNESS WHEREOF, the undersigned have hereunto set their hands and seals on the day and year first above written.

THREE-FIVE SYSTEMS, INC.

By: 
Name: Henry L. Hovela
Title: Chairman

JACK L. SALTICH

IN WITNESS WHEREOF, the undersigned have hereunto set their hands and seals on the day and year first above written.

THREE-FIVE SYSTEMS, INC.

By: _____

Name: _____

Title: _____

JACK L. SALTICH


29 Aug. 2005

Exhibit A

Executive Duties

Executive shall report to Carl Young, Chief Restructuring Officer of the Company, and diligently perform such duties, acts and responsibilities as shall reasonably be requested or delegated by the Chief Restructuring Officer.